



Financial Reporting and Analysis ACG 6175

Professor: Dr. Marcus Kirk
Spring 2018

Office hours: GER 318, Wed 10:30 – 11:30
(or by appointment)

Email: marcuskirk@ufl.edu

Class: GER 122
Section 2C58: MW 11:45 – 1:40 (Per 5 & 6)
Section 2D61: MW 1:55 – 3:50 (Per 7 & 8)

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Course Materials

- **Required:**

- Required and background readings will be available on Canvas
- **EquitiesLab:** An investment software program that gives you access to detailed real-time financial information for thousands of stocks traded on the major U.S. exchanges. You are eligible to purchase the semester version of the software (\$25/semester) with my course. EquitiesLab has the capabilities to screen stocks on multiple dimensions. Additionally, you will be able to develop your own search, evaluation and trading formulas with the ability to back test them. <https://www.equitieslab.com/>
- **STATA I/C:** FREE access through UF. If you want to purchase it, you only need a six-month license (\$69) for the course but have the option of purchasing an annual license (\$98) or perpetual license (\$189) at student-pricing (<http://www.stata.com/order/new/edu/gradplans/student-pricing/>).

- Supplemental Resources

- STATA
 - A Gentle Introduction to Stata: <http://www.stata.com/bookstore/gentle-introduction-to-stata/index.html>
 - ATS, UCLA: <http://www.ats.ucla.edu/stat/stata/>
- EquitiesLab
 - Quick Start Overview: <https://www.equitieslab.com/wiki/QuickStart>
 - Learn & Support: <https://www.equitieslab.com/learn-support/>
 - Complete the Equities Lab First Course tutorial: <https://www.equitieslab.com/wiki/QuickStart/courses/my-first-course>
 - Principles of Quantitative Equity Investment: A Complete Guide to Creating, Evaluation, and Implementing Trading Strategies. S. Ray (FT Press 2015).
- The Handbook of Equity Market Anomalies: Translating Market Inefficiencies into Effective Investment Strategies. L. Zacks (Wiley 2011).

Course structure

The course format is a combination of lectures, class discussions, problem solving, and presentations. The course has a very practical emphasis. You will apply quantitative analysis in a series of individual assignments, quizzes, and a group assignment and presentation. You are responsible for reading required papers in advance of the class sessions.

Course description and objectives

This course is about the analysis of a firm's financial and accounting information. More specifically, it will provide you with tools to analyze big data and exploit information in corporate financial statements. This is formally an accounting course and we will discuss accounting issues related to financial reporting. However, this course is intended to give you a *user's* perspective on financial reporting.

This course will teach you how to analyze financial statements, identify potential earnings management within financial statements, forecast future financial statements, and use the financial statement information for firm valuation and to identify under- or over-valued stocks.

This course emphasizes a top-down approach that begins with the universe of available companies and uses powerful statistical software (STATA and EquitiesLab) to evaluate and filter the "big data" into meaningful subsets.

We begin by introducing the fundamental framework of market efficiency and the use of analytical valuation models. We next examine frictions that are likely to exist in interpreting accounting information and limits to arbitrage. We will highlight the theoretical relationship between return and risk before considering practical methods of risk adjustment.

We then apply a set of tools to analyze financial statement data to assess the firm's past performance, risk, growth, and current financial health as well as to forecast the future performance of the firm. We will also apply various tools for diagnosing accounting quality and identify potential earnings management. Ultimately, we use accounting variables to identify potentially attractive investments.

Course requirements

The course will require an in-depth reading of the topics each week. You are required to read the relevant reading(s) and be ready for class discussion. Please plan your time ahead because some readings are quite long and others are more intricate.

Grading:

To help you achieve the objectives of the course, your grade will be based on:

Class Participation	10%
Quizzes (3)	45
Assignments	20
Final Project	25

Course Grade:

Final grades will be based on the obtaining the following percentage of total course points:

90-100% = A; 89-89% = A-; 87-88% = B+; 80-86% = B; 79-79% = B-; 77-78% = C+; 70-76% = C; 69-69% = C-; 60-68% = D; 0-59% = E. Required percentages may be reduced but will not be raised.

CLASS PARTICIPATION (10%)

Class participation (either during class time or on the course's conference) is important because it enhances everyone's learning experience. You should strive to be a contributing and valuable member of the class. Feel free to ask questions about issues that you or your peers are unclear, contribute your ideas and insights, offer examples, challenge everyone's assumptions and analyses, and raise interesting directions for class discussion. The emphasis of your class participation should be on the quality of your contribution, not on the duration of your "air time."

QUIZZES (45%)

There will be three in-class, closed-book quizzes. The content of the quizzes will reflect the content of the course to-date in terms of lectures, readings, class discussions, exercises, and assignments.

ASSIGNMENTS (20%)

You will choose a group of not more than 3 members to work on the assignments. Assignments will be due before the beginning of class unless otherwise noted. You must submit the assignment through Canvas or EquitiesLab following the instructions. Credit will not be given for late assignments.

GROUP PROJECT AND PRESENTATION (25%)

You will be formed into groups of no more than 5 members. The purpose of this assignment is to apply the concepts discussed in this course to build your own quantitative investment strategy. Groups should start working on the project well in advance of the submission date.

For the project, you need to *read widely, think creatively, reason logically, and write clearly*. The assignment involves developing and analyzing your own quantitative investment strategy. You should take the role of a prospective fund manager presenting this strategy internally to your Portfolio Manager.

The total length of the strategy pitch book should not exceed five double-spaced pages – informative figures and tables should be used but are not included in the page limit. A complete pitch book will include: (1) an investment strategy analysis, which includes an introduction of your fund manager team, the investment philosophy of your fund, an analysis of the underlying determinants for your strategy, and your competitive advantage; (2) a detailed portfolio construction analysis, which includes your screens (at least one must be a formula entered into EquitiesLab), and your rebalancing and other trading assumptions; (3) a back test, which includes return graphs; and (4) a performance and risk analysis, which includes a comparison of your strategy against other benchmarks, a risk-adjustment, and statistics such as returns, volatility, %positive periods, Sharpe ratios, and others. You may choose a format that best conveys your analysis.

The strategy pitch book is due by noon, Tuesday February 20 (day before final class). Please email me the final project and I will post them in Canvas prior to the final class.

Your group will be **present your group's quantitative investment strategy during the final class period** where you will have no more than 15 minutes to present your investment strategy in front of the class. Following the presentation, you will have no more than 5 minutes to address any specific follow-up questions from the class. All group members are expected to actively participate in the presentation.

Grading will be based on the following:

- Strategy pitch book (15%)
- Presentation (10%)

Examinations, Quizzes and other Matters:

1. You must attend only the section for which you are formally registered. Quizzes and assignments will only be graded for students legitimately registered in the section.
2. The policies in this syllabus do not change throughout the term. **However, circumstances may require changes in exam or quiz dates.**
3. The examinations will be a mixture of multiple choice questions, problems and essays. Examination and quizzes can address materials presented in class, assigned readings, suggested homework problems, and other topics/questions from the text.
4. The examination dates noted on the class schedule have priority over regular classes scheduled at the same times. There should be little, if any, reason for a valid conflict with these times. In some cases, other courses offer makeups which allow conflicts to be avoided. If you have a conflict involving another exam, notify me **at least 10 days before the examination date**. If an examination is missed without a valid, documented excuse, you will receive a grade of 0 for the exam. **Students MUST take the final exam at the scheduled time.** Note: employment situations, weddings, family reunions, employment, travel plans, etc. are not accepted as valid conflicts.
5. The dates for the mid-term exams are noted on the syllabus. Examination locations will be announced by your professor and posted, by professor and section number, on the class website.
6. Grades are not subject to negotiations.
7. A make-up exam will be given when the student has a valid verifiable reason for not taking the exam during the scheduled time. Barring a documented emergency, the request must be made a minimum of ten days prior to the scheduled exam. Exceptions are made if the policy conflicts with UF attendance requirements. More detail on acceptable reasons for absence and UF policies on attendance are found at: <https://catalog.ufl.edu/ugrad/current/regulations/info/attendance.aspx>

Attendance Policy:

Attendance is a minimum requirement in this course, and exam performance is adversely affected by absences. Material that is not in the text may be covered in lectures. Students should prepare for all classes even if they miss and are responsible for material covered in their absence. Students may not attend a class unless they are officially registered for the course. The Fisher School of Accounting does not approve requests to audit its courses. Students who do not attend at least one of the first two class meetings of a course or laboratory in which they are registered, and who have not contacted the School to indicate their intent, may be dropped from the course. The instructor adheres to all UF attendance policies.

The following are examples of absences that will not be excused:

- Participation in Intramural Sports or UF Sport Clubs;
- Coaching youth sports or leadership roles for similar extracurricular activities;
- Sorority or fraternity events;
- Family or personal vacations and obligations;
- Medical appointments scheduled in advance of class (including non-emergency surgical operations);
- Missing class due to problems associated with a car or other method of transportation to UF;
- Attending or watching sport events or concerts;
- Attending a wedding, birthday party, graduation or similar event;
- Venturing to the courthouse to resolve an issue (e.g., traffic citation);
- Requirements for your other classes; and
- Job and internship requirements (education takes priority).

Academic Honesty

In 1995 the UF student body enacted a new honor code and voluntarily committed itself to the highest standards of honesty and integrity. When students enroll at the university, they commit themselves to the standard drafted and enacted by students.

Preamble: In adopting this honor code, the students of the University of Florida recognize that academic honesty and integrity are fundamental values of the university community. Students who enroll at the university commit to holding themselves and their peers to the high standard of honor required by the honor code. Any individual who becomes aware of a violation of the honor code is bound by honor to take corrective action. The quality of a University of Florida education is dependent upon community acceptance and enforcement of the honor code.

The Honor Code: We, the members of the University of Florida community, pledge to hold ourselves and our peers to the highest standards of honesty and integrity.

On all work submitted for credit by students at the university, the following pledge is either required or implied: **"On my honor, I have neither given nor received unauthorized aid in doing this assignment."**

The university requires all members of its community to be honest in all endeavors. A fundamental principle is that the whole process of learning and pursuit of knowledge is diminished by cheating, plagiarism and other acts of academic dishonesty. In addition, every dishonest act in the academic environment affects other students adversely, from the skewing of the grading curve to giving unfair advantage for honors or for professional or graduate school admission. Therefore, the university will take severe action against dishonest students. Similarly, measures will be taken against faculty, staff and administrators who practice dishonest or demeaning behavior.

Student Responsibility. Students should report any condition that facilitates dishonesty to the instructor, department chair, college dean or Student Honor Court.

Faculty Responsibility. Faculty members have a duty to promote honest behavior and to avoid practices and environments that foster cheating in their classes. Teachers should encourage students to bring negative conditions or incidents of dishonesty to their attention. In their own work, teachers should practice the same high standards they expect from their students.

Administration Responsibility. As highly visible members of our academic community, administrators should be ever vigilant to promote academic honesty and conduct their lives in an ethically exemplary manner.

Academic dishonesty will not be tolerated. Students are required to know and comply with the university's policy on academic honesty. This policy is detailed in the Undergraduate Catalog and by reference is included in this course syllabus. For more information visit:

<https://www.dso.ufl.edu/sccr/process/student-conduct-honor-code/>

Civility:

This course will be conducted in a courteous and professional manner. Inappropriate classroom behavior of any form will not be tolerated. At the instructor's discretion, students acting in an uncivil manner will receive a grade reduction commensurate with the infraction. Students can be withdrawn from the course for excessive unacceptable behavior.

Disabilities:

Students requesting classroom accommodations must first register with the Dean of Students Office. Support services for students with disabilities are coordinated by the [Disability Resource Center](#) in the [Dean of Students Office](#). All support services provided for University of Florida students are individualized to meet the needs of students with disabilities. To obtain individual support services, each student must meet with one of the support coordinators in the Disability Resources Program and collaboratively develop appropriate support strategies. Appropriate documentation regarding the student's disability is necessary to obtain any reasonable accommodation or support service. The Dean of Students Office will provide documentation to the student who must then provide this documentation to the instructor a minimum of ten days prior to the requested accommodation.

Evaluation:

Students are expected to provide feedback on the quality of instruction in this course based on 10 criteria. These evaluations are conducted online at <https://evaluations.ufl.edu>. Evaluations are typically open during the last two or three weeks of the semester, but students will be given specific times when they are open. Summary results of these assessments are available to students at <https://evaluations.ufl.edu/results/>

Grade Values:

The grade-point value per credit hour associated with each letter grade is assigned by the Office of the University Registrar:

A = 4.0, A- = 3.67, B+ = 3.33, B = 3.0, B- = 2.67, C+ = 2.33, C = 2.0, C- = 1.67, D+ = 1.33, D = 1.0, D- = .67, E = 0.0

For more information visit: <https://catalog.ufl.edu/ugrad/current/regulations/info/grades.aspx>

Miscellaneous matters

- Please use the course discussion boards for general questions. If you do email me in the “subject” section, please indicate your course number “ACG6175.” For questions that require long answers, please come to see me during my office hours or talk with me after class.
- Grading issues should be raised within a week after the graded assignment is returned.
- You should attend and participate in all class sessions.

Course outline

DATE	CLASS PERIOD	TOPIC
1/8	L01	Introduction. Market efficiency.
1/10	L02	STATA. EquitiesLab. Applied econometrics.
1/15		No class (MLK Day)
1/17	L03	Stock prices and accounting earnings. Valuation models.
1/22	L04	Cost of capital. Factor models. Risk-adjusted returns.
1/24	L05	Quiz & Market frictions/Individual investors
1/29	L06	Accruals and cash flows
1/31	L07	Financial ratios
2/5	L08	Earnings manipulation
2/7	L09	Quiz & PEAD and momentum
2/12	L10	Forecasting & Fundamental analysis
2/14	L11	Analysts
2/19	L12	Quiz
2/21	L13	Wrapping up / Group presentations

Detailed class schedule

Class/date	Topic/Assignments
1 – Mon. 1/8	Introduction; Market efficiency
TOPICS:	Course format, requirements and expectations. Role of STATA and EquitiesLab. Quantitative “big data” analysis. Market efficiency.
READINGS:	Lee (2001) - required
2 – Wed. 1/10	STATA, EquitiesLab and Applied Econometrics
TOPICS:	Introduction to STATA and EquitiesLab. Useful STATA commands. Screening and backtesting in EquitiesLab. Introduction to basic econometrics and applied statistics.
DUE:	Assignment #1: Start in class (please come with STATA ready) – Due 1/15
Mon. 1/15	No Class
TOPICS:	Martin Luther King Day
DUE:	Assignment #1: Due by 9:30am today
3 – Wed. 1/17	Stock prices and accounting earnings; Valuation models
TOPICS:	Accounting information and valuation. Limitation of accounting information. Valuation models & the Residual Income Model (RIM).
READINGS:	Nichols and Wahlen (2004) - required Lee (1996) - required
DUE:	Assignment #1: Finish on your own (submit before class)
4 – Mon. 1/22	Cost of capital; Factor models; Risk-adjusted returns
TOPICS:	Cost of equity capital and beta. CAPM and factor models. Alpha and risk-adjusted returns.
READINGS:	Fama and French (2004) - required
DUE:	Assignment #2: EquitiesLab screens (submit before class)

Detailed class schedule

Class/date	Topic/Assignments
5 – Wed. 1/24	QUIZ (15%) – In-class and closed book. Market frictions; Individual investors TOPICS: Characteristics and considerations of trading strategies. Limits to arbitrage. Behavioral characteristics of individual investors. READINGS: Barber and Odean (2000) - required Grinblatt and Keloharju (2001) - background Shleifer and Vishny (1997) - background
6 – Mon. 1/29	Accruals and cash flows TOPICS: Evaluating a firm's cash flows. Accruals, cash flows and earnings quality. Accrual anomaly. READINGS: Bradshaw, Richardson, Sloan (2001) - required DUE: Assignment #3: Accruals anomaly (submit before class)
7 – Wed. 1/31	Financial ratio analysis TOPICS: Financial ratio analysis. Time-series vs cross-sections. Ratio framework. Profitability, turnover, and leverage ratios. Putting ratios together. READINGS: Soliman (2008) - required DUE: Assignment #4: EquitiesLab ratio analysis (submit before class)
8 – Mon. 2/5	Identifying earnings manipulation TOPICS: What is earnings management? Accrual versus real earnings management. Accounting quality. Abnormal accruals. Red flags. Benford's law. READINGS: Beneish, Lee, and Nichols (2013) - required Amiram, Bozanic, and Rouen (2015) - background DUE: Assignment #5: Earnings manipulation (submit before class)

Detailed class schedule

<u>Class/date</u>	<u>Topic/Assignments</u>
9– Wed. 2/7	QUIZ (15%) – In-class and closed book. PEAD and Momentum
TOPICS:	Post-earnings announcement drift (a.k.a. PEAD, a.k.a earnings momentum). Price momentum.
READINGS:	Chan, Jegadeesh, and Lakonishok (1996) - required Asness, Moskowitz, and Pedersen (2013) - background
10 – Mon. 2/12	Forecasting & Fundamental Analysis
TOPICS:	Statistical properties of accounting numbers. Persistent versus transitory accounting numbers. Econometric forecasts. Modelling bankruptcy and financing distress (Z-Score). Summary measures of fundamental attractiveness of a stock (G-Score, F-Score).
READINGS:	Mohanram (2005) - required Piotroski (2000) – background
DUE:	Assignment #6: Econometric forecasting (submit before class)
11 – Wed. 2/14	Analysts
TOPICS:	Role of analysts in capital markets. Earnings forecasts and recommendations. Analyst incentives and biases. Analyst forecasts and valuation.
READINGS:	Bradshaw (2004) - required Frankel and Lee (1998) - background Lee and So (2016) - background
DUE:	Assignment #7: RIM and abnormal analyst coverage (submit before class)

Detailed class schedule

<u>Class/date</u>	<u>Topic/Assignments</u>
12 – Mon. 2/19	QUIZ (15%) – In-class and closed book.
TOPICS:	In-class time to work on your group project.
13 – Wed. 2/21	Wrapping up / Group Presentations
TOPICS:	Group presentations.
READINGS:	Group projects on Canvas.
DUE:	Tuesday 2/20 (before noon) – written strategy pitch book