

UNIVERSITY OF PENNSYLVANIA
The Wharton School

FNCE 726: ADVANCED CORPORATE FINANCE

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Fall 2010

Office: Steinberg Hall-Dietrich Hall Room 2344
Office Hours: Mondays 3:30-5:00 pm or by appointment
Teaching Assistants: To be announced

Course Objective

The objective of this course is to teach students how to apply modern financial theory to the investment and financing decisions of a modern corporation. The course is designed for finance majors who will pursue careers in major corporations, the financial sector, and consulting firms. The core theory introduced in Financial Analysis course is extended for applications to the strategic financial decision areas of a firm.

Course Content

Financial theory explains the real world using abstract and simplified models. Such conceptual models are often not sufficiently rich for dealing with all the complexities of the real world. Financial decisions based on rigorous theory and models are superior to ad hoc alternatives. Concepts and techniques introduced in this course should help you express key decisions in terms of their impact on firm value.

This course consists of seven sections. The first four sections focus on a range of financial issues that confront managers in their ordinary course of doing business; mainly financial planning, capital budgeting, and the interaction between investment and financing decisions. The options approach to investment decisions is in Section IV. Section V deals with financing decisions, and security issuance and dividend policy is introduced in Section VI. The last two sections of the course focus on corporate restructuring, mergers, and acquisitions.

Course Format

This course is taught mostly with cases. We will have a few review lectures. The course will succeed only if all students come to class well prepared. Class participation is vital to your learning as well as the learning of others. Furthermore, to foster mutual trust and respect, it is imperative that students attend each class, arrive on time, and minimize subsequent class disruptions.

Textbooks

Cases are the only required reading materials in this course. For some cases, explanatory teaching notes on your reading list might be useful. If you need to review the prerequisite background materials for the cases, you may refer to the relevant chapters indicated in the following two or any similar texts:

R. Brealy, S. Myers, and F. Allen, *Principles of Corporate Finance*, 9th or any recent edition, Irwin, McGraw-Hill, 2006. (Henceforth, BMA)

T. Koller, M. Goedhart, and D. Wessels, *Valuation: Measuring and Managing the Value of Companies*, McKinsey & Company, Inc., John Willey & Sons, Inc., 4th Edition, 2005. (Henceforth KGW)

The text by Koller et al. is a valuation book written from practitioners' perspective. Copies of both texts will be on reserve in the Lippincott Library.

Readings in Course Pack

The course pack is available on line through Study.net. It contains all of the cases and other recommended readings. Students will be charged for class handouts that will be distributed regularly throughout the term

webCafé

The course site on webCafé contains suggested questions for cases; Excel files for exhibits for most cases and lecture notes and handouts will be distributed in class. You will find the most updated information and announcements for the course on webCafe, such as office hours and rooms for the teaching assistants, review sessions, exams, and guest speakers. webCafé is the information center for the course. Please check the course site regularly.

Grades

The final grade for the course will be based on:

1. Class attendance (20%)
2. Class participation (20%)
3. Midterm Exam (30%)
4. Final Exam (30%)

1. Class Attendance

Case courses require attendance. If you cannot attend the course for any reason, you should not take this course. Students will be excused for absences due to illness with the approval of the MBA Program Office or that are necessary to observe religious holidays.

2. Class Participation

Your active participation is expected. Your comment's impact on the understanding of the problem under discussion is more important than the right answer per se. Your class participation will be assessed on this metric, not on "air time" or the number of comments you make. A well articulated question in some instances is equally valuable as an abruptly delivered "right" answer.

Cold calling is the only incentive strong enough to ensure adequate preparation. I will start the class by cold calling a student to open the case discussion. Failure to prepare for class reflects an unacceptable disregard for your fellow students. Everyone's learning is dependent on everyone's preparation.

You are welcome to make a 15 minute presentation of any case at the beginning of class as a group. This will count toward your class participation.

If you cannot prepare for class for any reason, inform me of this prior to class.

3. Midterm Exam

The Midterm Exam is on Wednesday, October 27 from 6:00 to 8:00 PM. I will announce the rooms before the exam.

4. Final Exam

The date and the place for the final exam will be announced by the University Registrar.

Both exams are "open book" and "open notes". Exams will consist of problems similar to those in the cases, but they will be shorter and more focused. No laptops are allowed in the exams. You will need a financial calculator and know how to use it.

I will not allow anyone to take the exams at another time unless you have official permission from the MBA office. If your travel plans conflict with the exam dates, you should either change your travel plans now or enroll in a different section of the course.

All graded materials will be returned to your mail folders.

Study Groups

You are encouraged to form groups of four or five students during the first week of classes. Groups should offer an opportunity to leverage your strengths with other team members for a more comprehensive case analysis. Suggested study questions often require extensive calculations and/or valuations. Your team members also enable you to try out your own ideas prior to class discussion.

Guest Speakers

We will have one or two guest speakers during the term on current developments in financial markets. In order to accommodate the schedules of the guest speakers, we may have to reschedule one or two classes. I will notify you in advance if we need to reschedule any class.

Review Sessions and Office hours by Teaching Assistants

I will offer periodic review sessions for those needing extra help with the prerequisite finance theory. Teaching assistants will also hold office hours to answer your questions. The rooms and schedules of TA office hours will be posted on webCafé.

Correspondence by e-mail

I will not provide lengthy answers to your course related questions or hold tutorial sessions by e-mail. Use office hours, review sessions, or TA office hours for that purpose.

Workload

This course is very quantitative and the pace is fast. The work load is very heavy. Case preparation require significantly more time than lecture-based courses. Furthermore, you should be thoroughly familiar with the material taught in the Financial Analysis course. The course is designed for finance majors and is not a remedial course for those who want a second chance to learn finance. We will not review the materials covered in the first year finance course. Lectures will only cover new material.

Unlike an introductory finance course, this course uses real world cases where the information is seldom complete to make a decision or solve a problem. Your results may differ depending on the initial set of assumptions you have to make in the absence of complete information. If you have difficulty with such ambiguity and the case method of teaching, this course may not be for you.

Academic Integrity and Code of Ethics:

Most case materials in this course are based on real events and companies. In preparing for class discussions or presentations, you may use any publicly available past or current information about the companies covered in cases. You are strongly encouraged to study cases in a study group. Any submitted assignments for grading should be your own. In case of group work, it should be your group's joint work only. Each member of your group is expected to contribute equally to group work.

You cannot use work completed by other students, old notes or handouts, or solutions to the cases from previous years or other sections of this course at Wharton or similar courses at other business schools or elsewhere for any purpose. Violation of this rule will result in an automatic failing grade for the course. Furthermore, the violators will be reported to the Wharton Graduate Division for further disciplinary action.

If you use materials from any public or private source, including those sources on the internet, private company presentations, etc. in your submitted work for any reason, you should properly cite them. Otherwise, it may be considered plagiarism.

If you register for this course, you agree with the principles of academic integrity described above in conjunction with the Wharton Graduate Division Code of Ethics.

*** Acknowledgements:**

I would like to acknowledge the contributions of many colleagues and friends to the development of this course. They provided course outlines, teaching notes, reading materials, software, and assistance for case writing; and some shared their expertise as guest lecturers. I would like to thank:

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I fondly remember the great contributions of Isik Inselbag, Irwin Friend, James Walter, and Merton Miller. I owe a special debt to Isik Inselbag with whom we developed and taught this course for two decades at the Wharton School.

I. INTRODUCTION

Readings: BMA, Chapter 1
KGW Chapters 1-4

1. Lecture: Introduction and Course Overview

II. FINANCIAL ANALYSIS AND PLANNING

Readings: BMA, Chapters 29-31
Teaching Note: "Assessing the Financial Health of a Firm"

2. Case: Clarkson Lumber Company

III. VALUATION THEORY AND CAPITAL STRUCTURE

A. Identifying the Relevant Cash Flows for Capital Budgeting Projects

Readings: BMA, Chapters 2-6 and 10-12

3. Case: Empirical Chemicals A&B

B. DCF Methods for Valuation

Readings: BMA, Chapter 17-19
KGW, Chapters 5-9
Teaching Note: "Alternative Methods for Estimating Terminal Value"
Teaching Note: "An Introduction to Cash Flow Valuation Methods"
Teaching Note: "The Adjusted Present Value Method for Capital Assets"
Teaching Note: "Valuing Equity Cash Flows"

4. Lecture: Capital Structure and Valuation Theory I
5. Lecture: Capital Structure and Valuation Theory II
6. Case: M&M Incorporated (posted on WebCafé)

C. Cost of Capital and Capital Structure

Readings: BMA, Chapters 7-9, and 19
KGW, Chapters 10 and 11
"What Practitioners Should Know About Future Value" by M. Kritzman

7. Case: Marriott Corporation

D. Interaction between Investment and Financing Decisions

Readings: KGW, Chapters 11 and 12

8. Case: Galveston Fishing Company (posted at WebCafé)
9. Case: Kennecott Copper Corporation
10. Case: Southport Minerals
11. Case: American Chemical Company
12. Lecture: Review

13. MIDTERM EXAM Wednesday, October 27. 6:00-8:00 PM Room to be announced

IV. THE OPTIONS APPROACH TO CAPITAL INVESTMENT

- Reading: BMA, Chapters 20-22
Teaching Note: "Capital Projects as Real Options: An Introduction"
KGW, Chapter 20
"The Options Approach to Capital Investment" by Dixit and Pindyck
14. Lecture: Review of Option Valuation Models I
15. Lecture: Review of Option Valuation Models II
16. Case: Chrysler's Warrants
17. Case: MW Petroleum Corporation

V. DIVIDEND POLICY

- Readings: Brealy and Myers, Chapter 16
18. Case: Avon Products

VI. CORPORATE FINANCING DECISIONS

- Readings: BMA, Chapters 13-15 and 23-26
KGW, Chapter 17
19. Case: Airbus 380: Buy or Lease Decision

VII. FINANCIAL DISTRESS & CORPORATE RESTRUCTURING

20. Readings: Readings for this session are posted on the webCafé
Case: The KMART Restructuring

VIII. MERGERS & ACQUISITIONS

- Reading: BMA, Chapters 32-34
KGW, Chapter 7 and 17-19
21. Case: Philip Morris
22. Case: Conrail A&B
23. Case: SFM
24. Case: RJR Nabisco
25. Lecture: Overview

FINAL EXAM	December 22 at 6:00-8:00 PM. Room to be announced by the registrar's office
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**FNCE 726: ADVANCED CORPORATE FINANCE
COURSE SCHEDULE FOR FALL 2010**

Session #	Date	Topic and Assignments	Class Format
1	Sep 08	Introduction	Lecture/Case discussion
2	Sep 13	Clarkson Lumber Company	Case discussion
3	Sep 15	Empirical Chemicals A&B	Case discussion
4	Sep 20	Capital Structure and Valuation Theory I	Lecture
5	Sep 22	Capital Structure and Valuation Theory II	Lecture
6	Sep 27	M&M Inc.	Case discussion
7	Sep 29	Marriott Corporation	Case discussion
8	Oct 04	Galveston Fishing Company	Case discussion
9	Oct 06	Kennecott Copper Corporation	Case discussion
	Oct 11	Fall Break	NO CLASSES
	Oct 13	No class	Rescheduled to Oct 25 4:30-6:00 PM
10	Oct 18	Southport Minerals	Case discussion
11	Oct 20	American Chemicals	Case discussion
12	Oct 25	MCI	Case discussion
13	Oct 25	Review	Q&A Session 4:30-6:00 pm
14	Oct 27	MIDTERM EXAM	6:00-8:00 PM/No regular classes
15	Nov 01	Option Valuation Review	Lecture
16	Nov 03	Option Valuation Review & Real Options	Lecture
17	Nov 08	Chrysler's Warrants	Case discussion
18	Nov 10	MW Petroleum Corporation	Case discussion
19	Nov 15	Avon	Case discussion
20	Nov 17	Airbus 380: Lease or Buy Decision	Case discussion
21	Nov 22	Guest Speaker	4:30-6:30 PM
22	Nov 24	Philip Morris	Case discussion
23	Nov 29	Conrail A&B	Case discussion
24	Dec 01	SFM	Case discussion
25	Dec 06	RJR Nabisco	Case discussion
26	Dec 08	Overview	Lecture/Q&A Session
	Dec 22	FINAL EXAM	6:00-8:00 PM room TBA