

ECO359H1S Financial Economics II: Corporate Finance
Department of Economics
University of Toronto

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Office Hours: Wednesday 12-2pm at Max Gluskin House 329 (GE 329), 150 St. George Street

COURSE OUTLINE

ECO359 is an introduction to the theory, empirical evidence and practice of Corporate Finance. Students will learn about a set of financial decisions involving corporations. The main focus of the course will be on capital budgeting, capital structure and payout policy. We will also study mergers and acquisitions as well as initial public offerings. The main questions we will address in this course are the following:

- *What projects should the firm invest in?* (the capital budgeting decision)
- *How should the firm raise funds to finance its investments?* (the financing decision)
- *What fraction of its profits should the firm pay out to its shareholders?* (the payout policy decision)

In answering these questions, we will deal with some classic topics in economics such as discounting and the net present value of future payoffs, personal and corporate taxation, financial distress and asymmetric information. The lecture material will discuss the issues, develop the theory we use to understand these issues, examine the empirical evidence, and reflect on several practical aspects using real-world examples.

COURSE INFORMATION

Class Time: Wednesdays. Section L0101: 2-5pm. Section L5101: 5-8pm.
Class Location: WI1017 for Section L0101. LM162 for Section L5101.
Term Tests: February 8 and March 22 during class time in rooms TBA.
Prerequisite: ECO358H1
Exclusion: ACT349H1, RSM333H1

ASSESSMENT

Assessment for this course is based on the following components:

- Midterm Test 1 – **February 8, Location TBA:** 30%
- Midterm Test 2 – **March 22, Location TBA:** 30%
- Final examination – **Date and Location TBA** 40%

Note: The midterm tests will take place **3-5pm for Section L0101** and **5-7pm for Section L5101**. **The location of the midterm tests will be announced in class and on the portal.**

Each midterm test will last 2 hours. The final exam will last 3 hours.

If your grade on the final exam is better than the grade on your worst midterm test, and your worst midterm test grade is 30% or higher, then the weight on your final exam will be 70% and the weight on your worst midterm test will be 0%. For this rule to apply, the grade on your worst midterm test must be 30% or higher. If your worst midterm test grade is below 30%, no weight redistribution will occur.

Midterm Test Coverage

You are responsible for all material discussed in class, posted on Blackboard or assigned in the lectures. This includes textbook chapters, lecture handouts and problem sets.

Midterm test 1 will cover all material taught up to that date (weeks 1-4).

Midterm test 2 will cover all material taught up to that date beginning with the material after midterm test 1 (weeks 6-9).

The final exam will cover all material taught in this course.

Missing a Midterm Test

Midterm tests are a compulsory part of your assessment. If you miss a midterm test, your grade will be 0. However, if you miss one midterm test for legitimate reasons, the weight will shift to the final exam. In this case, you must provide supporting documentation within a week of the missed test. In the event of illness, you must provide a medical note (original, i.e., neither scanned nor emailed). The only accepted note is a fully completed *University of Toronto Verification of Student Illness or Injury form*. See <http://www.illnessverification.utoronto.ca> for details. The form must be completed by a qualified medical doctor or nurse practitioner (i.e., not an acupuncturist, chiropractor, or other health care professional). The doctor's OHIP registration number must be provided.

Appeals

If you appeal to re-grade one of the midterm questions, we will re-grade the entire midterm test. This may lead to a lower or higher overall grade. Your complaint has to be in writing, it must be submitted within two weeks from the day that graded midterms become available for pick-up, and it must explain why you believe the grading is incorrect. These conditions do not apply to clerical

errors (i.e., adding your scores incorrectly). If a clerical error occurs, please notify Professor Tsiakas as soon as possible.

TEXTBOOK AND LECTURE HANDOUTS

“Fundamentals of Corporate Finance” by Brealey, Myers, Marcus, Mitra, Maynes and Lim. 6th Canadian Edition. McGraw-Hill Ryerson 2016

You may use the Connect with Smartbook Online Access or the print version.

If you use a different edition of the textbook, you will be responsible for reconciling the differences.

Detailed lecture handouts and problem sets will be posted in advance on Blackboard. To access the ECO359 website, go to the UofT portal login page at portal.utoronto.ca and login using your UTORid and Password.

The problem sets will not be graded. In every topic, once we complete our discussion of the lecture handouts, we will try to solve as many questions from the assigned problem set. However, you are advised to solve the questions of the problems sets on your own in advance so you can benefit from our discussion.

Note that the problem sets will be taken by the instructor. We will not have separate tutorials run by TAs.

LECTURE TIMETABLE

INTRODUCTION (Week 1)

- Course Outline

TOPIC 1: Review (Week 2)

- Financial Calculus
 - Compounding and future value
 - Discounting and present value
 - Annuities and perpetuities
- Problem Set 1

TOPIC 2 (Weeks 3 and 4)

- Capital Budgeting
 - Net present value (NPV)
 - Internal rate of return (IRR)
 - Other project evaluation methods (e.g., payback method)
- NPV in action: a detailed example
- Problem Set 2

TERM TEST 1 (Week 5)

TOPIC 3 (Weeks 6 and 7)

- Financing and Capital Structure
 - Irrelevance proposition in perfect capital markets
 - The role of corporate taxes
 - The role of personal taxes
 - The role of bankruptcy and costs of financial distress
 - The role of asymmetric information
 - Weighted Average Cost of Capital (WACC)
 - Empirical evidence
- Problem Set 3

TOPIC 4 (Weeks 8 and 9)

- Payout Policy
 - Dividends vs. share repurchases
 - Irrelevance proposition in perfect capital markets
 - The role of personal taxes
 - The role of asymmetric information
 - Empirical evidence

- Problem Set 4

TERM TEST 2 (Week 10)

TOPIC 5 (Week 11)

- Mergers and Acquisitions
 - Vertical/horizontal; Friendly/hostile
 - Synergies and valuation of mergers
 - Empirical evidence

- Problem Set 5

TOPIC 6 (Week 12)

- Initial Public Offerings
 - Initial public offerings
 - Seasoned equity offerings
 - Empirical evidence

- Problem Set 6

- Final exam review and additional problems

ACADEMIC INTEGRITY AND RESPECT

Academic integrity is fundamental to learning and scholarship at the University of Toronto. Participating honestly, respectfully, responsibly, and fairly in this academic community ensures that the U of T degree that you earn will be valued as a true indication of your individual academic achievement, and will continue to receive the respect and recognition it deserves. As a result, the University treats cases of cheating and plagiarism very seriously.

Familiarize yourself with the University of Toronto's Code of Behaviour on Academic Matters (<http://www.governingcouncil.utoronto.ca/policies/behaveac.htm>). It outlines the behaviours that constitute academic dishonesty and the processes for addressing academic offences. Potential offences include, but are not limited to:

On tests and exams:

- Using or possessing any unauthorized aid, including a cell phone.
- Looking at someone else's answers.
- Letting someone else look at your answers.
- Misrepresenting your identity.
- Submitting an altered test for re-grading.

Misrepresentation:

- Falsifying or altering any documentation required by the University, including doctor's notes.
- Falsifying institutional documents or grades.

The University of Toronto treats cases of academic misconduct very seriously. All suspected cases of academic dishonesty will be investigated following the procedures outlined in the Code. The consequences for academic misconduct can be severe, including failing the course and a note on your transcript. If you have any questions about what is or is not permitted in this course, please do not hesitate to contact me. If you are experiencing personal challenges that are having an impact on your academic work, please speak to me or seek the advice of your college registrar.

Finally, 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 behaviours.

RESOURCES

Academic Success Centre: <http://www.studentlife.utoronto.ca/asc>

Accessibility Services: <http://accessibility.utoronto.ca>

Counseling & Psychological Services: <http://caps.utoronto.ca/>

College Registrars' offices: <http://uoft.me/advising>

English Language Learning: <http://www.artsci.utoronto.ca/current/advising/ell>

Office of Student Academic Integrity: <http://www.artsci.utoronto.ca/osai>

Rights & Responsibilities: <http://uoft.me/rights>

Writing help: <http://www.writing.utoronto.ca/>