Kellogg School of Management  
Northwestern University  
Finance 440 “Turbo Finance”  
Fall Quarter 2005  

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Course Description

Finance 440 combines the material of Finance 430 and Finance 441 into an intensive one-quarter course that provides an introduction to the major topics in the field of finance, with an emphasis on valuation and corporate finance principles.

Texts and Supplementary Materials

Required:  

Case Packet (contains Course Notes, articles, answers to recommended problems in B&M, and old exams.)

In addition to the Course Notes, a copy of the overhead slides for each lecture will be available on the course Web page. You should download these slides before each class, as they will greatly reduce the need to take notes.

Supplementary readings and other material also will be posted on the course Web page. You should bring your nameplate to each class, and have it out throughout the quarter.

Recommended:  
There is a handout in the case packet entitled Using Financial Functions in Excel, by Prof. Korajczyk. It is important to learn how to do these financial calculations on a spreadsheet, such as Excel. If you have a financial calculator and know how to use it, this can also be helpful, but it is not required.

For newcomers to finance, an introduction (such as Kenneth Morris and Alan Siegel, The Wall Street Journal Guide to Understanding Money and Investing, Fireside, 1999) may provide a helpful overview of financial markets and instruments.

Copeland, Koller, and Murrin, Valuation -- Measuring and Managing the Value of Companies, Wiley, 1994 (Brought to you by McKinsey and Company, this book on capital budgeting integrates finance and accounting in a more practical way than you'll find in any textbook, while staying true to the principles of the theory of finance.)
Office Hours

I will announce weekly office hours in class and on the web page when the term starts. If it is not possible for you to make this scheduled time, we can make an appointment (please try organize these at least a day ahead). It is often convenient to make appointments and send questions and/or comments via e-mail.

Review Sessions

The teaching assistant will run weekly review sessions to go over the problem sets and cover additional questions. These are optional and you should attend as you need to. There will be an additional review session before the midterm and the final.

Grading

The first day of class, each student will receive a card requesting some biographical data. It should be returned at the end of class; completing and returning the card is worth 2 points.

There are two exams; the midterm is worth 30% of your grade and the final is worth 44% of your grade. The midterm is a free option -- if it doesn't help your grade, 74% of the grade will be based on the final, which is cumulative. Requests for reconsideration of grading must be submitted in writing within a week of when the exam is returned. If a regrade is requested, the entire exam will be re-evaluated. I cannot discuss an exam for which a regrade will be requested, since the regrade (like the exam) must be based entirely on your own work.

*The Kellogg Honor Code strictly applies. Exams must be completed independently and within the allotted time. Only the specifically allowed materials may be used and nothing else. On the homework you can consult with any other class members and refer to class materials, except that answers to previous years’ problems are off limits.*

There are four graded homework assignments (three problem sets and a final problem with a valuation case), some requiring the use of a PC and spreadsheet program; each is worth 6 points (6% of your grade). The assignments may be submitted by groups of up to five; working on the homework in groups is highly recommended.

Assignment due dates are non-negotiable – in the interest of fairness and as required by the honor code, all students should face the same set of deadlines. If you foresee a problem, let me know immediately. To summarize:

\[
\text{final score} = \text{Bio Card} + \text{PS #1} + \text{PS #2} + \text{PS #3} + \text{PS #4/Valuation Case} + \max[\text{midterm} + \text{final}, \text{final} \times 1.682]
\]

The recommended problems from Brealey, Myers and Allen are very helpful in absorbing the material and preparing for the exams, but they will not be graded. Answers to the recommended problems are included in the case packet. Copies of the instructor's manual (with answers to all problems) and study guide for Brealey, Myers, and Allen are on reserve in the library.
**Course Outline and Assignments**

This is an approximate schedule of the topics that will be covered, recommended problems, and assignment due dates. This course moves very quickly. To keep up, it is essential that you complete the assigned readings prior to class, and that you work the practice problems along the way. Note that all the recommended problems refer to the "Practice Questions" section in Brealey, Myers, and Allen unless otherwise stated. "*" denotes optional readings.

**Topic 1: Introduction to Present Value Concepts and Value Maximization**  
Sept 22  
*Reading:  Chs. 1, 2, 3*  
*Course Notes #1*  
*Practice Questions: Ch. 2: 1, 3, 4; Ch. 3: 1, 2, 3, 7-11, 16, 17, 23*

**Topic 2: Risk and Return I: Diversification and Portfolio Choice**  
Sept 29  
*Reading: Chs. 7, 8*  
*Course Notes #2*  
*Great Expectations* (The Economist)  
*Practice Questions: Ch. 7: 3-5, 8, 10; Quiz 4 & 7, plus Challenge Question #1*  
*Ch. 8: 1, 3, 8, 11*  
*Problem Set #1 due at beginning of class Thursday, October 6*

**Topic 3: Risk and Return II: The CAPM and Capital Budgeting Under Uncertainty**  
Oct 6  
*Reading: Chs. 9, 10*, 11*  
*Course Notes #3*  
“How High a Hurdle?” (The Economist)  
*Practice Questions: Ch. 9: 2, 7, 10, and Challenge Question #2*

**Topic 4: Capital Budgeting and Security Valuation Under Uncertainty**  
Oct 13  
*Reading: Chs. 4, 5, 6, 12.4*  
*Course Notes #4*  
"The Real Key to Creating Wealth," (Fortune),  
“AT&T Uses Shareholder Wealth as a Guide to Strategy" (Planning Review)  
*Practice Questions: Ch. 4: 8, 11, 16; Ch. 5: 1, 3, 4, 5;*  
*Ch. 6: 10, 11, 13, 14, 16, 17, 19*  
*Problem Set #2 due at the beginning of class Thursday, October 20*

**Topic 5: Market Efficiency and Review for Midterm**  
Oct 20  
*Reading: Ch. 13*  
“Teaching Note on Market Efficiency”  
“Are Markets Efficient?” (The Wall Street Journal)  
“Behavioral Finance” (forthcoming in the Handbook of Judgment and Decision Making)*  
“The Motives and Consequences of Debt-Equity Swaps and Defeasances: more evidence that it does not pay to manipulate earnings” (Journal of Applied Corporate Finance) *  
*Practice Questions: Ch. 13: 3, 5-8 and Challenge Question #1*  
*The Take-home Midterm is due by 5 pm Friday, October 28*
Topic 6: Derivative Securities
Oct 24  Reading:  Chs. 20, 21, 22
Course Notes #6
Teaching note on “Valuing Loan Guarantees”
“The Options Approach to Capital Investment”* (Harvard Business Review)
Practice Questions:  Ch. 20: 2, 9, 12, 16; Ch. 21: 2; Ch. 22: 1

Topic 7: The Term Structure of Interest Rates (with Futures & Forwards), and Financing in Perfect Markets: Modigliani-Miller
Oct 31  Reading:  Chs. 23, 24.1, 27.1 - 27.3, 28.1 – 28.2*
Ch. 16 (focus on 16.5, perfect markets, for now), Ch. 17
Course Notes #7a & 7b
“A Guide to Investing in U.S. Treasury STRIPS” (AAII Journal)
Practice Questions:  Ch. 27: 5-6; Ch. 23: 4, 6-8, 10, Quiz #5;
Ch. 16: 3, 5, 7;  Ch. 17: 1, 5, 7, 11-12, Challenge Question #2
Problem Set #3 due at the beginning of class Thursday, November 10

Topic 8: Dividends and Payout Policy
Nov 7  Reading:  Ch. 16
Course Notes #8
“Using Capital Structure to Communicate with Investors: The Case of CUC International” (Journal of Applied Corporate Finance) *
“Payout Policy in the 21st Century”, Brav, Graham, Harvey, & Michaely 2004*
Practice Questions:  Ch. 16: 8, 11, 13

Nov 14  Reading:  Ch. 18
Course Notes #9a
“Debt and Taxes” (The Journal of Finance)
Practice Questions:  Ch. 18: 1, 8-9

Topic 9b: Capital Structure Policy II: The Interaction of Investment and Financing Decisions
Nov 21  Reading:  Chs. 19, 26*
Course Notes #9b
Practice Questions:  Ch. 19: 4, 6-8, 11

Topic 10: Raising Capital and Issuing Securities
Dec 1  Reading:  Chs. 14, 15*, 25*
Course Notes #10
Problem Set #4/ Valuation Case due at the beginning of class Thursday, December 1

Final Exam: Tuesday, December 6, 12 noon – 2:00 pm

“*” denotes optional readings
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