
Updated 1st March 2011

1. **Lecturer’s Details**

   **Name:** Dr Richard Fairchild

   **Office:** WH 8.52

   **Email:** mnsrf@bath.ac.uk

   **Personal home page:** [http://staff.bath.ac.uk/mnsrf/](http://staff.bath.ac.uk/mnsrf/)

2. **Teaching Assistant’s Details:**

   **Name:** Xinyi Huang (Currently PhD student: formerly MAF student)

   **Office:**

   **Email:** X.Huang2@bath.ac.uk

The course covers numerical, analytical and conceptual aspects of corporate finance. Therefore, students are expected to gain expertise in numerical and game-theoretic analysis, and deeper, conceptual understanding. Your performance on the course is assessed by exam only.

The exam consists of two sections. Section A will contain one numerical and one game-theory question. Section B will consist of two essay questions. All four questions are compulsory.

In order to provide you with practice/feedback in your exam preparation, throughout the semester, you will be required to complete homework exercises (numerical and game-theoretic). The teaching assistant will then go through the answers in your fortnightly seminars. These exercises will give an example of the type of questions that will come up in section A of the exam (there will also be some numerical/game-theoretic examples in the lectures: it is worth practicing these as well).
In relation to the essay questions, I am happy for you to attempt (in groups of 4 or 5) (non-assessed) essays in order for me to give you some feedback on your essay technique. Therefore, I have provided a list of typical essay questions that have appeared in previous years’ exams. For instance:

1. “The firm must understand that investing in a project is a now-or-never decision.” Discuss, with particular reference to real option theory.
2. “The firm’s capital structure is irrelevant.” Discuss.
3. Compare and contrast the trade-off and pecking order theories of capital structure.
4. “Our firm needs to cut the dividend this year, as we have a lot of exciting new investment projects available!” Discuss the dangers inherent in doing this, and how the firm should handle such a policy.
5. A firm is deciding whether to use its excess cashflow to pay dividends or repurchase shares. Does it matter which it does? In your answer, refer to the relevant theories, and the empirical evidence.
6. “Our firm should conduct an active takeover policy, as this will greatly enhance our shareholders’ wealth.” Discuss this, with reference to relevant theory.
7. “When negotiating contracts with entrepreneurs, venture capitalists must be aware of the potential for entrepreneurial opportunistic behaviour.” Discuss, with reference to relevant theory and evidence.
### 3. Course Outline:

<table>
<thead>
<tr>
<th>Topic</th>
<th>Relevant Chapters in CWS</th>
<th>Relevant chapters in Combined HRWJJ/Shefrin book.</th>
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<tbody>
<tr>
<td>1. Investment Appraisal, decision trees. Real options</td>
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<td>8, 22</td>
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<td>2. Information Asymmetry/agency theory</td>
<td>12</td>
<td></td>
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<tr>
<td>3. Capital Structure and Firm Value/Optimal Capital Structure.</td>
<td>15</td>
<td>15, 16</td>
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<td>4. Payout Policy (Dividends/repurchases.</td>
<td>16</td>
<td>18</td>
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<td>5. Mergers and acquisitions.</td>
<td>18</td>
<td>29</td>
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<tr>
<td>6. Venture Capital/Private Equity/hedge funds</td>
<td>Not applicable: but see papers below</td>
<td></td>
</tr>
<tr>
<td>7. Behavioural Corporate Finance</td>
<td>All of the Shefrin Chapters</td>
<td></td>
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### 4. Reading List

**Recommended Books:**

**Corporate Finance/ Behavioural Corporate Finance:** Special Hybrid book developed specifically for this course, combining relevant chapters from Hillier, Ross, Westerfield, Jaffe and Jordan with relevant chapters from Shefrin’s book on Behavioural Corporate Finance.
Financial Theory and Corporate Policy: Copeland, Weston, Shastri: You should already have this book from the first semester. The course will use this as the starting point.

Besides these books, I thoroughly recommend the following optional reading:

- **6 Roundtable Discussions of Corporate Finance** Editor Joel Stern (Available in the library).

- **Revolution in Corporate Finance** (3rd Edition preferred, but 4th edition also available) Stern and Chew editors (available in the library).

- **Dividend Policy: Its Impact on Firm Value**: Lease et al (I have a copy!).

You do not have to purchase any of these, but they will help you to research the subject beyond the lectures, and deepen your understanding of the issues in Corporate Finance.

*Please note that the text-books support (and are complementary to) the lecture slides. That is, the lectures do not follow the text-book exactly. The lectures cover material beyond the text-books (such as journal articles). It is up to the student to read/research beyond the text-book and the lectures (eg read the articles, use Google, SSRN and the financial press.)*

*Furthermore, if HRWJJ is unavailable to you, the library has a whole host of alternative corporate finance books around the 658.15 reference. They all cover similar topics.*

In addition to the chapters of CWS, and HRWJJ/Shefrin identified above, I recommend the following articles.

**General Corporate Finance articles:**


1. Investment Appraisal /Decision Trees/real options.

Recommended Readings:


Optional extra reading:


- “Are Real Options more valuable in the presence of agency conflicts?” Harreiter et al, RMS (2007).


Recommended Readings:

- “An investigation of the determinants of BT’s debt levels: what does it tell us about the optimal capital structure?” Fairchild, R. International Business and Economics research Journal.

Optional Extras:


III Payout Policy.

a) Dividend Policy.

Recommended Reading:


b) Repurchases:

Recommended:


Optional:

• McNally, W.J. “Open Market Stock Repurchase Signalling.” SSRN.

Fairchild’s papers:


Mergers and Acquisitions:
Garvey, G., and G. Hanka.

**Convertible Debt.**

Stein: “Convertible Debt as equity through the ‘back-door’”.
Mayers.

**10. Behavioural Corporate Finance.**

**Behavioral Corporate Finance:** Text-book chapters from Hersh Shefrin

- Gervais et al. “Overconfidence, Investment Policy, and Executive stock Options.” 2003 SSRN.
- Shefrin. “Behavioral Corporate Finance.” SSRN. *

- Fairchild’s papers:-

  - “The Effect of Managerial Overconfidence, Asymmetric Information, and Moral Hazard on Capital Structure Decisions.” Posted to SSRN database 29/04/05.
b) Venture Capitalism:


Ayayi, A. “Optimal Capital Structure and the interactions between New Venture Investment and Venture Capital Finance.” SSRN.


Fairchild’s papers:-


**Private Equity:**

TBA

You do not have to read all of these articles! Highly recommended articles are very important! Use your discretion regarding the other articles!

**Seminars: Class Exercises.**

In addition to the lectures, there will be weekly seminars (run by teaching assistant Xinyi Huang). These will commence in week 19 (week beginning 8th February).

In the exam, there will be an essay section, and a numerical/analytical section. The analytical section consists of a numerical question, and a game-theoretic question.

Throughout the course, you will receive exercises to do in your own time (these will provide good practice for the sort of questions that may arise in the numerical/game theoretic section of the Summer Exam). In the seminars, Xinyi will work through the answers.

Each of you will attend fortnightly seminars. Your exercise schedule is as follows:
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<tr>
<th>Week</th>
<th>Class Exercise</th>
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<tr>
<td>19/20</td>
<td>Decision Tree exercise/real options game theoretic exercise.</td>
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<tr>
<td>21/22</td>
<td>Capital Structure Firm X Exercise/credit signalling</td>
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<tr>
<td>23/24</td>
<td>Debt/dividend Signalling games.</td>
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<tr>
<td>25/26</td>
<td>M and A exercise.</td>
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<tr>
<td>30/31</td>
<td>Venture Capital Game/Behavioural Corporate Finance: debt signalling game with overconfidence.</td>
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