

**KARACHI UNIVERSITY BUSINESS SCHOOL
UNIVERSITY OF KARACHI**

FINANCE & INVESTMENT

Course Title : CORPORATE FINANCE

Course Number : BA(BS-FIN) – 662

Credit Hours : 03

Course Contents

1. The Financial Environment

- 1.1. The Flow of Savings to Corporations
 - 1.1.1. The Stock Market
 - 1.1.2. Other Financial Markets
 - 1.1.3. Financial Intermediaries
 - 1.1.4. Financial Institutions
 - 1.1.5. Total Financing of U. S. Corporations
- 1.2. Functions of Financial Markets and Intermediaries
 - 1.2.1. Transporting Cash Across Time
 - 1.2.2. Liquidity
 - 1.2.3. The Payment Mechanism
 - 1.2.4. Reducing Risk
 - 1.2.5. Information Provided to Financial Markets
 - 1.2.6. The Opportunity Cost of Capital

2. Valuing Bonds

- 2.1. Bond Characteristics
 - 2.1.1. Reading the Financial Pages
- 2.2. Bond Prices and Yields
 - 2.2.1. How Bond Prices Vary with Interest Rates
 - 2.2.2. Yield to Maturity versus Current Yield
 - 2.2.3. Rate of Return
 - 2.2.4. Interest Rate Risk
 - 2.2.5. The Yield Curve
 - 2.2.6. Normal and Real Rate of Interest
 - 2.2.7. Default Risk
 - 2.2.8. Variation in Corporate Bonds

3. Valuing Stocks

- 3.1. Stocks and Stock Market
 - 3.1.1. Reading the Stock Market Listings

- 3.2. Book Values, Liquidation Values, and Market Values
- 3.3. Valuing Common Stocks
 - 3.3.1. Today's Price and Tomorrow's Price
 - 3.3.2. The Dividend Discount Model
- 3.4. Simplifying the Dividend Discount Model
 - 3.4.1. The Dividend Discount Model with no Growth
 - 3.4.2. The Constant – Growth Dividend Discount Model
 - 3.4.3. Estimating Expected Rates of Returns
 - 3.4.4. Non–Constant Growth
- 3.5. Growth Stocks and Income Stocks
 - 3.5.1. The Price Earning Ratio
 - 3.5.2. Valuing Entire Businesses
- 3.6. There are No Free Lunches on Wall Street
 - 3.6.1. Method 1: Technical Analysis
 - 3.6.2. Method 2: Fundamental Analysis
 - 3.6.3. A Theory to Fit The Facts
- 3.7. Behavioral Finance and the Rise and Fall of the Dot.Coms

4. Using Discounted Cash Flow Analysis to Make Investment Decisions

- 4.1. Discount Cash Flows, Not Profits
- 4.2. Discount Incremental Cash Flows
 - 4.2.1. Include all Indirect Effect
 - 4.2.2. Forget Sunk Costs
 - 4.2.3. Include Opportunity Cost
 - 4.2.4. Recognize the Investment in Working Capital
 - 4.2.5. Beware of Allocated Overhead Costs
- 4.3. Discount Nominal Cash Flows by the Nominal Cost of Capital
- 4.4. Separate Investment and Financing Decisions
- 4.5. Calculating Cash Flow
 - 4.5.1. Capital Investment
 - 4.5.2. Investment in Working Capital
 - 4.5.3. Cash Flow from Operations

5. Project Analysis

- 5.1. How Firms Organize the Investment Process
 - 5.1.1. Stage One: The Capital Budget
 - 5.1.2. Stage Two: Project Authorizations
 - 5.1.3. Problems and Some Solutions
- 5.2. Some "What – If" Questions
 - 5.2.1. Sensitivity Analysis
 - 5.2.2. Scenario Analysis
- 5.3. Break Even Analysis
 - 5.3.1. Accounting Break Even Analysis
 - 5.3.2. Economic Value Added and Break Even Analysis
 - 5.3.3. Operating Leverage
- 5.4. Real Options and the Value of Flexibility
 - 5.4.1. The Option to Expand

- 5.4.2. A Second Real Option: The Option to Abounded
- 5.4.3. A Third Real Option: The Timing Option
- 5.4.4. A Fourth Real Option: Flexible Production Facilities

6. Introduction to Risk, Return, and the Opportunity Cost of Capital

- 6.1. Rate of Return: A Review
- 6.2. A Century of Capital Market History
 - 6.2.1. Market Indexes
 - 6.2.2. The Historical Record
 - 6.2.3. Using Historical Evidence to Estimate Today's Cost of Capital
- 6.3. Measuring Risk
 - 6.3.1. Variance and Standard Deviation
 - 6.3.2. A Note on Calculating Variance
 - 6.3.3. Measuring the variance in Stock Return
- 6.4. Risk and Diversification
 - 6.4.1. Diversification
 - 6.4.2. Asset versus Portfolio Risk
 - 6.4.3. Market Risk versus Unique Risk
- 6.5. Thinking about Risk
 - 6.5.1. Message 1: Some Risk Look Big and Dangerous but Really are Diversifiable
 - 6.5.2. Message 2: Market Risk are Macro Risks
 - 6.5.3. Message 3: Risk can be Measured

7. Risk, Return and Capital Budgeting

- 7.1. Measuring Market Risk
 - 7.1.1. Measuring Beta
 - 7.1.2. Betas for Amazon.com and Exxon Mobile
 - 7.1.3. Portfolio Betas
- 7.2. Risk and Return
 - 7.2.1. Why the CAPM Works
 - 7.2.2. The Security Market Line
 - 7.2.3. How well does the CAPM Work?
 - 7.2.4. Using the CAPM to Estimated Expected Return
- 7.3. Capital Budgeting and Project Risk
 - 7.3.1. Company versus Project Risk
 - 7.3.2. Determinant of Project Risk
 - 7.3.3. Don't add Fudge Factors to Discount Rates

8. The Cost of Capital

- 8.1. Geothermal Cost of Capital
- 8.2. The Weighted–Average Cost of Capital
 - 8.2.1. Calculating Company Cost of Capital as a Weighted Average
 - 8.2.2. Market versus Book Weights
 - 8.2.3. Taxes and the Weighted–Average Costs of Capital
 - 8.2.4. What If There Are Three (or More) Sources of Financing?
 - 8.2.5. Wrapping up Geothermal
 - 8.2.6. Checking our Logic
- 8.3. Measuring Capital Structure

- 8.4. Calculating the Required Rate of Returns
 - 8.4.1. The Expected Return on Bonds
 - 8.4.2. The Expected Return on Common Stock
 - 8.4.3. The Expected Return on Preferred Stock
- 8.5. Calculating the Weighted Average Cost of Capital
 - 8.5.1. Real Company WACCs
- 8.6. Interpreting the Weighted Average Cost of Capital
 - 8.6.1. When You Can and Can't Use WACC
 - 8.6.2. Some Common Mistakes
 - 8.6.3. How Changing Capital Structure Affects Expected Returns
 - 8.6.4. What Happens when the Corporate Tax Rate is not Zero
- 9. An Overview of Corporate Financing**
 - 9.1. Creating Value with Financing Decisions
 - 9.2. Common Stock
 - 9.2.1. Ownership of the Corporation
 - 9.2.2. Voting Procedures
 - 9.2.3. Classes of Stock
 - 9.3. Preferred Stocks
 - 9.4. Corporate Debt
 - 9.4.1. Debt Comes in Many Forms
 - 9.4.2. Innovation in the Debt Market
- 10. Debt Policy**
 - 10.1. How Borrowing Affects Values in a Tax Free Economy
 - 10.1.1. MM's Argument
 - 10.1.2. How Borrowing Affects Earnings per Share
 - 10.1.3. How Borrowing Affects Risk and Return
 - 10.1.4. Debt and the Cost of Equity
 - 10.2. Capital Structure and Corporate Taxes
 - 10.2.1. Debt and Taxes of River Cruises
 - 10.2.2. How Interest Tax Shields Contribute to the Value of Stockholders' Equity
 - 10.2.3. Corporate Taxes and the Weighted Average Cost of Capital
 - 10.2.4. The Implications of Corporate Taxes for Capital Structure
 - 10.3. Costs of Financial Distress
 - 10.3.1. Bankruptcy Costs
 - 10.3.2. Financial Distress without Bankruptcy
 - 10.3.3. Cost of Distress Vary with Type of Asset
 - 10.4. Explaining Financing Choices
 - 10.4.1. The Trade-Off Theory
 - 10.4.2. A Pecking Order Theory
 - 10.4.3. The Two Forces of Financial Stock
- 11. Dividend Policy**
 - 11.1. How Dividends are Paid
 - 11.1.1. Cash Dividends
 - 11.1.2. Some Legal Limitations on Dividends
 - 11.1.3. Stock Dividends and Stock Splits

- 11.2. Share Repurchase
 - 11.2.1. The Role of Share Repurchases
 - 11.2.2. Repurchases and Share Valuation
- 11.3. How Do Companies Decide on Dividend Payments?
- 11.4. Why Dividend Policy should not Matter?
 - 11.4.1. Dividends Policy is Irrelevant in Competitive Markets
 - 11.4.2. The Assumptions behind Dividend Irrelevance
- 11.5. Why Dividends may Increase Firm Value?
 - 11.5.1. Market Imperfections
 - 11.5.2. Dividends as Signals
- 11.6. Why Dividends may Reduce Firm Value?
 - 11.6.1. Why Pay any Dividends at All?
 - 11.6.2. Taxation of Dividends and Capital Gains under Current Tax Law

12. Financial Planning

- 12.1. What is Financial Planning
 - 12.1.1. Financial Planning Focuses on the Big Picture
 - 12.1.2. Why Build Financial Plans?
- 12.2. Financial Planning Models
 - 12.2.1. Components of a Financial Planning Model
 - 12.2.2. An Example of a Planning Model
 - 12.2.3. An Improved Model
- 12.3. Planners Beware
 - 12.3.1. Pitfalls in Model Design
 - 12.3.2. The Assumption in Percentage of Sales Models
 - 12.3.3. The Role of Financial Planning Models

13. Credit Management and Bankruptcy

Recommended Books

1. Marcus, B. M. (2006). *Fundamentals of Corporate Finance*. New Jersey: Irwin / McGraw–Hill.
2. Ross, S. (2007). *Corporate Finance*. New York: Irwin / McGraw–Hill.
3. Ross, Westerfield, & Jordan, (2009). *Corporate Finance*. New York: McGraw–Hill.
4. Gupta, N. & Sharma, C. (2008). *Corporate Accounting*. New Delhi: Ane Books.