



BUSINESS SCHOOL
Te Kura Pakihi

FINC460 Advanced Fixed Income Securities

COURSE OUTLINE

Semester Two, 2014

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Paper Description and Aims

The domestic and international fixed income markets account for a large proportion of investable assets as well as of trading volume. A good understanding of theories and tools is necessary for (1) practical valuation of fixed income assets and (2) corporate financial decisions. Hence, in this course the concepts, tools and techniques used to price fixed income securities and interest rate sensitive products at an advanced level are introduced and discussed.

Learning Outcomes

The main objectives of this course are to:

- Provide an introduction to term structure of interest rates.
- Review and synthesize the fundamental themes in fixed-income security research and practice.
- Explore the latest ideas for doing empirical research in fixed-income security.
- Provide opportunities to develop global and interdisciplinary perspectives.
- Provide learning environments where students develop both soft and hard skills required in a finance career.

Upon successful completion of this course, students should be able to:

- Demonstrate the understanding of financial theory pertaining to (1) term structure of interest rate and (2) how to price a range of fixed-income securities.
- Demonstrate the understanding of and skills in valuing fixed-income securities and interest rate sensitive products.
- Demonstrate the understanding and appreciation of critical thinking and lifelong learning.
- Demonstrate the understanding of and skills in writing quality research papers or consulting project reports.
- Demonstrate the ability to present authoritatively a set of ideas in a clear, concise, and professional manner.

Teaching Staff

Paper Coordinator

Name: Dr. Chaiporn Vithessonthi
Office: Room 5.04 Commerce Building
Email: chaiporn.vithessonthi@otago.ac.nz
Office Hours: Tuesday: 14:00-16:00 (by appointment)

You should contact the paper coordinator with any administrative enquiries about the course, e.g. tutorial changes, or requests for late submission of assignments.

Course Delivery

Lecture Day/Time: Tuesday and Thursday / 10:00am-12:00pm

Room: CO536

Tutorials and/or Labs Day/Time: NA

Every week students must attend two 2-hours lectures.

The readings and supportive texts have to be read and prepared before class. During class meeting, I will stress the most important issues addressed in the assigned readings. Therefore, it is important for you to attend classes. As punctuality is very critical in business, you must attend the class on time. Being late and/or missing classes will always have a negative effect on your class participation score. You are responsible for keeping yourself informed of all announcements and changes made in class.

Compulsory readings mainly consist of selected cases, journal articles, and book chapters. Investment or portfolio analysis textbooks are recommended as preliminary and/or supplementary readings for students who did not take any investment/portfolio analysis course at the undergraduate level.

Course Calendar The course calendar (in this outline) details scheduling information. Note that this calendar may change as the course proceeds. Any changes will be announced at lectures and be detailed on Blackboard.

Students are expected to prepare for and attend all classes to gain full benefit from the course

These activities should be prepared for by reviewing information detailed on Blackboard and completing any assigned readings. Students unable to attend a lecture are expected to catch up on missed material. Unless stated otherwise, all aspects of the course are examinable.

Expectations and Workload

Contact Hours:

Lectures: 52 hours

Non-contact Hours:

Preparation for classroom discussion: 30 hours

Preparation for exam: 40 hours

Preparation for case study: 12 hours

Research paper: 60 hours

Research paper presentation: 6 hours

Total contact and non-contact hours: 200 hours

Course Learning Resources

Please see below a list of compulsory readings (cases, books and journal articles).

Books

1. Back, Kerry 2005. *A Course in Derivative Securities: Introduction to Theory and Computation*. Berlin, Germany: Springer-Verlag.
(www.springer.com/mathematics/quantitative+finance/book/978-3-540-25373-0)
2. Britten-Jones, M. 1998. *Fixed Income and Interest Rate Derivative Analysis*.
(<http://www.sciencedirect.com/science/book/9780750640121>)

Cases are from Kester, C.W., Ruback, R., & Tufano, P. 2004. *Case Problems in Finance*. 12th ed. Chicago, IL: McGraw Hill.

1. Williams, 2002
2. Sally Jameson: Valuing Stock Options in a Compensation Package
3. Student Educational Loan Funds, Inc. (Abridged)
4. Arley Merchandise Corporation

Journal articles

1. Cochrane, J.H., Piazzesi, M., 2005. Bond risk premia. *American Economic Review* 95(1), 138-160.
2. Dwyer, G. P. & Tkac, P. 2009. The financial crisis of 2008 in fixed-income markets. *Journal of International Money and Finance*, 28(8): 1293-316.
3. Goyenko, R., Subrahmanyam, A., & Ukhov, A. 2011. The term structure of bond market liquidity and its implications for expected bond returns. *Journal of Financial and Quantitative Analysis*, 46(1): 111-39.
4. Flannery, M. J., Nikolova, S., & Öztekin, Ö. 2012. Leverage expectations and bond credit spreads. *Journal of Financial and Quantitative Analysis*, 47(4): 689-714.
5. Bansal, R. & Shaliastovich, I. 2013. A long-run risks explanation of predictability puzzles in bond and currency markets. *Review of Financial Studies*, 26(1): 1-33.
6. Friewald, N., Jankowitsch, R., & Subrahmanyam, M. G. 2012. Illiquidity or credit deterioration: A study of liquidity in the US corporate bond market during financial crises. *Journal of Financial Economics*, 105(1): 18-36.
7. Kalimipalli, M. & Nayak, S. 2012. Idiosyncratic volatility vs. liquidity? Evidence from the US corporate bond market. *Journal of Financial Intermediation*, 21(2): 217-42.
8. Shim, I. & Zhu, H. 2014. The impact of CDS trading on the bond market: Evidence from Asia. *Journal of Banking & Finance*, 40: 460-75.
9. Das, S., Kalimipalli, M., & Nayak, S. 2014. Did CDS trading improve the market for corporate bonds? *Journal of Financial Economics*, 111(2): 495-525.
10. Aboody, D., Hughes, J. S., & Bugra Ozel, N. 2014. Corporate bond returns and the financial crisis. *Journal of Banking & Finance*, 40: 42-53.

Blackboard

Blackboard <https://blackboard.otago.ac.nz/> provides you with access to course materials, class notices, and resources. Blackboard is used to email the whole class so it is important that you check your student email and Blackboard regularly.

Student Webmail

IMPORTANT – DO THIS NOW:

Forward your University email address to an email address that you use regularly as follows:

1. [Log into your StudentMail account](#) using your student username and password
2. Click **Cog button (top right corner) > Options**
3. Under **Account**, select the **Forward your email** shortcut under the **Short Cuts** menu on the right side of the screen.
4. Under the Forwarding heading, type in the email address you want your email to be forwarded to. You can also choose to have a copy of these emails kept on your StudentMail account, so please check the box if you would like this.
5. Click the **Start forwarding** button.

Assessment

All material presented is examinable (except where stated otherwise) by assignments and the examination. All important assessment information such as due dates and times, content, guidelines and so on will be discussed at lectures and, where appropriate, detailed on Blackboard. *Students are responsible for ensuring that they are aware of this information, keeping track of their own progress, and catching up on any missed classes.*

Assessment	Due date	% of final grade	Requirements to pass this paper
Classroom discussion	See requirements below	15%	NA
Mid-term exam	21 August 2014	30%	NA
Group case study presentation	See requirements below	10%	NA
Research paper	See requirements below	35%	NA
Research paper presentation	See requirements below	10%	NA
Total		100%	

Course Requirements

Class discussion (counting for 15% of final grade: 10% for a critical review & discussion; and 5% for general discussion) is assessed by your intellectual contribution for stimulating insightful dialogues in the classroom. The readings and supportive texts have to be read and prepared before class. Missing classes will always have a negative effect on your classroom discussion grade. At the beginning of the semester, each student will be randomly assigned to discuss one journal article during the course (counting for 10% of final grade). All students must individually prepare a two-page critical review for the assigned article, which must be electronically submitted (i.e. via email) by 17:00hr New Zealand standard time on the day prior to the class meeting, primarily focuses on (1) research question, (2) methodology and results, and (3) the strengths, weaknesses, and practical implications. Late submission of critical reviews may be accepted with point deductions of one percent (i.e. 1% of final grade) per day.

One open-booked mid-term exam (counting for 30% of the final grade) will be held during class on **21 August 2014, at 10:00-12:00**. The two-hour mid-term exam covers all materials discussed during Lectures 1 through 5. There is no make-up exam for the mid-term exam. Students are allowed to bring in any university-approved model of calculators, notes, and books into the mid-term exam. Under exceptional circumstances, a student who missed the mid-term exam will be allowed to count his/her research paper score towards the score for the missed mid-term exam.

Students will be randomly assigned into four groups during Week 2. Each group is required to study one randomly-assigned case and present proposed recommendations (counting for 10% of final grade). Hard copies of presentation slides must be made available at the beginning of the class.

Each student is required to write an individual empirical research paper on any topic related to fixed income securities (counting for 35% of final grade), which must be approved by the lecturer before 31 July 2014. To foster a deep understanding of theories and applications, an empirical replication of prior studies using a different data set is acceptable as well as encouraged. The research paper in a word format (including a data set and relevant program codes) must be electronically submitted (via email) no later than two weeks after the presentation (e.g., a paper presented on September 30, 2014 is due on October 14, 2014 at 17:00hr) and will be mainly assessed on the basis of the overall quality and exposition. The paper should not exceed 5,000 words in length (all inclusive), typewritten and double-line spacing on the A4 portrait format. Late submission of the research paper may be accepted with point deductions of five percent (i.e. 5% of final grade) per day.

Tentatively, each student will have 30 minutes (depending on the number of students) to present his/her research paper. The research paper presentation (counting for 10% of final grade) should focus on key messages. The order of presentation will be randomly assigned during Week 2.

Quality Assurance

At the Otago Business School we monitor the quality of student learning and your learning experience. Your assessed work may be used for assurance of learning processes, such as evaluating the level of achievement of learning outcomes, with the aim of improving the quality of our programmes. All material used for quality assurance purposes will be treated as confidential and the outcome will not affect your grades.

Learning Outcomes

Learning Outcome	Classroom discussion	Mid-term exam	Group Case study	Research paper	Research paper presentation	Total
Demonstrate the understanding of financial theory pertaining to (1) term structure of interest rate and (2) how to price a range of fixed-income securities.	✓	✓	✓	✓	✓	
Demonstrate the understanding of and skills in valuing fixed-income securities and interest rate sensitive products.	✓	✓	✓	✓	✓	
Demonstrate the understanding and appreciation of critical thinking and lifelong learning.	✓	✓	✓	✓	✓	
Demonstrate the understanding of and skills in writing quality research papers.				✓		
Demonstrate the ability to present authoritatively a set of ideas in a clear, concise, and professional manner.	✓		✓		✓	
Total	15%	30%	10%	35%	10%	100%

Grading System

The grading scheme used at Otago is:

A+	90-100	C+	60-64
A	85-89	C	55-59
A-	80-84	C-	50-54
B+	75-79	D	40-49
B	70-74	E	<40
B-	65-69		

Dishonest Practice and Plagiarism

Students should ensure that all submitted work is their own. Plagiarism is a form of dishonest practice (cheating). It is defined as copying or paraphrasing another's work and presenting it as one's own. Any student found responsible for dishonest practice in any piece of work submitted for assessment shall be subject to the University's dishonest practice regulations, which may result in serious penalties, including forfeiture of marks for the piece of work submitted, a zero grade for the paper, or in extreme cases, exclusion from the University. The University of Otago reserves the right to use plagiarism detection tools.

Students are advised to inform themselves about University policies concerning dishonest practice and take up opportunities to improve their academic and information literacy. If necessary, seek advice from academic staff, or the Student Learning Centre. The guideline for students is available at this link: <http://www.otago.ac.nz/study/plagiarism/>

The Library resource on ethical use of information is available via this link: <http://oil.otago.ac.nz/oil/module8.html>

Course Calendar

Week Number	Week Commencing*	Topic	Reading	Notes
1	7 July 2014	Fixed income concepts	Back, Ch. 11	
2	14 July 2014	Introduction to fixed income derivatives	Back, Ch. 12	
3	21 July 2014	Valuing Derivatives in the Extended Vasicek Model	Back, Ch. 13	
4	28 July 2014	Valuation of fixed cash flows with perfect replication	Britten-Jones, Ch. 1	
5	4 August 2014	Imperfect replication: Immunization and duration	Britten-Jones, Ch. 2	
6	11 August 2014	Journal article discussion	Articles #1 – 4	
7	18 August 2014	Journal article discussion	Articles #5 – 6	
Mid-Term Exam is held during class on Thursday 21 August 2014				

Mid Semester Break Monday 25 August to Friday 29 August				
8	1 September 2014	Journal article discussion	Articles #7 – 10	
9	8 September 2014	Case study presentation	Case #1 & 2	
10	15 September 2014	Case study presentation	Case #3 & 4	
11	22 September 2014	Research paper presentation	Papers #1 – 4	
12	29 September 2014	Research paper presentation	Papers #5 – 8	
13	6 October 2014	Reserve week		

* First week of Semester 2 is ACADEMIC WEEK 28

Lectures end Friday 10 October 2014
 University Exam Period First Semester Begins Wednesday 15 October
 End Saturday 8 November 2014

Student Learning Support and Information

Student Charter

<http://www.otago.ac.nz/about/otago005275.html>

Guidelines for Learning at Otago

<http://hedc.otago.ac.nz/hedc/wp-content/uploads/2012/12/Guidelines-for-Learning.pdf>

<http://hedc.otago.ac.nz/hedc/learning/>

Student Learning Centre

The Student Learning Centre, which is part of the Higher Education Development Centre, provides learning support, free of charge, to ALL enrolled students. Their services include:

- a workshop programme designed to help students to improve their learning strategies and their generic skills;
- individual assistance with learning issues;
- on-line study skills advice;
- a student leadership programme
- a student-led peer support programme for students of all ages and backgrounds.
- conversational English groups for students from a non-English speaking background

The Centre also provides two very helpful study guides, "Guidelines for Writing and Editing" and "Writing University Assignments" and these are available on the SLC website.

<http://slc.otago.ac.nz/>

Library Support

The University Library provides online resources for students. These include subject guides, and other research resources, and citation styles. Check it out at: <http://otago.libguides.com/selfhelp>

The Library website <http://www.otago.ac.nz/library> provides online access to resources and services, including group room bookings, library hours and locations, past exam papers, subjects guides and more.

From your mobile: <http://m.otago.ac.nz/library/> or use the Q code:



Māori Student Support

Tēnā koutou katoa,

Ko Corey Bragg tōku ingoa

Ko Ngāi Tahu, Kāti Mamoe, Waitaha me Ngāti Kahungunu ōku iwi

Kia ora, my name is Corey Bragg and I am the Māori student support person in the Business School. My role is to help link Māori students with the various support networks throughout the university and the community. Kāua e whakamā, don't be shy - come in for a chat. Mauri ora mai.

Tel 479 5342 Email corey.bragg@otago.ac.nz Room CO 3.21

Pacific Islands' Student Academic Advisor

Warm Pacific Greetings

Talofa lava, my name is Esmay Eteuati and my role is to liaise with Academic Departments and Student Services relating to Pacific students' and their course of study. I support both staff and students in the Business School and have a network of Pacific contacts in other Divisions around the University.

Tel +64 3 479 4756 Email: esmay.eteuati@otago.ac.nz

Disability Information and Support

Students are encouraged to seek support if they are having difficulty with their studies due to disability, temporary or permanent impairment, injury or chronic illness. It is important to seek help early, through one of the contacts below:

Name	Office	Email
Disability Information and Support	262 Leith St	disabilities@otago.ac.nz
Mr. Dyna Seng	547 Commerce	dyna.seng@otago.ac.nz

Student Feedback

We encourage your feedback. This can be in the form of contacting staff, participating in course evaluation surveys and communicating with class representatives. Continual improvements will be made to this course based in part on student feedback. Recent changes to this course as a result of constructive feedback include (*insert summary of improvements*)

Class Representatives

The class (or student) representative system is an avenue for encouraging communication and consultation between staff and students. It provides you with a vehicle for communicating your views on the teaching and delivery of the paper and provides staff with an opportunity to communicate information and gain constructive feedback from students. It contributes to the development of a sense of community within a department and it adds a further dimension to the range of support services offered to students.

Volunteers for the role of class representatives will be called early in the semester. The OUSA invites all class representatives to a training session, conducted by OUSA, about what it means to be a class representative and some of the possible procedures for dealing with issues that arise. They also provide information on the services that OUSA offers and the role OUSA can play in solving problems that may occur. The OUSA provides support to class representatives during the semester. Departmental staff will also meet with class representatives during the semester to discuss general issues or matters they wish to have considered.

Your class representative's name and contact details will be posted on Blackboard early in the semester.

Concerns about the Course

We hope you will feel comfortable coming to talk to us if you have a concern about the course. The Course Co-ordinator will be happy to discuss any concerns you may have. Alternatively, you can report your concerns to the Class Representative who will follow up with departmental staff. If, after making approaches via these channels, you do not feel that your concerns have been addressed, there are University channels that may aid resolution. For further advice or more information on these, contact the departmental administrator or head of department.

Disclaimer

While every effort is made to ensure that the information contained in this document is accurate, it is subject to change. Changes will be notified in class and via Blackboard. Students are encouraged to check Blackboard regularly. It is the student's responsibility to be informed.