

**MICHIGAN BUSINESS SCHOOL  
ANN ARBOR, MI 48109-1234**

**FINANCE 503  
FALL B 2004**

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**FINANCIAL MANAGEMENT**

**COURSE OBJECTIVES**

This is the introductory course in Financial Management in the MBA program. Its purpose is to equip students with the basic tools and techniques necessary to be a successful financial manager or a general manager with a good understanding of the basic principles of finance. Consequently, the course is designed with the following specific objectives:

- ❖ To teach the fundamental skills and methods of Financial Management. These skills are vital for most of the positions that students will seek and obtain, regardless of area of concentration or industry.
- ❖ To prepare students for subsequent finance course work and other professional activity at the Michigan Business School.
- ❖ To provide students a base level of sophistication regarding contemporary issues in financial policy and financial management. This will enable them to better understand the role of finance in debates over corporate strategy and public policy.

**COURSE DESCRIPTION**

This course is primarily devoted to the principles of financial valuation. We will first discuss the concept of present value in extensive detail, and then apply the principles of valuation to value (a) real projects (or what is commonly referred to as capital budgeting) and (b) financial securities (stocks and bonds). Since financial decision-making virtually always involves risk and uncertainty, we will then introduce the concept of (beta) risk, and the relation between risk and return. We will integrate our knowledge of cash flows with our understanding of risk to modify capital budgeting techniques. The course will end with an introductory treatment of international issues in finance, specifically the role of international parity conditions in cross-border capital budgeting decisions. Although the concepts of competitive capital markets and market efficiency will not be covered in a separate session, they will be woven in the fabric of the course.

**COURSE PEDAGOGY: THE IMPORTANCE OF PROBLEM SOLVING**

This is a demanding course that will require a lot of hard work, from both you and me. The emphasis of this course will be on **problem solving** and, consequently, I will make a deliberate attempt to introduce each topic with real-life examples. You will also be required to submit several assignments that involve multiple problem-solving exercises. Please note however that problems in the assignments are by design more complex than the examples we will do in class because class time needs to be utilized to explain the concepts. Doing problems soon after the material is covered in class is the best way to learn the material.

We have carefully coordinated both the content and the pace of the course. Since it is important to first acquire the basic concepts and skills of a subject matter before applying them to relatively complex situations, in the first half of the course we will concentrate more on the tools of finance. We will move at a fairly brisk pace and introduce you to several tools, which you will learn to apply within carefully constructed (but realistic) situations presented to you in “number-crunching” oriented assignments, including three cases.

## **COURSE MATERIALS**

The **textbook** for the course is **Corporate Finance** by Ross, Westerfield, & Jaffee (McGraw-Hill, Inc., Seventh Edition, 2005, **ISBN: 0072829206**). In the detailed course schedule, we refer to the textbook as **RWJ**. The purchase of this textbook should be viewed as a long-term investment; it will be a handy reference for many years to come. There is a useful study guide for students that accompanies the textbook: **Student Problem Manual (ISBN: 0072871911)**. This book is not required, but has some useful examples and pointers for understanding the material. It can be purchased separately, or bundled at a discount with the textbook by ordering **ISBN: 0072978627**.

There is a **packet** for this course that you need to purchase at your earliest convenience. This packet contains two types of material. The first is a set of **Chapters** prepared by present and past colleagues of mine at MBS. I will refer to these as **Chaps** in the schedule. The contents of these Chapters form the basis of all class discussions. The notes will allow you to focus on the ideas discussed in class, rather than having to spend most of the time taking notes. The packet also contains **three cases** that will be used in your assignments, and discussed in class. Since most of the materials in the packet are copyrighted, you will be charged copyright and printing fees for them.

Except for the textbook and packet, all materials are available at:

<https://ctools.umich.edu/portal?site=1089420030795-1207735>

This web site is meant to be the “one-stop-shopping” place for the course. Please make yourself familiar with the site at your earliest convenience.

All ongoing materials for the course are available by accessing the **Resources Link**.

The **Practice Problems** folder contains **four Practice Sets** that illustrate problems, with solutions, from past assignments and/or exams. These will guide you in your understanding of the workings of the course. The Practice Sets are organized according to the Chapters; I encourage you to carefully review the appropriate Practice Set *before* you attempt the Assignments. The problems in these sets will also give you a fair idea of the nature of the exams. The **Work folder** contains this Course Outline, all assignments, and a brief note containing a Review of Statistics. At appropriate junctures, we will post solutions to the assignments in this folder. **Although the submitted case assignments will also be graded, we will not provide detailed solutions (we never provide case solutions to students in finance classes).**

The web site contains several other links, including the **Schedule Link** that provides a detailed course schedule. Also familiarize yourself with the **Assignments Link**; you will be accessing assignments *and* submitting your answers electronically. Finally, all ongoing announcements and information will be made available on the web site.

I would like to also include some brief thoughts/advice about general reading that will help you appreciate the “goings on” in the real world on a regular basis. Since many of you may have had limited exposure to Finance, it is important to read “institutional material” at your own convenience. Subscribe to the *Wall Street Journal*, including its electronic version. Please cruise the web as often as possible not only to uncover the wealth of information at your disposal, but to also “learn” how things work. A good web site to begin your search is <http://finance.yahoo.com>. We will talk about more sophisticated sites in class.

## FINANCIAL CALCULATORS AND SPREADSHEETS

I will use a **financial calculator** to illustrate the logic and steps involved in making day-to-day financial calculations. I will use an **HP 10BII** to do so only because it is one of the cheaper financial calculators. You may choose to use any calculator you want, as long as it has financial functions. However, it is your responsibility to be familiar with all financial functions on your calculator. I do not want to spend class time covering alternative ways of calculating the same numbers on different calculators. The HP 10BII, and all calculators for that matter, come with very useful handbooks—you are advised to review these during the first week of classes. I have placed a short document titled **HP10BII** in the **Work folder** under the **Resources Link**; it lays out some very basic stuff that will help you work with the calculator. Though it is primarily your responsibility to familiarize yourself with the financial functions as well, most relevant financial functions will be covered in class. A final, but important, thought is in order. Although financial calculators are convenient devices to internalize the concepts and use them in many practical situations, they are limited both in scope and number-crunching ability. So I urge you to use **spreadsheets** extensively since they are very useful tools in conducting analyses in any (or every) business application.

**Please bring your financial calculators to class.**

## COURSE REQUIREMENTS AND EVALUATION

You will be evaluated over the seven-week period based on a set of assignments and examinations.

## ASSIGNMENTS

**PLEASE USE THE ASSIGNMENT LINK ON THE WEB SITE TO ACCESS AND SUBMIT ASSIGNMENTS. THE SUBMISSION DEADLINE IS THE ALSO INDICATED HERE. LATE PAPERS WILL NOT BE ACCEPTED!**

**The assignments for this course are quite intense.** We will have **seven** assignments. Please work on all assignments in teams of no less than one and no more than **four** members. We believe that working in teams is extremely valuable because (a) doing so resembles real world situations where analysis and decision-making is done in teams, and (b) open discussions will help team members to better understand the issues. **Each team should submit only one paper for grading.**

The assignments are designed to help students grasp new concepts covered in class. **By design, the problems in the assignments are more difficult than examples presented in class.** I believe you will better understand the concepts by thinking through the issues involved in solving these problems. **Moreover, I may ask you to solve a limited number of problems before we discuss the relevant concept(s) in class.** I impose this burden on you because I believe it will result in a more thorough understanding of the material to be discussed in class. The cases involve the use of spreadsheets to solve integrative problems in finance to give you a chance to immediately apply concepts covered in class to relatively complex real life situations.

## EXAMINATIONS

Apart from the assignments, there will be **two exams** during the course of the seven weeks: one **mid-term** exam, **M**, and a **final** exam, **F**. Each exam is **closed book**, but you will be allowed to bring an 8x11 sheet of paper with any information you want to write on both sides. You will also be allowed to use a financial calculator, but **no laptops will be permitted**. Although both exams will involve “number-crunching,” their main goal is to test your understanding of the concepts. You will therefore not need spreadsheets. The Assignments, on the other hand, will be heavy on number-crunching.

## COURSE EVALUATION

Due to the many time constraints imposed on you at MBS, I have designed a flexible grading scheme for this course. Under this scheme, you will get points on assignments whenever you submit them, but you will not be heavily penalized if you skip an assignment, submit a partial assignment, or get partial credit on one. Specifically, we will calculate the course grade as follows.

## ASSIGNMENTS

Each of the **seven** assignments has a maximum of **four points**. Thus, you can earn any number of points, call it **H**, between **zero** and **28** on the assignments.

## EXAMS

The mid-term and the final examinations will each have 100 points. Suppose you get **M** points on your mid-term examination and **F** points on your final examination, your overall grade on all the exams taken together, **E**, will be

$$E = 0.40M + 0.60F.$$

The weight on the final exam is higher because it is **cumulative**.

## COURSE GRADE

Recall that **H** denotes the total points you earned on your assignments, and **E** is your overall exams' grade.

Your course grade, **C**, is given by

$$C = H + (1 - H/100)*E.$$

Note that if you get 100 on each of your exams (and it has happened, albeit very rarely), your course grade will be 100; the assignments cannot harm you. Conversely, if you get less than 100 on the exams, any points that you get on your assignments will result in a higher course grade.

To see how this works, consider the following two hypothetical situations:

**Student A:** Gets 25 points on assignments, 75 on the midterm, and 50 on the final. Her course grade is 70.00.

**Student B:** Gets 15 points on assignments, 85 on the midterm, and 80 on the final. Her course grade is 84.70.

Note that Student B's weak performance in assignments is outweighed by her really good performance in the exams. On the other hand, Student A does not do as well because her really good performance in the assignments is not repeated in the exams. This comparison suggests that you will not be penalized heavily for not handing in a perfectly executed assignment, each and every time. I would nevertheless encourage you to try and work through all the assignments because it is a reliable way of learning the material and performing well on exams. If you do not have time to complete an assignment, my advice is that you submit what you have and get back to the remaining parts at a later date.

I want to make one last point about grades. In marginal cases I will increase the course final grade by one grade for students who actively contribute to the success of the class during the semester by, for example, asking and/or answering questions in class. However, it is the quality (as opposed to the quantity) of your participation that matters.

## **COURSE ADMINISTRATION**

### **CLASS REPRESENTATIVES**

I propose that each section nominate a couple of students to serve as class representatives to facilitate discussion of course related issues between all of you and me. While students can and do approach me with their individual feedback, concerns and/or difficulties, my experience is that at times there are more general issues that the class as a group would like to discuss that individual students feel reluctant to raise.

### **HONOR CODE**

Following the MBS Honor Code, all assignments are to be done by group members only. Exams are to be done individually. Moreover, since instructors of other MBA classes may distribute past assignments, I have decided to clarify my position on your use of past assignment, handouts, and exams. Please do not consult other current or past students of mine on assignment-related issues, and do not refer to previous materials that I or other instructors may have distributed to former or current students, including assignments and solutions, sample exams, and exams.

### **CLASS SCHEDULE**

F503 - 001	T, TH	10:20 am - 12:40 pm	K1310
F503 - 003	T, TH	2:10 pm - 4:30 pm	E0540

I strongly encourage you to come to class on time and during your section's scheduled slot. If, due to an unusual circumstance, you need to attend an alternative section of mine, please email me in advance.

### **OFFICE HOURS**

I encourage you to **use email** to communicate with me about any issues relating to the class. I will respond to your emails promptly. I will also hold office hours according to the following schedule:

**Mondays, Wednesdays, 11:00 am – 12:30 pm, in D6213.**

If you need to schedule another time, please e-mail me to make an appointment at a mutually convenient time.

## **TEACHING ASSISTANCE**

Our experience has shown that at times you need clarification of the concepts covered in class. While I encourage you to contact me should such a need arise, some of you find it more productive to talk to another person. We have therefore arranged for Teaching Assistants, who will conduct public tutoring sessions on a regular basis throughout the semester. The timing and classrooms for the tutoring sessions are indicated in a document titled **Tutor Schedule** in the **Work folder** of the **Resources Link**. Due to scheduling issues, the room(s) in which the tutoring is held changes often; please make sure you have consulted the Tutor Schedule before showing up for a session.

## **REVIEW SESSIONS**

Since the class time will be devoted to a wide array of essential concepts, we will not always have time to do detailed problems or to repeat concepts. I will therefore hold **two** review sessions during the seven-week period, each a few days prior to an exam. These sessions will be geared toward students who need to revisit fundamental concepts and/or need to understand and internalize the problem-solving approach integral to this course. We will determine the timing of the review sessions during class.

## **DETAILED SCHEDULE**

A detailed schedule of the course is attached herewith. Classes are held over six weeks in two 120-minute periods per week. For clarity of topics and coverage, the schedule lists 24 sessions, i.e., two one-hour sessions per period separated by a 15-minute recess. The detailed schedule is also available on the course web site, under the **Schedule Link**.

**TOPICS and READINGS**

**NOTE: WE EXPECT STUDENTS TO READ RELEVANT MATERIALS BEFORE CLASS!**

<b>Day-Date-Hour</b>	<b>Topic</b>	<b>Chap.</b>	<b>RWJ Ch.</b>	<b>Assignments and Notes</b>
Tue - 11/2-1	Introduction	1	1	
Tue - 11/2-2	Time Value of Money: PV & FV for Single Cash Flows	2	4	<i>Familiarize yourself with your Financial Calculator. Read the short note on HP10BII.</i>
Thu - 11/4-1	Time Value of Money: PV & FV for Multiple Cash flows	2	4	
Thu - 11/4-2	Time Value of Money: PV & FV for Multiple Cash flows (Cont.)	2	4	
Tue - 11/9-1	Capital Budgeting Under Certainty: Competing Capital Budgeting Criteria	3	6	<i>Assignment 1 is due at MIDNIGHT of 11/9.</i>
Tue - 11/9-2	Capital Budgeting Under Certainty: Competing Capital Budgeting Criteria (Cont.)	3	6	
Thu - 11/11-1	Capital Budgeting Under Certainty: Competing Capital Budgeting Criteria: Problems with IRR	3	6	
Thu - 11/1-2	Practice of Cash Flow Estimation: General Principles	4	7	
Tue - 11/16-1	Practice of Cash Flow Estimation: Working Capital & Inflation	4	7	<i>Assignment 2 is due at MIDNIGHT of 11/16.</i>
Tue - 11/16-2	Practice of Cash Flow Estimation: A Comprehensive Example	4	7	
Thu - 11/18-1	Case Discussion – Columbia Alloys			<i>Assignment 3 is due at MIDNIGHT of 11/18. Groups should be prepared to present case analysis in class.</i>
Thu - 11/18-2	Project Interactions: Optimal Timing of an Investment	5	7	
<i>Mon - 11/22 (4:30 – 6:30 pm)</i>	<b>MIDTERM</b> <i>(Section 001: Hale, Section 003: D1270)</i>			<i>Covers all book chapters, notebook chapters, class discussions, and assignments associated with classes held till (and including) 11/18.</i>

<b>TOPICS and READINGS</b>				
<b>NOTE: WE EXPECT STUDENTS TO READ RELEVANT MATERIALS BEFORE CLASS!</b>				
<b>Day-Date-Hour</b>	<b>Topic</b>	<b>Chap.</b>	<b>RWJ Ch.</b>	<b>Assignments and Notes</b>
Tue - 11/23-1	Project Interactions: Different-Lived Projects	5	7	
Tue - 11/23-2	Security Valuation: Bonds	6	5	
<b>Thu - 11/28</b>	<b>THANKSGIVING BREAK. HAVE FUN!</b>			
Tue - 11/30-1	Security Valuation: Equity	6	5	<i>Assignment 4 is due at MIDNIGHT of 11/30.</i>
Tue - 11/30-2	Security Valuation: Equity with Growth	6	5	
Thu - 12/2-1	Security Valuation: Equity with Growth, Comprehensive Example	6	5	
Thu - 12/2-2	Risk and Diversification	7	9	Read <i>Review of Statistics</i> .
Tue - 12/7-1	CAPM	8	10	<i>Assignment 5 is due at MIDNIGHT of 12/7.</i>
Tue - 12/7-2	Capital Budgeting with Risk	9, 10	12, 13	<i>Chapter 10 of the Notebook, and Ch. 13 of RWJ will not be covered in class.</i>
Thu - 12/9-1	Case Discussion – Pioneer Petroleum			<i>Assignment 6 is due at MIDNIGHT of 12/9. Groups should be prepared to present case analysis in class.</i>
Thu - 12/9-2	International Finance: Parity Conditions	11	31	
Tue - 12/14-1	International Finance: Capital Budgeting	11	31	
Tue - 12/14-2	International Finance: Capital Budgeting, A Comprehensive Example	11	31	<i>Assignment 7 is due at MIDNIGHT of Friday, 12/17.</i>
<b>Thu - 12/21/04 (10:30 am – 12:30 pm)</b>	<b>Final</b> <b>(Section 001: D1276, Section 003: D1279)</b>			<i>Comprehensive final covers all book chapters, notebook chapters, class discussions, and assignments.</i>