Managerial Finance MBA 643 002

Wednesdays 7:20 pm to 10:00 pm; August 29 – December 12, 2012 (no class November 21)

Innovation Hall 204

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Course Objective

The goal of this course is to develop in the student the analytical skills for making corporate investment and financial decisions and risk analysis. Topics covered include the concepts of present value and the opportunity cost of capital, discounted cash flow analysis and other valuation techniques, issues of short and long term financial management, risk and return, capital asset pricing model, capital budgeting and risk analysis, corporate capital structure and financing decisions, dividend policy, investment and financial decisions in the international context, including exchange rate/interest rate risk analysis, mergers and acquisitions, leveraged buyouts and private equity, derivatives and issues of corporate governance and control.

The course is oriented towards practice rather than theory and is designed for practitioners with guidance for those interested in pursuing theory, computational finance or risk/financial engineering in the future.

Pedagogical Method

The course teaching methodologies will be based on both lectures and Harvard Business School cases with some outside readings. You must complete the readings and assignments prior to each class. You are responsible, as in any work environment, for arriving prepared to discuss the assignments when they are due. Class participation, constructive and thoughtful, is an important part of your grade. Students are responsible for making their identities known so that their class participation contributions can be properly evaluated.

Case materials and notes are obtained from the Harvard Business School Publishing website. The link to the Harvard Business School Publishing site for this course is http://cb.hbsp.harvard.edu/cb/access/14474864. You must create an account, user name and password in order to purchase the materials. Materials noted on this syllabus with an asterisk* are optional. You will be responsible for the materials in the non-optional cases and notes. All text readings are for your reference.
The course is roughly divided into two sections: in the first part you must acquire certain basic skills including financial statement and cash flow analysis, preparation of pro forma statements, the cost of debt, equity and capital, discounting cash flows and valuation techniques. During this part of the course there will be frequent homework assignments and quizzes for practice and to assess whether the students have acquired knowledge of these techniques. The second part of the course will require the students to apply this knowledge in a variety of settings.

**Teams**

A characteristic of financial firms (and the finance function, generally) is that they typically work in small teams. You are encouraged to form study groups to prepare the cases for class discussion. A substantial amount of the homework and assignments for this course, as in the work environment, must be done in teams. You are responsible for the formation of teams. The list of teams and team members will be finished by the end of the second class. The first assignment to be completed by teams will be due at the beginning of the third class. Collaboration may be possible via online resources provided by GMU through Blackboard or other methods. You are responsible for making these arrangements.

**Written Assignments and Oral Class Presentations**

All written assignments are due typewritten in hard copy at the beginning of class. You are encouraged to make professional presentations in these assignments. Teams are expected to use powerpoint slides in their oral presentations- bring the presentation on a flash drive and supply a hard copy prior to the presentation.

The information and background required for completion of the assignments are contained in the assigned readings and cases. The assignments test, among other things, your ability to acquire and use information on your own and in collaboration with a team.

All assignments, including the oral presentations, will focus upon answering the questions posed in the syllabus and will be graded based upon the quality of those answers: there is no particular “correct answer” to many of those questions.

**Written Assignment Due Dates**

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<th>Date</th>
<th>Assignment</th>
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<td>September 5</td>
<td><strong>Statement of Cash Flows: Three Examples</strong> (Individual)</td>
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<td><strong>Bond Math</strong> (Team)</td>
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<td><strong>Capital Budgeting: Discounted Cash Flow Analysis</strong> (Team)</td>
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<td><strong>Goldman, Sachs &amp; Co. Nikkei Put Warrants-1989</strong> (Team)</td>
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<td>October 10</td>
<td><strong>Foreign Exchange Markets and Transactions</strong> (Team)</td>
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<td>October 17</td>
<td><strong>Long-Term Capital Management A, B, C, D</strong> (Team)</td>
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<td>October 24</td>
<td><strong>Bear Stearns, (A) and (B)</strong> (Team)</td>
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Classes 10-15 Teams will select/be assigned two cases for analysis and presentation to the class during this period.

**Quizzes**

Certain fundamental techniques which must be mastered early in the MBA program will be the subject of quizzes which will be administered at the beginning of class early in the semester. These quizzes are open book/open notes/calculator required. NO CELLPHONES OR COMPUTERS MAY BE USED AT ANY TIME DURING THE QUIZZES.

Class No. 2 September 5 Drivers of Industry Structure company identification
Class No. 3 September 12 Preparation of cash flow statement from historical financials
Class No. 4 September 19 Net Present Value of future cash flow
Class No. 5 September 26 Cost of Capital and cash flow valuation

**Grading**

Grades will be assigned based upon the following weights:

- Class participation: 30%
- Six top grades from eight written assignments: 30%
- Two oral presentations: 20%
- Three best of four quiz grades: 20%

All team members will receive the same grade on all team assignments and presentations. Class participation will be heavily weighted in the second half of the semester towards contributions made in respect of presentations made by teams of which the class participant is not a member: you must participate constructively in discussions when you are not presenting to get class participation credit.

There will be no excuses for failure to attend quizzes, failure to turn in assignments when due at the beginning of class or failure to make team presentations without written documentation in accordance with GMU policy.

**Primary Materials**

Harvard Business School cases and notes will constitute the primary course materials. The course packet can be downloaded at the HBS Publishing website. Principles of Corporate Finance, 11th ed., Brealey, Meyers and Allen is not required; it could be useful as background and chapter references are supplied.

Materials noted on this syllabus with an asterisk* are optional.

**Course Outline**

**Class One: August 29**

**Topics**

- Review of housekeeping details for the course
- Overview of what will be covered in the course
• Basic tools of financial analysis: cash flow and ratio analysis
• Case analysis of Clarkson Lumber

Readings

Case Studies and Notes:
1. Clarkson Lumber Company, 9-297-028
2. Note on Financial Analysis, 9-206-047
3. Drivers of Industry Structure, 5-201-049
4. Introduction to Financial Ratios and Financial Statement Analysis, 9-193-029*

Textbook Chapters:
• Chapters 1 and 6

CLARKSON LUMBER COMPANY

The owner of a rapidly growing retail lumber company is considering the financial implications of continued rapid growth. The magnitude of the company's future financing requirements must be assessed in the context of the company's access to bank finance and/or equity finance.

Objectives:
1. To develop skills in financial analysis, financial forecasting, and financial planning.

Questions:
1. Why has Clarkson Lumber borrowed ever increasing amounts despite its consistent profitability?
2. How has Mr. Clarkson met the financing needs of the company during the period 1993 through 1995? Has the financial strength of Clarkson Lumber improved or deteriorated?
3. How attractive is it to take the trade discounts?
4. Do you agree with Mr. Clarkson's estimate of the company's loan requirements? How much will he need to finance the expected expansion in sales to $5.5 million in 1996 and to take all trade discounts?
5. As Mr. Clarkson's financial adviser, would you urge him to go ahead with, or to reconsider, his anticipated expansion and his plans for additional debt financing? As the banker, would you approve Mr. Clarkson's loan request, and, if so, what conditions would you put on the loan?

Class Two: September 5

Quiz
During class there will be a quiz which will require the student teams to prepare answers to the “Drivers of Industry Structure” case listed for Class 1. This quiz may require the use of a calculator. The use of computers or cellphones will not be permitted. Open book, open notes. Name and student ID numbers of the team members will be clearly noted on the submission.

Topics
• Financial Analysis, cont’d.
• Preparation and Use of Cash Flow Statements and Forecasts

Readings

Case Studies and Notes:
2. The Balance Sheet, 9-101-108 *
3. The Income Statement, 9-101-109 *

Textbook Chapters:
• Chapters 5, 28 and 29

Written Assignment Homework (Individual)

Answers to the questions I and II in the case, “Statement of Cash Flows: Three Examples”. This case introduces the statement of cash flows through three examples of multi-year statements of cash flows from three unidentified companies and requires an examination of cash flows, and analysis of profitability of operations, investment policies, and financing.

Each student will submit, in hard copy prior to class, three excel spreadsheets (one each for Company 1, Company 2 and Company 3) with the years 1991, 1990 and 1989 as the headings across the top of each Company’s spreadsheet and the captions for the questions down the left side with answers to those questions in the corresponding cells.

Class Three: September 12

Quiz

At the beginning of class there will be a quiz which will require the students to prepare a summary cash flow statement and forecast based upon historical financial statements. This quiz will require the use of a calculator. The use of computers or cellphones will not be permitted. Open book, open notes.

Topics
• Introduction to compounding interest, annuities and perpetuities, IRR, FV, PV and NPV
• Government bond market
• Zero coupon bonds and the treasury yield curve

Readings

Case Studies and Notes:
1. Bond Math, 9-201-101
3. Cougars, 9-295-006

Textbook Chapters:
• Chapters 2, 3, 4, 23 and 24

COUGARS

Objectives:
1. Introduction to zero coupon bonds and stripping coupon bonds.

2. Concerns the relationship between the spot curve, the strip curve, and the coupon curve and the U.S. Government Debt Market and various conventions used to depict the structure of interest rates.

This case presents four exercises that teach compounding interest and valuing bonds. Generalization to the application of bond math to cash flows generally.

Questions:

1. Why have riskless zero coupon bonds been so successful with investors?
2. What relationship do the prices of riskless zero-coupon bonds have with the term structure of interest rates?
3. How are the spot, strip, and coupon yield curves related?
4. How much value did A.G. Becker Paribas create for itself through the COUGARS offering? What was the source of this value? (Assume that the Treasury bill maturing on December 6, 1983 is trading at a 8.11% discount yield on November 16, 1983.)

Written Assignment Homework
Each team will submit written answers to the four questions/problems in the “Bond Math” case in hard copy prior to the start of the class. Name and student ID numbers of the team members will be clearly noted on the submission.

Class Four: September 19

Quiz
At the beginning of class there will be a quiz which will require the students to prepare a summary cash flow statement and forecast based upon historical financial statements of a hypothetical company and calculate the Net Present Value of the Company’s cash flow (the value of the firm). The terminal value and discount rate will be given as assumptions. This quiz will require the use of a calculator. The use of computers or cellphones will not be permitted. Open book, open notes.

Topics
- Capital budgeting and the use of NPV analysis
- CAPM and WACC
- Risk and return

Readings

Case Studies and Notes:
1. Capital Budgeting: Discounted Cash Flow Analysis, 9-298-068
2. Business Valuation and the Cost of Capital, 9-201-037
3. An Introduction to Cash Flow Valuation Methods, 9-295-155

Textbook Chapters:
- Chapters 8,9,10 and 19
Objectives:
1. Introduction to the cost of capital as used in discounted cash flow valuation analyses.
2. Basic financial economic principles and practical problems encountered in calculating the cost of capital, especially WACC.

Cautionary advice about computing and applying WACC. The exercise comprises seven problems that collectively allow students to work through each type of cash flow that is encountered in capital budgeting, also covering such issues as product cannibalization and real options.

Written Assignment Homework
Each of the groups formed by class members will submit in hard copy, before the class, written answers to the seven questions in the Note, “Capital Budgeting: Discounted Cash Flow Analysis”. Group members may be called upon during the class to present solutions to one or more of the problems. Answers will be contained on two typewritten pages, including graphs and charts, with conventional margins. Name and student ID numbers of the team members will be clearly noted on the submission.

Class Five: September 26

Quiz
At the beginning of class there will be a quiz which will require the students to calculate the cost of capital, given selected assumptions, and to use that cost of capital to value a firm’s free cash flow, which will be given. This quiz will require the use of a calculator. The use of computers or cellphones will not be permitted. Open book, open notes.

Topics
- Cost of Capital
- CAPM, WACC
- Hurdle rates
- Risk management
- Dividends, share repurchases and payout policy

Readings
Case Studies and Notes:
1. Marriott Corporation: The Cost of Capital, 9-289-047
2. Why Manage Risk?, 9-294-107

Textbook Chapters:
- Chapters 7 and 16

Written and Oral Class Presentation Assignment Homework
Each of the groups formed by class members will submit in hard copy, before the class, the answers to the questions below in respect of the case “Marriott Corporation: The Cost of Capital”. Answers will be contained on two typewritten pages, including graphs and charts, with conventional margins. Name and student ID numbers of the team members will be clearly noted on the submission. Group members may be called upon during the class to present solutions. The presentations will be in powerpoint format.
MARRIOTT CORPORATION

Objectives:
1. Use of CAPM to compute WACC
2. Riskless rate and market premium
3. Use of comparable companies and adjustments for leverage to calculate beta

Questions:
1. Are the four components of Marriott’s financial strategy consistent with its growth objective?
2. How does Marriott use its estimate of its cost of capital? Does this make sense?
3. What is the weighted average cost of capital for Marriott Corporation?
   a. What risk-free rate and risk premium did you use to calculate the cost of equity?
   b. How did you measure Marriott’s cost of debt?
4. What type of investments would you value using Marriott’s WACC?
5. If Marriott used a single corporate hurdle rate for evaluating investment opportunities in each of its lines of business, what would happen to the company over time?
6. What is the cost of capital for the lodging and restaurant divisions of Marriott?
   a. What risk-free rate and risk premium did you use in calculating the cost of equity for each division? Why did you choose these numbers?
   b. How did you measure the cost of debt for each division? Should the debt cost differ across division? Why?
   c. How did you measure the beta of each division?
7. What is the cost of capital for Marriott’s contract services division? How can you estimate its equity costs without publicly traded comparable companies?

Class Six: October 3

Topics
- Introduction to foreign exchange market
- Behavior economics and finance
- Efficient Market Hypothesis
- Theory versus practice in finance

Readings
Case Studies and Notes:
1. Foreign Exchange Markets and Transactions, 9-205-016
2. The End of Rational Economics, Harvard Business Review, Reprint R0907H *
3. The Origin of Wealth, A Harvard Business Press Book Summary, HBP Product #5397ES *

Textbook Chapters:
Written Assignment Homework
Each team will submit a paper with written answers to the eight exercises in the “Foreign Exchange Markets and Transactions” case. Answers will be contained on two typewritten pages, including graphs and charts, with conventional margins. Answers will be contained on two typewritten pages, including graphs and charts, with conventional margins. Name and student ID numbers of the team members will be clearly noted on the submission.

Class Seven: October 10
Topics
- Derivative securities: equity and foreign exchange options
- Options pricing
- Pricing a securities offering

Readings
Case Study and Notes:
1. Equity Derivatives, 9-208-117
2. Risk Management For Derivatives, UV1047 *
3. Interest Rate Derivatives, 9-294-095 *
4. An Overview of Credit Derivatives, 9-297-086 *

Textbook Chapters:
- Chapters 20 and 21

Written Assignment Homework
Each team will submit written answers to the following questions in the “Goldman, Sachs & Co. Nikkei Put Warrants-1989” case in hard copy prior to the start of the class. Answers will be contained on two typewritten pages, including graphs and charts, with conventional margins. Name and student ID numbers of the team members will be clearly noted on the submission.

GOLDMAN, SACHS & CO. NIKKEI PUT WARRANTS

Objectives
1. Analysis of a transaction which employs a variety of derivatives
2. Overview of a capital markets transaction
3. Competition and regulatory considerations in investment banking

Questions:
1. Why were Nikkei-linked Eurobonds issued? Make sure you understand how the embedded puts can be stripped from the Nikkei-linked Eurobonds, and how these puts can be repackaged and resold. What other type of instrument could you design to satisfy the preferences of the alleged buyers of these bonds? As a bank owing these puts, what can you do with them?
2. Study the proposed design for the Nikkei Put Warrant (NPWs). What features are primarily designed to appeal to the target U.S. retail clientele? What features are
primarily designed to simplify the process of creating (hedging) the NPWs? How do the features of the proposed NPWs differ from those sold to institutional investors? To ritual investors in Toronto?

3. Why is the Kingdom of Denmark issuing these warrants? What do they gain? What risks do they bear in the proposed transaction?

4. What risks does GS&Co. bear in executing this transaction? How are these risks mitigated? Specifically, compare how the security design chosen and the raw materials available affect the exchange rate risk faced by GS&Co. and by BT Bank of Canada (seller of the first Toronto-listed Nikkei put warrant) Describe how you think GS&Co.’s QUANTOS product will mitigate the risk of exchange rate changes over time.

5. Assuming GS&Co. must invest $1.00 per warrant to hedge its currency risk using QUANTOS, what is the lowest price per warrant that GS&Co. could charge for the currency-hedged NPWs and still breakeven?
   a. A. If the NPWs were European-style, and not American-style, what would the minimum break-even be?
   b. How will the American-style feature affect GS&Co.’s break-even? Why? How much of a difference do you think it will have on the break-even price you calculated?

6. How should GS&Co. price the warrant? Why?

Class Eight: October 17

Readings

Case Studies and Notes:

1. Long-Term Capital Management A, 9-200-007
2. Long-Term Capital Management B, 9-200-008 *
3. Long-Term Capital Management C, 9-200-009
4. Long-Term Capital Management D, 9-200-010 *
6. Securities Lending After the Financial Crisis, 9-31-130 *

Textbook Chapters:

• Chapter 18

Written Assignment Homework

Each team will submit a paper with written answers to the questions below in respect of the four Long-Term Capital Management cases. The paper may be no longer than two pages, including charts and tables, single-spaced typewritten with standard margins. Name and student ID numbers of the team members will be clearly noted on the submission.

LONG-TERM CAPITAL MANAGEMENT
Questions:
1. Describe the investing strategy of LTCM.
2. Explain Exhibit 3 in LTCM (A), pg. 21; see also pp 10-11.
3. What does “selling volatility” mean, pp 7-8, LTCM (A)?
5. Is LTCM a “systemically important” institution? Explain.

Class Nine: October 24

Topics
- “Subprime crisis” and global financial crisis
- Principal-agent problems
- Informational asymmetry: moral hazard and adverse selection

Readings
Case Studies and Notes:
1. Investment Banking in 2008 (A): Rise and Fall of the Bear, KEL378
2. Investment Banking in 2008 (B): A Brave New World, KEL 380

Textbook Chapters:
- Chapter 32

Written Assignment Homework:
Each team will submit a paper with written answers to the questions below in respect of the two Bear, Stearns cases. The paper may be no longer than four pages, including charts and tables, single-spaced typewritten with standard margins. Name and student ID numbers of the team members will be clearly noted on the submission.

BEAR STEARNS (A)

Objectives
1. Understanding the “subprime crisis” background of the case
2. Examination of Bear Stearns actions in relation to the crisis
3.

Questions:
1. What role did Bear’s culture play in its positioning vis-à-vis its competitors, and what role might that culture have played in its demise?
2. How did Bear’s potential collapse differ from that of LTCM in the eyes of the Federal Reserve?
3. What could Bear have done differently to avoid its fate:
   a. In the early 2000s?
b. During the summer of 2007?
c. During the week of March 10, 2008?
4. Who stood to benefit from Bear’s implosion?
5. Is market perception of liquidity more important for an investment bank than it is for a traditional manufacturing or distribution business? If so, why?
6. How could Bear have addressed perceptions of it illiquidity? Could it have stopped the run on the bank, and if so, how?
7. Did Bear’s failure undermine the viability of so-called “pure-play” investment banks?
8. What role should the Fed play in maintaining order in world securities markets?

**BEAR STEARNS (B)**

**Objectives:**
1. Regulatory and competitive factors affecting demise of Bear Stearns
2. Bear Stearns’ competitive strategy and its effects
3. Future of the investment banking industry

**Questions:**
1. Why were proponents of deregulation so successful in the late 1990s? How much can we blame deregulation for the meltdown in the investment banking industry, and how could the government have foreseen and/or stopped the domino effect before the crisis of 2008?
2. Could any one of the investment banks have remained competitive without following the industry trend of taking on increasing amounts of leverage to boost returns on investment? If so, how?
3. Why was Lehman Brothers allowed to collapse while Bear Stearns was not?
4. Did the compensation structure of the investment banking industry encourage banking executives and employees to take on excessive risk to boost short-term profits? Why or why not?
5. How much of the industry-wide crisis stemmed from the investment banks’ financials and the current economic climate as opposed to investor panic and speculation?
6. Both Bear and Lehman bailed out their proprietary hedge funds. Did they have any other option? What would have happened had they not done so?
7. Could Morgan Stanley and Goldman Sachs have survived without becoming bank holding companies? What were the benefits and disadvantages of becoming bank holding companies? What does designation as bank holding companies mean for the way Morgan and Goldman operate going forward?

**Class Ten: October 31**

**Topics**
- IPO’s
- Industry analysis, valuation based on comparable companies and transactions
- Cross-border, international finance
- Analysis of company’s competitive position and effects on valuation
- Private equity industry
Readings

Case Studies and Notes:
1. Rosneft’s Initial Public Offering (A), TB0085
2. Sula Vineyards, NA0054
3. A Note on the Initial Public Offering Process, 9-200-018
4. SWOT Analysis I: Looking Outside for Threats and Opportunities, 5528BC
5. SWOT Analysis II: Looking Inside for Strengths and Weaknesses, 5535BC
6. The Five Competitive Forces that Shape Strategy, HBR Reprint

Textbook Chapters:
- Chapters 13 and 27

Homework
TEAM PRESENTATION ASSIGNMENT on Rosneft (A)

ROSNEFT (A)

Objectives:
- Valuation of natural resources company in IPO setting
- Assessment of cross-border investment in BRIC

Questions:
1. How does Rosneft’s complex history affect an investor’s assessment of its investment potential?
2. What are the fundamental drivers of the value of an oil and gas company like Rosneft?
3. As an oil and gas company, is Rosneft likely to be a high quality producer and fundamentally sound over the foreseeable future?
4. What specific risks should an investor consider in this specific IPO?
5. What are the pros and cons of the various valuation techniques explored in the case?
6. What are the key features of a discounted cash flow valuation (DCF) of Rosneft?
7. What are the issues which must be resolved in your DCF analysis?
8. What conclusions would one draw from the comparables analysis of Case Exhibit 7?
9. What is Rosneft worth in total? Does its value change in any way relative to what percentage share of the firm is floated publicly?

Homework
TEAM PRESENTATION ASSIGNMENT on Sula Vineyards

SULA VINEYARDS
Objectives:
1. Develop an understanding of a particular industry (wine-making) in a developing country (India) context
2. Conduct a valuation of a small (entrepreneurial) business using a variety of financial valuation methods
3. Use common statement and ratio analyses that give credence to strategic decision-making
4. Use of typical SWOT/Five-Force Analyses to aid in strategic decision-making

Questions:
1. Evaluate the attractiveness of the Indian wine industry using the “Five Forces” model. How is Sula positioned?
2. Perform a SWOT analysis for Sula: what areas require improvement?
3. Assess Sula’s financial performance over the last five years using the data in case Exhibits 5-7 by preparing common size financial statements and financial ratios. What conclusions can you make?
4. Evaluate the three alternative action plan scenarios presented in case Exhibits 11-16. Create pro forma income statements for each growth scenario based on data from case Exhibits 5-10. What conclusions can you draw?
5. Create pro forma balance sheets for each scenario. Use “Additional Funds Needed (AFN)” on the balance sheet as the “plug figure”, as a current asset or current liability. Add or subtract interest income/expense from income statement.
6. Prepare Free Cash Flow statements for the past five years and for the projected period. Compare these and state how these affect your scenario choice.
7. Project the value of the firm over the next five years. How do these projections affect the firm’s capital structure ratios when compared to the book value ratios?
8. Based upon your expectation for the Indian wine industry growth, what recommendations would you make to Rajeev to enable Sula to participate profitably over the next few years? Which growth rate should Sula use as a target, and what strategic and financial courses of action should be taken to support your proposal?

Class Eleven: November 7

Topics
- Leveraged buyouts
- Corporate governance, conflict of interest
- Valuation in going-private transaction setting

Readings

Case Studies and Notes:
1. HCA, Inc. (A), 9-207-076
2. A Note on Valuation in Private Equity Settings, 9-297-050

Homework
TEAM PRESENTATION ASSIGNMENT on HCA (A)
**HCA (A)**

Objectives:
1. Understand the motives for an LBO of HCA
2. Review the LBO process
3. Valuation Approaches: i. Free cash flow; ii. Capital Cash flow; iii. Incremental interest tax shield

Questions:
1. Why is the senior management of HCA pursuing an LBO of the firm?
2. How is HCA performing? What are the challenges of the firm going forward without the LBO? How does the LBO help resolve these challenges?
3. What is your estimate of the maximum price that the LBO firms should be willing to pay for HCA? i. Use the CCF approach based upon the cash flow forecasts in Exh. 9 along with the assumptions about the risk free rate, the risk premium and the tax rate in Exh. 10; Use the comparable trading and transaction multiples based on the information in Exh. 12 and 13.
4. How do your estimates of the maximum price that the LBO firms should be willing to pay for HCA compare to the discounted cash flow values in Exh. 11? How do you explain the differences, if any?
5. Is the offer fair to shareholders? What should you compare the offer price to when deciding if an offer is fair or not?
6. Are there any reasons for shareholders to be concerned about the LBO process? What are the conflicts, if any?
7. If you were a member of the special committee evaluating the proposed LBO would you recommend that the proposed deal be approved?

**Class Twelve: November 14**

**Topics**
- Negotiations and dispute resolution
- Value-added private equity investing
- Cross-border investments
- Environment for foreign investors in China

**Readings**

*Case Studies and Notes:*
1. Shenzhen Development Bank, 9-210-020
2. Analyzing Complex Negotiations, 9-9-03-088
3. Deal Structure and Deal Terms, 9-806-085

**Homework**

TEAM PRESENTATION ASSIGNMENT on Shenzhen Development Bank
**SHENZHEN DEVELOPMENT BANK**

**Objectives:**
1. Provide an opportunity to assess the investment thesis and risk factors for a private equity investment by foreign investors in an emerging market setting. In particular, the case highlights potential political and regulatory risks that are present in most emerging markets, and provides a vehicle to assess the severity of these risks and discuss the strategies that may be used to mitigate them.
2. Provide an opportunity to value a private equity takeover target using multiples from comparable companies and precedent transactions. In doing so, the case provides a vehicle to discuss the concepts of illiquidity discount and control premium and illustrate ways to quantify them.
3. Illustrate the importance of managing relationships for private equity investing, especially in emerging markets where formal market mechanisms are under-developed, and where relationships with relevant local and central government entities play a crucial part in determining deal success.
4. Highlight the importance of effective control rights in turnaround deals, especially in situations where conflicts of interests among powerful stakeholders could derail restructuring efforts, e.g., at state-owned companies with politically connected managers.

**Questions:**
1. What makes SDB an attractive target for investment, and what are the potential sources of value?
2. What are the key risks for investing in SDB, and how can Newbridge mitigate these risks? Consider: SDB's financial performance; Key risk factors for investing in SDB;
3. Why can Newbridge win the deal? Which multiples can be used to value SDB? 2. B) Is Newbridge paying the right price for SDB? What is an appropriate valuation range?
4. Why has the Newbridge-SDB deal Jailed to go through the transition stage? What are the key lessons that can be learned from the failure? Given the public falling-out, should Newbridge continue to pursue the investment or should it walk away? If Newbridge decides not to give up, what should it do immediately to save the deal, and what should be the key initiatives in Newbridge's turnaround plan post investment?

**Class Thirteen: November 28**

**Topics**
- Raising funds for new ventures
- Environment for foreign investors in India
- Pricing IPO’s

**Readings**

*Case Studies and Notes:*
1. Motilal Oswal Financial Services Ltd.: An IPO in India, 9-807-095
2. Bharti Tele-Ventures, 9-704-426

Homework

TEAM PRESENTATION ASSIGNMENT on Motilal Oswal Financial Services, Ltd.

MOTILAL OSWAL FINANCIAL SERVICES LTD.

Objectives:
1. Discuss investments in emerging markets
2. Review the timing of an IPO and how interests can differ between not just the company and investors, but even amongst the private equity investors.
3. Explore alternative valuation approaches.

Questions:
1. The case mentions an IRR at which the PE firms could put their shares back to the company in five years. What IRR seems reasonable?
2. Value MOFSL, using the following assumptions: Revenue CAGR of 34% between FY 2006 and FY 2009; Profit growth of 35% over the same period; the customer base rises to 320,000 by end of FY 2009; no long-term debt, and liabilities and assets both have CAGR of 43% between FY06 and FY09.
3. Given the information in the case regarding P/E multiples of companies above and below $100 million in revenues, should MOSFL go public or hold off? Why?

Homework

TEAM PRESENTATION ASSIGNMENT on Bharti Tel-Ventures

BHARTI TEL-VENTURES

Objectives:
1. Identify sources of success for entrepreneurial venture
2. Analyze current competitive position of successful venture
3. Chart the course of the venture going forward

Questions:
1. Why did Bharti become so successful? What are the key competitive advantages that Bharti has developed over time? How can an entrepreneur with limited access to capital, in a capital-scarce country, succeed in a capital-intensive industry?
2. Should Bharti worry about the entry by the much larger Reliance and Tata Group into mobile telephony? Which company is best positioned to succeed in mobile telephony in India in the long-run?
3. How should Bharti evolve its business model to deal with future opportunities and threats?
Class Fourteen: December 5

Topics
- Investing in securities of distressed companies
- Political and regulatory environment of financial transactions
- High yield debt market, junk bonds
- Venture capital in China

Readings
Case Studies and Notes:
1. SAIF: May, 2004, 9-805-091
2. First Capital Holdings Corp., 9-296-032

Homework
TEAM PRESENTATION ASSIGNMENTS on SAIF: May, 2004

SAIF: MAY, 2004

Objectives:
1. Study of venture capital in China
2. Consider the Shanda investment, whether it was a good deal and how the IPO should be priced
3. Contrast the strategy of SAIF with that of Gobi and state which of the two is more likely to succeed in China
4. Explore corporate venture capital

Questions:
1. How would Shanda’s IPO at $11 per share affect Cisco and Softbank, in addition to Shanda and SAIF? How might the goals of the four differ?
2. How does VC in China differ from that in Silicon Valley? What aspects of the Shanda transaction and due diligence feel unique to China?
3. Andy says SAIF is not a corporate VC. Might you call it a fund-like strategic investor? What would be the difference between the two? If a corporate VC is an unsustainable model, what explains the long history of Intel Capital? Is there a role for corporate VC in the venture ecosystem, or does it seem that corporate VC efforts will get into fewer deals as entrepreneurs become more sophisticated and VC firms have more to invest?
4. Given Shanda’s performance, was the company well-priced? If usage had plateaued at 500,000 peak concurrent users, would you still think so (see Exh. 9)?
5. Why has the investment banker demanded that the offering price be cut? How far would you be willing to cut the offering price to complete the offering (see Exh. 11, 12)?

Homework
TEAM PRESENTATION ASSIGNMENTS on First Capital Holdings Corp.

FIRST CAPITAL HOLDINGS CORP.

Questions:
1. What should Carolyn Shepard recommend regarding the proposed investment in First Capital Holdings?
2. What risks would such an investment entail? What are the potential returns to such an investment?
3. In view of the recent events at First Executive, should Shepard reject the proposed investment in FCH as too risky? What is the likelihood that California regulators will also seize FCH’s California insurance subsidiary, FCLIC? Do you think this risk is any greater for FCLIC than for other insurers licensed to do business in California?
4. If you were the California State Insurance Commissioner, what evidence could you present to your constituents that would justify seizing FCLIC?
5. Should Shepard consider making a direct, control-oriented investment in FCH, possibly in partnership with Shearson Lehman Brothers?
6. How much confidence should Shepard have in FCH’s current management?

Class Fifteen: December 12

Topics
- Mergers and acquisitions
- Competitive advantage via scale economies and market share

Readings

Case Studies and Notes:
1. Hony, CIFA, and Zoomlion: Creating Value and Strategic Choices in a Dynamic Market, 9-811-032

Homework

TEAM PRESENTATION ASSIGNMENTS on HONY, CIFA and Zoomlion

HONY, CIFA and ZOOMLION

Objectives:
1. Overview of the Private Equity market in China
2. Study of structuring cross-border leveraged buyout transactions
3. Examine challenges associated with translating the private equity model in emerging markets
4. Illustrate the development of competitive strategies by private equity organizations

Questions:

China is one of the hottest markets for private equity financing today, and Chinese groups are looking to invest not only in China, but also in Europe.

1. What are the risks of pursuing the CIFA acquisition? What are the potential benefits?
2. How is investing in Zoomlion’s acquisition of CIFA different from investing in Zoomlion itself? Does this pose fewer or more risks for Hony?
3. What is the valuation of CIFA? Please use cash flows and cost of capital data from the case. You can assume that CIFA will grow at 5% per year through 2012 and 2% per year thereafter.
4. Another source of profits for Zoomlion is sales of its own products through CIFA’s distribution network. This might be assumed to begin in 2010 and grow at the same rate as CIFA’s sales. How significant will the after-tax profits from such sales need to be (if any) to justify a valuation of 500 million Euros?
5. How much do you believe Zoomlion should bid for CIFA, based on the answers above?
6. What is the estimated return on the CIFA deal for Hony? Assume that a) Hony will exit in 5 years; b) Hony will exercise the option at the time; c) CIFA’s entry trailing EV/EBITDA multiple was 10 and Zoomlion would be trading at an average EV/EBITDA multiple of 20 at time of exit.

Case Packet: Obtain the case packet from Harvard Business School Publishing via this link:
http://cb.hbsp.harvard.edu/cb/access/14474864

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There will be no credit for late assignments, missed assignments or failures to attend quizzes without written excuse from GMU administration. No makeups or extra credit will be accepted. Failure to turn in a written assignment or quiz will result in a 0 grade subject to the above “Grading” rules. Consult the GMU Catalog for additional guidance.

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You will not need to use your laptop or cellphone during the class. Their use is distracting to other students, so they are not permitted. In case of emergency please speak with me.

The use of a calculator will be necessary for quizzes—bring a calculator to class. Sharing will not be permitted.

Oral presentations by the teams are expected to use powerpoint slides—bring your presentation on a flash drive and supply a hard copy prior to the presentation.

Accommodations for Students with Disability
If you are a student with a disability and you need academic accommodations, please contact the Office of Disability Services (ODS) at 993-2474. All academic accommodations must be arranged through the ODS.

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greater academic and personal achievement, we, the student members of the University Community have set forth this: “Student members of the George Mason University community pledge not to cheat, plagiarize, steal, or lie in matters related to academic work.” See http://academicintegrity.gmu.edu/honorcode/

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