



## Case Seminar Advanced Corporate Finance

Tuesday 10:00 – 13:00, Room 23

Team: Tim Adam & Jan Wilimzig

This case seminar discusses real-world business cases, which relate to the materials covered in *Finance Theory* and *Advanced Corporate Finance*. The main topics are company valuation, capital structure, bankruptcy, corporate governance, project finance and corporate risk management. The main objective of the seminar is to apply the theoretical concepts of corporate finance and corporate governance to real-world situations. To do so we will discuss six Harvard Business School cases. In addition, there will be several company presentations of real-world business cases.

This seminar has a high level of practical relevance, but it is also very labor intensive. Expect to spend at least eight hours each week on case preparations.

### Prerequisites

All participants must have successfully passed *Finance Theory*, and take *Advanced Corporate Finance* parallel or prior to this case seminar.

### Registration

Students need to register for this seminar. Please submit your applications electronically (CV, most recent transcript) to Mrs. Bulwahn by April 10. If you do not attend the first session, your place may be given to other students on the waiting list.

### Evaluation

Five case reports (80%), class participation (20%). Seminar attendance is obligatory.

## Course materials

Cases can be purchased from HBSP for a total cost of approx. US\$ 26.00 using a credit card: <http://cb.hbsp.harvard.edu/cbmp/access/78627783>

Additional readings are available from Moodle (**Password: CS2017**)

## Preliminary Outline

Date	Topic	HBS Case No.
April 17	Introduction - Learning with cases	
April 24	1. Team meeting	
May 1	Vereinigung Hamburger Schiffsmakler und Schiffsagenten e.V. (VHSS): Valuing Ships	9-210-058
May 8		
May 15	<b>Winfield Refuse Management, Inc.: Raising Debt vs. Equity</b>	<b>9-913-530</b>
May 22		
May 29	<b>Bankruptcy and Restructuring at Marvel Entertainment Group</b>	<b>9-298-059</b>
Jun 5		
Jun 12	<b>Kennecott Copper Corp.</b>	<b>9-278-143</b>
Jun 19		
Jun 26	<b>Stone Container Corp. (A)</b>	<b>9-297-047</b>
Jul 3		
Jul 10	<b>Iridium LLC</b>	<b>9-200-039</b>
Jul 17	<b>Iridium LLC (continued)</b>	

## KPMG International Case Competition

The best performing students will be invited to participate in KPMG's annual international case competition in the Fall (KICC). Information about this competition can be found at the following website.

<https://home.kpmg.com/xx/en/home/careers/graduates/kpmg-international-case-competition.html>

## Case teams

All seminar participants must form teams consisting of four students. You can make use of the bulletin board on Moodle to find teammates. Students who are not part of a complete team by the end of the first week of class will be allocated randomly to other incomplete teams.

Each team should try to find reasonable answers to all cases and be prepared to present their solutions in class. Since the cases are challenging, you are unlikely to grasp the main ideas/problems within a few days. You should therefore start working on each case two weeks ahead of the case discussion in class. It is advisable that teams meet at least twice to discuss a particular case. The discussion of the case questions within your team is crucial for understanding and “solving” a case. Therefore, it is not advisable to assign different questions to different team members, but to work on all questions together. Note, there is not always a right or wrong answer.

The workload for preparing the case reports and presenting a case question in class should be shared equally among all members of a team. If you experience any free-rider problems you should inform Prof. Adam as soon as possible. All complaints will be handled absolutely confidentially. At the end of the semester there will be a confidential peer evaluation, which may affect your grade for the case reports and hence your overall seminar grade.

## Case reports

Case reports must be submitted for the four cases printed in **bold** in the course outline. They consist of answers to the study questions below. Good case reports are concise, brief, and to the point. The maximum number of pages for a case report is 6-9 pages, using a 12-point font. Make sure you adequately address all study questions. If the strategy options given are insufficient in your opinion then feel free to consider additional options.

Support any claims you make by references to the information given in a case, graphs, or figures. Good case reports do not contain vague statements or guesses. It is possible that the information in a case does not provide enough information to form a clear judgment. It is common that decision makers need to make decisions under incomplete and imperfect information. Try to refrain from making wild guesses.

The purpose of the cases is to **apply** the financial concepts covered in *Corporate Finance* and *Advanced Corporate Finance*. You need not explain these concepts in your case reports, but can assume that the reader is familiar with the relevant theory.

Any spreadsheet printouts provided should be *self-contained*, i.e., one should be able to understand the information given in a table without relying on the main text of the analysis. Tables should include all your assumptions as well as the formulas that are not immediately transparent.

Both a hardcopy of your report and a computer file containing the report are due at the beginning of the class the case is scheduled for discussion. The computer file that contains the report should be sent as an e-mail attachment. Use the following file name convention: *Case x Team y.pdf*. Since we discuss the case solutions in class, late reports cannot be accepted.

Case reports that include plagiarism will receive zero credit. Each case report must contain the following statement, signed by all team members.

*"We hereby declare that we as a team have worked on this report independently and not received any help from others or used any unauthorized materials, such as internet solutions, answer keys, reports submitted others, etc. All sources, including sources from the Internet, that we have reproduced in either an unaltered or modified form (particularly sources for texts, graphs, tables and images), have been acknowledged by us as such. We understand that violations of these principles will result in proceedings regarding deception or attempted deception."*

### **Class participation**

Your class participation grade will depend on your presentations and the quality (not the quantity!) of your comments/remarks in class, which are a function of the depth of your preparation. Quality includes sound, rigorous, and insightful diagnoses, sharpening of key issues under discussion, relating theory to a particular case, asking relevant questions, etc. To make sure you receive credit for your class participation, you should **display your name card at all times** during the class. Given that there is no exam in this course, class participation is the main way of individual evaluation.

## Case questions

### **Vereinigung Hamburger Schiffsmakler und Schiffsagenten e.V. (VHSS): Valuing Ships**

1. Based on prices from comparable transactions, how would you assess the reasonableness of the Bet Performer's \$133 million purchase price in May 2008?
2. How much was the golden Wing worth in January 2009? Is this value more, less, or the same as its purchase price of \$27 million?
3. Which valuation method, using comparable ship prices or DCF, is more appropriate for the valuation of ships?
  - a. Under what conditions are market prices for ships likely to equal their fundamental values?
  - b. Under what conditions are market prices likely to deviate from fundamental values in the market for ships specifically and in markets for other assets more generally (e.g., houses, shares of stock, etc.)? Consider both positive and negative deviations.
  - c. What permits or prevents large and long-lasting deviations in the shipping market?
4. As a ship owner or a ship lender (e.g., Deutsche Schiffsbank), would you adopt the Hamburg Ship Evaluation Standard? What are the arguments for and against adoption? What are the alternatives?
5. As a German bank regulator (e.g., an executive at the BaFin), would you approve the use of the Hamburg, Ship Evaluation Standard (HSES)? Why, or why not?

### **Winfield Refuse Management, Inc.: Raising Debt vs. Equity**

1. What are the annual cash outlays associated with the bond issue? The common stock issue?
2. How would you respond to each director's assessment of the financing decision?
3. How should the acquisition of MPIS be financed, taking into account the issues of control, flexibility, income, and risk??

### **Marvel Entertainment Group**

1. Why did Marvel file for Chapter 11? Were the problems caused by bad luck, bad strategy (flawed business model), or bad execution?

2. Evaluate the proposed restructuring plan (the one proposed in Jan. 1997). What are the details of the plan? Will the plan solve Marvel's problems?
3. How much is Marvel's equity worth (in \$/share) under the proposed restructuring plan, assuming it acquires Toy Biz as planned? Why is it sensible to use the CCF method here? (Assume a long-term market risk premium of 7.5%.) Consider performing a sensitivity analysis of your assumptions. Hint: In Exhibit 9, the position "Provision for income taxes" contains actual taxes paid as well as provisions for not yet paid (deferred) taxes. These provisions are shown under the header "CASH FLOW DATA".
4. How does your valuation compare with Perelman's investment at \$0.85/share and the current market value of Marvel? What is your assessment of Perelman's financial projections and liquidation assumptions? Why is Perelman interested in making an equity investment in Marvel?
5. As a public debt holder, would you vote for or against the proposed restructuring plan? Why, or why not? How would you expect Carl Icahn and the other secured and unsecured creditors of Marvel to vote? Hint: What options do public debt holders have, and how much would they gain under each alternative?
6. Optional: Why did the price of Marvel's zero-coupon bonds drop on Tuesday, November 12, 1996? Why did portfolio managers at Fidelity and Putnam sell their bonds on Friday, November 8, 1996? Did they break any rules/laws?

### **Kennecott Copper Corp.**

1. Analyze the economic rationale of the Carborundum acquisition. Under what conditions would an acquisition be expected to add to shareholder value in general? Do any of these reasons apply to the Carborundum acquisition?
2. Kennecott's management team determined, based on Exhibit 7, that the value of Carborundum to Kennecott would be about \$70-\$85 per share (page 7). Critically evaluate the methodology used to determine this value.
3. Use the information given in Exhibit 7 to determine the value of Carborundum to Kennecott using the **Flow-to-Equity Method**. Assume that the market risk premium ( $E_{r_M} - r_f$ ) based on short-term rates equals 8.3%. The betas given in Exhibit 4 and 5 refer to equity betas.

4. Why is management pursuing the acquisition? As an outside director of the board, how would you argue and vote on the resolution to tender for Carborundum?
5. Review management's decisions over the 10 years covered by the case, including the acquisition of Peabody, its divestiture, the proposed use of the proceeds of the Peabody sale and the selection of Carborundum as an acquisition target. What were the motivations underlying these decisions? Were they in the best interest of shareholders?
6. Optional: Critically evaluate the actions and recommendations by Kennecott's financial advisors (Morgan Stanley and First Boston) and its legal advisors (Sullivan and Cromwell).

### **Stone Container**

1. What was the basis of Stone Container's successful growth during its first fifty years? What was the product market strategy? What was its financial strategy? How did Roger Stone's management of the company compare to that of his predecessors?
2. Describe Stone's current financial condition. What would be the impact on its financial situation if paper prices rebounded? How efficient are Stone's operations?
3. How would a recovery of paper prices affect Stone's current financial condition? Estimate the effect on earnings and cash flows of a \$50 (and \$100) per ton industry-wide increase in prices.
  - a. Assume Stone Container's sales volume approximates its 1992 production level of 7.5 million tons per year, while costs remain the same. Also assume a 35% tax rate.
  - b. What would be the effect under both these pricing scenarios if production and sales volume increased to full capacity of 8.3 million tons per year? For simplicity, assume costs per ton remain constant.
4. What should be Stone Container's long-term financial strategy? What capital structure do you recommend?
5. What should Stone Container do now? Develop a financial plan, which sees it through the rest of the paper-pricing cycle, and restore it to some degree of financial stability. Hints: What are Stone's financing needs for 1993? How should these needs be met, i.e., how much debt should be issued, if any? How much equity should be issued, if any?

## Iridium LLC

1. Assuming the market was rational at the time (i.e. market prices reflect fundamental values), how much was Iridium worth on a per share basis at the end of 1998 according to the projections in Exhibit 5? What are the important determinants of value? How confident are you in your answer? (Please assume the long-term market risk premium equals 7.5%)
2. What caused Iridium to fail: was it a bad strategy, bad execution, or bad luck? Was Iridium's financial structure to blame for its ultimate failure? Why, or why not?
3. With regard to Iridium's financial strategy, did it have the wrong target capital structure, issue the wrong kinds of capital, or issue capital in the wrong sequence? Which capital structure theory justifies its target debt-to-total book capitalization ratio of 60%?
4. Why did Motorola finance Iridium with project debt instead of corporate debt?
5. What lessons regarding the financing of large, Greenfield projects do you draw from this case study?



## Confidential Peer Evaluation

Your Name:

Team No:

This evaluation is strictly confidential. Your personal response will not be made available to the other group members or any other member of the class.

- Please rate each group member, including yourself, on his/her contribution to the case report which you submitted using the following scale.

4 *Excellent Contributor* - The person significantly contributed to our case discussions. Without this person, the quality of the final case report would have been considerably diminished.

3 *Good Contributor* - The person contributed to our case discussions. Without this person, the quality of the final case report would have been diminished.

2 *Marginal Contributor* - The person barely contributed to our case discussions. Without this person, the quality of the final case report would have been about the same.

1 *Unsatisfactory Contributor* - The person failed to contribute in any meaningful way to our case discussions. Other members of the group had to do more because of this person's performance. Without this person, the quality of the final case reports may actually have been improved.

DK *Don't Know* - I don't have enough information about the person's performance to assess his/her contribution reliably.

Name (include yourself!)	Report I	Report II	Report III	Report IV	Report V	Overall

- Please provide any additional comments if possible. In particular, explain significant differences in the evaluations of your team members, if any.