

Syllabus for ECO359H1S. Financial Economics II: Corporate Finance

The aim of this course is to give you an overview of the major theories, tools and results in corporate finance. Modern finance is a highly mathematical field, and we will use some math. However the purpose of using math is to enhance one's understanding, 'the major hurdles in Finance are conceptual rather than mathematical' (John Cochrane). We will not go through all institutional details — I leave this for your securities courses. The course focusses mainly on theoretical issues, but naturally we also want apply the ideas to understand some real-world examples. Students are required to follow current events.

Course Information

- Class Times: Tuesdays. Section L0101: 3-5pm. Section L5101: 6-8pm.
See exceptions to class times below.
- Class Location: Section L0101 (day): UC 179. Section L5101 (evening): SS 2127.
- Office Hours: Tuesdays 2-3pm (Ding Ding, GE 313)
Thursdays 1:30-2:30pm (Professor Malinova, GE 211)
Please check portal for the office hour schedule during weeks of your term tests and during the study and exam period.
- Course Webpage: <http://portal.utoronto.ca>
- My office: Max Gluskin House 211 (GE 211), 150 St. George Street.
Phone: 416 978 5283.
Email: katya.malinova@utoronto.ca
- Exclusions: ACT349H, MGT331Y, MGT337Y, RSM333H.
Prerequisite: ECO358H.

Exceptions to Class and OH Times

There will be the following exceptions to class times above:

1. The first lecture (January 08, 2012) will take place at 2-4pm and 5-7pm.
2. Your term tests will take place 3-5pm and 5-7pm. Locations are TBA.
3. Regular office hours are held in term (through April 05), except for the weeks of your term tests. Office hours during the weeks of your term tests and during the study and exam period will be posted on the course webpage.

TA Support

Our teaching assistants for the course is Ding Ding (d.ding@utoronto.ca), a PhD student in financial economics.

Academic Integrity and Respect: An important part of your university education involves always choosing to behave with integrity despite difficult and tempting situations. As explained in the University of Toronto *Code of Behaviour on Academic Matters*, academic integrity is a serious matter. Also, you are expected to respect your classmates and me. For example, during lecture do not chat, surf the Internet, read the newspaper, sleep, eat nor engage in any other disruptive behaviors.

Exams and Grade Composition

There will be three exams: two in-class midterm tests (2 hour-long 3-5pm and 5-7pm; check the course webpage for the test location) and a 3-hour final. The weights are as follows:

- Midterm 1: 30%
- Midterm 2: 30%
- Final: 40%

If your score on the final is better than your worst midterm score **and** your worst midterm score is above 30%, then your worst midterm will not count and its weight will be automatically shifted towards the final. Specifically, provided your worst midterm score is above 30%, your course-grade is determined as follows

$$\begin{aligned} & 40\% \times \text{final} \\ + & 30\% \times \max\{\text{midterm I}, \text{midterm II}\} \\ + & 30\% \times \max\{\text{final}, \min\{\text{midterm I}, \text{midterm II}\}\}. \end{aligned}$$

If both of your midterm scores are below 30% or if your score on the final exam is below that of your worst midterm, then no weight redistribution will occur.

Appeals. If you appeal to re-grade one of the exam questions, we will re-grade the *entire* exam. This may lead to a lower or higher overall grade. Your complaint has to be in writing, it must be submitted within one month from the day that graded midterms become available for pick-up, and it must explain why you believe grading to be incorrect.

These conditions do not apply to clerical errors (i.e. adding your scores incorrectly); if a clerical error occurs, please notify me as soon as possible.

Midterm Tests

Dates: The midterms will be written during class. The first midterm will take place on February 05 (in class, **3-5pm and 5-7pm**), the second takes place on March 19 (again, in class, **3-5pm and 5-7pm**). Exam room locations will be announced in class and on the course webpage. **Important: the test locations will differ from your regular classroom locations! Note also the times!**

Term Test Coverage: If a concept, skill, or topic is addressed in lectures, readings, or on Blackboard, then it is testable. Additionally, you are required to follow current events.

Missing a Midterm Test:

Midterms are crucial components of our course, and they are compulsory. If you cannot complete the tests as scheduled, consider re-taking the course when you are able.

No make-up tests are offered for missed midterms. A missed midterm counts as 0. When you miss a midterm for legitimate reasons, I will shift the weight of the missed midterm to the final exam. To receive this accommodation, (a) you will be required to complete a midterm test at home and (b) you must obtain a score of 30% on this test. Your take-home test will be reviewed to assess whether you obtain 30%, but it will not be graded further.

If you miss a midterm, please follow the steps as outlined below.

Step 1: Send an e-mail to Professor Malinova meeting **all** of the following specifications.

- (a) Your e-mail must be sent **before** the start of the missed test. (In cases of extreme emergencies, e.g. a traffic accident, up to 24 hours will be allowed.)
- (b) The subject line must be "ECO359: missed test".
- (c) The e-mail is sent from your U of T account (i.e., not gmail, yahoo, etc.)
- (d) It concisely explains why you missed the test.
- (e) It lists all the other courses that you are currently taking, with the times these courses meet and the names and contact information of your other professors. It identifies all term work (e.g., tests, class attendance, homework assignments) that you have submitted or will submit in other courses during the week of

your missed test or it says “no other term work was submitted and no classes were/will be attended during the week of my missed test.”

- (f) The last sentence is “I understand that it is a punishable academic offence to present false information in support of my request for accommodation for missed term work”.
- (g) The e-mail concludes with your name and student number.
- (h) The writing is clear and appropriate for an academic setting. Everything except the last sentence must be written in your own words.

Step 2: You will receive an e-mail from Professor Malinova within 24 hours of your e-mail with a notification of your take-home test time frame. You will be required to pick up a copy of the test in person from the Department of Economics (you will be given at least a 24-hour notice). Failure to check your e-mail or to pick up your test in time will not be considered legitimate excuses for not being able to complete the take-home test.

Step 3: Complete the take-home test during your take-home time frame and return it to the Department of Economics (reception), Max Gluskin House, 150 St. George Street, within your take-home test time window.

- (a) Your take-home term test will be reviewed, but the score will not count toward your course grade beyond the assessment of whether or not you have obtained a score of 30%.
- (b) If you receive a score of 30% or higher on the take-home test, then the weight of the missed term test will be shifted to the final. If you receive a score of 29% or lower, then your missed term test will be assigned a score of 0.

Problem Sets

There will be no graded problem sets, however sample (“practice”) problems, with answers and hints to select questions, will be made available to you. While these problems are helpful to check whether you understand the concepts taught in lecture, doing practice problems alone are not sufficient to gain deep understanding of the material that is required in this course. Furthermore, you must aim to provide full length solutions on your own prior to checking the answers that are provided to you.

Email Communication

I will use Blackboard to post and to send out announcements. It is imperative that you **update your email-address on ROSI** and *that you register on ROSI with a U-of-T-email-address!*

Students must consult the course outline, other handouts and the course website **BEFORE** submitting inquiries by email. If your question is not addressed in any of the course materials, please send an e-mail to Ding Ding (d.ding@utoronto.ca), cc'd to me, outlining your question. Where a question cannot easily or briefly be answered with a reply email (e.g., it requires that we solve a lengthy practice problem prior to responding), we will simply indicate to you that we will need to chat during the announced office hours.

We will reply to legitimate email inquiries from students within two working days. If you do not receive a reply within this period, resubmit your question(s). We will not answer emails over the weekend (Friday 17:00 – Monday 10:00), and we will not answer emails in the last 36 hours before a test.

Each email message must include in the “subject” the course number and a concise and clear statement of purpose. In the first few weeks of class, please include your *full name* and your *student number* in your message. Do NOT send any attachments with your email messages.

Information about the Blackboard System — The Official Statement from the University

The following is the university’s official statement; not corrected for typographical errors.

Logging in to your Blackboard course website. Like a many other other courses, ECO359 uses Blackboard for its course website. To access the ECO359 website, or any other Blackboard-based course website, go to the UofT portal login page at portal.utoronto.ca and login using your UTORid and Password. Once you have logged in to the portal using your UTORid and Password, you’ll find the link to ECO359 course website along with the link to all your other Blackboard-based courses.

Activating your UTORid and password. If you need information on how to activate your UTORid and set your password for the first time, please go to www.utorid.utoronto.ca. Under the “First Time Users” area, click on “activate your UTORid” if you are new to the University or “create your UTORid” if you are a returning student, then follow the instructions. New students who use the link to “activate your UTORid” will find reference to a “Secret Activation Key”. This was originally issued to you when

you picked up your T-card at the library. If you have lost your “Secret Activation Key” you can call 416-978-HELP or visit the Help Desk at the Information Commons on the ground floor of Robarts library to be issued a new one. **The course instructor will not be able to help you with this.** 416-978-HELP and the Help Desk at the information commons can also answer any other questions you may have about your UTORid and Password.

Email communication with the course instructor. At times, the course Instructor may decide to send out important course information via email. To that end, all UofT students are required to have a valid UofT email address. You are responsible for ensuring that your UofT email address is set up AND properly entered in the ROSI system. You can do that by using the following instructions:

To submit the information to activate your UTORid and Password (see above), you will need to click the “Validate” button. Follow the instructions on the subsequent screens to receive your utoronto.ca address. Once you have your UofT email address go to the ROSI system, (www.rosi.utoronto.ca) log in and update the system with your new institutional email address.

You can check your UofT email account from either

1. The UofT home page <http://www.utoronto.ca/> (Choose “quick links” - choose “myutoronto.ca” - enter your UTORid and Password - choose “webmail” Or
2. Via Outlook, Mozilla etc. Visit the helpdesk at the information commons for help with the set up.

Forwarding your utoronto.ca email to a hotmail, gmail, yahoo mail or other types of accounts is not advisable. In many cases, hotmail/gmail/yahoo automatically filters email from any utoronto.ca address into the junk mail folder. Therefore emails from your course instructor will end up in your junk mail folder.

You are responsible for:

1. Ensuring you have a valid UofT email address that is properly entered in the ROSI system
2. Checking your UofT email account on a regular basis.

The official statement ends.

Tentative Course Structure

Specific literature and book chapter references will be posted on the course website. Please check the webpage regularly to obtain the most up-to-date course information.

Week 1 Introduction, Basic investments.

Week 2 Basic of accounting and balance sheet analysis, NPV and other investment valuation tools; basics of real options.

Week 3 Capital Budgeting under uncertainty. Background on long-term financing.

Week 4 Modigliani-Miller: Capital Structure.

Week 5 Midterm I.

Week 6 Modigliani Miller and Dividend Policy, an overview of Agency Costs.

Week 7 Managerial Effort and Capital Structure; optimal contracting with debt and equity; a case study on how financial leverage promotes internal change.

Week 8 Background on Air Canada's restructuring; Underinvestment: The Debt Overhang Problem.

Week 9 Corporate Governance.

Week 10 Midterm II.

Week 11 Mergers and Acquisitions.

Week 12 Initial Public Offerings; Overview and popular models.

Literature

The main text:

- Ross, Westerfield, Jaffe, Roberts: *Corporate Finance*, McGraw-Hill. 6th Canadian Edition. Hereafter: RWJR.

Earlier editions are acceptable for background reading, but keep in mind that practice problems will be assigned from the latest (6th) edition.

Optional Reading:

A helpful textbook, which is a classic text and your choice for a second opinion, is

- Thomes Copeland and Fred Weston: *Financial Theory and Corporate Policy*, Addison-Wesley.

If you would like to have a look at a more advanced text, check

- Jean Tirole: *The Theory of Corporate Finance*, 2006, Princeton University Press. This is a great textbook; it covers much more than this course, but some topics that are covered (specifically those in the second half of the course), are explained very nicely.

As the course progresses, I will update the reference list for each lecture. Please check the portal's webpage frequently.