

Finance 203
Course Outline and Reading List

PROFESSOR RICHARD KIHLMSTROM

Fall, 2004

• **Readings**

- Brealey and Myers, *Principles of Corporate Finance*, Sixth Edition, McGraw Hill, 2000 (BM) or Ross, Westerfield and Jaffe, *Corporate Finance*, Sixth Edition, McGraw Hill, 2002 (RWJ)
- Higgins, R., *Analysis for Financial Management*, Seventh Edition, McGraw Hill, 2004. (H)
- Bulk Pack, Available from Wharton Duplicating (B)
- Additional readings and notes will be handed out in class. These will be duplicated by the instructor at Wharton duplicating and charged to students enrolled in the class.

• **Grading**

– **Written Case Analyses: (50%)**

- * Students should organize themselves into groups of three or four. **Larger groups are absolutely not permitted.** This should be accomplished by Thursday, Sept. 16. The list of students in each group should be e-mailed to the instructor prior to class on that date or given to the instructor at the beginning of class on that date. Consult with the instructor if you are having a problem joining or forming a group.
- * The written analyses will be done by each group for each of the cases for which a student write-up is required. The written analysis will be **at most five pages** and will, if necessary, be supported by appendices. The analysis will be preceded by a one page executive summary. (The one page summary will not count as one of the five pages of analysis.) **The written analyses will be turned in at the beginning of the class during which the case is to be discussed.** (Make additional copies for your own use during the class discussion.) **Late analyses will not be accepted!**

- There are three starred cases. Each of those will be worth one-quarter of the case grade (meaning 12.5% of the course grade). These case write-ups will each be given a grade between 1 and 10.
- The other six cases for which a write-up is required will, therefore, in total also represent one-quarter of the case grade (meaning 12.5% of the course grade). These cases will each simply be given a grade of check, check-minus or check-plus.

– **Quizzes: (50%)**

- * There will be periodic short (15-20 minute) quizzes. Most of the quizzes will be unannounced.
- * There will be eight to ten quizzes in total.
- * Each quiz will be given a grade between 1 and 10.
- * Quizzes may occur at the beginning or at the end of class. They may cover the case to be discussed that day or cases discussed on previous days. They may also cover the reading material assigned for that day or the preceding days.
- * The first possible quiz will be on Tuesday, September 21. There will be no quiz on Thursday, October 28, the first class after the fall break. There will be no quiz on Tuesday, November 30, the first class after the Thanksgiving break.
- * The bottom two quiz grades will be dropped when the grade is computed.

– **Class Discussion:** This will enter the grade determination only informally. It will be used for the purpose of determining grades only in borderline cases.

– **There will be no exams!**

- **Office:** SH-DH 2255
- **Phone:** 8-4378
- **e-mail:** kihlstro@wharton
- **Office Hours:** Mon and Tues 4:30-5:30 and by appointment
- **Thurs, Sept 9: Course Overview, Review and Introduction**

– **Readings**

- * Benninga and Sarig, Chapters 1 and 2, B

- * BM, Chapters 1-13 or RWJ Chapters 1-12.
- * H, Chapters, 1-4, 7 and 9 (pp. 319-337)

- **Tues, Sept 14 and Thurs, Sept 16: Financial Statements, the Evaluation of Financial Performance and Financial Planning**

Instructor Case Presentation and Class Discussion: Clarkson Lumber (No student write up required)

– Readings

- * Benninga and Sarig, Chapters 1 and 2, B
- * BM, Chapters 27-29 or RWJ Chapters 26 and 27
- * H, Chapters, 1-4, 7 and 9 (pp. 319-337)
- * Note on Bank Loans, B

- **Tues, Sept 21 (First date for a possible quiz) and Thurs, Sept 23: Risk Adjusted Discount Rates**

Instructor Case Presentation and Class Discussion: Comsat (No student write up required)

– Readings

- * “Diversification, The Capital Asset Pricing Model, and the Cost of Equity Capital,” B
- * BM, Chapters 7-9 or RWJ Chapters 8-11
- * H, Chapter 8

- **Tues, Sept 28: Leverage, the Discount Rate and WACC**

– Readings

- * BM, Chapters 17-19 or RWJ Chapters 15-17
- * “Financial Leverage, The Capital Asset Pricing Model, and the Cost of Equity Capital,” B.

- **Thurs, Sept 30: Instructor Case Presentation and Class Discussion: Harris Seafood (No student write up required)**

- **Tues, Oct 5: Class Discussion: All America Pipeline (Student write up required)**

- **Thurs, Oct 7: Capital Structure and Three DCF Approaches: WACC, APV and ROE**

- **Readings**

- * BM, Chapters 17-19 or RWJ Chapters 15-17
- * H, Chapters 5-6
- * Barclay, et.al., “The Determinants of Corporate Leverage and Dividend Policy,” B.
- * Inselbag and Kaufold, “Two DCF Approaches for Valuing Companies Under Alternative Financing Strategies (and How to Choose Between Them),” B

- **Tues, Oct 12: Class Discussion: American Chemical (Student write up required)**

- **Thurs, Oct 14: Instructor Case Presentation and Class Discussion: American Home Products (No student write up required)**

- **Tues, Oct 19 Class Discussion: Case TBA* (Student write up required. Worth 12.5% course grade.)**

- **Thurs, Oct 21: Options and Warrants**

- **Readings on Options and Warrants**

- * BM Chapters 20-22 or RWJ Chapters 22-23
- * Garbade, “Options and Related Securities,” B.
- * Garbade, “Equilibrium Call Option Prices,” B.

- **Thurs, Oct 28: (No quiz on this day) Options, Warrants and Convertibles**

- **Readings on Convertibles**

- * BM Chapters 20-22 or RWJ Chapters 22-24
- * Brennan and Schwartz, “The Case for Convertibles,” B.
- * Jen, et. al., “Some New Evidence on Why Companies Use Convertible Bonds,” B.
- * Ganshaw and Dillon, “Convertible Securities: A Toolbox of Flexible Financial Instruments for Corporate Issuers”
- * Arzac, “PERCS, DECS and Other Mandatory Convertibles,” B.

- **Tues, Nov 2: Class Discussion: Chrysler’s Warrants (Student write up required)**
- **Thurs, Nov 4: Class Discussion: British Petroleum (Student write up required)**
- **Tues, Nov 9: Real Options**
 - **Readings**
 - * BM Chapter 21 or RWJ Chapters 22-24
 - * Dixit and Pindyck, “The Options Approach to Capital Investment,” B
- **Thurs, Nov 11: Class Discussion: MW Petroleum Corporation (Student write up required)**
- **Tues, Nov 16: Takeovers, Mergers and “The Market for Corporate Control”**
 - **Readings**
 - * BM Chapter 33 or RWJ Chapter 30
 - * H, Chapter 9
 - * Jensen, “The Takeover Controversy: Analysis and Evidence,” B.
 - * Jarrell, Brickley and Netter, “The Market for Corporate Control: The Empirical Evidence Since 1980,” B
 - * Dodd, “The Market for Corporate Control: A Review of The Evidence,” B.
 - * Schleifer and Vishny, “The Takeover Wave of the 1980’s” B
 - * “Do Mergers Work?” B
 - * “Why All Takeovers Aren’t Created Equal,” B
 - * Jensen, “Agency Costs of Free Cash Flow, Corporate Finance, and Takeovers,” B
- **Thurs, Nov 18: Class Discussion: Avon (Student write up required)**
- **Tues, Nov 23: Instructor Case Presentation and Class Discussion: Gulf (No student write up required)**
- **Tues, Nov 30: (No quiz on this day) Leverage, LBOs and Financial Distress**

– Readings

- * BM Chapter 34 or RWJ Chapter 30 and 31
 - * Jensen, “Agency Costs of Free Cash Flow, Corporate Finance, and Takeovers,” B
 - * Schleifer and Vishny, “Management Buyouts as a Response to Market Pressure,” B.
 - * Schleifer and Vishny, “Value Maximization Process,” B
 - * “Leveraged Buyouts,” B
 - * Bhide, “Reversing Corporate Diversification,” B.
 - * Kaplan and Stein, “The Evolution of Buyout Pricing and Financial Structure (or, What Went Wrong) in the 1980’s,” B.
 - * Allen, “The Evolution of Financial Structures and Strategies,” B.
 - * “Note on Bankruptcy in the US,” B
-
- **Thurs, Dec 2: Class Discussion: Case TBA* (Student write up required. Worth 12.5% course grade.)**
 - **Tues, Dec 7: (No quiz on this day) Instructor Case Presentation and Class Discussion: Continental Airlines-1992 (No student write up required)**
 - **Thurs, Dec 9: Class Discussion: Case TBA* (Student write up required. Worth 12.5% course grade.)**