JOETTA FORSYTH

MBFE 655.62

FINANCIAL MANAGEMENT OF THE FIRM

SUMMER 2006

TUESDAYS

6:00PM – 10:00PM

WESTLAKE VILLAGE

SYLLABUS
Financial Management of the Firm  
MBFE 655.62  
SUMMER 2006  

Tuesdays 6:00pm – 10:00pm  
Westlake Village  

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Introduction  
Understanding financial principles is essential in the business world. Many of the activities of firms center around finance. How firms raise money, how they are valued, how they spend money, and their strategic decisions are all based on financial principles. Firms communicate using the language of finance. In addition, an understanding of financial principles is essential in order for individuals to successfully invest their own money in the complex environment of today.

Some of you may find this course challenging because of its emphasis on numbers. However, the mathematics of the course are not difficult and the rewards are great. Mastering the material will gain you entry into a whole new world of understanding business.

Course Description  
The major aspects of the financial functions of firms are covered. These include estimating the cost of capital of the firm, raising capital, allocating capital, and deciding the capital structure of the firm. Additional topics include the term structure of interest rates, options, and working capital decisions.

Students are expected to have read the material before class and are encouraged to speak during class. I will constantly ask questions to ensure that the students understand the material and to promote further understanding. I am also more than happy to make myself available outside of class for questions. I simply ask that students read the material before asking for additional help.

It is essential that you come prepared for class. Classes are four hours, and cover a great deal of material – much of it mathematical. Students who do not prepare for class by reading the assigned material will become lost and fall behind.

It is especially important that students thoroughly understand the time value of money. Most of the rest of the material is based on the time value of money. I recommend that students place special emphasis on understanding this material. The reward will be learning the rest of the material much more easily.
There will be a number of cases that will be discussed in class. You should prepare the questions listed, and should typically have a set of numbers or a spread sheet. Do not research the case on your own or collect your own information (which I will consider an ethics violation). I have no objections to students getting together into groups to prepare the cases. In fact, I encourage it although it is not required. I recommend that groups do not exceed five students. Any readings that are assigned with cases should be done first – these readings will provide a foundation for analyzing the case. There will be a group paper. These groups are different from any study groups that might form, and will consist of three students. The paper will be due at the end of the course, and the assignment will be handed out in class. *Note: students who form groups early and set aside a set time each week to study do much better on the exams.

I make my PowerPoint presentations available on the portal. Sample exams will also be posted, along with assignments and handouts. In addition, I expect the students to check the portal for announcements, and to check their campus email regularly. Please download the spreadsheet provided in the portal for Session 5A. You will be required to bring a laptop, or have one other person to share a laptop with.

Prerequisites: MBFE 652 or equivalent.

Course Objectives
Upon completion of the course, students will have a workable knowledge of the following topics:

1. Financial statement analysis
2. The use of financial ratios
3. The time value of money
4. How risk-free bonds are priced
5. The term structure of interest rates
6. Investment risk and return
7. Diversification
8. The Capital Asset Pricing Model
9. Stock valuation
10. Capital budgeting
11. Dividends
12. The Difference Between a Dividend and Stock Buyback
13. Capital structure
14. Working capital management
15. Business funding
16. The securities issuance process
17. Financial distress
18. Corporate governance
19. Budgeting cash flow and financing needs
20. Understanding how investing does or does not contribute to firm value
21. Relating investment to corporate strategy
22. Ethical issues in finance
23. Preliminary view of options and hedging
Texts and Course Materials

The textbook for the course is Ross, Westerfield, and Jaffe (RWJ), Corporate Finance, 7th ed. McGraw-Hill Irwin. There is also a required course packet that contains case materials and newspaper articles.

Students should have a financial calculator. It should perform present value, future value, NPV, IRR, and mortgage functions. The Hewlett Packard 10BII is a good (and inexpensive) one. I recommend using the 10BII even if you have a different financial calculator. The reason is that we will go over how to use the 10BII in class. If you do not have the same calculator you may not be able to figure out how to use your calculator and fall behind. The following is always a problem at the beginning: **Set the calculator to END, not BEG (under the MAR key) and set P/YR to 1 (under the PMT key). The default is 12.** A note is in order here. There are some financial calculations that cannot be solved easily by hand. This will happen rarely in the class, but there will be a couple of instances where this is true and a calculator will be needed. However, my past experience has been that some students may try to use their calculators as a crutch. Because of this, I will almost always expect students to write down the formulas that they use to get their answers. This is important because in presenting the formula, a student demonstrates that they understand the underpinnings of their calculations. There is little value in parroting how to get an answer by learning which buttons to press. In class, students will gain intuition for what the numbers mean. Students should learn how to use their calculators because once they are in the business world, their calculator will be a useful tool for speeding up calculations. A calculator will also come in handy during the exams. If the student has gotten the formula right, then the numeric solution that they derive should agree with the calculator. This can provide a handy double check.

We will begin each class with a discussion of the same day Wall Street Journal. I will have a subscription sheet available on the first day of class for those students who wish to subscribe. Students can subscribe at the student discount rate.

Grading

Your grade will be based on the following:

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<thead>
<tr>
<th></th>
<th>Points</th>
<th>%</th>
</tr>
</thead>
<tbody>
<tr>
<td>Participation</td>
<td>90</td>
<td>18</td>
</tr>
<tr>
<td>Paper</td>
<td>80</td>
<td>16</td>
</tr>
<tr>
<td>Midterm I</td>
<td>90</td>
<td>18</td>
</tr>
<tr>
<td>Midterm II</td>
<td>90</td>
<td>18</td>
</tr>
<tr>
<td>Final</td>
<td>150</td>
<td>30</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>500</strong></td>
<td><strong>100</strong></td>
</tr>
</tbody>
</table>

*Note: in order to receive a B- or higher, the weighted average grade on exams (the two midterms and the final) must be at least a B-.

You can expect problems and short essay questions on the exams. The midterms will last 1½ hours each (90 points – 90 minutes), and the final will be 2½ hours (150 points – 150 minutes). The number of points for each question on the exams will correspond to how much time I think that you should spend on each question. In other words, if a question has 10 points,
then my suggestion is that you spend ten minutes on the question. I do this in order to help students budget their time and decide how much detail to include. The exams are closed book. However, any equation that has a box around it on the PowerPoint slides will be provided in a formula sheet for the exam. I will post the formula sheet ahead of time on the portal, but will hand out a clean sheet for the exam. Some formulas will not be on the formula sheet and will have to be memorized. Most will be on the formula sheet.

I strongly encourage students to ask questions and participate in class. More specifically, the participation grade will be based on how a student contributes to the understanding of the entire class. There are two kinds of participation. One is where the student asks questions for their own benefit or to clear up their own confusion. I strongly encourage this kind of participation, although it is neutral to your participation grade. Your participation grade increases according to your contribution to the class. For instance, quality participation could include an insightful question that improves the understanding of other students or clears up a source of confusion for other students as well as yourself. Another example would be relating the material being presented to a business situation from your background in an insightful way. I place special emphasis on days when there are cases.

In addition, I will pay special attention to case discussions, and whether students are prepared. I may possibly collect the student’s notes on cases. *If I discover that a student has not prepared a case for class, they will receive an F in participation.

There are several strategies for those students who are not naturally inclined to speak in class. Students can use our Wall Street Journal discussions as a way of participating. Just pick an article ahead of time to bring up in class, along with some comments that you would like to make on the article. This way, you can reduce the discomfort level you feel at public speaking by avoiding having to spontaneously come up with something to say. Another possibility is to work with a group on a case, and put together an analysis for the case. This way, other members of the group can give you comments on your analysis before you bring it up in class. This will reduce the anxiety that your comment will not be well received.

**Attendance Policy**

Attendance will be part of your participation grade. If you cannot attend, please give or send me a note or email with an explanation, preferably in advance. I consider business reasons to be a legitimate excuse (aside from simply having a lot of work to do), along with family emergencies. If a student cannot attend an exam (for a very good reason) then their other exam scores will be proportionately weighted more. Students must attend the final or receive an incomplete in the course. If I am teaching another section at a different location, it may be possible for a student to take the exam at the other location. Students should consult with me about this possibility.

It will take a student about three classes of strong participation to make up for an unexcused absence from class. If a student shows up for all classes and does not say a word, they can expect a B- in participation. If a student misses more than two classes without an excuse and does not talk in class they can expect a C or less. Typically the average class grade in participation is a B+. 
Conduct

“The University expects from all of its students and employees the highest standard of moral and ethical behavior in harmony with its Christian philosophy and purposes. Engaging in or promoting conduct or lifestyles inconsistent with traditional Christian values is not acceptable.

The following regulations apply to any person, graduate or undergraduate, who is enrolled as a Pepperdine University student. These rules are not to be interpreted as all-inclusive as to situations in which discipline will be invoked. They are illustrative, and the University reserves the right to take disciplinary action in appropriate circumstances not set out in this catalog. It is understood that each student who enrolls at Pepperdine University will assume the responsibilities involved by adhering to the regulations of the University. Students are expected to respect order, morality, personal honor, and the rights and property of others at all times. Examples of improper conduct for which students are subject to discipline are as follows:

- Dishonesty in any form, including plagiarism, illegal copying of software, and knowingly furnishing false information to the University.
- Forgery, alteration, or misuse of University documents, records, or identification.
- Failure to comply with written or verbal directives of duly authorized University officials who are acting in the performance of assigned duties.
- Interference with the academic or administrative process of the University or any of the approved activities.
- Otherwise unprotected behavior that disrupts the classroom environment.
- Theft or damage to property.
- Violation of civil or criminal codes of local, state, or federal governments.
- Unauthorized use of or entry into University facilities.
- Violation of any stated policies or regulations governing student relationships to the University.

Disciplinary action may involve, but is not limited to, one or a combination of the alternatives listed below:

Dismissal – separation of the student from the University on a permanent basis.
Suspension – separation of the student from the University for a specified length of time.
Probation – status of the student indicating that the relationship with the University is tenuous and that the student’s records will be reviewed periodically to determine suitability to remain enrolled. Specific limitations to and restrictions of the student’s privileges may accompany probation.”

GSBM Catalog, pgs. 195-196.

Policy on Disabilities

Assistance for Students with Disabilities

“Students with disabilities, whether mental or physical, are encouraged to contact the Equal Opportunity Office before the academic year begins or soon after classes are in session. This office will assist each student by providing general information about campus facilities and available resources. The office will assist in providing reasonable accommodation to students with disabilities pursuant to applicable laws. Inquiries should be directed to equal opportunity officer, Lauren Breeding, (310) 506-6500. (Students who wish to file a formal grievance should refer to the “Nondiscrimination Policy,” which is listed in the “Legal Notices” section of this catalog.)”

GSBM Catalog, pg. 35.
<table>
<thead>
<tr>
<th>Date</th>
<th>Session</th>
<th>Topic</th>
<th>Readings</th>
</tr>
</thead>
<tbody>
<tr>
<td>May 2</td>
<td>1</td>
<td>Introduction &amp; Financial Statements</td>
<td>Ch. 1, Ch.2 including appendix, +Ch.3</td>
</tr>
<tr>
<td>9</td>
<td>2</td>
<td>Time Value of Money</td>
<td>Ch. 4</td>
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<tr>
<td>16</td>
<td>3A</td>
<td>Time Value of Money (continued)</td>
<td>Packet pg. 1 (Download Amt. Schedule)</td>
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<td></td>
<td>3B</td>
<td>Discuss paper topic</td>
<td>Pg.s 447-450</td>
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<tr>
<td></td>
<td></td>
<td>Case: Clarkson Lumber Company</td>
<td>Packet: Clarkson Lumber + Questions</td>
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<tr>
<td>23</td>
<td>4A</td>
<td>Bond Pricing and the Term Structure of Interest Rates</td>
<td>Ch. 5.0 – 5.3 + appendix</td>
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<td>4B</td>
<td>Capital Budgeting</td>
<td>Ch. 6,7</td>
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<tr>
<td>30</td>
<td>5A</td>
<td>Capital Budgeting (continued, bring laptops)</td>
<td>(Download Spreadsheets)</td>
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<td></td>
<td>5B</td>
<td>Introduction to Risk and Reward</td>
<td>Ch. 9, 10.0 - 10.5</td>
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<tr>
<td>June 6</td>
<td>6A</td>
<td>The Capital Asset Pricing Model (CAPM)</td>
<td>Ch. 10.6 – 10.10 + appendix</td>
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<td>6B</td>
<td>The Pricing of Stock</td>
<td>Ch. 5.4-5.10</td>
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<tr>
<td>13</td>
<td>7A</td>
<td>Midterm I (Through Session 5A)</td>
<td>Ch. 12, including pgs. 343-345</td>
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<td></td>
<td>7B</td>
<td>The Cost of Capital</td>
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<td>20</td>
<td>8A</td>
<td>Capital Structure</td>
<td>Ch. 15, 16</td>
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<td>8B</td>
<td>APV, Leveraged Firms, and Comparables</td>
<td>Ch. 17, Packet: Using APV</td>
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<td>27</td>
<td>9A</td>
<td>Case: Hospital Corporation of America</td>
<td>Packet: HCA + Questions</td>
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<td></td>
<td>9B</td>
<td>Consolidation Session</td>
<td>Handout</td>
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<tr>
<td>July *5</td>
<td>10A</td>
<td>Dividend Policy, The Market for Lemons, and The Pecking Order</td>
<td>Ch 13, 18</td>
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<tr>
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<td>10B</td>
<td>Long-term Financing &amp; M&amp;A</td>
<td>Ch. 19, 20, 29, 30</td>
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<tr>
<td>11</td>
<td>11A</td>
<td>Midterm II (Through Session 9B)</td>
<td>Packet: Dividend Policy at FPL + Questions</td>
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<tr>
<td></td>
<td>11B</td>
<td>Case: Dividend Policy at FPL</td>
<td></td>
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<td>18</td>
<td>12A</td>
<td>Case: O.M. Scott</td>
<td>Packet: O.M. Scott + Questions</td>
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<tr>
<td></td>
<td>12B</td>
<td>Cash Management and Credit Management</td>
<td>Ch. 27,28</td>
</tr>
<tr>
<td>25</td>
<td>13</td>
<td>Introduction to Options, Warrants, and Convertibles</td>
<td>Ch. 22 + pg.s 655-659, Packet pg. 75</td>
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<tr>
<td>Aug. 1</td>
<td>14</td>
<td>Final</td>
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*Rescheduled