

FINA 7A10

Intermediate Corporate Finance: Valuation

Spring 2016, First Half-Semester, Thu, 6-9pm

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), we develop and use standard valuation tools based on "discounted cash flow" techniques: valuation using the WACC (weighted average cost of capital), valuation using the APV (adjusted present value), and (to a lesser extent) valuation using the cash-flow-to-equity approach. We will develop the ideas and tools, and we will apply this knowledge when working on in-class problems, individual and team assignments, and case studies. You learnt about some of this material in FINA 6A35. This course will go into much more depth.

Valuation is the central theme in this course: In order to make or understand financial decisions, you need to examine what consequences they have (we will focus on risky future cash flows) and how to compare the alternatives. You need to practice the proper approach to valuation: forecast expected future cash flows, and estimate the appropriate discount rate for that cash flow stream. The "value" of an asset is then estimated as the present value of the cash flows it generates, discounted using the appropriate discount rate. The valuation techniques we will use go beyond that, by building in the effects of tax shields and other "side effects" of financing decisions.

A lot of this work is technical (requiring calculations, usually with spreadsheet software), but a lot of it requires that you apply experience and common sense. So "valuation" often seems more like an art than a science. Therefore, I will not insist that "my" answers are the correct ones. However, I will require that (1) you use the techniques correctly, and that (2) you explain and justify assumptions and non-obvious decisions in your work.

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 any decision made in corporations may

add or destroy value, and this course will improve your ability to judge whether value is being added or destroyed. The techniques developed here will be the foundation for the advanced corporate finance courses, including FINA 7A30 (Advanced Corporate Finance) and FINA 7A33 (Mergers and Acquisitions).

Note that this will not be an easy course. You may initially find it hard to become familiar with the concepts, so 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)	<u>Assignments</u>
Week 1: Thu, Jan 21, 2016	1: Overview; review of time value of money calculations, the CAPM, and capital budgeting. 2: Using information from financial statements.	Work through Section 0 of the Lecture Notes, in particular the problems. Review basics of accounting.
Week 2: Thu, Jan 28, 2016	3: DCF techniques I: The WACC (Weighted Average Cost of Capital). Delevering and unlevering betas or returns.	Homework Assignment 1 Team lists
Week 3: Thu, Feb 04, 2016	Discuss the first part of the Marriott Cost of Capital case (no write-up due). Examples: WACC valuation.	Read the <i>Marriott</i> case (no write-up due, yet → next week!)
Week 4: Thu, Feb 11, 2016	<i>CASE: Marriott Cost of Capital</i> 4: DCF techniques II: The APV (Adjusted Present Value).	<i>Marriott</i> case write-up
Week 5: Thu, Feb 18, 2016	4: DCF techniques II: The APV (Adjusted Present Value). <i>CASE: Ocean Carriers</i>	<i>Ocean Carriers</i> case write-up Homework Assignment 2
Week 6: Thu, Feb 25, 2016	<i>CASE: Joyce's Juice</i> . Examples: APV valuation.	<i>Joyce's Juice</i> case write-up
Week 7: Thu, Mar 03, 2016	<i>CASE: Valuation of AirThread Connections</i> Practice problems, questions, etc.	<i>AirThread</i> case write-up due! Homework Assignment 3
Week 8: Thu, Mar 10, 2016	Final exam	

Prerequisites:

Finance: You should have taken FINA 6A35 (Managerial Finance). You need to have practiced "time value of money" calculations: discounting of future cash flows, given a rate of return; and calculating the present value of annuities and perpetuities. You need to have some familiarity with the CAPM (working with betas). Some of you have a Finance background. If you don't, no worries, you're here to learn how these techniques work. The important thing is not to let those with pre-existing knowledge do your work for you. In order to learn the material, you must actively engage with it.

Accounting: You need some basic knowledge. 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.

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. If you do not regularly use spreadsheet software, this is the ideal time to learn how to use it.

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.

Three case studies are copyrighted by Harvard Business School. (The *Joyce's Juice* case study is not copyrighted, so it will be part of the downloadable lecture notes.) 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/42645450>. 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:

- Marriott Corp.: The Cost of Capital (Abridged) (HBS Case 289047) [\[webpage\]](#)
- Ocean Carriers: (HBS Case 202027) [\[webpage\]](#)
- Valuation of AirThread Connections (HBS Case 4263) [\[webpage\]](#)

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 will keep you more than busy. Another reason is that the standard corporate finance textbooks do not cover this material in sufficient depth.

If you are interested in a book that covers the material **in great depth**, I recommend this book:

- *Valuation: Measuring and Managing the Value of Companies*
by McKinsey & Company Inc.; authors: Tim Koller, Marc Goedhart and David Wessels
Wiley Finance, 6th Edition, 2015, ISBN 9781118873700
<http://www.wiley.com/WileyCDA/WileyTitle/productCd-111887370X.html>
[\(Click here to check out prices\)](#)

Unlike the standard textbooks, this book is affordable (shop around a little). It goes into great depth, so it will be a valuable on-the-job resource.

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 7A10 Sec 01, Class #20860	Thursday, 6-9pm	Room: UCBB 108 MH 118

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 . 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: T.B.A.

Cases

There will be four 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.

Homework Assignments

There will be three homework assignments, to be completed independently from other students. The second and third assignments will be graded. We will discuss the answers in class.

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)
40%	Final exam
20%	Homework assignments
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.
