

Strategic Financial Management

10056 ECON 5040 – R11

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Department of Economics

Prof. Erick W. Rengifo

Office: Dealy E-513, extension X4061

Email: rengifomina@fordham.edu

Office Hours: By appointment

Website: www.fordham.edu/economics/rengifo

The aim of this course is to present the tools and techniques that will allow the students to think strategically when facing financial problems inside or outside a given firm. The course will start analyzing the basic functions of the treasurer and controller of the firm: the information they must know along with their interpretation and use.

To understand the functions of the treasurer, the most important tools to learn are based on financial mathematics which will be helpful to understand the time value of money, to understand how cash flows in different periods should be compared and how this mathematics can be used in a firm to maximize its value or, from an investor perspective, to determine the firm's value. Moreover, it will be introduced the way in which short and long term debt instruments are valued and how the CFO can use them in behalf of the firm.

Related to the controller's function, the course will present an exposition of the cost of capital, how a given capital structure can influence the future investment and financial decisions and, how these decisions exert an influence on the actions of different financial agents (investors and lenders). For this, a brief introduction to financial accounting will be presented in order to familiarize the students with the basic financial statements, with the way these statements are constructed, showing what is the relationship among the different components of each statement and, most importantly, what kind of information can be obtained from them and how they can be used.

Finally, with the knowledge of the previous topics, the course will cover the basics of firm valuation under uncertainty. For this, some game theory will be presented and discussed in class, focusing on its empirical application and how this can help to perform financial strategies to maximize the firm value.

The grade will be based on:

Class participation	25%
Three exams	75%

The content of the exams will be based on the topics covered during the previous week of class with a focus on strategic decisions that potentially could help the firm to maximize its value. The time of each exam will be of 30 minutes. The class participation is crucial as soon as it will allow the spread of opinions and experiences that will increase the class quality. Open questions and real case problems are encouraged during the whole class.

Some interesting readings related to the topics to be covered in the present course are presented below.

I. Empirical Measurement in Corporate Finance

1. F. Modigliani and M. H. Miller, "The Cost of Capital, Corporation Finance and the Theory of Investment." *AER* 48 (1958), 261-297.
2. R. W. Masulis, "Leverage Ratios and Financing Decisions: The Empirical Evidence." *The Debt/Equity Choice* Ch. 1
3. R. W. Masulis, "Capital Structure Change and Its Relation to Firm Value." *The Debt/Equity Choice* Ch. 2
4. R. Thompson, "Empirical Methods of Event Studies in Corporate Finance." R. Jarrow et al., Eds, *Handbooks in OR & MS*, Vol. 9 (1995), 963-992.

II. Debt and Taxes

1. R. W. Masulis, "Tax Effects of Capital Structure." *The Debt/Equity Choice* Ch. 3
2. J. R. Graham, "Proxies for the Corporate Marginal Tax Rate." *Journal of Financial Economics* 42 (1996), 187-221.
3. H. DeAngelo and R. W. Masulis, "Optimal Capital Structure Under Corporate and Personal Taxation." *Journal of Financial Economics* 8 (1980), 3-29.
4. J. K. MacKie-Mason, "Do Taxes Affect Corporate Financing Decisions?" *The Journal of Finance* 45 (1990), 1471-1493.

III. Corporate Dividends

1. LaPorta, et. al. "Agency Problems and Dividend Policies Around the World," *Journal of Finance* 55 (2000) pp. 1-33.
- *2. M. Frank and R. Jagannathan, "Why Do Stock Prices Drop by Less Than the Value of the Dividend? Evidence from a Country Without Taxes." Federal Reserve Bank of Minneapolis Research Department Staff Report 229 (1997).
3. F. Allen and R. Michaely, "Dividend Policy." R. Jarrow et al., Eds, *Handbooks in OR & MS*, Vol. 9 (1995), 963-992.

IV. SEO's and IPO's

1. T. Loughran and J. R. Ritter, "Why Don't Issuers Get Upset About Leaving Money on the Table in IPOs?" *The Review of Financial Studies* 15 (2002), 413-443.
2. A. Safieddine and W. J. Wilhelm, Jr., "An Empirical Investigation of Short-Selling Activity Prior to Seasoned Equity Offerings." *The Journal of Finance* 51 (1996), 729-749.
3. B. E. Eckbo and R. W. Masulis, "Seasoned Equity Offerings: A Survey." R. Jarrow et al., Eds, *Handbooks in OR & MS*, Vol. 9 (1995), 1017-1072.

4. R. G. Ibbotson and J. R. Ritter, "Initial Public Offerings." R. Jarrow et al., Eds, Handbooks in OR & MS, Vol. 9 (1995), 993-1016.

V. Alternate Valuation Plans

1. Booth et. al., "Capital Structures in Developing Countries," Journal of Finance 56 (2001), pp. 87-130.

*2. K. J. Leslie and M. P. Michaels, "The Real Power of Real Options." The McKinsey Quarterly, 1997 Number 3.

3. E. Teach, "Will Real Options Take Root?" CFO Magazine, July 2003.

4. W. Carl Kester, "Today's Options for Tomorrow's Growth." Harvard Business Review (1984), 153-163.

5. L. Trigeorgis, "Real Options and Interactions with Financial Flexibility." Financial Management (1993), 202-224.

6. P. G. Berger, E. Ofek and I. Swary, "Investor Valuation of the Abandonment Option." Journal of Financial Economics 42 (1996), 257-287.

VI. Bankruptcy

1. L. W. Senbet and J. K. Seward, "Financial Distress, Bankruptcy and Reorganization." R. Jarrow et al., Eds, Handbooks in OR & MS, Vol. 9 (1995), 921-961.

2. E. S. Hotchkiss, "Postbankruptcy Performance and Management Turnover." The Journal of Finance 50 (1995), 3-21.

VII. Agency Problems in Corporate Finance

1. R. W. Masulis, "Debt/Equity Agency Costs" The Debt/Equity Choice Ch. 5

2. R. W. Masulis, "Stockholder-Manager Conflicts of Interest" The Debt/Equity Choice Ch. 6

*3. M. C. Jensen, "Agency Costs of Overvalued Equity and the Current State of Corporate Finance." European Financial Management 10 (2004), 549-565.

4. A. V. Thakor, "Game Theory in Finance." Financial Management (1991)

5. M. C. Jensen, "Agency Costs of Free Cash Flow, Corporate Finance, and Takeovers." AER 76 (May 1986), 323-329.

VIII. Bank Lending

1. E. F. Fama, "What's Different About Banks?" Journal of Monetary Economics 15 (1985), 29-39.

2. T. F. Cosimano and B. McDonald, "What's Different Among Banks?" *Journal of Monetary Economics* 41 (1998), 57-70.
3. P. Breuer, "Measuring Off-balance-sheet Leverage." *Journal of Banking & Finance* 26 (2002), 223-242.
4. J. H. Boyd and M. Gertler, "Are Banks Dead? Or Are the Reports Greatly Exaggerated?" NBER Working Paper 5045 (1995).