

NORWEGIAN SCHOOL OF ECONOMICS AND BUSINESS ADMINISTRATION

AFA Module 6

ASSET PRICING AND PORTFOLIO MANAGEMENT

Friday August 26 – Sunday August 28, 2011

Place: Vika Atrium Konferansesenter, Oslo

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COURSE DESCRIPTION

The overall goal of this intensive 3-day course is to help students develop a way of thinking about and quantitatively frame investment decisions. The course discusses market efficiency, basic theory of portfolio selection, mean-variance efficient portfolios, capital asset pricing (two-fund) theory, arbitrage pricing theory (multifactor pricing), empirical identification of pervasive risk factors, fund performance evaluation, and some basic market micro-structure issues. The course uses a combination of lecture notes, discussion of journal articles, and exercises.

COURSE READINGS

Bodie-Kane-Marcus (BKM) is the main textbook for this course. It provides a comprehensive overview of the investment field. The most relevant chapters from this book are listed in the detailed session description below. Students should begin reviewing these chapters prior to the start of the module in August:

Bodie, Zvi, Alex Kane and Alan J. Marcus, 2011, **Investments and Portfolio Management**, Global Edition (9th ed). (McGraw-Hill/Irwin), ISBN 978-007-128914-6 (BKM)

Students must also read the 2009 report on the performance of Norwegian Sovereign Wealth Fund, by professors Andrew Ang, William Goetzman, and Stephen Schaefer. It's available on It's Learning and <http://www.regjeringen.no/upload/FIN/Statens%20pensjonsfond/rapporter/AGS%20Report.pdf>

Professor Eckbo provides students with his lecture notes, in a compendium which will be handed out at the beginning of the module in August. This compendium also contains the research articles listed in the session description below. The research articles are also available on It's Learning.

The textbook, the SWF report, and the lecture note compendium, constitute compulsory readings for the course. Students are also encouraged to discuss current events/investment news in class.

**ASSET PRICING AND PORTFOLIO MANAGEMENT
SCHEDULE**

Friday, August 26: Efficiency, Portfolio Theory, and Trading Costs

- Session 1, 10:00 – 12:00: **Market Efficiency and Behavioral Finance**
Lunch 12:00 – 13:00
- Session 2, 13:00 – 14:00: **Costs of Active Investing**
Coffee break 14:00 – 14:15
- Session 3, 14:15– 16:00 **Basic Portfolio Theory**

Saturday August 27: Asset Pricing Theories

- Session 4, 09:00 – 10:30: **Capital Asset Pricing Model**
Coffee break, 10:45 – 11:00
- Session 5, 11:00 – 12:00: **The Arbitrage Pricing Theory**
Lunch 12:00 – 13:00
- Session 6, 13:00 – 14:45 **Asset Pricing: Empirical Tests**
Coffee break 14:45 – 15:00
- Session 7, 15:00 – 16:00: **Exercises**

Sunday August 28: Portfolio Management

- Session 8, 09:00 – 10:30 **Portfolio Performance Evaluation**
Coffee break, 10:30 – 10:45
- Session 9, 10:45 – 12:00: **Active Fund Management**
Lunch, 12:00 – 13:00
- Session 10, 13:00 – 14:30: **Performance of Insider Trades and IPO Stocks**
Coffee break 14:30 – 14:45
- Session 11, 14:45 – 16:00: **SWFs and Hedge Funds**

**ASSET PRICING AND PORTFOLIO MANAGEMENT
SESSION TOPICS AND READINGS**

DAY 1: Efficiency, Portfolio Theory, and Trading Costs

Session 1: Market Efficiency and Behavioral Finance

- Efficiency and no-arbitrage
- The efficient amount of inefficiency
- “Behavioral” finance

BKM chapter 11, 12

Session 2: Costs of Active Investing

- Fund types
- The zero-sum game
- Costs of active investing

BKM chapters 1, 2, 3, 4

French, Kenneth R., 2008, “The Cost of Active Investing”, *Journal of Finance* 63, 1537-1573.

Session 3: Basic Portfolio Theory

- The magic in portfolios
- Efficient portfolio frontier
- Total versus marginal risk

BKM chapters 5, 6, 7, 8

DAY 2: Asset Pricing Theories

Session 4: Capital Asset Pricing Model

- Assumptions about investors and markets
- Equilibrium asset pricing (CAPM)
- Relaxing model assumptions

BKM chapter 9

Session 5: The Arbitrage Pricing Theory

- Law of one price
- Factor premiums
- Factor mimicking portfolios

BKM chapter 10

Session 6: Asset Pricing: Empirical Tests

- Key empirical implications of asset pricing theories
- CAPM anomalies
- The cross-section of expected stock returns

BKM chapter 13

Fama, Eugene F. and Kenneth R. French, 2004, "The Capital Asset Pricing Model: Theory and Evidence", *Journal of Economic Perspectives* 18, 25-46

Fama, Eugene F. and Kenneth R. French, 1996, "Multifactor Explanations of Asset pricing Anomalies", *Journal of Finance* 51, 55-84

Session 7: Exercises

DAY 3: Portfolio Management

Session 8: Portfolio Performance Evaluation

- Performance measurement pitfalls
- Mutual fund performance
- The zero-sum game - again

BKM chapter 24, 25

Wermers, Russ, 2000, “Mutual Fund Performance: An Empirical Decomposition into Stock-Picking Talent, Style, Transactions Costs, and Expenses”, *Journal of Finance* 55, 1655-1695

Fama, Eugene F. and Kenneth R. French, 2010, “Luck versus Skill in the Cross-Section of Mutual Fund Alpha Estimates”, *Journal of Finance* 65, 1915-1947.

Session 9: Active Fund Management

- Strategies for active management
- Sryles
- Tilting

BKM chapter 27

Session 10: Performance of Insider Trades and IPO stocks

- Performance measurement with changing portfolio weights
- Performance of insider trades
- Performance of IPO stocks

Eckbo, B. Espen and David C. Smith, 1998, “The Conditional Performance of Insider Trades”, *Journal of Finance* 53, 467-498.

Eckbo, B. Espen and Øyvind Norli, 2005, ““Liquidity Risk, Leverage and Long-Run IPO Returns””, *Journal of Corporate Finance* 11, 1-35.

Session 11: SWFs and Hedge Funds

- Performance of Norway’s SWF
- Hedge fund investments
- Costs

BKM chapter 27

Ackermann, Carl, Richard McEnally, and David Ravenscraft, 1999, “The Performance of Hedge Funds: Risk, Return, and Incentives”, *Journal of Finance* 54, 833-874.

Ang, Andrew, William Goetzman and Stephen Schaefer, 2009, “Evaluation of Active Management of the Norwegian Government Pension Fund – Global” (unpublished).