

VANDERBILT UNIVERSITY
OWEN GRADUATE SCHOOL OF MANAGEMENT

MGT 432b
Prof. Craig Lewis
Mod II
Fall 2000

CORPORATE FINANCIAL POLICY

Course Objectives

This course further develops analytical tools used in corporate finance and is intended to enhance ones confidence, skill and sophistication in applying these tools to more realistic case study problems. Current theoretical developments and empirical findings are also covered. The case study assignments should improve ones effective use of accounting and other economic data for asset valuation and optimal corporate finance decisions.

The course consists of approximately equal numbers of lectures and cases. Lectures will cover corporate governance, raising debt and equity capital, dividend policy, capital structure policy, bankruptcy and reorganization, managerial incentives, and managerial compensation. Cases are integrated throughout the course to reinforce and clarify major topics.

Case Presentations

You need to form a case group of five students, where at least one member is not a finance concentrator and at least one student is not US educated. Each group will act as management consultants and will formerly present one case and be prepared to critique any of the remaining case presentations. The consultants will have 15 minutes to present their case analysis. The presentation should include an outline of the main issues, additional assumptions and data needed to arrive at conclusions, and specific recommendations supported by a thorough analysis. This should be formalized in a typed report of at most 6 pages (excluding cover sheet, tables, and figures) prepared for distribution to the class (one for each case group) and to me by 4:30 P.M. on the day prior to the scheduled presentation. Most cases will involve two case groups independently presenting solutions to the class.

At the beginning of class a second case group will be randomly selected to spend ten minutes following the consultant's presentation critiquing their analysis and recommendations and offering an alternative analysis. Other class members will have an opportunity to make substantive comments over the following 30 to 40 minutes. I will attempt to bring some clarity to the problem and to suggest alternative solutions in the last 15 minutes.

All students should come to class prepared to discuss the case being presented, the assigned readings, and any relevant lecture material. Each student not in the consulting group is to turn in a two-page memo summarizing the case at the start of class. If a student is not prepared to participate, he/she should alert me prior to class. After a case group's consulting report is

submitted and again at the end of the semester, each member of the group is to independently grade the intellectual contributions of each member of his/her case group.

Paper Requirement

Each group will be required to write a paper that reviews the academic readings associated with the case you present to the class. This should be formalized in a typed report of at most 6 pages. It should be comprised of two sections. The first will be an intuitive discussion of the authors' findings. The second will be a discussion of the relevant managerial applications. Due date is December 11, 2000.

Honor Code

First, some cases and problem sets in this course have been used before at Owen. Do not consult with students who have used these cases or use their notes, or other materials they developed in analyzing these cases. Second, evaluations and critiques found in books or articles from the business press concerning the corporate actions described in these cases are not to be used in your case preparation. However, public information available prior to the decision point in the case can be used. I will treat the use of any prohibited information source as a violation of the Owen Honor Code.

Grading

Class Participation	20%
Case Presentation/ Analysis	20%
Course Paper and Written Reports	20%
Final Exam	40%

Course Prerequisite: MGT 331, 432a

Required Texts

Grinblatt, R. and S. Titman, Financial Markets and Corporate Strategy, Irwin McGraw Hill, 1998.

Recommended Texts

Brealey, R. and S. Myers. Principles of Corporate Finance, 5th ed., McGraw Hill, 1996.

Chew, D., The New Corporate Finance: Where Theory Meets Practice, McGraw Hill, 1993.

Course Outline

I. Corporate Governance: Shareholders, The Board of Directors, and the CEO (1 lecture)

Grinblatt, R. and S. Titman, 1998, Chapter 17.

Bhide, A. "Efficient Markets, Deficient Governance," *Harvard Business Review* (Nov-Dec 1994), 129-139.

Jensen, M., "Agency Costs of Free Cash Flow, Corporate Finance and Takeovers." *American Economic Review*, May 1996, 323-329

Rosenstein, S. and J.G. Wyatt. "Inside Directors, Board Effectiveness, and Shareholder Wealth" *Journal of Financial Economics*, v. 44, 229-250.

Jensen, M. and W. Meckling. "Theory of the Firm: Managerial Behavior, Agency Costs, and Ownership Structure," *Journal of Financial Economics*, v 3, 305-343 (only).

Kaplan, S. "Corporate Governance and Corporate Performance: A Comparison of Japan, Germany and the U.S., *Journal of Applied Corporate Finance* (Winter 1997), 86-93.

Smale, J.G., A.J. Patricof, D. Henderson, B. Marcus, D.W. Johnson, "Redraw the Line Between the Board and the CEO," *Harvard Business Review* (March-April 1995), 5-12.

Vefreas, N., "Board Meeting Frequency and Firm Performance" *Journal of Financial Economics*, 1999, 113-141.

Lecture notes for [download](#).

II. Managerial Compensation and Corporate Decision Making (1 lecture & 1 case)

Grinblatt, R. and S. Titman, 1998, Chapter 17.

Harvard Business School, "Compensation Incentives in High-Potential Ventures," 9-392-035

Core, J. R.W. Holthausen, D. F. Larcker, "Corporate Governance, Chief Executive Officer Compensation, and Firm Performance," *Journal of Financial Economics*, 1999, pages 371-406.

Gordon, J., "Employees Stock Ownership in Economic Transitions: The Case of United Airlines," *Journal of Applied Corporate Finance* (Winter 1998), pp. 39-62.

Hogan, C. and C. Lewis, "The Long-Run Performance of Firms Adopting Economic Profit Plans," 2000, unpublished Vanderbilt University working paper.

Jensen, M. "The Eclipse of the Public Corporation," *Harvard Business Review* (Sept-Oct 1989), pp. 61-74.

Jensen, M. and K. Murphy, "CEO Incentives: It's Not How Much You Pay Them, But How," *Journal of Applied Corporate Finance* (Fall 1990), pp. 36-49.

Lehn, K. and A.K. Makhija, "EVA, Accounting Profits, and CEO Turnover: An Empirical Examination 1985 – 1994," *Journal of Applied Corporate Finance* (Summer 1997), pp. 90-97.

Zimmerman, "EVA and Divisional Performance Measurement: Capturing Synergies and Other Issues," *Journal of Applied Corporate Finance* (Summer 1997), pp. 98-109.

Stewart, G.B., "EVA: Fact or Fantasy," *Journal of Applied Corporate Finance* (Summer 1994), pp. 72-84.

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CASE: Duckworth Industries, Inc. - Incentive Compensation Programs, Case questions for [download](#).

III. Debt Contracts and Financing (2 lectures and 1 case)

Grinblatt, R. and S. Titman, 1998, Chapter 1, 2.

Harvard Business School, "Note on Bank Loans," 9-291-026

Brennan, M. and E. Schwartz, "The Case for Convertibles," in *The New Corporate Finance Where Theory Meets Practice*, ed. by J. Stern and D. Chew, (Blackwell 1992), 217-229.

Datta, S., M. Iskandar-Datta, and A. Patel, "Some Evidence on the Uniqueness of Initial Public Debt Offerings," *Journal of Finance*, 2000, pages 715-743

Lummer, S. and J. McConnell, "Further Evidence on the Bank Lending Process and the Capital Market Response to Bank Loan Agreements," *Journal of Financial Economics*, 1989, pages 99-122.

James, C., "Some Evidence on the Uniqueness of Bank Loans," *Journal of Financial Economics*, 1987, pages 217-235.

Mikkelson, W. and M. Partch, "Valuation of Security Offerings and the Issuance Process," *Journal of Financial Economics*, 1986, pages 31-60.

Spies D. K. and J. Affleck-Graves, "The Long-Run Performance of Stock returns Following Debt Offerings," *Journal of Financial Economics*, 1999, pages 45-74.

Lecture notes for [download](#).

CASE: Metromedia Broadcasting Corporation, case questions for [download](#).

Guest Lecturer. Michael Lalor – Laylor, Bynum and Associates (Friday, November 10)

IV. Equity Financing (1 lecture & 1 case)

Grinblatt, R. and S. Titman, 1998, Chapter 3.

Benveniste, L. and W.J. Wilhelm, Jr., "Initial Public Offerings: Going by the Book," *Journal of Applied Corporate Finance* (Spring 1997), pp. 98-108.

Chen, H. and J. Ritter, "The Seven Percent Solution," *Journal of Finance*, 2000, pages 1105-1132.

Ellis, K. and R. Michaely, and M. O'Hara, "When the Underwriter is the Market Maker: An Examination of Trading in the IPO Aftermarket," *Journal of Finance*, 2000, pages 1039-1074.

Ibbotson, R.G. and J. Ritter, "Initial Public Offerings," in *Handbook in Finance*, ed. Jarrow, R., V. Maksimovic, and B. Ziemba, (North Holland 1995), pp. 993-1016.

Eckbo, B.E. and R.M. Masulis, "Seasoned Equity Offerings: A Survey," in *Handbook in Finance*, ed. Jarrow, R., V. Maksimovic, and B. Ziemba, (North Holland 1995), pp. 1017-1072.

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CASE: Amazon.com: Going Public, case questions for [download](#).

V. The Capital Management Process: Capital Acquisition and Security Choice (1 lecture and 1 case)

Grinblatt, R. and S. Titman, 1998, Chapter 13.

Brealey and Myers. 1996, Chapters 17, 18, and 19.

Opler, T. and S. Titman, "Designing Capital Structure to Create Shareholder Value," *Journal of Applied Corporate Finance* (Spring 1997), pp. 21-32.

Bank of America Roundtable On The Link Between Capital Structure and Shareholder Value," *Journal of Applied Corporate Finance* (Summer 1997), pp. 40-67.

"Vanderbilt University Roundtable on the Capital Structure Puzzle," *Journal of Applied Corporate Finance* (Spring 1998), 8-24.

Jung, K., Y. Kim, and R.M. Stulz, "Timing, Investment Opportunities, Managerial Discretion, and the Security Issue Decision," *Journal of Financial Economics*, v42 (1996), pp. 159-185.

Lewis, C.M., R.J. Rogalski, and J.S. Seward, "Understanding the Design of Convertible Debt," *Journal of Applied Corporate Finance* (Spring 1998), pp. 45-53.

Parrino, R. and M. Weisbach, "Measuring Investment Distortions Arising from Stockholder-Bondholder Conflicts," *Journal of Financial Economics*, 1999, pages 3-42.

Lecture notes for [download](#).

CASE: MCI Communications, case questions for [download](#).

VI. The Capital Management Process: Cash Dividends and Stock Repurchases: Taxes and Agency (1 lecture and 1 case)

Grinblatt, R. and S. Titman, 1998, Chapter 14.

Bartov, E., "Some Evidence on How Companies Choose Between Dividends and Share Repurchases," *Journal of Applied Corporate Finance* (Spring 1998), pp. 89-96.

LaPorta, R., F. Lopez-Di_Silanes, A. Schleifer, and R. Vishny, "Agency Problems and Dividend Policies around the World," *Journal of Finance*, 2000, pages 1-34.

Lie, E.. and J. McConnell, "Earnings Signals in Fixed-Price and Dutch Auction Self-Tender Offers," *Journal of Financial Economics*, 1998, pages 161-186.

Nohel, T. and V. Tarhan, "Share Repurchases and Firm Performance: New Evidence on the Agency Costs of Free Cash Flow," *Journal of Financial Economics*, 1998, pages 99-12187-222.

Stephans, E. and M. Weisbach, "Actual Share Requisitions in Open-Market Repurchase Programs," *Journal of Finance*, 1998, pages 313-333.

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CASE: Intel Corporation, case questions for [download](#).

VII. The Information Management Process: The Information Conveyed by Financial Decisions (1 lecture and 1 case)

Grinblatt, R. and S. Titman, 1998, Chapter 18.

Bernard, V. L., J. K. Thomas, and J. S. Abarbanell. "How Sophisticated Is the Market in Interpreting Earnings News?" *Journal of Applied Corporate Finance* (Summer 1993), pp. 54-63.

Dann, L.Y. and W.H. Mikkelson, Convertible Debt Issuance, Capital Structure Change and Financing Related Information: Some New Evidence,” *Journal of Financial Economics*, v 13 (1984), pp. 157-186.

Healey, P.M. and K. Palepu, Earnings Information Conveyed by Dividend Initiation and Omissions,” *Journal of Financial Economics*, v 21 (1988), pp. 149-175.

Rendleman, R., P. Jones, and A. Latane. “Empirical Anomalies Based on Unexpected Earnings and the Importance of Risk Adjustments,” *Journal of Financial Economics*, v 10, 269-288.

Yermack, D., “Good Timing: CEO Stock Option Awards and Company News Announcements,” *Journal of Finance*, v 52 (June 1997), pp. 449-476.

Schwert, G.W., “Markup Pricing in Mergers and Acquisitions,” *Journal of Financial Economics*, v 41 (June 1996), pp. 153-192

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CASE: Mebel, Doran & Company, case questions for [download](#).

Cases to be Covered

<u>Topic</u>	<u>Case</u>
Executive Compensation:	Duckworth Industries, Inc. (10/30)
Debt Contracts:	Metromedia (11/6)
Equity Financing:	Amazon.com (11/13)
Security Choice:	MCI Communications (11/27)
Dividend Policy:	Intel Corporation (12/4)
Information Management:	Mebel, Doran & Company (12/11)