



## THE UNIVERSITY OF WESTERN AUSTRALIA

### Accounting and Finance Discipline

### Advanced Investments FINA7481

### Course Outline

### Semester 1, 2009

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**Lectures:** What a muddle 2009 has turned out to be. The lectures are currently scheduled to be held in the Conference Room on the third floor of the Economics and Commerce building (the old building). If we can get better accommodation, we will.  
There will be a lecture at 10 am each Tuesday and Thursday. A detailed timetable may be found towards the end of this document.

<b>Assessment :</b>	1. Revision exam (2 hours):	20%
	2. Mid-semester exam (1 hour):	10%
	3. Statistical exercise	10%
	3. Final exam (4 hours):	60%

**The revision exam (2 hours) will be held in class on Tuesday, March 3rd. All of the readings from 2008 will be examinable (the list is attached at the end of this outline).**

**The mid-semester exam (1 hour) will be held in class on Thursday, April 2<sup>nd</sup>.**

**The statistical exercise is to be submitted at the beginning of the lecture on Tuesday, April 21<sup>st</sup>.**

**The final exam will be held on Saturday, June 6<sup>th</sup> (noon to 4pm).**

The revision exam will cover the material you are expected to have read (or learned how to read) in Investment Analysis; it will consist of **2 essays**. I trust that having a revision exam so early in the semester will convince you that, at this level of study, we are serious when we assume that you have mastered the material in earlier years. The list of readings, which are those included in the curriculum for *Investment Analysis* in 2008, may be found in the attachment to this document.

If something exceptional and beyond your control has interfered with your ability to study in the normal way you should consider completing an application for special consideration. The forms can be obtained at the Business School Student Centre or Postgraduate Reception Desk, or from the Student Administration website <http://www.studentadmin.uwa.edu.au/welcome/forms>

In exceptional circumstances you can also apply for a deferred mid-semester exam or a deferred end of semester/trimester exam within three (3) university working days from the date of the exam. Application forms can be obtained at the Business School Student Centre or Postgraduate Reception Desk.

A student may be granted a deferred examination in one or more of their units if the Sub-Dean of the UWA Business School is satisfied that on the basis of medical or other exceptional reasons the candidate was either:

- substantially and unusually hindered in their preparation for an examination; or
- unavoidably absent from or unable to complete an examination.

Further information concerning Special Consideration and Deferred Examinations is available on the Business School website <http://www.business.uwa.edu.au/studentnet/assessments>

### **Prerequisite**

- 1) Investment Analysis Investment Analysis FINA3324 (the course formerly known as 460.324) or equivalent.
- 2) A moderate ability in basic statistics (econometrics) will make your life comfortable. While knowledge beyond basic statistics of (at least) Economic and Business Statistics will not be assumed, students will be on a steep learning curve as we revise and introduce concepts that are required to adequately understand the material we need to cover. Damodar Gujarati's Basic Econometrics (Third edition, Mc-Graw-Hill, New York, 1995) is an old favourite that students have benefited from reading.
- 3) In particular, **you must be familiar with the ideas presented in** Fama's two seminal papers (which you surely must be familiar with from your previous reading) and the preliminary reading in your course reader:
  - Fama, E.F., 1970. Efficient Capital Markets: A Review of Theory and Empirical Work", *The Journal of Finance* 25, 383-417.
  - Fama, E.F., 1991. Efficient Capital markets: II, *Journal of Finance* 46, 1575-1617.

The better you remember Investment Analysis, and the better you understand statistics, the better you will do in Advanced Investments.

### **Textbook**

Advanced Investments is based on articles published in leading Finance journals; they will be available from the bookshop in the first week of semester (before Thursday). I will bring along a copy of the first reading to the first lecture. A complete list of *all* of the articles will also be provided to you in class; sadly, due to the confusion involved in moving buildings, typing this is a low priority at the moment.

### **Additional reading (strongly recommended)**

**You should re-read** the following sections from Durand (compiler) FINA3324 Investment Analysis (Pearson, 2008):

1. pages 1 to 61 before beginning the course;
2. pages 277 to 400 before February 26<sup>th</sup>;
3. pages 64 to 153 before March 24<sup>th</sup>.

### **Additional reading (recommended where required)**

Other books that may be useful will be available in the closed reserve of the library. They are:

1. **Finance** (Elsevier, Amsterdam, 1995) edited by R.A. Jarrow, V. Maksimovic and W.T. Ziemba. An excellent overview of Finance as it stood in the mid-1990's written by the leading experts in their fields. This will fill in many of the gaps that I may leave. Indeed, I expect that you will find this book so valuable that you will look at it every week to see if the material we're covering is covered in it.
2. **The Econometrics and Financial Markets** (Princeton University Press, Princeton, N.J., 1997) by John Y. Campbell, Andrew W. Lo and A. Craig MacKinlay. This book has useful (though, perhaps in some cases, dated) discussions of many of the econometric techniques you will encounter. You may find aspects of this book difficult.
3. **Asset Pricing** (Princeton University Press, Princeton, N.J., 2001) by John Cornell. This is particularly daunting in parts but it contains excellent technical discussions of many of the topics we cover. I am told that it has been adapted from notes from a particularly fearsome second year doctoral course at the University of Chicago. While technically very good, the author has an unfortunate fixation for examples featuring Happy Meals.
4. **Beyond Greed and Fear: Understanding Behavioral Finance and the Psychology of Investing** (Harvard Business School Press, Boston, Mass., 2000) by Hersh Shefrin is a good introduction to Behavioural Finance (and may indeed be the only introduction to Behavioural Finance). I really like this book but student reviews have been mixed. I think it may be a generational thing. Anyway, you're going to get a good dose of Behavioural Finance so you need to come to terms with it; this book may help.
5. **Inefficient Markets: An Introduction to Behavioral Finance** (Oxford University Press, Oxford, 2000) by Andrei Shleifer is more advanced than Shefrin's offering and equates "introduction" with the material he has been involved in preparing. A very useful volume as the author has worked on many seminal papers in the field.

### **Ethical Scholarship, Academic Literacy and Academic Misconduct**

Ethical scholarship is the pursuit of scholarly enquiry marked by honesty and integrity.

Academic Literacy is the capacity to undertake study and research, and to communicate findings and knowledge, in a manner appropriate to the particular disciplinary conventions and scholarly standards expected at university level.

Academic misconduct is any activity or practice engaged in by a student that breaches explicit guidelines relating to the production of work for assessment, in a manner that compromises or defeats the purpose of that assessment. Students must not engage in academic misconduct. Any such activity undermines an ethos of ethical scholarship. Academic misconduct includes, but is not limited to cheating, or attempting to cheat, through:

- Collusion
- Inappropriate collaboration
- Plagiarism
- Misrepresenting or fabricating data or results or other assessable work
- Inappropriate electronic data sourcing/collection

- Breaching rules specified for the conduct of examinations in a way that may compromise or defeat the purposes of assessment.

Penalties for academic misconduct vary according to seriousness of the case, and may include the requirement to do further work or repeat work; deduction of marks; the award of zero marks for the assessment; failure of one or more units; suspension from a course of study; exclusion from the University, non-conferral of a degree, diploma or other award to which the student would otherwise have been entitled. Refer to the Ethical Scholarship, Academic Literacy and Academic Misconduct located on the University's website at

[http://www.teachingandlearning.uwa.edu.au/tl4/for\\_uwa\\_staff/policies/student\\_related\\_policies/academic\\_conduct](http://www.teachingandlearning.uwa.edu.au/tl4/for_uwa_staff/policies/student_related_policies/academic_conduct)

### **Learning Outcomes**

Advanced Investments extends material introduced in your undergraduate Finance courses (notably, Investment Analysis FINA3324 - formerly 460.324 - or the equivalent).

We focus on equity markets and address the three “big questions” of investment finance:

1. Why do returns vary through time?
2. Why do returns differ between portfolios?
3. Are markets efficient?

These “big questions” were also at the core of Investment Analysis FINA3324; in this course, we pursue these questions in greater depth.

On completion of this unit, you should be able to:

- appraise and integrate the papers studied in Advanced Investments;
- evaluate the reasoning and empirical analyses of the researchers' whose papers we study in Advanced Investments;
- evaluate proposed answers to the three “big questions” posed in Advanced Investments; and
- appraise and criticize advanced research in Investment Finance.

"THROUGH me you pass into the city of woe:  
Through me you pass into eternal pain...  
All hope abandon ye who enter here."  
Such characters in colour dim I mark'd  
Over a portal's lofty arch inscrib'd...

DON'T PANIC!

Dante Aligheri, The Divine Comedy

Douglas Adams, The Hitchhiker's Guide to the Galaxy

The structure of the course is as follows:

Week	Date	Topic
1	<b>Tuesday, February 24, 2009</b>	<i>Introduction</i>
	Thursday, February 26, 2009	<i>Behavioural Finance</i>
2	<b>Tuesday, March 03, 2009</b>	Preliminary exam (2 hours)
	Thursday, March 05, 2009	
3	<b>Tuesday, March 10, 2009</b>	<i>Behavioural Finance (cont.)</i>
	Thursday, March 12, 2009	
4	<b>Tuesday, March 17, 2009</b>	<i>Experimental and clinical studies in Behavioural Finance</i>
	Thursday, March 19, 2009	
5	<b>Tuesday, March 24, 2009</b>	<i>Return predictability</i>
	Thursday, March 26, 2009	
6	<b>Tuesday, March 31, 2009</b>	
	Thursday, April 02, 2009	Mid-semester exam (1 hour)
7	<b>Tuesday, April 07, 2009</b>	
	Thursday, April 09, 2009	
8*	<b>Tuesday, April 21, 2009</b>	<i>Fama and French's three-factor model</i>
	Thursday, April 23, 2009	
9	<b>Tuesday, April 28, 2009</b>	<i>Risk and return</i>
	Thursday, April 30, 2009	
10	<b>Tuesday, May 05, 2009</b>	<i>Liquidity</i>
	Thursday, May 07, 2009	
11	<b>Tuesday, May 12, 2009</b>	<i>Momentum</i>
	Thursday, May 14, 2009	
12	<b>Tuesday, May 19, 2009</b>	<i>Conclusion</i>
	Thursday, May 21, 2009	

## Results

The results of this unit may be scaled in accordance with Faculty guidelines.

In the first instance, students are strongly advised to talk informally to the lecturer about the grade awarded. The University provides the opportunity for students to lodge an appeal against any mark which he or she feels is unfair. Any student making an appeal is under an obligation to establish a prima facie case by providing particular and substantial reasons for the appeal. It is recommended that students contact the Guild Education Officers to aid them in the appeals process.

There is a 20 day time limit for making any such appeal. An appeal against academic assessment may result, as appropriate, in an increase or decrease in the mark originally awarded. The University regulations relating to appeals and the form on which the appeal should be lodged can be found at

<http://www.secretariat.uwa.edu.au/home/policies/appeals>

Robert Durand.  
February 13<sup>th</sup>, 2009

## Appendix. Investment Analysis Reading List 2008

- i. Fama, E.F., 1970. Efficient Capital Markets: A Review of Theory and Empirical Work. *Journal of Finance* 25, 383-417.
- ii. Fama, E.F., 1991. Efficient Capital Market II. *Journal of Finance* 46, 1575-1617.
- iii. Gaunt, C., Gray, P., McIvor, 2000. The impact of share price on seasonality and size anomalies in Australian equity returns. *Accounting and Finance* 40, 33-50.
- iv. Huberman, G., Regev., T., 2001. Contagious Speculation and a Cure for Cancer: A Nonevent that Made Stock Prices Soar. *Journal of Finance* 56, 387-396.
- v. Lee, D.D., Chan, H., Faff, R.W., Kalev, P.S., 2003. Short-term contrarian investing – is it profitable?...Yes and No. *Journal of Multinational Financial Management* 13, 385-404.
- vi. Elton, E.J., Gruber, M.J., Spitzer, J., 2006. Improved Estimates of Correlation Coefficients and their Impact on Optimum Portfolios. *European Financial Management* 12., 303-308.
- vii. Fama, E.F., French, K.R., 2004. The Capital Asset Pricing Model: Theory and Evidence. *Journal of Economic Perspectives* 18, 25-46.
- viii. Gaunt, C., 2004. Size and book to market effects and the Fama French three factors asset pricing model: evidence from the Australian stockmarket. *Accounting and Finance* 44, 27-44.
- ix. Durand, R.B., Limkriangkrai, M., Smith, G., 2006. In America's thrall: the effects of the US market and US security characteristics on Australian stock returns. *Accounting and Finance* 46, 577-604.
- x. Zaretsky, K., Zumwalt, J.K., 2007. Relation between distress risk, book-to-market ration and return premium. *Managerial Finance* 33, 788-797.
- xi. Seyhun, H.N., 1986. Insiders' Profits, Costs of Trading, and Market Efficiency. *Journal of Financial Economics* 16, 189-212.
- xii. Barber, B., Lehavy, R., McNichols, M., Trueman, B., 2001. Can Investors Profit from the Prophets? Security Analyst Recommendations and Stock Returns. *Journal of Finance* 56, 531-563.
- xiii. Barber, B., Lehavy, R., Trueman, B., 2001. Comparing the Stock Recommendation Performance of Investment Banks and Independent Research Firms, *working paper*.
- xv. Durand, R.B., Koh, S.W., Ng, H.G., 2003. From gold to silicon. *Journal of Multinational Financial Management* 13, 273-286.
- xvii. Ibbotson, R.G., Kaplan, P.D., 2000. Does Asset Allocation Policy Explain 40, 90, 100 Percent of Performance? *Financial Analysts Journal* 56:1, 26-33.
- xviii. Faff, R., Gallagher, D.R., Wu, E., 2005. Tactical Asset Allocation: Australian Evidence. *Australian Journal of Management* 30, 261-282.
- xix. Gorjaev, A., Zobotkin, A., 2006. Risks of investing in the Russian stock market: Lessons of the first decade. *Emerging Markets Review* 7, 380-397.
- xxi. Jun, S-G., Marathe, A., Shawky, H.A., 2003. Liquidity and stock returns in emerging equity markets. *Emerging Markets Review* 4, 1-24.
- xxii. Froot, K.A., Dabora, E.M., 1999. how are stock prices affected by the location of trade? *Journal of Financial Economics* 53, 189-216.
- xxiii. De Bondt, W.F.M., 1998. A portrait of the individual investor. *European Economic Review* 42, 831-844.
- xxiv. Da Silva Rosa, R., Durand, R.B., 2008. The role of salience in portfolio formation. *Pacific-Basin Finance Journal* 16, 78-94.
- xxv. Barber, B.M., Odean, T., 2001. Boys Will Be Boys. Gender, Overconfidence, and Common Stock Investment. *Quarterly Journal of Economic*, 261-292.
- xxvii. Hirshleifer, D., Shumway, T., 2003. Good Day Sunshine: Stock Returns and the Weather. *Journal of Finance* 58, 1009-1032.
- xxviii. Durand, R.B., Newby, R., Sanghani, J., 2008. An Intimate Portrait of the Individual Investor. *Journal of Behavioral Finance*, forthcoming.
- xxix. Ciarlone, A., Trebeschi, G., 2005. Designing an early warning system for debt crises. *Emerging Markets Review* 6, 376-395.