

IOWA STATE UNIVERSITY
College of Business

Finance 501: Financial Valuation and Corporate Financial Decisions
Spring 2017

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Office hours: MW 11:00am-12:00pm, and by appointment

Meets: Jan 9 – Feb 15

Section A: MW, 7:30am-10:50am
Gerdin 2117

Section XA: MW, 5:50pm-9:10pm
Des Moines campus

Course Objectives

This course will introduce you to the basic concepts and tools of modern financial economics. We will learn these tools by studying the major decisions facing corporate financial managers. Corporate financial decisions revolve around two key issues: i) deciding which potential investments to undertake (“capital budgeting decision”), and ii) determining how best to finance the investment opportunities that add value to the firm (“capital structure decision”). The course provides you with the concepts and skills needed to make these decisions, focusing on techniques for valuing real and financial assets and appropriate ways to measure the cost of capital. We will also discuss the attributes of different financing sources (debt vs. equity), how we might identify a company’s optimal financial structure, and how financing constraints can affect real investment decisions. If time permits, we will also examine short-run issues related to financial planning, cash budgeting, and working capital management. A list of course learning objectives is included at the end of the syllabus.

Course Materials

The textbook for the course is the 11th Edition of *Principles of Corporate Finance* by Brealey, Myers, and Allen. Other relatively recent editions of the book should be sufficient, although chapter numbers may be slightly different from those listed below. Additional readings may be distributed throughout the semester.

You will definitely need a calculator (or calculating device) of some kind. A financial calculator with a cash flow function is strongly recommended. I use the BAI Plus financial calculator made by Texas Instruments, and this is how I will work through most problems in class. You are also welcome to use Excel for the assignments and quizzes.

Evaluation

Grades will be based on the following:

| | |
|--------------------------------------|-----|
| Group problem solving and mini-cases | 50% |
| Individual online quizzes | 40% |
| In class contributions | 10% |

The problem solving and mini-cases are designed to help you better understand the material covered in class and introduce you to various practical ways the material can be applied. You should work these assignments with your group, and all group members will receive the same grade. There will be approximately five of these problem sets/mini-cases distributed during the semester. Your team’s

responses to the problems should be submitted in a typed, professional manner, with clear explanations of how you approached the problem and arrived at the final answer (supporting materials, such as Excel files, can be submitted alongside the main document if you wish).

There will also be approximately five quizzes to check your comprehension of the material as we move through the course. The quizzes will be administered individually to each student online via Blackboard. Please understand that each student is responsible for completing his/her own quiz without help or consultation with any other persons. Quiz and assignment due dates will be announced well ahead of time in class and on Blackboard and will depend on how fast we cover the material.

A small percentage of the final grade is based on in-class contributions over the semester. These contributions can take many forms, including raising pertinent questions, engaging in classroom discussions, or making presentations to the class.

Letter grades will be assigned as follows:

| | |
|---------------------------|----|
| $\geq 95\%$ | A |
| $\geq 90\% \ \& \ < 95\%$ | A- |
| $\geq 87\% \ \& \ < 90\%$ | B+ |
| $\geq 83\% \ \& \ < 87\%$ | B |
| $\geq 80\% \ \& \ < 83\%$ | B- |
| $\geq 77\% \ \& \ < 80\%$ | C+ |
| $\geq 73\% \ \& \ < 77\%$ | C |
| $\geq 70\% \ \& \ < 73\%$ | C- |
| $\geq 60\% \ \& \ < 70\%$ | D |
| $< 60\%$ | F |

Disability Accommodation

If you have a documented disability and anticipate needing special accommodations in this course, please make arrangements to meet with me early in the semester. You will need to contact the Disability Resources office (515-294-7220) to provide documentation of your disability and to obtain a Student Academic Accommodation Request (SAAR) form. Disability Resources is located on the main floor of the Student Services Building, Room 1076.

Tentative Schedule for Finance 501 (*Subject to change*)

| Topic | Brealey, Myers & Allen |
|---|-----------------------------------|
| Introduction; Goals of the firm; Computing net present value; Annuities and perpetuities | Chapters 1 and 2 |
| Valuing financial assets: Bonds and interest rates | Chapter 3 |
| Valuing financial assets: Common stock; Capital market history; Portfolio risk and return | Chapters 4 and 7 |
| Portfolio theory and CAPM | Chapter 8 |
| Risk and the cost of capital | Chapter 9 |
| Valuing real investments: Alternative decision rules | Chapter 5 |
| Valuing real investments: Using NPV | Chapter 6 |
| Capital budgeting in practice | Chapter 11 |
| Does capital structure matter? | Chapters 17-19 |

Learning Outcomes for Finance 501 – Financial Valuation and Corporate Financial Decisions

- I. The time value of money
 - a. Compute the present and future value of a single cash flow
 - b. Compute the present and future value of multiple cash flows
 - c. Recognize and value annuities and perpetuities

- II. The value of financial assets and the determinants of interest rates
 - a. Compute the value of a bond and solve for a bond's yield-to-maturity
 - b. Understand how interest rate risk, default risk, and time-to-maturity impact bond yields
 - c. Compute the value of common and preferred stock and find the cost of equity

- III. Portfolio theory and the trade-off between risk and return
 - a. Understand diversification and compute portfolio risk and return
 - b. Distinguish between systematic and unsystematic risk
 - c. Use the Capital Asset Pricing Model (CAPM) to compute expected returns and the cost of capital
 - d. Find the weighted average cost of capital (WACC) based on the firm's capital structure

- IV. Capital budgeting and the value of real investments
 - a. Understand the appropriate investment criteria for capital budgeting decisions
 - b. Isolate the relevant incremental cash flows for the capital budgeting decision
 - c. Evaluate investments based on net present value (NPV) and internal rate of return (IRR)

- V. Capital structure and financing constraints
 - a. Understand the Modigliani and Miller (MM) propositions and the conditions under which capital structure affects firm value
 - b. Understand alternative theories of capital structure
 - c. Understand the factors that make external finance costly and implications of financing constraints for real investment