249 – Introduction to Accounting and Finance (Spring 2014)

Time: Tuesday 8:00-9:50 a.m.

Location: Room 10

Instructor: David Mendel

Office hours: Tuesdays 7:30 to 8:00 a.m. and 10:00 a.m. to noon or by appointment

Location: Room 308

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**Course Overview**

The course will begin with a review of financial documents. We will use reports from Apple, IBM, and Amazon among others to obtain a working knowledge of the financial document landscape and a basic understanding of accounting (the language of finance). Throughout the course the basic accounting text will be supplemented by study materials from my bSpace, the Internet and the databases available through the library. You should budget $20 for books and materials.

As there are considerable differences between the accounting and financing needs of different businesses (e.g., a utility company and a grocery store) we will use the skills acquired to investigate how various companies manage their finances. In particular we will look at a real estate investment trust, a restaurant, banks, insurance companies, and manufacturing firms to follow the money through these businesses and to gain some insight into how the greater financial system works.

We will use the skills acquired to analyze companies and financial transactions. We will study in detail the initial public offering (IPO) of Groupon and the merger of the Union Pacific Railroad with Berkshire Hathaway.

Throughout the course you will learn how to go about the research of businesses and some basic business skills. We will use current events for class discussions. Sprinkled liberally throughout the course will be discussions about the personalities and the culture of the financial markets.

While focused on the accounting skills necessary to understand financial statements the courses ultimate goal is to teach analytical skills that will enable you to add value in your practice. To get the full benefit of this course you will need to do the homework, attend the class, and participate in the discussion.

## Syllabus

1/7/14 Class 1

**No Numbers Class**

We will use documents from IBM’s investor relations website to get an overview of [financial documents](http://www.ibm.com/investor/).

Using the footnotes to the Apple Inc. annual report we will begin the process of exploring the contents and the interpretation of financial documents. In particular we will look at the effect of an accounting change on [the company’s reported earnings and cash flow](http://online.wsj.com/news/articles/SB125372511435934619).

You will learn how to get financial documents from the Internet starting with this class.

1/14/14 Class 2

**Balance Sheets**

We will examine the balance sheet of Typical Manufacturing in the [Merrill Lynch Guide to Understanding Financial Reports](http://ospflor63.stanford.edu/upload/handouts/Merrill_Lynch.pdf) (pages 2 -20).

There will also be a short tutorial on Excel for those not familiar the program. We will use excel spreadsheets periodically and a familiarity with their use is just one of the practical skills taught in this course.

1/21/14 Class 3

**Income Statements**

We will examine the income statement of Typical Manufacturing in [Merrill Lynch Guide to Understanding Financial Reports](http://ospflor63.stanford.edu/upload/handouts/Merrill_Lynch.pdf) (pages 22 -31).

[JPM Industries](http://articles.chicagotribune.com/1988-09-21/business/8802010141_1_jpm-investment-adviser-securities-officials) was a penny stock operator. We will use the 1985 annual report of the company to gain familiarity with financial reports and to learn how to spot red flags.

We will also study the time value of money.

1/28/14 Class 4

**Cash flow**

Cash and cash flow are the lifeblood of all businesses. We will study the difference between earnings and cash and examine the way cash cycles through different businesses.

Read this article from the Charles Schwab website [cash flow vs. earnings](http://www.schwab.com/public/schwab/resource_center/expert_insight/investing_strategies/stocks/cash_flow_vs_earnings_which_is_more_meaningful.html)

We will compare and contrast the finances of [Amazon](http://phx.corporate-ir.net/phoenix.zhtml?p=irol-irhome&c=97664) vs. [Barnes and Noble](http://www.barnesandnobleinc.com/for_investors/for_investors.html).

2/4/14 Class 5

**Start-ups**

You and your team will build an income statement for International Widget; a business you will model based on selling [Financial Most Wanted playing cards](http://www.financialcrisiscards.com). You will determine how much capital will be needed to start this business and estimate how many units you will need to sell to break even.

2/11/14 Class 6

**Ratio Analysis**

We will apply the ratio analysis techniques from our text to a number of real world companies to understand their meaning and application.

We will use ratio analysis and the [Z-score methodology](http://www.grahaminvestor.com/articles/quantitative-tools/the-altman-z-score/) to forecast the potential for bankruptcy of Sears Holdings, RadioShack, and JC Penny.

2/18/14 Class 7

**Restaurants**

Angeline’s Louisiana Kitchen is a restaurant on Shattuck Avenue in Berkeley. We will get an inside look at the restaurant business and details on the start-up of [Angeline’s Louisiana Kitchen](http://www.angelineskitchen.com/). You will have the opportunity to ask questions of the restaurant’s management.

2/25/14 Class 8

**Debt and Equity**

We will learn the language and mechanics of [the bond market](http://www.asiaing.com/an-investors-guide-to-bond-basics.html). We will study the various types of equity and the equity markets.

There will also be an overview of debt and equity in bankruptcy.

3/4/14 Class 9

**Initial Public Offerings (IPOs)**

Ignore the fifteen-second ad preceding this [video clip](http://www.cnbc.com/id/45066957/Cramer_s_Groupon_IPO_Strategy) of Jim Cramer’s rant from the CNBC show Mad Money about the Groupon IPO. Also ignore everything after 6 minutes and thirty seconds of the clip. We will use the [prospectus for the Groupon IPO](http://www.sec.gov/Archives/edgar/data/1490281/000104746911005613/a2203913zs-1.htm) to learn how to read one of these documents, how one might think about public offerings in general and Groupon in particular.

3/11/14 Class 10

**Manufacturing**

We will be studying [Rogers Corporation](http://www.rogerscorp.com/), a manufacturer of specialty materials that goes into products such as smart phones and iPads.

We will look in detail at the company’s decision to move operations to China.

3/18/14 Class 11

**Banking**

Commercial banking is principally about two things (1) the spread between the cost of deposits and the return one can earn on that money and (2) the amount of leverage a bank can employ in earning that spread. We will look at the [cost of funds](https://www.wellsfargo.com/savings_cds/cds) and the [return on investment](https://www.wellsfargo.com/credit_cards/) for Wells Fargo Bank and discuss the relative merits of taking out a fixed vs. variable mortgage.

You will do a simple investing exercise using Excel to learn the [power of compounding](https://personal.vanguard.com/us/insights/saving-investing/power-of-compounding).

3/25/14 no class

**Spring recess**

4/1/14 Class 12

**Real Estate**

Mission West Properties was a Real Estate Investment Trust (REIT) that engaged in the ownership and management of R&D buildings in the Silicon Valley.We will get an inside look at the operations of the Mission West portfolio of 108 properties. We will delve into company’s effort to optimize their assets in [the aftermath of the Internet Bubble in the late 1990s](http://www.bloomberg.com/apps/news?pid=20601103&sid=a7pUR5eBwlJI).

4/8/14 Class 13

**Insurance**

The principal business of the Berkshire Hathaway Corporation is insurance. Legendary investor Warren Buffett is the chairman of the board of the company. We will use the [chairman's letter](http://www.berkshirehathaway.com/2002ar/2002ar.pdf) from the 2002 Berkshire Hathaway annual report as our source document for our study of the insurance business.

4/15/14 Class 14

**Mergers**

You will read background material to get an overview and some of the accounting aspects of mergers. We will take an in-depth look at the [Berkshire Hathaway merger with Burlington Northern](http://www.cnbc.com/id/33602516).

4/25/14 Review session

Room 10 from 1:10 – 3:00

**Grades**

I will be teaching a method of thinking as well as a body of knowledge. The easiest and best way to demonstrate your understanding will be through class participation. You can distinguish yourself by the quality of the questions you ask as much as by the answers to the questions I may ask. Show up to class prepared to participate. There will small amount of homework to hand in. The final will be a take-home exam and will be comprehensive as you will need to employ skills accumulated during the semester.