ATHENS UNIVERSITY OF ECONOMICS AND BUSINESS

MSc in International Shipping, Finance and Management

FINANCIAL MANAGEMENT

Lecturer: Professor Spyros Spyrou
Office: Patision 76, Antwniadou Building, 5th floor, 10434, Athens
Tel: 210 8203169, **Email:** sspyrou@aueb.gr

EDUCATIONAL AIM

The goal of this course is to analyze corporate decisions from a financial perspective. To this end, the course focuses on investment and financing decisions, valuation, and the treatment of risk. The course covers issues such as the decision to go public, financial statement analysis, capital budgeting techniques, the estimation of the cost of capital, the valuation of stocks and bonds, the risk-return trade-off, the capital structure and the dividend policy of corporations.

ASSESMENT

Written Examination: 70%; Assignment: 30%

EDUCATIONAL OBJECTIVES

- Introduce students to investment and financing decisions made by corporations.
- Explain how to reach such decisions using the theory of financial management.

The course will make it possible for participants:

- To acquire a clear understanding of investment and financing decision making, valuation of investment projects through various capital budgeting techniques, estimation of the cost of capital and its relation to risk, the role of capital structure and dividend policy and the management of short-term assets and liabilities.
- To be able to understand the treasury department operations of a corporation.

LEARNING OUTCOMES

On completing the course participants will:

- Understand how and why firms raise capital from the market, and how stocks and bonds are priced
- Understand various types of debt securities and instruments, such as interest rate swaps, and understand how a firm can use these instruments to manage risk
- Have an understanding of how projects are valued, and will be able to use the key capital budgeting techniques (NPV and IRR)
- Understand how risk affects the value of the asset in equilibrium, and how this affects, in turn, the company cost of capital
- Become familiar with capital structure and dividend policy theory
- Be able to explain how firms manage their short-term assets and liabilities

THEMATIC AREAS

- **Thematic area 1: Introduction to Financial Management**
  Financing Decisions
  Initial Public Offerings
  Equity Valuation
  Financial Statement Analysis

- **Thematic area 2: Fixed Income Securities**
  Valuing bonds using present value
  The term structure of interest rates
  The risk of default, credit rating
  Duration, Convexity

- **Thematic area 3: Swap Markets**
  Interest Rate Swaps (IRS)
  Currency Swaps (CS)
  The use of IRS to transform the nature of assets/liabilities
  The use of CS to transform the nature of assets/liabilities
  Swap Valuation

- **Thematic area 3: The Present Value Rule**
  Introduction to present value
  Risk and present value
  Present value rule and shareholders' preferences

- **Thematic area 4: Cash flows for investment analysis**
  Accounting earnings vs cash flows
  Cash flows for the firm and the equity investors

- **Thematic area 5: Investment decision rules & capital budgeting**
  Accounting-income based decision rules
  Net Present Value (NPV)
  Payback period
  Internal rate of return (IRR)

- **Thematic area 6: Risk – Return**
  Portfolio risk and diversification
  The capital asset pricing model (CAPM)
  Cost of Capital

- **Thematic area 7: Capital Structure**
  Theories of capital structure
  The after-tax weighted average cost of capital (WACC)

- **Thematic area 8: Payout Policy**
  Dividend payments and stock repurchases
  Empirical evidence on dividend policy
  The payout controversy

BRIEF DESCRIPTION OF THEMATIC AREAS

- ***Introduction to Financial Management***

Financing decisions, equity vs debt, the decision to go public, Initial Public Offerings (IPOs), theory and practice of IPOs, IPO under-pricing, equity valuation, financial statements, analysis of financial statements, ratio analysis. Dividend discount model, cost of equity, Gordon growth model, dividend-price ratio, growth and income stocks, market efficiency,

- ***Fixed Income Securities***

Bond characteristics, yield to maturity, zero-coupon bonds, the yield curve, term structure of interest rates, risk of default, bond ratings, yield spread, credit score systems, duration and convexity, Credit Default Swaps (CDS), Interest Rate Swaps (IRS), Currency Swaps (CS).

- ***Swap Markets***

Definitions and examples of Interest Rate Swaps (IRS) and Currency Swaps (CS). Examples of hedging with swaps, the use of IRS to transform the nature of assets/liabilities, the use of CS to transform the nature of assets/liabilities. The comparative advantage argument. Swap Valuation.

- ***The present value rule, investment decision rules & Capital Budgeting***

The arithmetic of present value, the time value of money, opportunity cost of capital, net present value (NPV), risk and present value, project rate of return, shareholders' preferences and the present value rule, discounted cash flow (DCF) formula for valuing long-lived assets, perpetuities and annuities, loan payments calculation. Operating expenses and capital expenses, depreciation, working capital, sunk costs, opportunity costs, calculate cash flows to the firm and equity investor, free cash flow to equity discount model. Return on capital (ROC), return on equity (ROE), payback period, internal rate of return (IRR), the relation between IRR and NPV, advantages and disadvantages of these rules.

- ***Risk & Return***

The variability of capital markets investments, calculating portfolio risk, the benefits of diversification, systematic and unsystematic risk, the beta of an individual security, the capital asset pricing model (CAPM) and the security market line (SML), estimate the cost of equity using the CAPM, estimate the company cost of capital (weighted average cost of capital), estimate the project cost of capital, cyclicality and operating leverage.

- ***Financing and Valuation***

Definition of the capital structure, the optimal capital structure in perfect capital markets, financial leverage and the debt-to-equity ratio, the optimal capital structure given corporate and personal taxes, the role of financial distress effects, the pecking order of financial choices, the after-tax WACC, adjusted present value calculation.

- ***Payout Policy***

Dividend payment procedure and stock repurchases, empirical evidence of dividend policy, the information content of dividends and stock repurchases the three schools of dividend policy, payout policy is irrelevant in perfect capital markets, the role of corporate taxes in dividend policy.

INDICATIVE READING MATERIAL

- Lecture notes/slides uploaded in e-class
- **Berk, J., De Martzo, P., 2017 "Corporate Finance" Pearson publications, 3rd edition (or a more recent edition)**
- Other references - publications in the area as discussed during lectures

In addition to the above, it is recommended to read:

- Berk, J., De Martzo, P., Harford, J. 2023 "Fundamentals of Corporate Finance" Pearson publications, 6th edition
- The finance related journals, such as: Journal of Finance, Review of Financial Studies, Journal of Financial and Quantitative Analysis, Journal of Financial Economics, Review of Finance, Financial Analysts Journal, Journal of Corporate Finance, Journal of Applied Corporate Finance, Financial Management, etc.
- Financial periodicals/papers: Financial Times, Economist, Wall Street Journal, Nautemporik, among others
- Web pages with international market and corporate news including: www.investing.com, www.reuters.com, www.bloomberg.com

Useful Databases for data collection:
Reuters, Bloomberg, Datastream, Web pages of Companies and Stock Exchanges.

Other references - publications in the area which may be used during lectures

• Black F., "Beta and Return," *Journal of Portfolio Management* 20 (Fall 1993), pp. 8–18.
• Brav A., J. R. Graham, C. R. Harvey, and R. Michaely, "Payout Policy in the 21st Century," *Journal of Financial Economics* 77 (September 2005), pp. 483–527.
• Brennan M. J., "Corporate Investment Policy," *Handbook of the Economics of Finance, Volume 1A, Corporate Finance,* eds. G. M. Constantinides, M. Harris, and R. M. Stulz (Amsterdam: Elsevier BV, 2003).
• Campbell J. Y., "Asset Pricing at the Millennium," *Journal of Finance* 55 (August 2000), pp. 1515–1567.
• Dittmar A., "Corporate Cash Policy and How to Manage It with Stock Repurchases," *Journal of Applied Corporate Finance* 20 (Summer 2008), pp. 22–34.
• Graham J. and C. Harvey, "How CFOs Make Capital Budgeting and Capital Structure Decisions," *Journal of Applied Corporate Finance* 15 (spring 2002), pp. 8–23.
• Harris M. and A. Raviv, "The Theory of Capital Structure," *Journal of Finance* 46 (March 1991), pp. 297–355.
• Mehra R. and E. C. Prescott, "The Equity Risk Premium in Prospect," in *Handbook of the Economics of Finance,* eds. G. M. Constantinides, M. Harris, and R. M. Stulz (Amsterdam, North-Holland, 2003).
• Miles J. and R. Ezzell, "The Weighted Average Cost of Capital, Perfect Capital Markets, and Project Life: A Clarification," *Journal of Financial and Quantitative Analysis* 15 (September 1980), pp. 719–730.

• Miller M. H., “The Modigliani-Miller Propositions after Thirty Years,” *Journal of Applied Corporate Finance* 2 (Spring 1989), pp. 6–18.
• Petersen M. A. and R. G. Rajan, “Trade Credit: Theories and Evidence,” *Review of Financial Studies* 10 (Fall 1997), pp. 661–692.
• Rajan R. G. and L. Zingales, “What Do We Know about Capital Structure? Some Evidence from International Data,” *Journal of Finance* 50 (December 1995), pp. 1421–1460.