Finance Professors Analyze the Credit Bubble and its Aftermath

Asset bubbles have long been a part of financial history. Lately we have had two: the high tech bubble and the real estate bubble. Inevitably we will have more. Bubbles can’t be predicted but their aftermath must be dealt with promptly.

That’s the assessment of three experts from the Finance Department who took a look at the current state of the U.S. economy as the country works to pull out of a recession sparked for the most part by a subprime mortgage crisis that burst the real estate bubble.

“Solutions now must be swift and decisive – Americans have no patience for long-term rescue plans,” says Finance Professor Herb Kaufman.” But if the government overcorrects, Kaufman warns, we could plunge into a bout of inflation – or stagflation – with a resultant stagnant economy.”

Kaufman was joined in his assessment of the economic situation by Anthony Sanders, Bob Herberger Arizona Heritage Chair and Professor of Finance and Real Estate, and Clinical Associate Professor of Finance Werner Bonadurer. All three praised Federal Reserve Board Chairman Ben Bernanke for his decision to pump vast amounts of liquidity into the economy. “This was called for in this economic downturn, which is unprecedented in the post-World War II years,” Kaufman says. “I think he’s handled this right.”

But Kaufman and Sanders caution that the pendulum could swing too far in the opposite direction.

“I think it’s a risky strategy, because if this doesn’t work…we’re going to have a declining economy with a powerful dose of inflation on top of it, better known as stagflation, the ghost of the Carter years,” Sanders says. “That is going to be very destructive in the long term. Everyone’s hoping that this works, but there are some people blaming the Federal Reserve’s monetary policies for some of the problems we’re in right now. It can be argued that they failed to monitor the housing and mortgage market while the...
bubble was growing and then had to pump trillions of dollars of liquidity into the financial system to avoid its collapse.”

Once that liquidity is disgorged, Kaufman agrees, it will take an “artful Fed” to mop up the excess. “Probably nothing’s going to happen in 2009, but 2010 could be the risk year,” he says.

Bonadurer believes a major issue is how to assess or fight asset bubbles, which have plagued the U.S. economy repeatedly in recent decades. In the late 1990s the country saw the bursting of the Internet or dot-com bubble, followed by the collapse of the real estate market bubble with widespread repercussions.

“You cannot reliably identify asset price bubbles ahead of time,” Bonadurer insists. “If bubbles burst, we need the Fed to have enough weaponry, monetary policy, balance sheet capacity, conviction and authority in policy design and implementation.”

While the Internet bubble was mostly contained to certain regions of the country, such as Silicon Valley, the real estate crisis has snaked along Main Street, Sanders says, and was not so easily contained.

“The housing bubble,” Sanders says, “was caused by several factors, one of which was that we opened the floodgates to borrowers who never before had taken out home loans. They were part of the impetus, but also the fact that we lowered underwriting standards across the board allowed many more mortgages to be made. The financial system that the Fed monitored allowed this bubble to occur. I’m not overly happy with the Federal Reserve System at the moment. They saw this coming. They did nothing about it. And now we’re stuck with it.”

The crash seemed to come unexpectedly and suddenly. The problem, Sanders says, is that when debt financing persists, whether by municipalities, governments or banks, returns become magnified and investors are happy but they don’t see the oncoming cliff.

“We just kept issuing more and more debt,” he says. “There were a few warning signals, but when you hit the edge of that cliff, you fall.” Warning signs were vague and not well articulated, he says.

Exacerbating the problem, says Bonadurer, was the leverage employed by the non-bank sector and the lack of transparency in the credit derivatives market.
Kaufman agrees that the crisis spread beyond housing.

“What has happened is because of the way in which those mortgages were financed in the capital markets for securitization, it really became not only a real estate bubble, but it became a capital markets bubble that was widespread across all asset categories, all credit categories.”

Never before, he says, had the country embraced a policy in which risk did not exact a price. Credit spreads among various categories of debt, including sovereign debt and emerging market debt, which historically had been anywhere between 700 and 1,200 basis points, closed to 300 basis points, Kaufman says. That provided “ridiculous amounts of availability of credit at low rates that did not account for the risk. We’re paying for a lot of that right now.”

And most of the world is also paying. Our global economy has led to a global crisis, Bonadurer says. Though the downturn might have begun in the U.S., Europe and Asia have also suffered and each country has implemented its own solutions, with varying degrees of success.

Most European nations, China and Japan have created financial stimulus packages, and the U.S. will follow suit.

“The Bank of England moved fairly aggressively in the U.K. compared to continental Europe,” Kaufman says. “When you go to continental Europe, you look at the Eurozone and the European Central Bank where timidity certainly ruled. Now, going to our fiscal stimulus plan, you’re talking anywhere between $500 billion and $1 trillion over two years. We’re talking 5 percent potentially of GDP. And that should make a difference.”

Are U.S. banks doing their part to aid in the nation’s recovery?

Bonadurer sees two issues. Banks, he says, are not much in the driver’s seat currently. “All they’re doing right now is deleveraging. And they’ll do so for quite some time…They’re not going to bail us out.”

The other question, he says, is what are governments and central banks doing? “Are they throwing enough at the problem? Are they recapitalizing the financial sector enough? My answer is they are not. They’re not yet at the stage where they’re overcapitalizing banks, which is necessary to regain confidence. They are not yet ahead of the curve.”

Kaufman uses the analogy of a pail of water. The pail must be filled with enough water to prevent its being blown over in the wind, and then it must be filled to overflowing. “I don’t think we’re there,” he says. “It was naïve for us to expect that an infusion of about $250 billion into bank capital would immediately turn around the result, when the asset side of their balance sheets was so badly depleted.”

The solution, Kaufman says, will not be heavy-handed regulation, which can kill financial creativity, but transparency. Overregulation, Sanders says, would prevent anyone with poor credit from ever receiving a loan.

We haven’t seen the last of the asset bubbles, he adds, which seem to come every four years.

But however we solve the current crisis and put in place safeguards to prevent another such situation, the next crisis will come from a different and unexpected corner, Bonadurer says.

Kaufman is hoping for “a credible commitment back to financial sanity,” and it must come soon.

“The appetite in the body politic is to move forward very swiftly with decisive action even if it’s sometimes not correct. That’s just the nature of the beast,” Kaufman says. “I think people are losing their jobs, people are seeing banks close, and they’re saying, ‘Do something, do something.’ If you sit down and say we have a five-year plan, that’s not fast enough.”

“We’re still in a crisis where we need to take care of the fires and not worry about the fire code at this stage,” says Bonadurer. “I think the end game scenario is very high inflation or stagflation and very sluggish growth for a couple years to come.”
It’s no secret that housing prices are dropping across metropolitan Phoenix. But just how much value individual homes are losing year to year is the more useful statistic being tracked by the Arizona State University-Repeat Sales Index (ASU-RSI), a tool for realtors, developers and homeowners.

The ASU-RSI is based on repeat sales, the most reliable way to estimate price changes in the housing market. Repeat sales compare the prices of a single house against itself at different points in time, instead of comparing different homes with different quality factors.

Although the ASU-RSI was created just a year ago, it uses data gleaned as far back as 1989. The home price information is taken from the S&P/Case-Shiller Index for Phoenix, says Karl Guntermann.

Ask Michael Hertzel what he loves about his work, and he’ll tell you mentoring students and collaborating with his colleagues.

“You share your experiences and create new knowledge together,” he says. That generosity has earned Hertzel an appointment as the Richard C. and Carole Kraemer Professor of Finance, a fitting honor for a man with a distinguished and sustained research career, says Jeffrey Coles, Finance Department Chair. “Mike has shown outstanding intellectual achievement.”

“Prestigious chairs are not awarded lightly,” Coles says. “They are given out not only to attract but to retain the highest quality educators. Hertzel might have been wooed by other universities, which would have been unthinkable. We wanted to be preemptive in retaining Mike,” Coles says. Modest about his accomplishments, Hertzel says simply, “It’s a nice honor and nice recognition from the department.” Hertzel never seems to stand still. In addition to directing the Ph.D. program and teaching at the honors level, he serves as faculty director of the Intel Collaborative Thesis Program, which he developed in cooperation with Intel Corp.’s Embedded Products Controller and finance alum Bob Auer. Now in its eighth year, the program pairs selected Business Honors students with Intel employees eager to gain management skills. Students get such real-world experience as researching the health of Intel suppliers to forge long-term relationships between corporation and vendor. “It’s worked out great for them and been fantastic for us,” Hertzel says.

Hertzel’s own research has focused on corporate finance, law and economics, accounting, loan contracting and behavioral finance. Five years ago, he began examining how bankruptcies affect a company’s suppliers and customers and the resulting contagion in intra-industry valuation consequences. These have become timely topics. With the economic downturn, he says, “people are more interested in our ideas. It’s a hot topic.” Of course, not even finance professors are immune to the vagaries of the market. Hertzel jokes, “I’m working out more at the gym so that I can work till I’m 85.”
When the W. P. Carey School’s Economics Department decided to create the Edward C. Prescott Center for Advanced Studies in Economic Efficiency, one man was the obvious choice for director: Rajnish Mehra. Mehra is the longtime colleague, co-author and friend of Prescott, a Nobel Prize winner who holds the W. P. Carey Chair in Economics.

“He was very keen that I would head it,” says Mehra, the E.N. Basha Arizona Heritage Visiting Professor who comes to ASU from the University of California, Santa Barbara. “It was an offer I couldn’t refuse.”

Mehra and Prescott are the authors of one of the most cited research papers, “The Equity Premium: A Puzzle,” which examines the paradox between the relatively low yields from government bonds and high yields from stock in U.S. companies.

In addition to Mehra’s work at the Prescott Center, he also will teach in the Finance Department, an arrangement that thrills Finance Department Chair Jeffrey Coles. “He’s a very important addition to our intellectual profile in teaching and research, in that he brings world-class expertise in important areas,” Coles says. “He will provide depth of perspective in capital markets, asset pricing and current issues in market liquidity.” Mehra’s background, Coles says, gives him the expertise and opportunity to be directly relevant to students during the ongoing, current, historical events.

In the Finance Department, Mehra will teach a Ph.D.-level investments course and an MBA course in applied finance. At the Prescott Center, the focus will be on research, knowledge dissemination and opportunities to host visiting scholars, creating an environment that facilitates creative discussions, he says.

“It’s a center to honor Ed Prescott’s contribution to economics,” Mehra says. “His ideas have fundamentally changed how we think about economic paradigms.”

Mehra will continue his research into intermediation, as well as a theory of financial crises and what causes them. He says it is possible to design a crisis-free model, such as a world in which the government owns all the capital. But there’s a tradeoff if we want the most talented entrepreneurs to run businesses rather than those who simply hold the capital.

The current crisis, he says, is due in part to a failure of regulation that allowed individuals and businesses to over-leverage. Many of those given loans were not credit worthy.

Still, the U.S. currently has one of the soundest economies in the world, he says. “We have a lack of liquidity in the financial sector, but the economy is resilient.”

What Guntermann and Liu have learned is that while every region is declining, the rate is beginning to stabilize. That’s good news for home sellers, Guntermann says, noting that the rate of decline must level off before it can reach zero and then begin climbing.

The ASU-RSI has been good for the W. P. Carey School, Liu says. “I think this makes us the cutting edge of research and disseminating data to practitioners. There’s interest across the country. Phoenix is a hot market.”

For updates from the monthly RSI report, check out The Center for Real Estate Theory and Practice Web site at wpcarey.asu.edu/realestate/Housing-Market-Reports.cfm. The report is currently free of charge.
Chuck and Chris Michaels are only beginning to think about the day they’ll send their children, 4 and 2, to college. But they have 10 other children attending ASU, thanks to their generosity.

For five years, the couple has awarded scholarships to Phoenix-area high school students. At first they honored their own alma maters, Shadow Mountain High School and Arcadia High School. Now they include applicants from Paradise Valley, Scottsdale and Tempe.

“We wanted to broaden it,” Chris says.

Chuck, a 1985 finance graduate, is vice president of the private wealth management division at Goldman Sachs in San Francisco. Chris earned her degree in health sciences at ASU and worked for several years in the healthcare industry. She now stays home with their children.

Their ties to ASU remain strong. “Chuck and Chris are both longtime supporters of ASU,” says Finance Department Chair Jeffrey Coles. Chuck serves on the board of the Student Investment Management Fund, has earned a distinguished alumni award and recruits graduates on campus for Goldman Sachs.

With their scholarship program, the Michaels are trying to recognize students who might otherwise fall through the cracks. They’re not looking to reward those at the top. Such students will be taken care of, Chuck says. What he’s looking for is the student “who has shown something else” and may not have been able to attend ASU because of the expense.

One recent recipient is a boy who has muscular dystrophy, one of four sons in his family with the illness. But the young man builds Web sites and also has begun organizing charity golf tournaments.

Another is a girl whose single mother emigrated from Iran speaking little English and supports her family working as a hairdresser. “We look at what they’ve overcome,” Chuck says.

Each student receives $2,500 a year, or about half of their tuition costs. The couple also mentors and tutors the students and keeps in touch by e-mail and personal visits.

Chuck and Chris are giving back for the education they received at ASU. Chuck remembers his dedicated finance teachers and learned how solid his training was when he earned his MBA at the University of Chicago alongside students from Columbia, Harvard and Yale.

Today’s students are equally prepared, he says. “I think the undergraduate students are outstanding. Pound for pound they’re really strong.”

Chuck and Chris Michaels intend to foster lifelong relationships with the students they’re assisting with scholarships, instill a positive outlook and teach them to in turn help others.

“It’s our hope to watch them graduate and realize how lucky they are even though they’ve had some difficult challenges,” Chuck says, “and that the idea of giving back is really important.”
Robert Konski has an apartment at the top of Telegraph Hill, near San Francisco’s Coit Tower, complete with a view of the Transamerica Pyramid and the Golden Gate Bridge. On weekends, he and his girlfriend explore Muir Woods and frequent the great restaurants in the City by the Bay. Oh, and he also has a great new job as a research associate in Wells Fargo’s Proprietary Portfolio Group.

“I love it,” he says, meaning his new job and his new city.

Konski graduated from ASU last year with a B.S. in finance and a B.A. in political science. Through ASU alum Sebastian Szendzielorz, a principal in the loan syndication group, he found out about an opening at the Wells Fargo PPG and flew in for the last day of interviews. The company wanted someone right out of college with no professional experience – but maybe with a slight edge.

The edge for Konski? He had once managed the undergraduate Student Investment Management Fund. At the time, he didn’t know that would be his ticket to a career, but no other young candidate had applicable experience, he says. How did he feel when he got the job? “Ecstatic is the way to put it.”

ASU and the Finance Department gave him the foundation. “It had everything to offer,” Konski says. “We’re a large school with a leading business program. The resources were there if you were willing to put in the effort.”

Now Konski’s hustle is paying off professionally. Some days are 16 hours long, but he likes a fast pace and challenging workload. His group is responsible for investing the company’s assets. “We’re a buy and hold group,” he says, a long-term program that provides a buffer from market turmoil.

When Wells Fargo bought struggling Wachovia Corp. in October, after battling with Citigroup Inc., for the sale, Konski celebrated along with his colleagues. “It was exciting. We finally got it.” Konski’s next goal is to manage a portfolio. Wells Fargo, he says, would be the right place to do that.
Teachers can't always tell which students will be special. Luke Millikin, the Turken Family Outstanding Graduating Senior of the W. P. Carey School of Business for fall 2008, is one of those special students.

When finance professor Herbert Kaufman first met Millikin, the young man seemed quiet, more sober than his classmates. As Kaufman got to know him, the pieces began to fall into place. Millikin had been a freshman at the University of Maryland when terrorists struck the World Trade Center on Sept. 11, 2001. He left college and joined the U.S. Army as a medic, eager to serve his country.

Millikin's tour of duty included assignments in Germany, Kosovo and combat zones in Iraq, where he handled 100 casualties. When he met Sgt. Tyler Prewitt, the two young men became best friends. Together they continued their education by taking online courses through the University of Maryland to earn associate degrees. Prewitt had grown up in Phoenix and extracted a promise from Millikin that after the service they would finish their degrees at ASU—together.

Prewitt was on a mission Sept. 24, 2004, when an armor-piercing RPG hit his vehicle. While under fire, two soldiers helped Tyler out of the vehicle, and he directed his own medical care until he was evacuated. Tyler never recovered and died on Sept. 28. Inspired by his friend, Millikin was committed to keep his promise and attend ASU.

When Kaufman learned Millikin's story, his mature demeanor made sense. “It all fits together,” Kaufman says. “He's a remarkable person. This is a pretty amazing man.”

Millikin was the Finance Department’s candidate for Outstanding Graduating Senior and was chosen by a seven-member committee from among candidates in all departments at the W. P. Carey School of Business.

Department Chair Jeffrey Coles was delighted with the news, saying he was proud of Millikin as a student in Barrett, The Honors College with a 3.97 grade point average, and as a member of the community.

“Many people will throw their stone into the ocean,” Coles says. “The ripples move outward for a while and then disappear in the ebb and flow of the tides. For a few unusual people, their stone generates ripples that in the end wash up on distant shores. Luke is one of these people. He has contributed to our community and country in ways that most of us can't hope to match.”

Millikin says he is “excited, flattered, honored and humbled” by the award, which comes with a $1,500 stipend from the Turken family. At graduation, he addressed the business college convocation, stressing the reality that one person can make a difference.

Millikin also remembered Sgt. Prewitt in his remarks.

“He was my best friend, and he had an impact on a lot of people. He was a hero and an inspiration.”
Leveraging Initiative and Determination Generates Results

Jazmin Medina is having a stellar year. Last summer, the finance senior completed an internship in investment banking at Goldman Sachs in New York City. In September, the company extended a job offer. And two days before her birthday Nov. 7, she was crowned Fiesta Bowl queen, an honor that is less beauty pageant than scholarship program helping to pay off Medina’s student loans.

She is accustomed to being busy. Drive and personality are what brought her to ASU and earned her six internships before launching her on a career path.

Finance Department Chair Jeffrey Coles calls Medina “an unbelievable student. She is voracious in seeking other ways of acquiring knowledge.”

When the American economy began to falter earlier this year, Coles was concerned that job openings in the financial sector would dry up for his students. “We worried a lot,” he says. But industry has proven kind to ASU finance graduates like Medina. “The ones at the top show initiative in the business world. That really shows through.” Industry, he says, is “looking for energetic and bright young people to mentor and groom. Our undergrads are well equipped.”

Medina, 22, grew up in Chicago and moved to Humble, Texas, when she was 12, easily making friends. “I wanted to meet people who were different and could challenge me, who could teach me things,” she says. She honed her skills in math. Laughingly calling herself a “nerd,” she says, “I just love numbers.”

Originally a journalism major, Medina switched to finance believing a career in the financial industry would take advantage of her natural gift with numbers and be more profitable. She wanted to be able to help her family financially. Her first ventures were in accounting. She secured a summer internship in the internal audit department of a Houston natural gas and oil company but found it tedious.

More satisfying was an internship at Inlign Wealth Management in Phoenix, again in accounting, but this time she picked the brains of those working in investment banking. Drawn to the competitive aspect of the field, Medina knew she had

JAZMIN MEDINA
’09 Finance Major
found her calling. She began to absorb as much experience as possible, volunteering for the undergraduate Student Investment Management Fund, which gives students a chance to work with the stock market.

She joined the ASU chapter of the Association of Latino Professionals in Finance and Accounting and became co-president. In 2007, Medina was named one of 32 ALPFA National Scholarship recipients. She next found a mentor in Gary Trujillo, founder of the Phoenix-based Be A Leader Foundation for underprivileged and minority students, which also awarded Medina a scholarship.

The financial field was not without challenges. Medina sought out an international scholars program, Sponsors for Educational Opportunity, that helps students of color find internships in investment banking. Her first interview with SEO was a grueling one that left her drained but determined to improve.

Following her sophomore year, Medina interned at the KPMG accounting firm in Tempe. When she next interviewed with SEO, she had boned up on banking (“I ate and breathed markets”) and also had set her sights on Goldman Sachs.

This time, Medina put her heart on the line. She was admitted into the SEO program, but Goldman Sachs offered her an investment banking internship. The internship introduced her to new mentors and new challenges as she worked extremely long and intense hours. She was impressed by the culture at the company, calling it “the best experience I could ever ask for.” In July, Medina joins Goldman Sachs in leveraged finance and investment banking. “I definitely think this is the best time for me to learn, to be creative,” she says. “I am so excited.”
What better way is there for a student to gain practical experience than getting on-the-job training and insight? And if one can earn credit hours while doing it, who can beat the opportunity?

That’s what junior and senior finance majors are able to accomplish in the department’s internship program. They can earn from three to six credit hours in a semester, depending on the number of hours worked and the project selected. Opportunities are available in corporate, institutional and sponsored situations. The experiences enable students to be compensated while taking on employment responsibilities that include an academic component in which they apply financial and/or accounting principles they have learned.

In 2008, 64 students completed the program, with most engaged in corporate internships with companies ranging from local small businesses to Fortune 500 firms. The enduring benefit for students taking part in internships is that the experience they gain translates to better job prospects. Companies gain, too, because they can observe potential future employees in action and identify bright, talented students whom they can hire for full-time positions upon graduation. Corporations hiring interns include national financial services companies; local, regional and national financial consulting firms; venture capitalist firms; real estate development corporations, healthcare corporations, and international technology companies.

If you or your company is interested in collaborating with the Department of Finance through the internship program, please contact Professor John Cesta at (480) 965-2969 or john.cesta@asu.edu.

WE WOULD LIKE TO THANK THE FOLLOWING COMPANIES FOR SPONSORING THE 2008 INTERNSHIP PROGRAM

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RECIPIENT

Justin Curran and Christopher Peters
Melissa Lou
Lance Olson
Robert Konski
Angela O’Connell
Luke Millikin

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Christopher Hoffman
Jeffry LaFrance
C. E. Christian Edin
Daichi Katase and Eric Lougher
Eric Lougher, Steven Thompson and Jenny Yi
Luke Millikin
Alia Eccles
Natalie Shvetsova
Robert Kennedy
Adam Markovich
Robert Harden

Robert Kennedy (left) accepts the Larry Seay & Barb Walchli Scholarship from Larry Seay.
Justin Curran (’08 Finance) receives the Wells Fargo Bank Award for Leadership in Finance from Wells Fargo representative, Melissa Shaw.
Alia Eccles celebrates being named the Craig Cerny Outstanding Scholar in Finance with Department Chair Jeffrey Coles.
MBA News

Well, we did it! The W. P. Carey School of Business MBA – Full-time Program is listed 22nd in the nation by U.S. News & World Report’s latest rankings of top MBA programs. Now, we have our sights on dislodging University of Texas at Austin, University of North Carolina at Chapel Hill, Indiana University and USC as we continue efforts to improve our position.

Entering enrollment in the full-time day program continues to be two cohorts of about 100 students. The GMAT score for this year’s entering class improved 21 points over last year’s class and now stands at 676. This score competes with many of the schools ranked above us.

Enrollment in the Evening and Online MBA Programs continues to increase. During the 2007-08 academic year, the school initiated an Accelerated Evening MBA Program with great success. Students complete the degree in 18 months as opposed to two years.

The Online MBA Program has a target of admitting four cohorts a year. In the past, there were two cohorts.

Evening MBA students continue to demand more finance courses. Last year we initiated an “emphasis” in finance, which requires nine credit hours. Classes filled.

The Executive MBA Program has now completed its transition to a bi-weekly format. The primary purpose of the change was twofold. First, provide greater classroom diversity by attracting managers from a broader mix of corporations, both within Arizona and from nearby states. Second, increase the managerial experience of the students. Both objectives have been accomplished. Currently, about 10 percent of the students are out-of-state and the experience level, as measured by salary and title, has increased.

In the full-time day program, our joint effort with the Supply Chain Management Department on the Supply Chain Financial Management Specialization continues to be popular with students and recruiters. The specialization provides a good blend of managerial finance issues with supply chain tasks.

Due to market declines, demand for the Real Estate Finance Specialization has not been as large as expected. To help the program through some growing pains, we opened enrollment to W. P. Carey School of Business honors students. Our expectations have not changed with respect to this program: We believe that it can become the best in the country.

An important part of the full-time MBA learning experience is an internship during the summer after the program’s first year. Our current first-year students found interesting positions at Intel, Apple, Motorola and a local biotech firm.

MBA students COLIN NELSON, BILL PAPPA, JAY KRUMME and JEREMY KELSTROM (left to right) discuss MBA Investment Management Fund performance.
Economic Conditions Provide Critical Real-World Experience for Students

For more than a decade, finance students have had a unique laboratory for learning about the stock market. The Student Investment Management Funds allow students to study the intricacies of the market by researching stocks and investing seed money donated by alumni. The students bear no personal financial risk but reap a wealth of knowledge.

In the 1990s, several ASU alums put up thousands of dollars so that MBA students could gain experience buying and selling equity without the students investing their own money. An undergraduate fund was added later – one of the few student investment programs in the country at the undergraduate level.

“It’s a real-world learning opportunity,” says Colin Nelson, manager of the MBA fund, which now is around $300,000.

Nelson and three other students who manage the portfolio meet weekly to discuss which new stocks might be added. Each student is responsible for researching four to five companies to determine whether they would make sound investments. Currently the fund is invested in such firms as General Electric, Johnson & Johnson, Walmart and General Dynamics.

“The main purpose is educational,” says Finance Professor Herbert Kaufman, faculty advisor to the funds.

Luke Millikin managed the undergraduate fund, which is now around $95,000. Its top performers are Pfizer and Verizon. The fall semester was Millikin’s third semester working with the fund along with six other students. Though two semesters are customary, Millikin wanted to provide a transition between James Booth, last year’s faculty advisor, and Kaufman.

A graduate in December, he’s learned not only how to invest but how to manage his team. “I’ve been able to get everyone’s input and have diversity of thought,” he says.

Current economic conditions have taught the student managers how to operate during adversity. Faltering markets might even be beneficial. “It’s certainly an experience the students last year didn’t have,” Nelson says. “It’s unique.”

Says Kaufman, “It’s an extraordinary moment.” He says students are learning that “stock selection can be overwhelmed by economic forces. A sinking boat takes down all hands.”

Both students said the mission of the funds is long-term investment, ameliorating the effects of a market roller coaster. “We consider ourselves investors, not traders,” Millikin says.

The financial laboratory can have career implications. Recent graduate Robert Konski believes his work on the undergraduate fund helped secure him a job with Wells Fargo in San Francisco. Other students applying for his job, he says, had no applicable experience.

2008 Stock Market Challenge

Arizona State University might not have been able to defeat our southern rivals in football this year, but when it comes to the stock market we have their number. In October, the Undergraduate Student Investment Management Fund sent two teams to compete in the National Bank of Arizona Stock Market Challenge, a charity event benefitting students in kindergarten through 12th grade in Junior Achievement. Teams from investment companies in the Phoenix area, including Charles Schwab and American Express, paid for their executives to attend the event and compete against not only one another, but ASU and the University of Arizona, as well.

The premise was simple: to invest a mock portfolio of $500,000 in 26 fictitious companies, with the winner being the team with the most money at the end of 60 trading days. The Sun Devils started off strong but were lagging behind the Wildcats after 30 days on the trading floor. The gap narrowed until the last trading day, when the ASU undergrads were behind their rivals by only a couple thousand dollars. The final bell rang and Arizona was announced as the winning school, and needless to say the ASU teams were unhappy. But disappointment turned into elation with the discovery that a mistake was made and the Sun Devils had actually passed the U of A in the last trade of the competition.

There was, however, one problem: the Wildcats, realizing the error, made a quick run for the door with the trophy that was rightfully ours. Luckily, the ASU fund manager, Luke Millikin, managed to track the group down and negotiate the release of the prized trophy. The event was a great experience and raising money to help Junior Achievement was a great cause, but taking the trophy back from U of A was certainly a highlight of the evening.
Wealthy investors love them. Wall Street admires their performance. The financial press demonizes them. We’re talking about hedge funds, which lately have been taking some of the rap for the nation’s economic downturn.

But 2008 ASU finance doctoral graduate Chris Clifford, who began teaching at the University of Kentucky in August, sees both sides of the hedge fund coin and says they are often unfairly disparaged because of the secrecy surrounding their portfolios.

Clifford published an article in the September issue of The Journal of Corporate Finance, “Value Creation or Destruction? Hedge Funds as Shareholder Activism.” Feedback from the article has been positive, Clifford says.

Hedge funds are the purview of so-called sophisticated investors – the wealthy, as well as pension funds, endowments and foundations. In the last 10 years, Clifford says, the hedge fund industry has more than doubled. While Americans want to be wealthy, they’re suspicious of those who attain wealth, he notes.

Hedge fund managers, grilled this fall on Capitol Hill, don’t do themselves any favors by being secretive and resisting attempts to further regulate what traditionally are lightly regulated holdings, Clifford says.

But highly paid managers work hard to create a vigorous portfolio for their clients, he adds, and shouldn’t have to share proprietary information. “This is their intellectual capital,” Clifford says. Heavy regulation could stifle what has been superior performance.

ASU finance professor George Aragon, who has published extensively about hedge funds, says it wasn’t surprising that in casting about for explanations in the faltering economy Congress would come down on hedge funds, some of whose managers have become billionaires. “It’s helpful to assign some blame,” he says.

The future of the funds is hard to predict, Aragon says as he reviews the latest data and examines the wide gap between the best and worst performers. “It warrants further exploration,” he says.

Clifford believes hedge funds could be more regulated but not heavily. “The pros and cons have to be weighed,” he says. Hedge funds should not be subject to the same regulation as mutual funds, for instance, but may benefit from greater transparency. Fund managers could file their dealings with regulatory bodies but not disclose that information to the public, he suggests. Bad managers could be weeded out. The wealthy would continue to invest, as would pension and institutional funds. Hedge funds would continue to operate privately with an array of investment tools and options available to them.

But hedge funds are here to stay. “I think they’re a very important part of the market,” says Clifford, who teaches corporate finance.

A strong connection between the Department of Finance and financial professionals is critical to the success of our world-class program. Finance Advisory Board members contribute significantly with their insight and feedback about curriculum, placement and research issues, ensuring that the department’s focus and efforts provide students with the skills and attributes important to business needs and current business finance practices so they can be successful. Many members also take their involvement steps further by offering internships to our undergraduate and MBA students, providing scholarships, and hiring graduates as full-time employees.

Our program is enriched because these executives share their talent and expertise to help us continually advance and improve. Mark Sokol of Vanguard joined this illustrious team in 2008, and Bob Auer now represents Intel Corporation, taking the place of Swati Lingnurkar, who played a vital role on the Board for many years.

If you or members of your firm are interested in learning more about the board and possible membership opportunities, please contact Jeanne Elliott at 480-965-5876.
Department Welcomes New Faculty Members

ANAND BHATTACHARYA
Professor of Practice

Universities don't often hire their own graduates. Anand Bhattacharya, who earned a Ph.D. in Finance in 1984, was an exception, says Finance Department Chair Jeffrey Coles. With Bhattacharya's background in industry, “he's a clear winner,” Coles says. “Anand was interested in the idea of giving back.”

Bhattacharya comes to ASU as a professor of practice after serving as president and CEO of Countrywide Capital Markets, a subsidiary of Bank of America. Before joining Countrywide, he held management roles in capital markets and risk management at Imperial Credit Industries Inc., and fixed income research and strategy, at Prudential Securities Inc.

Eager to return to academia and with family living in Arizona, Bhattacharya was happy to bring his industry savvy into the classroom. He will begin teaching in spring 2009.

GEORGE OLANDER
Lecturer

At 18, George Orlander’s father introduced him to investments. After a long career in financial analysis and portfolio management, Olander came to academia and spent eight years with the School of Global Management and Leadership at ASU West. He has joined the W. P. Carey School of Business Finance Department as a lecturer to teach introductory finance courses.

Olander holds a B.S. degree in political science-pre law from Xavier University, Cincinnati, Ohio; an MBA from Pepperdine University, Malibu, Calif.; and a DBA from United States International University in San Diego.

He brings real-world experience to the classroom as well as a year-long stint as the host of Money Matters, a San Diego television talk show. And as honorary Norwegian Consul for Arizona, his connections allow him to help students seeking careers overseas. He’s happy to be at the W. P. Carey School of Business. “This is new and different,” he says. “It’s good. I like it a lot.”

NEERU MEHRA
Lecturer

Neeru Mehra began her career as a social scientist and psychologist in India. After marrying economist Rajnish Mehra, she came to the United States in the late 1970s. She earned an MIA from the School of International Affairs and an MBA from the Graduate School of Business, Columbia University.

Since 1991, she has taught finance at the University of California, Santa Barbara. “Teaching was where my heart was,” she says. Now on leave of absence from UC Santa Barbara, Mehra has come to ASU with her husband, who will direct the new Edward C. Prescott Center for Advanced Studies in Economic Efficiency (see related story on page 5). “I am very comfortable at Santa Barbara, but I always like to have a challenge,” Mehra says. When her husband mentioned his offer from ASU, “I said it would be adventurous. Let’s go.”

Mehra will begin teaching undergraduate financial management as a lecturer in February.

WERNER BONADURER
Clinical Associate Professor

The first week of fall classes, newly hired Werner Bonadurer’s office was filled with students seeking investment banking advice as the U.S. economy took a tumble. “I felt I was counseling them on how to approach the industry,” he says with a laugh.

Students aren’t the only ones who value Bonadurer’s experience. Bonadurer, who has worked in global banking in the United States, Europe and Asia, was the guy the European press consulted as the U.S. economy took a tumble. “I felt I was counseling them on how to approach the industry,” he says with a laugh.

Bonadurer has been joint-chief operating officer of UBS’ Investment Banking division, a member of the Group Executive Board and global head of UBS’ Group Division Trading & Sales, and CEO of UBS Hong Kong. He also holds an MBA from the Wharton School of the University of Pennsylvania, and earned his doctorate at the University of St. Gallen in his native Switzerland. With an eye on research as well as a full teaching schedule, he’s happy to leave industry for academics. “This is my mission in life,” he says. “I just love it.”
ASU Finance Ph.D. candidates have a bright outlook for finding jobs despite the economic downturn, says finance professor Michael Hertzel.

“All indications right now are that the job market seems to be strong,” he says. Although many state schools and some private schools have announced hiring freezes, Hertzel believes top ASU graduates will ultimately be successful in finding positions in academia.

Chen (Ken) Wu is one of those job seekers hoping his efforts pay off. Wu has applied to more than 100 universities. Reared in California, he is hoping to stay in the West, and that’s where he’s found the most interest. He’s already had several interviews and has visited many of those campuses. He plans to graduate in May or August and will teach investments.

Wu is working on how the cross-listing of foreign company equity shares affects corporate governance. His results suggest that the benefits of cross-listing are more important for firms from developing countries and that external regulatory scrutiny from U.S. markets leads to less reliance on internal corporate governance measures. Wu is optimistic about finding a position. “ASU has a reputation as being a really good school,” he says. “It’s been a great experience.”

Sabatino Silveri is also in the job market. In his doctoral work, Silveri has been doing work in the area of mergers and acquisitions. Hertzel notes that “his research has uncovered some interesting findings on how shareholder composition and preferences affect method of payment and bid premiums in mergers.”

Every year the quality of finance doctoral candidates becomes more impressive, Hertzel says, resulting in better job placements. He believes last year’s class was outstanding. Graduates Chris Clifford, Zhi Li, Marko Svetina and Sriram Villupuram all found top-level jobs at universities (see related story on page 17).

Such alumni have helped build ASU’s reputation through performance and publications that garner high visibility, Hertzel says. “When students are seeking a Ph.D. program, the support of our alums often leads them to ASU.”

Competition is tough. Typically, only three new candidates are admitted each year. More foreign students are also discovering ASU, Hertzel says. They come to the U.S. to study and contribute. “Their objective is to teach students to advance the field with their dissertations, with their research,” he says.

Faculty members who have begun teaching at the doctoral level in finance include George Aragon, Hertzel, Tingjun Liu, Robert Marquez, Rajnish Mehra, Rajdeep Singh, Deniz Yavuz and Finance Department Chair Jeffrey Coles.

It’s a great roster, Hertzel says. “The impressive thing about this is that students get exposed to a broad spectrum of world-class faculty.”

To view a complete list of publications from ASU Ph.D. finance alumni, please visit wpcarey.asu.edu/fin/phd_alumni_research.cfm.

Interested in joining this group of top-notch ASU students? Be a part of the Ph.D. finance program and the tradition of academic and research excellence. For more information, contact Hertzel at Michael.Hertzel@asu.edu or visit wpcarey.asu.edu or visit wpcarey.asu.edu/fin/phd-program-main.cfm.
Chris Clifford has secured a job teaching corporate finance at the University of Kentucky in Lexington. “It’s great. I really like it here,” he says.

Best part of the job: meeting and interacting with bright students. Clifford also loves research and hopes to continue his work in hedge funds, mutual funds and shareholder activism. Since his teaching duties don’t begin until the spring semester, he’s devoting his time to research.

An August graduate, Zhi Li teaches corporate finance at Tulane University in New Orleans. Though smaller than the W. P. Carey School, with a smaller finance department, the Freeman School of Business at Tulane is “a nice research school with good research support,” Li says.

Li continues to work in research with Michael Hertzel, Richard C. and Carole Kraemer Professor of Finance. Her interest in the motivation of firms to issue seasoned equities was nurtured at ASU. “I think ASU was very important in training students how to do research,” she says. “ASU has a good environment encouraging students to work with faculty members.”

Marko Svetina might have traded the balmy weather of the Valley of the Sun for harsher climes when he graduated last summer, but instead he landed in equally balmy San Diego, where he now teaches corporate finance at the University of San Diego. “It’s just beautiful,” he says. “I couldn’t be more pleased.”

A faltering U.S. economy has provided an unexpected educational experience. The drama of the crisis has captivated Svetina’s San Diego students, who bring it up in virtually every lecture, he says. And special events on finance open to all students have packed auditoriums. Finance, he says, is now the second most popular major at the USD business school.

As an assistant professor of finance and real estate at Colorado State University, Sriram Villupuram is making connections. First, he is connecting with his students, whom he calls motivated and hard working. He’s also connecting with his community. In Fort Collins, CSU has become a brain trust that provides resources for those working in real estate. The university holds monthly conferences.

In his teaching role, Villupuram has settled comfortably into academia and credits his educational foundation at ASU, where Ph.D. candidates are given classroom experience. “The faculty were very helpful,” he says. “They get you started on teaching.” From his instructors, he learned how to gauge students’ strengths and weaknesses and now applies that intuition to his classes, which are made up of seniors and some ambitious juniors.
Seminar Series Generates Academic Interaction

Students, faculty and industry professionals regularly come together at Department of Finance seminars to learn about the most state-of-the-art research, discuss ideas and share feedback with researchers from throughout the country. The events also provide faculty and students with forums for sharpening presentation skills, engaging in interactive collaboration and networking to advance their professional and academic careers.

Additionally, through the Carr and Stephanie Bettis Distinguished Scholar Award Program two of the most renowned scholars in financial economics knowledge creation will share their expertise and insights during one-week visits to the W. P. Carey School of Business Department of Finance. Professors Philip E. Strahan of Boston College and Richard C. Green of Carnegie Mellon University will visit February 23-27 and April 6-10, respectively, and will present seminars February 27 and April 10.

Strahan, the John L. Collins S.J. Chair in Finance at the Carroll School of Management at Boston College, is a Sloan Fellow at the Wharton Financial Institutions Center and previously spent seven years in the Research and Market Analysis Group of the Federal Reserve Bank of New York. He earned a Ph.D. in economics from the University of Chicago in 1993.

Green, the Richard M. and Margaret S. Cyert Professor of Economics and Management at the Graduate School of Industrial Administration at Carnegie Mellon University, is a former director of the National Bureau of Economic Research. Green is also a former president of both the American Finance and Western Finance Associations.

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RICHARD C. GREEN—Carnegie Mellon University

MAY 1
TONI WHITED—University of Rochester

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ANTTI PETAJISTO—YALE UNIVERSITY
Topic: Should Benchmark Indices Have Alpha? Revisiting Performance Evaluation

DAVID ROBINSON—DUKE UNIVERSITY
Topic: The Importance of Being an Optimist: Evidence from Labor Markets

DETAILS ABOUT THE SEMINAR SCHEDULE ARE AT: wpcarey.asu.edu/fin/seminars.cfm
Honors Theses: Scholarly Projects

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JANAYE BURT
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AMBER WESSION
U.S. Wine Industry Analysis: The Profitability of Corporate Wine Investments


Information and Efficiency in Tender Offers by Robert Marquez, Bilge Yilmaz. Econometrica, September 2008 (Vol. 76, Iss. 5; pp. 1075-1101)


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$275 for industry professionals who are ASU alumni or members of the Economic Club of Phoenix. Discounts are available for groups and for individuals with government or university affiliation.

Sponsorship opportunities are available, and your involvement would be welcome. Please call (480) 965-5876 for information.