Investing, Psychology, and Human Behavior Course Curriculum:

The Value Investor and the Shrink: Going beyond just the numbers – Learning the methods of some of the all time great investors while studying how Psychology and Human Behavior impacts long term investment results.

Value investing can take the shape of many forms. Modern day value investors may still study Graham and Dodd (the so-called fathers of value investing), however, most go well beyond the analysis of book and liquidation value. Value investing was originally formulated in the 1920's with the publishing of Graham and Dodd's text book "Security Analysis." How has the approach to value investing evolved over the years? How have concepts such as relative value, replacement value, private market value, normalized earnings, franchise value and future projected earnings growth become integrated within the camp of value investors?   What are the other popular investment strategies and how do they differ from the value approach?

There have been numerous academic studies illustrating the efficiency of capital markets. Over the past fifty years, business school students have been exposed to the Efficient Market Hypothesis and the Capital Asset Pricing Model, which promote the theory that it is futile for investors to attempt to outperform the stock market over a long period of time. Over the years, individual investors as well as most professional investors have failed to do better than the market indexes. However, investors such as Warren Buffet, Peter Lynch and even the economist John Maynard Keynes have demonstrated the ability to outperform market averages over multiple year periods. What are the attributes that have enabled these select investors to consistently post returns better than that of the market over a period of years? How does human psychology and behavioral analysis have such a strong influence on individual investment decisions?   Why do certain assumptions of the Efficient Market Hypotheses not hold up in the real world?

A stock is not just a ticker on a tape or a quote in a newspaper. A stock represents an actual business. The ability to value the assets of a particular business is crucial to forecasting the direction of its stock price. Companies are managed by people. Understanding the impact psychology and human behavior have on the vision and decision making of an executive management team is instrumental on formulating an opinion on the future potential of a company's share price.

This course will highlight the methodology of successful investors like Warren Buffet, Charlie Munger, Peter Lynch and John Maynard Keynes who have (had) consistently beaten the stock market and have proven that however difficult it may be, one with diligent research and proper temperament can deliver superior long term investment results. Students will learn basic financial metrics and valuation tools to aid their understanding of the investment process. Students will also study behavioral analysis and learn how psychology plays an important role in one's investment success. The goal of this course is to expose students to basic investment tenets and help them develop a foundation that will guide them to become better educated investors in the future.

The course will also include the role financial markets have on society. Students will explore how access to financial capital serves as a multiplier effect to human capital, social capital and real assets. We will explore the ways financial innovation meets the needs of society. Can a good financier and investor also be considered a social scientist?

There will be a section on the 2008 financial crisis. How did certain investors such as Michael Bury and Steven Eisman anticipate the collapse of the mortgage market and the subsequent financial fall-out while exceptionally successful financial executives fail to see the depth of the 2008 crisis unfold? There will also be a section on how ethics could drive financial decisions. What are the warning signs (red flags) of bad behavior and how can investors become armed to avoid falling for Ponzi schemes and/or outright fraud?

Reading Material will include a combination of selected material written by investors, academics and articles from major financial publications as well as documents published by publicly traded companies.

Each class session will have a focus on the technical skills and tools necessary to perform basic financial and security analysis as well as evaluate academic research on group think and the psychological factors related to investing. During class there will be a review of the assigned weekly reading material, which will include a number of company case studies. Throughout the semester, we will feature guest speakers from corporate America as well as professional portfolio managers that will share their own personal experiences towards investing.

There will be a mid-term exam on the basic concepts of Portfolio Management Theory and Behavioral Finance. Class participation will be a meaningful factor in the grading for students. Groups of four students each will be assigned a topic to present during a class session. These groups will also be assigned a particular company where they will be required to write an in-depth research paper and conduct a financial analysis. The last class session will require the groups to give a short presentation on the merits of their selected company.

Week One (September 6th):

Introduction to Portfolio Management:

What are the different paths to becoming a Portfolio Manager:

Sell-side Wall Street Firms

Buy-side Asset Management Firms

Insurance Companies

Corporate Pension Departments

Hedge Funds

What are the major types of investing strategies:

Long-only (Growth, Value, GARP and anything in between)

Long-short strategies

Distressed Investing

Technical Analysis and Momentum Investing

What are the attributes needed to become a successful Long-Term Investor:

The Three Pillars of Investing

- Comprehension
- Interpretation & Projection
- Psychological make-up of the decision maker (Behavioral Science)

An Initial Stroll through "A Random Walk Down Wall Street" (Chapters 1,2,3,4 & 13)

- A Study of the History of Market Bubbles
- Four Separate Market Periods from 1946-2009

A Look at the World of Peter Lynch

- Interview with Peter Lynch , Betting on the Market (Frontline/PBS 1996)
- Use Your Edge by Peter Lynch (Worth Magazine 1996)
- Peter Lynch – Inside the Brain of an Investing Genius (Value Walk 2015)

Week Two (September 13th):

How Management Teams Add Value:

Featured Guest Speaker – Ben Fink, CEO Western Gas Partners

Student Group Discussion Assignments:

Weekly Topic Presentations

Individual Company Projects

Memos to Clients from Howard Marks, Chairman of Oaktree Capital

"Dare to Be Great II", "Getting Lucky"

The Most Important Thing, Chapters 1 & 3

Week Three (September 20st):

Introduction to the basic concepts on the impact Psychology has on Investing

"The Psychology of Investing", (Chapters 1, 2 and 3)

Prospect Theory – How people frame and value a decision involving uncertainty

- **Prospect Theory Value Function**
- **Mental Accounting (viewing each investment separately vs. viewing a single investment as part of a whole portfolio)**
- **Self Deception/Overconfidence (illusion of knowledge, illusion of control)**
- **Heuristic Simplification**

Disposition Effect

- **Mental Accounting (Holding on to Losers)**
- **Framing and Anchoring**
- **Perceptions on Risk**

What you see is all there is?

Student Group #1:

Introduction to Financial Accounting and Financial Statement Analysis: The Language of Business

Formulating the ability to read and more importantly procure relevant information from a company's financial statements. Students will be expected to identify the financial strengths and weakness in a particular company and business

Students will be expected to gain a basic understanding and perform financial analysis for the following financial metrics:

Identifying and analyzing the relevant information in a company's Balance Sheet, Income Statement and Cash Flow Statement

Calculating Basic Valuation Metrics such as Price to Earnings, Price to Book Value, Price to EBITDA, Price to Free Cash Flow and construct a Dividend Discount Model to comprise an intrinsic value for a company

Introduction to Financial Ratios and Financial Statement Analysis – Gillette Company example (Harvard Business School September 13, 2004)

Case Study:

Fran Tarkenton and Knowledgeware: Identifying Red Flags inside Financial Statements

Week Four (September 27th):

Student Group #2:

The Origins of Value Investing

Graham and Dodd's Security Analysis

Graham's formula for Value

Concepts of Intrinsic Value and Margin of Safety and the Defensive Investor

The evolution of what Value Investing means from Graham to Buffet through today.

Competing investment approaches and their impact on the world of Value Investing

Value Investing: A Look at the Benjamin Graham Approach (Stock Analysis Workshop)

The Evolution of Value Investing, Past, Present and Beyond (Financial History – www.MoAF.org, spring 2014)

Identifying the Characteristics of a sustainable and successful business model:

The best businesses have the following:

- **A Distinct Competitive Advantage**
- **High Barriers to Entry**
- **Resilient Revenue Stream**
- **Low Capital Investment to Maintain Profitability**
- **A Meaningful Level of Free Cash Flow Generation**
- **Strong Balance Sheet**

Why buying a great business at a fair price is better than buying a mediocre business at a low price

The Power of Compounding Positive Returns Year after Year

The Dynamic Duo: Warren Buffet and Charlie Munger

Chapters on Warren Buffet and Charlie Munger and The Kelly Principle "Concentrated Investing Strategy" (Chapters 3, 4 and 5)

Investing Lessons of Warren Buffet (Business Dictionary.com)

Week Five (October 4th):

Student Group #3:

The Efficient Market Hypothesis and other Myths

What are the basic concepts behind The Efficient Market Hypothesis (EMH) and The Capital Asset Pricing Model (CAPM)?

The efficient market hypothesis (EMH) is an investment theory that states it is impossible to "beat the market" because stock market efficiency causes existing share prices to always incorporate and reflect all relevant information. According to the EMH, stocks always trade at their fair value on stock exchanges, making it impossible for investors to either purchase undervalued stocks or sell stocks for inflated prices. As such, it should be impossible to outperform the overall market through expert stock selection or market timing, and the only way an investor can possibly obtain higher returns is by purchasing riskier investments.

According to The Capital Asset Pricing Model, the only reason an investor should earn more, on average, by investing in one stock rather than another is that one stock is riskier. The model has come to dominate modern financial theory. But does it really work?

Modern Portfolio Theory

Risk and Volatility: Are the two the same?

Building Behavioral Portfolios

The Study of Individual Investor Behavior, "The Psychology of Investing", (Chapters 7 & 9 & 11)

Modern Economic Research, including the EMH and the CAPM has been built on the notion that human beings act rationally in the attempt to maximize wealth while minimizing risk. However, there is a large body of empirical research that show individual investors do not make rational investment decisions. And as a group, individual investors make systematic, not random, buying and selling decisions. There are a variety of factors such as "the disposition effect" as well as social influences that prevent individuals from making rational investment decisions.

Behavior Analysis and the impact of Psychology on the decision making for Professional Investors

A look inside the (Dis)Incentive Structure for various managers of Mutual Funds, Hedge Funds, Pension and Endowment Investors as well as the Industry Consultants:

Why smart people who manage and oversee billions of dollars have difficulty delivering above average market results?

What are the pressures from clients and bosses which can materially influence an investment professional's behavior?

How compensation structure of professional investors can meaningfully affect their investment decisions.

Sell Side Research: Why relying on recommendations from sell side research analysts (specialists on Wall Street who supposedly are experts for the particular industry groups which they follow) may be bad for your financial health. (**A Random Walk Down Wall Street, Chapter 7**)

The Dangers of:

- **Group Think**

- **Short-Term Focus**
- **Social and Media Hype**

2016 Berkshire Hathaway Shareholder Letter

Buffet Asks Big Money: Why Pay High Fees? (Andrew Ross Sorkin, NY Times, February 27, 2017)

A Quiet Giant of Investing Weighs in on Trump (Andrew Ross Sorkin, NY Times, February 7, 2017)

How well can an economist invest money: The story of John Maynard Keynes (*Concentrated Investment Strategies, Chapter 2)*

John Maynard Keynes: Courage Is the Key to Investing (The Wall Street Journal, October 17, 2016)

Week Six (October 11th):

Featured Guest Speaker: Allen Benello – co-author of Concentrated Investment Strategy: Strategies of the World's Greatest Concentrated Value Investors.

Student Group #4 Debates: Active vs. Passive (Which side are you on?)

Week Seven (October 18th):

The Big Short – The stories of Michael Bury and Steven Eisman: A look inside the psychological make-up of two investors who bet big and won during the 2008 mortgage crisis

Featured Guest Speaker: Steven Eisman – Portfolio Manager, Neuberger Berman

Student Group #5: Case Study: Chainsaw Al and the demise of Sunbeam Oster

Beware of Financial Gimmicks

The Importance of Financial Disclosures and Transparency of Financial Results

Week Eight (October 25th):

Mid-term exam

Week 9 (November 1nd):

Student Group #6: A case study of Lehman Brothers – The downfall of a Wall Street titan

Class Case Study:

Enron – The Smarterst Guys in the Room

How decision making and strategic vision of management can lead to the creation or destruction of shareholder value.

Week Ten (November 8th):

The Best Financier and Investor is a Social Scientist

A presentation by Michael Milken from the Wells Fargo Middle Market Symposium December 8th, 2016

The History of Cedar Fair – 1987 to Present

Why the choices a management makes regarding a company's balance sheet and its uses of free cash flow are crucial in the long term health of a business.

More from Howard Marks:

The Most Important Thing, Chapters 5 (Understanding Risk), 7 (Controlling Risk) and 9 (Awareness of the Pendulum)

A Discussion on Bill Miller: The Joe DiMaggio of Mutual Fund Managers

The Greatest Money of our time (Fortune magazine, November 15, 2006)

The Greatest Investors: Bill Miller (Investopedia)

Week Eleven (November 15th):

Ethics

A Lesson on MLPs

Generating Cash Flow and Income throughout the Energy Cycle

Case Study: Kinder Morgan vs. Enterprise Products Partners

Addressing Potential LP/GP Conflicts (Midstream Business.com, July/August 2015)

A Case Study on Ethics and Greed: Goldman Sachs and Dragon Systems

Week Twelve (November 29th):

Class Case Study: BJ's Restaurant and Brew House and Investing in Restaurant Stocks: **Eating one's way to profits?**

How market and business cycles can affect the valuation of a company's share price.

How "herd mentality" can have a strong impact on how a stock may trade during a certain period of time.

Why it is imperative for successful investors to remain disciplined during extreme times of volatility and market dislocation.

Why the determination of intrinsic value is the key recipe for investment success.

Week Thirteen (December 6th):

Final Presentations

Grading:

Class Participation: 25%

Group Projects

- Class Discussion Assignment: 20%
- Company Review and Analysis: 25%

Mid-Term Exam: 30%

Students will be expected to have done the following Prepared Readings for each week:

Week 1: "A Random Walk Down Wall Street", chapters 1,2,3,4 & 13

Week 2: Howard Marks Memos "Dare to be Great II" and "Getting Lucky"

"The Most Important Thing", chapters 1 & 3

Week 3: "The Psychology of Investing", chapters 1, 2 and 3

Introduction to Financial Ratios and Financial Statement Analysis – Gillette Company

Week 4: Value Investing: A Look at the Benjamin Graham Approach

The Evolution of Value Investing, Past , Present and Beyond

"Concentrated Investing Strategy", chapters 3, 4 and 5

Week 5: Does the Capital Asset Pricing Model Work?

"A Random Walk Down Wall Street", chapter 7

"The Psychology of Investing", chapters 7, 9 & 11

"Concentrated Investing Strategy", chapter 2

Week 6: "Concentrated Investing Strategy", preface, introduction, chapters 1, 7 and 8

Barron's and Wall Street Journal articles on "Active vs. Passive Investing"

Week 7: Betting on the Blind Side

Steve Eisman, Part Deux

Sunbeam Corporation: "Chainsaw Al," Greed and Recovery

Week 8: Review for Mid-term Exam

Week 9: Lehman Brothers – 2005 Institutional Investor article, 2006 Fortune Magazine article and 2009 New York Magazine article Power, Greed and Glory on Wall Street – The Fall of the House of Lehman Brothers

Excerpts from "Enron – The Smartest Guys in the Room

Week 10: Cedar Fair Earnings Transcripts 2009 & 2013

Cedar Fair Fun World Article

2017 Cedar Fair Investment Presentation

"The Most Important Thing", chapters 5, 7 & 9

The Greatest Money Manger of our Time

The Greatest Investors

Week 11: Goldman Sachs and the $580 Million Black Hole

MLP 101

Addressing Potential LP/GP Conflicts

Enterprise Products/Kinder Morgan Investment Presentations 2007-2016

Week 12: BJ's Restaurant and Brew House Annual Reports, Investment Presentations and select

Sell-side analyst reports

Course Reading Material:

A Random Walk Down Wall Street, by Burton Malkiel

The Psychology of Investing, by John Nofinger

Concentrated Investing Strategy: Strategies of the Worlds' Greatest Concentrated Value Investors (Benello, Van Biema, Carlisle)

Excerpts from Howard Marks – Oaktree – The Most Important Thing: Uncommon Sense for the Thoughtful Investor

Memos from Howard Marks, "Dare to be Great II" and "Getting Lucky"

Introduction to Financial Ratios and Financial Statement Analysis – Harvard Business School Case Study September 13, 2004

The Evolution of Value Investing: Past, Present and Beyond, by Joseph Calandro, Jr. and Frederick Sheehan

Value Investing: A Look at the Benjamin Graham Approach, by Maria Crawford Scott

Berkshire Hathaway 2016 Shareholder Letter (March 2017)

"Numbers and Narrative: Modeling, Story Telling and Investing" by Aswath Damodaran

Warren Buffet – Investing Lessons of Warren Buffett (by Thomas Murcko, CEO of BusinessDictionary.com)

Excerpts from "Thinking Fast and Slow" by Daniel Kahneman, Chapters 19 (Illusion of Understanding), 20 (Illusion of Validity – Stock Picking Skills, pages 212-217) & 31 (Risk Policies)

Sunbeam Corporation: "Chainsaw Al, Greed, and Recovery"

Goldman Sachs and Dragon Systems

"Betting on the Blind Side – the story of Michael Burry" Vanity Fair March 1st 2010

Michael Bury and Steve Eisman – Excerpts from the "The Big Short"

Lehman Brothers – 2005 Institutional Investor, 2006 Fortune and Money, 2009 New York Magazine

Excerpts from "Enron – The Smartest Guys in the Room"

Annual Reports, 10Ks, 10Qs, earnings conference call transcripts and presentation of selected companies

Group Discussion Assignments:

- Group 1: Financial Statement Analysis
- Group 2: Value Investing
- Group 3: Efficient Market Hypothesis and Modern Portfolio Theory
- Group 4: Active vs. Passive Debate
- Group 5: Ethics Case Study (Chainsaw Al and Sunbeam Oster)
- Group 6: Lehman Brothers

Company Research and Analysis:

- Group 1: Dominos
- Group 2: Starbucks
- Group 3: Costco
- Group 4: Apple
- Group 5: Colgate
- Group 6: Coke

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