

UNIVERSITY OF PENNSYLVANIA
The Wharton School

Corporate Valuation
FNCE207 & FNCE728

Professor Vincent Glode
Spring, 2012

DETAILED COURSE OUTLINE

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I will also answer emails that can be answered with a simple reply (for example, "yes" or "no" or a few sentences). I will not answer emails that require long explanations. In those cases, I will ask you to attend office hours or ask me in class.

Office Hours: See course website for details about office hours and TAs.

Class Times: Section 001: Monday/Wednesday, 12:00 --- 1:20 PM in SHDH 211
Section 002: Monday/Wednesday, 1:30 --- 2:50 PM in SHDH 211
Section 003: Monday/Wednesday, 3:30 --- 4:20 PM in SHDH 211

1. Course Objectives.

The objective of this course is to learn firm, debt and equity valuation methods from both a conceptual and practical framework. The approach combines both accounting and finance into a practical framework for valuing firms, debt and equity. While there is some new finance theory introduced in this course, the emphasis is on the practical application and integration of finance and accounting concepts to valuing companies.

Students with weak accounting and finance backgrounds will be at a disadvantage in this course. Working knowledge of EXCEL is also important. *Students who hope to never see a financial statement again should not take this course.*

The course utilizes extensive and detailed readings, chapter exercises, valuation projects, and two exams. Students should expect the workload for this course to be demanding, as such, it is only recommended for those students who are interested in learning valuation techniques in depth. Students interested in broader topical coverage and a less detailed examination of valuation techniques should consider the Advanced Corporate Finance course.

This course is designed for students with little or no practical work experience in valuing companies. I do not believe that the "value added" from this course for students who have previous job related valuation experience is as high as for those with no relevant prior experience, but several former students with prior work experience disagree with me on this issue. We do explore current practices in the lectures and I will be critical of some of them when appropriate.

2. Minimal Prerequisites.

- A. Introductory Financial Accounting
- B. Introductory Corporate Finance.
- C. Introductory Statistics or Econometrics.
- D. Basic knowledge of EXCEL or some other spreadsheet package.

Note that knowledge of intermediate accounting (ACCTG 201 and/or ACCTG 202 OR ACCTG 742) might be 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 Texts.

A. Course Textbook

The textbook contains most of the readings for the class and is currently available from Wharton Reprographics. **Students should read the relevant material before class.** Unless otherwise specified, students will be held responsible for all material in the textbook, whether covered in class or not. NOTE: The textbook is still a work in progress as Robert Holthausen from the accounting department at Wharton and Mark Zmijewski from the University of Chicago are in the process of publishing the textbook (the book is under contract and that is why this cannot be released through Study.Net). The textbook is updated constantly; hence students should not use textbooks/bulkpacks from earlier semesters.

B. Required References.

Principles of Corporate Finance by Brealey, Myers, and Allen, Ninth Edition, McGraw Hill. This is a text virtually all of you should own having taken Corporate Finance. If you own another edition of that book or any other corporate finance textbook (such as Corporate Finance by Ross, Westerfield and Jaffe), that will suffice as well, though you will have to figure out the relevant chapters for reading. *This text is just background reading for concepts you should already know.*

Financial Accounting by Libby, Libby, and Short, Sixth Edition, McGraw Hill. This is a text virtually all of you should own having taken Introduction to Financial Accounting. If you own another edition of that book or any other financial accounting textbook (such as Intermediate Accounting by Kieso, Weygandt, and Warfield), that will suffice as well. *This text is just background reading for concepts you should already know.*

C. Course website

Material for the projects and additional readings will be posted for student access via Canvas. There will be copies of the PowerPoint slides I will use during lectures available on the website as well. These will not be distributed in hard copy as they generally follow the notes in the textbook, but students wishing to have them prior to class, can print them out. The final version of these will be available by at least 8:00AM on the day of class. If you are registered for the class, you can gain access to the Canvas room at <https://wharton.instructure.com/>.

Mark Zmijewski and Robert Holthausen would also appreciate if you would report typos, errors and comments. Thus, there will be a place on the course website where you can report typos, errors and passages that confused you. Your feedback will help the authors rewrite their new material as it gets closer to publication.

D. Other Interesting but not Required Material.

Damodaran on Valuation, by Damodaran, Second Edition, John Wiley & Sons. This valuation textbook is quite popular and covers most of the concepts covered in this class, but with less depth than our textbook.

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

Valuation: Measuring and Managing the Value of Companies, McKinsey & Co., Koller, Goedhart and Wessels, Fourth Edition, John Wiley & Sons. This valuation book is written from a practitioner's perspective.

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. Current financial news should be helpful for valuing your company.

For those who would like to learn useful Excel shortcuts and how to build standard investment banking models, you might want to purchase Knowledge Base Level I or Knowledge Base Level II from DealMaven, Inc. (which is now owned by FactSet). Knowledge Base Level I teaches Excel shortcuts and how to build a standard IBANK model. Knowledge Base Level II discusses LBO and M&A transactions and how to build an LBO model and an accretion/dilution analysis for an M&A deal. To purchase or learn more about either of these products, go to:

<http://store02.prostores.com/servlet/factsetdealmavenorders/StoreFront>

There is student pricing available, but it is not cheap.

4. Grading.

Grading in the course will be based on the following criteria:

Valuation of a Company (divided in 3 stages)	30%
Exam I	30%
Exam II	30%
Class Participation (e.g., in-class exercises)	10%
Total	100%

UNDERGRADUATES PLEASE NOTE: If an undergraduate student wants to drop the course after the deadline for dropping from finance courses (January 25th) AND I allow it (which is unlikely as it risks putting other team members in academic trouble), a "W" will appear on his or her transcript.

A. Class and Participation and Attendance

Class participation counts 10 percent of your total grade. Some classes require you to be prepared for class discussion, while other classes will strictly follow a lecture format. During lectures, I encourage you to ask questions. Voluntary class participation is expected, however, I will also cold call on individuals in class from time to time. The education experience for everyone suffers if participation or attendance for the class becomes a problem.

B. Seating

I will bring a class roster with photos for every class. But in order for me to get to know your names, I would like students to sit in the same part of the classroom every week.

C. Examinations

The first examination will be administered **in class** on **February 22nd**. The exam covers Chapters 1-10. The final examination will be administered **during the final exam period (exact day/time TBA)**. The final exam is cumulative and covers all material mentioned in the course. These exams will be "open book" as you may bring your textbook, your class notes, and a calculator. No other material is allowed. **The best way to prepare for these exams is by going through examples from the lecture notes and the textbook after each lecture and by working through past exams.**

Please note the scheduling of the two exams. You are responsible for ensuring that you are available and on campus to take both exams. I will not FAX exams to remote locations. I will not permit anyone to take the exams at another time unless you are gravely ill, face a significant emergency or have an exam conflict. If your travel plans conflict with the date of an exam, you should change your travel plans now, or drop the course. You must ensure that you are available for both examinations. Please advise potential employers that you cannot schedule interviews that conflict with your exam schedule.

D. Projects and In-Class Exercises

Students will have to hand in reports for the three stages of the valuation project during the semester. Late submission will incur a penalty of 10% per day, counting the day of the class itself. Students must turn in these projects before noon. **Students who rely on team members to do all their valuation projects will fail to learn the material necessary to pass the exams.**

Note that the in-class exercises to prepare and project submission deadlines are marked on the outline as either D, D & S or S. If marked D, it means you must be prepared to discuss the exercise, which I will post on the course website, though it will not be submitted. If marked D & S, you must be prepared to discuss the assignment or project and you must submit it at the beginning of the class. If marked with just an S, you will just be submitting part of your valuation project in class, but it will not be discussed in class.

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 submitted work is considered a violation of the codes of academic honesty. Moreover, it is likely your exam performance will suffer as these assignments and projects are intended to help you prepare for exams.

You may work individually or in teams of up to **four individuals** on the valuation project. If you work as a team, all members of the team will receive the same grade on submitted work. No team can have more than four members (more on teams later).

The first page of a submitted assignment should indicate the name of the valued company, the names of the individuals participating in the grade and the section in which each student is registered.

As part of the course requirements, you will pick a company of your own choosing and value it. There will be a separate write-up of the valuation project available in a few weeks. In the interim, you should consider possible companies you want to value. There are several criteria that you should keep in mind in choosing a company to value:

1. This has to be a company that you and your teammates have not done any valuation work on in a prior course or in a job or internship or in any other capacity. In other words, you may not value a company where

some of the valuation work has already been completed by you or any of your teammates.

2. The company you pick should be publicly traded in the U.S. and there should be at least three years of historical data available for this company. **Check this before submitting company names.**

3. I advise you to pick a company that is in a single line of business as valuing diversified companies like General Electric is challenging from just publicly available data.

4. There should be at least three U.S. publicly traded competitors in the same business with at least three years of historical data. It is best if these are “pure-plays” (e.g. only in the business of the firm being valued). **Check this before submitting company names.**

5. You do not have to pick a purely domestic company, but valuing companies that are truly multinational in nature is also potentially challenging from just publicly available data.

6. On one hand, you should pick a company where you believe you have some ability to create reasonable forecasts. In other words, picking a technology company where the technology is unproven and the demand for the technology is highly uncertain is going to create special challenges in forecasting. On the other hand, you should value a **company that interests you and will keep you motivated for the whole semester (even if that means picking a company that is more challenging to value).**

You and your team should begin to think about what company you want to value. Additional information about this project will be available in a few weeks. It would be wise, however, to target a few companies and select your team members as soon as possible. **Team composition and the names of companies you would like to value are due on January 25th, which is also the official drop deadline for finance courses.**

5. Attendance and Class Etiquette

Students should attend the section of the class for which they are registered. Students are expected to attend class throughout the semester. In the case of a **rare conflict**, students can attend another of my sections. I teach the same class at 12:00, 1:30, and 3:00 PM the same room on Mondays and Wednesdays. You should notify me by 9:00 AM by email if you are planning to attend a different section and you should come up to me prior to the start of the class you will attend.

Students are expected to arrive on time for class. Once in class, students should remain until the class is completed. Arrivals and departures during class time interfere with the educational process and are not fair to the other students or myself. If you choose to schedule an interview on-campus during class, do not come to class for part of the period, come to another section and notify me in advance.

6. Workload

The subject matter of this course is quite 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 the technical nature of this course, the course does not appeal to all students. I believe in communicating the complexity of the issues one faces in valuation. I will rarely gloss over something even if it is difficult.

7. Relation to Corporate Finance Case Course

This course concentrates on valuation issues only and looks at them in detail. The Advanced Corporate Finance course generally examines a variety of issues such as working capital management, optimal capital

structure, dividend signaling, capital budgeting and valuation. Thus, while the advanced corporate finance course deals with valuation issues, it does not look at them in as much detail. However, the course has a much broader topical coverage.

8. Academic Integrity

Students are expected to follow the rules of academic honesty in this class. This means that examinations are to be the work of the individual student using only the material permitted during the examination. Regarding submitted assignments and projects, the work should be the work of *only the team members* reported on the front of the document. Students should not in any way rely on the work of prior students or current students that are not members of 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 or valuation model, the use of a forecasting or valuation model not created exclusively by the student team for this course is a violation of the codes of academic integrity. In other words, **for all submitted assignments, you must start with an Excel spreadsheet which is at most populated with some raw data.** Moreover, as indicated previously, the company you value 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.

Please note that if you violate this policy, failing the class will constitute the minimum penalty, regardless of the degree of your violation.

9. Teams

Assignments and valuation projects can be worked on individually or in teams of up to four students. Teams of five or more are not allowed (no exceptions). MBAs and undergraduates may not be on a same team but teams can include students from different sections. I encourage you to work in teams to maximize the learning experience. **I will not become involved in any group problems.** In choosing teammates, consider the skills your team needs to possess: accounting, finance and excel modeling expertise. Also make sure that your teammates' expectations for their performance in this course are consistent with yours.

The composition of your team needs to be decided by the time you submit the names of the potential companies you would like to value.

10. Lunches

In an effort to get to know more of you personally, I am happy to take as few as three students and as many as six students to lunch at a nearby restaurant. Because I teach on Mondays and Wednesdays and have other lunchtime commitments on Tuesday and Friday, I am generally available for lunch only on Thursdays at noon. There will be a sign-up function for lunches on the course website with the Thursday dates when I am available during the semester. If a group of you cannot meet for lunch on Thursday at noon and wish to arrange an alternative, please email me and we will see if we can schedule an alternative time.

COURSE CALENDAR**SPRING 2012**

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

Date	Topic	H & Z Chapter	Assignment (D=Discussion & S=Submission)
11-Jan	Introduction to Course and Valuation	1	
18-Jan	Creating Economic Value	2	
23-Jan	Measuring Value & Analyzing Financial Statements	3, 4	
25-Jan	Free Cash Flow Basics and the SCF	5	S - Names of 3 Companies to Value (coincides with drop deadline for finance courses)
30-Jan	Creating a Financial Model	6	D - Changes in Financial Ratios
1-Feb	Creating a Financial Model	6	D - Free Cash Flow Computation
6-Feb	Forecasting and Free Cash Flow Measurement Issues	7	
8-Feb	The APV and WACC DCF Valuation Methods	8, 8.A	D - Tax Shield Computation
13-Feb	Excess Earnings Valuation Models	10	D - APV Computation
15-Feb	Measuring Continuing Value	9	D & S - Valuation Project: Stage 1
20-Feb	Catch-Up (and Review if Time Permits)		
22-Feb	MIDTERM EXAM (IN CLASS)		
27-Feb	Cost of Equity Capital	11	
29-Feb	Cost of Equity Capital	12	
5-Mar	NO CLASS - Spring Break		
7-Mar	NO CLASS - Spring Break		
12-Mar	Cost of Debt	13	
14-Mar	Levering and Unlevering	14	
19-Mar	Levering and Unlevering	14	D & S - Valuation Project: Stages 1+ 2
21-Mar	WACC and Special Issues	15	D - Cost of Capital Computation
26-Mar	Market Multiples	16	
28-Mar	Market Multiples	17	
2-Apr	Advanced Topic: LBOs	18	
4-Apr	Advanced Topic: Financial Institutions	TBA	
9-Apr	Advanced Topic: Insider Trading	TBA	
11-Apr	Student Presentations		D & S - Valuation Project: Stages 1+ 2+ 3
16-Apr	Student Presentations		
18-Apr	Student Presentations		
23-Apr	Catch-Up (and Review if Time Permits)		
TBA	FINAL EXAM (DURING FINAL EXAM PERIOD)		