



## *FIN 394.1 Advanced Corporate Finance*

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**Office Hours: Thursdays, 1:30pm to 3:30pm, and by appointment at other times**

### **Course Overview**

The objective of this course is to develop an understanding of the decisions financial managers face. In this course we will approach problems from the perspective of the Chief Financial Officer. We will focus on decisions concerning raising money (equity, debt, convertible bonds, etc.), and spending money (project valuation, acquisitions). The first part of the course will deal with real investment decisions, while the second part will address decisions about how to finance those investments. In the final part we will talk about M&A and the market for corporate control.

Understanding CFO-type decisions will be helpful long before you become a CFO. For example, if you are working at a treasury group of a corporation, the material is directly relevant. If you are an investment banker you need to understand the rationale for designing and issuing securities. If you are in marketing or production, evaluating projects and understanding how the CFO makes her decisions are important. Finally if you are in consulting, capital budgeting and capital structure decisions will be the main agenda in many of your contracts.

Much of the material will be presented using simple examples designed to demonstrate how financial decisions can create, destroy, or modify value. Homework assignments will expand on these examples. However, the main issues we cover are conceptual. This is not the sort of class where solving a lot of exercises is useful; rather, it is important to master the main concepts.

## Prerequisites:

Financial Management and Statistics are required; Valuation is strongly recommended.

## Books and Materials:

**(Required) Textbook:** Mark Grinblatt and Sheridan Titman, *Financial Markets and Corporate Strategy*, 2<sup>nd</sup> Edition (Irwin/McGraw-Hill, 2002)

- The book is available in several different formats:
  1. The chapters that we will cover are available as a custom book, which will be available at the University Co-op (ISBN: **9781121112759**).
  2. The book is also available as an e-book at <http://create.mcgraw-hill.com/shop/>. Two versions are available: The custom book that includes only the chapters we will cover (ISBN **9781121125766**), or the whole book that includes the remaining chapters as well (ISBN: **9781121125759**).
  3. You may find a used copy of the hardcover version.

## **(Required) Course Packet**

- You can obtain the course packet from the copy center on the third floor of GSB.

## **(Required) Lecture Notes and Class Handouts**

- These will be available on Blackboard as the course develops.

The following books are **NOT** required. I have listed them here in case you wish to get a different perspective on a topic. Alternatively, once you land the CFO job, you might want something for the bookshelf.

- Robert C. Higgins, **Analysis for Financial Management** (7<sup>th</sup> ed.) Irwin/McGraw-Hill, 2004.
- Richard A. Brealey, Stewart C. Myers, and Franklin Allen, *Principles of Corporate Finance* (8<sup>th</sup> ed.), Irwin/McGraw-Hill, 2006.
- Stephen A. Ross, Randolph W. Westerfield, and Jeffrey F. Jaffe, *Corporate Finance* (6<sup>th</sup> ed.), Irwin/McGraw-Hill, 2002.
- Joel M. Stern and Donald H. Chew, Jr. eds. *The Revolution in Corporate Finance*, (4<sup>th</sup> ed.), Blackwell Business, 1998.

## Other Sources

- *The Wall Street Journal*, *Financial Times*, the *New York Times* business section, the *Economist*, or *Business Week* are all recommended. We will cover the conceptual material to help you think through financial decisions. However, details of a particular issue a recruiter might ask your thoughts on may come from the press.

## Grading:

Homework Assignments and Case Write-ups	25%
Class Participation	10%
Midterm Exam	25%
Final Exam	40%

- There is one exception to the above grading rule. **If your final exam score is in the top 20% of the score distribution (of the two sections that I teach), you will get an A in this course, regardless of your midterm and assignment scores.** The only condition for this is that you have been a “good citizen,” that is, participated in lectures, handed in homework assignments and case write-ups, and took the midterm exam.
- You may work in groups of **up to five** for homework assignments and cases. Please submit one write-up per group, and make sure to indicate all group members’ names on the first page. There is no need to work with the same group of people throughout the term. Assignments must be handed in *at the start* of the class in which it is due. Late assignments will not be accepted.
- Homework assignments include applied problems and exercises. Case write-ups should be memos of at most five double-spaced pages (excluding exhibits and appendices). For each case, I will assign some specific questions to be addressed. Grading of case reports will be based on how well you justify your arguments and support them with detailed and careful analysis. You should think of case reports as presentations you make to a board; to receive credit, your arguments must be convincing.

## How to do well on the exams:

- Problem sets and in-class exercises provide the best preparation for the exams.
- The exams will be closed book. The final exam will cover the entire course, although it will be weighted toward the material we will cover after the midterm.

## Discussion board:

I will use Blackboard's Discussion Board to answer questions about problems we solve in class, homework problems, sample exam problems, etc. If you have a question, please post it to Blackboard. I will try to respond to questions on the Discussion Board at least once per day, and more frequently right before assignment due dates and exams.

## Schedule:

A tentative schedule appears below.

## Articles and Cases Included in the Course Packet

### Articles

1. Alex Triantis and Adam Borison, “*Real Options: State of the Practice*,” Journal of Applied Corporate Finance 14-2, 2001. (Reprinted in *Stern and Chew*, 2003).
2. Thomas Copeland and Peter Tufano, “*A Real-World Way To Manage Real Options*,” Harvard Business Review, March 2004.
3. John R. Graham and Campbell R. Harvey, “*Theory and Practice of Corporate Finance – Evidence from the Field*,” Journal of Financial Economics 61, 2001.
4. “*Vanderbilt University Roundtable on the Capital Structure Puzzle*,” Journal of Applied Corporate Finance, 11-1, 1998.
5. Bengt Holmstrom and Steven N. Kaplan, “*The State of U.S. Corporate Governance: What’s Right and What’s Wrong?*” Journal of Applied Corporate Finance, 15-3, 2003.
6. Robert F. Bruner, “*Where M&A Pays and Where It Strays: A Survey of the Research*,” Journal of Applied Corporate Finance 16-4, 2004.
7. George Andrade, Mark Mitchell, and Eric Stafford, “*New Evidence and Perspectives on Mergers*,” Journal of Economic Perspectives, Vol. 15-2, Spring 2001, pp. 103-120.

### Cases

1. Arundel Partners (HBS 9-292-140)
2. Massey Ferguson, 1980 (HBS 9-282-043)
3. MCI Communications Corp., 1983 (HBS 9-284-057)
4. Paramount Communications Inc. 1993 (Casenet South-Western College Publishing)
5. Paramount Communications Inc. 1994 (Casenet South-Western College Publishing)

## **Class Schedule & Assigned Readings**

Date                      Topic (numbers represent sections in Grinblatt & Titman's textbook)

### **January**

#### **PART I: VALUATION**

Tue. 18                      Valuation of Corporate Assets: Basic Concepts and Methods (Ch. 10, 11)  
Thu. 20                      Valuation of Corporate Assets - continued  
Tue. 25                      Option Pricing (Ch. 8)  
Thu. 27                      Real Options and Corporate Strategy (12.1, 12.2, Articles 1, 2)

### **February**

Tue. 1                      Real Options and Corporate Strategy – continued – *Homework 1 due in class*  
Thu. 3                      Real Options and Corporate Strategy – continued (Article 3 Part I)

#### **PART II: CAPITAL STRUCTURE AND FINANCIAL POLICY**

Tue. 8                      Capital Structure I: The MM Benchmark (14.1, 14.2, 14.3, 15.2)  
Thu. 10                      CS I continued, Capital Structure II: Trade-off, Tax Considerations (14.4, 14.5, 15.3, 15.5, 15.6) – *Homework 2 due in class*  
Tue. 15                      CS II continued (14.4, 14.5, 15.3, 15.5, 15.6)  
Thu. 17                      **Case 1: Arundel Partners**  
Tue. 22                      Midterm review – *Homework 3 due in class*  
Thu. 24                      *Midterm Exam, 6-8pm, room TBA, no classes*

## March

- Tue. 1 Capital Structure III: Bankruptcy and Financial Distress (16.1, 17)
- Thu. 3 Capital Structure III - continued
- Tue. 8 **No class – Plus trips**
- Thu. 10 **No class – Plus trips**
- Tue. 15 **No class – Spring break**
- Thu. 17 **No class – Spring break**
- Tue. 22 Capital Structure Recap; Bankruptcy Costs and Debt Holder – Equity Holder Conflicts (16.2, 16.3, 16.4, Article 4)
- Thu. 24 Bankruptcy Costs and Debt Holder – Equity Holder Conflicts – continued
- Tue. 29 Bankruptcy Costs and Debt Holder – Equity Holder Conflicts – continued
- Thu. 31 Corporate Risk Management (Ch. 21)

## April

- Tue. 5 Corporate Risk Management – continued
- Thu. 7 **Case 2: Massey-Ferguson**
- Tue. 12 Information Conveyed by Financial Decisions (Ch. 19) – **Homework 4 due in class**
- Thu. 14 Information Conveyed by Financial Decisions – continued (Article 3 Part II)
- Tue. 19 Corporate Governance and Managerial Compensation (Ch. 18, 10.3, Article 5)
- Thu. 21 **Case 3: MCI**

## **PART III: MERGERS, ACQUISITIONS, AND THE MARKET FOR CORPORATE CONTROL**

- Tue. 26 M&A and the Market for Corporate Control (Chapter 20, Articles 6 and 7) – **Homework 5 due in class**
- Thu. 28 M&A and the Market for Corporate Control - continued

## May

- Tue. 3 **Case 4: Paramount 1993**
- Thu. 5 **Case 5: Paramount 1994**