STUDENTS ARE EXPECTED TO HAVE COMPLETED

The course presumes some exposure to undergraduate finance, economics, statistics and econometrics. In addition, knowledge of Matlab programming is required to do one of the practical exercises. Basic knowledge in Matlab and Excel are required.

COMPETENCES AND SKILLS THAT WILL BE ACQUIRED AND LEARNING RESULTS.

This course provides a rigorous panoramic analysis of the interplay between portfolio selection, asset pricing theory, and the empirical evidence. Firstly, we present the main asset pricing models including the CAPM, multi-factor asset pricing models (Fama-French (1993) or Carhart (1997), and conditional models. Secondly, we introduce the main concepts on Portfolio Management and the mean-variance model. Thirdly, a complete description of Investment Companies (mutual funds, hedge funds, among others) and the most relevant performance measures are studied. Students will learn how to create and evaluate a portfolio. Finally, the restrictions of the mean-variance framework are pointed out and potential improvements are suggested. This course combines both theoretical foundations and practical exercises using real data from financial markets or mutual funds industry.

Professors of the Course:
1- David Moreno  (Associate Professor Uc3m, PhD)

DESCRIPTION OF CONTENTS: PROGRAMME

1. Mean-Variance Model
   - Descriptive statistics of asset returns
   - Expected return and risk on a portfolio
   - Diversification
   - The Markowitz Model without risk-free asset
   - The Markowitz Model with risk-free asset

2. Asset Pricing Models
   - CAPM
   - Fundamentals of APT
   - Multifactorial Asset Pricing Models
   - Fama and French Model (1993): Size and Book-to-market factors
   - Carhart Model (1997): The momentum factor
   - Using Investment and Profitability factors
   - The Quality factor
   - Conditional Asset Pricing Models

3. Investment Companies
   -Introduction to Investment Companies
   -Description of main ICs (Mutual Funds, ETF, Closed-Funds)
   -Pricing Mutual Funds

4. Performance Measures and Mutual Funds Evaluation
   -Traditional Performance Measures
   -Performance measures based on APT
   -Conditional Performance Evaluation
   -Performance measures based on Portfolio Holdings
   -Market Timing Ability
Other Performance Measures used by practitioners.
Performance Measurement of Hedge Funds

4. Drawbacks of Mean-Variance model and potential improvements
   - Main problems of Mean-Variance in practice
   - Resampled Efficient Frontier (Michaud, 1998)
   - Robust Portfolio Optimization and Bayesian Models (Shrinkage estimators)
   - Non-normal return distributions: Optimizing Downside Risk
   - Back and Littermann Model

5. Other Topics in Portfolio Management
   - Behavioral Finance
   - Value Investing Philosophy
   - Technical Analysis
   - Non-traditional assets

LEARNING ACTIVITIES AND METHODOLOGY

The theoretical contents are presented using Power Point slides. In all classes empirical exercises will be solved, most of them using real data, with the aim of a practical application and visualization of theoretical concepts. The students will work in teams and using computers. The software used will be Excel and Matlab.

Practical application on Portfolio Choice:
With real data about individual asset returns, the student will have to obtain:
- The mean-variance efficient frontier without riskless asset.
- The minimum variance portfolio.
- The optimal portfolio and efficient frontier with a riskless asset.
- The optimal investor portfolio for different levels of risk aversion.
- The mean-variance efficient frontier for the stochastic discount factor.
- Resampling Efficient Frontier
- Optimar asset allocation under Black-Letterman model

Practical application on Asset Pricing:
With real US market data, students must have to discuss:
- Testing the CAPM
- Estimating the Multifactorial model of Carhart
- The performance of mutual funds using Jensen's alpha
- The performance of alternative multifactor asset pricing models.

ASSESSMENT SYSTEM

Students will solve problems and empirical exercises with real data that could have a weight of 40% in the final grade. The rest 60% will come from the final exam (which has a 40% weight from Matlab and 60% of written exam).

All students must obtain at least 4 out of 10 points in the final exam to take into account the 50% of the grade from the exercises. Otherwise, the final grade will completely be based on the final exam.

% end-of-term-examination: 60
% of continuous assessment (assignments, laboratory, practicals...): 50

BASIC BIBLIOGRAPHY
- Andrew Ang Asset management: A systematic Approach to Factor Investing, Oxford University Press, 2014
- Bodie, Kane and Marcus Investments, McGraw Hill, 2012