Course Description

This course will use cases to examine how the concepts and methods that you learned in your core finance classes can be applied to real world situations. The course will also seek to build upon and expand on these foundational finance skills by giving them a good workout.

This is a course for future CFOs and business leaders. The course will use problem assignments and case analysis to study the major financial decisions companies face and illustrate how financial analysis and corporate finance tools aid strategic decision making. The emphasis throughout is on developing new ways of thinking to cope with a variety of financial problems. Many of these problems have no right solution, so judgment will necessarily play a major role in the decision making process. We will apply corporate finance concepts and techniques to actual situations requiring strategic decisions. In addition to analyzing particular financing problems, we will consider how financing problems relate to the strategic objectives of the firm.

Learning Objectives

Here are the key learning objectives of FBE 532:

- To explore the interrelated character of company decisions in different areas.
- To explore the full range of issues associated with financing tactics and the attainment of the strategic objectives of the firm.
- To examine the interaction of competitive strategy and financial policy (and the use of finance as a competitive weapon).
- To learn how to explain and argue a position under adverse conditions.

Required Materials

Cases: The course pack with our cases can be purchased online at the following link (each case is $3.95): [https://cb.hbsp.harvard.edu/cbmp/access/32567012](https://cb.hbsp.harvard.edu/cbmp/access/32567012) For most of the cases, exhibits are also available as spreadsheets at no cost.
The materials included are:

1. Blaine Kitchenware, Inc.: Capital Structure
2. Sealed Air Corp’s Leveraged Recapitalization (A)
3. Mercury Athletic: Valuing the Opportunity
4. Medfield Pharmaceuticals
5. Kolher Co. (A) and (B)
6. Stryker Corp.: In-sourcing PCBs and Stryker Corporation: Capital Budgeting
7. MW Petroleum Corp. (A)
8. Aqua Bounty
10. RJR Nabisco
11. Valuing a Cross-Border LBO: Bidding on the Yell Group

Optional Materials

The textbook from your first-year corporate finance course. Hopefully you have all been through this, or a similar textbook before.

If you have already traded-in or sold back your corporate finance text, please see the optional textbook option.


Class Participation

Please arrive to class on time and prepared. Be prepared for cold calling, bring your name card to class.

Grading Policies

Final grades represent how you perform in the class relative to other students (your z-score will be calculated based on the class average and standard deviation). Historically, the average grade target for this class is a 3.5 (A-/B+).

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<th>Grade</th>
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<tr>
<td>Case Analysis/Participation</td>
<td>55%</td>
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<tr>
<td>Group Peer Evaluation</td>
<td>5%</td>
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<td>Midterm Exam</td>
<td>15%</td>
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<td>Final Exam</td>
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Class Participation

High Score:

- Regular attendance and active and consistent participation in the class sessions with insightful questions and comments.
- Consistently very high levels of preparation for class sessions and activities.
• Superior and sophisticated understanding, insights, and syntheses of the course material as reflected in group assignments and class discussions.
• Proactive and very high levels of involvement in the group assignments.
• Very high levels of professionalism manifested in interactions with speakers and classmates.

**Case Analysis**
We will analyze real companies and work through problems by analyzing different scenarios and courses of action. In your analysis of case studies you should place yourself in the role of the decision maker as you read through the situation and identify the problems and issues. The next step is to perform the necessary analysis. To get the most out of cases, you should read and reflect on the case individually, and then meet in study group teams prior to class to “warm up” and discuss your findings with other classmates. In class we will probe underlying issues, compare different alternatives, and finally, suggest courses of action in light of the objectives of the case.

For every case I present a number of study questions. These questions are designed to get you going in addressing the case. Note that a case write-up does not consist of answering the study questions. The study questions should be the start of your thinking about the case, not the end.

For each case, teams of 4-6 people should submit a two-page, memo of analysis and recommendations, plus supporting appendices, at the beginning of the case discussion. Write the memorandum as if you were addressing the Board of Directors in the case. Please submit case deliverables on Blackboard before the start of class. Memoranda will not be accepted after the class has met. Cases that must be handed in will be scored on a 0-1-2 basis:
• 0 = missing, substantially incomplete, or of very poor quality;
• 1 = partially incomplete or of marginal quality; and
• 2 = complete and of good or excellent quality.

**Exams**
Exam questions will include both qualitative and quantitative questions from material covered during class.

**Technology Policy**
Laptop and Internet usage is not permitted during academic or professional sessions unless otherwise stated. Use of other personal communication devices, such as cell phones, is considered unprofessional and is not permitted during academic or professional sessions. ANY e-devices (cell phones, PDAs, iPhones, other texting devices, laptops, iPads) must be completely turned off during class time. No student may record any lecture, class discussion or meeting with me without my prior express written permission. I reserve all rights, including copyright, to my lectures, course syllabi and related materials, including summaries, prior exams and all supplementary course materials available to the students enrolled in my class.

**Statement for Students with Disabilities**
Any student requesting academic accommodations based on a disability is required to register with Disability Services and Programs (DSP) each semester. A letter of verification for approved accommodations can be obtained from DSP. Please be sure the letter is delivered to me as early in the semester as possible. DSP is located in STU 301 and is open 8:30 a.m.–5:00 p.m., Monday through Friday. The phone number for DSP is (213) 740-0776.
Emergency Preparedness/Course Continuity
In case of a declared emergency if travel to campus is not feasible, the USC Emergency Information web site (http://emergency.usc.edu/) will provide safety and other information, including electronic means by which instructors will conduct class using a combination of Blackboard, teleconferencing, and other technologies.

Academic Conduct
Plagiarism – presenting someone else’s ideas as your own, either verbatim or recast in your own words – is a serious academic offense with serious consequences. Please familiarize yourself with the discussion of plagiarism in SCampus in Section 11, Behavior Violating University Standards https://scampus.usc.edu/1100-behavior-violating-university-standards-and-appropriate-sanctions/. Other forms of academic dishonesty are equally unacceptable. See additional information in SCampus and university policies on scientific misconduct, http://policy.usc.edu/scientific-misconduct/.

Discrimination, sexual assault, and harassment are not tolerated by the university. You are encouraged to report any incidents to the Office of Equity and Diversity http://equity.usc.edu/ or to the Department of Public Safety http://capsnet.usc.edu/department/department-public-safety/online-forms/contact-us. This is important for the safety of the whole USC community. Another member of the university community – such as a friend, classmate, advisor, or faculty member – can help initiate the report or can initiate the report on behalf of another person. The Center for Women and Men http://www.usc.edu/student-affairs/cwm/ provides 24/7 confidential support, and the sexual assault resource center webpage https://sarc.usc.edu/reporting-options/ describes reporting options and other resources.

Statement on Academic Integrity
USC seeks to maintain an optimal learning environment. General principles of academic honesty include the concept of respect for the intellectual property of others, the expectation that individual work will be submitted unless otherwise allowed by an instructor, and the obligations both to protect one’s own academic work from misuse by others as well as to avoid using another’s work as one’s own. All students are expected to understand and abide by these principles. SCampus, the Student Guidebook, contains the Student Conduct Code in Section 11.00, while the recommended sanctions are located in Appendix A. http://www.usc.edu/dept/publications/SCAMPUS/gov/

Students will be referred to the Office of Student Judicial Affairs and Community Standards for further review, should there be any suspicion of academic dishonesty. The Review process can be found at: http://www.usc.edu/student-affairs/SJACS/ Failure to adhere to the academic conduct standards set forth by these guidelines and our programs will not be tolerated by the USC Marshall community and can lead to dismissal.

Other
The material presented and the classroom discussions are not intended to be financial advice to students in connection with any issue(s) they or others may have. If students have a financial matter, they are advised to promptly consult an experienced professional who can fully review the facts and advise them accordingly.
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<td>26-Jan</td>
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<td>Blaine Kitchenware, Inc.: Capital Structure</td>
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<td>Mercury Athletic: Valuing the Opportunity</td>
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<td>Medfield Pharmaceuticals</td>
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<td>2-Mar</td>
<td>Private Company Valuation, Family Businesses and Legal Issues</td>
<td>Kolher Co. (A) and (B)</td>
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<td>Capital Budgeting</td>
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<td>7-9pm Final Exam</td>
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Jan 26
Blaine Kitchenware, Inc.: Capital Structure

Discussion Questions:
1. Do you believe Blaine’s current capital structure and payout policies are appropriate? Why or why not?

2. Should Dubinski recommend a larger share repurchase to Blaine’s board? What are the primary advantages and disadvantages of such a move?

3. Consider the following share repurchase proposal: Blaine will use $209 million of cash from its balance sheet and $50 million in new debt (bearing interest at the rate of 6.75%) to repurchase 14 million shares at a price of $18.50 per share. How would such a buyback affect Blaine? Consider the impact on, among other things, BKI’s EPS and ROE, its interest coverage and debt ratios, the family’s ownership interest, and the company’s cost of capital.

4. As a member of Blaine’s controlling family, would you be in favor of this proposal? Would you be in favor of a non-family shareholder?

Feb 2
Sealed Air Corp’s leveraged Recapitalization (A)

Discussion Questions:
1. How did Sealed Air undertake a leveraged recapitalization? Do you think it was a good idea? For whom?

2. How much value was created? Where did it come from?

3. Is pursuing a program of manufacturing excellence inconsistent with leveraging up?

4. Why did Dunphy feel it was necessary to change the company’s priorities and incentive structure following the recap?

5. Why did Sealed Air’s investor base turn over completely after the recap? Is this something managers should be concerned about?

6. Was the constraint imposed on capex under the bank lending arrangement good or bad for the company? Do you think managers will be able to successfully renegotiate this covenant?

7. Would such an increase in leverage be good for all companies? Why or why not?
Feb 9

Mercury Athletic: Valuing the Opportunity

Discussion Questions:
1. Is Mercury and appropriate target for AGI? Why or why not?

2. Review the projections formulated by Liedtke. Are they appropriate? How would you recommend modifying them?

3. Estimate the value of Mercury using a discounted cash flow approach and Liedtke’s base case projections. [Assume a market risk premium of 5%]

4. Do you regard the value you obtained as conservative or aggressive? Why?

5. How would you analyze possible synergies or other sources of value not reflected in Liedtke’s base case assumptions?

Feb 23

Medfield Pharmaceuticals

Discussion Questions:
1. What is the financial value that might be created if Medfield decides to pursue the Fleximat reformulation as described in the case?

2. What is the value of Medfield’s existing drugs and drug pipeline? Is the takeover offer price reasonable?

3. Should Johnson recommend accepting the acquisition offer at the given price?

4. What factors should Johnson consider in choosing whether to initiate the reformulation? What factors should Johnson consider in choosing a recommendation regarding the takeover offer?

Mar 2

Kolher Co. (A) and (B)

Discussion Questions:
1. What is the total enterprise value of Kolher Co. using a DCF approach? What is the total enterprise value using a multiples (market value of comparable companies) approach? What is the value of a share held by a minority shareholder in Kolher Co. that is implied by your valuation?

2. What assumptions can you use to arrive approximately at the share price of $55,400 that was estimated by Kolher Co.? Show how these assumptions impact your valuation.

3. What assumptions can you use to arrive approximately at the share price of $273,000 that was estimated by the dissenting shareholders? Show how these assumptions impact your valuation.
Mar 9

Stryker Corp.: In-Sourcing PCBs and Stryker Corporation: Capital Budgeting

Discussion Questions:

Stryker Corp.: In-Sourcing PCBs
1. State the business for option #3, the PCB In-Sourcing proposal
2. Use the projections provided in the case to compute incremental cash flows for the PCB project, as well as its NPV, IRR, and payback period.
3. How would you compare this proposal to options #1 and #2?
4. Based on your analyses, would you recommend that Stryker Instruments fund this project?

Stryker Corp.: Capital Budgeting
1. What are the missions of CERs and the capital budgeting process at Stryker? To what extent have they been shaped by elements of corporate finance history? To what extent are they shaped by Stryker’s particular industry, history, and culture?
2. What the primary strengths and weaknesses of the current system? How should the performance of such a system be evaluated?
3. Given Stryker’s strategy and its long-run goals, what modification to the current system – analytical, organizational, and/or procedural – would you recommend? Develop some specific proposals and be prepared to explain how they address specific problems.

Mar 23

MW Petroleum Corp. (A)

Discussion Questions:
1. Evaluate Amoco’s and Apache’s corporate objectives and strategies. Is it reasonable to expect that the MW properties are more valuable to Apache than to Amoco? What sources of value most plausibly account for the difference between buyer and seller?
2. Structure and execute a DCF valuation of all the MW reserves using APV. How much are the reserves worth? Is your estimate more likely to be high or low? What are the sources of bias?
3. How would you structure an analysis of MW as a portfolio of assets-in-place and options? Specifically, which parts of the business should be regarded as assets-in-place and which as options? What kind of options are present? Should this approach yield a higher or lower value than the all-APV approach you employed above?
4. Execute the analysis you structured in question 3, beginning with assets-in-place. How risky are the assets that underlie the options; i.e., how would you estimate \( \sigma \) for each? How much is the whole portfolio worth?
5. Assuming a sale goes through, how does Apache exercise each of the various options? When should it do so?
Discussion Questions:

1. What are the principal sources of uncertainty facing Aqua Bounty? Does it make sense for the firm to launch an IPO now?

2. Baseline projections for Aqua Bounty’s revenues and costs from their product are given in case Exhibit 5. For discounting purposes, please assume that these costs and benefits occur at the end of the year. Note that they will be realized only if FDA approval is received for the product, which the company estimates as being a one-in-three chance. Assuming approval is forthcoming, Aqua Bounty believes that there is an equal chance of each of the three commercialization scenarios occurring. Under the “low” scenario, revenues would be 75% lower than under the “baseline”; under the “high” scenario, revenues would be 75% higher. In all three scenarios, COGS will be 20% of revenues, and annual SG&A costs of £4 million plus 5% of revenues will be incurred. Commercialization costs would be the same in all three scenarios, as shown in case Exhibit 5.

3. Build a simple cash flow model for Aqua Bounty’s revenues from its AquAdvantage fish, assuming that FDA approval is received. Use this to calculate the value of the product line under each of the three scenarios given. For each session, calculate the:
   a. PV of FDA approval costs (discounted at rf);
   b. PV of product commercialization costs (discounted at rf); and
   c. PV of the free cash flows from the product line, not including commercialization costs of FDA approvals costs (discounted at rA)

You should assume:
   a. Aqua Bounty will face costs of £2.5 million per year for the first three years, associated with its regulatory trials and submissions;
   b. no interest payments, as the firm’s debts will be paid in full using capital raised from the IPO;
   c. a corporate tax rate of 35%; and
   d. an unlevered cost of capital of 14%.

Using your estimates of the costs and revenues generated above, sketch out a decision tree incorporating regulatory and commercialization uncertainty. What would be the value of the product if Aqua Bounty were to proceed with the commercialization in each of the three scenarios? What if Aqua Bounty pursued commercialization only if, at that stage, the product were to have an NPV greater than zero.

4. Use the values calculated above, along with your knowledge of the situation, to generate inputs for a Black-Scholes model of Aqua Bounty’s option to commercialize AquAdvantage fish if the FDA grants approval. How would you incorporate this into your decision tree? What value does this suggest for the business unit?

5. How would further delay in the FDA process affect the valuation of the product line? Which factors within the real option framework would drive this?
Apr 13
Stanley Black & Decker, Inc.

Discussion Questions:
1. What is the incremental value to shareholders of the cost savings (synergies) projected in this merger? How will the value of the synergies be shared in the proposed transaction?

2. After failing to complete a merger following three prior attempts noted in the case, why should the proposed transaction be successful this time?

3. How much of the incremental value created in this transaction will go to the CEOs of the two firms involved?

4. How do you think the leadership team at Black & Decker (other than the CEO) will view this transaction? How about the governor of Maryland (Black & Decker’s headquarters state)?

5. What issues of corporate governance and social policy are raised by the Stanley-Black & Decker merger?

6. If you were a shareholder of Stanley, would you vote in favor of this transaction? Would you vote in favor of the compensation arrangement? Would you vote to re-elect the directors at the next annual meeting?

Apr 20
RJR Nabisco

Discussion Questions:
1. What was the value of RJR Nabisco under:
   a. The pre-bid operating strategy?
   b. The management group’s operating strategy?
   c. KKR’s operating strategy?

2. What accounts for any difference in the value of the three operating plans?

3. Evaluate the special committee’s use of an auction of RJR Nabisco.

4. Which bid should the special committee select, if any? What other actions should the special committee take?
Apr 27
Valuing a Cross-Border LBO: Bidding on the Yell Group

Discussion Questions:
1. Is Yell a good buyout candidate?
2. How similar are the U.K. and U.S. businesses? Do the management projections in Exhibit 6 and Exhibit 7 make sense to you? In other words, if you were part of the Apax/Hicks-Muse team, would you trust them?
3. How does Yell’s projected debt affect its valuation?
4. How does the cross-border nature of the Yell deal affect the valuation of the firm?
5. How much is Yell worth? How much would you bid?
6. If you were Apax/Hicks-Muse, would you do the deal?