

The Wharton School – University of Pennsylvania
FNCE 707
Valuation

Spring 2022
Preliminary Course Syllabus

(Please note that this syllabus is subject to change over the duration of the course; however, the general structure and content of the course will remain the same.)

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Teaching Assistants

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Classroom tbd

FNCE 207 – M/W at 3:30 p.m. – 5:00 p.m.

Course Description

Key benefits:

After taking this course, participants will have a deep understanding not only of ‘what’ steps to follow in assessing the value of a company, but also ‘why’ those are the steps to follow. Our focus will be on developing discounted cash flow (DCF) models and estimating the appropriate discount rate to obtain the present value of the expected future free cash flows. We will emphasize the importance of the process employed to perform the valuation. Specifically, participants will know how to (1) perform historical analysis to identify a company’s potential for value creation, (2) produce a forecast of the expected future cash flows to be discounted, (3) incorporate the continuing value of the firm, and (4) estimate the appropriate discount rate for calculating present value. In addition, by understanding the conceptual basis for these elements, participants will be prepared to explain and persuade others why their valuation is reasonable and how it can be used in decision-making.

Course Overview

In this course, we will cover three general “themes”: (1) Why is value, and thus also valuation, so important and relevant in the world of business, (2) How to perform a high quality and robust valuation, and (3) How to explain the valuation to ensure it is actually used in decision-making. This third point is highly challenged by a widespread practice of using “pricing” rather than “valuation” to support and drive decision making. We will contrast “pricing” with “valuing” a business. In many situations which claim to use value and valuation for decision-making, it has been noted that many very often factors other than value-impact are incorporated into the decision

process, either deliberately or inadvertently. In many cases, this is due to a lack of full understanding of why the valuation is being performed and the critical importance of value creation as the over-riding objective in the “modern” world.

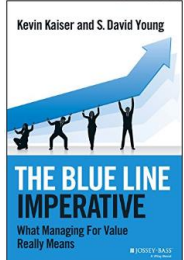
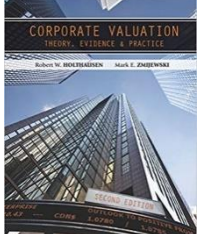
Throughout the course we will emphasize the importance of understanding both the “what” as well as the “why” of valuation techniques. To improve the effectiveness and impact of the valuation process, we will ensure that participants are able to both do a quality valuation as well as have the deeper understanding of the process necessary to be able to explain why they have done what they have done to persuade decision-makers to have confidence and to rely on the output of the valuation for driving decisions. Conceptually, the course will focus on the two core elements of any valuation: (1) how do we forecast the expected future free cash flows, and (2) how do we estimate the opportunity cost of capital to be used to discount these forecasted cash flows to estimate the value.

The course will cover both the conceptual and theoretical basis for the approach used in valuation as well as the ‘nuts and bolts’ application of valuation in a real-world context. The emphasis throughout will be on ‘why’ you are doing what you are doing. It is therefore important that every student strives to understand the theories behind the practice to be comfortable and capable of explaining why they are doing what they are doing in every context.

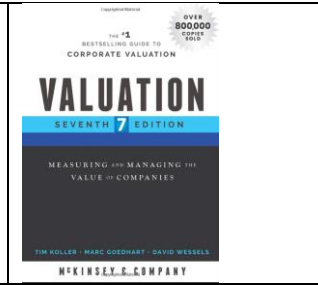
Reading Materials:

- Case materials and lecture notes on course webpage (Canvas)
 - Ferrari IPO, UV7259
 - Bidding for Hertz: Leveraged Buyout, UV1056

- Textbooks:

<p><i>“The Blue Line Imperative,”</i> by Kaiser and Young, 2013 (readings will be assigned from this book)</p>	
<p><i>“Corporate Valuation, 2nd edition”</i> by Holthausen and Zmijewski, 2019 (readings will be assigned from this book)</p>	

“*Valuation, 7th edition*”, by Koller, Goedhart and Wessels (anyone serious about valuation needs to own a copy of this book)



Format:

The structure of the course includes lectures, teamwork, case discussions, and team presentations. The major objective of the case method in finance is to **use the logic of financial theory to arrive at sensible conclusions** when faced with real world problems. While **there is not one absolutely right answer to a case, there are approaches which are not consistent with the principles of finance and others which are not**. One of the objectives of this course is to help you to distinguish between sensible and senseless arguments. Considering the professor’s analyses as the correct solution defeats the purpose of this course and contributes to the silly notion that in the “real world” there is a single correct recipe to be followed in the case of a valuation.

Student Responsibilities and Assessment:

1. Case Study Assignments: (40% of the course grade).

Students will organize themselves into groups of two to four members (groups of five will not be accepted) to work on all group assignments. Groups must be fixed throughout the course. Diverse background within the group is beneficial. Valuation is a team activity and the functioning of the team is a key determinant to the quality of the valuation. Students are expected to take steps throughout the course to ensure a high level of team engagement and effective teamwork. Although brief discussions across different groups are allowed, exchange of analysis and calculations is not. The major objective of the case method in finance is to **use the logic of financial theory to arrive at sensible conclusions** when faced with real world problems. Therefore, demonstration of the key concepts of financial theory is imperative in all cases.

Supporting computations and tables can be described in the text of the report or in an appendix and submitted in Excel format. All of the inputs and formulas used should be provided. Some of the case assignments contain questions that need to be addressed, however you will also be graded based upon how well you identify the relevant questions and issues to be addressed. Therefore, whether there are questions for the case or not, please consider what the relevant questions are in the context of each case and discuss why and then perform the necessary analysis to address these questions. **A subset of groups may be chosen to lead the discussion by presenting their analysis.**

2. Class Participation and Attendance: (15% of the course grade)

A goal of this course is to provide students with the opportunity to learn how to best contribute to discussions about complex financial issues. Therefore, this class depends and thrives on

class participation. It is an important and essential part of this course. Because so much learning in this course occurs in the classroom, it is important that you attend every class. **Voluntary class participation is encouraged. "Cold calls" will be made as to ensure that the class enjoys the benefit of every student's contribution.** Inadequate class participation combined with several absences can lead to a failing grade. Performance will be judged based on the quality of comments/answers. **Students are expected to prepare for each case and participate actively in class.** To facilitate recording of class participation, please keep the same sitting arrangement throughout the semester.

3. Team Valuation Project: (40% of the course grade)

As part of the course, students will be asked to value a company of their own choosing. Each team will have to submit four separate reports, one for each stage of the valuation project. Late submission will incur a penalty of 10% per calendar day, counting the day of submission. Complete instructions for this project will be available on the course website. It would be wise to form teams and start thinking about potential companies to value as soon as possible. Team composition and company names are due on February 1st.

4. Individual Reflection paper (5% of the course grade)

Learning is an effortful process and I have added this assignment in place of a final exam. The purpose of this exercise is to ensure that each individual devotes some time (a couple hours or more) to reflecting back on this course and trying to recall and deepen your understanding of the many topics and concepts covered. You are expected to submit (along with the group paper) your individual reflections on what you learned during this course and the insights you gained. It is expected to be between 2-5 pages and address the following elements: (1) Summarize and demonstrate understanding of the concepts taught in this course, (2) Summarize the insights you gained, and (3) Describe how these insights will impact you/your behavior going forward.

Please do not be evaluative (e.g., please avoid statements such as "I really loved the session when we talked about..." or "I found the discussion around xxx to be very confusing...") Simply emphasize your learning by structuring your reflections as, "What I learned was" Grading will be based on the depth and quality of your reflections as reflected in the depth and quality of the learning and insights you share in this report.

Important Note Concerning Group Grading Process:

To provide effective governance and to encourage effective teamwork, grades for groupwork will be allocated according to contribution allocations as assessed by the other members of your group for ALL group members of ALL groups. All group members are required to provide a response to the survey question below after all group work for the course has been completed. The results will apply to group grade allocation across group members for ALL of the groupwork throughout the course,

Survey question to be answered by all students enrolled in the course:

Please provide an allocation out of 100% for the contribution made by the individual members of your group to all group work submitted in this course, excluding any measure of

your own contribution, such that the sum totals 100%.

Each group member’s contribution will be assessed as the average of the percentages reported by the other members of the group. For example, if you are in a 5-member group and the other four members of your group gave you contribution allocations of 20%, 20%, 25% and 15%, then your average is 20% across 4 people, which translates into 16% across 5 (which puts you below average).

See the chart below as a sample template:

Group member name:	Howard Marks	Marie Curie	Mary O'Connor	Martin Luther King, Jr	Michael Jordan	Allocation (out of 25%)	Percent allocation (out of 20%)
Howard Marks		20%	20%	15%	25%	20%	16%
Marie Curie	25%		25%	25%	25%	25%	20%
Mary O'Connor	35%	30%		35%	30%	33%	26%
Martin Luther King, Jr.	35%	30%	35%		20%	30%	24%
Michael Jordan	5%	20%	20%	25%		18%	14%
TOTAL	100%	100%	100%	100%	100%	125%	100%

Your own grade will be the average of the contribution allocated by you as reported by your teammates. For example, if your 4 teammates gave you contribution allocations of 20%, 20%, 15% and 25%, such as for Howard Marks above, then your average allocation would be 20% as assessed by your 4 teammates, which results in a relative contribution of 16% out of 20% for your contribution to the team. In this case, your team grade will be reduced by 4% of the team average grade. As another example, had your teammates given you contribution allocations of 25%, 25%, 25%, and 25%, such as for Marie Curie above, then your average allocation would be 25%, which results in a relative contribution of 20% out of 20%.

Your resulting relative contribution allocation as rated by your teammates will then be used to either add to or deduct from the team’s overall grade on the group assignments according to the distance your relative contribution allocation is away from 20% (for groups of 5) or 25% (for groups of 4). Each 1% above/below the mean will result in an addition/deduction of 1% of the group grade. Therefore, for example if your group grade is 18/20 on the TER Negotiation exercise and your relative contribution is rated 24% in a team of 5, such as for Martin Luthor King, Jr. above, so that you are 4% above the mean of 20% for relative contribution, then your grade on the TER Negotiation exercise will be $104\% \times 18 = 18.72/20$. As another example, if you are in the same group with a group grade of 18/20 but your relative contribution is rated 14% in a team of 5, then your grade will be $94\% \times 18 = 16.92/20$.

Code of Ethics:

Submitted assignments for grading should be your own or your team’s own work only. Failure to observe this rule may result in an automatic failing grade for the course.

Kevin Kaiser:

Office Hours: tbd

Email: kaiserk@wharton.upenn.edu

Course Schedule: All dates and topics, including due dates of assignments, are subject to change

707 Spr 2022: JMHH 350, 3:30pm-5:00pm

Class #	Date	Topic	Assignment
1	Wednesday, January 19, 2022	Intro to the course	no assignment due today
2	Monday, January 24, 2022	Defining Value and Value Creation - The Opportunity	no assignment due today
3	Wednesday, January 26, 2022	Why is value and valuation important and for whom	no assignment due today
4	Monday, January 31, 2022	The hardest thing: TOCC \neq COF	no assignment due today
5	Wednesday, February 2, 2022	Valuation Elements and Historical Analysis	Ferrari #1
6	Monday, February 7, 2022	Historical Analysis in practice	no assignment due today
7	Wednesday, February 9, 2022	Defining and Forecasting Free Cash Flow	Valuation Project #1 - Historical Analysis
8	Monday, February 14, 2022	Valuation Project Deliverable #1	no assignment due today
9	Wednesday, February 16, 2022	Defining and Forecasting Free Cash Flow	Ferrari #2
10	Monday, February 21, 2022	Forecasting with Integrity #1	no assignment due today
11	Wednesday, February 23, 2022	Estimating the Continuing Value	Ferrari #3
12	Monday, February 28, 2022	Estimating the Continuing Value	no assignment due today
13	Wednesday, March 2, 2022	EXAM 1	EXAM 1
MBA Opportunity Week			
14	Monday, March 14, 2022	Everything except the discount rate	no assignment due today
15	Wednesday, March 16, 2022	Everything except the discount rate	Valuation Project #2 - Forecasting & Modelling
16	Monday, March 21, 2022	Estimating the discount rate	no assignment due today
17	Wednesday, March 23, 2022	Reviewing the conceptual foundations of CAPM	no assignment due today
18	Monday, March 28, 2022	Modigliani-Miller: WACC & APV	no assignment due today
19	Wednesday, March 30, 2022	Unlevering and Levering	no assignment due today
20	Monday, April 4, 2022	Concluding the Discount Rate	Ferrari #4
21	Wednesday, April 6, 2022	Reflection Session	no assignment due today
22	Monday, April 11, 2022	Complications and special situations (LBOs, etc.)	Hertz
23	Wednesday, April 13, 2022	Complications (M&A, emerging markets, etc.)	Mini-cases due today
24	Monday, April 18, 2022	Reflection Session dedicated to Exam-related Q&A	
25	Wednesday, April 20, 2022	EXAM 2	
26	Monday, April 25, 2022	No class - Exam week for MBA	
27	Wednesday, April 27, 2022	No class - Exam week for MBA	Valuation Project #3 - Completed Valuation

Cases (non-Wharton)

Ferrari IPO, UV7259

Bidding for Hertz: Leveraged Buyout, UV1056