

University of Pennsylvania – The Wharton School
Advanced Corporate Finance

FNCE 726
MW 9:00-10:30
Huntsman Hall: TBD
Spring 2003

Matthew McBrady
Office: Steinberg Hall-Dietrich Hall 2206
Tel: 746-0004
mmcbrady@wharton.upenn.edu
Office Hours: M 2:30-4:30 and by appointment
Course Webcafe at URL TBD
Teaching Assistants: Pete Jensen, Todd MacLean, Scott Segal

Summary

Advanced Corporate Finance extends the core theory introduced in Financial Analysis. It is designed for students intending to pursue careers in corporate finance (e.g. as members of the finance department of an industrial corporation or the corporate finance group of an investment bank). The course is also well-suited to students wishing to gain experience in applying the theory introduced in Financial Analysis to real world case examples.

My section of the course is taught entirely with cases. The case method of instruction offers a number of distinct advantages. In preparing cases, you learn more than just the financial theory at the heart of each case. You learn about the agents, institutions, and transactions that comprise modern financial systems. You also “learn” to contribute effectively to fast-paced discussions about complex financial issues – issues for which there rarely is a “right” answer.

These benefits come at a cost, however. Discussion-based classes succeed only if *all* students come prepared to discuss the case material. To foster mutual trust and respect, it is pivotal that students attend *each* class, arrive on-time, and minimize subsequent class disruptions. Class participation is vital – to your learning as well as the learning of all others. Accordingly, it figures heavily in determining your final grade (see “Grading” below). In my experience, “cold calling” is the only incentive strong enough to ensure adequate preparation. I will cold call at least one student to “open” each case discussion (see “Format” below). Unexcused absences from class and opening comments that reflect little prior preparation will be weighted heavily in determining your final grade.

Course Content and Organization

The theme of this course is value-based management. A common criticism of complex financial techniques is that they are imperfect. The value-based management response is simple: these techniques substitute measurement error for chaos in financial decision-making. They discipline managers by expressing key decisions in terms of their *measurable* impact on firm value.

Consistent with this theme, the course consists of 6 modules (**Exhibit A**). The first three modules focus on “Financing Operations.” These modules cover a range of financial issues that confront firms in their ordinary course of doing business. The final three modules focus on “Financing Transitions.” These modules illustrate the importance of finance in facilitating – and, sometimes in *precipitating* – major organizational changes. Given recent market developments, the second

half of the course emphasizes Bankruptcy and Restructuring, issues not covered as thoroughly in other sections.

Initial cases review and supplement techniques learned in Financial Analysis. More sophisticated valuation techniques are introduced as they become necessary to tackle the managerial problems featured in each case. During the term, you will use virtually all valuation techniques used on Wall Street. Beginning with simple weighted average cost of capital (WACC) valuations, you will value projects and companies with alternative present value (APV), real options, method of multiples, and equity cash flows (ECFs). By encountering these techniques in the context of specific managerial problems, you should emerge from the course knowing not only how to use them, but *when* to use them as well.

Exhibit B depicts the resulting matrix structure of the course. It plots course modules across the top and valuation techniques on the left side.

Course Materials

As evident in **Exhibit A**, we will cover 18 cases in 26 class meetings. All cases are required reading. For cases in which new valuation techniques are introduced, explanatory notes are also assigned. If you are already familiar with the relevant technique, you need not read the explanatory note. Even those of you with investment banking experience, however, are likely to find the notes quite useful. Cases and notes comprise the majority of the required reading for the course. They are included in a bulk pack along with selected journal articles that are strictly optional.

In addition to the cases and notes, I will also direct you to relevant background material in the following two texts:

Brealey & Myers, 2000, Principles of Corporate Finance (6th Edition).

Higgins, 2000, Analysis for Financial Management (6th Edition).

You should already own a copy of Brealey&Myers. Any recent edition will do, though I will refer you to readings from the 6th edition. The only required readings from these texts will come from Higgins. It is the only good source of explanatory material for the techniques and analyses featured in Module 1. It is expensive, particularly for a paperback. I will have several copies on reserve, but you may wish to purchase your own copy for convenience.

Those of you interested in corporate restructuring might also want to purchase:

Gilson, 2001, Creating Value through Corporate Restructuring: Case Studies in Bankruptcy, Buyouts, and Break-ups. (1st Edition).

Like Brealey&Myers, this text is *not* required. All required cases and notes from Gilson's book are in your bulk pack.

Course Format

There are *no* written case assignments during the term. Your only assignment is to read carefully the assigned cases and, where necessary, associated technical notes as well. The lack of written work can be both a blessing and a curse. It leaves you with more time to read, analyze, and discuss the cases before class. It also, however, leaves you with little "objective" feedback as the term progresses. Half way through the term, I will provide you with written feedback regarding your class participation (see "Assessing Class Participation" below). Throughout the term, I will also be happy to schedule individual meetings with you to discuss class participation.

Nonetheless, if you know yourself to prefer frequent external feedback, you might prefer enrolling in another section of FNCE 726.

Despite the lack of written work, you will find that preparing adequately for class discussions represents a taxing workload. Suggested study questions typically require detailed calculations. In many cases, they require full-blown valuations. Each student is responsible for these questions. All questions are “fair game” if you are cold called to open class.

To help manage your workload, you will be required to self-select into groups of three or four students during the first week of class. Groups offer an invaluable opportunity to leverage your efforts with regard to the calculation-intensive study questions. They also enable you to “try out” ideas prior to class discussion. Group meetings prior to class are not mandatory, *per se*. But you will find it difficult to succeed in the course without them. Groups will also be responsible for completing a joint mid-term case analysis (see “Grading” below).

Assessing Class Participation

A primary goal of this course is to provide you with the opportunity to learn how best to contribute to discussions about complex financial issues. Corporate financial decisions are inevitably made in groups. In group settings, a well articulated expression of confusion is more valuable than an abruptly delivered “right” answer (former investment bankers beware). What is important is how your comments impact our overall understanding of the managerial decisions at hand. I assess your class participation according to this metric. Not having a background in finance does *not* put you at a disadvantage with regard to class participation.

You might worry that grades for class participation are subjective. Some degree of subjectivity is unavoidable. Unfairness is not. To minimize subjectivity, your class participation is marked *daily* on a 0 to 3 point scale. The TAs provide your initial mark, and I discuss the marks with them after class. In determining your grades, we consider the degree to which your comments advance *everyone’s* learning. Quality is much more important than quantity. We expend a great deal of effort to ensure your grades are as objective as possible.

At the time of the mid-term exam, I will provide you with written feedback on your class participation. This feedback will include specific examples of your most helpful contributions, as well as the grade you would have received at that point. Time permitting, I will be available for individual meetings to discuss your mid-term feedback. I am also happy to meet with you to discuss class participation more generally as the term progresses.

Grading

Class Participation

Given the pivotal importance of case discussions, class participation will count for 33% of your final grade. Students will be excused for absences due to illness or that are necessary to observe religious holidays. Unexcused absences will have a significant impact on your final grade.

Failure to prepare for class reflects an unacceptable disregard for your fellow students. Everyone’s learning is dependent on *everyone’s* preparation. Inevitably, circumstances will arise that leave you with insufficient time to prepare. If so, I ask only that you inform me of this prior to class. If you do not and are cold called to open class discussion, it will be embarrassing for you and disastrous for the subsequent discussion. I will consider it an explicit breach of trust, and you will find it difficult to get more than a QC grade for the course.

Mid-term exam

The mid-term exam will consist of both quantitative and qualitative short-answer essays. Like class participation, it will count for 33% of your final grade. It will be a two-hour exam, and is intended to be time-sensitive. In many financial settings, *timely* answers are as important as “correct” ones. Unless you meet regularly with your Group and work through the case analyses we discuss, you will be unable to complete the exam in two hours.

Final Exam

The final exam will be a take-home case analysis that you will also complete individually. It will count for the remaining 33% of your final grade. The final exam is not intended to be time-sensitive. The “question,” however, will be much more open-ended than questions from your midterm exams. To answer it, you will need to synthesize much of the material we cover throughout the course.

Academic Integrity

There are a limited number of good cases in finance. In preparing for class discussions, you are permitted to use any publicly available information about the individuals and companies we consider. You are strongly encouraged to prepare cases with members of your Group. You are *not* permitted to use work completed by any other students. This applies to members of other Groups, as well as previous Wharton students or students from other business schools.

Your ability to retain the knowledge gained in FNCE 726 will be a direct function of the amount of time you spend working through the cases. Inappropriate reliance on the work of others is self-defeating. It is a form of plagiarism and will not be tolerated.

Exhibit A: Module Structure for FNCE 726

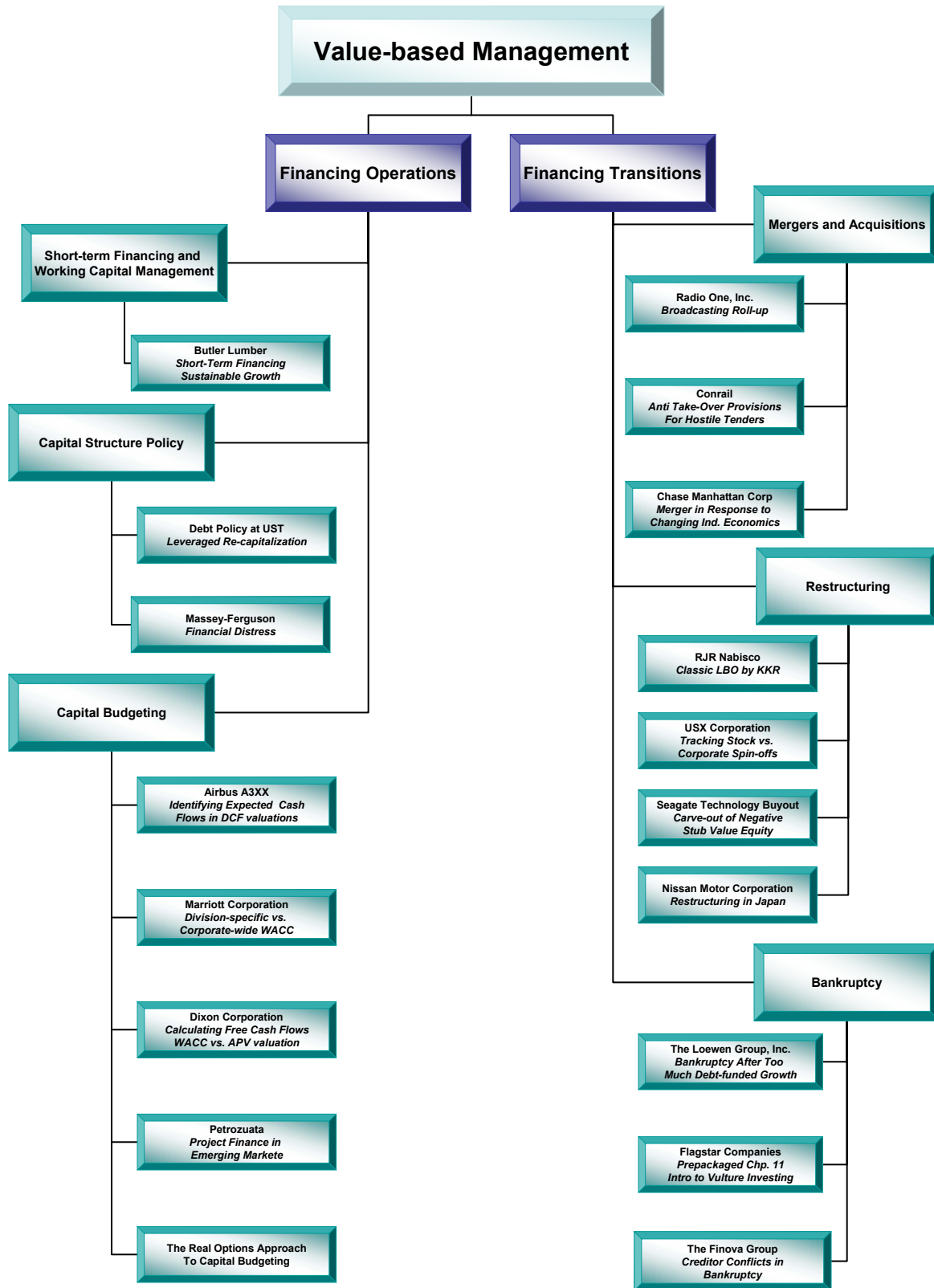


Exhibit B: FNCE 726 Case Breakdown by Module and Valuation Technique

Valuation Technique	Financing Operations			Financing Transitions		
	Module 1: Working Capital Management	Module 2: Capital Structure Policy	Module 3: Capital Budgeting	Module 4: Mergers and Acquisitions	Module 5: Restructuring	Module 6: Bankruptcy
WACC / Review of Basic Techniques from Financial Analysis	3 classes Butler Lumber Dell's Working Capital	2 classes Debt Policy at UST Massey-Ferguson	8 classes Marriott Corp. Dixon (Day 1) Airbus	6 classes Radio One (Method 1) Conrail	4 classes	3 classes The Loewen Group
Alternative Present Value (APV)			Dixon (Day 2)	RJR Nabisco	Seagate	Flagstar (Method 1)
Real Option Valuation			Options Approach to Capital Investment			
Multiples				Radio One (Method 2)	USX Corp. Nissan	Flagstar (Method 2)
Equity Cash Flows			Petrozuata	Chase Manhattan		Finova Group