

Chapter

00

AN OVERVIEW OF CORPORATE FINANCING



Brealey, Myers, and Allen
Principles of Corporate Finance
11th Global Edition

00-1 PATTERNS OF CORPORATE FINANCING

- How Firms Raise Funds
 - Plowing back profits
 - Seeking external financing
 - Debt sources
 - Equity sources

FIGURE 1 SOURCES OF FUNDS, U.S. NONFINANCIAL CORPORATIONS

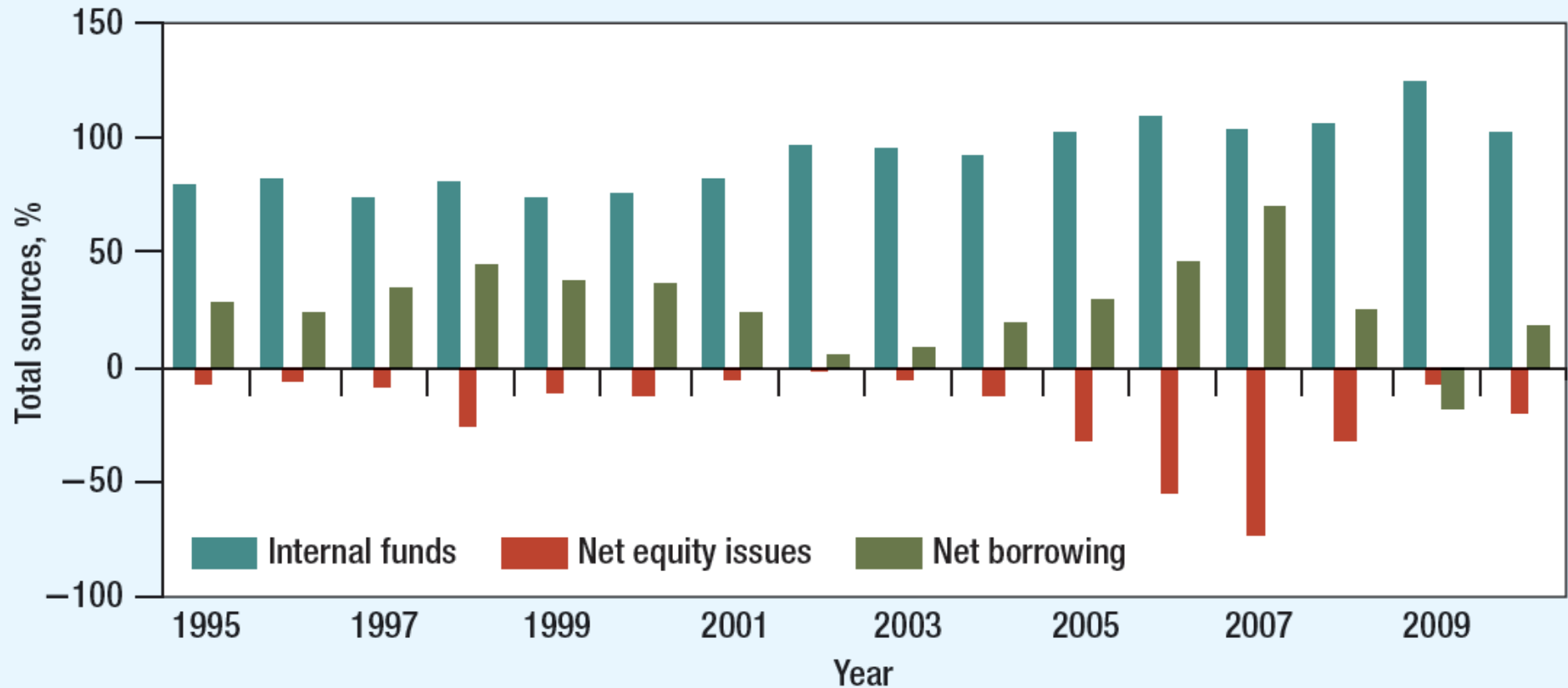


TABLE 1 U.S. MANUFACTURING, THIRD QUARTER, 2011 (\$ BILLIONS)

Assets		\$ Billions	Liabilities		\$ Billions
Current assets ^a		\$2,238	Current liabilities ^a		\$1,579
Fixed assets	\$2,897		Long-term debt	\$1,618	
Less depreciation	<u>1,556</u>		Other long-term liabilities ^b	<u>1,107</u>	
Net fixed assets		1,341	Total long-term liabilities ^b		2,725
Other long-term assets		<u>4,276</u>	Stockholders' equity		<u>3,552</u>
Total assets		\$7,856	Total liabilities and stockholders' equity		\$7,856

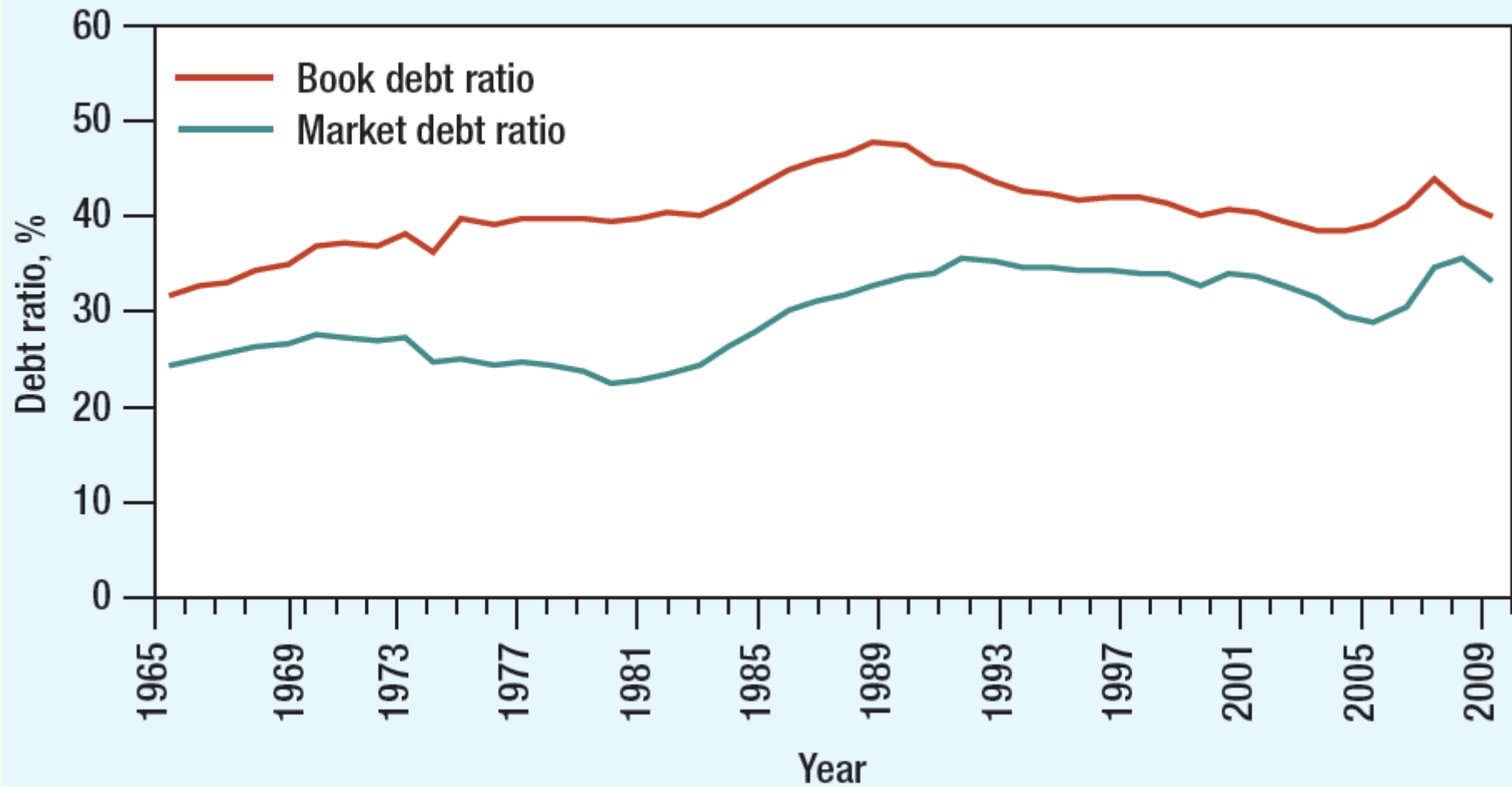
00-1 PATTERNS OF CORPORATE FINANCING

- How Do We Define Debt?

$$\frac{\text{Debt}}{\text{Total assets}} = \frac{1,759 + 2,362}{7,856} = .52$$

$$\frac{\text{Long - term liabilities}}{\text{Long - term liabilities + equity}} = \frac{1,618}{1,618 + 3,552} = .31$$

FIGURE 2 DEBT TO NET WORTH, NONFINANCIAL CORPORATIONS, 1955-2010

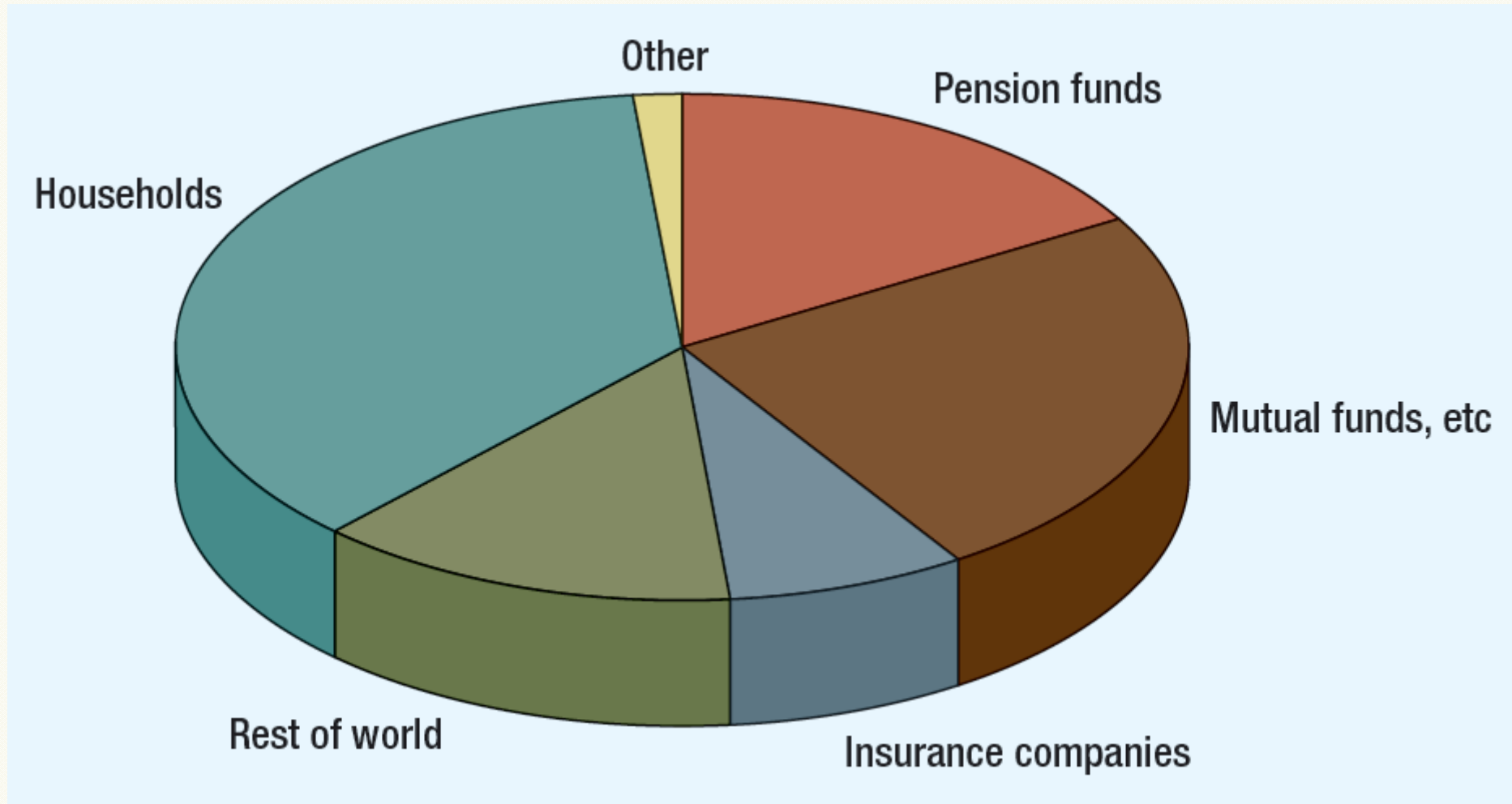


00-2 COMMON STOCK



- Common Stock
 - Residual claim on assets and cash flow
 - Mostly held by financial institutions
 - Stockholders have ultimate right of control

FIGURE 3 CORPORATE EQUITY HOLDINGS, THIRD QUARTER, 2011



00-2 COMMON STOCK



- Voting Procedures
 - Board of directors comes up for re-election every year
 - Classified board of directors
 - One-third of directors come up for re-election every year
 - Entrenches management

00-2 COMMON STOCK

- Dual-Class Shares and Private Benefits
 - Some companies have two classes of stock
 - Same cash-flow rights, different control rights
 - Greater control rights grant private benefits

00-2 COMMON STOCK



- Equity in Disguise
 - Partnerships
 - Avoid corporate income tax
 - Limited life span
 - Trusts
 - Passive ownership of asset
 - Real Estate Investment Trust (REIT)
 - Not taxed
 - Limited to real estate

00-2 COMMON STOCK

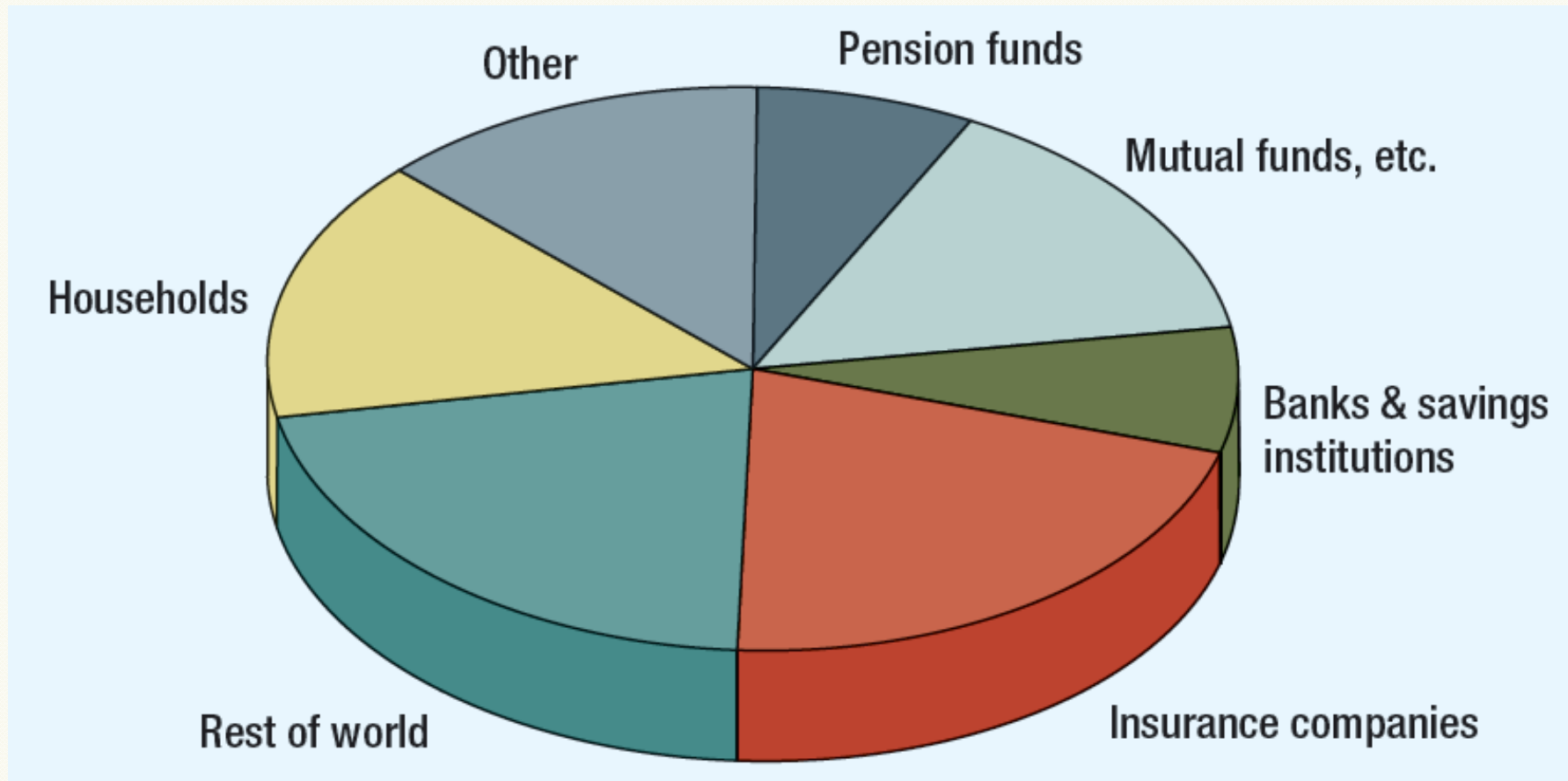
- Preferred Stock
 - Takes priority over common stock when receiving dividends
 - Gains some voting rights if corporation fails to pay preferred dividend

00-3 DEBT



- Debt Comes in Many Forms
 - Short-term versus long-term
 - Fixed versus floating rate
 - Dollars versus foreign currency
 - Senior versus junior debt
 - Straight versus convertible bonds

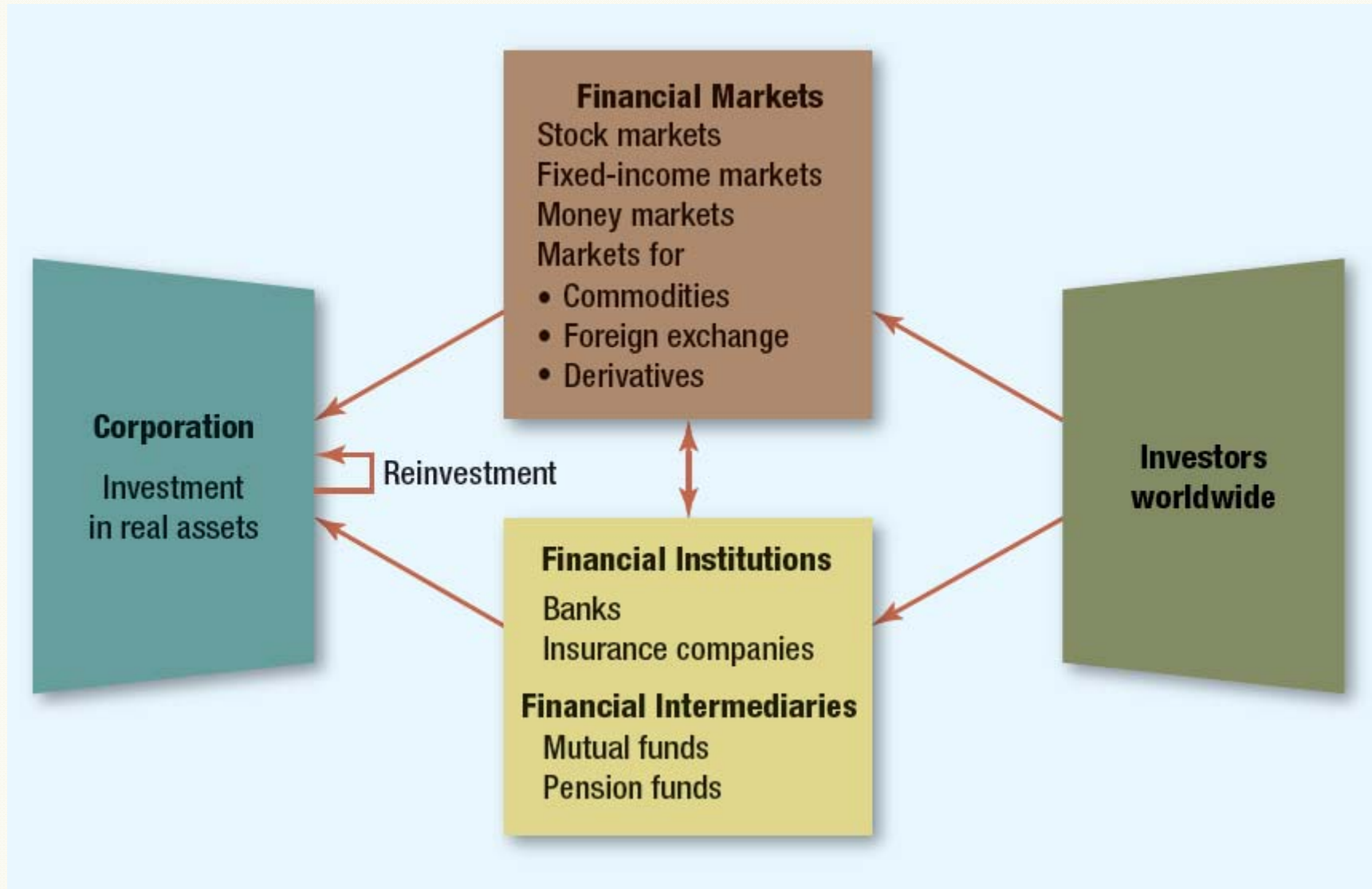
FIGURE 4 U.S. BOND HOLDINGS, THIRD QUARTER, 2011



00-3 DEBT

- Debt by Any Other Name
 - Some debts treated differently in accounts
 - Accounts Payable
 - Good received, not yet paid for
 - Very short-term debt
 - Unfunded obligations
 - Senior debt, e.g., employee pensions
 - Special-Purpose Entities (SPEs)
 - Raise cash through equity and debt
 - Do not show up on balance sheet

FIGURE 5 FLOW OF SAVINGS TO INVESTMENT



4 FINANCIAL MARKETS AND INSTITUTIONS



- Financial Markets
 - Used to raise money through primary issues
 - Allow investors to trade amongst themselves
 - Help firms manage risks
- Financial Intermediaries
 - Raise money from investors, provide financing
 - Banks, insurance companies, investment funds

TABLE 2 FINANCIAL ASSETS OF U.S. INTERMEDIARIES, THIRD QUARTER, 2011

	\$ Billions
Mutual funds	\$ 7,513
Money market funds	2,578
Closed-end funds	236
ETFs	947
Hedge funds ^a	1,297
Pension funds	9,836
Banks and savings institutions	17,611
Insurance companies	6,617

00-4 FINANCIAL MARKETS AND INSTITUTIONS

- Investment Funds
 - Mutual Fund
 - Raises money by selling shares to investors
 - Attempts to beat market
 - Money Market Fund
 - Invests in short-term safe securities
 - Closed-End Fund
 - Fixed number of shares

00-4 FINANCIAL MARKETS AND INSTITUTIONS



- Investment Funds
 - Exchange-Traded Fund (ETF)
 - Portfolio bought or sold in single trade
 - Hedge Fund
 - Restricted access
 - Limited partnership
 - Performance-related fees

00-4 FINANCIAL MARKETS AND INSTITUTIONS



- Financial Institutions
 - Commercial banks
 - Provide loans, safe money storage
 - Investment banks
 - Assist companies in raising financing
 - Advise on takeovers, mergers, and acquisitions
 - Insurance companies
 - Invest in corporate stocks and bonds

00-5 THE ROLE OF FINANCIAL MARKETS AND INTERMEDIARIES



- Payment Mechanism
 - Allows individuals to make and receive payments quickly and safely over long distances
- Borrowing and Lending
 - Channels savings towards those who can best use them

00-5 THE ROLE OF FINANCIAL MARKETS AND INTERMEDIARIES



- Pooling Risk
 - Allows individuals to share risk, i.e., insurance companies
- Information
 - Allows estimation of expected rates of return