

Econ 261- Principles of Finance
Lahore University of Management Science
Department of Economics

Course Instructor: Tareena Musaddiq

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Course Description:

This course introduces the theory and practice of finance to students who are largely unfamiliar with finance. This course explores the first part of Financial Management and introduces the framework, tools and techniques for making Investment decisions. Specifically, we will cover Time Value of Money, Stock and Bond Valuation, Capital Budgeting, Modern Portfolio Theory and Risk-Return Relationship and Dividend and Debt Policy. In addition a brief introduction is given to international financial management. At the end of the course students should have a clear understanding of financing and investment decision and project analysis – making practices required to be an effective manager.

Pre requisite: Microeconomics 1 and Macroeconomics 1, Statistics,

Recommended: Although it is not a pre requisite for this course Principles of Accounting or A levels Accounting is highly recommended

Grading Plan

Quizzes -25%

Mid term-25%

Final Exam-35%

Project/Presentation-15%

There will be 5 quizzes over the entire semester and the best 4 will be counted. **There will be no makeup quizzes.**

Reading Material:

Brealey, Myers & Marcus, 2004 (International Fourth Edition), “Fundamentals of Corporate Finance”, McGraw-Hill Irwin

Session No	Topics	Readings
1	Introduction to the course An Introduction To Finance The firm and the financial manager An Overview Financial Environments. (Capital Markets & Corporate Finance.); An Introduction to Financial Markets, Financial Institutions and Financial Instruments. Consumption Savings & Investment,	BMM Ch 1&2
2,3,4	Accounting and Finance; Balance Sheet; Income Statements & Cash Flow Statements; Taxes Ratio analysis and DuPont	BMM Ch 3 & 17
5	Time Value Of Money Compounding & Discounting; Future and present value	BMM Ch 4
6 Quiz 1	Perpetuities and Annuities; Various Application of TVM; TVM as Basis Of Valuation of Financial Instruments, Effective interest rate; Inflation and real interest rate	BMM Ch 4
7 & 8	TVM and Bond Valuation Bond Characteristics; Basic Valuation Model; Bond Prices and Yields; Different Types of yields;	BMM Ch 5
	Valuation -Valuing Bonds Bond Prices and Interest Rates: Price Volatility: Price Sensitivity; Bond Duration and Convexity	
9 and 10 Quiz 2 in session 10	Valuation – Stocks Different Type of Stocks and markets they are traded in; Some Stock Classifications. Book Value and Market Value;Dividend Discount Models and Other Models	BMM Ch 6
	Valuation -Valuing Bond & Stocks DDM with constant growth ; Intro to technical and fundamental analysis; Puzzles in stock valuation	BMM Ch 6

Session No	Topics Body of Knowledge	Readings Book & Handouts
11 and 12	Investment Criteria; Net Present Value. NPV; Other Investment Criteria(IRR, payback); Mutually Exclusive Projects; Capital Rationing	BMM Ch 7
13	Discounted Cash Flow Analysis DCF; Sunk Costs and Opportunity Costs; Discount Nominal Cash Flow by Nominal Cost of Capital; Separate Investment and Financing Decision; Calculating Cash Flows.	BMM Ch 8
14 Quiz 3	Project Analysis How Firms organize the Investment Process; Sensitivity Analysis and Scenario Analysis; Accounting Breakeven Analysis; Operating Leverage and Financial Leverage; Real Options	BMM Ch 9
15	Mid term	
16	An Introduction to Risk and Return Risk and Return Basics; Opportunity Cost of Capital; A Review of Rate of Return; Measuring Risk; Risk and Diversification; Different Varieties of Risks.; Expected Risk & Return	BMM Ch 10
17	An Introduction To Portfolio Theory Risk and Return , Portfolio of Risky and Risk less Assets; Efficient Frontiers; Capital Market Line;	BMM Ch 10
18	An Introduction to Assets Pricing Measuring Market Risks; The CAPM Model; Beta and Security Market Line; Use of CAPM for Estimating and Calculating Risk, Company vs Project Risk	BMM Ch 11
19	Cost of Capital Weighted Average Cost Of Capital; Measuring Capital Structure; Calculating Required Rate of Return; Calculating and Interpreting the Weighted Average Cost of Capital; Beta levering and re levering	BMM Ch 12
20 & 21 Quiz 4 in session 21	Debt Policy MM Proposition 1 and 2, Tax shield, Financial distress costs, WACC and debt financing, Pecking Order theory	BMM Ch 15
22	Dividend Policy	BMM Ch 16

	Cash vs. Stock Dividends, Dividend irrelevance proposition, Tax clienteles, Signalling mechanism of dividends	
23	International Financial Management Exchange rates, Purchasing Power Parity, Interest Rate Parity, Spot and Forward Rates	BMM Ch 23
24 & 25	Options Introducing derivative securities, Call options, Put Options, Protective Put, Covered Call	BMM Ch 24
26, 27 28	Presentations and quiz 5	