

Corporate Finance

1. Introduction

This Corporate Finance course explores issues that every manager needs to know regarding their companies, the investors that provide them with capital, and the interaction between them in capital markets.

2. Objectives

The ultimate goal of this course is to provide you with an analytical framework that will enable you to answer the questions posed below, many variations of them, and very different ones too. By the end of this course you should be able to assess the value of a bond; measure the risk and return of assets; estimate a cost of capital; evaluate investment projects; find the mix of debt and equity a company should have in its balance sheet; implement a reasonable dividend policy; determine whether a company is creating value; and assess the value of stocks.

3. Learning Outcomes

To illustrate some of the questions we will raise, and hopefully answer during the course, consider the following:

- ☞ How do investors assess the return of an asset? How do they assess its risk? Why do investors tend to diversify? We will address related issues in **Risk, Return, and Diversification**.
- ☞ What are credit ratings and how do they affect the return of a bond? Why does a 30-year bond typically have higher yield than a 1-year bill? We will address related issues in **Bonds**.
- ☞ Where does a company observe its cost of debt? How does it estimate its cost of equity? How does it determine its hurdle rate? We will address related issues in **The Cost of Capital**.
- ☞ How does a company separate 'good' projects from 'bad' projects? What is the role of sensitivity analysis in the evaluation of a project? We will address related issues in **Project Evaluation**.
- ☞ Why do airlines usually issue large amounts of debt but technology companies issue very little? How does a company come up with the right mix of debt and equity? We will address related issues in **Capital Structure**.
- ☞ Why do some companies like Amazon pay no dividends? Why do others like GE typically pay high and increasing dividends? We will address related issues in **Dividend Policy**.
- ☞ How does a company determine whether it is creating value? Should managers focus on shareholders or on stakeholders? We will explore related issues in **Corporate Value Creation**.
- ☞ What is a multiple such as the P/E ratio and how is it used in valuation? How is the DCF approach properly implemented to value a company? We will address related issues in **Stocks**.

4. Content

See a list of all the topics to be discussed during the course, and the required cases and readings for each session, in section 7.

5. Methodology

The course consists of a combination of cases and discussions. Before each session, you are expected to read the material indicated in the outline, prepare the assigned case, and often both. An excellent textbook that covers most of the topics discussed in the course is *Corporate Finance*, by Ross, Westerfield, and Jaffe.

6. Evaluation

The credit for the course is split in the following way:

☞ Open-book final exam:	75%
☞ Class participation:	25%

7. Outline

1. Overview

- Case: *Warren E. Buffett, 1995* (Prep sheet)
- Readings → N/A

2. Risk, Return, and Diversification

- Discussion
- Readings → 'The Essential Financial Toolkit – Tool 2' (After class)
- 'The Essential Financial Toolkit – Tool 3' (After class)
- 'The Essential Financial Toolkit – Tool 4' (After class)

3. Bonds I – Return and Default Risk

- Case: *Atlas Investment Management* (Prep sheet I)
- Readings → 'Bond Basics Tutorial'

4. Bonds II – Interest-Rate Risk and Duration

- Case: *Atlas Investment Management* (Prep sheet II)
- Readings → 'Bonds (III) – Duration and Convexity' (Excerpt)
- 'The Essential Financial Toolkit – Tool 10' (After class)

5. The Cost of Capital

- Case: *Boeing & the 777: The Cost of Capital and Project Evaluation* (Prep sheet I)
- Readings → 'The CAPM, the Cost of Capital, and Project Evaluation'

6. Project Evaluation

- Case: *Boeing & the 777: The Cost of Capital and Project Evaluation* (Prep sheet II)
- Readings → Same as for the previous session

(Continues)

7. Outline (Cont.)

7. Capital Structure I

- Case: *Tonka Corporation* (Prep sheet)
- Readings → 'The Modigliani-Miller Propositions: A Simple Example'

8. Capital Structure II

- Case: *Polaroid Corporation, 1996* (Prep sheet)
- Readings → 'Beta, Leverage, and the Cost of Capital'

9. Dividend Policy I

- Case: *Consolidated Edison Company* (Prep sheet)
- Readings → 'Dividend Policy'

10. Dividend Policy II

- Case: *Telefónica: The Dividend Decision* (Prep sheet)
- Readings → Same as for the previous session

11. Corporate Value Creation

- Discussion
- Readings → 'All About EVA'
→ 'Value Driven'

12. Stocks I – Multiples

- Case: *Hilton Hotels, Corp.* (Prep sheet)
- Readings → "P/E Ratio Tutorial"
→ 'The Essential Financial Toolkit – Tool 9' (*After class*)

13. Stocks II – Discounted Cash Flow

- Case: *Hertz & Dollar Thrifty* (Prep sheet)
- Readings → 'Stocks (II) – The WACC Model'

14. Assessment – Essential Takeaways

- Discussion
- Readings → N/A

8. Professor's Biography



Javier Estrada is a Professor of Finance at IESE Business School in Barcelona, Spain. He is also a partner and financial advisor at Sports Global Consulting Investments, a company that specializes in providing wealth management advice to professional athletes. Javier holds an M.S. in Finance and a Ph.D. in Economics from the University of Illinois at Urbana-Champaign (USA), and a B.A. in Economics from the National

University of La Plata (Buenos Aires, Argentina). His areas of specialization are wealth management, portfolio management, investments, and law & economics.

Javier held positions at both the Economics Department and the Finance Department at Carlos III University (Madrid, Spain). He is also a regular visiting professor at HANKEN (Helsinki, Finland), IPADE (Mexico City, Mexico), Torcuato Di Tella University (Buenos Aires, Argentina), and the University of Montevideo (Montevideo, Uruguay), and has lectured to executives, graduates, and undergraduates in many countries.

Javier is the author of *Finance in a Nutshell* (FT Prentice Hall, 2005), originally written in English and subsequently translated into Spanish, Italian, and Chinese; a second edition of this book was published in 2011, is entitled *The FT Guide to Understanding Finance*, and was translated into Korean. He is also the author of *The Essential Financial Toolkit – Everything You Always Wanted To Know About Finance But Were Afraid To Ask* (Palgrave Macmillan, 2011).

Javier has done extensive research in the areas of portfolio management, investment strategies, and risk with a special focus on downside risk. He has also done research on emerging markets and insider trading. His articles have appeared in the *Journal of Portfolio Management*, the *Journal of Investing*, the *Journal of Asset Management*, and the *Journal of Wealth Management*, among other journals. He was also the founding editor of the *Emerging Markets Review*, the leading journal on emerging markets; was editor of the journal between inception in 2000 and the end of 2006; and remains an associate editor. He is also in the advisory board of several other academic journals.

Javier is a member of the CFA Institute's Speaker Retainer Program; is Director of both the Senior Executive Program (SEP) that takes place between New York and Miami and the open-enrollment program on Managing Your Own Portfolio; and was a tennis instructor.