

EC317: Investments

Block 8 – Spring 2014
Colorado College

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Class location:	Palmer 230
Class Hours:	Typically 2pm~5pm M-Th, and am class on Fridays. See schedule for daily meeting times, which vary.
Homework Lab Assistants:	Lauren Nelson, Ben Munyao, Thamanna Vasan
Homework Lab Hours:	Noon-2pm on Days 1-9 and 11 (see CANVAS or syllabus)
Office Hours:	Normally an hour prior to class, or by appt.

DEPARTMENT OF ECONOMICS AND BUSINESS MISSION STATEMENT

MISSION

We engage exceptional students
who think critically, analytically and creatively
with intellectual competence and confidence,
leveraging the advantages of the Block Plan,
drawing on the art and science of the discipline,
at home and abroad,
for now and for life.

Our students can:

-  COMMUNICATE EFFECTIVELY
 -  Write effectively
 -  Speak and present effectively
 -  Use the language of economics and business accurately and persuasively

-  FRAME AND RESOLVE PROBLEMS
 -  Apply relevant knowledge creatively
 -  Appreciate the complexity of multiple perspectives
 -  Engage ambiguous contexts

-  ANALYZE DATA
 -  Interpret evidence in a reason-based approach
 -  Generate insightful analysis in a theoretical context

-  WORK INDEPENDENTLY
 -  Demonstrate initiative and perseverance
 -  Manage projects effectively

NOTE: This course addresses each of the above the goals in some fashion.

COURSE DESCRIPTION:

Students will be introduced to the prevailing theories, models and philosophies of investment analysis and management for an environment where individuals make investment decisions under uncertainty. We will explore both investment fundamentals with a brief introduction into portfolio management. Specific topics of interest include a comprehensive TVM review, fundamentals analysis, market behavior, asset allocation, portfolio theory, ethics, risk & return, and behavioral finance.

COURSE LEARNING OBJECTIVES

To introduce students to the theories of security and portfolio analysis. At the completion of the course, students should have a solid understanding of the following concepts:

- o The securities environment
- o Rates of return
- o Measures of risk
- o Stock valuation
- o Bond valuation
- o Asset allocation
- o Price indexes
- o Diversification
- o Capital Asset Pricing Model
- o Interest rates and inflation
- o Passive versus active investment management
- o Derivatives (options and futures)

TEXT AND MATERIALS

1. Bodie, Kane and Markus, *Investment Essentials*, (9th Ed). ISBN: 978-0078034695.
2. Malkiel, Burton. *A Random Walk Down Wall Street*. (2011 edition). ISBN: 978-0393081435.
3. The Essays of Warren Buffett: Lessons for Corporate America (3d edition) by Warren Buffett and Lawrence Cunningham. Published by the Cunningham Group (2013). ISBN-13: 978-1611634099. Also on Kindle (March 14, 2013), ASIN: B00BUBALZW.
4. Other required readings as provided during the course via CANVAS.

COURSE ADMINISTRATION

Class meeting time and location: This class is normally scheduled to meet at 2:00pm during Monday through Friday for each of the first three weeks during the block. Please check the schedule on CANVAS for exceptions, particularly when we have guest speakers as times may change. Most classes will last approximately three hours. There is no specific “end time” to any class.

Performance evaluation: Grades will be assigned on the basis of your performance on the following evaluation vehicles:

<u>Activity</u>	<u>Weight</u>
Class Participation (daily)	20%
Problem Set (Day 9)	10%
Analysis Paper (Day 10)	10%
Exam (Day 11)	20%
Endowment Analysis Presentation (Day 17)	15%
<u>Endowment Analysis Paper (Day 18)</u>	<u>25%</u>
	100%

College policy states that grades of “A” are reserved for “excellent work that reflects superior understanding and insight, creativity, and skill;” grades of “B” are assigned to “good work that reflects a high level of understanding and insight, creativity, or skill;” grades of “C” are assigned to “adequate work that indicates readiness to continue study in the field;” and grades of “D” are assigned to “marginal work, only minimally adequate.” In general, letter grades will be based on a curve (not on a 90/80/70 contract). Although there is no desired target or “correct” distribution of grades, students that are well-prepared, engage each other in thoughtful dialogue during class meetings and demonstrate an intellectual curiosity about the material typically receive “A”s and “B”s. Late work or missed assignments will typically receive no credit.

Daily Participation: Participation will be judged on the following criteria:

1. active participation in each class’s discussion and activities (mere attendance isn’t enough);
2. your insightful questions and responses to the presentations given by other students at the end of the course;
3. attendance at the Berkshire-Hathaway field trip;
4. assigned homework.

Homework: You will have assigned problems from the course text during the first two weeks of the course, as annotated on the syllabus and on CANVAS. For every day there is assigned homework, there will be a "HOMEWORK LAB" offered in the assigned classroom (usually two hours preceding our class). The lab assistants for the block will be in the classroom during the entire period of the offered homework lab. It is strongly encouraged you go to the lab to complete your daily assignments. Attendance will be taken and considered as part of your participation grade. Homework problems will come from the previous day's reading and class topic. The purpose of the homework is to solidify the concepts already covered. All daily homework assignments are due at 2pm on the assigned day to the student lab assistant in the assigned classroom. Assignments must be written legibly or typed, stapled (if multiple pages) and include your name. You may work in groups, but every person must turn in his/her own assignment. Homework will be graded primarily based on the level of effort put forth. Getting the correct answers is far less important than genuinely attempting to work all of the problems. Graded homework assignments from the previous day will be available for pickup the following day by 2pm in the assigned classroom at the conclusion of the daily Homework Lab. Assignments not picked up by the end of the week will be discarded. Because of the volume of and frequency of assignments, late homework assignments will not receive any credit. No exceptions.

Field trip: As part of this course, you will be expected to attend a department-sponsored field trip to the Berkshire-Hathaway Annual Shareholder’s Meeting in Omaha, NE from 2-4 May 2014. This is a required activity for the course. Although the Economics & Business Department will cover all ground transportation costs from CC to the event and back, students are individually responsible for covering the costs of food, lodging and incidentals. To secure hotel accommodations, all students must pay \$125.00 by cash or check (payable to Colorado College) **by March 12, 2014** to cover the costs of lodging. The Econ & Business department will make all necessary reservations and arrangements.

Students needing financial aid or other special requests should immediately notify the instructor. Students are not permitted to make their own travel arrangements except in exceptional circumstances and only with prior approval of the instructor. If approved (in writing), students traveling on their own would assume all liability and responsibility for themselves for the duration of the field trip (to include transportation, lodging, food, etc.)

Exam: The exam is scheduled for the Monday, May 5th — the day after we rerun from the field trip (Day 11 of the course). It will be comprehensive and principally based upon the course readings, homework, problem sets and field trip. It will consist of two parts. During Part I, each student will take the exam by themselves. This part of the exam will be closed book, closed notes. However, you will be permitted to use a single 3"x5" standard notecard during the exam subject to the following constraints:

- (1) You may handwrite anything on the front and back of your card.
- (2) The card must have your name legibly written in the top corner. (A standard piece of paper may be trimmed to 3"x5" and substituted for a notecard if one isn't otherwise available.)
- (3) You may collaborate with other students in developing your respective card, but each student must produce his or her own.
- (4) Cards may not be mechanically created or reproduced (e.g. photocopied, computer printed).
- (5) You may not share notecards once the exam begins.
- (6) Each notecard must be turned in with the exam

During Part II of the exam, students will collaborate within their project groups complete a single exam. This part of the exam will be unrestricted (open book, open notes). Your final exam grade will be a weighted average of Parts I and II (80% for Part I, 20% for Part II).

Problem Set: The problem sets, unlike the homework assignments, will be graded for accuracy. You are encouraged to work with others in accomplishing them. The problem set will be highly similar to the previous week's homework problems, so if you keep up with the homework, you should find the problem sets to be rather straight forward. Although you may work with one another in completing the problem sets, everyone must turn in his or her own work. Duplicate files are not acceptable and will receive zero credit. The problem set will be available online at the conclusion of class on Day 4 (Thursday) and due at the start of class on Day 9 (Thursday). *PLEASE NOTE: No assistance will be given on problem sets 24 hours prior to due date/time.*

Investment Analysis Paper: After reading *A Random Walk Down Wall Street* and *Essays of Warren Buffett*, compose a 5-page (absolute maximum length, double-spaced, 12pt Times new Roman font) essay critiquing each investment philosophy. This assignment will be due AS YOU BOARD THE BUS for the field trip at 9am on Friday (Day 10 of the course). Late assignments will not be accepted. Specifically:

- (1) Based on the readings, **compare and contrast** Malkiel's and Buffett's investment philosophies. Support with evidence from both assigned readings. Cite specific examples and reference them using in-text citations (use APA format, and include a "Works Consulted" page -- required).
- (2) Analyze the relative weaknesses/shortcomings of each philosophy as viewed through the lens of the other (how would Malkiel critique Buffett's investment philosophy, and what would Buffett have to say about the "random walk" philosophy). Again, use specific examples from the reading and your experience at the meeting cite your supporting evidence (using APA - good practice for your thesis).
- (3) Weighing the evidence from all perspectives, articulate your own investment philosophy with respect to investing in equities (common stocks). Justify your position (it must be more than your mere opinion).

Your essay will be graded on:

- (1) Adherence to assignment guidance;
- (2) Degree to which you incorporate key ideas from both books;
- (3) Accurate but succinct analysis (not description) of both Malkiel's and Buffett's investment philosophies;
- (4) Logical coherence of ideas;
- (5) Supporting evidence;
- (6) Proper citations;
- (7) Creativity of thought;
- (8) Depth of analysis.

The challenge of this assignment, given its limited length, will be to clearly articulate a precise argument that contains more analysis than description. To be successful, you must find creative ways to give examples from the book and the meeting in a limited space. Obviously, quotations should be kept to a minimum, and should rarely exceed one sentence.

NOTE: All of Warren Buffett's letters to Berkshire-Hathaway shareholders (1977-2013) are located on CANVAS. If you choose to read these instead of the *Essays of Warren Buffett* book, that's acceptable.

Endowment Analysis Project: As a class, we will have an opportunity to review, analyze and make recommendations to the CC Board of Trustees' Investment Committee on the management of the CC Endowment. In doing so, we will break up into six groups of four members each. Each group will analyze the following four potential strategies:

(1) The Status Quo Approach: Each group should analyze the following subset of current managers actively managing a sizable portion of the CC Endowment:

- (1) CD&R (private equity buyout)
- (2) Maverick (long/short)
- (3) Silchester (international long)
- (4) L Capital Asia (international)
- (5) JW Bristol (balanced equity/fixed income)

All groups will have access to the asset allocation history and recent portfolio performance history of the above managers.

(2) The Malkiel Approach: Construct a comparable portfolio of passively-managed index funds that could provide an alternative investment opportunity. Be sure to maintain a relatively similar risk profile. Pay attention to the asset allocation of both the Status Quo and your proposed Malkiel Portfolio.

(3) The Buffett Approach: Your group should consider companies held in the Berkshire-Hathaway portfolio (or an investment directly in BRK-A).

(4) The Divestment Approach - Sustainability: There are routinely articles in the Catalyst to "go green" and adopt an ideological-driven portfolio that excluded equities that derive profits from fossil-fuel reliant companies. Using suggestions from the "divestment" group at CC (you'll need to do a bit of research here), construct a portfolio that meets their criteria.

The essence of this project is to construct what YOUR GROUP DEEMS to be the "optimal portfolio" for the CC Endowment given the four options outlined above. Specifically, you must (at a

minimum) consider the assets allocation, liquidity premium, fees, performance, risk profile, total returns (both tangible and intangible - the latter which need to be quantified), benchmarking, and opportunity costs.

Your group is to approach this ill-defined task as you would if you were a professional investment analysis company. You are expected to perform a DETAILED ANALYSIS using concepts covered in the course. The type of analysis, organization and presentation will be a decision to be made by each group. Given this project will comprise 20% of your grade, the level of effort, engagement and output will be judged accordingly.

At the end of each project, groups will be required to make specific recommendations to the CC Board of Trustee's Investment Committee. Recommendations are expected to be firmly grounded in data-driven analyses. We will be inviting the members of the Board, so please please don't be surprised if we have some visitors come by.

DUE DATE: All presentations will occur during class during Day 17. Each group will be required to upload their group's paper to CANVAS by the beginning of class on Day 18.

PAPER SPECIFICS: The paper should be analytical in nature. There is no specific format, style or required topics to cover. There are no length requirements, but your paper should be concise and sufficiently cover all required areas with an emphasis on justified recommendations. There is a strong expectations for appropriate charts, tables and figures (of your own creation, not copied from elsewhere). Be careful not to simply describe what you found, but provide both analysis using concepts learned in class AND make specific recommendations, which flow from your analysis.

PRESENTATION SPECIFICS: The presentation should not exceed 15 minutes in length. The focus of your presentation should focus exclusively on your recommendation(s) to the CC Board of Trustees' Investment Committee as to your proposed strategy. All of your recommendations must be backed by analysis/evidence. At a minimum, you should address (compare/contrast) the fees, performance, benchmarks, asset allocation and opportunity costs of your recommended strategy with respect to the status quo. Be very careful on your choice in how you approach using AV support (e.g. PowerPoint slides). Overly complicated slides (read: too many words, crowded, etc) can negatively affect a group's overall grade. (NOTE: For the record, I strongly discourage the use or Prezi as I've never seen a presentation incorporate it effectively. Every year a group tries to prove me wrong, and every year, well, "life's about choices...")

EVALUATION: You will be evaluated on your breadth and depth of analysis using the tools, themes and concepts from the course. An "A" presentation and paper would go well beyond the minimum guidance (in terms of *quality of analysis*, not quantity). All members in the group will receive the same grade on both the paper and presentation, initially. However, group members will have an opportunity to anonymously and privately communicate their own evaluation of group member contribution and performance in accomplishing the project. A consensus of input can have a significant impact on adjustments (both up and down) to individual grades.

DAILY TOPICS AND READING ASSIGNMENTS

<u>Class</u>	<u>Day/Time</u>	<u>Topic</u>	<u>Reading</u>	<u>Notes</u>	<u>Homework</u>
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1	Mon, Apr 21 2:00pm-5:00pm	Course Intro and Overview	BKM: Ch 1 Start reading Random Walk and Buffett essays (due by Day 10)	TVM handout BF Quiz (A,B) Video: Inside Job	Connect: 1.1 - 1.7 WebMaster: 1.1, 1.2
2	Tues, Apr 22 2:30pm-6:00pm	Markets, Securities and Indices	BKM: Ch 2, 3		Connect: 2.1, 2.2, 2.4, 2.7, 2.13, 2.19, 3.3, 3.6, 3.12, 3.15, 3.24
3	Wed, Apr 23 2:00pm-5:00pm	Risk, Return and Diversification	BKM: Ch 5 (all) 6.1, 6.2, 6.3		Connect: 5.2, 5.5, 5.6, 5.10, 5.12, 5.13, 6.8, 6.9, 6.10, 6.11, 6.17
4	Thurs, Apr 24 2:00pm-5:00pm	Modern Portfolio Theory	BKM: Ch 7.1, 7.2, 7.3, 7.4, 8.1, 8.2, 8.3	Problem set assigned	Connect: 7.3, 7.4, 7.5, 7.6, 7.7, 7.9, 7.10, 7.13 thru 7.19, 7.21, 8.12, 8.13, 8.17, 8.19, 8.20
5	Fri, Apr 25 2:00pm-5:00pm	The CC Endowment	Review CANVAS endowment materials	Guest: Stacy Lutz-Davidson	None
6	Mon, Apr 28 2:00pm-5:00pm	Securities Analysis (Equities)	BKM: Ch 13		Connect: 13.5, 13.9, 13.10, 13.14, 13.16
7	Tues, Apr 29 2:00pm-5:00pm	Securities Analysis (Debt)	BKM: 10.1, 10.2, 10.3, 10.4, 10.5		Connect: 10.4, 10.5, 10.6, 10.8, 10.9, 10.12, 10.14
8	Wed, Apr 30 2:00pm-5:00pm	"Post-Modern" Portfolio Theory (P-MPT)	See CANVAS	Guests: Adam Farver and Matt DuPree	Connect: 15.2-15.8
9	Thurs, May 1 2:00pm-5:00pm	Mutual Funds, ETFs and Derivatives	BKM: Ch 4; Ch 15.1, 15.2, 17.1, 17.2 RW: Appendix	Problem set due	Connect: 4.2, 4.3, 4.5, 4.11, 4.12, 4.13, 4.16, 4.26.
10	Fri, May 2 8:00am	Berkshire-Hathaway Field Trip	Complete Random Walk and Buffett essays	Depart CC at 8am for Omaha, NE Analysis Paper due	None
11	Mon, May 5 2:00pm-5:00pm	Exam		Final day of homework lab	None
12	Tues, May 6 2:00pm-5:00pm	Perspectives on Portfolio Management	None	Guest: Scott Schoelzel	Work on project
13	Wed, May 7 2:00pm-5:00pm	Perspectives on Portfolio Management	None	Guest: Steven Halvorsen	Work on project

14	Thurs, May 8 2:00pm-5:00pm	Perspectives on Portfolio Management	None	Guest: Judy Colvin Guest: Brian Payne	Work on project
15	Fri, May 9 2:00pm-5:00pm	Perspectives on Portfolio Management	None	Guest: Thayer Tutt	Work on project
16	Mon, May 12 2:00pm-5:00pm	Perspectives on Portfolio Management	None	Guest: Tom Keene	Work on project
17	Tues, May 13 9:00am	Endowment Analysis Project Presentations	None		None
18	Wed, May 14 11:00am	Course Critique and Summary	None	Meet in Econ Lab or bring computer Final Paper due	None

MISCELLANEOUS COURSE POLICIES

Honor Code: It should go without saying that the Honor Code firmly applies to all activities within this course. The only way in which we can all grow as scholars is to rely on each other's integrity and responsible behavior. Please help each other to preserve the strength of the Honor Code. If you are uncertain about whether your behavior conforms, ask. The general rule is simple: always cite your sources. On the written exam, no outside sources are permitted. For homework and other projects that involve research beforehand, all sources are permitted with appropriate attribution.

The Honor System encompasses the student body, the Honor Council, and the Honor Code to form an essential part of the academic program at Colorado College. Its purpose is to help recognize each student's maturity and individual ability. Accordingly, the Honor System provides an atmosphere of mutual trust that contributes to students' personal growth and academic development. The spirit of this constitution and the principles it embodies are intended to provide a foundation for a personal ethical code that will continue long after graduation from Colorado College.

Every Colorado College student is responsible for obtaining a working knowledge of all rules and regulations of the Honor System and for understanding this constitution and other materials describing the Honor System. Also, the student is obliged to know how the principles apply in each class. Ignorance of the principles embodied in this constitution and of the way in which they apply in a particular class will be no excuse for a violation of the Honor System.

General Guidelines

THESE GENERAL GUIDELINES ARE ONLY A BRIEF SUMMARY OF THE HONOR SYSTEM. EVERY STUDENT IS EXPECTED TO BECOME FAMILIAR WITH THE DETAILS OF THE CONSTITUTION, WHICH FOLLOWS THESE GENERAL GUIDELINES.

1. The Honor System applies to all work done for credit — exams, papers, laboratory reports, daily assignments, and any other assigned work. Unless the professor specifically states otherwise, work done on all tests and assignments shall be entirely the student's own.

2. In papers, direct quotations must be acknowledged by quotes and footnotes. Ideas or paraphrasing taken from outside sources (including course textbooks) must be properly acknowledged, unless the professor specifically states otherwise. In oral reports, verbal acknowledgment of sources is usually sufficient.

3. Exams must be taken at the place and within the time limits designated by the professor. Except as otherwise stated in this constitution, each professor has the right to set such exam and term paper guidelines as the professor deems appropriate.

4. A student's work may not be submitted for simultaneous credit in two different classes without the explicit permission of both professors. Replications of one's own earlier work may be submitted for subsequent credit only with the explicit permission of the professor to whom the work is now being submitted.

5. An attempt to violate the Honor System, which is not completed because the student is observed in the attempt, will be considered a full violation.

6. A student or professor reporting a suspected violation will remain anonymous to everyone except the Honor Council. If the case is appealed, the identity of the accuser will also be revealed to an appeal board consisting of five (5) randomly selected students pledged to confidentiality.

By posting any assignment to CANVAS for this course, you are acknowledging that, on your honor, you have neither given nor received any unauthorized aid on the respective graded assignment.

Disabilities: If you have a disability and require accommodations for this course, please speak with the professor privately as soon as possible so that your needs may be appropriately met. If you have not already done so, you will need to register with Disability Services in the Learning Commons at Tutt Library (Rm 152, 227-8285). This is the CC office responsible for coordinating accommodations and services for students with disabilities.

Final Note: This class is scheduled to meet regularly (read: daily) through the final day of class at noon. Please don't ask permission to miss class or leave early. Life is about choices, and choices have consequences. Since both the choices and consequences are exclusively yours, it is only a decision you can make. Generally speaking, missing a single class can reduce your final grade by a full letter grade. If you miss more than three classes, you can be dropped from the class, IAW college policy. Failure to attend the required course field trip may also result in a NC ("no credit") grade for the class.