

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.

Course Webpage: <http://portal.utoronto.ca>

Office Hours: To be announced on the portal.

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.

TA Support. Our teaching assistant for the course is David Cimon (david.cimon@mail.utoronto.ca), a PhD student in financial economics. His office hours will be announced on the portal.

Exceptions to Class and OH Times

There will be the following exceptions to class times above:

1. The first lecture (January 07, 2014) will take place at 2-4pm and 5-7pm.
2. Your term tests (Feb 04 and March 18) will take place 3-5pm and 5-7pm. Locations: TBA.
3. Regular office hours are held until the last lecture (i.e., through April 01), 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.

Tests, Exams, and Grade Composition

There will be three exams: two in-class midterm tests (2 hour-long 3-5pm and 5-7pm on February 04 and on March 18; check the course webpage for the test locations) 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 your worst midterm score is 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.

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.

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.

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 David Cimon (david.cimon@mail.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.

Do NOT send any attachments with your email messages.

Information about the Blackboard System

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. 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.

Midterm Tests

Dates: The midterms will be written during class. The first midterm will take place on February 04 (in class, **3-5pm and 5-7pm**), the second takes place on March 18 (again, in class, **3-5pm and 5-7pm**). Exam room locations will be announced 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, in problem sets, 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. No make-up tests are offered for missed midterms, and 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 make-up midterm test at home and (b) you must obtain a score of 30% on this take-home 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) Except for cases of extreme emergencies, your e-mail must be sent **before** the start of the missed test.
- (b) The e-mail is sent from your U of T account (i.e., not gmail, yahoo, etc.).
- (c) Your e-mail concisely explains why you are missing/have missed the test (e.g., it states that you are ill).
- (d) 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 with a weight of more than 10% of your course grade (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.”

- (e) The last sentence is “I understand that it is a punishable academic offense to present false information in support of my request for accommodation for missed term work”.
- (f) The e-mail concludes with your name and student number.

Step 2: You will receive an e-mail from Professor Malinova within 48 hours of your e-mail with a notification of your take-home test time frame (typically, you will be told the earliest possible time for you to pick up the test and the deadline to return in; you will be given at least a 24-hour notice). You will be required to pick up a copy of the test and an academic integrity check-list in person from the Department of Economics. 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 together with a completed academic integrity check-list to the Department of Economics (reception), Max Gluskin House, 150 St. George Street.

- (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.

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.