Program: FPM

Course Title: Capital Structure and Valuation

Course Instructor: Prof. Ram Kumar Kakani

Course Objective: The objective of the course is to introduce research scholars to the issues that link capital structure decisions with the valuation of firms. After going through this course, research scholars are expected to develop a thorough understanding of the nature of the interaction between capital structure and valuation that have influenced researchers over past five decades.

Session Plan

Session 1

Valuation of Fixed Income Securities I

Reading: Kim, I.J., Ramaswamy, K., & Sundaresan, S.1993.Does default risk in coupons affect the valuation of corporate bonds? : A contingent claims model. ***Financial Management.***22:3, pp.117-131

Session 2

Valuation of Fixed Income Securities II

Reading: Asness, C.S. 2000. Stocks vs. bonds: Explaining the equity risk premium. ***Financial Analysts Journal. 56:2,*** pp.96-113.

Session 3

Valuation of Stocks I

Reading: Baginski, S.P. & Wahlen, J.M. 2003. Residual income risk, intrinsic values and share prices. ***The Accounting Review***, 78:1, pp.327 -351.

Session 4

Valuation of Stocks II

Reading: Bradshaw, M.T. 2004. How do analysts use their earnings forecasts in generating stock recommendations? ***The Accounting Review***. 79:1, pp.25-50.

Session 5

Valuation of Stocks III

Reading: Welch, I. 2004.Capital structure and stock returns. ***The Journal of Political Economy***. 112:1, pp. 106-132.

Session 6

PE and PEG Ratios

Reading: Easton, P.D. 2004. PE ratios, PEG ratios and estimating the implied expected return on equity capital. ***The Accounting Review***.79:1, pp. 73-95.

Session 7

Capital Structure Question and the Pie Theory

Reading: Harris, M. & Raviv, A.1991. The theory of capital structure. ***The Journal of Finance***. 46:1, pp.297-355.

Session 7

Propositions of Modigliani and Miller

Reading: Miller, M.H.1988. The Modigliani-Miller propositions after thirty years .***The Journal of Economic Perspectives,*** 2: 4, pp. 99-120.

Session 8

Financial Leverage and Firm Value

Reading: Stewart, M.C.2001. Capital structure. ***The Journal of Economic Perspectives***. 15:2, pp.81-102

Session 9

Optimal Capital Structure

Reading: Scott, J.A.Jr. 1976. A theory of optimal capital structure. ***The Bell Journal of Economics.*** 7:1, pp.33-54.

Session 10

Leverage and Stock Price under Corporate Taxes

Reading: Brennan, M.J. & Schwartz, E.S. 1978. Corporate income tax, valuation and the problem of optimal capital structure. ***The Journal of Finance.***51:1, pp.103-114.

Session 11

Limits to the Use of Debt

Reading: Leland, H.E. 1998. Agency costs, risk management, and capital structure. ***The Journal of Finance.*** 53:4, pp.1213-1243.

Session 12

The Pecking Order Theory

Reading: Rajan, R.G. & Zingales, L. 1995. What do you know about capital structure? : Some evidence from international data. ***The Journal of Finance.*** 50:5, pp. 1421-1460.

Session 13

Growth and the Debt-Equity Ratio

Reading: Vanderbilt University roundtable on the capital structure puzzle .1998***. The Journal of Applied Corporate Finance,*** pp.8-24.

Session 14

Determinants of Capital Structure

Reading: Barclay, M.J. & Smith, C.W. 2005. The capital structure puzzle: The evidence revisited. ***The Journal of Applied Corporate Finance,*** 17:1, pp. 8-17.

Session 15

Valuation and Capital Budgeting for the Levered Firm

Reading: Masulis, R.W.1983. The impact of capital structure change on firm value: Some estimates. ***The Journal of Finance***.38:1, 107-126.

Session 16

Adjusted Present Value Approach to Valuation

Reading: Morck, R., Shleifer, A & Vishny, R.W.1988. Management ownership and market valuation. ***Journal of Financial Economics.*** 20, pp.293-315

Session 17

Flow to Equity Approach to Valuation

Reading: Adsera, X. & Vinolas, P. 2003. FEVA: A financial and economic approach to valuation. ***Financial Analysts Journal.*** 59:2, pp.80-87.

Session 18

Weighted Average Cost of Capital Approach to Valuation

Reading: Sanders, W.G. & Boivie, S. 2004. Sorting things out: Valuation of new firms in uncertain markets. ***Strategic Management Journal***. 25:2, pp.167-186.

Session 19

Estimation of the Discount Rate

Reading: Ang, A. & Liu, J. 2004. How to discount cash flows with time-varying expected returns. ***The Journal of Finance.***59:6, pp. 2745 -2783.

Session 20

Beta, Leverage and Firm Value

Reading: Chen, W.P., Chung, H., Hsu, T.L. &Wu, S. 2010. External financing needs, corporate governance and firm value. ***Corporate Governance: An International Review.*** 18:3, pp.234-249

Evaluation:

50% on assignments.

50% on a written test at the end of the course.

Reference Books:

1) Ross, S.A., Westerfield, R.W., Jaffe., J. & Kakani, R.K. 2008. ***Corporate Finance,*** 8th Edition, Tata McGraw-Hill.
2) Brealey, R.A., Myers, S.C., Allen, F. & Mohanty, P.2007.Principles of Corporate Finance, 8th Edition, Tata McGraw-Hill.
3) Grinblatt, M., & Titman. S.2002. ***Financial Markets and Corporate Strategy***, 2nd Edition, Irwin/McGraw-Hill.
4) Damodaran, A. 2006. ***Damodaran on Valuation***, 2nd Edition, Wiley India
5) Koller, T., Goedhart, M. & Wessels, D. (McKinsey & Co). 2005. ***Valuation***. 4th Edition, John Wiley & Sons.
