Course Introduction

Course Instructor and TA

- Course instructor
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- TA
  - Mr Tinglong Cheng; Office: T3-502-R26; Tel.: 3620182
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Office Hours

- Tuesday 16:00-17:50
- Wednesday 14:00-17:50
- Thursday 10:00-11:50, 14:00-14:50, 16:00-16:50

Objectives

- Give an introduction to students on basic concepts and principles of finance.
- Focus on the theoretical aspects of these topics.
- Examine the application of the knowledge learnt from the lectures.

Course Content

- Basic concepts in finance
  - Time value of money
  - Cost of money
  - Risk and return
  - Financial statement analysis
- Financial securities
  - Stock and bond
  - Financial derivatives: options and futures
- Corporate finance
  - Cost of capital
  - Capital budgeting
  - Forecasting

Course Grading

Tasks	Assessment Details	Weighting
Class Participation	To engage students to the coverage of lectures.	**10%**
In-class Exercises	To assess students' ability to identify the relevant concepts and use them to answer questions as well as their ability to apply financial concepts and theories to explain and solve financial and economic problems.	**30%**
Written Assignments	To assess Students' understanding of the knowledge learned and their ability to apply them correctly in different contexts.	**20%**
Final Exam	To see how far students have achieved their intended leaning outcomes especially in the knowledge domain.	**40%**

Class Participation

- Factors include
  - Attendance
    - Attendance checking through iSpace
  - Participation in class discussions

In-class Exercises

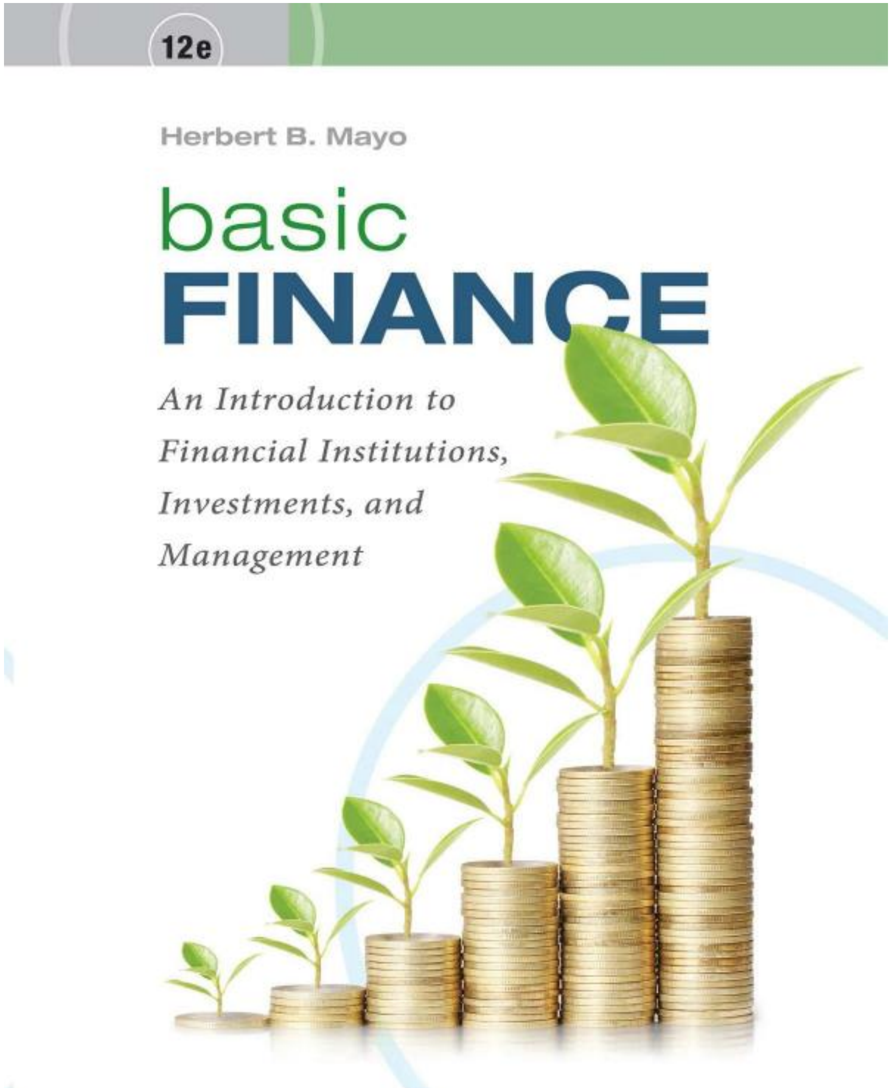
- Quiz (10%) and Mid-term test (20%)
  - Closed book; Closed notes
  - Formula sheet may be provided
  - Normally no make-up quiz or mid-term test will be given
  - Dates will be informed in advance

Written Assignments

- Group project
  - two to four students per group
  - Topic: TBA
  - Report + Presentation
  - Tentative due date of report: 11:59pm on 22 December 2023
  - Tentative presentation arrangement: 5-10 minutes each project in the last week.
  - Marking scheme for report: course instructor + teammate evaluation

Textbook

- Herbert B. Mayo, Basic Finance: An Introduction to Financial Institutions, Investments, and Management (12^{th} Edition), Cengage 2019. (simplified as BF)
- Scott Besley and Eugene F. Brigham, Principles of Finance (6^{th} Edition), Cengage 2015. (simplified as PF)
- Textbook is not compulsory but you are strongly suggested to have one copy.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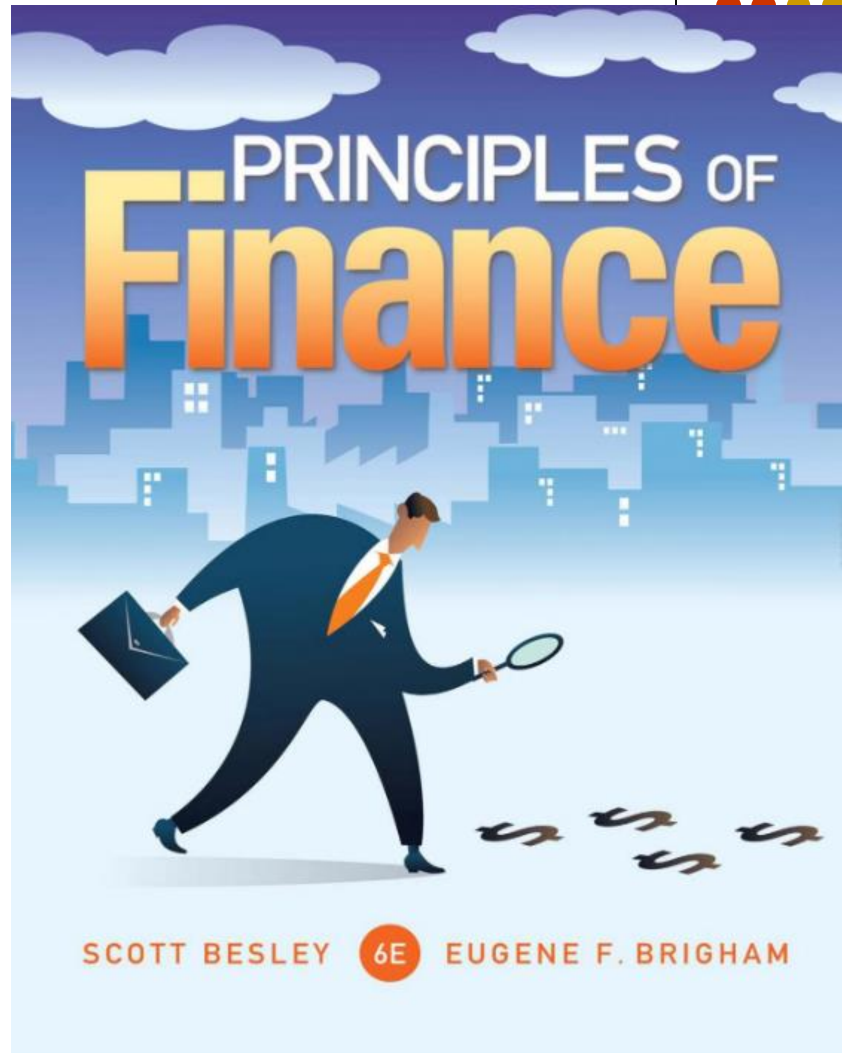
FINANCE
An Introduction to
Financial Institutions,
Investments, and
Management


PRINCIPLES OF
Finance
SCOTT BESLEY
6E
EUGENE F. BRIGHAM

An Overview of Finance

Chapter 1

Outline

- What is finance
- Financial market
- Financial intermediaries
- Investment banking
- Securities markets
- References: BF Chaps 1-4; PF Chaps 1, 3, 4

What is Finance?

- Finance is concerned with decisions about money.
- To make sound financial decisions, remember:
  - More value is preferred to less
  - The sooner cash is received the more value it has
  - Less risky assets are more valuable than risky assets

Divisions of the Finance Discipline

- Institutions
- Investments
- Corporate finance

Key Financial Concepts

- Sources of finance
  - Debt
  - Equity
- Sources of return
  - Income
  - Price appreciation
- Risk
  - The uncertainty that the expected return will not be achieved

Key Financial Concepts (Cont'd)

- Financial leverage
  - The use of borrowed funds
- Valuation
  - determination of what an asset is currently worth
  - goal of management: maximization of shareholder value

Financial Markets

- A system comprised of individuals and institutions, instruments, and procedures that brings together borrowers and savers.

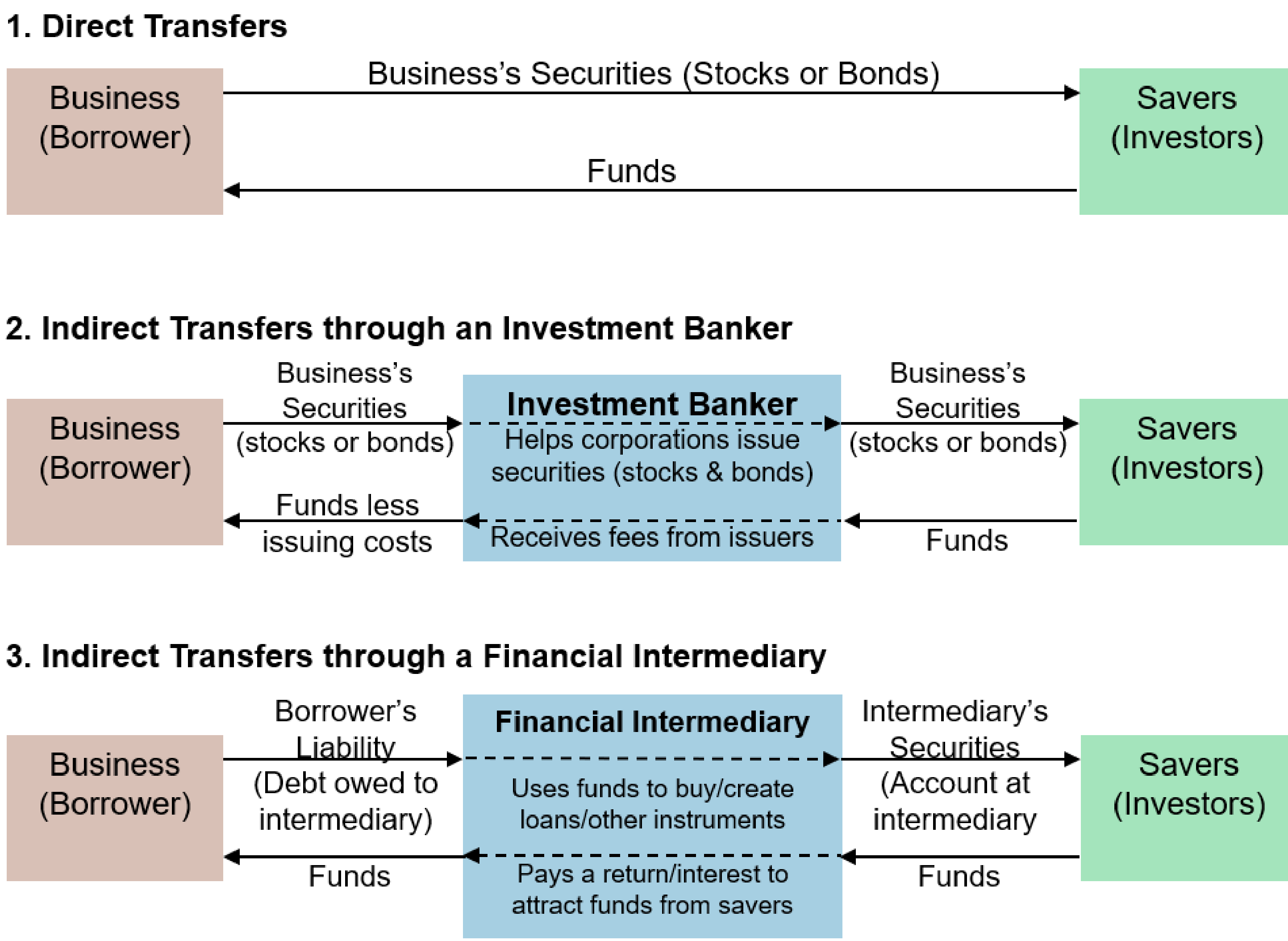
Flow of Funds

- Provides the ability to transfer income through time
  - Borrowing sacrifices future income to increase current income
  - Saving, or investing, sacrifices current income in exchange for greater expected income in the future

Flow of Funds

- Direct transfer
  - Business sells its stock directly to investors
- Indirect transfer through investment bankers
  - Investment banker acts as middleman and facilitates issuance of securities by reselling the securities to savers
- Indirect Transfer through financial intermediary
  - Organizations such as banks or mutual funds obtains funds from savers and then use the money to lend or to purchase securities

Flow of Funds



Benefits of Intermediaries

- Reduced costs
- Risk/diversification
- Funds divisibility/pooling
- Financial flexibility
- Related services

Types of Intermediaries

- Commercial banks
- Credit unions
- Mutual funds
- Life insurance companies
- Pension funds

Types of Financial Markets

- Money markets
  - Instruments traded mature in one year or less (short-term markets)
- Capital markets
  - Includes instruments with maturities greater than one year (long-term markets)

Types of Financial Markets

- Debt markets
  - Loans
- Equity markets
  - Stock markets
- Primary market
  - Corporations raise funds by issuing new securities
- Secondary market
  - Securities are traded among investors after they have been issued

Types of Stock Market Transactions

- Secondary market
  - Trading existing stocks
- Primary market
  - Established firm issues additional shares
- Initial public offering (IPO)
  - Privately held company offers stock to the public for the first time
  - Called “going public”

Investment Banker

- Organization that underwrites and distributes new issues of securities
- Helps businesses and other entities obtain needed financing

Investment Banking Process

- Help corporations design securities with the features that are most attractive to investors given existing market conditions.
- Generally buy these securities from the corporations.
- Then resell the securities to investors (savers).

Securities Markets

- Types of markets:
  - Direct search
    - Buyers and sellers seek each other
  - Brokered markets
    - Brokers search out buyers and sellers
  - Dealer markets
    - Dealers have inventories of assets from which they buy and sell
    - Spreads between dealers' buy/bid prices and sell/ask prices are a source of profit
  - Auction markets
    - Traders converge at one place (physically or electronically) to trade

Types of Orders

- Market orders
  - Executed at the current bid or ask
  - Assured transaction
- Limit orders
  - Specified price
  - Transaction may not occur

Cost of Investing

- Commissions: fee paid to broker for making the transaction
  - Explicit cost of trading
  - Full service vs. discount brokers
- Spread: difference between the bid and asked prices
  - Implicit cost of trading

Trading Mechanisms

- Physical stock exchanges
- Over-the-counter (OTC) market
  - Collection of brokers and dealers connected electronically
  - Provides for trading in securities not listed on the physical and other organized exchanges
- Electronic communications networks (ECN)
  - Electronic systems that transfer information about securities transactions to facilitate the execution of orders
  - Automatically matches buy and sell orders for a large number of transactions

Long and Short Positions

- Long (bullish) position
  - Anticipates prices rising
- Short (bearish) position
  - Anticipates prices falling
- Short sale
  - Sale of borrowed securities
  - Contract for future delivery
  - To close position: purchase the stock and return the borrowed securities

Summary

- Finance is concerned with decisions about money.
- Financial market is a system comprised of individuals and institutions, instruments, and procedures that brings together borrowers and savers.

Summary

- Flow of funds
  - Direct of transfer
  - Indirect transfer through investment bankers
  - Indirect Transfer through financial intermediary
- Types of intermediaries
- Types of Financial Markets
- Types of orders
- Types of positions