

FNCE 207 & 728: CORPORATE VALUATION

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Wharton School
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I will only answer emails containing simple questions about administrative issues. I will not answer emails that ask for long explanations about the material. These questions should be asked in class, during the TAs' daily office hours, or by scheduling an appointment with me.

Office Hours: For convenience, my office hours are by appointment. Simply send me an email to schedule a meeting. See course website for the TAs' daily office hours.

Class Times: Section 207-001: Monday/Wednesday, 12:00 - 1:20 PM in JMHH 250
Section 728-001: Monday/Wednesday, 1:30 - 2:50 PM in JMHH 250
Section 728-002: Monday/Wednesday, 3:00 - 4:20 PM in JMHH 250

1. *Course Objectives.*

The objective of this course is to learn firm, debt, and equity valuation methods in a framework that is both conceptually rigorous and relevant for practice. While there are new concepts introduced in this course, the emphasis is on the practical application of finance and accounting concepts already covered in other courses to valuing real companies.

The subject matter of this course is relatively technical and difficult. Students who took this course in the past have indicated that the **workload is extremely heavy** compared to other courses. Because of its technical nature, this course does not appeal to all students and is only recommended for students motivated to learn valuation techniques in great depth. I believe in communicating the complexity of the tradeoffs one faces when valuing companies. We will not gloss over important issues, even if they are difficult to understand. **Students who hope to never see financial statements again should not take this course. Working knowledge of Microsoft Excel is also essential.** Students interested in broader topical coverage and a less detailed examination of valuation techniques should consider the Advanced Corporate Finance course instead.

This course is designed for students with little or no practical work experience in valuing companies. However, several former students with prior work experience or a CFA training still found this course valuable to take. From time-to-time we will discuss common

errors that practitioners make or issues that they tend to ignore. It is important to fully understand the meaning and consequences of each shortcut we might consider using when valuing a company. In some cases, a few shortcuts are justified because they will have little to no impact on the valuation outcome and more complex methods would not be worth the time required. In other cases, the same shortcuts will lead to serious errors in the valuation outcome. We will discuss areas where there is uncertainty about how best to perform certain tasks and what is typically done or ignored. We will then discuss the relevant academic research on the topic, so that students have an appreciation of the issues and the alternative views on the matter.

2. *Non-Negotiable Pre-Requisites.*

- A. Introductory Corporate Finance.
- B. Introductory Financial Accounting.
- C. Working knowledge of regression analysis.
- D. Working knowledge of Microsoft Excel.

Students coming in with a weak understanding of the accounting and finance concepts covered in the core courses will feel at a disadvantage in this course. Note also that knowledge of intermediate accounting is preferable for this course, although it is not required. Stronger accounting skills will, of course, make some of the material easier to understand.

3. *Course Material.*

- A. Course Textbook

The required text is Corporate Valuation: Theory, Evidence and Practice (2nd Edition) by Robert Holthausen and Mark Zmijewski, published by Cambridge Business Publishers. Make sure to purchase the **newly published 2nd edition**, as it contains essential updates about the U.S. tax code. The book is available through the bookstore or at this link:

<https://cambridgepub.com/book/corpval2e>

- B. Course Website

Material for the valuation projects and additional readings will be posted for student access on Canvas. I will also upload **abridged** versions of the PowerPoint slides used for the lectures. Slides will not be distributed in hard copy as they generally follow the notes in the textbook, but students wishing to access the abridged slides prior to class will be able to print them out or upload them on their tablets in the morning of each lecture. You can gain access to the Canvas website at:

<https://canvas.upenn.edu/>

- C. Other Useful References

Corporate Finance by Berk and Demarzo. This is a text virtually all students should own

having taken Introductory Corporate Finance. If you own an alternative corporate finance textbook (such as Principles of Corporate Finance by Brealey, Myers, and Allen), that will suffice as well. This text is just background reading for finance concepts you should already know.

Financial Accounting by Libby, Libby, and Short. This is a text virtually all students should own having taken Introductory Financial Accounting. If you own an alternative financial accounting textbook (such as Intermediate Accounting by Kieso, Weygandt, and Warfield), that will suffice as well. This text is just background reading for accounting concepts you should already know.

Damodaran on Valuation by Damodaran. This valuation textbook is quite popular and covers many of the concepts covered in this class, but with less depth than our main textbook.

The Dark Side of Valuation by Damodaran. This valuation textbook covers advanced concepts linked to the valuation of young, distressed, and complex businesses.

The Signal and the Noise by Silver and Superforecasting by Tetlock and Gardner. Entertaining introductions to the process of forecasting under uncertainty: **we are not trying to forecast everything perfectly, we are simply trying to be as precise as possible given the information we have!**

Reading the Financial Times (<http://www.ft.com>), the Wall Street Journal (<http://www.wsj.com>), or any close substitute (<http://www.thestreet.com>) is highly recommended. Following financial news will be essential for valuing your company.

4. **Grading.**

Student grades will be based on the following weights:

Class Participation (e.g., attendance, preparation, discussion)	10%
Valuation of a Company (divided in 3 stages)	30%
Exam I	30%
Exam II	30%

A. Class Participation and Classroom Etiquette

Class participation counts for 10% of your grade. I will base my grading **on attendance, preparation, and participation**. Some classes require students to be prepared to discuss in-class exercises, while others will follow a lecture format. **I expect students to have read the assigned chapters prior to the lectures.** During lectures, I encourage students to ask questions. Voluntary class participation is expected, but I will also **cold call** on individuals from time to time.

The educational experience for everyone suffers if participation or attendance becomes a problem. Students are thus expected to **attend every single lecture and refrain from using**

electronic devices for non-educational purposes. Phones and laptops are not allowed in class --- only tablets in a flat position are allowed for digital note-taking purposes. Students should arrive on time for class and remain there until the lecture is completed. Arrivals and departures during class time interfere with the educational process and are disrespectful to other students and to the instructor. Since my sections tend to be at full capacity, **students must attend the section for which they are registered.** In the case of a **rare conflict**, students may attend another section; I teach the same class in the same room at 12:00, 1:30, and 3:00 PM on Mondays and Wednesdays. However, students must notify me by 10:00 AM on the day of the lecture if they plan to attend a different section. **Violating these basic norms of classroom etiquette will significantly lower students' participation grade.**

Note also that attendance to the first lecture is mandatory for all registered students. It is also strongly encouraged for the students on the waitlist. Any registered student who fails to attend the first lecture will be automatically de-registered from the course. The first lecture is used to set clear expectations about the course's objectives and its workload. Students should then acquire the necessary information to make a quick decision about whether they want to stay enrolled and form a team for the valuation project or leave their spots to students relegated to the waitlist (if applicable).

B. Projects and In-Class Exercises

As part of the course, students will be asked to value a company of their own choosing in a team of up to four students (more on teams later). Each team will have to submit three separate reports, one for each stage of the valuation project. Late submission will incur a penalty of 10% per calendar day, counting the day of submission. Complete instructions for this project are available on the course website. It would be wise to form teams and start thinking about potential companies to value as soon as possible. **Team composition and the names of 3 candidate companies you would like to value are due on January 29.**

Note that exercise and project deadlines are marked on the calendar below as either S or D. If marked S, students must submit their assignment **before noon** on that day. If marked D, students must be **prepared to discuss the exercise in class**, though it does not need to be submitted.

Using solutions handed out in prior years for discussed exercises or the work of prior or current students who are not members of your group on any submission is considered a violation of the code of student conduct. If caught, the penalty will be severe. Moreover, your exam performance (assuming you did not get caught) will suffer as these assignments and projects are intended to help you learn the material.

C. Exams

The best way to prepare for the two exams is by going through examples from the lecture notes and the end-of-chapter exercises in the textbook after each lecture and working through past exams prior to taking the actual exams.

The first exam will be administered **in class** on **February 26** and will cover Chapters 1-7. The second exam will be administered **in class** on **April 13** and will cover all material mentioned in the course (with an emphasis on Chapters 8-14). **You are responsible for ensuring that you are available to take both exams on campus.** I will not email exams to remote locations. I will not permit anyone to take the exams at another time unless that person is gravely ill or faces a significant emergency (which needs to be documented).

If your travel or interview plans conflict with the schedule of the course, you must change your plans now or drop the course.

5. *Teams.*

Assignments and valuation projects can be worked on individually or in teams of up to four students. MBAs and undergraduates may not be on a same team but teams can include students from different MBA sections. I encourage all students to work in teams to maximize the learning experience. **I will not become involved in group problems.** In choosing teammates, students should keep in mind the broad skillset that each team needs to possess: accounting, finance, and Excel modeling. **Also make sure that all teammates' performance/grade targets for this course line up.** Team composition needs to be set by the time teams submit the names of the candidate companies they would like to value.

6. *Academic Integrity.*

Students are expected to follow the university code of academic integrity. Examinations are to be the work of the individual student using only the material permitted during the examination. Submitted assignments should be the work of **only the team members** listed on the title page of the document. **Students should not in any way rely on the work of prior students or current students who are not on their team.** This prohibition extends to prior homework, cases, or projects that are directly relevant to the assignment being completed. When a project requires you to produce a forecasting/valuation model, the use of a model not created exclusively by the students on the team for the purposes of this class is a violation of the code of academic integrity. **For all submitted assignments, students must start with an Excel spreadsheet which is at most populated with raw data.** Moreover, as indicated previously, the company being valued must be one that none of the team members has valued previously. If you have questions concerning this policy, please see me for a clarification before you use any questionable material. **If you violate this policy, failing the class will constitute the minimum penalty, regardless of the degree of your violation.**

COURSE CALENDAR**SPRING 2020**

NOTE: TOPICS COVERED, ASSIGNMENTS, AND DATES ARE SUBJECT TO CHANGE

Date	Topic	H & Z Chapter	Assignment (D=Discussion & S=Submission)
15-Jan	Introduction to Course and Valuation	1	
22-Jan	Creating Economic Value	1	
27-Jan	Measuring Economic Value	2	
29-Jan	Computing Free Cash Flows	3	S - Names of 3 Companies to Value
3-Feb	Creating a Financial Model	4	D - Interpreting Financial Ratios: P2.1, P2.3
5-Feb	Creating a Financial Model	4	D - Computing Free Cash Flows: P3.1
10-Feb	Various Forecasting and Measurement Issues		
12-Feb	DCF Valuation Methods	5	D - Computing Interest Tax Shields: P3.12
17-Feb	Excess Earnings Valuation	7	
19-Feb	Measuring Continuing Value	6	D & S - Valuation Project: Stage 1
24-Feb	Catch-Up and Review		D - Using DCF Method: P5.6
26-Feb	EXAM I (IN CLASS)		
2-Mar	Cost of Equity Capital	8	
4-Mar	Cost of Equity Capital	8	
16-Mar	Cost of Debt	9	
18-Mar	Levering and Unlevering	10	
23-Mar	Levering and Unlevering	10	
25-Mar	WACC and Special Issues	11, 12	D & S - Valuation Project: Stages 1+ 2
30-Mar	Market Multiples	13	D - Computing Cost of Capital: P10.7
1-Apr	Market Multiples	14	
6-Apr	Advanced Topic: Insider Trading Regulations	See Canvas	
8-Apr	Catch-Up and Review		
13-Apr	EXAM II (IN CLASS)		
15-Apr	Q & A about Projects		
20-Apr	Student Presentations		D & S - Valuation Project: Stages 1+ 2+ 3
22-Apr	Student Presentations		
27-Apr	Student Presentations		
29-Apr	Project Feedback and Final Words		