Instructor: Professor Jacopo Ponticelli

Contact Information
Office: Kellogg Global Hub 4485
email: jacopo.ponticelli@kellogg.northwestern.edu

Office Hours: By appointment

Course Description:
This course covers the basic financial knowledge needed to run a firm—whether the firm is a multi-billion dollar international conglomerate or a three-person start up. In Finance 1, you learned how to value projects to help decide in which projects to invest. That investment decision, which is often called capital budgeting, is the first fundamental decision in corporate finance. In Finance 2, we will use a combination of lectures and business cases to examine the other two fundamental decisions in corporate finance: how firms fund their projects (capital structure) and how they allocate the return on their investments (payout policy). We will then apply the frameworks we develop to analyze applied corporate finance decisions, including corporate security design, mergers and acquisitions, and corporate risk management.

This course is designed both for managers who will initially specialize in a different functional area (e.g., marketing, operations) and for managers who will be directly involved in making or analyzing corporate finance decisions (e.g., future senior executives, general managers, investment bankers, consultants, securities analysts, money managers, investment advisors).

Textbook:
Berk and DeMarzo, Corporate Finance, (Edition 1, 2, 3 or 4), Prentice Hall (BD). Do not purchase “The Core” or “Fundamentals” versions of the textbook. You do not need the "My Finance Lab" that comes with the textbook.

Cases:
“Sampa Video, Inc.” (HBS 9-201-094)
“UST Inc.” (CaseNet)
“Facebook, Inc.: The Initial Public Offering (A)” (Ivey 9B12N031)
“Safeway, Inc.’s Leveraged Buyout (A)” (HBS 9-294-139)
“Dividend Policy at FPL Group, Inc. (A)” (HBS 9-295-059)
“Valuation of AirThread Connections” (HBS 4263)
“Marriott Corporation (A)” (HBS 9-394-085)
“United Grain Growers Limited (A)” (HBS 9-201-015)
“RJR Nabisco” (HBS 9-289-056)

The course is organized into three modules:
I. Capital Structure (Lectures 1-6; 4 cases)
II. Dividend Policy (Lecture 7; 1 case)
III. Applied Topics (Lectures 8-10; 4 cases)

I. Capital Structure

1. Introduction
   - Role and objectives of financial manager
   - How market efficiency affects financial decision making
     BD: Chapter 1.2 (pages 7-14) and Chapter 9.5 (pages 294-300)

2. Why Does Capital Structure Matter?
   - What is debt and equity?
   - MM irrelevance proposition
     BD: Chapter 14

3. Capital Structure: Taxes
   - Tax subsidies for corporate borrowing
   - Adjusted present value (APV) and weighted average cost of capital (WACC)
     BD: Chapters 15 and 18

Case application: “Sampa Video, Inc.”

   - Costs of financial distress
     BD: Chapter 16 and Chapter 24.3 (pages 845-848)

Case application: “UST Inc.”

5. Capital Structure: Security Mispricing
   - Signaling with capital structure
     BD: Chapter 16.8 (pages 564-571) and Chapter 23

Case application: “Facebook, Inc.: The Initial Public Offering (A)”

6. Capital Structure: Conflicts of Interest
   - Separation of ownership and control
   - Private equity
     BD: Chapter 16.6 (pages 559-563) and Chapter 29

Case application: “Safeway, Inc.’s Leveraged Buyout (A)”

II. Dividend Policy

7. Dividend Policy
   - MM irrelevance proposition
   - Dividends and taxes
   - Signaling with dividends
     BD: Chapter 17
Case application: “Dividend Policy at FPL Group, Inc. (A)”

III. Applied Topics

8. Security Design
   - Convertible securities
   - Callable/Exchangeable securities
   - Warrants
     BD: Chapter 24

9. Mergers & Acquisitions
   BD: Chapter 28

Case application: “Valuation of AirThread Connections”

Case application: “Marriott Corporation (A)”

10. Risk Management
    BD: Chapter 30

Case application: “United Grain Growers Limited (A)”

Case application: “RJR Nabisco”

LECTURES AND CLASS DISCUSSIONS

The lectures will be based on the outlines posted on Canvas. You should read the relevant lecture outlines carefully prior to class. I will encourage class participation and preparation is essential.

ASSIGNMENTS AND EXAMS

Deadlines for this class are non-negotiable. If you have a question about a deadline, you should resolve your question prior to the deadline. Under special circumstances you may arrange to turn in assignments early. Assignments will not be accepted after the due date and exams may not be taken late. Turning in assignments after the due date or taking an exam later than the scheduled time may provide a student with an “unfair advantage over other students.” Students unable to complete the course assignments and exams by the due date will receive a zero and therefore may not pass this class.

Homework Assignments:

The homework assignments are not graded and should be completed for your benefit. I will post answers on Canvas, but I will not collect your answers. Doing the homework will make the concepts much clearer and will help you immensely when it becomes time for the exams. The solution to the homework assignments will be discussed in TA review sessions.
Case Assignments:

**Long Cases:** a case memo (detailed written answer) is due before the beginning of the class on the day that we discuss each of the following cases:

<table>
<thead>
<tr>
<th>Case</th>
<th>Due date</th>
</tr>
</thead>
<tbody>
<tr>
<td>UST</td>
<td>TBD</td>
</tr>
<tr>
<td>Facebook</td>
<td>TBD</td>
</tr>
<tr>
<td>AirThread</td>
<td>TBD</td>
</tr>
<tr>
<td>RJR Nabisco</td>
<td>TBD</td>
</tr>
</tbody>
</table>

**Short Cases:** written answers to a short assignment are due before the beginning of the class on the day we discuss each of the following cases:

<table>
<thead>
<tr>
<th>Case</th>
<th>Due date</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sampa Video</td>
<td>TBD</td>
</tr>
<tr>
<td>Safeway</td>
<td>TBD</td>
</tr>
<tr>
<td>FPL</td>
<td>TBD</td>
</tr>
<tr>
<td>Marriott</td>
<td>TBD</td>
</tr>
<tr>
<td>United Grain Growers</td>
<td>TBD</td>
</tr>
</tbody>
</table>

The four long cases are worth 25 points each. The five short cases are worth 10 points each. I will not handout answers for either the long or the short cases. Answers will be discussed in class.

Each memo for the long cases should be 3-5 written pages plus tables. Case questions are on Canvas. Brevity is a virtue. Do not repeat the facts of the case – I have read it. You should turn in your memo at the beginning of class, but keep a copy as you will be expected to contribute to the class discussion based on your analysis. I expect the answers to be both well reasoned and well presented. The cases are your opportunity to apply the concepts you have learned thus far to messy, real world situations. In the real world, understanding the ideas is important – being able to explain them to your boss and coworkers is equally important. Thus your case write ups will be graded on both your answers and how well you defend your proposed solution.

Your answers must not only be correct, but also must be clear. You will find a spreadsheet program essential for preparing your answers, but handing in your excel spreadsheets is not considered a sufficient answer. It should be clear both what your answer is and how you arrived at it. You should be able to integrate the spreadsheets and graphs into the text of your answers. This doesn’t mean you should hand in elaborate presentations – these are homework assignments.

For the long cases you may work in groups of up to 6 individuals. It is sufficient to turn in 1 copy of the case memo per group. Clearly states the names of group members on the first page. I strongly urge you to work in groups. In the past, groups have been more successful than individuals in preparing the cases.

For the short cases, each student should submit the assignment individually.
Exams:

There will be two exams. The midterm exam will be given in class during the fifth week of the course. It will cover the first four weeks of material. The final exam will be given during exam week (the eleventh week of the course). It will cover the entire course. The midterm will count for 120 points, and the final exam will count for 240 points.

GRADING

Your total score for the class will be computed as follows:

<table>
<thead>
<tr>
<th>Assignment</th>
<th>Total Points</th>
</tr>
</thead>
<tbody>
<tr>
<td>Case memos (4)</td>
<td>25 each</td>
</tr>
<tr>
<td>Case polls (5)</td>
<td>10 each</td>
</tr>
<tr>
<td>Midterm</td>
<td>120</td>
</tr>
<tr>
<td>Final</td>
<td>240</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>510</strong></td>
</tr>
</tbody>
</table>

Total score = 4 cases memos + 5 case polls + max (midterm + final, 1.5 × final)

REGRADE POLICY

If you feel that your homework assignments, cases, or exams have been graded incorrectly, you can submit a regrade request. I adhere to the Kellogg regrade policy. All requests must be made in writing within 10 working days after the exam or assignment has been graded and returned. They should consist of a short explanation of why you think the grading is incorrect. Upon submission of a regrade request, I will review your entire assignment/exam. Your final grade will be based on this complete review. Therefore, your grade can either be raised or lowered as a result of a regrade request.

HONOR CODE

The Kellogg honor code strictly applies to all aspects of this course, including class assignments, class participation, and exams. Exams are to be completed individually and are closed book. Solutions to previous year’s problems should not be used in solving homework or case assignments. The complete honor code can be found on the Office of Student Affairs website. Ask if there is any uncertainty as to how the honor code applies to this course.
OTHER ADMINISTRATIVE DETAILS

The class notes, homework assignments and answers, and past exams are the intellectual property of the instructor. You may not distribute class notes electronically or in any form to any one outside the class or outside Kellogg. You may not duplicate these notes for use by your employers after graduating from Kellogg without my written consent.

Appointments to discuss anything related to the course may be made by e-mailing me at jacopo.ponticelli@kellogg.northwestern.edu. Please make appointments at least a day in advance.