



Northwestern University

Finance 935 (AMP III)
Winter 2013
Wednesday, 6:30 pm – 9:30 pm

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Asset Management Practicum III - Syllabus

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This is the third quarter of a four quarter sequence in asset management, of which the first three quarters (AMP I, II, and III) are required and the fourth (AMP IV) is optional. This course provides students both a theoretical foundation and practical experience in the management of investment portfolios. Students in the Asset Management Practicum are responsible for managing a portion of the University's endowment portfolio, which is currently divided into four funds (Commingled, Crown, Kenney, and Nash). The equity portions of the funds follow strategy based on the fundamental security analyses of students in the class. Three of the funds allow short positions as well as long positions, whereas the fourth fund (Nash) is long only. The funds allow the use of quantitative strategies as overlays to the fundamental analyses.

Information about the course is available at the course **Blackboard** site with the title "Kellogg Asset Management Practicum." The Blackboard site is for all four sections of the AMP and so contains a significant amount of material. All assignments will be posted on the Blackboard site (under "AMP III – Winter 2013"). All class presentations (stock pitches, research papers) are posted on the website (Under "COURSE DOCUMENTS").

Office hours: I am available by appointment. If you would like to set up an appointment, please email me at phillip-braun@kellogg.northwestern.edu.

There are three enclosures for this syllabus:

- 1. Winter 2013 AMP Schedule*
- 2. Winter 2013 AMP Grading Structure*

Overview of AMP III:

The ramifications of most portfolio management decisions are only understood over time and through market cycles. Therefore, students registering for Asset Management Practicum I (FINC 933) in the spring of 2011 must also register for Asset Management Practicum II and III (FINC 934 and 935) in the fall of 2011 and winter 2013. Students who have completed Asset Management Practicum III have the **option** of registering for Asset Management Practicum IV (FINC 936 or FINC 936C) in the spring of 2010.

- **Attendance:** Students are expected to attend all class sessions
- **Honor Code:**

All students enrolled in the Asset Management Practicum must abide by the Kellogg Honor Code. If you are unsure of what this means, read the honor code:

http://www.kellogg.northwestern.edu/stu_aff/policies/honorcode.htm

Most of the formal assignments in the Practicum are individual assignments. You may discuss ideas and issues for your assignment with other member of the class, but the final work product must be your original work.

- **Code of Ethics and Plagiarism Policy**

Please review the *Practicum Code of Ethics* and the *Practicum Plagiarism Policy* documents that you signed last spring before the first AMP class, thereby agreeing to abide by the Code of Ethics throughout the Practicum. Deliberate or “accidental” plagiarism will not be tolerated by the Kellogg AMP. Direct quotations as well as paraphrases of others’ work must be cited properly and direct quotes must be enclosed in quotation marks.

Student Responsibilities:

Investment committee members (portfolio managers)

- *Investment committee assignments are in the winter 2013 AMP Funds enclosure.*
- Investment Committee members are responsible for managing the fund’s portfolio and ensuring that the portfolio is in compliance with the Investment Policy Statement. Managing the portfolio includes making decisions on whether to take a position in a security and, if so, how large a position, as well as when to add to a position, decrease a position, or close out a position, including ETFs. Investment Committee members meet at least weekly to make such determinations.
- Investment Committee members report on the fund’s activities to the class on a weekly basis (see **Attachment I**) and to the Advisory Board on an annual basis.
- Investment committee members will assist in evaluating analyst recommendations and are welcome to present equity analyses of their own.
- Investment committee members will request the execution of trades using the AMP Trade Order Request Form (on the course website in spreadsheet form).

Each trade order request should be emailed to all AMP instructors and the fund’s trader.

- **Traders** are responsible for determining the optimal trading strategies in order to minimize the implementation shortfall due to order execution; advising portfolio managers on the appropriate execution strategies; and devising pre-trade estimates and post-trade evaluation of execution costs. Traders must be familiar with trading procedures (e.g., Radical at ITG, our executing broker, and Goldman Sachs, our prime broker) and must maintain a cumulative record of trades as outlined in the trade data spreadsheet (on the course website in excel form).

Copies of the trade data spreadsheet must be emailed to the portfolio managers requesting the trade as well as to:

- r-korajczyk@kellogg.northwestern.edu
 - phillip-braun@kellogg.northwestern.edu
 - l-vincent@kellogg.northwestern.edu
- **Traders** and their shadows should read the research reports by Kim (F '09) "AMP Trading Tutorial," Hennegan and Stott (F '08) "A Primer on Trading Costs & Methods for AMP Funds," Brusznicki and Rangaswami (W '08) "A Process Oriented Approach to Measure Trading Costs," and Carlson and Qiao (F'07) "A Study on AMP Funds' Trading Costs and Trading Venues." The reports are on the course website.

Analysts.

- AMP III students who are assigned the role of analyst are responsible for making at least one stock pitch and one stock update to the class during the quarter.
- Students select the stock to be pitched from their assigned industries (see **Attachment II**). The schedule for the stock pitches is provided below in the syllabus and the requirements for the stock pitch, similar to previous quarters, are provided in **Attachment IV**.
- AMP III analysts are responsible for following and updating one stock during the quarter.
- Which stock analysts will follow will be determined during the first week of class. The portfolio managers must arrange a meeting with the instructor within the first few days of the quarter to determine what stocks will be followed and updated during the quarter. Analysts will then be assigned a stock and will be informed of what stock they will monitor and update by their respective portfolio managers and via an update of this syllabus.
- **Attachment II** contains guidelines as to what "following" entails.
- Analysts are also assigned to their previous investment committee. Analysts should attend the investment committee meetings and understand the rationale for the portfolio positions.

Class Organization:

Guest speaker, stock pitches, research reports. We will begin with a guest speaker, student stock pitches, or student research reports. A detailed schedule is below.

Stock updates. Following the stock pitches and research reports will be updates on stocks that are currently held in the portfolio; a schedule for these updates is provided below. Volunteers are also encouraged. Next, current students who have pitched stocks are encouraged to provide updates on their pitches regardless of whether any portfolio currently holds the stock.

Portfolio updates. Each class will end with an update by each investment committee on the fund's performance, including:

- the positions in the portfolio
- the performance and risk profile of the portfolio
- trades made since the last class
- when appropriate (that is, when we have had stock pitches), the basis for decisions on the previous week's stock pitches.

Specific requirements and suggestions for the content of the update are provided in **Attachment I** of this syllabus.

Speaker dinners. Visiting speakers are invited to dinner before class from 5:15-6:15. If you do not have a class ending at 5:00, try to be there at 5:00, otherwise be there by 5:15. For each speaker, up to 10 students may attend the dinner. We have three dinners scheduled for the winter quarter: the speakers and their date will be announced in the first class. If you wish to attend any of these dinners, please email Deborah Brauer (d-brauer@kellogg.northwestern.edu).

Grading:

Because the first three quarters of the course are meant to be taken as an integrated whole, students will receive formal course grades for FINC 933, 934, and 935 at the completion of the sequence. **All quarters are weighted equally in determining the sequence grades.**

Completion of co-requisites: if a student does not complete the four course co-requisites by the end of the year-long sequence (AMP I, II, III) then a one letter-grade reduction will be imposed for each course deficit. (Students who have scheduling issues should discuss options with the instructor.)

A more extended discussion of grading policies is available on the Course Blackboard site under "Course Information"/"AMP Grading Policies."

Please see the enclosure on grading for the grading structure for winter 2013

Research Topics for Paper:

Trading: Traders need to present a short report on the cost of trading for the funds. In addition, they can choose to either write a research paper on trading or a research paper in an additional area. Possible trading topics are (1) The costs and benefits of different types of orders (2) should AMP be considering dark pools as trading venues? (3) Should AMP be concentrating trades at particular times of the day?

Quantitative Overlay Strategies: Should AMP be considering quantitative strategies as overlays to the fundamental analysis done in the stock pitches?

Analyst Performance Measurement: Perform a historical analysis of the risk-adjusted performance of analyst recommendations. What is the relation between analyst target prices and subsequent returns? What is the relation between class target price expectations and ranges and subsequent returns and risk?

Asset Allocation: Develop and test a specific model designed to guide PMs choice of market exposure.

Feedback on Stock Pitches, Research Reports, and Guest Speakers

After each class, you will receive an email directing you to an online survey for the class presentations. You will have two days (48 hours) to complete the survey for stock pitches/research reports. The short time period is due to two reasons. First, with respect to stock pitches, the Investment Committees generally meet before the end of the week and should have access to the stock pitch evaluations for use in their deliberations. Second, the best evaluations were provided shortly following the presentation when the information and impressions were fresh.

For stock pitch presentations, you will be asked to provide numerical and qualitative evaluations that will be given to the analyst (without attribution). Thoughtful written comments are more valuable than the numerical score and the comments will receive more weight in the participation grade. Comments lacking substantive feedback (e.g., “good presentation!”) will receive the same grade as no comment.

Textbooks and References

Recommended Texts:

Maginn, John L., Donald L. Tuttle, Jerald F. Pinto, and Dennis W. McLeavey, *Managing Investment Portfolios: A Dynamic Process*, 3rd edition. Hoboken: Wiley, 2007.

Litterman, Bob, *Modern Investment Management: An Equilibrium Approach*. New York: Wiley, 2003.

Rappaport, Alfred, and Michael J. Mauboussin, *Expectations Investing*. Boston: Harvard Business School Press, 2001.

Bodie, Zvi, Alex Kane, and Alan J. Marcus, *Investments*, 7th edition. New York: McGraw-Hill, 2008.

Attachment I

Requirements for Weekly Portfolio Updates by Investment Managers

The three AMP investment committees should present weekly reports on the risk and performance of the four funds. The report is due each Wednesday the class meets. The report should include, at a minimum:

- A statement of the committee's chosen target asset allocation. This should include an analysis of cash versus equity, market capitalization of the fund's holdings, and exposure to "Value" and "Growth" styles.
- Total return on the fund: since inception (April 11, 2007); calendar year to date; calendar quarter to date; and any other period of your choice. Compare these returns to the benchmark return. All of these returns can be obtained from the "Performance: Fund Performance" section of the Goldman web site.
- An analysis of each position's contribution to the fund's performance. This can be obtained from the "Performance: Security Performance" section of the Goldman web site.
- A graph of the Risk Decomposition Chart from the MSCI Barra Aegis Portfolio Manager as of the previous Friday.
- A graph of the Active Risk Index Exposures and Active Industry Exposures from the MSCI Barra Aegis Portfolio Manager as of the previous Friday.
- A check of adherence to all of the fund's restriction as outlined in the current Investment Policy Statement (please use the BARRA estimated beta rather than the Goldman computed beta because the BARRA beta is forward looking rather than historical).
- An analysis of the risk-adjusted performance of the fund using Barra's Performance Analyst.

An electronic version of this report should be emailed to all class members, the instructors, and Debbie Brauer (this can be accomplished through the Blackboard website via the Email tab and then – Send Email – All Users) by 5:00 PM on class days.

Attachment II

Stock Pitch Guidelines and Requirements

Analysts choose the company on which they make stock recommendations (long or short) from the industry group or groups to which they are assigned (the assignments are the same as Fall quarter and are provided in **Attachment II**). Because we are making recommendations for investments, the goal is to choose a stock for which a **buy** or **sell** (short) recommendation can be made. Hold recommendations should be avoided.

A fundamental analysis should include, at a minimum:

- 1) an analysis of the firm's business and its industry, including its strategy and the competitive landscape
- 2) an analysis of the firm's financial condition including profitability, balance sheet, and cash flow generation
- 3) a forecast of the firm's future performance structured as pro forma financial statements with well-articulated assumptions about the key value drivers
- 4) a DCF valuation of the firm based on the financial projections

Additionally, we encourage students to reach out to representatives in the firm or one of the firm's competitors.

The stock pitch analysis comprises two parts. The first is a written report with supporting exhibits, the equivalent of a sell-side analyst's report, providing an in depth analysis of the company and the bases for the recommendation. Included in this written report, in excel format, must be a complete set of pro forma financial statements for the firm as well as a DCF valuation analysis. Additional analyses may be provided but the pro forma financial statements and DCF valuation analysis are required. The analyst should specify the assumptions behind the pro forma financial statements and provide both sensitivity analysis and scenario analysis when appropriate.

Analysts have generally provided a Word or PDF document for the report and the pro forma financial statements in a separate Excel document. Make sure that any Word or PDF documents have a title page with your name, date and the name of the company being pitched. It is important that the pro forma financial statements be in excel format, not PDF, so students in the class can trace the analyses and even do their own sensitivity analysis if desired. To that end, the spreadsheets should be formatted so that they can be printed easily by the class members.

The report and spreadsheets **must** be emailed to all class members (this can be accomplished through the Blackboard website from the Email tab– Send Email – All Users) by **9 am on the Monday before the Wednesday presentation**. All students are expected to read the report and study the spreadsheet financials before class. The report must contain all of the substantive information and analyses for the stock pitch.

The second component of the analysis is a set of power point slides for presentation to the class. Because all students will have read the report before class, the purpose of the power point slides is not to educate the audience of potential investors but rather to emphasize the main points and the recommendations from

the written report. The power point presentation must be emailed to all class members (using the Blackboard procedure) by **3 pm on the day of the presentation**. Again, make sure that the PowerPoint presentation has a title page with your name, date and the name of the company being pitched.

All students and faculty will provide a written evaluation (electronically on a form provided – see **Attachment III**) of the stock pitch, assessing the quality of the written report and of the oral presentation. The key considerations are the quality and effectiveness of the stock pitch and whether the evaluator would support the recommendation made in the stock pitch for the AMP funds. The written evaluations consist of numerical scores for several portions of the evaluation and written comments to support those scores.

The stock pitches will be broadcast via WEBEX to the AMP's Board of Advisors and interested alumni who may ask questions of the presenter. Analysts should bring their pitches to class on a memory stick/flash drive because they must use the laptop computer attached to the WEBEX system for the presentation.

Attachment III

Stock Pitch Evaluations

The procedure for evaluating the stock pitches will be similar to that of Fall Quarter. After the pitch, all members of the class will receive a link to a website with the evaluation form. The evaluations are due by **5 pm of the Friday** following the stock pitch presentation.

Although the focus is on being constructive, positive comments such as “good pitch” may be considered supportive but they lack the information content to make them constructive. Why was it a good pitch? What in particular distinguished the pitch? What was compelling about the pitch? Comments such as “presenter really seemed to know the business” are likewise not sufficiently informative. How was this knowledge demonstrated? What did you find convincing about the presentation? Would you recommend implementing the buy or sell recommendation? Why or why not? What recommendations can you make for improving the structure and effectiveness of the stock pitch?

The numerical scores are important but the most valuable element of the evaluation to the person presenting the pitch is the written section of suggestions for improvement.

Attachment IV

Updates on Portfolio Holdings

The portfolio managers will assign each analyst stocks to “follow.”

Following the stock involves making recommendations to the investment committee about continuing to hold the stock, purchasing more of the stock, reducing the position, or closing out the position.

The assigned analyst should review the original stock pitches (generally posted on the course website) in order to understand the original investment thesis.

An initial update on the stock should be made to the class (5 – 10 minutes in length) which would include the stock’s performance since its addition to the portfolio and performance relative to the pitch’s target price and target date. The portfolio managers provided a summary of each of the stocks in the portfolios for this meeting. The presentation to the class should be more detailed than this summary but cover the same basic points.

The analyst should keep abreast of new developments with respect to the stock that could affect the recommendation in the future—for example, earnings announcements, management changes, regulatory issues, etc. The analyst should communicate these updates via an email to the class, summarizing the recent development and providing any change in recommendation as a result. However, if there is a potentially important change, a short presentation (5 – 10 minutes) to the class is warranted. An invitation to provide updates on the existing positions will be made at the beginning of each class.

Attachment V

Research Reports

The portfolio managers will present the research reports during the last class of the quarter. Research reports from prior quarters are posted on the course website and we strongly urge you to review those papers as they provide some excellent suggestions and implementable procedures for managing the AMP portfolios. They may also provide assistance in developing a topic for future research reports. In some instances, it may be possible to expand and extend a previous research report.

Please make an appointment to discuss the topic and design of your research report with the instructor as soon as you have some thoughts and ideas about it.

Presentations and Q&A should be approximately 45 minutes (e.g., 30 minutes for the presentation and 15 minutes for Q&A). The reports are due the Monday before the presentation class and should be sent to the class via Blackboard. Presentation slides should be sent to the class via Blackboard by 5:00 PM the day of the presentation. Again, make sure that the presentation has a title page with your name and date on it.