

William Paterson University
Department of Economics, Finance, and Global Business

Course: Finance: Econ 320-80

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Course Description

Corporate Finance is designed to provide a framework for understanding of working capital management and capital budgeting decisions of corporations, the relationship between risk and return, how prices of financial assets are set, and how financial markets function.

Course Pre-requisites

Acct 211 and Econ 202

Course Outcomes

Analyze financial statements

Compare and contrast financial markets

Calculate asset risks

Formulate the values of stocks and bonds

Evaluate long-term financing techniques

Examine capital structures

Evaluate short-term financing techniques

Formulate forecasting methods

Required Text

Eugene F. Brigham, Joel F. Houston

Fundamentals of Financial Management, Concise Edition

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http://websites.swlearning.com/cgi-wadsworth/course_products_wp.pl?fid=M20b&flag=student&product isbn issn=9780324664553&discipline number=414

Grading

Class Discussions and online Field Trips	15%
Quizzes/Homework	45%
Mid-term	20%
Final	20%

Extra Credit is not allowed

100-95	A	76.99-74	C
94.99-90	A-	73.99-70	C-
89.99-87	B+	69.99-67	D+
86.99-84	B	66.99-64	D
83.99-80	B-	63.99-60	D-
79.99-77	C+	59 <	F

Discussion questions

- When responding to the Discussion Questions, students should post complete, well thought-out responses in their own words (not copy and paste) in colors navy blue or black.
- Students should proofread responses for spelling and grammar before posting to the Board.
- Students should post messages in the 100-word.
- Students should respond to at least two classmate's message on each of the discussion questions and respond to all follow up questions.

Students are expected to take online quizzes via Blackboard on each chapter. Late submissions of Discussion Questions, Quizzes and Exams are **NOT** allowed and must be taken within the assignments due dates, a grade **ZERO** will be assigned to missed quizzes and exams, unless you have the proof of a legitimated excuse. Students are expected to have solved the assigned end of the chapter questions and post their question for class discussion for each chapter.

Code of Conduct

Appropriate online classroom decorum, attention, and participation are expected of each and every student.

Honesty and integrity are necessary to the academic and professional functions of business. Acts of dishonesty undermine the basic foundation of the academic environment. Improper academic conduct on the part of students shall be interpreted to mean the obtaining and using of information during an examination by means other than those permitted by the instructor, including the supplying of such information to other students. All forms of academic dishonesty, including cheating, and plagiarism, are subject to disciplinary action according to the William Paterson University guidelines.

Course Outline

1. An Overview of Financial Management.
2. Financial Markets and Institutions.
3. Financial Statements, Cash Flow, and Taxes.

4. Analysis of Financial Statements.
5. Time Value of Money.
6. Interest Rates.
7. Bonds and Their Valuation.

Mid term

8. Risk and Rates of Return.
9. Stocks and Their Valuation.
10. The Cost of Capital.
11. The Basics of Capital Budgeting.
12. Cash Flow Estimation and Risk Analysis.
13. Capital Structure and Leverage.
14. Distributions to Shareholders: Dividends and Share Repurchases.
15. Working Capital Management.
16. Financial Planning and Forecasting.

Final (will cover chapters covered after the mid-term exam)

Timeline:

Saturday, December 26, 2009	1. An Overview of Financial Management.	Quiz 1
Sunday, December 27, 2009	2. Financial Markets and Institutions.	Quiz 2
Monday, December 28, 2009	3. Financial Statements, Cash Flow, and Taxes.	Quiz 3
Tuesday, December 29, 2009	4. Analysis of Financial Statements.	Quiz 4
Wednesday, December 30, 2009	5. Time Value of Money.	Quiz 5
Thursday, December 31, 2009	6. Interest Rates.	Quiz 6
Friday, January 01, 2010		
Saturday, January 02, 2010	7. Bonds and Their Valuation.	Quiz 7
Sunday, January 03, 2010	Midterm (review)	
Monday, January 04, 2010	Midterm (deadline 10:00PM)	Midterm
Tuesday, January 05, 2010	Chapter 8: Risk and Rates of Return	Quiz 8
Wednesday, January 06, 2010	Chapter 9: Stocks and Their Valuation	Quiz 9
Thursday, January 07, 2010	Chapter 10: The Cost of Capital	Quiz 10

Friday, January 08, 2010	Chapter 11: The Basics of Capital Budgeting	Quiz 11
Saturday, January 09, 2010	Chapter 12: Cash Flow Estimation and Risk Analysis	Quiz 12
Sunday, January 10, 2010	Chapter 13: Capital Structure and Leverage	Quiz 13
Monday, January 11, 2010	Chapter 14: Distributions to Shareholders: Dividends and Share Repurchases	Quiz 14
Tuesday, January 12, 2010	Chapter 15: Working Capital Management	Quiz 15
Wednesday, January 13, 2010	Chapter 16: Financial Planning and Forecasting	Quiz 16
Thursday, January 14, 2010	Final Exam Review	
Friday, January 15, 2010	Final Exam (will cover chapters after the mid-term exam)	Final

Lesson 1: Financial Management, Financial Statements, Cash Flow, and Taxes

Purpose

This lesson begins with an overview of corporate finance. It explores career opportunities in the field of finance; advantages and disadvantages of alternative forms of business organizations; agency relationship; and corporate goals within the context of social responsibility and ethics. This lesson also reviews the four major financial statements (balance sheet, income statement, statement of retained earnings, and statement of cash flows) and presents a number of formulas associated with measuring company performance.

Lesson Objectives

After completing this lesson, you should be able to:

- ▶ Explain the goals of a publicly traded firm and the potential conflict of interest between the stakeholders
- ▶ Examine the different forms of business organizations
- ▶ Analyze corporate financial statements (balance sheet, income statement, statement of retained earnings and statement of cash flows)
- ▶ Demonstrate the shortcoming of traditional financial statements and apply the new measures of a business firm's performance
- ▶ Analyze the tax treatment of different types of business organization

Key Concepts

Chapter 1 introduces some of the basic ideas in business finance.

Stockholder wealth maximization is a financial manager's ultimate goal. (Profit maximization would not necessarily lead to stock price maximization due to the timing of profits and the riskiness of different operating plans.)

Chapter 2 introduces the nuts and bolts of financial statements, taxes, and cash flow.

- The *goal of financial management* is to maximize the market value and not the book value of stocks (the book values on an accounting balance sheet can be very different from market values).
- Managers can control some of the factors that determine the price of a company's stock, but there are other factors outside of their control. Of course when a company formulates its goals, there are other aspects such as social responsibility and ethics to consider besides maximizing the value of the firm.
- *Financial statements are used both by debt and equity investors* in order to make intelligent decisions about which firms to invest in. Managers need financial statements to operate their businesses, and taxing authorities need them to assess taxes.
- *Operating cash flow* arises from normal ongoing operations. :

Lesson 2: Analysis of Financial Statements and the Financial Environment

Purpose

Lesson 2 discusses how financial ratios are used to analyze financial statements. In order to put these statements into a real-world context, it is necessary to understand the financial environment and markets in which companies operate. Therefore, Lesson 2 explores the various types of financial markets and institutions as well as their instruments.

Lesson Objectives

After completing this lesson, you should be able to:

- Elaborate on the significance of using financial ratios to evaluate a firm's financial position
- Analyze how a firm's financial standing changes over time relative to its competition
- Analyze the effect of expected future inflation on the relative risk of securities with different maturities
- Explain the relationship between bond yields and maturities and plotting yield curves

Key Concepts

Chapter 3 discusses aspects of financial statement analysis.

- Ratios are accounting numbers that compare the financial statement information of different size firms.
- Ratios are divided into the following general groups:
 - 1 Liquidity: Analyzes the relationship between a firm's cash and other current assets and its current liabilities.
 - 2 Asset management: Analyzes the right amount of assets vs. sales.
 - 3 Debt management: Analyzes the right mix of debt and equity.
 - 4 Profitability: Analyzes sales prices and unit costs and if sales are high enough.
 - 5 Market values: Analyzes a firm's stock price by taking into account its earning, cash flow, and book values per share.
- Some of the potential problems and limitations of financial ratio analysis are as follows:

- 1 Inflation causes ratios that compare current flows with historic values to become distorted over time.
- 2 Comparison with industry averages is difficult for corporations with many different divisions.
- 3 Different operating and accounting practices can distort comparisons.
- 4 "Window dressing" techniques can make statements and ratios look better.

Chapter 4 discusses aspects of the financial markets and institutions.

- Market (nominal or quoted) interest rates are determined by real risk-free rate, inflation premium, and a security's riskiness and marketability (liquidity).
- Money markets are markets for the short term (less than a year) that trade highly-liquid debt securities.
- Capital markets are markets for the long term (more than a year) that trade less-liquid debt securities.
- Yield curve shows the relationship between bonds yields and maturity. The shape of the yield curve depends primarily on: 1) expectations about future inflation, and 2) the relative risk of securities with different maturities.

Lesson 3: Risk, Return, and the Time Value of Money

Purpose

Lesson 3 addresses the essentials of the risk and return tradeoffs of assets and their valuations. This lesson also presents the key conceptual and computational aspects of the time value of money by differentiating between present value and future value of a single amount; present value and future value of annuities; present value of perpetuities; and present values of uneven cash flows.

Lesson Objectives

After completing this lesson, you should be able to:

- Classify types of risks and the methods used to measure risk and rate of return for a single asset and a portfolio
- Explain the tradeoff between risk and rate of return using the Capital Asset Pricing Model (CAPM) and the Security Market Line (SML)
- Analyze present value and interest rate of a single cash flow over different time periods
- Analyze the future value and interest rate of a single cash flow over different time periods
- Calculate the present value and future value of ordinary annuity and annuity due

Key Concepts

Chapter 5 discusses risk and a number of methods of measuring risk and return.

- *Risk* is defined as the chance that the actual return will be different from the expected return.
- A *risk-averse* investor or financial manager requires an increase in return to compensate for a given increase in risk.
- An *estimate of an asset's risk* can be expressed by plotting a probability distribution of expected returns.
- The *coefficient of variation* (CV) is another indicator of asset risk-- it measures relative dispersion.
- The *total risk of a security* is the combination of diversifiable and nondiversifiable risk.
- *Diversifiable risk* refers to the portion of an asset's risk that is attributable to firm-specific events that can be eliminated by diversification.
- *Nondiversifiable risk* refers to the portion of an asset's risk that is attributable to market factors that can affect any firm.
- The *portfolio risk beta* measures nondiversifiable risk. It is an index of the degree of change in an asset's return in response to a change in the market return.
- The *Capital Asset Pricing Model* (CAPM) provides financial managers and investors with a link between risk and return.

Chapter 6 discusses time value of money.

- *Present value (PV)* techniques use a discounting method to find the present value of a single cash flow or a series of future cash flows at time zero (the present time). Because financial managers and investors are at time zero when making decisions, they rely primarily on present value techniques.
- *Future value (FV)* techniques use a compounding method to find the future value of a single cash flow or a series of cash flows at a specific time in future.
- An *annuity* is a series of equal-amount payments during a specific number of time periods.

Lesson 4: Bonds and Stocks

Purpose

Lesson 4 examines the different types of stocks and bonds and their characteristics. Stocks and bonds are the two main sources of raising capital for a corporation. Placing a value on stocks and bonds involves applying the time value of money concepts learned in Lesson 3 as well as understanding the risks unique to each type of security. Lesson 4 also explores the factors that can affect a firm's stock price and how financial managers react to these factors in order to maximize stock prices.

Lesson Objectives

After completing this lesson, you should be able to:

- Classify the types of bonds and their provisions
- Analyze the current yield, the yield to maturity, and/or the yield to call on a bond

- Formulate the value of a share of common stock with different dividends growth rate
- Analyze the markets in which stocks are traded
- Assess efficient markets hypothesis (EMH) and differentiate the three levels of market efficiency

Key Concepts

Chapter 7 discusses the types of bonds and the techniques of bond valuations.

- Bonds are long-term debt instruments that can be classified according to the issuer as follows: treasury bonds, corporate bonds, municipal bonds, and foreign bonds.
- All bonds have a par (face) value, coupon interest rate, and a maturity date.
- *U.S. Treasury bonds* are considered risk free because they are backed by the U.S. government.
- Coupon interest is the product of the coupon rate and the par value of the bond.
- Coupon payment per year is based on the coupon interest rate times the par value.
- Current yield is the outcome of dividing the coupon interest payment per year by the current price of the bond.
- Bond values (market price) increases when the market interest rate decreases and vice versa.
- *If a bond is purchased and held to maturity*, the bondholder's yield to maturity (YTM) will not change regardless of what happens to interest rates.
- The value of any asset (including bonds and stocks) is the present value of all expected future cash flows from that asset.
- Value of a bond (market price) is the present value of all future cash flows (coupon payments) plus the principle.

Chapter 8 discusses the types of stocks, stock markets, and stock valuations.

- The expected value of a share of stock is the present value (PV) of its expected future cash flow streams. The expected cash flows consist of the sum of expected yearly dividends and an expected capital gain.
- *Market efficiency theories* explore the relationship between the price that the market puts on various securities and the types of information that are available about those securities. The faster volume information is reflected in the prices of securities, the more efficient the market is.
- *Strong-form efficiency* suggests that stock prices fully reflect all public as well as private information.
- *Semistrong-form efficiency* suggests that stock prices fully reflect all publicly available information.
- *Weak-form efficiency* suggests that all past information is fully reflected in the current stock prices.

Lesson 5: Capital Budgeting

Purpose

Lesson 5 examines the cost of capital and the ways financial managers can determine this cost in order to make investment decisions. Lesson 5 also integrates the cost of capital into a discussion of capital budgeting and the process of deciding which assets to choose and which to reject.

Lesson Objectives

After completing this lesson, you should be able to:

- * Analyze the three major cost components and calculate the component costs of debt, preferred stock, and common equity
- * Analyze the approaches used to estimate the component cost of retained earnings and the cost of new common equity
- * Assess how interest rate, investment policy, risk, and other factors affect the composite cost of capital, and explain the procedure many firms use when developing subjective risk-adjusted costs of capital
- * Compare and contrast the payback period, discounted payback period, net present value (NPV), internal rate of return (IRR), and modified internal rate of return (MIRR) of independent and mutually exclusive projects and explain their accept/reject decisions
- * Explain why the post-audit is a key element in the capital budgeting process

Key Concepts

Chapter 10 introduces you to some of the cost of capital.

- * The cost of capital is the rate of return a firm must earn on its investment in order to maintain the market value of its stock.
- *Capital component consists of all items on the right-hand side of a balance sheet (a variety of debts, preferred stocks, and common stocks--each of which has a unique cost of capital).
- *The weighted average cost of capital (WACC) is an average of the firm's cost of long-term financing (a variety of debts, preferred stocks, and common stocks). WACC is a key component in capital budgeting, and each company has its own unique optimal capital structure.
- * The cost of capital is measured on an after-tax basis in order to be consistent with the capital budgeting framework. The only component of the cost of capital adjusted for tax is the cost of debt (interest on debt is a tax-deductible expense).
- * The cost of retained earnings is the rate of return required by stockholders on a firm's common stock. The cost of retained earnings is technically less than the cost of new common stock, since by using retained earnings (cash) the firm avoids flotation cost associated with new equity.

Chapter 11 introduces you to basics of capital budgeting.

- * Independent projects are projects whose cash flows are independent of each other.

* Mutually exclusive projects have the same function as the other projects being considered, therefore the projects compete with one another and accepting one eliminates the others.

? Capital budgeting is the process of weighing the potential costs and cash flows (returns) associated with any fixed asset.

* There are at least five techniques used in capital budgeting: payback period, net present value (NPV), internal rate of return, multiple internal rate of return (multiple IRRs), and modified internal rate of return (MIRR).

* A post-audit is an important aspect of capital budgeting that compares an operation's predicted results with the actual results.

Lesson 5: Read Chapters 9 and 10 in Your Textbook

Chapter 10 introduces the concept of the cost of capital, and the technicalities of estimating the sources of capital: debt, preferred stock, common stock, and retained earnings.

Chapter 11 applies the time value money concepts learned earlier in the course to business planning. The chapter presents several types of capital budgeting procedures, including payback period, net present value, internal rate of return, multiple internal rate of return, and modified internal rate of return.

Lesson 6: Cash Flow and Capital Structure

Purpose

Lesson 6 focuses on how to estimate cash flow and account for a project's unique level of risk. Estimating cash flows is one of the most challenging aspects of capital budgeting. Because projects and the business environment are not static, the optimal capital structure for a business can change, as can the cost of capital for a business.

Lesson Objectives

After completing this lesson, you should be able to:

* Explain the four major ways that project cash flow differ from accounting and the difficulties in estimating net cash flows

* Analyze an expansion project and determine a decision rule on whether the project should be accepted on the basis of standard capital budgeting techniques

* Analyze project risks using risk measurements techniques: the Sensitivity Scenario, Monte Carlo Simulation, and Decision Tree

* Assess how operating leverage contributes to a firm's business risk and conduct a breakeven analysis and a breakeven chart

* Analyze capital structure theory in terms of tax structure, trade-off theory, signaling theory, and bankruptcy costs

Lesson 6: Read Chapters 12 and 13 in Your Textbook

Chapter 12 introduces procedures for estimating and identifying relevant cash flows for business decision making. This chapter also looks at project risk and the general principles for determining an optimal capital budget.

Chapter 13 shows how the capital structure of a business has a direct impact on the overall risk of a firm and thus its stock price. Chapter 12 also introduces different capital structure theories and illustrates the tradeoffs between risks and rate of return.

Key Concepts

Chapter 12 discusses risk and a number of methods of measuring risk and return.

* Cash flow is crucial to companies because having sufficient cash on hand ensures that creditors, employees, and others can be paid on time.

* Relevant cash flow is the specific set of cash flows (not accounting income) that should be taken into account in capital budgeting.

* Change in net operating working capital is the difference between the required increase in current assets and the spontaneous increase in current liabilities.

* Incremental cash flow is the change in cash flows attributable to a proposed investment project.

* Operating cash inflows are additional cash flows received because of implementing an investment project.

* Each project has its own stand-alone risk (like an individual investment) that also affects the overall risk of the entire company (like a portfolio).

* Three techniques are introduced as risk measurement tools: sensitivity analysis, scenario analysis, and Monte Carlo simulation:

1. Sensitivity analysis is a risk analysis technique that specifies the change in net present value (NPV) of a firm due to a given change.
2. Scenario analysis is a risk analysis technique that creates "good" and "bad" financial scenarios and compares them to a most-likely scenario, the base-case.
3. Monte Carlo Simulation is a statistical approach to risk analysis that randomly simulates various cash flows associated with a project, calculates NPV based on these cash flows, and estimates the rate of return and risk indexes.

Chapter 13 discusses long term capital structure decision making.

* Capital structure is a mix of a firm's long-term debt, preferred stocks, and common stocks.

* Target capital structure is a mix of debt, preferred stocks, and common stocks (equity) that a firm plans to use to raise capital. This target mix may change over time to adjust to changing conditions.

* Business risk is the inherent risk associated with a firm's operations. (In a leverage-free firm, business risk can be measured by the standard deviation of return on common equity (ROE).)

* Financial risk is the additional risk over and above business risk that stockholders bear because of debt financing.

* Operating leverage is the extent to which fixed costs are used in operations.

* Financial leverage is financing by use of fixed income securities (debt and preferred stocks).

* Capital structure theory is based on the Modigliani and Miller theory of cost of capital, which states that under certain assumptions, a firm's value is unaffected by its method of financing and that capital structure is irrelevant in finding the value of a firm.

* The trade-off theory is based on the firm's trade-off favorable tax treatment of debt financing which increases the common stocks expected rate of return, therefore a higher stock price with the higher interest payments and possible bankruptcy costs.

Lesson 7: Dividends and Capital Management

Purpose

Lesson 7 deals with how a company uses and distributes free cash flows among its shareholders. After discussing dividend policy, the lesson turns to capital management.

account the credit policies of competitors.

Lesson 7: Read Chapters 14 and 15 in Your Textbook

Chapter 14 focuses on how money can be returned to stockholders through dividends or by repurchasing shares of stock. The first part of the chapter deals with issues related to dividend policy, including investor preferences and setting dividend policy. (There is a debate in the academic community about the real value of dividends to investors; some argue dividends are meaningless, while others contend that taxes determine the real value of dividends to investors.) The second part of the chapter deals with the pros and cons of stock repurchases.

Chapter 15 introduces working capital management. Capital management deals with the current assets of a firm. Much of the chapter focuses on cash, cash management, and the cash budget. Accounts receivable and accounts payable are also discussed, along with inventory and marketable securities.

Lesson Objectives

After completing this lesson, you should be able to:

* Analyze target payout ratio and optimal dividend policy

* Analyze Modigliani and Miller capital structure theory, trade-off theory, signaling theory, and the effect of taxes and bankruptcy costs on capital structure

* Explain working capital management and the pros and cons of cash conversion cycle model

* Assess cash management, cash budget, and the advantages and disadvantages of cash conversion cycle

* Explain inventory cost, inventory carrying cycle, inventory ordering costs, and alternative current asset financing policies

Key Concepts

Chapter 14 introduces some of the basic ideas of dividend policies.

*Target payout ratio is the percentage of net income paid out as cash dividends based on investors' preferences.

* Optimal dividend policy is the combination of current dividend payout and future growth (dividend reinvestment) that maximizes the firms' stock price.

* The three theories of investors preferences are:

1. The Dividend irrelevance theory claims that a dividend policy has no effect on the value and the cost of a firm.
2. The bird-in-the-hand theory claims that setting a high dividend payout ratio maximizes a firm's value
3. The tax preference theory claims that investors prefer firms with a lower dividend payout ratio policy because income from capital gains is taxed at a lower rate than income from dividends.

(Unfortunately, empirical tests have failed to offer overwhelming support for any of the above dividend theories.)

* The advantage of having an announced dividend policy is that such policies reduce investor uncertainty, and reductions in uncertainty are generally associated with lower capital costs and higher stock prices. The disadvantage of having such a policy, however, is that it may decrease corporate flexibility.

* The Information Content (Signaling) Hypothesis proposes that investors regard dividend changes an important information, or signals of management earnings forecasts.

* The Residual Dividend Model calculates a dividend payout ratio according to an optimal capital budget and the equity needed to finance the target capital structure.

Chapter 15 introduces some of the basic ideas in working capital management.

*Working capital policies decide the level of each type of current asset to hold, and how to finance current assets. It involves:

1. Cash management
2. Inventory management
3. Accounts receivable management

4. Working capital financing policies

5. Trade credit

*Working capital policy is reflected in a firm's current ratio, cash and securities turnover ratio, and inventory turnover ratio. These ratios indicate how large the amounts of working capital are relative to the level of sales.

*The reasons a business demands cash are:

1. Transactions balance
2. Precaution balance or safety stock?
3. Compensating balances
4. Speculation balance

*Ways to minimize cash holdings:

1. Use a lockbox
2. Insist on wire transfers from customers
3. Synchronize inflows and outflows
4. Use a remote disbursement account
5. Increase forecast accuracy to reduce need for safety stock? of cash
6. Hold marketable securities (also reduces need for safety stock?)
7. Negotiate a line of credit (also reduces need for safety stock?)

* The cash conversion model is a model of cash conversion cycle that calculates the length of time between when a company makes payments to its creditors and when it receives payments from its customers.

* Cash Conversion Cycle = Inventory Conversion Period + Receivables Collection Period - Payables Deferral Period

* The four elements in a firm's credit policy are: credit standards, credit period, discount policy, and collection policy.

* A firm is not required to accept the credit policies of its competitors, but an optimal credit policy cannot be established without taking into

Lesson 8: Forecasting and Multinational Financial Management

Purpose

Lesson 8 examines techniques for forecasting the future performance of a corporation. The ability to generate a variety of "what if" scenarios to project the future profitability of a firm is an important skill for a financial manager.

Lesson 8: Read Chapter 16 and 17 in Your Textbook

Chapter 16 explains the development process and the use of pro forma financial statements. With the introduction of pro forma financial statements, the course has come full circle. Chapters 2 and 3 of the text demonstrated how to analyze existing financial statements-- this chapter explains how to project the future results of a company's operations onto these statements.

Chapter 17 presents an overview of multinational financial management and the major factors that distinguish financial management in firms operating entirely within a single country from those that operate in several different countries. Management must understand the connection between interest rates, foreign currency exchange rates, and inflation risks, and it must become aware of a large number of different financial market regulations and tax systems.

Lesson Objectives

After completing this lesson, you should be able to:

- * Analyze the significance of pro forma financial statements, sales forecasts, and assumptions about the relationship between sales and the various asset and liability accounts
- * Define AFN formulas and the ratio analysis for determination of internal versus external and short-term versus long-term financing
- * Analyze computerized, linear regression, and excess capacity models
- * Describe the six major factors of financial management that distinguish a global operation from a domestic operation
- * Assess IMF, Eurodollar, international bonds and stocks markets, and trading instruments

Key Concepts

Chapter 16 introduces some of the basic ideas of forecasting.

- * An operating plan provides detailed implementation guidelines based on corporate strategy to help meet corporate objectives.
- *The competitive advantage period is the period during which a firm grows at a faster rate than the long-term rate of growth.
- *The financial planning process is the development of long-term strategic financial plans that steer the foundation of short-term operating plans and budgets.
- *A pro forma financial statement forecasts a firm's financial position for a period of one year.
- *Financial forecasting often begins with a sales forecast. Investors and managers want to maximize the value of their investments, and doing so requires a forecast of what is going to happen to their investments. Specifically, investors want to know how future performance may affect the value of a firm's stock.

*In the percent-of-sales method for preparing a pro forma income statement, the financial manager uses sales forecasts based on the most recent sales trends, plus forecasts of the economic prospects for the nation, region, industry, and uses the forecasted sales values for cost of goods sold, operating expenses, and interest expense as a percentage of projected sales.

*Additional Funds Needed (AFN) are funds that a firm must raise externally through borrowing or by selling new common or preferred stock to support forecasted level of sales.

*If the ratios for the forecasted income statement and balance sheet are expected to remain constant, then $AFN = \text{Required increase in assets} - \text{Spontaneous increase in liabilities} - \text{Increase in retained earnings}$

* Cash planning requires preparation of the cash budget; profit planning involves preparing a pro forma income statement and balance sheet.

Chapter 17 introduces the financial environment of a multinational corporation.

* A Eurodollar is a dollar deposit in a foreign bank (so-called because financial managers frequently choose European banks).

* Political risk is the chance that a multinational corporation's resources may be expropriated by a foreign government without compensation.

* Exchange rate is the number of units of a certain currency that can be exchanged with one unit of another currency.

* Floating exchange rates allow currency prices to fluctuate without government intervention.

* Spot rate is the rate of exchange of one currency to another "on the spot."

* Forward rate is an agreed upon rate at which two currencies are exchanged.

* Interest rate parity is the idea that the risk-adjusted rate of return on an investment should be the same in all countries.

* Purchasing power parity, sometimes referred to as "the law of one price," is the idea that the cost of identical goods in different countries is the same due to the adjustments in exchange rate.

All the assignments are tentative changes will be posted/announced in class.