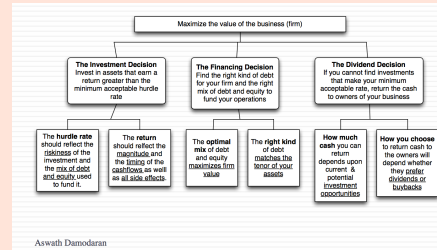


Corporate Finance BIG PICTURE



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What is Corporate Finance?

Investment Decision--

The **hurdle rate** to reflect the riskiness of the investment and the mix of debt and equity used to fund it.

The **return** should reflect the magnitude and the timing of the cashflows as well as all side effects.

What is Corporate Finance? (cont)

Financing Decision--

The **optimal mix** of debt and equity maximizes firm value, also:
the **right kind of debt matches the tenor** of your assets.

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What is Corporate Finance? (cont)

Dividend Decision--

How much cash can you return? and

How you choose to return cash to the owners should it be dividend or buybacks?

Themes of Corporate Finance

1. Corporate finance is **common sense**



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Themes of Corporate Finance (cont)

2. Corporate finance is **focus** on maximizing the value of the business.

Themes of Corporate Finance (cont)

3. The focus of the Corporate finance in corporate finance **changes** across the life cycle.



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Themes of Corporate Finance (cont)

4. Corporate finance is **universal** (Small/large, public/private, US/emergent)

Themes of Corporate Finance (cont)

5. If you violate first principles, you will pay a price (no matter who you are)

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Who owns/runs your firm?

Case 1: Splintering of Stockholders (Disney)

Who owns/runs your firm? (cont)

Case 2: Voting versus Non-voting shares & Golden Shares. (Vale)

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Who owns/runs your firm? (cont)

Case 3: Pyramid holdings (Tata)

Who owns/runs your firm? (cont)

Case 4: Legal rights & COrporate Structures (Baidu)



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Examples of Companies

1. Institutional Default (No body will push for you - Disney 2003)

Examples of Companies (cont)

2. Self Holdings (Largest holder is the company itself - China Mobile Ltd)

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Examples of Companies (cont)

3. The Government Influence (Vale - GDF Suez)

Examples of Companies (cont)

4. Different voting rights (Facebook, Google, LinkedIn)

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Examples of Companies (cont)

5. Family Group Company (Tata, LVMH)

Examples of Companies (cont)

6. Founders hang on (Las Vegas Sands Corp, Microsoft)

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Examples of Companies (cont)

7. Corporate Cross Holdings (Lufthansa owns Jet Blue)

Examples of Companies (cont)

8. Activist Investors (Danone SA - Triun fund management)

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Measuring Market Risks

Step 1: Defining Risk		
The risk in an investment can be measured by the variance in actual returns around an expected return.	Low Risk Investment	High Risk Investment
EV	EV	EV
Step 2: Differentiating between Residual and Unsystematic Risk		
Can one's overall investment (the portfolio) be diversified away in a portfolio of stocks? Can the investment be diversified away in a portfolio of stocks? Can the investment be diversified away in a portfolio of stocks?	Can one's overall investment (the portfolio) be diversified away in a portfolio of stocks? Can the investment be diversified away in a portfolio of stocks? Can the investment be diversified away in a portfolio of stocks?	Can one's overall investment (the portfolio) be diversified away in a portfolio of stocks? Can the investment be diversified away in a portfolio of stocks? Can the investment be diversified away in a portfolio of stocks?
Step 3: Measuring Market Risk		
The CAPM	The Beta	Market Risk
1. The market return is the return on a portfolio of all stocks in the market. 2. The market return is the return on a portfolio of all stocks in the market. 3. The market return is the return on a portfolio of all stocks in the market.	1. The beta of a stock is the measure of its sensitivity to the market return. 2. The beta of a stock is the measure of its sensitivity to the market return. 3. The beta of a stock is the measure of its sensitivity to the market return.	1. Market risk is the risk that affects all stocks in the market. 2. Market risk is the risk that affects all stocks in the market. 3. Market risk is the risk that affects all stocks in the market.
Step 4: Using Beta to Measure Market Risk	Step 5: Using Beta to Measure Market Risk	Step 6: Using Beta to Measure Market Risk
1. Beta is a measure of the sensitivity of a stock's returns to the market return. 2. Beta is a measure of the sensitivity of a stock's returns to the market return. 3. Beta is a measure of the sensitivity of a stock's returns to the market return.	1. Beta is a measure of the sensitivity of a stock's returns to the market return. 2. Beta is a measure of the sensitivity of a stock's returns to the market return. 3. Beta is a measure of the sensitivity of a stock's returns to the market return.	1. Beta is a measure of the sensitivity of a stock's returns to the market return. 2. Beta is a measure of the sensitivity of a stock's returns to the market return. 3. Beta is a measure of the sensitivity of a stock's returns to the market return.

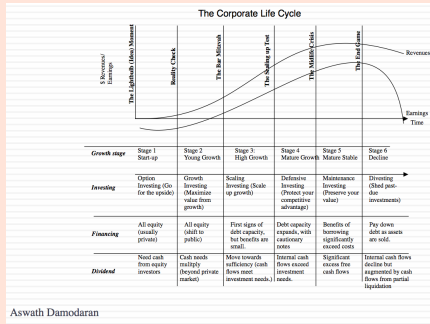


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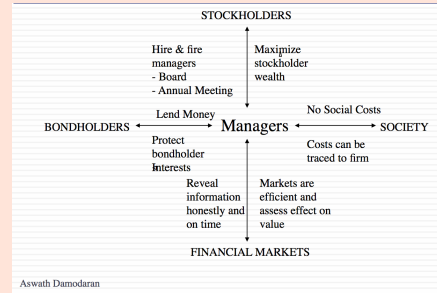
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Life Cycle of Corporation



Classical Objective Function

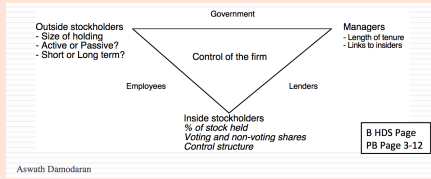


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Who owns/runs your firm?



Solutions to failed corporate financial theory

Assign responsibility for monitoring managers to someone other than stockholders.

Who are the top stockholders? Any potential conflicts of interests?

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Solutions to failed corporate financial theory (cont)

Choose **different objective**

maximize earnings, maximize revenues, maximize market share.

Expected Return

Expected Return = Riskfree Rate + Beta * (Expected Return on the Market Portfolio - Riskfree Rate)

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Company Profiles

	Assets	Debt	Yield (pre-tax)	Tax Rate	WACC (Case A)
Unlevered	100%	0%	10%	40%	10%
Levered	100%	30%	10%	40%	10%
Unlevered	100%	0%	10%	40%	10%



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