Master of Business Administration

BADM 7090 – Financial Management
Spring Semester 2002

Day: Monday/Wednesday    Location: 1116 CEBA    Time: 1:30-3:00; 3:00-4:30
Professor: Chip Ryan           Office: 2168 CEBA
Phone:   (225) 578-6258       e-mail: cryan@lsu.edu     Fax: (225) 578-6366
Mailing Address: 2163 CEBA, Louisiana State University, Baton Rouge, LA 70803
Personal Web Site: http://www.bus.lsu.edu/academics/finance/faculty/cryan/
Course Web Site: http://blackboard.lsu.edu

Office Hours: Monday and Wednesday 10:00 – 12:00 or by appointment. No office hours on January 30.

Course Objectives: The overall objective of this course is to build the theoretical understanding and the application skill sets required to formulate financial policy toward capital investment and valuation decisions in a dynamic and global business environment. The impact of legal, social, technological, and ethical considerations on efficient economic outcomes is stressed. Effective written and oral communication skills necessary to communicate and implement financial policy will be developed. Upon successful completion of this course, students will be able to apply finance principles to firm analysis, stock pricing, bond valuation, the valuation of the firm, and the capital investment decision. Students will also be able to apply risk-return principles to the estimation of a firm’s cost of capital, portfolio risk, and capital pricing applications. Students will become familiar with many of the extant models that are used in financial applications today including the Net Present Value rule, the Capital Asset Pricing model, the Arbitrage Pricing theory, the Constant Growth Model, and the Free Cash Flow model.

Required: Principles of Corporate Finance, 6th edition by Richard A. Brealey and Stewart C. Myers (BM)*
Darden Cases (available at LSU Bookstore)
Atlantic Southeast Airlines
Empirical Chemicals, Ltd. A &B (a two-part case we will treat as one case)
Financial calculator capable of computing NPV & IRR (I recommend Hewlett Packard)

Learning Methodology: We will use an objective-based active learning approach. Research has shown that people learn more effectively when they 1) clearly identify their objectives and 2) actively participate in the learning process. Each lecture will begin with a statement of learning objectives. These learning objectives provide a road map to success -- they identify what is most important! We will reinforce these objectives with lectures, discussions, problem solving, review questions, and in-class exercises. Students should stay abreast of current event in business and finance since we will often use relevant events as a basis for class discussion and illustration. If you are not already a reader, students are encouraged to read the Wall Street Journal on a daily basis.

Evaluation: Midterm Exam (Mar 13) 20%
Final Exam (TBA) 20%
Atlantic Southeast Airlines – team effort (Feb 25) 20%
Empirical Chemicals A&B Case team effort (March 20) 20%
Problem Sets (Feb 18, April 8) 10%
Class/Case Participation 10%
You may submit take-home assignments via the mail, fax, or as an attachment to an e-mail if there is a professional conflict. Clear conflicts with a scheduled examination before the examination date.

<table>
<thead>
<tr>
<th>Grading: Grades:</th>
<th>&gt; 90%</th>
<th>A</th>
<th>80-90</th>
<th>B</th>
<th>65 - 80</th>
<th>C</th>
<th>&lt; 65%</th>
<th>F</th>
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<tr>
<td>I do not &quot;curve&quot; grades, but I will assign a heavier weight to a student’s final exam if it is higher than the midterm exam (30% weight on the final and 10% on the midterm).</td>
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| Exams: | There will be two in-class examinations, a midterm examination and the final examination. Examinations are closed book/closed notes. The final examination will be cumulative. |

| Cases: | We will analyze two cases, one on financial statement analysis (Atlantic Southeast Airlines) and another on capital investment decision-making (Empirical Chemicals, Ltd., A&B). Students must analyze these cases in teams of 4-6 students. Each team will turn in one case report for the entire team. We will discuss the cases in class and your classroom contributions will be factored into your individual participation grade. You may not use teaching notes or old case reports from other students |

| Teams: | You will form teams to analyze the cases. I will give you the opportunity to form your own teams, but reserve the right to assign members if necessary to place everyone on a team. Though not required, you are encouraged to use your team as a study group in addition to the required case activities. To mitigate “free rider” problems, I require each team member to assign everyone on his or her team a % of the grade that the member deserves. For each team member, I will eliminate the high and low % and average the remaining evaluations. The team member will then receive the team grade multiplied by the average percentage. For example, suppose Joe is a member of the Nutria Team and his evaluations are 100%, 100%, 90%, 85%, and 80%. I will drop one 100% and the 80% and average the 100%, 90%, and 85%, which comes to 91.67%. Suppose that the Nutria’s team grade is 95. Joe will receive a grade of 95*0.9167 = 87. In extreme cases, a team may vote a member off their team for lack of contribution. This requires that all other team members must vote the person off the team and present me with a written explanation of why the person is voted out. If I accept the explanation, the exiled member must convince another team to accept him or her on their team or complete the assignment by themselves. If this does happen (and I hope it does not), the solo assignment will receive a letter grade penalty. |

| Problem Sets: | There will be two problem sets to reinforce fundamental skills, primarily valuation mechanics and risk-return models. Additional problems at the end of the chapter are recommended for practice. Solutions to the end-of-chapter problems are posted on the blackboard web site. Students may work together on problem sets, but each student is responsible for doing his or her own work and turning in an individual assignment. It is not acceptable to copy another student’s problem set. |

| Participation: | Quality participation improves the learning experience for the individual student as well as for his or her classmates. Participation includes class discussion, in-class learning exercises, attendance, promptness, and professional behavior. Participation will be evaluated for merit and for frequency. Students that make positive contributions to class discussions, attend regularly, arrive to class on time, and exhibit professional behavior will be rewarded. Students that miss class, engage in disruptive behavior during class, work on assignments for other courses in class, or make low quality contributions will be penalized. It is not acceptable to skip class to study for an examination in another course. |

| Financial Calculator: | Students are required to have a financial calculator that is capable of accepting uneven cash flows and calculating NPV and IRR (look for these two functions). I recommend Hewlett Packard, but products by Texas Instrument and Sharp (perhaps among others) will also work. Acceptable calculators include the HP 10B, the HP 17B II, the HP 19B, the TI Business Analyst II Plus, or the Sharp EL 733A. One can generally purchase an acceptable calculator for approximately $35-$45. The TI Business Analyst and the TI BA 35 are not acceptable. It is the student’s responsibility to learn how to use his or her own calculator. Read the manual that comes with your calculator! I will offer some pointers in class and in my posted materials, but they may or may not be specific to your calculator. Bring your calculator to all classes. Students may not share calculators on examinations. |

| Lecture Notes: | Lecture notes, calculator instructions, review materials, and additional examples are downloadable from the class web site, http://blackboard.lsu.edu. You can also purchase a bound set of lecture notes at
Serve-U-Center at 4410 Highland Road (768-7742), next to CC’s Coffee House outside the South Gates of LSU. I recommend that you purchase a bound copy of the notes.

Academic Honesty:
Cheating will not be tolerated. Cheating is defined to be copying the work of others, the use of “cheat sheets” on exams, or attempting in any way to present the work of others as your own. Anyone caught cheating will be subject to penalties as prescribed by the University policy.

Professional MBA students preparing for their careers should pay special attention to acting, dressing, and preparing their assignments in ways that conform to professional expectations. What does this mean? Basically, it means that you should act and dress like a professional businessperson (and all business people are not professional). Although there is no one correct definition of professional behavior and appearance, I list a few guidelines below that are generally accepted across most professional fields. If you follow these guidelines, you will go a long way toward achieving professionalism and building a professional image. I expect that you will conform to these guidelines in this class. You should expect the same from yourself and from your classmates.

1) Be where you are supposed to be when you are supposed to be there. Be on time for class. Be on time for team meetings.

2) Dress appropriately. Depending on your firm, this could range from extremely casual to very formal. For this class and for the Flores Full-time MBA program, appropriate dress is defined to be business casual. Roughly, this means no jeans, no shorts, no baseball caps, no t-shirt (there are exceptions such as silk dress t-shirts for women), no sneakers, etc.

3) Make sure that you do high quality work and that you present it in a format that is readable and easy to follow. Anything else wastes people’s time (see the next point).

4) Don’t waste other people’s time. Be prepared for your team meetings. Be prepared if you come to see me for assistance. Be prepared for class. Time is one of our most valuable assets.

5) Participate in class (or in your team activities) in a way that raises the quality of the class (team) and benefits others. Students often have insights that elevate those around them to a higher level of understanding and performance. Businesses define this attribute as leadership. For the successful businessperson, it is not an option, it is expected.

6) Respect other people’s opinion and be considerate. You can and should disagree with someone when you think his or her opinion is not correct, but never belittle others. Nobody likes a jerk.
### COURSE SCHEDULE

<table>
<thead>
<tr>
<th>Week</th>
<th>TOPIC</th>
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<tr>
<td>Jan 23</td>
<td>CLASS ORGANIZATION</td>
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<tr>
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<td>We will discuss the class format, learning methods, and expectations.</td>
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<td>Jan 28</td>
<td>INTRODUCTION TO FINANCE AND VALUE</td>
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<tr>
<td></td>
<td>Introduces the theory of financial value as a motivation for the study of finance. Specific topics include the concept of opportunity cost, an introduction to Present Value, and the concept of separation of the investment and financing decision.</td>
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<td>Read: BM Chapters 1 &amp; 2 (section 2.2 is optional).</td>
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<td><strong>Turn in a copy of your resume. Please attach a picture (e.g., your MBA picture)</strong></td>
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<td>Jan 30/</td>
<td>ANALYZING FINANCIAL PERFORMANCE &amp; FINANCIAL FORECASTING</td>
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<td>Feb 4</td>
<td>Cash flow analysis, ratio analysis, common size statements and financial forecasting are introduced as techniques for gaining insight into a firm’s financial performance. Although this topic covers a wide range of financial performance metrics, emphasis is placed on the analysis of working capital and sustainable growth.</td>
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<td>Read: Lecture notes (very important); BM Chapter 28 &amp; 29</td>
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<td>Feb 5</td>
<td>College of Business Career Reception, 5:00 -8:00, Lod Cook Alumni Center</td>
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<td>Feb 6</td>
<td>Career Day, 9:00 - 2:30, Pete Maravich Assembly Center</td>
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<td>Feb 6/13</td>
<td>VALUATION MECHANICS AND BOND VALUATION</td>
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<td>The mathematical and mechanical skills necessary to make value based decisions are developed. Specific topics include the calculation of present value, future value, net present value, and bond prices. This session stresses both mathematical and financial calculator approaches.</td>
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<td>Read: BM Chapter 3</td>
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<td>Suggested Practice Questions: 1-32 (use math &amp; a calculator)</td>
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<td><strong>Valuation mechanics problem set is distributed on February 6</strong></td>
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<td>Feb 11/12</td>
<td>Mardi Gras Holiday</td>
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<td>Feb 18/20</td>
<td>STOCK AND FIRM VALUATION</td>
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<td>This session covers the theory and application of stock and firm valuation. The perpetuity model, the constant growth model, and the free cash flow model are covered. Ties are established between common rules of thumb such as the P/E ratio and financial valuation theory.</td>
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<td>Read: BM Chapter 4</td>
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Valuation mechanics problem set is due on February 18

Feb 25  Atlantic Southeast Case is due – Class Discussion

Feb 27/ CAPITAL INVESTMENT DECISION CRITERIA

Mar 4  Decision criteria leading to the efficient investment in real assets are developed. Alternative decision criteria such as Payback, Accounting Rate of Return, and the Internal Rate of Return method are compared with the value-based Positive Net Present Value Criteria. Applying financial decision criteria to the practical problem of capital rationing is also discussed.

Read: BM Chapter 5  Suggested Practice Questions: 1-12.

Mar 6/11 CAPITAL BUDGETING

This session builds practical skills in applying the Net Present Value criterion to capital budgeting investment decisions. Students will learn how to estimate incremental cash flows from pro forma accounting projections. Topics include sunk costs, externalities, and the relevance of cash flows.


Mar 13  Midterm Examination

Mar 18/20 INTRODUCTION TO RISK AND RETURN

Risk, return, and the relationship to the firm’s opportunity cost of capital are introduced. A theoretical framework is developed from both an intuitive and a statistical approach. The statistical measures of variance, standard deviation, and coefficient of variation are presented as quantifiable measures of risk. The impact of diversification on portfolio risk and appropriate risk measurement techniques for portfolios are developed. Finally, the concept of Beta as a measure of market risk is introduced.

Read: BM Chapter 7  Suggested Practice Questions: 1-21.

Risk-return problem set is distributed on March 18

March 25/27  EFFICIENT PORTFOLIO AND MARKET PRICING THEORY

This lecture exposes students to the concept of portfolio theory and efficient portfolios. Basic risk-return relationships are explored leading to the introduction of extant capital pricing models. Specifically, we will discuss the Capital Asset Pricing Model (CAPM) and the Arbitrage Pricing Theory (APT). Empirical evidence on the validity of these models will be presented.

Read: BM Chapter 8  Suggested Practice Questions: 1-17.
April 8 OTHER ISSUES IN CAPITAL BUDGETING

This lecture combines risk analysis and capital investment criteria to develop tools useful for advanced capital budgeting decision analysis. Topics include multi-divisional capital budgeting, the interaction of capital structure and the cost of capital, and estimating the firm’s cost of capital. We will conclude our treatment of capital budgeting by discussing decision tree analysis and Monte Carlo simulation.

Read: BM Chapter 9 (9.5 optional)  Suggested Practice Questions: 1-9
Read: BM Chapter 10&11  Suggested Practice Questions: 1-9
Read: BM Chapter 19 section 1  Suggested Practice Questions: 1-4

RISK-RETURN PROBLEM SET IS DUE ON APRIL 8.

April 10 MAKING SURE MANAGERS MAXIMIZE NPV

This topic will review the capital investment process as it is influenced by agency and information problems. Specific attention will be given to value-based management techniques including EVA®, stock-based compensation, and the use of stock options in compensation schemes.

Read: BM Chapter 12

April 15 FINANCING DECISIONS AND MARKET EFFICIENCY

We will discuss corporate financing decisions in an efficient capital market. Topics include the three forms of market efficiency, empirical evidence, and the six lessons of market efficiency. We will also explore implications for decision-making when conditions deviate from ideal markets.

Read: BM Chapter 13

FINAL DATE TO DROP WITH A GRADE OF ‘W’

April 17 Empirical Chemicals Case is due – Class Discussion

April 22/24 CORPORATE FINANCING AND ISSUING SECURITIES

This session describes the financing choices facing the firm and how a publicly held corporation issues securities. Students will understand the differences between common stock, preferred stock, debt, convertible securities, and derivative securities. A general description of the investment banking process, including the steps required to issue new securities, is included. We conclude with a discussion of initial public offerings and the well documented ‘underpricing’ (or ‘first-day pop’) of these issues.

Read BM Chapter 14 &15

April 29 DIVIDEND POLICY
Several stylized facts provide an introduction into how and why managers pay dividends. These facts lead into a discussion of the extant dividend theories, including the information content associated with a change in dividends (dividend signaling). We will also review the key institutional details of how dividends are paid, and will conclude with a discussion of alternative measures of rewarding shareholders such as repurchases, stock splits, and stock dividends.

Read: BM Chapter 16

May 1    **DEBT POLICY**

What is the ‘right’ amount of debt in a firm? The seminal research on this topic in the 1950s by Franco Modigliani and Merton Miller established finance as a discipline based on economic principles and the scientific approach. We will review the Modigliani and Miller outcomes, along with subsequent criticisms leading to tradeoff solutions. We will also examine the debt choice under the more realistic assumption of asymmetric information and illustrate how market imperfections may lead to distortions to the optimal investment rule. Finally, we will review the relevant empirical evidence on debt choice.

Read: BM 17&18

May 6    **SO, WHAT HAVE WE LEARNED? -- CLASS ROUNDTABLE DISCUSSION**

May 8    **REVIEW SESSION**

**FINAL EXAM – Time and location to be determined**

NOTE: This syllabus is a general guideline. Deviations may be necessary. Students are responsible for all announcements made in class or posted on the course web site.

Finally, I asked you for some information, so here is a little about me.

Harley E. Ryan, Jr. (Chip), Ph.D.

Harley E. Ryan, Jr. (Chip) is an Assistant Professor of Finance at the E. J. Ourso College of Business Administration at Louisiana State University in Baton Rouge, Louisiana. Professor Ryan has been at LSU since the summer of 1998. Before joining LSU, he was an assistant professor at Northeastern University in Boston, Massachusetts (1994-1998) and an instructor at Georgia State University in Atlanta, Georgia (1992-1994). He also has been employed as a research assistant at Georgia State University (1989-1992) and as a sales engineer for the Westinghouse Electric Corporation (1983-1989). Professor Ryan has a Ph.D. in Finance and an MBA from Georgia State University, and a Bachelor of Electrical Engineering from the Georgia Institute of Technology in Atlanta, Georgia. His research interests span a wide array of topics in finance including mergers and acquisitions, the role of financial intermediaries in corporate decision-making, agency theory, capital investment decisions, compensation and incentive systems, and insurance. He has been published in journals such as *Financial Management*, the *Journal of Corporate Finance*, *Journal of Risk and Insurance*, the *Quarterly Review of Economics and Finance*, and *Financial Practice and Education* and has made over 50 presentations at national and regional conferences. Professor Ryan has provided
executive education for candidates preparing for the *Certified Turnaround Manager* examination to clients such as Arthur Andersen, BBK, BDO Seidman, Ernst & Young, Executive Sounding Board, Glass & Assoc., Jay Alix & Assoc., Pate, Winter, & Stone, and PriceWaterhouseCoopers.

Personal: I enjoy running, weight training, cooking, traveling, reading, and college (mainly Georgia Tech) football.