Fall 2012

Finance 423: Financial Analysis and Management

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Office Hours: MW: 10:30 am – Noon or by appointment

COURSE OBJECTIVE

To explore the role of the finance function in a shareholder value based framework. This framework recognizes that choosing between corporate strategic initiatives involves a balance between finance, marketing and operating decisions of a firm. The course will provide a comprehensive understanding of: financial analysis and planning; investment, capital structure, and cash disbursement decisions; valuation and corporate restructuring.

Student Learning Outcomes (SLOs)
• Develop a comprehensive understanding of key financial drivers of shareholder value
• Develop a comprehensive understanding of financial statements, analysis of financial performance, and determinants of growth
• Develop a comprehensive understanding of firm financial needs, sources and terms of financing alternatives
• Develop a comprehensive understanding of the drivers and evaluation of firm investment decisions
• Develop an understanding of how finance, marketing, and operations must work in concert to enhance shareholder value

These SLOs are related to the BSBA program goals of effective communication, critical thinking, understanding ethical and global perspectives, and acquisition of essential business knowledge.

Required Material

Course Prerequisites:
FIN 321: Managerial Economics, FIN 325: Intermediate Finance, and

Grading Standard
1. Mid-term Exam 40%
2. Case Assignments 40%
3. Class Participation 20%
<table>
<thead>
<tr>
<th>Dates</th>
<th>Assignment</th>
</tr>
</thead>
<tbody>
<tr>
<td>August 27</td>
<td>Introduction</td>
</tr>
</tbody>
</table>
| August 29, Sep 5 | Interpreting Financial Statements  
Higgins, Ch. 1: Problems 4, 6, 9, 11 |
| September 10, 12 | Evaluating Financial Performance  
Higgins, Ch. 2: Problems 5,7 |
| September 17 | *Case: Assessing a Company’s Future Financial Health*                        |
| September 19 | *Case: Sears, Roebuck & Co. vs Wal-Mart Stores, Inc.*                        |
| September 24 | Financial Forecasting  
Higgins, Ch. 3: Problems 8, 9, 10 |
| September 26 | *Case: Jones Electrical Distribution*                                        |
| October 1    | *Case: Tire City, Inc.: Questions 2, 3*                                     |
| October 3    | Managing Growth  
Higgins, Ch. 4: Problems 4, 8                                               |
| October 8, 10| Valuation  
Higgins, Ch. 9: Problems 7, 11                                               |
| October 15   | *Case: Google Inc.’s Acquisition of AdMob: Questions 1,4*                   |
| October 17   | *Case: Commercial Fixtures, Inc*                                             |
| October 22, 24 | **MID-TERM EXAM – Parts I & II**                                             |
| October 29, 31| Financing Decision  
Higgins Ch. 5: Problems 6, 7  
Higgins Ch. 6: Problems 11, 12 |
| November 5   | *Case: Debt Policy at UST*                                                  |
| November 7   | *Case: Marriott Corp.: Cost of Capital; Questions:3, 6, 7*                  |
| November 14, 19 | Investment Decision  
Higgins Ch. 7: Problems 3, 7  
Higgins Ch. 8: Problems 3, 9 |
| November 26  | *Case: Flash Memory, Inc.: Questions 1, 2*                                  |
| November 28  | *Case: Diamond Chemicals PLC (A)*                                            |
| December 3, 5| M&A and Corporate Restructuring  
Higgins Ch. 9: Problems 2, 3, 6  
*Case: Takeover of Norton Co.* |
Case Preparation Questions

Jones Electrical Distribution
1. How well is Jones Electrical Distribution performing?
2. What drove the increase in Jones’s accounts receivable and inventory balances in 2005 and 2006?
3. Is Nelson Jones’s estimate that a $350,000 line of credit is sufficient for 2007 accurate?
4. When will Jones be able to repay the line of credit?
5. What could Jones do to reduce the size of the line of credit he needs?

Tire City, Inc.
1. Evaluate Tire City’s financial health. How is the company performing?
2. Based on Mr. Martin’s prediction for 1996 sales of $28.206 million, and for 1997 sales of $33.847 million and relying on the other assumptions provided in the case, prepare proforma income statements and balance sheets for 1996, 1997. Assume any financing required will be in the form of bank debt; assume all debt bears an interest rate of 10%.
3. Using your set of proformas, assess the financial health of Tire City as of year-end 1997.
4. As a lender would you be willing to loan funds needed to expand its warehouse facilities and finance its growth? Why or why not?

Sears Roebuck & Co. v/s Wal-Mart Stores, Inc.
1. How do the retailing strategies of Sears and Wal-Mart differ?
2. Wal-Mart’s average ROE for the 1997 fiscal year was 19.7% $3525/($18,503+$17,143)/2 while Sears’ average ROE over roughly the same period was 22.0% $1188/($5862+$4945)/2. Don Edwards was puzzled by these numbers because of Wal-Mart’s reputation as a premier retailer and Sears’ financial difficulties not long ago. What is driving the performance of these two companies during fiscal 1997?
3. What ratios are most important in assessing current and predicting future value creation for Sears? For Wal-Mart?
4. How useful are financial ratios in evaluating the current performance of each of the two companies?
5. How useful are financial ratios in evaluating the relative performance of each of the two companies?

Google Inc.’s Acquisition of AdMob
1. How do investors evaluate young technology companies such as Google and how do these investor evaluations in turn impact management decisions?
2. What is the role of acquisitions in Google’s growth strategy?
3. Evaluate the structure of the online advertising market as well as the structure of the mobile advertising segment (within the online advertising market).
4. How is AdMob positioned in the mobile advertising market segment?
5. How would you value AdMob at the end of 2009:
   (i) as a stand-alone firm, and
   (ii) as an acquisition target.

Commercial Fixtures, Inc.
1. What do you expect Albert Evans to bid for Gordon’s half interest? Why?
2. What should Gordon Whitlock bid for Albert’s half interest? Why?
3. What would you as an outside third party bid under the same conditions for the entire company (both halves)? Why?
4. How would you structure the purchase of the business?

Debt Policy at UST
1. What are the primary business risks associated with UST, Inc.? What are the attributes of UST, Inc.? Evaluate from the viewpoint of a bondholder.
2. Why is UST considering a leveraged recapitalization after such a long history of conservative debt policy?
3. Should UST undertake the $1 billion recapitalization? Calculate the marginal (or incremental) effect on UST’s value assuming that the entire recapitalization is implemented immediately (January 1, 1999).
   (a) Assume a 38% tax rate.
   (b) Prepare a pro-forma income statement to analyze whether UST will be able to make interest payments.
   (c) For the basic analysis, assume the $1 billion in new debt is constant and perpetual. Should UST alter the new debt via a different level or a change in the amount of debt through time.
4. UST Inc. has paid uninterrupted dividends since 1912. Will the recapitalization hamper future dividend payments?

Marriott Corp: Cost of Capital
1. Are the four components of Marriott’s financial strategy consistent with its growth objective?
2. How does Marriott use its estimate of cost of capital? Does this make sense?
3. What is the WACC for Marriott?
4. What types of investments would you value using Marriott’s WACC?
5. If Marriott used a single corporate hurdle rate for evaluating investment opportunities in each of its lines of business, what would happen to the company over time?
6. What is the cost of capital for the lodging and restaurant divisions of Marriott?
7. What is the cost of capital for Marriott’s contract services division?

Diamond Chemicals PLC (A)
1. What changes, if any, should Lucy Morris ask Frank Greystock to make in his DCF analysis? Why? What should Morris be prepared to say to the Transport Division, the Director of Sales, her assistant plant manager and the analyst from the Treasury Staff?
2. How attractive is the Merseyside project? By what criteria?
3. Should Morris continue to promote the project for funding?

Flash Memory, Inc.
1. Assuming the company does not invest in the new product line, prepare forecasted income statements and balance sheets at year-end 2010, 2011, and 2012. Based on these forecasts, estimate Flash’s required external financing: in this case all required external financing takes the form of additional notes payable from its commercial bank, for the same period?
2. What course of action do you recommend regarding the proposed investment in the new product line? Should the company accept or reject this investment opportunity?
3. How does your recommendation from question 2 impact your estimate of the company’s forecasted income statements and balance sheets, and required external financing in 2010, 2011, and 2012? How do these forecasted income statements and balance sheets differ if the company relies solely on additional notes payable from its commercial bank, compared to a
sale of new equity?
4. As CFO Hathaway Browne, what financing alternative would you recommend to the board of directors to meet the financing needs you estimated in questions 1 – 3 above? What are the costs and benefits of each alternative?

Takeover of Norton Co.
1. Evaluate Norton Co. as a takeover target by BTR plc relative to BTR’s strategy as formulated in the mid-1960s.
2. Owen Green, Chairman of BTR “anticipated that Norton would fetch full price.” Discuss.
3. In light of valuation estimates of Norton in appendix 1, how should BTR formulate its bid for Norton Co. – magnitude and financing of its bid.