Tuck School at Dartmouth

ADVANCED CORPORATE FINANCE

Winter 2013
Mon/Tue 10:15—11:45

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DESCRIPTION

This advanced course highlights much of the up-to-date scientific empirical evidence in the field of corporate finance. It exposes students to the empirical research process and develops economic intuition about key corporate finance decisions in practice. The readings and class discussions are largely non-technical, but students must have a good understanding of basic statistics and regression analysis. Among the topics are corporate governance and control, investment banking and the capital acquisition process, corporate capital structure choice and payout policies, resolution of financial distress and bankruptcy, and executive and director compensation policies.

GRADING

- 60% of the grade consist of the following three components:
  - Individual class participation.
  - Four individual (two-page) memos on required readings
  - Two group case write-ups (15 minute power points)
- 40% of the grade: Group term paper (due and presented last week of class)

READINGS:

Course readings consist of individual articles (in course package) and the two-volume set below. The books contain unique and comprehensive reviews of empirical evidence spanning all core areas of corporate finance. The set is available in the local Hanover bookstore and on the web. It is also available in Chinese.

Eckbo, B. Espen (ed.), 2007, *Handbook of Corporate Finance: Empirical Corporate Finance, Volume 1*, (Elsevier/North-Holland Handbook of Finance Series), ISBN-9780444508980 (BEE-1)

Eckbo, B. Espen (ed.), 2008, *Handbook of Corporate Finance: Empirical Corporate Finance, Volume 2*, (Elsevier/North-Holland Handbook of Finance Series), ISBN-9780444530905 (BEE-2)

ADVANCED CORPORATE FINANCE

STUDENT WRITE-UPS AND PRESENTATIONS

I, Two-page memos

Each student submits electronically to Professor Eckbo (email to academic course coordinator Kati LeBrun at kati.lebrun@tuck.dartmouth.edu) a total of four two-page memos answering the sets of questions listed below in this outline, under the session where the memo is due (at the beginning of the class). The memos are compulsory but will not be graded nor returned. Their purpose is to enhance the level of class preparedness and discussion.

II. Cases

Each group will prepare a 15-minute power point presentation of the two cases listed below.

III. Group term paper (expected group size is four)

(1) Timeline and format
The term paper is due for presentation to class in Sessions 17 and 18. You need to submit electronically to Professor Eckbo a paper of maximum 10 double-spaced pages (plus tables and references) as well as a 15-minute power point presentation of the main results and conclusions.

(2) Objective
The objective of the term paper is to describe and analyze a case which you think raises interesting corporate financing issues in some part of the world. If you are familiar with or interested in a country other than the U.S., you are encouraged to present a case from your own region and culture.

You are free to select the topic and emphasis. Previous classes have presented term papers on cases addressing intricate financing solutions to investment problems, decisions to go public, corporate takeover bidding, target defenses to hostile bids, charges of insider trading, evidence of "excessive" compensation, self dealing and other forms of wealth expropriation of minority shareholders, conflicts in bankruptcy, institutional activism, etc.

(3) Literature
Include a brief summary of one or more academic study that you think is relevant for the case, either directly or as background. If you cannot find a suitable academic paper in the syllabus or readings, consult with Professor Eckbo. Note that if you are dealing with a foreign country, you should include a brief description of key aspects of that country's financial and governance systems as these may not be widely known to the class.

A proposal for the term paper should be emailed to Professor Eckbo by Session 11 (Feb 11).

Advanced Corporate Finance
Winter 2012
B. Espen Eckbo

Session #	Date		Topic	Write-ups Due
			I. Introduction and Valuation review	
1	Mon	1/7	Valuation Review and the “Bad Model Problem”	
			II. Corporate Governance and Control	
2	Tue	1/8	The Corporate Governance System	
3	Mon	1/14	Governance Breakdown: Interco Case	Case 1
4	Tue	1/15	Legality of Takeover Defenses	
			III. Financial distress and bankruptcy	
5	Tue*	1/22	Navigator Gas Transport PLC	Case 2
6	Wed*	1/23	Bankruptcy Design: Do Auctions Work?	
			IV. Raising Capital	
7	Mon	1/28	Why are IPOs Underpriced?	Memo 1
8	Tue	1/29	Adverse Selection in Issue Markets	
9	Mon	2/4	Issue Costs and the Rights Offer Paradox	
10	Tue	2/5	Behavioral Finance and the New Issues Puzzle	Memo 2
			V. Capital Structure and Dividends	
11	Mon	2/11	Capital Structure Choice – 1	Memo 3
12	Tues	2/12	Capital Structure Choice - 2	
13	Mon	2/18	Dividends and Stock Repurchases	
			VI. Executive Compensation and Incentives	
14	Tue	2/19	Optimal Compensation Policies	Memo 4
15	Mon	2/25	A Compensation Consultant’s View	
16	Tue	2/26	Board Diversity and Corporate Ethics	
17	Mon	3/4	Term project presentations	Term Paper
18	Tue	3/5	Term project presentations	Term paper

ADVANCED CORPORATE FINANCE
SESSION TOPICS AND READINGS

I. INTRODUCTION AND VALUATION REVIEW

SESSION 1: Valuation Review and the "Bad Model Problem"

- *Valuation techniques*
- *Valuation pitfalls*
- *Why model values may differ from market values*

Corporate Valuation and Market Multiples (HBS 9-206-039)

II. CORPORATE GOVERNANCE AND CONTROL

SESSION 2: Corporate Governance and Control

- *Investor rights protection*
- *What's unique about the U.S.?*
- *Institutional investor activism*

"Norway Sells Wal-Mart" (HBS 9-308-019)

Becht, Marco, Patric Bolton and Ailsa Roell, 2005, "Corporate Governance and Control", ECGI Working Paper no. 02/2002.

SESSION 3: Governance Breakdown: Interco

- *Bidding strategy*
- *Target management response*
- *Board deliberations*

Case 1: Interco (HBS 9-291-033). Student presentations.

SESSION 4: Legality of Takeover Defenses

- *Brief history of the hostile takeover*
- *Legality of defenses*
- *The Circon Pill*

Betton, Eckbo and Thorburn, "Corporate Takeovers", Section 3.5 in BEE-2

III. FINANCIAL DISTRESS AND BANKRUPTCY

SESSION 5: Navigator Gas Transport PLC

- *Financial distress*
- *Restructuring of claims*
- *Investing in distressed situations*

Case 2: Navigator Gas Transport PLC (HBS 207-092). Student presentation.

SESSION 6: Bankruptcy Design: Do Auctions Work?

- *What is bankruptcy law trying to accomplish?*
- *Auction as a bankruptcy mechanism*
- *Do auctions cause "fire-sales"?*

Hotchkiss, Edith S., Kose John, Robert Mooradian, and Karin S. Thorburn, 2008, "Bankruptcy and the Resolution of Financial Distress," Ch.14 in BEE-2.

Eckbo, B. Espen and Karin S. Thorburn, 2009, "Bankruptcy as an Auction Process: Lessons from Sweden", *Journal of Applied Corporate Finance* 21, 36-50.

III. RAISING CAPITAL

SESSION 7: Why are IPOs Underpriced?

- *The IPO selling process*
- *Book building and the partial adjustment phenomenon*
- *IPO auctions*

Ljungqvist, Alexander, 2007, "IPO Underpricing", Ch. 7 in BEE-1.

Two-Page Memorandum #1:

(1) Summarize the main arguments for why issuers and banks would rationally agree to underprice IPOs.
(2) If you were the issuing firm, how would you try to minimize the underpricing cost?
(3) In a one-page Appendix, report results of regressing underpricing on issue characteristics (data file in course folder).

SESSION 8: Adverse Selection in Issue Markets

- *What is adverse selection?*
- *Effects of adverse selection and on issue costs*
- *Market reaction to issue announcements*

Eckbo, B. Espen, Ronald Masulis and Oyvind Norli, 2007, "Security Offerings," Ch. 6, Sections 2 and 3, in BEE-1.

SESSION 9: Issue Costs and the Rights Offer Paradox

- *Alternative flotation methods and their costs*
- *Effects of adverse selection and on issue costs*
- *Why have equity rights offers almost disappeared in the U.S?*

Eckbo, B. Espen, 2008, "Equity Issues and the Disappearing Rights Offer Phenomenon", *Journal of Applied Corporate Finance* 20 (4), 72-85.

SESSION 10: Behavioral Finance and The New Issues Puzzle

- *Long-run returns following SEOs, IPOs, and Debt Offerings*
- *Behavioral versus risk explanations for low long-run returns*
- *Accounting for liquidity risk*

Eckbo, B. Espen, Ronald Masulis and Oyvind Norli, 2007, “Security Offerings,” Ch. 6, Section 5, in BEE-1.

Baker, Malcolm and Jeffry Wurgler, 2007, “Behavioral Corporate Finance”, Ch. 4 in BEE-1

Two-Page Memorandum #2:
(1) Try to formulate a concise definition of the term “behavioral” versus the term “rational”
(2) Suggest corporate actions that you believe are best explained by behavioral activities.
(3) What empirical evidence supports your suggestions under (2)?
(4) Is a “behavioral” perspective is useful for our understanding of corporate finance decisions?

IV. CAPITAL STRICTURE AND DIVIDENDS

SESSION 11: Capital Structure Choice – 1

- *CFOs survey*
- *Debt and taxes*
- *Do firms follow pecking order or tradeoff models*

Graham, 2008, “Taxes and Corporate finance”, Ch. 11 in BEE-2

Frank, Murray and Vidhan Goyal, 2007, “Tradeoff and Pecking Order Theories of Debt,” Ch. 12, BEE-2

Two-Page Memorandum #3:

(1) Briefly characterize the “tradeoff theory” and list what you think are its empirical implications.
(2) Briefly characterize the “pecking order theory” and list what you think are its empirical implications
(3) Which theory do you believe best characterizes actual corporate capital structure decisions? Explain

SESSION 12: Capital Structure Choice – 2

- *Corporate uses and sources of funds*
- *The dominance of internal finance*
- *Debt and equity issue activity*

Eckbo, B. Espen and Michael Kisser, 2012, “Capital Structure: Who Finances Externally?”, Tuck Working Paper.

SESSION 13: Dividends and Stock Repurchases

- *Stock liquidity and investor demand for dividends*
- *Drivers of dividend policy*
- *Stock repurchases*

Kalay, Avner and Michael Lemon, 2008, “Payout Policy”, Ch. 10 in BEE-2.

VI. EXECUTIVE COMPENSATION AND INCENTIVES

SESSION 14: Optimal Compensation Policies

- *How do you determine the pay level?*
- *Is CEO pay-performance sensitivity significant?*
- *Does option-based compensation induce excessive risk taking?*

Aggarwal, Rajesh, 2008, "Executive Compensation and Incentives", Ch. 17 in BEE-2.

Jensen, Michael C. and Kevin J. Murphy, 2004, "Remuneration: Where We've Been, How we Got to Here, What are the Problems, and How to Fix them", Working paper, HBS and USC.

Two-Page Memorandum #4:

(1) How would you determine the total size of CEO compensation (sum of all pay components)? Do you think observed total CEO compensation packages are competitive?
(2) Discuss pros and cons of stock option programs. What are they trying to achieve and are they successful?
(3) Do you think investor "say on pay" is useful? Why or why not?

SESSION 15: CEO Pay: A Compensation Consultant's View

Class Visitor:
Stephen O'Byrne, President, Shareholder Value Advisors, Inc.

O'Byrne, Stephen F. and S. David Young, 2010, "Six factors that Explain Executive Pay (and its Problems)", *Journal of Applied Corporate Finance* 22 (Spring), 109—117.

For background:
O'Byrne, Stephen F. and S. David Young, 2010, "How Executive Pay Lost Its Way"

O'Byrne, Stephen F., "Assessing Pay for Performance", *The Conference Board* October 2011

SESSION 16: Board Diversity and Corporate Ethics

Class Visitors:
Art Lindenauer T'59, former Chairman of the Audit Committee of Schlumberger Technology Corporation.

Susan B. Linendeauer, former General Counsel if the Legal Aid Society of New York City.

SESSIONS 17 and 18: Term paper presentations