

# FINA 7A30, Advanced Corporate Finance

Spring 2016, First Half-Semester, Tue/Thu, 10-11:30am

Prof. Paul Povel

## Syllabus

This is the syllabus for this course. This page can be found through the University of Houston's "BlackBoard Learn" at <http://www.uh.edu/blackboard>. It may be easier to bookmark this page directly. In fact, you should use this web site, only, since I do not plan on using BlackBoard much. A PDF version of this syllabus can be downloaded [here](#).

### Course Overview:

Building on the core finance class (FINA 6A35) and the Valuation course (FINA 7A10), we examine financial decisions that managers face, with an emphasis on how decisions on the financing side of a firm's business can create or destroy value. We will develop the ideas and tools that help you make decisions, and we will apply this knowledge when working on case studies.

The goal of the course is to help you understand optimal capital structure choices for different businesses. We will discuss the advantages and disadvantages of different securities that firms may issue to raise funds, looking at them from the perspectives of both managers and investors. We will discuss how corporate strategy affects a firm's optimal capital structure, and how capital structure affects corporate strategy.

Specific issues covered include:

- The Modigliani-Miller "Irrelevance Results"
- The role of corporate income taxes
- Costs of financial distress, including conflicts between different investor groups
- Effects of financing decisions on managerial incentives
- The cost of issuing different types of securities
- Dividends and share repurchases

Throughout the course, our primary viewpoint is that of a corporate financial manager; however, since corporations get funds from investors, we will often look at issues from an investor's point of view and then examine the implications for managers. Managers who understand the issues will anticipate their investors' reaction and therefore make decisions that maximize value for all investors.

You will notice that valuation is a central theme in this course: In order to make or understand financial decisions, you need to examine what consequences they have and how to compare the alternatives. You need to practice the proper approach to valuation: the expected future cash flows matter! For that reason, the Valuation course is a prerequisite for this course.

You will also be surprised to learn that while we deal with numbers a lot, I will rarely insist that one particular answer or point of view is “correct”, and all others are “wrong”. You will learn to use tools that improve your decisions, but they do not automatically or mechanically produce easy answers. Experience and common sense will remain essential, and these tools will allow you to make better-informed decisions (and to avoid certain types of mistakes).

This course is essential for anyone planning a career in finance, whether at a corporation or a financial institution. It is recommended for all business students, since it gives you a thorough understanding of what determines the cost of capital that you use in NPV calculations.

Note that this will not be an easy course. You should expect to spend time reviewing your notes and working on problems outside of class. The case studies also take time, first to prepare your own answers, second to meet with your team to compare your answers and create a team write-up. Hard work is required, and you will not get a good grade just for showing up.

Want to see [advice from earlier students](#), advice that they left for you after finishing their courses? Click [here!](#)

### **Course Outline**

The course outline is only **tentative**; depending on the progress that we make, it may change.

<u>Week, day</u>	<u>Topics covered and to be prepared</u> (numbers refer to sections in the lecture notes)
Week 1: Tue, Jan 19, 2016	0: Review of valuation techniques (WACC, APV, FCFE)
Week 1: Thu, Jan 21, 2016	1: Capital structure: Introduction
Week 2: Tue, Jan 26, 2016	[Team lists due!] 2: Corporate Income Taxes
Week 2: Thu, Jan 28, 2016	3: Financial distress
Week 3: Tue, Feb 02, 2016	<i>CASE: Mercury Athletic</i> (write-up!)
Week 3: Thu, Feb 04, 2016	3: Financial distress
Week 4: Tue, Feb 09, 2016	4: Issuing securities
Week 4: Thu, Feb 11, 2016	5: Managerial Incentives
Week 5: Tue, Feb 16, 2016	6: Capital structure
Week 5: Thu, Feb 18, 2016	<i>CASE: National Convenience Stores</i> (write-up!)
Week 6: Tue, Feb 23, 2016	<i>CASE: National Convenience Stores</i> (continued)
Week 6: Thu, Feb 25, 2016	7: Payout policy: dividends and stock repurchases
Week 7: Tue, Mar 01, 2016	Practice Problems, Questions
Week 7: Thu, Mar 03, 2016	<i>CASE: FPL</i> (write-up!)
Week 8: Tue, Mar 08, 2016	(no class)
Week 8: Thu, Mar 10, 2016	Final exam (starts at 9:00am!)

## **Prerequisites:**

**Finance:** It is essential that you have taken FINA 7A10 (Intermediate Corporate Finance: Valuation) before taking this course. I will assume that you have a thorough understanding of standard “DCF” valuation techniques (WACC, APV), and that you have practiced using these techniques, both with practice problems and case studies. That includes delevering and relevering returns or betas, and using the CAPM to estimate returns. I will also assume that you know how to calculate present values of future cash flows, including using the annuity and perpetuity formulas, working with terminal values, etc.

**Accounting:** You need some basic knowledge. You should be familiar with the structure of simple financial statements, in particular balance sheets, income statements, and (partly) cash flow statements. You should be able to compute unlevered free cash flows, given such financial statements. If you don’t know what assets, liabilities, EBITDA, EBIT, Net Income, Operating Cash Flow, etc. mean, you definitely need to improve your knowledge. You may want to use the two *Merrill Lynch* brochures on understanding financial statements that I mention (with web-link) on the [“materials” web page](#) (they are well written, and free!).

**Maths:** We will not do anything difficult in this course, but it would be good if you are comfortable dealing with numbers and performing simple calculations. If you are not comfortable working with equations with “x” and “y”, you may be at a disadvantage.

**Computer skills:** This course involves some number-crunching, and spreadsheet software will come in extremely handy. In fact, you will be at a considerable disadvantage when working on the case studies, if you are not familiar with spreadsheet software. Your expertise need not be deep, but you should not be new to using spreadsheets.

**Time and effort:** This course requires significant work outside of class. If you cannot make time available each week for reviewing lecture notes, working on problems and working on cases, you will struggle and get very little out of this course.

## **Equipment:**

You will need a calculator in the exams, and you will sometimes find it useful in class. A basic scientific calculator that does powers is fine. Large-display calculators with parentheses buttons and back buttons are helpful. If you have a financial calculator, you can use it in this class. Two remarks on exams. First, no computers are allowed. Second, you may use a financial calculator, but you must nevertheless convince me that you know what you are doing: just writing down a result or the variables you keyed in is *not* convincing; you should write down *both* the correct formula *and* the correct result. If your answer seems unconvincing, you won’t get full credit, even if the numbers are right.

I assume that you have access to a computer and spreadsheet software. I also assume that you have access to the web, and that you regularly check your email.

## **Readings and other materials**

Required readings consist of the lecture notes and the case studies. The lecture notes are available as PDF files (for free) from this course's “BlackBoard Learn” page (at <http://www.uh.edu/blackboard>).

The lecture notes have gaps where you should add your own comments, answer questions, take down details of calculations, etc. The lecture notes help me structure the course, and they make your life easier because you do not have to write down everything. They will also make it easier for you to compare your notes with other students', or to ask me clarifying questions.

You should bring the current chapters of the lecture notes to every class. **You should print out the pages and use them to take notes with a pen.** Just bringing a notebook to class won't work, unless it is a tablet with a digitizer pen (so you can write onto the screen).

The last two chapters of the lecture notes contain practice problems and answers to practice problems.

The case studies are copyrighted by Harvard Business School. You can go to the HBS website (<http://hbsp.harvard.edu>) and purchase them (after registering). I set up a "coursepack webpage" on the HBS website that may be helpful: <https://cb.hbsp.harvard.edu/cbmp/access/41165091>. The regular price of HBS materials is \$6.95; if you order through the coursepack webpage, it is \$3.95. (I do not receive anything, in case you were wondering.)

The materials you need to purchase are:

- Mercury Athletic: Valuing the Opportunity (HBS Case 4050) [\[webpage\]](#)
- National Convenience Stores, Inc. (HBS Case 294068) [\[webpage\]](#)
- Dividend Policy at FPL Group, Inc. (A) (HBS Case 295059) [\[webpage\]](#)

Additional material will be handed out during the semester. It will also be downloadable from the [Materials page](#).

In the past, students also tried to find information on the web. That tends to be a bad idea. If you are unsure about something, gathering more information is less useful than thinking about what exactly is unclear, and why. Often, you will be able to answer your own question very quickly; if not, you can ask me a very precise question. That's "learning". All the information you need is in the course packet and the class notes. You need to "digest" it, and that requires hard work.

### **Textbooks:**

There is ***NO required textbook*** for this course --- the lecture notes and case studies will keep you more than busy.

In case you want to buy a textbook anyway: There are three standard MBA textbooks on Corporate Finance, that are used in all good MBA programs.

- [Principles of Corporate Finance](#), by Richard A. Brealey, Stewart C. Myers, and Franklin Allen, 11th edition, 2014.
- [Corporate Finance](#), by Jonathan Berk and Peter DeMarzo, 3rd edition, 2013.
- [Corporate Finance](#), by Stephen A. Ross, Randolph W. Westerfield, and Jeffrey F. Jaffe, 10th edition (2013).

If you really want a textbook, I would recommend the Brealey-Myers-Allen textbook or the Berk-DeMarzo textbook (the latter is a little more rigorous in its arguments and logic). The textbooks are

usually sold as a package, with access to websites with practice problems or other things included in the package. (Access to online practice problems may be a good idea, but I won't use that feature in this course.) However, note that we will cover only a few of the chapters of these textbooks.

Judging from past experience, the UH bookstore charges high prices for textbooks. You should be able to get them *much* cheaper online. Note that publishers change ISBN numbers every year, to confuse the second-hand market. So there can be several ISBN numbers for one book, and more for the various packages. Also, international editions of US textbooks can look slightly different (different cover, monochrome print, paperback), but they can be much cheaper. There also exists a loose-leaf version of the book, again, cheaper than the book.

Actually, you may want to look for the second-last editions of the textbooks, which were fine, and those would be much cheaper.

It is a good idea to have a textbook, so you have a second source of information, and, more importantly, so you have additional practice problems (the end-of-chapter problems) to work on and think about. However, I won't insist on you buying a textbook, and I won't assign problems from the textbook.

### **Accessibility Statement:**

The C. T. Bauer College of Business would like to help students who have disabilities achieve their highest potential. To this end, in order to receive academic accommodations, students must register with the Center for Students with Disabilities (CSD) (telephone 713-743-5400), and present approved accommodation documentation to their instructors in a timely manner.

### **Classes**

Class	When	Where
FINA 7A30 Sec 02, Class #24530	Tuesday and Thursday, 10:00AM - 11:30AM	Room: <a href="#">MH 365A</a>

Class participation is mandatory. The course is a mix of lecture/discussion and cases. I expect students to come to class prepared for active participation in both situations.

To make the most efficient use of limited class time, students who miss a class or are late are responsible **themselves** for getting notes, assignments, and announcements from their classmates. Handouts may be obtained from me outside of class, or you can download them from the [Materials page](#).

### **Classroom Etiquette**

Please remember to turn off your cell phones, in particular during exams.

If you bring your notebook or tablet into the classroom, please act in a mature fashion: no emailing, surfing of web pages, etc., i.e., activities that distract you and (much more importantly) other students sitting near you. As I explain below, there is a participation component in the overall course grade --- violating this no-internet rule will *seriously* reduce your participation score.

## **News**

If something should come up (e.g. schedule changes, corrections of materials, announcements, etc.) I will let you know by email, and I will post messages on the [News page](#).

## **Getting in touch with me**

The easiest way will be to use email: [povel@uh.edu](mailto:povel@uh.edu) . My office phone number is (713) 743-4759. My office is Melcher Hall 220C.

Given that you are all busy at different times and many of you have full-time jobs, I won't have scheduled office hours. You can get in touch with me when you have time, by email or in person. In the past, many questions could be answered right after class. But please do not come to my office right before class, when I am busy preparing for class.

It is important that you contact me immediately if you are uncertain or worried about your performance: I may be able to give you feedback on your performance, what you can improve, etc. The sooner problems are identified, the better.

## **Teaching Assistant**

Teaching Assistant: None. I will grade everything myself

## **Cases**

There will be three case studies that require write-ups from your teams. Specific instructions are provided for each case in the lecture notes.

The write-ups must be prepared in groups of 3-4 people. You must give me a list of your group members in the second week of class; groups may not be changed after that.

When working on the cases, you are free to make use of all class materials, but do not use outside sources without my permission, and do not get help from anyone outside your group. I regard use of outside sources or help without my permission as [academic misconduct](#).

The case write-ups (one submission per team, by email) are due before class on the day we will discuss the case. There is no need to print out your write-ups. Instead, please email me your documents (text, spreadsheets, etc.), so I can check how you calculated your numbers.

The [schedule](#) is preliminary and may be changed.

Please set aside enough time to work on cases. The ideal approach is for every team member to prepare a rough sketch of a possible write-up, including in particular spreadsheets; then you can meet, discuss your ideas and put together a team write-up that you will submit. You should resist the temptation to free-ride on your team members' efforts. Working on cases is a learning experience, and that type of learning is crucial in this course.

## **Exams**

There will be one [final exam](#). The final will include topics from the entire course.

The final exam is closed-book / closed notes. However, you are allowed to bring a “cheat-sheet” with notes, written on one side of one sheet (8.5"x11"). I regard these “cheat-sheets” as helpful tools for studying: You should carefully put together material that you feel will help you in the exam; that will help you structure the material, recall essential formulas and procedures, etc. You should start working on your “cheat-sheet” from the first class, and you should plan to re-write it often.

You should bring a calculator. If you decide to use a financial calculator, make sure you know how to operate it; see above, under [Equipment](#).

## **Grading**

Your performance (both individually and within your team) will add up to an overall score, which will then be translated into a course grade. I grade on a curve, so I cannot tell you ex-ante what the cutoffs for an A, an A-, etc. are going to be. On average, a little over half of students received A or A- grades in the past, and a little less than half the students received B+ or lower grades.

Your overall score is computed as follows:

30%	Team work (case studies)
60%	Final exam
10%	Participation

For the "Team work" score, I will incorporate feedback that I will collect from your team mates at the end of the course. I will ask all students for feedback about their team mates' contributions to the team work. There have been problems of free-riding in the past, unfortunately. Such behavior will severely reduce the Team work score. Please make sure everybody contributes at all stages of all case studies (a great opportunity to apply your leadership skills).

For the "participation" score, I will incorporate feedback that I will collect from your fellow students, about who made particularly helpful class contributions. Please take class participation seriously, not only because it affects your grade, but because it helps you learn. The purpose of grading class participation is to encourage you to take active control of your learning: the more involved you get and the better prepared you are, the more you will benefit from this class. (Note, however, that simply taking up "air time" without really making a contribution will not improve your participation score.)

Questions about grading: Requests for a regrade must be made in writing within two weeks of the time the graded work is returned, and must clearly and specifically explain where and why you think you were graded incorrectly.

## **Academic Misconduct**

Academic Honesty: The University of Houston's Academic Honesty Policy is strictly enforced by the Bauer College and by this professor. A discussion of the policy is included in the UH Student Handbook, <http://www.uh.edu/dos/studenthandbook/>. It is your responsibility to fully understand and

comply with all principles contained within this Handbook. Please make sure you understand this policy and in particular, you understand the meaning of plagiarism.

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