

UNIVERSITY OF FLORIDA
DEPARTMENT OF FINANCE
WARRINGTON COLLEGE OF BUSINESS ADMINISTRATION

Fin 5439 Section 2140

CAPITAL STRUCTURE AND RISK MANAGEMENT
Fall 2016

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This course, also known as Corporate Finance II or Fin 2, continues and expands the material presented in Corporate Finance I, FIN5437. It will primarily cover:

- (1) The cost of capital, capital structure (leverage), and the valuation of the firm.
- (2) Dividend policy and share repurchases.
- (3) The use of derivatives by corporations, including financial options, interest rate and currency swaps, and credit derivative swaps.

The goal of the course is to present a set of concepts for evaluating business decisions. Taken together, FIN5437 and FIN5439 are intended to provide students with a core set of financial concepts that should be known by all MBA students. These concepts will provide the background for graduate elective courses in finance and real estate, and should be useful throughout students' careers, whether they be in business, finance, journalism, government, or non-profit organizations.

Course materials:

1. Eugene F. Brigham and Michael Ehrhardt, *Financial Management*, 15th edition, 2011, ISBN: 978-1-305-63229-5. It is referenced below as "BE."
2. Articles to supplement the textbook. These will be available in the course packet for the class from Target Copy and on the course's e-learning site (Canvas). Most of them are also available electronically through UF's business library at <http://businesslibrary.uflib.ufl.edu>
3. Three cases, all included in the course packet: (1) *Midland Energy Resources, Inc.: Cost of Capital*, Harvard Business Publishing (June 19, 2009); (2) *Diageo plc*, Harvard Business School (August 6, 2003); and *Daktronics: Dividend Policy in 2010*, University of Denver (2012).

The PowerPoint slides for each lecture will be posted on the course's e-learning site (Sakai), along with supplemental articles and other course materials.

The cases: Each case will be presented by a team. The team will turn in their presentation slides after the case discussion; no separate case write-up is necessary. Those students not presenting the case will take a quiz on the case and get an individual grade. The quizzes and case presentations will be worth the same number of points.

In preparing the Diageo PLC case it would be helpful to look at Richard Passov, "How Much Cash Does Your Company Need?" *Harvard Business Review* (November 2003). It is available online through the UF business library and in the course packet for the course.

Students new to the case method may wish to consult *Note to the student: How to study and discuss cases*, Robert F. Bruner, University of Virginia Darden School Foundation (2001) available at <https://store.darden.virginia.edu> and in the course pack.

Grading:

Grades will be determined by the cases and case-related quizzes (15%), class participation (5%), a mid-term exam (30%), problem sets (5%), and a final exam (45%). The exams will be closed-book, with a one-page, single-sided "cheat sheet" of text (but no slide reproductions) allowed. Grading will be in accord with Graduate School policy: <http://www.registrar.ufl.edu>

The class participation grade will depend on a student's contribution to class discussions, especially those involving the cases. Presenting teams will be asked to rate each teammate's contributions to the cases.

Class attendance: Students are expected to attend all classes. Arrangements can be made to make up assignments and exams missed because of unforeseen events such as illnesses, accidents, or family emergencies provided the make-ups are arranged beforehand. Any make-up exams for the mid-term and the final will each be offered to students on a single date only. In-class problem sets missed without a make-up arranged beforehand will not be counted toward the final grade.

Students with disabilities will be accommodated. University policy is that such students must first register with the Dean of Students Office. The Dean of Students Office will provide documentation to the student who must then provide this documentation to the Instructor when requesting accommodation. <http://www.dso.ufl.edu/drc/>

Laptop policy:

Laptop computers may be open during class, but must be closed during exams and quizzes. Students overly absorbed in their lap tops during class, however, are unlikely to do well on the class participation part of the course grade.

Office hours:

Wednesday 3:00-5:00, in Stuzin 308. I am also available to meet before class, after class, during the class breaks, and by appointment. I also respond to e-mails, usually within 24 hours.

Final exam:

Thursday, December 15 from 11:45A to 1:40P, HGS240.

Lectures

1. Review of core concepts.

Review: BE Chapter 6, on risk, return and the CAPM, and Chapter 7, on stocks, stock valuation, and market equilibrium.

The Dow at 36,000? Read the debate between James K. Glassman of the American Enterprise Institute and Clive Crook of the *Economist* about which cash flows should be discounted when estimating the value of the stock market. Available on Sakai as *Crook and Glassman on The Stock Market*.

2. The cost of capital and value of the firm.

BE Chapter 9, on the cost of capital and Chapter 24, on portfolio theory, pp. 931-950.

Eugene F. Fama and Kenneth R. French, "The Capital Asset Pricing Model: Theory and Evidence," *Journal of Economic Perspectives*, Vol. 18, No. 3 (Summer 2004).

Michael Jacobs and Anil Shivdasani, "Do You Know Your Cost of Capital?" *Harvard Business Review* (July-August 2012).

Case I: Midland Energy

3. Choosing the firm's capital structure.

BE Chapters 15 and 26 (which is mostly Chapter 15 in more detail) on capital structure decisions.

Aswath Damodaran, "Valuing Young Growth Companies," *AAll Journal* (December 2011).

Merton H. Miller, "The Modigliani-Miller Propositions after Thirty Years," *Journal of Economic Perspectives*, Vol. 2, No.4 (Fall 1988), pp. 99-120.

Michael Jensen, "Agency Costs of Free Cash Flow, Corporate Finance, and takeovers," *American Economic Review*, Vol 76. No. 2 (May 1986).

If you wish to review some important institutional features of capital markets read some or all of BE chapters 20, 21, and 22. These chapters are meant to build up your practical knowledge. If you can follow the lectures and the cases, you are probably up to speed on these matters.

Case II: Diageo plc

4. Distributions to shareholders.

BE Chapter 14 Dividends and repurchases

Case III: Daktronics: Dividend Policy

5. Financial and real options.

BE Chapter 8 Financial options

BE Chapter 26 Real options

Aswath Damodaran, "The Promise of Real Options," *Journal of Applied Corporate Finance*, Vol. 13.2 (Summer 2000), pp. 29-44.

Many option value calculators are available on the Web. One can be found at:

<http://www.cboe.com>

6. Risk management and hedging.

BE Chapter 23 Derivatives and risk management