



California Polytechnic State University

GSB 501

Managerial Accounting and Managerial Economics
Fall 2008

Instructor information:

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Office Hours: Monday, 1.30-3:30 pm, and Wednesdays, 1.30-3:30 pm, and by appointment

Course Objective:

This course is a faculty generated student research project. As such the student is introduced to academic finance and accounting research. A large part of the course consists of hands on data collection and analysis. We will employ statistical analysis, use commercial databases and write up results very similar to the academic research process. During the course I will also offer a brief introduction to the methods and tools of financial statement analysis and quantitative portfolio management. The course discusses stock screening, relative valuation, and catalytic analysis. At the end of the course, the student should have an introductory tool set to pursue a career in the investment banking field, but is also introduced into the professional life of a Professor at a university.

Research project:

The research we will be working on is a project I plan on submitting to the "Financial Analyst Journal" (see abstract below). In particular, the study would investigate how financial analysts derive long-term earnings growth forecasts for firms they cover, and what role long-term earnings growth forecasts play in the valuation models they use. The contribution of the project would be to: (i) understand the optimistic bias in the long-term earnings growth forecasts, (ii) test market efficiency using abnormal return models exploiting the bias, and (iii) make suggestions in how to reduce the bias, which would benefit academic studies that use long-term earnings growth as a proxy and investors that rely on analyst investment advice. This project would greatly benefit students seeking a position in the investment banking industry as it covers stock market efficiency research and how accounting/finance information are incorporated into equity valuation and forecasts. It would also benefit students interested in forensic accounting and securities litigation work, as the bias in analyst outputs is examined.

Research abstract:

This study investigates the self-selection of analysts' long-term earnings growth (LTG) forecasts. I find that analysts who forecast LTG differ in their ability, characteristics, information environment and incentive structure from analysts who do not forecast LTG. Specifically, I find that analyst's forecasting LTG (i) have higher predictive ability; (ii) more experience, follow fewer firms, and have more resources available; (iii) have more private information; and (iv) worked prior the Regulation period for brokers with underwriter relationships (post Regulation FD these incentives conflicts disappear). Tests of firm characteristics reveal that analysts' selective forecasting behaviour is not dependent on whether firms have (i) high earnings volatility or (ii) high market-to-book ratios. Analysts issuing LTG forecasts tend to pick larger firms with high intangible asset bases. These findings are intriguing as it shows that analysts are more likely to issue LTG forecasts for firms with future growth prospects that cannot be captured by short-term earnings forecasts.

Course Materials:

There is no required text for the course. Required readings are available on the Blackboard site and will include lecture slides, academic research papers, and user guides. In general, these should be read in advance of the class for which they are assigned. Copies of lecture slides, handouts etc. will be made available on the Blackboard website

Grading

Course grades will depend on significant data collection and analysis assignments and a final research project.

Tentative Schedule

Meeting 1 – Wednesday, October 1, 2008, 12-3 pm

- Market efficiency and portfolio management
- Evidence on market efficiency
- Arbitrage trading and efficiency
- Performance measures and benchmarking – alpha and active risk

Meeting 2 – Wednesday, October 8, 2008, 12-3 pm

- Student Managed Fund
- Introduction to stock screening
- Discuss academic literature
- Data collection

Meeting 3 – Wednesday, October 15, 2008, 12-3 pm

Constructing a stock screen
Basic valuation ideas
Empirical evidence on forecasting returns – strategies that have worked
Translating a screen result into alpha

Meeting 4 – Wednesday, October 22, 2008, 12-3 pm

Valuation and catalytic analysis
Applying simple valuation models
Searching for price catalysts – events that move prices
Putting screening and further analysis together – estimating alpha

Meeting 5 – Wednesday, October 29, 2008, 12-3 pm

Data analysis

The rest of the quarter will be used to cover the following research stages:

| Detail of project | Professor's deliverables | Student deliverables | Time commitment |
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| Analysis of financial analyst reports on the use long-term earnings growth forecasts | Give student an overview of research area and importance Specify sample period, sample firms and financial analysts and download reports from Investext database Determine search criteria for data collection | Read some seminal papers in analyst research, and discuss contribution of the project. Read reports and code criteria into sub-categories based on criteria determined in prior research. | Similar to a 4 unit class, the commitment would be <u>5-7 hours a week</u> over the duration of the quarter. The majority of the work would be during <u>Fall quarter 08</u> . |
| Testing the hypotheses using the collected data | Provide econometric models and explain to student how to use statistical and data management software | Arrange data so it can be imported into statistical software, and test the hypotheses based on the theory. The student | This part of the study moves away from data collection, and allows student to <u>go beyond</u> |

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| | | will also have to use data management software (Excel), or based on experience SAS or other programming language to arrange the data and test the hypotheses. | <u>application of knowledge</u> , and rather think critically about learned material. This should be greatly relevant for practice. The time commitment will be <u>4-6 hrs</u> with more emphasis on professor-student discussion. |
| Write up and presentation of results | Tie all the analysis together and guide student through scientific reasoning and writing | Draft of results and presentation in class/ brown bag of results. The student will have to write up the results and draw conclusions from the findings. | The time commitment will get less as student will have to study for exams. However, the presentation of results will take considerable preparation time. |