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|  | **Course Title: FBE 529: FINANCIAL ANALYSIS AND VALUATION** |
| **Syllabus for Fall 2015(revised)** |
| **Professor: Lloyd Levitin**  |
| **Office: Acc. 301E**  |
| **Office Phone: 310-740-6524** |
| **E-mail: levitin@marshall.usc.edu** |

Classes Held: Mondays and Wednesdays 2:00 – 3:20

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| Office Hours: Monday, Tuesday 4:00-5:00 P.M. |
| Teaching Assistants | Erika Johnson ( Erika.Johnson.2016@marshall.usc.edu) will keep grade book |
|  | Fortunato Carlo Cordero (fcordero@usc.edu) available for office hour |

**I. COURSE OBJECTIVE**

Understanding what determines the value of a firm and how to estimate that value is a prerequisite for making rational business decisions. Entire industries (investment banking, securities analysis, and consulting) have grown prosperous providing valuation skills to investors and managers. The objective of this course is to provide you with a competent foundation in various valuation approaches, with an emphasis on the “best practices.” We cover discounted cash flow models, market multiple models, as well as specialized models used for M&A transactions and LBOs. We focus on valuation of individual investment projects and businesses at the divisional and corporate levels. The course emphasizes practical and “real world” applications of valuation methodologies.

**II. LEARNING OBJECTIVES**

By the end of the course, students should be able to:

* Perform a valuation for any individual investment project or public or private company.
* See clearly how industry fundamentals and competitive forces directly impact financial results and, in the process, drive stock valuation.
* Assess whether a company is creating value for its shareholders.
* Pull apart the financial statements to get at the relevant information for valuing equities.
* To identify “red flags” that indicates manipulation of financial statements and/or an impending liquidity crisis.
* Evaluate the reports of business valuation experts and to be able to ask the “right” questions of these experts.

**III. WHO SHOULD TAKE THE COURSE**

The course is of interest to those contemplating careers in investment banking, security analysis, consulting, private equity, and corporate finance. And it will also help with personal investing.

**IV. PREREQUISITE KNOWLEDGE**

This course assumes that the background knowledge of students include basic finance and accounting. Prerequisites are one from GSBA 521 or GSBA 521b or GSBA 548.

**V. TEACHING METHODS**

The course will be in the form of lectures, class discussions, cases and practice problems. During class, we will not have time to discuss all the material covered in the assigned text readings. Class time will be spent deepening our understanding of the major topics in the chapter, clarifying points of possible confusion, working out exercises and problems in the textbook, and discussing the material via cases or from my business experiences. This places on you a responsibility to read the assigned material whether it is covered in class or not.

**VI. ABOUT YOUR INSTRUCTOR**

Lloyd Levitin is a Professor of Clinical Finance and Business Economics at Marshall. He was Executive Vice President and CFO of Pacific Enterprises from 1982-1995 (now Sempra Energy), and was actively involved in the firm’s diversification program which included numerous acquisitions. He testified as an expert on utility diversification to the Senate Finance Committee of the U.S. Congress and has been a consultant for JurEcon, Inc., a nationwide consulting and research firm for management and counsel. He has a MBA from Wharton and a JD from University of San Francisco. He practiced as a CPA after receiving his MBA, and as an attorney after receiving his JD.

**VII. VALUATION REQUIRES A SKILL SET THAT COMBINES BOTH ART AND SCIENCE**

Various valuation models and formulae will be taught in this class. Learning how to plug numbers into models and formulae to produce a valuation answer is the easy part. The quality that separates winners from losers in the world of valuation is the ability to decide which information to use under the circumstances and what assumptions to make that become inputs to the models and formulae. In other words, one has to exercise good judgment to be a winner. This course will sharpen your skills in making these judgments.

The instructor will provide cases from his business career and his knowledge of valuation successes and failures of others to help students sharpen their ability to improve decision making. In the financial world, judgment is the quality that can make the difference between success and failure in one’s career.

**VIII. REQUIRED COURSE MATERIALS**

1. Textbook: “Valuation – The Art and Science of Corporate Investment Decisions,” 3rd edition, by Sheridan Titman and John D. Martin, 2016. Pearson Education, Inc. ISBN# of this book is 978-0-13-347952-2. Bring this text to class as we will work out some of the textbook’s exercises and problems in class.
2. Cases published by Harvard Business School and Ivey Publishing.
3. Instructor’s Valuation Notes to be posted to “Blackboard.” I have copywrited these notes.
4. PowerPoint presentations to be posted to Blackboard.
5. Financial calculator capable of performing discounted cash flows (please bring calculator to each class).

**IX. GRADING SUMMARY**

Students will be graded on a point basis with 100 available points:

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|  | **% of Grade** |
|  |  |
| 4 Quizzes  |  20% |
| Final Exam |  35% |
| Group Project: Valuation of PepsiCo  |  25%  |
| Peer Evaluation |  10% |
| Class Participation |  10% |
|  |  |
| **TOTAL** |  100% |

Final grades represent how you perform in the class relative to other students. Your grade will not be based on a mandated target, but on your performance. Three items are considered when assigning final grades:

1. Your average weighted score as a percentage of the available points for all assignments (the points you receive divided by the number of points possible).
2. The overall average percentage score within the class.
3. Your ranking among all students in the class.

**Quizzes and Final Exam (55% of your grade)**

Final exam and Quizzes will be open-notes, closed book. You may use any handouts provided by the professor and any materials such as notes or outlines written and prepared exclusively by you. During the exam, you may not use any other materials, written, digital, or recorded. Laptops or any hand-held device with email capabilities cannot be used. The date of quizzes is on the class schedule. There are 4 quizzes. Each quiz is worth 5 points. Quizzes will consist of 5 multiple choice questions. If you are unable to take a quiz, the following rules apply:

1. If you fail to inform me in writing before the quiz begins, you will receive a zero grade, even if you have a valid excuse. An exception will be made if you have a note from your doctor that you were unable to communicate your excuse.
2. If you inform me in writing before the quiz begins, and you have an acceptable excuse, then the final exam will count for an additional 5% of your grade.

You should bring a calculator to perform calculations. The final exam is similar to the quizzes in format, but cumulative in coverage.

**Group Project**

Valuation of PepsiCo (25% of your grade). Students will divide themselves into teams of 4-8 students each by September 9. Any student who cannot find a team should inform me by September 10. The requirements for this group assignment are set forth on page 14 of this syllabus. The due date is December 2.

**Peer Evaluation on Group Project (10%)**

Group Projects provide a valuable learning experience – how to work effectively and efficiently in groups (a common practice in Corporate America), learning from others, and sharpening a student’s ability to communicate to others. However, human nature being what it is, some students are tempted to relax and let others carry their load. In order to provide an incentive for all students to make maximum contributions to the team project, students will be asked to grade each team member’s contributions on a 10-point scale.

This evaluation is to be submitted by email to the Instructor before the last day of classes. No form will be provided. Simply list each person on the team and your score for the student. *Any team member who does not email his (her) evaluation of team members will be deemed to have given a 10-point score to each member of the team.*

**Class Participation (10% of your grade)**

Attendance and participation are essential for success in this course.

You may earn up to 10 points for class participation (i.e., 10% of your final grade). Each of you will be awarded these 10 points on the first day of class. Your objective will be to keep these 10 points throughout the semester. This requires attendance at classes and your participation in the discussion of the cases set forth in the Class Schedule of this syllabus. I will cold-call to ask you to discuss one of the assigned questions, or additional ones pertaining to the case, and if it appears to me that you did not prepare for the case discussion, I will subtract one or two points from the 10 point maximum. The assigned questions are set forth on pages 12-14 of this syllabus.

To help me out, you should bring a name card and place it on the desk in front of you.

**X. ACADEMIC INTEGRITY**

USC seeks to maintain an optimal learning environment. General principles of academic honesty include the concept of respect for the intellectual property of others, the expectation that individual work will be submitted unless otherwise allowed by an instructor, and the obligations both to protect one’s own academic work from misuse by others as well as to avoid using another’s work as one’s own. All students are expected to understand and abide by these principles. *SCampus*, the Student Guidebook, ([www.usc.edu/scampus](http://www.usc.edu/scampus) or <http://scampus.usc.edu>) contains the University Student Conduct Code (see University Governance, Section 11.00), while the recommended sanctions are located in Appendix A.

Students will be referred to the Office of Student Judicial Affairs and Community Standards for further review, should there be any suspicion of academic dishonesty. The Review process can be found at: <http://www.usc.edu/student-affairs/SJACS/> . Failure to adhere to the academic conduct standards set forth by these guidelines and our programs will not be tolerated by the USC Marshall community and can lead to dismissal.

**XI. STUDENT DISABILITY**

Any student requesting academic accommodations based on a disability is required to register with Disability Services and Programs (DSP) each semester. A letter of verification for approved accommodations can be obtained from DSP. Please be sure the letter is delivered to be as early in the semester as possible. DSP is located in STU 301 and is open 8:30 AM to 5:00 PM, Monday through Friday. The phone number for DSP is (213) 740-0776. For more information visit [www.usc.edu/disability](http://www.usc.edu/disability).

**XII. TECHNOLOGY POLICY**

Laptop and Internet usage is not permitted during academic or professional sessions unless otherwise stated by the professor. Use of other personal communication devices, such as cell phones, is considered unprofessional and is not permitted during academic or professional sessions. ANY e-devices (cell phones, PDAs, iPhones, Blackberries, other texting devices, laptops, iPods) must be completely turned off during class time. Videotaping faculty lectures is not permitted, due to copyright infringement regulations. Audiotaping may be permitted if approved by the professor. Use of any recorded material is reserved exclusively for USC students registered in this class.

**XIII. ADD/DROP PROCESS**

If you are absent for the two classes prior to September 3, I may drop you from the class by that date. These policies maintain professionalism and ensure a system that is fair to all students.

**XIV. RETENTION OF GRADED COURSEWORK**

Final exams and all other graded work which affected the course grade will be retained for one year after the end of the course ***if*** the graded work has not been returned to the student (i.e., if I returned a graded paper to you, it is your responsibility to file it, not mine).

**XV. EMERGENCY PREPAREDNESS/COURSE CONTINUITY**

In case of a declared emergency if travel to campus is not feasible, USC executive leadership will announce an electronic way for instructors to teach students in their residence halls or homes using a combination of Blackboard, teleconferencing, and other technologies.

Please activate your course in Blackboard with access to the course syllabus. Whether or not you use Blackboard regularly, these preparations will be crucial in an emergency. USC's Blackboard learning management system and support information is available at [blackboard.usc.edu](http://blackboard.usc.edu/).

**XVI. CLASS NOTES POLICY**

Notes or recordings made by students based on a university class or lecture may only be made for purposes of individual or group study, or for other non-commercial purposes that reasonably arise from the student’s membership in the class or attendance at the university. This restriction also applies to any information distributed, disseminated or in any way displayed for use in relationship to the class, whether obtained in class, via email or otherwise on the Internet, or via any other medium. Actions in violation of this policy constitute a violation of the Student Conduct Code, and may subject an individual or entity to university discipline and/or legal proceedings.

*Policy approved by Lloyd Armstrong, Jr., Provost and Senior Vice President for Academic Affairs, on January 26, 2000.*

**XVII. CLASSES CANCELLED**

Classes scheduled September 14, 23, 28 and October 5 are cancelled. Make-up classes for 3 of these classes will be on Sept. 25 and Oct. 9 from 1-3pm. These make-up classes will be videotaped for those students unable to attend and posted to Blackboard.

**XVIII. CLASS SCHEDULE AND ASSIGNMENTS**

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| **DATE** | **TOPIC** | **ASSIGNMENT** |
| Aug 24 | Introduction to Valuation | LN-1 |
| Aug 26 | Key Valuation Concepts |  |
| Aug 31 | Key Valuation Concepts – continued | Text: Chapter 1 |
| Sep 2 | Industry and Company Fundamental Analysis  | LN-2 |
| Sep 7 | HOLIDAY |  |
| Sep 9 | Industry and Company Fundamental Analysis – continued | Text: Chapter 6 (pages 188-198)Work problems provided in slides for LN-2 |
| Sep 14 | Industry and Company Fundamental Analysis – continued |  |
| Sep 16 | DCF Models | LN-3 |
| Sep 21 | DCF Models – continued |  |
| Sep 23 | DCF Models – continued | Text: Chapter 4 |
| Sep 28 | DCF Models – continued | Text: Chapter 6 (pages 198-217) |
| Sep 30 | DCF Models – continued | Text: Chapter 7 |
| Oct 5 | DCF Models – continued | Text: Chapter 9 |
| Oct 7 | Market Multiples | LN-4 |
| Oct 12 | Market Multiples – continued | Text: Chapter 8 |
| Oct 14 | Market Multiples – continued |  |
| Oct 19 | Mergers and Acquisitions | LN-5 |
| Oct 21 | Mergers and Acquisitions – continued |  |
| Oct 26 | Mergers and Acquisitions – continued |  |
| Oct 28 | Mergers and Acquisitions – continued |  |
| Nov 2 | Restructuring | LN-6 |
| Nov 4 | Restructuring – continued |  |

**CLASS SCHEDULE AND ASSIGNMENTS - continued**

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| **DATE** | **TOPIC** | **ASSIGNMENT** |
| Nov 9 | Private Company Valuation | Text: Chapter 10 |
| Nov 11 | Analysis of Cases | Valuation of Airthreads Connections |
| Nov 16 | Analysis of Cases – continued | Pinkerton (A) and (B) |
| Nov 18 | Analysis of Cases – continued | Auction for Burger King (A) and (B) |
| Nov 23 | Analysis of Cases – continued | Canadian Pacific, LTD |
| Nov 25 | HOLIDAY |  |
| Nov 30 | Project Valuation | Text: Chapters 2 and 5 |
| Dec 2 | Review | PepsiCo Group Project – Due |
| Dec 11 | Final Exam 2:00-4:00 P.M. |  |

LN refers to Levitin’s Notes. LN-1 is chapter 1 of Levitin’s Notes. LN-2 is Chapter 2 of Levitin’s Notes, etc.

**Quiz Dates**:

 September 9 October 21

 September 30 November 11

1. **CASE ASSIGNMENTS TO BE DISCUSSED IN CLASS; NO WRITE-UP REQUIRED**

Harvard Business School Cases

1. Pinkerton (A) #9-291-051 (Rev. May 24, 2001)
2. Pinkerton (B) #9-292-136 (Rev. August 5, 1999)
3. Valuation of Airthread Connections #4263
4. The Auction of Burger King (A) #9-906-012 (Rev. October 10, 2012)
5. The Auction of Burger King (B) #9-906-013 (Rev. November 16, 2005)

Ivey Publishing Cases

1. Canadian Pacific LTD: Unlocking Shareholder Value In a Conglomerate #9B14N017

Discussion Questions are attached on following pages 10 to 14.

**DISCUSSION QUESTIONS FOR ASSIGNED CASES (NO WRITE-UP REQUIRED)**

**Pinkerton (A)**

1. How does CPP plan to create value? Does this make sense to you?
2. How will you determine the value of Pinkerton to American Brands?
3. What valuation methodology would you use to determine what Pinkerton is worth to CPP?
4. What are the synergies involved in the deal?
5. Assuming you are doing a FCF/WACC valuation, how would you estimate WACC? What capital structure would you use? What is cost of equity?
6. What analysis would you make to determine whether CPP should accept the 75% debt alternative? The 100% debt alternative?
7. Should an illiquidity discount be applied to your valuation?
8. How do we take into account the costs of financial distress?

**Pinkerton (B)**

1. What are the costs of financial distress facing Pinkerton?
2. What financial analysis would you make to determine:
3. Whether Pinkerton can service its debt and pay dividends without the IPO?
4. The value of a share of Pinkerton before vs after the IPO?
5. How much value is given up by the IPO?

**Valuation of Airthreads Connections**

1. What is American Cable’s debt policy for the acquisition?
2. What valuation method would you use to value Airthread Connections?
3. FCF/WACC?
4. APV?
5. FCFE?
6. Some combination of above?
7. What formula would you use to estimate the terminal value?
8. What discount rate would you use for
9. Intermediate cash flows (1st 5 years)?
10. TV cash flows?
11. How should the nonoperating investments in equity affiliates be accounted for in the valuation?
12. How would you estimate the cost of equity in computing WACC?
13. What growth rate would you use in computing the TV?
14. Do you need to value the tax shields for the intermediate period? For the TV? If so, how would you do it?
15. What analysis would you make to determine if the acquisition’s cash flow would support the acquisition debt?
16. How would you value the synergies?
17. Would you employ an illiquidity discount?
18. How would you value costs of financial distress?

**THE AUCTION FOR BURGER KING (A) and (B) Cases**

1. How did Diageo come to own Burger King?
2. What attempts were there to turn the unit around?
3. Describe the auction process.
4. What were the various bidders’ tactics to gain advantage in the auction?
5. What enhancements to the inferior bids would make them equivalent to the first-ranked bid?

**Canadian Pacific LTD: Unlocking Shareholder Value in a Conglomerate**

1. Why did a conglomerate structure make sense for CPL in the past? Does it still make sense?
2. How would you estimate the size of the conglomerate discount using sum-of-parts valuation? Discuss the necessary steps.
3. What assumptions are you making in doing a sum-of-parts valuation that may not be valid?
4. What options does CPL have to eliminate the conglomerate discount and what are the pros and cons of each option?
5. If CPL pursues the starburst strategy, what methodology would you use to allocate CPL’s corporate debt?
6. How would you determine the implied price per share for each business in a spinoff?
7. **PEPSICO VALUATION PROJECT - Due Date December 2, 2015**

The group project counts for 25% of your grade. The group project is to prepare a valuation report on PepsiCo. The purpose of the project is for you to apply what you have learned in class, including how to analyze the financial performance of a company, and how to value it applying the valuation techniques presented in the course. The completed valuation report is to include the following sections:

Table of Contents

1. Summary and Investment Conclusion
2. Capsule description of the company
3. Recommendation (buy, hold, or sell). Explain your reasoning for your recommendation (there is no right answer)
4. Industry and Company Analysis
5. Company description
6. Industry analysis
7. Competitive analysis
8. Historical financial performance past 3-5 years
9. Valuation
10. DCF Valuation based on FCF/WACC Model. Use a spreadsheet. Include a discussion of key valuation inputs.
11. Market comparables valuation
12. Valuation Range and comparison to current stock price
13. Statement of Conclusions