

FNCE 207 & 728: CORPORATE VALUATION

Professor Vincent Glode, CFA
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Wharton School
University of Pennsylvania

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I will only answer emails containing simple questions about administrative issues. I will not answer emails that require long explanations about course content. In those cases, I ask you to attend office hours, ask me in class, or schedule an appointment.

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

Class Times: Section 207-001: Monday/Wednesday, 12:00 --- 1:20 PM in SHDH 1206
Section 207-002: Monday/Wednesday, 1:30 --- 2:50 PM in SHDH 1206
Section 728-001: Monday/Wednesday, 3:00 --- 4:20 PM in SHDH 1206

1. Course Objectives.

The objective of this course is to learn firm, debt, and equity valuation methods from a conceptual and practical framework. 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 is as high for students who have previous job-related valuation experience or those who went through the CFA program as it is for those with no relevant prior experience. Several former students with prior work experience, however, found this course extremely valuable.

My goal in this course is to give you a thorough grounding in the theory and practice of valuation. From time-to-time I will discuss common errors that practitioners make and I will discuss some issues that practitioners often ignore. My view is that you need to fully understand the meaning and the consequences of any shortcut you might take when valuing a company. In some cases, those shortcuts are justified because they will have little to no impact on the valuation and more complex methods would not be worth the time required. In other cases, taking those shortcuts will lead to serious errors. I will discuss areas where there is uncertainty about how best to perform certain tasks. In these situations, I will indicate what is typically done or what is typically ignored and discuss relevant research in the area, so you at least have an appreciation of the issue and the alternative views on the matter.

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 is preferable for this course, although it is not required. Stronger accounting skills will, of course, make some of the material easier to understand.

2. Course Texts.

A. Course Textbook

The required text is *Corporate Valuation: Theory, Evidence and Practice* by Robert Holthausen and Mark Zmijewski, published by Cambridge Business Publishers. The book is a substantially revised version of the softbound pre-publication versions used in prior years, hence students should not use those older versions. The book is available through the bookstore or at this link:

<https://store.collegiatelearning.com/product/corporate-valuation-1st-ed/>

Note that if you decide to order it through Amazon, make sure you get the hard copy version with the 2014 copyright date – Amazon is carrying some incorrect versions of the book (there should be a picture of a skyscraper on the front cover) and Amazon is pricier than the link provided above.

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 Introductory 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. *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 Introductory 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 on Canvas. There will be copies of the PowerPoint slides I use in my lectures 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 in the morning of each lecture. You can gain access to the Canvas room at:

<https://wharton.instructure.com/>

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 many 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.

3. 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., attendance, in-class exercises)	10%
Total	100%

PLEASE NOTE: The Finance Waitlist for undergraduate students will be open from January 10th through January 22nd, 2014 at 5:00 PM. **The Finance Department's Drop Deadline is Friday, January 24th, 2014 and is different than the University's deadline.** Should you decide to drop a Finance course, you must do so through Penn In Touch prior to the Finance Department's drop deadline. **If you drop a Finance course that is full after the department deadline you will receive a "W" on your transcript.**

A. Class and Participation and Attendance

Class participation counts for 10% of your grade. Some classes require you to be prepared for 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 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. Exams

The first exam will be administered **in class** on **February 26** and covers Chapters 1-7. The final exam will be administered **during the final exam period (exact day/time TBD later)**. The final exam is cumulative and covers all material mentioned in the course. **The best way to prepare for these exams is by going through examples from the lecture notes and exercises at the end of each chapter in the textbook after each lecture and 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, or face a significant emergency (which needs to be documented). **If your travel plans or interview plans conflict with the course, you should change your plans now, or drop the course.**

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 the 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 before class. If marked with just an S, you will just be submitting the assignment before 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, 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).

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” (i.e., 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 a little bit 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 29, which is right after 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 one 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 9AM 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, instead 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, that 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* listed 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 your 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 between 3 and 6 students to lunch at a nearby restaurant most weeks. 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. 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 2014**

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

Date	Topic	H & Z Chapter	Assignment (D=Discussion & S=Submission)
15-Jan	Introduction to Course and Valuation	1	
22-Jan	Creating Economic Value	2	
27-Jan	Measuring Economic Value	2	
29-Jan	Computing Free Cash Flows	3	S - Names of 3 Companies to Value
3-Feb	Creating a Financial Model	4	D - Interpreting Financial Ratios: P2.1, P2.3
5-Feb	Creating a Financial Model	4	D - Computing Free Cash Flows: P3.1
10-Feb	Various Forecasting and Measurement Issues		
12-Feb	DCF Valuation Methods	5	D - Computing Interest Tax Shields: P3.9
17-Feb	Excess Earnings Valuation	7	
19-Feb	Measuring Continuing Value	6	D & S - Valuation Project: Stage 1
24-Feb	Catch-Up and Review		D - Using DCF Method: P5.6
26-Feb	MIDTERM EXAM (IN CLASS)		
3-Mar	Cost of Equity Capital	8	
5-Mar	Cost of Equity Capital	8	
10-Mar	NO CLASS - Spring Break		
12-Mar	NO CLASS - Spring Break		
17-Mar	Cost of Debt	9	
19-Mar	Levering and Unlevering	10	
24-Mar	Levering and Unlevering	10	
26-Mar	WACC and Special Issues	11, 12	D & S - Valuation Project: Stages 1+ 2
31-Mar	Market Multiples	13	D - Computing Cost of Capital: P10.8
2-Apr	Market Multiples	14	
7-Apr	Advanced Topic: LBOs	15	
9-Apr	Advanced Topic: Financial Institutions	See Canvas	
14-Apr	Advanced Topic: Insider Trading	See Canvas	
16-Apr	Q&A on Valuation Project and Presentations		
21-Apr	Student Presentations		D & S - Valuation Project: Stages 1+ 2+ 3
23-Apr	Student Presentations		
28-Apr	Student Presentations		
30-Apr	Catch-Up and Review		
	FINAL EXAM (DURING FINAL EXAM PERIOD)		