Acc 280K.7– Summer 2017

Financial Statement Analysis

Professor
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By appointment

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TA
John Bunde (MPA and former student).

Course Summary: This Financial Statement Analysis course focuses on using an array of financial information to best determine the why behind past performance. To achieve this we combine quantitative and qualitative factors to understand drivers of performance and to tell the story of the firm. With a solid understanding of the past, we move towards motivating sound forecasts and briefly discuss well-supported inputs to valuation models.

This course is advised for individuals who possess all of the following:
1) an interest in learning and a willingness to develop new skills and perspectives;
2) an interest in how businesses operate, make decisions, change and report their performance;
3) a willingness to benefit from and contribute to the UT/McCombs’ educational experience;
4) a general, but strong, understanding of financial accounting at an introductory level as the logical language of business. This course builds off of your Financial Accounting class.

What you should expect:
Historically this has been a challenging class that requires a commitment. It is not challenging as you must memorize complex formulas that you could easily look up in the real world, but as it will challenge perspectives and require critical thinking and the synthesis of information. This is also a class that actively shuns memorization of terms and formulas and the regurgitation of anything. We will not waste your time (and your educational investment) with memorizing items such as ratios or formulas or emphasizing jargon and catchphrases over thoughtful analysis. Instead we will focus on more useful ways of approaching various issues. Therefore, you may hear many “Yes, but…” questions: “Yes, but in your own words,” “Yes, but why?” “Yes, that is the general economic argument, but how has it played out in this scenario?” “Yes, that is the change, but what drove that change? …We will get dirty trying to best understand various firms and how to best use financial information. You need to be involved in these discussions.

How to do well and get the most out of the experience:
This class is also one that has a straightforward plan for success as directly affirmed by former students. Students who truly commit to all of the following usually end up with solid grades: (1) consistently preparing for class; (2) being active learners within the classroom and on the Discussion Board and (3) carefully reviewing the material with peers after class.

1 This is a draft syllabus, but major changes are not expected. The official schedule will be posted and updated on Canvas.
A Broader Background of the Course

Our objectives include:

- Increase our understanding of financial filings (including financial statements, managers’ commentaries, footnotes and other sources of financial information) in order to:
  - Understand how firms operate and create value—*we put considerable emphasis on understanding how financial information helps us understand and guide operating decisions.*
  - Concisely articulate the firm’s past—*without this, valuation and forecasting could be misguided, so we must be able to tell the story of the firm.*
  - Increase our understanding and ability to use tools to analyze information presented in financial statements. Understand the benefits and limitations of financial information provided in financial filings and the motivation for and process of making adjustments to this information—*we will adjust, change and challenge ratios, metrics and formulas to ensure they work in specific real-world situations.*
  - Use our understanding of the firm and its financials to make informed predictions about future performance—*we will stress how understanding financial information provides us with an excellent framework for considering the future.* Motivate, understand, construct and implement various inputs in valuation models—we will very briefly note the mechanics of valuation while stressing the more useful and challenging steps of motivating inputs to valuation. *Real valuation is not only a mechanical exercise.*
  - The course will be taught using a combination of examples, discussion questions, cases and homework problems. We will learn new concepts using various firms’ historical and current financial data.

To achieve these objectives, during the semester we will learn a framework for business analysis and valuation. The steps in the framework include:

1. **Business Strategy Analysis**: The purpose of business strategy analysis is to assess the profit potential of the firm at a qualitative level. This involves understanding the firm’s strategy and its industry and considering how these affect and are affected by the firm’s financial performance.

2. **Financial Analysis**: The purpose of financial analysis is to assess the firm’s historical financial performance in the context of its goals and strategies. Tools used for financial analysis include ratio analysis, cash flow analysis, and common-size financial statements. *Ratio Analysis is not computing ratios (i.e., division), but carefully using and changing ratios to provide us with information.*

3. **Accounting Analysis**: The purpose of accounting analysis is to develop an understanding of whether a firm’s accounting captures its true underlying economic condition(s). This involves understanding accounting transactions, identifying accounting flexibility, evaluating the appropriateness of accounting policies and estimates, and at times, altering financial statements to enhance decision making.

4. **Valuation/Prospective Analysis**: The purpose of valuation/prospective analysis is to forecast the firm’s future financial performance and determine a potential valuation of the firm—our best assessment of intrinsic value. To do this we will learn the mechanics and intricacies of forecasting financial statements and we will (very briefly) note the components and usage of valuation models.

We will review (and learn) accounting concepts as this knowledge is critical to making decisions with financial information. However, the primary objective of the course is *not to improve our understanding of Generally Accepted Accounting Principles (US GAAP or IFRS)*; the goal is to improve our ability to interpret and use financial statements in a variety of settings including a primary focus on credit and equity analyses and supplemental coverage of corporate finance, planning and control. *This is not a journal entry class; in fact, we will likely not see any journal entries.*
Structure, Materials and Logistics

Course Structure
- The class format involves coverage of the main areas and tools noted above. In addition, there will be a considerable amount of discussions/cases that focus on specific firms and specific financial issues. These cases will involve a careful analysis of the financials, the opportunity to dig deeper to support (or challenge) information that is presented, and the consideration of the benefits and limitations of various tools, metrics and ratios.
- The course will be taught using a combination of examples, discussion questions, cases and homework problems. We will learn new concepts using various firms’ historical and current financial data.
- A tentative schedule of class meetings is attached to the end of this document. This schedule may be revised and all updates will be posted on Canvas or discussed in class.

Materials
- **Required:** It is required that you read, used and retained the materials and information from the financial accounting class. Our course builds off these and works on the assumption that you are a responsible adult who did not slack off in that class (or dismissed that class as you foolishly took the exceptionally dated (and wholly incorrect) perspective that accounting is just bookkeeping.
- **Required:** Cases, slides and other materials created by the professor and available on Canvas.
- **Required:** We will also have a Discussion Board on Canvas, with both required and additional material.
  - To ensure the highest dissemination of information and to maintain a fair playing field, all non-personal questions must be asked on the Discussion Board and not emailed to me.
- **Strongly Recommended Text:** The textbook for the course is *Financial Reporting, Financial Statement Analysis and Valuation: A Strategic Perspective* by Wahlen, Baginski and Bradshaw, *eighth edition*. ISBN: 978-1285190907
  - The textbook is strongly recommended for students who have not had sufficient exposure to the material we cover in class. The class moves fast and assumes you mastered material from prior classes. We do not have slides, cover or read from the text; it provides background reading.
  - Suggested Texts:
    - *Accounting for Value* by Stephen Penman; Ben Graham’s *The Intelligent Investor*; Michael Lewis’s *The Big Short*; Pat Dorsey’s *The Little Book that Builds Wealth* and Michael Shearn’s *The Investment Checklist: The Art of In-Depth Research*. This is not a comprehensive list and I am open to your suggestions.
- Throughout the course we will be examining publicly available material including corporate press releases, corporate filings (10K’s, etc.), analyst reports, and articles from the business press. When appropriate, these and other supplemental information (or links to these documents) will be provided via the Canvas class pages or Discussion Board. You will be responsible for downloading and printing these articles and using links posted on Canvas.
Assignments and Grading Information (page 1 of 4)

Course Requirements and Grading

We will determine the final distribution of letter grades at the end of the semester. This means that numerical scores on specific assignments do not correspond to a particular letter grade prior to the end of the semester. Final grades are determined by summing up all pieces, then ranking all students and then following the class distribution. Some areas of the distribution may be very tight. This means that it is mathematically unavoidable that some students with similar grades do not get the exact same final letter grades. Ultimately, someone must fall at each “break point” that means that someone gets the lowest of one grade (for example, the lowest A-) and someone else, with similar grades, gets the highest of the next letter grade (for example, the highest B+). The class’s distribution dictates the percentage of each of the letter grades. That is, you and your classmates’ performance, more than I, determine your final letter grade. Students may not ask for exclusive extra credit or grade changes at the end of the semester. This is unprofessional and requesting specific treatment violates our University’s academic goals. Moreover, challenging the grades, points, allocation or policies after the semester has begun is unprofessional and may result in a lower final grade as it signifies a departure from the expectations of the class. Constructive comments are warmly welcomed as long as they are made by the first day of class.

Your numerical grade will be determined as follows:

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<thead>
<tr>
<th>Requirement</th>
<th>Percentage</th>
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<tbody>
<tr>
<td>Exam (7/17/2017)</td>
<td>40%</td>
</tr>
<tr>
<td>Cases</td>
<td>50%</td>
</tr>
<tr>
<td>Class Participation</td>
<td>10%</td>
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<td><strong>Total</strong></td>
<td><strong>100%</strong></td>
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Description of Requirements

Exams (40%)

There will be one exam. It will be held during class on Monday, July 17, 2017. This is cumulative exam covering all FSA classes. The exam will involve the lessons from class applied to a set of financial information from one or a small number of publicly traded firms. Please notify me immediately if you have a conflict with the exam date. All notifications of exam conflicts must be received before the start of the class.

The exam is primarily built around class discussions and cases and involves your analysis of an actual company’s (or companies) financial information. This exam is not one for which you should try to cram. You prepare for the exam by doing the work day to day in this class and then by relaxing the week before the exam. Cramming is not useful and a class for which you can cram is a good example of a class not worth taking.
Assignments and Grading Information (page 2 of 4)

Cases (50%)

The primary objective of the Cases is to help you review the material before attending class. The fancy term for this is the “flipped classroom” but this is simply old-fashioned education from your rather old-school professor that helps ensure you can master the material by getting exposure and taking direct ownership of working through new ideas. Unless clearly noted otherwise, all Cases are due before class. These Cases will be posted on Canvas. Submissions are also on Canvas.

There are seven pre-class cases required by all students and one in-class case.

You are required to submit ALL of Cases #1 through #7 and the in-class case. Cases cannot be submitted late. Cases must be submitted on Canvas in the respective link.

Group Work

You must submit your own case for each Case. However, you are encouraged to work in a group of up to three people on all of the Cases (groups of four or more are not allowed and must split into smaller groups). This means you can discuss answers within this group of two or three people, but cannot simply copy/paste answers—each student needs his or her own submission and set of answers. You must list the other people you worked with on your case submission and you must ensure that all group members are on the same page and list each other. The goal of allowing groups is to enable you to actively share ideas but still be involved; the case discussions are most important. There is a cap to group sizes as large groups remove the benefit from working through the material. If a name is missing, all members get a 10% penalty for the first transgression and a 50% penalty thereafter. Group work means you are encouraged to discuss the questions and answers. Directly sharing files or copying answer (including copied answers with minor edits) across group members and/or other groups is a violation of the policies of our University and will not be accepted.

In the past, students have effectively used Skype, Facetime, etc. to collaborate from different locations and good, old-fashioned meetings to collaborate in person. All assignments should be submitted electronically through Canvas using a program that is compatible with Microsoft Office. You are responsible for uploading the final version, checking and re-checking any issue with formatting or other errors before submission.
Assignments and Grading Information (page 3 of 4)

Class participation and leadership (10%)

Much of class is conducted in a discussion setting during which we will analyze specific firms and discuss which metrics are important, the reasons for our approach, and the implications of our choices. The assignments are geared to prepare you to participate in and learn from these discussions. Accordingly, your completion of the assignments and your participation in our discussions are vital. If you are not involved in the discussion on your own, you should prepare for cold calling. At times, I will only be a facilitator of your discussions with each other. After most classes, I will make class notes, with particular attention to the quality of comments or questions, not the quantity. You do not need to be correct to participate: insightful questions and thoughtful answers are also important and I encourage students to answer, even when they are unsure. Moreover, a strong, smart and vibrant academic community is a part of why you and your classmates are here at UT.

Consistent with what is noted above and in light of the expectations of this program and much you’re your jobs, you are clearly expected but not forcibly required to attend all classes. As your absence can detract from the learning experience of others, if you will miss part of or a whole class, you should post to our Discussion Board before (or after) class when this occurs. The post can include an apology to your classmates, if sincere, and can include whatever information you believe is both personally and professionally prudent. If, for any reason, you are uncomfortable posting the circumstance to the class, you may email me. That being said, you do not need to apologize to me—you and your classmates, not I, lose out from your absence. If you miss class you should obtain the slides, talk to your colleagues (classmates) about the course materials and discussions and post any unresolved issues to the Discussion Board.

Here’s a general idea of how I plan to grade your class participation over the course of the semester:

• Outstanding Contributor: Consistent and sustained contributions to large-group discussions reflect thorough preparation. Ideas offered are usually substantive, provide good insights and sometimes change the direction of the class for the better. Arguments, when presented, are generally well-substantiated and often persuasive. If this person were not a member of the class, the quality of the large-group discussions would be diminished significantly. In addition to exceptional large-group discussion contributions, also actively participates in small-group discussions.

• Good Contributor: Consistent contributions to large-group discussions reflect satisfactory preparation. Ideas offered are usually substantive, generally provide useful insights, and occasionally offer a new direction for the discussion. Arguments, if presented, are reasonably well-substantiated. If this person were not a member of the class, the quality of the large-group discussions would be diminished. In addition, also offers comments in small-group discussions.

• Marginal Contributor: Generally routine contributions to large-group discussions reflect some minimal preparation. Ideas offered are occasionally substantive but seldom provide clear insights or new directions for the discussion. Arguments may be occasionally presented but are generally not well-substantiated. If this person were not a member of the class, the quality of the large-group discussions would be diminished only slightly.

• Non-participant (around 0-2 percentage points out of 10%): This person has maintained good attendance, but has said little or nothing in class; hence there is no adequate basis for evaluation. If this person were not a member of the class, the quality of the discussions would be unchanged.

• Disruptive Contributor (negative points): If present in class at all, contributions to discussions reflect inadequate preparation. Ideas offered are rarely substantive, provide few, if any, insights and never offer a constructive direction. At best, contributions are obscure, confused, and indicate a lack of familiarity with the fact of the issues under discussion. At worst, comments demonstrate disrespect for others in the academic community. If this person were not a member of class, valuable airtime would be saved.
Assignments and Grading Information (page 4 of 4)

- Disruption includes consistently arriving late, leaving or packing up early or using a cell phone during class or other disruptive behaviors. I hope no one achieves this grade as this represents a major lack of professionalism and respect for our University. A student in this category may not pass the class, regardless of the other grades.

Our class will also make use of Discussion Board. This is the forum for outside-of-class questions related to assignments, our class coverage and any related current events. In addition, as the Discussion Board is an important way to share information and knowledge across the class, each student must post a constructive question or comment or respond a class-related post at least once during the semester. Moreover, constructive Discussion Board involvement can help enhance your Class Participation and Leadership grade, but the primary driver of performance is the classroom experience. (Logistical questions such as “Where is the Excel file?” are always welcomed, but cannot enhance your grade.)

Grading Disputes
My grader and I make every effort to grade all of your work fairly and accurately, but grading errors can occur. If you believe there is an error, you may request a re-grading of the assignment. Be aware, however, that grading errors can occur in both directions - errors can make grades too high as well as too low. Therefore, if you request a re-grading, your entire assignment will be re-graded, and all grading errors will be corrected. By requesting a re-grade, you accept the possibility that your grade may go either up or down. To request a re-grade, you must submit a written request to me within 72 hours from the time in which the assignment’s grade was released to students (whether or not you were present in class on that day or checking email). The request must be accompanied by the original, if I do not retain it, and must state the area of dispute, your recommendation for change in grade, an explanation or justification for your recommendation and any limitations to this recommendation. The re-grade request must refer to the guidelines established in this syllabus.

Informal discussions about how a student can perform better are allowed, but a student should first be able to clearly articulate (in person or in writing) how their submission compared to the discussion from the class (and any posted materials) for the pre-class cases or the posted materials for the post-class cases and also be able to discuss the expectations as noted in this syllabus.
Academic Integrity and University Policies (page 1 of 2)

Cheating involves copying work across groups, cheating on the exam, plagiarizing your assignments and other things as well. Don’t cheat as (1) it is wrong; (2) the costs far outweigh the benefits: you don’t want to get kicked out in a short-sighted attempt to make a B a B+; and (3) there is a very good chance that your cheating will be revealed and we will all be extremely disappointed.

Policy on Scholastic Dishonesty

The McCombs School of Business has no tolerance for acts of scholastic dishonesty. The responsibilities of both students and faculty with regard to scholastic dishonesty are described in detail in the BBA Program’s Statement on Scholastic Dishonesty at [http://www.mccombs.utexas.edu/BBA/Code-of-Ethics.aspx](http://www.mccombs.utexas.edu/BBA/Code-of-Ethics.aspx). By teaching this course, I have agreed to observe all faculty responsibilities described in that document. By enrolling in this class, you have agreed to observe all student responsibilities described in that document. If the application of the Statement on Scholastic Dishonesty to this class or its assignments is unclear in any way, it is your responsibility to ask me for clarification. Students who violate University rules on scholastic dishonesty are subject to disciplinary penalties, including the possibility of failure in the course and/or dismissal from the University. Since dishonesty harms the individual, all students, the integrity of the University, and the value of our academic brand, policies on scholastic dishonesty will be strictly enforced. You should refer to the Student Judicial Services website at [http://deanofstudents.utexas.edu/sjs/](http://deanofstudents.utexas.edu/sjs/) to access the official University policies and procedures on scholastic dishonesty as well as further elaboration on what constitutes scholastic dishonesty.

Copyright and Intellectual Property

The course packet and other materials are the intellectual property of your professor and are given to you, for free, on an individual basis only. You may not, in anyway, share, distribute or post electronic, hardcopy or other versions of the class materials with other people or on websites or other avenues of social media without explicit permission from me. Posting or sharing materials, or even snippets of materials, will be considered a violation of our University’s Academic policies for all parties involved and may lead to a failing grade in this class. This includes all websites, apps and social media; the only exception is that you may post class-related material to our class’s Canvas Discussion Board during the semester.

Recording Class:

Recording all or any part of class without explicit written permission from the professor is strictly prohibited. Violations will constitute a violation of the academic integrity policies of our University and may lead to a failing grade in this class and legal prosecution. If you need to record the class, please email me to seek permission at least a week in advance and include details about the date, topics, individuals involved and a clear explanation of the reasons for this need.

Privacy in Canvas:

Information in Canvas is protected by your UTEID login. If applicable, please be aware that I will use a merged Canvas site for all sections, if there is more than one, of a course that I teach. This will allow students in other sections to see that you are enrolled in the course and send you email from within Canvas. However, they will not actually learn your email address and no other personal data will be revealed through Canvas. If you have any concerns, please contact the ITS Help Desk at 475-9400 for help removing your name from view of other students.
Additional Important Notifications

Students with Disabilities
Students with disabilities may request appropriate academic accommodations from the Division of Diversity and Community Engagement, Services for Students with Disabilities, 512-471-6259, http://www.utexas.edu/diversity/ddce/ssd/.

Religious Holy Days
By UT Austin policy, you must notify me of your pending absence at least fourteen days prior to the date of observance of a religious holy day. If you must miss a class, an examination, a work assignment, or a project in order to observe a religious holy day, you will be given an opportunity to complete the missed work within a reasonable time after the absence.

Students with Personal Challenges
If you face any personal challenges that may affect your coursework or need advice or assistance for any serious health or personal matter, please reach out to the Student Emergency Services. Information can be found here: http://deanofstudents.utexas.edu/emergency/

Campus Safety
Please note the following recommendations regarding emergency evacuation from the Office of Campus Safety and Security, 512-471-5767, http://www.utexas.edu/safety:

- Occupants of buildings on The University of Texas at Austin campus are required to evacuate buildings when a fire alarm is activated. Alarm activation or announcement requires exiting and assembling outside.
- Familiarize yourself with all exit doors of each classroom and building you may occupy. Remember that the nearest exit door may not be the one you used when entering the building.
- Students requiring assistance in evacuation should inform the instructor in writing during the first week of class.
- In the event of an evacuation, follow the instruction of faculty or class instructors.
- Do not re-enter a building unless given instructions by the following: Austin Fire Department, The University of Texas at Austin Police Department, or Fire Prevention Services office.
- Behavior Concerns Advice Line (BCAL): 512-232-5050
- Further information regarding emergency evacuation routes and emergency procedures can be found at: http://www.utexas.edu/emergency.
Case and class details are provided on Canvas, see each specific class page for the official assignments and schedule.