
Section 15326 T-TH 10am-11:50am Room: JFF LL 125

Office: Hoffman Hall 221, Office hours before/after class by appointment

See Blackboard for TA contact info/office hours schedule

Course Description

This course develops and uses tools of financial analysis to evaluate the performance and assess the value of individual companies in an industry context. The focus of this course is to learn firm, debt and equity valuation methods from both a conceptual and practical framework. While there is some new finance theory introduced in this course, the emphasis is on the practical application and integration of finance and accounting concepts to valuing companies. There are many approaches to determine fair market value of a firm. We will discuss different valuation methodologies with a focus on DCF and relative valuation. The course will cover methods for utilizing financial data and applying valuation techniques to make strategic and financial decisions. The course introduces topics such as mergers and acquisitions, financial restructuring, leveraged buyouts, valuation of private companies, distressed companies and the impact of financial leverage.

Learning Objectives

This course covers the theory and practice of financial analysis and valuation. Our coverage of the material is designed to allow you to become comfortable with the fundamentals so that you may improve your proficiency in participating in future financial and strategic discussions within a company or organization and with external analysts and service providers.

1. Describe the key aspects of financial analysis and valuation to effectively manage different types of enterprises. Gain knowledge of the following areas: accounting, finance, strategy and industry analysis.
2. Demonstrate critical thinking skills in the application of techniques in financial analysis and valuation. Gather, categorize, analyze, interpret, and evaluate relevant qualitative and quantitative information and develop the ability to be creative and innovative through the completion of a final valuation project.
3. Develop communication strategies for discussing financial analysis and valuation.
4. Conduct research using a broad range of sources, synthesizing and judging the quality of collected information and support written or oral claims logically and persuasively.
5. Apply valuation in a global context, considering the interplay of international markets, and economic, social and cultural issues.

Required Materials

Textbook: *Valuation: The Art and Science of Corporate Investment Decisions*, 3rd Edition
By Sheridan Titman, John D. Martin. Published by Prentice Hall Copyright © 2016 ISBN-13: 978-0133479522 ISBN-10: 0133479528

Cases: The course pack with our cases can be purchased online at the following link:

<http://cb.hbsp.harvard.edu/cbmp/access/58188936>



Recommended:

Wall Street Journal student subscription rates are available: <http://wsjstudent.com>

Prerequisites and/or Recommended Preparation:

Prerequisite: BUAD 215 or BUAD 306. This course assumes knowledge of intro corporate finance and accounting. It will be assumed that students are comfortable with the topics of standard corporate finance texts such as Ross, Westerfield and Jaffe or Brealey & Myers. Please review your basic finance and accounting concepts. The pace and schedule of topics covered in this class does not allow for review of these concepts. Students with weak accounting and finance backgrounds will be at a disadvantage in this course. Working knowledge of excel is also important.

Course Notes

Slides, handouts and supplemental readings/articles will be posted on Blackboard. Notes or recordings made by students based on a university class or lecture may only be made for purposes of individual or group study, or for other non-commercial purposes that reasonably arise from the student's membership in the class or attendance at the university. This restriction also applies to any information distributed, disseminated or in any way displayed for use in relationship to the class, whether obtained in class, via email or otherwise on the Internet, or via any other medium. Actions in violation of this policy constitute a violation of the Student Conduct Code, and may subject an individual or entity to university discipline and/or legal proceedings.

Grading Policies

Final grades represent how you perform in the class relative to other students. Historically, the average grade target for this class is a 3.3/4 (B+). Three items are considered when assigning final grades: 1) your average weighted score as a percentage of the available points for all assignments (the points you receive divided by the number of points possible) 2) the overall average percentage score within the class 3) your ranking among all students in the class.

<u>Grade Breakdown</u>	
Assignments and Group Case Analysis	30%
Participation and Peer Evaluation	10%
Midterm 1 Exam:	30%
Final Exam:	30%
Total	<hr/> 100%

Class Participation and Peer Evaluation

Please arrive to class on time and prepared. Be prepared for cold calling, bring your name card to class. Please handle mobile phone and text messaging outside of class and perform unrelated web browsing outside of class. Please come to class rested (if you sleep in class you will be asked to leave).

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 case analysis 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.

Scores for individual student contributions to team projects (peer evaluation) are assigned by me, based on my observations of the team's working dynamics, my assessment of the team's project quality, and thoughtful consideration of the information provided through your peer evaluations.

Assignments and Group Case Analysis

We will analyze real companies and work through problems by analyzing different scenarios and courses of action. In your analysis of our HBS 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.

All cases are used as a means to assess class participation assessment. Your team/group case analysis will be turned in as a written deliverable. Do your best to work through the case utilizing readings and other supporting materials. Seeking assistance or “hints” from the instructor, the T.A. or past students is not authorized. A written case analysis should consist of a written (executive summary) using a standard font and font size (such as Times New Roman size 11-12), addressing the case questions with supporting computations and tables in a separate appendix (if relevant).

Assignment and case grading is based on the quality of your analysis, how well you support your assumptions and apply valuation techniques, and the judgment you exercise and on the professionalism of your presentations. The quality of work product should be reflective of what you would be comfortable presenting to a current or prospective employer. Case grades will be determined relative to the analyses of other groups in the class. Groups will be randomly selected to verbally present their findings on *both* the graded and discussion cases during the class session.

I encourage you to work in teams to maximize the learning experience. Please work on your cases in groups of 3-6 people. I will not become involved in any group problems. Teams may change composition during the course of the semester. If a set of teammates decides they can no longer work together, they are free to separate. If any member of the team cannot find another suitable team to join, he or she will have no choice but to hand in the rest of the valuation cases individually. In choosing teammates, consider the skills your team will want to possess: accounting, finance and excel modeling expertise. Also make sure that your teammates’ expectations for their performance in this course are consistent with your expectations for yourself.

In addition to the group cases, there will be several individual and group assignments to help you apply the material. These will be posted on Blackboard and are designed to complement the textbook and lecture material.

Assignment Submission Policy

Assignments must be turned in on the due date/time electronically via Blackboard. The cover sheet of each written assignment should contain the first and last names of the students submitting the assignment arranged alphabetically. All of the names of the members in the group must appear at the top of the memo to receive credit.

Add/Drop Process

This class will remain open enrollment (R-clearance) through the add deadline. If there is an open seat, students can add the class using Web Registration. If the class is full, students will need to continue checking the *Schedule of Classes* (classes.usc.edu) to see if a space becomes available. Students who do not attend class the first two weeks may be dropped from the course if they do not notify the instructor prior to their absence. It is the responsibility of a late add student to get caught up on any missed classes or work. There are no special accommodations for late adds.

Technology Policy

Laptop and Internet usage is not permitted during academic or professional sessions unless otherwise stated by the respective professor and/or staff. 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, iPads, other texting devices, laptops, I-pods) must be completely turned off during class time. Upon request, you must comply and put your device on the table in off mode and FACE DOWN. You might also be asked to deposit your devices in a designated area in the classroom. Videotaping faculty lectures is not permitted due to copyright infringement regulations. Audiotaping may be permitted if approved by the professor. Use of any recorded or distributed material is reserved exclusively for the USC students registered in this class.

Academic Integrity and Conduct

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 (plagiarism). 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. All students are expected to understand and abide by the principles discussed in the *SCampus*, the Student Guidebook (www.usc.edu/scampus or <http://scampus.usc.edu>). A discussion of plagiarism appears in the University Student Conduct Code (section 11.00 and Appendix A).

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.

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://dps.usc.edu/contact/report/>. 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. *Relationship and Sexual Violence Prevention and Services* (RSVP) <https://engemannshc.usc.edu/rsvp/> provides 24/7 confidential support, and the sexual assault resource center webpage <https://sarc.usc.edu/reporting-options/> describes reporting options and other resources.

Support Systems

Students whose primary language is not English should check with the *American Language Institute* <http://dornsife.usc.edu/ali>, which sponsors courses and workshops specifically for international graduate students. *The Office of Disability Services and Programs* (www.usc.edu/disability) provides certification for students with disabilities and helps arrange the relevant accommodations. If an officially declared emergency makes travel to campus infeasible, *USC Emergency Information* (<http://emergency.usc.edu/>) will provide safety and other updates, including ways in which instruction will be continued by means of blackboard, teleconferencing, and other technology.

Students with Disabilities

The Office of Disability Services and Programs (www.usc.edu/disability) provides certification for students with disabilities and helps arrange the relevant accommodations. 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 (or to your TA) as early in the semester as possible. DSP is located in GFS (Grace Ford Salvatori Hall) 120 and is open 8:30 a.m.–5:00

p.m., Monday through Friday. The phone number for DSP is (213) 740-0776. Email: ability@usc.edu.

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.

FBE 421 Spring 2017 Schedule of Classes and Assignments

Course schedule is subject to change based on availability of guest speakers.

	Topics/Daily Activities	Readings/Deliverables
1/10 1/12	Course Overview and Intro to Valuation Value Based Management <i>Discussion regarding returns measures ROE, ROIC</i>	Chapter 1 See Blackboard for Value-Based Management reading and video
1/17 1/19	Forecasting and Valuing Cash Flows Understanding Financial Statements and Cash Flow <i>Cash flow, ratio analysis, telling a story with #s</i>	Chapter 2 Chapter 6
1/24 1/26	Understanding Financial Statements and Cash Flow <i>Cash flow, ratio analysis, telling a story with #s</i> Cash Flow Statement Analysis	Chapter 6 See Blackboard
1/31 2/2	Estimating Cost of Capital - WACC <i>Quantifying firm and project cost of capital, betas, review of concepts</i> Relative Valuation Using Market Comps <i>Application of the comps method</i>	Chapters 4-5 Chapter 8
2/7 2/9	<i>Guest Speaker: Luke Sikora, Vulcan Ventures</i> <i>Growth equity, venture capital</i> Relative Valuation Using Market Comps <i>Application of the comps method, discussion re: pricing IPOs</i>	See Blackboard, Chapter 10 Chapter 8
2/14 2/16	Valuation and Strategic Decision Making <i>Hansson Private Label case discussion</i> Midterm Exam	Hansson HBS group case due
2/21 2/23	<i>Guest Speaker: Bob Gatto, VP Corp Strategy Development, Nestlé USA</i> Enterprise Valuation Methods	See Blackboard Chapter 9
2/28 3/2	Enterprise Valuation Methods Valuation in a Private Equity Setting	Chapter 9 Chapter 10
3/7 3/9	Private Company Valuation <i>Spyder case discussion</i> No Class Scheduled*	Spyder HBS case due
3/14-3/16	Spring Break – No Class Scheduled	
3/21 3/23	Mergers and Acquisitions Mergers and Acquisitions	Chapter 26 BUAD 306 text
3/28 3/30	Valuation in a Private Equity Setting, <i>LBOs</i> <i>Guest Speaker: Mike Krumwiede, Colony Starwood Homes</i> <i>Real estate finance and case study on a deal</i>	Chapter 10 See Blackboard
4/4 4/6	No Class Scheduled* Special Topic	
4/11 4/13	Distressed Valuation/Financial Restructuring <i>Guest Speaker: Andy Fohrer, Aurora Capital</i> Leveraged Buyouts and Financial Restructuring <i>Heinz case discussion</i>	See Blackboard Heinz HBS case due
4/18 4/20	Special Topic Real Options Analysis	Chapters 11-12
4/25 4/27	Review Course Wrap-Up	
5/9	Final Exam 11am-1pm	

**M-W Classes observe both MLK Birthday and President's Day.*

Group Case Deliverable: Expansion and Risk at Hansson Private Label

Case: Hansson Private Label Inc.: Evaluating an Investment in Expansion HBS: 4021

Article: Fortune Magazine, "Inside the secret world of Trader Joe's" <http://tinyurl.com/297usn3>

DCF analysis is a key building block for valuation. In this session we will review the process for applying DCF analysis to a capital budgeting proposal. The case includes a comprehensive forecasting example that focuses on the process one goes through to link production capacity utilization, units sold, unit revenues and unit costs to investment cash flows. This case also reviews the time value of money mechanics of discounting investment cash flows to estimate project value.

We will: 1) introduce the standard financial tools for assessing the attractiveness of a proposed capital investment; 2) discuss the complementing of discounted cash flow analysis with industry analysis; 3) examine issues surrounding capital planning process, especially as it applies to a large investment.

HPL, a manufacturer of private-label personal care products must decide whether to fund an unprecedented expansion of manufacturing capacity.

- How would you describe HPL and its position within the private label personal care industry?
- Evaluate HPL's historical financial performance (Exhibit 1). How has the company performed? Consider analysis of financial performance ratios and peer benchmarking (Exhibit 6).
- Using Exhibit 5 Excerpt of Financial Assumptions in Capital Request Form, estimate the project's Free Cash Flows. Are the projections realistic? If not, what changes might you incorporate?
- Using the projected WACC schedule in Exhibit 7, what discount rate would you choose? What flaws, if any, might be inherent in using the WACC as the discount rate?
- Utilizing the data provided in the exhibits, determine whether the project is attractive in strategic and economic terms. Calculate the total project cash flows, NPV, and IRR, given the supplied project forecasts. (see hints on Blackboard). Perform sensitivity analysis.
- Would you recommend that Hansson proceed with the investment? Will the expansion position HPL for any form of sustainable competitive advantage? Will it allow HPL to improve long-term profitability?
- What are the risks of the investment? What might be done to mitigate these risks? If HPL wants to decline the proposal, what practical alternatives does he have?

Group Case Deliverable - Spyder Active Sports
Valuing a Private, High-Growth Company and Evaluation of Strategic Alternatives

David Jacobs founded a high-end ski apparel company in 1978. He successfully built and grew the company, establishing a major international brand that appealed to ski racers and other active skiers. In 1995, he sought external financing to support further growth of the company and structured a financial deal with CHB Capital Partners, a private equity firm in Denver. By 2004, Jacobs was ready to consider alternative types of equity transactions that would provide a source of liquidity to him and his family, including sale of Spyder to another apparel company and sale of a large block of stock to a private equity firm.

- Identify the different “exit” options that are feasible for Spyder in 2004, and analyze the benefits and costs of each alternative. Consider the interests and needs of the owner(s), the current state and future prospects of the company, and the current state of the financial markets.
- Perform a standalone valuation of Spyder. Provide a football field summary valuation showing implied values from 1) Discounted Cash Flow valuation (DCF), 2) Market Approach (Public Comps); 3) Precedent Transactions (M&A Comps). The case does not provide descriptions of the merger and acquisition comparables. However, I have provided these descriptions in a tab in the excel workbook “Exhibit 9 Comp M&A description.” Descriptions of the public companies are provided in the exhibit 10 of the case. I have also provided some historical financial performance for these companies in the excel worksheet.
- Risks? What are the risks to the valuation? Perform a basic sensitivity analysis and address the uncertainty in the assumptions and valuation approach.
- Perspectives of Each Stakeholder: Compare the alternative transactions described on the last page of the case. Which exit option would you choose if you were: 1) David Jacobs; 2) a general partner in CHB Capital; 3) Shimokubo?

Group Case Deliverable – H. J. Heinz M&A¹

During December 2012, Jorge Paulo Lemann, a co-founder and partner at 3G, proposed to Warren Buffett that 3G and Berkshire Hathaway acquire H. J. Heinz Company. Lemann and Buffett, who had known each other for years, jointly decided that the Heinz turnaround had been successful and that there was significant potential for continued global growth. 3G informed Heinz CEO William Johnson that it and Berkshire Hathaway were interested in jointly acquiring his company. Johnson then presented the investors' offer of \$70.00 per share of outstanding common stock to the Heinz board. After much discussion, the Heinz board and its advisors informed 3G that without better financial terms they would not continue to discuss the possibility of an acquisition. Two days later, 3G and Berkshire Hathaway returned with a revised proposal of \$72.50 per share, for a total transaction value of \$28 billion (including Heinz's outstanding debt). Following a forty-day "go-shop" period, Heinz, 3G, and Berkshire Hathaway agreed to sign the deal. But was it a fair deal? And what about the future consequences for shareholders, management, employees, and citizens of Pittsburgh, the location of the company's headquarters?

Complete a valuation of Heinz for this acquisition based on the financial information provided. Determine whether the company is a good candidate for an LBO.

Financial Forecast FCF and TV:

- Revenue, EBITDA and EBIT for 2014E-2018E are provided in Exhibit 2. For working capital I evaluated the historical days of trade and other receivables, inventories and prepaid expenses and also payables and accrued liabilities. Then I kept those assumptions relatively constant to forecast the projected balance sheet working capital items for 2014-2018.
- For CapEx I assumed a historical % of sales (3%).
- For Terminal Value I assumed a conservative perpetual growth rate of .75-1.25% and exit multiple assumptions were taken from the comps.

WACC Assumptions:

- Exhibit 2 provides information for K_e including beta, R_f , MRP assumptions, corporate tax rates and the pre-tax cost of debt (I assumed 4.7%, the most recent weighted average).
- For capital structure weights: For the value of "E" I assumed the pre-announcement stock price of \$60 and the fully diluted shares outstanding from 4/28/13 of 323 million. For total "D" I added the short and long term interest bearing debt from 4/28/13 and subtracted the cash and equivalents.
- Complete a separate valuation based on the Heinz alternative financial assumptions found in the Heinz Exhibits Spreadsheet, under the HNZ Alt tab.

For the ALT scenario the spreadsheet provided shows sensitivity in assumptions:

- Revenue to grow at 1.3% per year
- EBITDA margin to remain constant at 17.6% per year
- Capex to increase to \$450M in 2013, then decline by 10% per year until 2018
- Depreciation expense to grow from 75% of Capex in 2013 to 100% of Capex in 2018, Amortization to remain at \$47M per year
- Net working capital needed to fund growth will be \$50M in 2013, then \$30M per year until 2018
- Tax rates remain constant at 35%, Discount rate to be 6.5% for every forecast year

COMPS - For the implied value of Heinz based on the "market approach" evaluate the transactions and comps provided to help determine whether the offer price was "fair."

¹ Supplement Information: <http://www.sec.gov/Archives/edgar/data/46640/000119312513089866/d491866dprem14a.htm>
https://www.bcgperspectives.com/content/articles/mergers_acquisitions_postmerger_integration_divide_conquer_deals_split_synergies/