

**C15.0002002**  
**Foundations of Financial Markets**  
SUMMER 2010  
June 29, 2010 to August 5, 2010

**Instructor**

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Office Hours: Wednesday, 2:00 - 3:30 pm, in KMEC 9-193

**Class Time and Location**

Tuesdays and Thursdays 12:00 - 2:55 pm

**Description of the Course**

This is the first course in finance for most students, and it gives an introduction to financial markets. We will learn the basics of financial securities, how they are valued and traded, and how to make optimal investment decisions with these securities. The main topics are portfolio selection, equilibrium asset pricing, arbitrage, fixed income securities, and derivatives. The course is rigorous and quantitative. Students are expected to understand and apply quantitative methods. Examples illustrate important real-world applications of the theory.

A tentative schedule is attached at the end of this document.

**Textbooks**

1. (BKM) Bodie, Kane, and Marcus, “Essentials of Investments”, 7th edition
2. (S) Bodie, Kane, and Marcus, “Solutions Manual to Essentials of Investments”, 7th edition
3. (RWJ) Ross, Westerfield, and Jordan, “Essentials of Corporate Finance”, Custom Edition (includes Chapter 4, 5 and 8)
4. (H) Handouts - distributed in class

**Prerequisites**

Students should be comfortable with statistics, linear algebra and calculus. The course assumes no prior knowledge of finance.

**Assessment (Provisional)**

There will be weekly assignments (problem set and investment game), a midterm exam and a final. The breakdown of the final grade:

Participation	10%
Assignments	20%
Midterm	30%
Final	40%

Details follow.

**Problem Sets:** There will be a problem set assigned during the Tuesday session of each week. It will correspond to material covered that week - on Tuesday and Thursday. The problem set will be due one week from the day assigned and all homeworks should be handed in at the beginning of class. Answers to the problem set must be your own, and must be handwritten. You are encouraged to acknowledge any help you received on the front page of your problem set solution. Late problem sets will not be accepted.

**Investment Game:** We will run an investment game throughout the semester:

- At the beginning of the semester, students should form groups of three or four. Each group will receive (virtual) sum of 10,000 USD and should pick a name for the group.
- During the Thursday session of each week, you will receive a set of "securities" from which you should choose a portfolio.
- On the following Tuesday, you should submit your portfolio choices (with the homework) and explain your decision.
- On the following Thursday, securities payoffs will be realized, and you will receive a new set of "securities".

**Exams:** The midterm exam will be on July 21. The final exam is on August 6. The exams will be based on material taught in class and on homework problems. The final exam is cumulative. You will be allowed one double-sided page of notes for the midterm and two double-sided pages of notes for the final exam. The sheets must be no larger than 8.5 inches by 11 inches. Sample exams will be distributed a few days before the midterm and final.

### *Warning*

The course is intense and quantitative. What students are asked to absorb in a full semester of four months, you will be asked to absorb in a month and a half. You should be prepared to stretch yourself.

## Schedule

(Asterisks indicate key issues)

Note: This schedule is tentative. Readings might be revised as we go through the material,  
Additional handouts will be distributed in class throughout the semester

Class	Topic	Material
1. Tuesday June 29	Introduction and Overview of Investments,	BKM: 1.1-1.5*, 3.1-3.7*, 2.1-2.5
2. Thursday July 1	Time Value of Money and Return Measures	RWJ: 4*, 5.1-5.3*
3. Tuesday July 6	Risk and Return	BKM: 5.1*, 5.2*, 5.3*, 5.5* RWJ: 5.3*
4. Thursday July 8	Diversification	BKM: 6.1*, 6.2*, 6.3*, 6.4*
5. Tuesday July 13	Equilibrium: The Capital Asset Pricing Model	BKM: 6.5*, 7.1*, 7.2, 7.3
6. Thursday July 15	Efficient Market Hypothesis Performance Evaluation	BKM: 8*, 17.1*
7. Tuesday July 20	Midterm Arbitrage	BKM: 7.5
8. Thursday July 22	Equity Valuation	BKM: 12*
9. Tuesday July 27	Fixed Income Securities and Valuation	BKM: 9.1, 9.2, 9.3- 9.4*,9.6*, 10.1*, 10.2, 10.3
10. Thursday July 29	Options Markets and Valuation	BKM: 14.1*, 14.2*
11. Tuesday August 3	Options Markets and Valuation	BKM: 15.1*, 15.2, 15.3*, 15.4
12. Thursday August 5	Final	