

Finance 321

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Required Text: *Corporate Finance*, by Ross, Westerfield and Jaffe, McGraw Hill, Sixth Edition.

Course Objectives: The purpose of this course is to give the students an advanced and hands-on exposure to key issues in corporate finance that are either not covered or only briefly touched upon in Finance 111. Topics that are emphasized are: capital budgeting decisions, finding the cost of capital, how capital structure decisions affect firm value, valuation of companies using DCF and other techniques, and M&A (merger and acquisition) decisions. Students taking this course should be well prepared to pursue careers in investment banking, financial analysis, and consulting.

Pre-requisites: Finance 111, Finance 221.

Course Web Site: A course web site under webCT has been set up. Please check the web site regularly for course materials and announcements. Please post discussion questions on webCT. I will answer questions posted on webCT every Monday, Wednesday, and Saturday.

Also, please make a note of the office hours. You should make it a point to see me at least once during the term. Asking questions face-to-face is much more effective than posting questions on the website.

Sources of Material: There are three sources of material for the topics covered in this course. The lectures will be organized around a set of PowerPoint presentations that will be available at the course website. These should be supplemented by more detailed notes on each chapter, available in the document "CFnotes.pdf" posted in the website. The order in which the material is presented in this document is very similar to that in the textbook, and the chapter references correspond to those in the text book as well. Finally, the textbook constitutes a third source of material.

Ideally, for each topic, you should first go through the PowerPoint presentations, then read the material in my lecture notes (CFnotes.pdf), and then read the text book. There are useful problems at the back of the chapters in the text that can give you additional practice. We will post a list of practice problems and solutions on the web site.

For several topics, we will illustrate concepts using some selected cases from the Harvard case book, *Case Problems in Finance*, 11th Edition and *Case Studies in Finance*:

Managing for Corporate Value Creation by Robert F. Bruner. Copies of the cases to be discussed will be held in reserve in the library, and it is not necessary for you to buy these books.

Course Structure and Pedagogy

Groups:

You are required to form groups in the first week of class. Each group will consist of 6 members. The names of group members must be handed in by February 10.

There will be FIVE in-class exercises that will be graded. Your group will be asked to solve these exercises in class, and for each group exercise, I will randomly pick a group to present its solution before the class. Sometimes, more than one group may be called for a particular exercise. Besides, there will be ONE group project based on some of the cases. You will have to submit a case report for this project at the end of the term.

Group members will be required to sit together at all times and work together on in-class group exercises. They will also work together on the group project.

The course outline and timetable (see below) indicates the date/dates a particular case will be discussed and the in-class group exercises will be held.

Be sure that on each such date, at least one member of your group is able to bring a laptop computer to the class. This will be very helpful in working out the cases, as well as the in-class exercises.

Students who are not a part of a group of size 6 on February 10 will be combined in an arbitrary manner into groups. If the number of students enrolled in your section is not divisible by 6, one group of size smaller than 6 will be necessary.

Seating Plan: There will be a seating plan for the course. Each group must seat in one row, and every member of the group will have a designated seat. This is important because otherwise, we cannot keep track of your class performance.

To make sure that we can match names to faces (especially in the early part of the course), you need to give us a small photograph of yourself by February 10, with your name and student I.D. number written at the back.

Class Participation: Class participation will be evaluated and will play an important role in the determination of the final grade. Class participation includes asking questions during regular lecture and answering questions addressed to the class, as well as your input when cases are worked out in class, and when the group exercises are being discussed in class. Be forthcoming and speak up! In the past, class participation has had significant impact on the final grades in this course.

Points to remember about the Case Report due at the end of the term:

1. Please note that *you need to turn in a hard copy of the report*. Soft copies of reports (disks or e-mail attachments) cannot be graded.
2. For each question, there must be a section called “Key Assumptions” where you need to indicate the list of important assumptions you have made to answer the questions.
3. You must have a detailed written answer to each question. Charts or tables cannot constitute an answer – they are considered as supporting material for your answers.
4. All tables and charts should appear at the end. The discussion in the report should make very clear references to the charts and tables.
5. There must be a section called “Explanatory Notes to Tables and Charts” where the calculations in the tables are explained in complete detail.
6. Excluding the Tables and Explanatory Notes, the Case Report should not exceed 10 pages.

Grading: The course grade will be determined on the basis of

	Weight
(i) a mid-term examination	20%
(ii) a final examination	30%
(iii) five in-class group exercises	20%
(iv) an end-of-term case report	20%
(v) class participation.	10%

For the in-class group exercises and the end-of-term case report, all group members will receive the same Basic Grade to begin with. The Basic Grade will then be adjusted according to a peer evaluation scheme.

Each member of your group will be asked to rank every other member on a scale of 1 to 5, indicating their evaluation of each member’s relative contribution to the group’s efforts (excluding himself/herself). A rank of 5 is the best possible, and 1 is the lowest possible. The average rank of each group member will then be computed. Suppose this average rank for an individual is x (a number between 1 and 5). Then the eventual Group Project Grade for that individual will be determined by the following formula:

$$\text{Group Project Grade} = (\text{Basic Grade}) + (0.15) (\text{Basic Grade}) * (x - 3) / 2$$

Thus, if your average rank is 5 and the Basic Grade is 130 for your group, your Group Project Grade is $(130) + (0.15)(130)(2/2) = 149.5$

The peer evaluation will be confidential, and will be done at the time of the final examination. Note that you will **not** be allowed to give the same rank to any two people in your group. If you do, or if you do not rank someone in your group, those individuals will be assigned a rank of 2.5 from you. Also, as a penalty to you, your average rank will be lowered by 1.

If the number of group members is less than six, then the formula will be adjusted accordingly. Thus, if the number of group members is 5, the best possible rank is 4. In this case, the formula will be

$$\text{Group Project Grade} = (\text{Basic Grade}) + (0.15) (\text{Basic Grade}) * (x - 2.5) / 1.5$$

(the number subtracted is the mid point of the highest possible and lowest possible ranks).

Here is an example of how the score for the entire course will be computed. Suppose your group gets the following points on the case reports:

Class Exercise 1:	15/20
Class Exercise 2:	11/20
Class Exercise 3:	10/20
Class Exercise 4:	13/20
Class exercise 5:	17/20
Total (Class Exercise)	66/100
Case Report	70/100
Total from Group Projects	136/200

Your peer evaluation score: 3.5

$$\text{Group Project Grade: } 136 + (0.15)(0.5/2)(136) = 141.1$$

Midterm: 75/100

Final Exam: 110/150

Class participation: 30/50

$$\text{TOTAL (out of 500): } 141.1 + 75 + 110 + 30 = 356.1$$

Course Outline and Time Table:

<u>Week of</u>	<u>Topic</u>	<u>Reference</u>	<u>Comments</u>
Feb 3	Introduction; NPV, IRR and Alternative Investment Rules	Chapters 6	Read Lockheed Case
Feb 10	Lockheed Tri Star Case		
	Project Cash Flows	Chapter 7,8.	Read Super Project Case
Feb 17	Group Class Exercise 1 on February 17. Super Project Case.		
February 24	Review of Risk and Return CAPM and SML	Chapters 9,10	Read Beta Management Case
March 2	Discount Rates	Chapter 12	
March 9	Group Class Exercises 2 on March 9. M&M Theorem and Capital Structure	Chapter 15	
March 16	M&M Theorem and Capital Structure Group Class Exercise 3 on March 18.	Chapter 15	
March 23	Midterm Examination Taxes, WACC and Firm Value	Chapter 15	Read Marriott Case
March 30	Taxes, WACC and Firm Value Marriott Case		
April 13	APV method	Chapter 17	Read Appendix 17A Read Brown-Forman case
April 20	M&A Valuation Group Class Exercise 4 on April 22.	Chapter 30	
April 27	APV; NPV again Bankruptcy and Limits on Debt	Chapter 17	
May 4	Bankruptcy and Limits on Debt. Adverse Selection and Equity Issuance	Chapter 16.	
May 11	Adverse Selection and Equity Issuance Group Class Exercise 5 on May 13.	Notes	

Case Report Due: May 19.

Final Examination May 20-31