

DARTMOUTH COLLEGE
Department of Economics

Economics 36
Theory of Finance

Professor Samwick
Fall 2008

Course Description:

Economics 36 is an introduction to the fundamental concepts of financial theory and the methods that are used to understand the financial markets and corporate finance. Underlying all of finance is the impact of time and uncertainty on the valuation of economic opportunities. Topics to be discussed include capital budgeting decision of firms, portfolio theory, financial market efficiency, option pricing, and problems of asymmetric or incomplete information.

Prerequisites: Economics 10, 21, and 26; good quantitative skills

Office Hours and X-Periods:

Regular office hours have been scheduled to coincide with the course's two x-periods on Wednesday afternoons to ensure that students have no academic conflicts with their timing. On three occasions, the x-periods will be used as dedicated time to review problem sets. These sessions are optional and are for students in both sections together. In all other weeks, office hours will be held in my Economics Department office, Rockefeller 322. Note that on some occasions, my work at the Rockefeller Center or on College committees require these office hours to be rescheduled. These are noted on the course schedule on the next page of this syllabus.

Course Requirements and Grading:

The course grade is determined as follows:

- 1) Exams: There will be one midterm exam held in class on October 23 and a final exam scheduled for December 6 at 3:00 p.m. The midterm is worth 25 percent and the final exam is worth 40 percent of the course grade. All students are expected to take the exams on the scheduled dates. Any student needing to do otherwise must submit a written request to do so by the end of class on October 8.
- 2) Problem Sets: There will be five problem sets, graded on a scale of 0 to 5 points based on the effort shown to complete all of the problems correctly. Each point earned represents a percentage point of the course grade, up to a maximum of 25 points. All problem sets are due on a Tuesday or Thursday at 4 p.m., as specified on the Course Schedule below. Problem sets may be turned in during the class periods that day or, failing that, at 4 p.m. in my office in the Economics department. Late or illegible problem sets will not be accepted.
- 3) Class Participation: Regular attendance and positive contributions to classroom discussions account for the remaining 10 percent of the course grade.

Required Readings:

Brealey, Richard A., Stewart C. Myers, and Franklin Allen. *Principles of Corporate Finance*. 9th ed. (New York: McGraw Hill, Inc., 2008). [Chapters marked as B# on Course Outline]

Journal Articles [Marked as J# on Course Outline, Posted to Blackboard Page]

[1] Shleifer, Andrei and Lawrence H. Summers, "The Noise Trader Approach to Finance," *Journal of Economic Perspectives*, Vol. 4, No. 2 (Spring 1990): 19-33.

[2] Bernheim, B. Douglas and Adam Wantz (1995). "A Tax-Based Test of the Dividend Signaling Hypothesis," *American Economic Review*, Vol. 85, No. 3, 532-551.

Other Articles as assigned and posted to the course blackboard page.

Other Readings (Not Required but Very Good):

Malkiel, Burton G. (1999). *A Random Walk Down Wall Street*. New York: Norton. (Available electronically at: <http://libcat.dartmouth.edu/record=b3097580>)

Shiller, Robert J. (2005). *Irrational Exuberance*. Princeton: Princeton University press.

Buffett, Warren. *Letters to Shareholders*. <http://www.berkshirehathaway.com/letters/letters.html>.

Additional Information:

Class Meetings: Rockefeller 2, TTh 10:00 – 11:50 a.m. (x-period W 3:00-3:50 p.m.) and TTh 2:00 – 3:50 p.m. (x-period W 4:15 – 5:05 p.m.) Students may occasionally attend the other section to accommodate their schedules. However, students must take the midterm exam on October 23 during their assigned class period unless prior permission is given.

Class Materials: Course materials are accessible to students at www.dartmouth.edu/~blackboard.

Honor Principle: All exams will be closed-book, closed-note, and timed. Any student giving or receiving assistance during an exam violates the Academic Honor Principle. Studying and doing problem sets with classmates is encouraged. When there is collaboration on problem sets, each student must submit his or her own set of solutions and must acknowledge collaborators on the first page of the solutions.

Equal Access: Students with disabilities enrolled in this course and who may need disability-related classroom accommodations are encouraged to make an appointment to see me before the end of the second week of the term. All discussions will remain confidential, although the Student Accessibility Services office may be consulted to discuss appropriate implementation of any accommodation requested.

Religious Observances: Some students may wish to take part in religious observances that occur during this academic term. If you have a religious observance that conflicts with your participation in the course, please meet with me before the end of the second week of the term to discuss appropriate accommodations. To accommodate my own religious observances, classes on 9/30 and 10/09 have been moved to the X-periods those weeks (10/01 and 10/08, respectively).

Course Schedule:

Date	Topic	Readings (to be done in advance when possible)	Problem Sets (Must be turned in by 4 p.m.)
Th 9/25	Introduction; Present Value	B 1-3	
W* 10/01	Valuing Bonds and Stocks	B 4-5	
Th 10/02	Using the NPV Rule	B 6-7	
T 10/07	Portfolio Theory	B 8	#1 Due
W* 10/08	The Capital Asset Pricing Model	B 9	
T 10/14	CAPM Tests and Alternatives	B 9 (cont.)	
Th 10/16	Project Analysis & Capital Budgeting	B 10	
T 10/21	Catch up and Review		#2 Due
W* 10/22	Review of Problem Sets #1 and #2		
Th 10/23	MIDTERM EXAM		
T 10/28	Efficient Markets	B 14	
Th 10/30	Noise Trading and Herd Behavior	J 1	
T 11/04	Initial Public Offerings	B 15-16	
Th 11/06	Dividends	B 17, J 2	
T 11/11	Capital Structure and Financial Distress	B 18-19	#3 Due
W* 11/12	Review of Problem Set #3		
Th 11/13	More Financial Distress		
T 11/18	Understanding Options	B 21	#4 Due
Th 11/20	Simple Option Pricing	B 22.1-2	
T 11/25	More Complicated Option Pricing	B 22.3-6	
T 12/02	Real Options	B 23	#5 Due
W* 12/03	Review of Problem Sets #4 and #5 Additional Review During Reading Period		
Sa 12/06	FINAL EXAM at 3 p.m. [Cumulative, emphasizing second half of course]		

When problem set reviews are scheduled for the x-periods, there will be no separate office hours that week.

Adjustments to the Schedule not shown in the table above:

- 10/01: Regular office hours moved to Monday afternoon, 3:00 – 4:00, 09/29
- 10/08: Regular office hours moved to Monday afternoon, 3:00 – 5:00, 10/06
- 10/29: Regular office hours moved earlier to 2:30 – 4:30.
- 11/12: Problem Set Review will end early, 3 – 4:30.
- 11/19: Regular office hours moved to Monday afternoon, 11/17.