

**The Wharton School – University of Pennsylvania
FNCE 7070
Valuation**

**Spring 2023
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

tbd

Classroom JMHH 255

FNCE 7070001 – 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

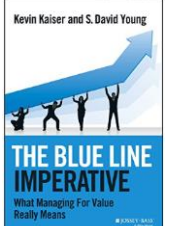
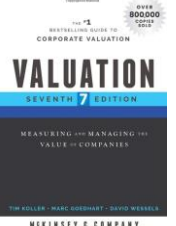
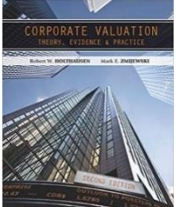
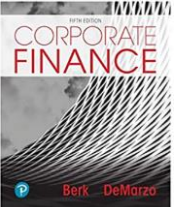
been noted that very often factors other than value-impact are incorporated into the decision process, either deliberately or inadvertently. In many cases, this is due to a lack of full understanding of why the valuation is being performed and the critical importance of value creation as the over-riding 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 (may or may not be covered in depth)
- Textbooks: The required textbook for this course is Corporate Valuation, 2nd edition, by Holthausen and Zmijewski. Recommended books include the following:

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|--|---|--|---|
| <p>“<i>The Blue Line Imperative</i>,” by Kaiser and Young, 2013 (readings will be assigned from this book)</p> |  | <p>“<i>Valuation, 7th edition</i>”, by Koller, Goedhart and Wessels (anyone serious about valuation needs to own a copy of this book)</p> |  |
| <p>“<i>Corporate Valuation, 2nd edition</i>” by Holthausen and Zmijewski, 2019 (readings will be assigned from this book)</p> |  | <p>“<i>Corporate Finance, 5th edition</i>”, by Berk and DeMarzo</p> |  |

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 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.

This course involves a high degree of teamwork. Valuation is a team activity, and the functioning of the team is a key determinant to the quality of the valuation. As we will learn, diverse backgrounds within the group is beneficial and you are encouraged to team up with people with whom you are unfamiliar. All students are expected to take steps throughout the course to ensure a high level of team engagement and effective teamwork by all members of the team. These steps may include scheduling times for team feedback and team assessment discussions and designing team processes for ensuring openness and honesty in feedback and peer-coaching.

Student Responsibilities and Assessment:

1. Case Study Assignments: (30% of the course grade).

Students will organize themselves into groups of four members (groups of three or five will not be accepted except to ensure all students are allocated to groups) to work on all group assignments. Groups must be fixed throughout the course. 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 case work, independent of the concepts. Late submission of any assignment relative to the deadline posted on Canvas will incur a penalty of 10% of the assignment grade per calendar day, counting the day of submission.

Supporting computations and tables can be described in the text of the report or in an appendix and are to be 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 assignment 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 in class.**

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 and valuation 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 in the course. Performance will be judged based on the quality of comments/answers. **Students are expected to prepare for each class and participate actively in class.** To facilitate recording of class participation, please keep the same seating arrangement throughout the semester.

3. Team Valuation Project: (30% 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 three separate reports, one for each stage of the valuation project. Late submission of any assignment relative to the deadline posted on Canvas will incur a penalty of 10% of the assignment grade per calendar day, counting the day of submission. Complete instructions for this project will be available on the course website and will be discussed in class. 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. Mid-term Exam (15% of the course grade)

There will be one exam covering the first half of the semester which will count toward 15% of the final course grade.

5. Individual Reflection paper (10% 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, including 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 19%, 20%, 18% and 19%, then your average is 19%.

See the chart below as a sample template:

| Group member name: | Howard Marks | Marie Curie | Mary O'Connor | Michael Jordan | Tom Brady | Percent allocation (out of 20%) |
|---------------------------|--------------|-------------|---------------|----------------|-------------|--|
| Howard Marks | 20% | 22% | 22% | 19% | 21% | 21.0% |
| Marie Curie | 21% | 18% | 22% | 19% | 21% | 20.8% |
| Mary O'Connor | 22% | 24% | 20% | 19% | 21% | 21.5% |
| Michael Jordan | 18% | 16% | 18% | 24% | 19% | 17.8% |
| Tom Brady | 19% | 20% | 18% | 19% | 18% | 19.0% |
| TOTAL | 100% | 100% | 100% | 100% | 100% | 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 21%, 22%, 19% and 21%, such as for Marie Curie above, then your average allocation would be 20.8%. In this case, your team grade will be increased by 0.8% of the team average grade. As another example, had your teammates given you contribution allocations of 19%, 20%, 18%, and 19%, such as for Tom Brady above, then your average allocation would be 19%.

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 group exercises and your relative contribution is rated 21.5% in a team of 5, such as for Mary O’Connor above, so that you are 1.5% above the mean of 20% for relative contribution, then your grade on the group work will be $101.5\% \times 18 = 18.27/20$.

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.

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

| Class # | Date | Topic | Assignment | Pre-reading |
|-----------------------------|------------------------------|--|---------------------------------|--|
| 1 | Wednesday, January 18, 2023 | Intro to the course | no assignment due today | K&Y TBLI - Chs 1-2 |
| 2 | Monday, January 23, 2023 | Why is value and valuation important and for whom | no assignment due today | K&Y TBLI - Chs 1-2, H&Z CorpVal - Ch 1 |
| 3 | Wednesday, January 25, 2023 | The hardest thing: TOCC ≠ COF | no assignment due today | KK lecture note: Perspectives and Roles in Corporate Finance |
| 4 | Monday, January 30, 2023 | Valuation Elements and Historical Analysis | no assignment due today | K&Y TBLI - Chs 3-4 |
| 5 | Wednesday, February 1, 2023 | Historical Analysis in practice | no assignment due today | H&Z CorpVal - Ch 2 |
| 6 | Monday, February 6, 2023 | Defining and Forecasting Free Cash Flow | Ferrari #1 | Ferrari: The 2015 IPO |
| 7 | Wednesday, February 8, 2023 | Forecasting and building a Financial Model | no assignment due today | H&Z CorpVal - Ch 3 |
| 8 | Monday, February 13, 2023 | Customer-based Corporate Valuation #1 | VP #1 - Historical Analysis | Guest lecture: Prof. Peter Fader |
| 9 | Wednesday, February 15, 2023 | Customer-based Corporate Valuation #2 | no assignment due today | Guest lecture: Prof. Peter Fader |
| 10 | Monday, February 20, 2023 | Forecasting in practice | Ferrari #2 | Ferrari: The 2015 IPO |
| 11 | Wednesday, February 22, 2023 | Continuing Value | no assignment due today | K&Y TBLI - Chapter 7, H&Z CorpVal - Ch 6 |
| 12 | Monday, February 27, 2023 | Mid-term Exam | Mid-term Exam | |
| | Wednesday, March 1, 2023 | No class - MBA Core exams | | |
| MBA Opportunity Week | | | | |
| 13 | Monday, March 13, 2023 | Exam feedback, Intro to Multiples & Discount Rates | no assignment due today | H&Z CorpVal - Ch 5 |
| 14 | Wednesday, March 15, 2023 | Intro to Multiples & Discount Rates | no assignment due today | H&Z CorpVal - Ch 5 |
| 15 | Monday, March 20, 2023 | Estimating the discount rate | Ferrari #3 | Ferrari: The 2015 IPO |
| 16 | Wednesday, March 22, 2023 | Reviewing the conceptual foundations of CAPM | VP #2 - Forecasting & Modelling | H&Z CorpVal - Ch 8 |
| 17 | Monday, March 27, 2023 | Modigliani-Miller: WACC & APV | no assignment due today | H&Z CorpVal - Chs 5 & 10 |
| 18 | Wednesday, March 29, 2023 | Unlevering and Levering | no assignment due today | H&Z CorpVal - Ch 10 |
| 19 | Monday, April 3, 2023 | Estimating the Opportunity Cost of Debt | no assignment due today | H&Z CorpVal - Ch 9 |
| 20 | Wednesday, April 5, 2023 | Multiples, Pricing and Valuation | Ferrari #4 | Ferrari: The 2015 IPO |
| 21 | Monday, April 10, 2023 | Complications and special situations : EM & Scenario DCF | no assignment due today | |
| 22 | Wednesday, April 12, 2023 | Complications and special situations : LBOs | no assignment due today | |
| 23 | Monday, April 17, 2023 | Complications and special situations : Distress | no assignment due today | |
| 24 | Wednesday, April 19, 2023 | Reflection Session for Course Content | no assignment due today | |