UNIVERSITY OF ROCHESTER

William E. Simon Graduate School of Business Administration

Finance 423/523
Corporate Financial Policy & Control
Spring 2013
Th 1:00-4:00

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This course will cover the theory and evidence concerning major corporate financial policy decisions. FIN 423/523 discusses alternative methods of issuing and retiring securities, mergers and acquisitions, and the market for corporate control. We will have one class meeting per week. Grading will be flexible – students will have input to determine what type of evaluation procedure will be used.

The reading assignments will be announced in class and will more or less follow the sequence given below. I have included additional references, ***which are not required***, for students who want more information on particular topics. These are not on reserve, but copies of these journals are available in the Management Library (and they are available electronically through the Management Library). There are a few ***recommended*** texts for this course:

J. Fred Weston, Mark L. Mitchell, and Harold Mulherin, *Takeovers, Restructuring, and Corporate Governance*, (4th ed.), Prentice-Hall, New York, 2004, ISBN-10: 0131407376 [referred to as "*WMM*" in the reading assignments].

Stuart C. Gilson, *Creating Value Through Corporate Restructuring: Case Studies in Bankruptcies, Buyouts, and Breakups*, (2nd ed.), Wiley, New York, 2010, ISBN: 978-0-470-50352-2.

Donald Chew, The New Corporate Finance: Where Theory Meets Practice, (3rd ed.), McGraw-Hill, 2001, ISBN-10: 007233973X. [Articles in the Chew book are indicated by "(*DC*)" in the list below.]

Richard Brealey, Stewart Myers, and Franklin Allen, *Principles of Corporate Finance*, (10th ed.), McGraw-Hill, New York, 2010, ISBN-10: 0073530735.

Finally, and perhaps most important, I would like all of the students in the class to read the *Wall Street Journal* or some similar publication on a regular basis since the topics covered in this course are discussed regularly in this newspaper.

Relation to Other Finance Courses

This course is targeted at Ph.D. students who are interested in being exposed to the theoretical and empirical literature on securities offerings and mergers and acquisitions (M&A). Highly motivated MBA students are also encouraged to participate in the course, but should understand that the expectations and workload will not be typical of most MBA courses.

Expectations of Student Performance

My expectations are that students will come to class prepared by having read the necessary material. The lectures will not rehash the readings. Rather, we will discuss different perspectives on the arguments presented in the readings. Active, high quality class participation will enhance the grades of students who are near margins in the final grade distribution.

I will hand out notes to accompany some of the lectures. Occasionally, I will also hand out stories reproduced from the popular business press (e.g., the *Wall Street Journal*). Class attendance is very important to successful completion of this course. If you know that you will be unable to attend more than a few of the classes, you should probably not register for this course. If you know that you have to be late for class, or leave early, please show courtesy to the rest of the class (and to me) by entering and leaving the room as discretely as possible. If you miss a class, or are late in arriving, it is your responsibility to obtain copies of any handouts that were distributed in class [***do not rummage around on the teaching desk looking for handouts if you arrive late!***] I suggest that you form study teams and help each other out -- get extra copies of handouts for missing team-mates. I will not provide an inventory of class handouts for people who miss class, but most of the handouts will be available on the class web page (see below).

There may be some guest lecturers (other faculty members and Ph.D. students). In addition, every student who is registered for the course to be responsible for leading the discussion of one or more related papers during some part of the course (MBA students may work in a group to prepare and lead the discussion). Of course, I will be available to help you plan your lecture, and I will supplement what you say in class. You should find a topic that interests you and volunteer early.

Grading

The grading for this course will be based on a flexible system. All Ph.D. students will be required to write a paper, and groups of MBA students will also be expected to write a paper. There may be a few homework assignments (in addition to the replication assignment mentioned previously), which for MBA students may be “reading responses” that describe your thoughts on particular assigned readings. PhD students may be asked to write “referee’s reports” on particular papers. There will be no exams.

The topic of the paper can be anything related to the course. I will approve paper topics that are unconventional, but you do not need to ask permission to write a paper on a topic similar to those listed below. For MBA students, these papers should simulate a business research report to your boss. For example, if you are analyzing a potential merger, you might pretend that you are a junior staff member of an investment banking firm (or one of the companies involved in the transaction), and I (your boss) have asked you to report your analysis and recommendations concerning the merger (for example, Is the price a 'good' one? Why? What are the purported gains from this merger? Does the stock market think it is a wise transaction for our company or the other company? Are there likely to be regulatory problems or litigation? etc.) You may ask for general guidance as you might ask your boss, but don't come and ask me what you should write because I (your boss) expect you to be able to do this analysis yourself. Examples would be:

(1) an event study on price performance of new issues in recent years;
(2) an analysis of the use of "real options" methods in valuing IPOs (with an example);
(3) a case study (similar to Ruback's paper on Conoco) on a major acquisition, spin-off, or proxy fight. Students in the past have studied Chase-Lincoln, Norstar-Security, Xerox-Crum & Forster, Computer Consoles-N.B.I., and Kodak-Sterling Drug;
(4) a case study of the performance of a successful merger or tender offer from 1 to 5 years after it was completed;
(5) or any other topic that I approve.

Course Information on the World Wide Web (WWW)

Most of the materials for this course will be posted on the home page for this course [http://schwert.simon.rochester.edu/f423/f423.htm]. For example, I plan to post copies of the slides used in the classroom presentations as Adobe Acrobat files (so they can be viewed and printed from the WWW). In addition, I have collected lists of sites that students can use to collect information on security prices (if you want to do an event study), on financial news, on securities filings with the S.E.C. (if you want to study a particular IPO prospectus, for example), and so forth. I want to encourage all students to use this resource throughout the course. One possible "paper" that students might do is to create web pages that would allow future students to analyze particular types of deals that are discussed in this course (e.g., information and data sources, examples of similar transactions, etc.) If you are interested in pursuing that option, please see me early in the quarter.

Topics and Readings

Required readings are indicated with an asterisk "*" Additional journal articles, ***which are not required***, are included for students who want more information on particular topics. These are not on reserve in the library, although copies of the *Journal of Financial Economics*, the *Journal of Finance*, and the *Review of Financial Studies* are available in the Management Library (and available online through these links if you are logged into the UR network).

I. Introduction to the Course

Smith, Clifford W., "Raising Capital: Theory and Evidence," (*DC*, 277-293).

Brealey, Myers & Allen, Ch. 14 and 15.

Henderson, Brian J., Narasimhan Jegadeesh and Michael S. Weisbach, "World markets for raising new capital," *Journal of Financial Economics*, 82 (October 2006) 63-101.

II. Venture Capital and Initial Public Offerings of Common Stock

*Ritter, Jay and Ivo Welch, "A Review of IPO Activity, Pricing, and Allocations," *Journal of Finance*, 57 (August 2002) 1795-1828.

*Lowry, Michelle and G. William Schwert, "IPO Market Cycles: Bubbles or Sequential Learning?" *Journal of Finance*, 57 (June 2002) 1171-1200.

*Lowry, Michelle and G. William Schwert, "Is the IPO Pricing Process Efficient?" *Journal of Financial Economics*, 71 (January 2004) 3-26.

*Lowry, Michelle Micah S. Officer, and G. William Schwert, "The Variability of IPO Initial Returns," *Journal of Finance*, 65 (April 2010) 425–465.

*Gao, Xiaohui, Jay R. Ritter, and Zhongyan Zhu, "Where Have All the IPOs Gone?"

Abrahamson, Mark, Tim Jenkinson, and Howard Jones, "Why Don't U.S. Issuers Demand European Fees for IPOs?" *Journal of Finance*, 66 (December 2011) 2055–2082.

Acharya, Viral V., Oliver F. Gottschalg, Moritz Hahn, and Conor Kehoe, "Corporate Governance and Value Creation: Evidence from Private Equity," *Review of Financial Studies*, 26 (2013) 368-402.

Aggarwal, Rajesh K., Laurie Krigman, and Kent L. Womack, "Strategic IPO Underpricing, Information Momentum, and Lockup Expiration Selling," *Journal of Financial Economics*, 66 (October 2003) 105-137.

Aggarwal, Reena, "Stabilization Activities by Underwriters after Initial Public Offerings,"

Journal of Finance, 55 (June 2000) 1075–1103.

Aggarwal, Reena, "Allocation of Initial Public Offerings and Flipping Activity," *Journal of Financial Economics*, 68 (April 2003) 111-135.

Aggarwal, Reena, and Pat Conroy, "Price Discovery in Initial Public Offerings and the Role of the Lead Underwriter," *Journal of Finance,* 55 (December 2000) 2903–2922.

Aggarwal, Reena, Nagpurnanand R. Prabhala, and Manju Puri, "Institutional Allocation in Initial Public Offerings: Empirical Evidence," *Journal of Finance,* 57 (June 2002) 1421–1442.

Altı, Aydoğan, "IPO Market Timing," *Review of Financial Studies*, 18 (2005) 1105-1138.

Amihud, Yakov, Shmuel Hauser, and Amir Kirsh, "Allocations, Adverse Selection, and Cascades in IPOs: Evidence from the Tel Aviv Stock Exchange," *Journal of Financial Economics*, 68 (April 2003) 137-158.

Ang, James S. and James C. Brau, "Concealing and Confounding Adverse Signals: Insider Wealth-maximizing Behavior in the IPO process," *Journal of Financial Economics*, 67 (January 2003) 149-172.

Aruğaslan, Onur, Douglas O. Cook, and Robert Kieschnick, "Monitoring as a Motivation for IPO Underpricing," *Journal of Finance*, 59 (October 2004) 2403–2420.

Asquith, Daniel, Jonathan D. Jones, and Robert Kieschnick, "Evidence on Price Stabilization and Underpricing in Early IPO Returns**,"** *Journal of Finance,* 53 (October 1998) 1759-1773.

Atanasov, Vladimir, Vladimir Ivanov, and Kate Litvak, "Does Reputation Limit Opportunistic Behavior in the VC Industry? Evidence from Litigation against VCs," *Journal of Finance*, 67 (December 2012) 2215–2246.

Ball, Eric, Hsin Hui Chiu, and Richard Smith, "Can VCs Time the Market? An Analysis of Exit Choice for Venture-backed Firms," Review of Financial Studies, 24 (2011) 3105-3138.

Barry, Christopher B., Chris J. Muscarella, John W. Peavy III, and Michael R. Vetsuypens, "The Role of Venture Capital in the Creation of Public Companies: Evidence from the Going-Public Process," *Journal of Financial Economics*, 27 (September 1990) 447-471.

Beatty, Randolph P. and Jay R. Ritter, "Investment Banking, Reputation, and the Underpricing of Initial Public Offerings," *Journal of Financial Economics*, 15 (1986) 213-232.

Benninga, Simon, Mark Helmantel and Oded Sarig, "The Timing of Initial Public Offerings," *Journal of Financial Economics*, 75 (January 2005) 115-132.

Benveniste, Lawrence M., Alexander Ljungqvist, William J. Wilhelm Jr., and Xiaoyun Yu, "Evidence of Information Spillovers in the Production of Investment Banking Services," *Journal of Finance*, 58 (April 2003) 577–608.

Black, Bernard S. and Ronald J. Gilson, “Venture Capital and the Structure of Capital Markets: Banks versus Stock Markets,” *Journal of Financial Economics*, 47 (March 1998) 243-277.

Bodnaruk, Andriy, Eugene Kandel, Massimo Massa, and Andrei Simonov, “Shareholder Diversification and the Decision to Go Public,” *Review of Financial Studies*, 21 (2008) 2779-2824.

Bradley, Daniel J., Bradford D. Jordan, and Jay R. Ritter, “The Quiet Period Goes out with a Bang,” *Journal of Finance,* 58 (February 2003) 1–36.

Brau, James C., and Stanley E. Fawcett, “Initial Public Offerings: An Analysis of Theory and Practice,” *Journal of Finance,* 61 (February 2006) 399–436.

Braun, Matías, and Borja Larrain, “Do IPOs Affect the Prices of Other Stocks? Evidence from Emerging Markets,” *Review of Financial Studies*, 22 (2009) 1505-1544.

Brav, Alon and Paul A. Gompers, “Myth or Reality? The Long-run Underperformance of Initial Public Offerings: Evidence from Venture and Non-venture Capital-backed Companies,” *Journal of Finance*, 52 (December 1997) 1791-1822.

Brav, Alon, and Paul A. Gompers, The Role of Lockups in Initial Public Offerings *Review of Financial Studies,* 16 (2003) 1-29.

Brav, Omer, “Access to Capital, Capital Structure, and the Funding of the Firm,” *Journal of Finance*, 64 (February 2009) 263–308.

Brennan, Michael J., and Julian Franks, “Underpricing, ownership and control in initial public offerings of equity securities in the U.K.,” *Journal of Financial Economics*, 45 (September 1997) 391-413.

Busaba, Walid Y., Lawrence M. Benveniste, and Re-Jin Guo, “The Option to Withdraw IPOs during the Premarket: Empirical Analysis,” *Journal of Financial Economics*, 60 (April 2001) 73-102.

Cao, Jerry, and Josh Lerner, “The performance of reverse leveraged buyouts,” *Journal of Financial Economics*, 91 (February 2009) 139-157.

Carter, Richard B., Frederick H. Dark, and Ajai K. Singh, “Underwriter Reputation, Initial Returns, and the Long-Run Performance of IPO Stocks,” *Journal of Finance*, 53 (February 1998) 285-311.

Carter, Richard, and Steven Manaster, “Initial Public Offerings and Underwriter Reputation,” *Journal of Finance*, 45 (September 1990) 1045–1067.

Celikyurt, Ugur, Merih Sevilir, and Anil Shivdasani, "Going public to acquire? The acquisition motive in IPOs," *Journal of Financial Economics*, 96 (June 2010) 345-363.

Chambers, David, and Elroy Dimson, "IPO Underpricing over the Very Long Run," *Journal of Finance*, 64 (June 2009) 1407–1443.

Chemmanur, Thomas J., "The Pricing of Initial Public Offerings: A Dynamic Model with Information Production," *Journal of Finance*, 48 (March 1993) 285–304.

Chemmanur, Thomas J., and P. Fulghieri, "A theory of the going-public decision," *Review of Financial Studies*, 12 (1999) 249-279.

Chemmanur, Thomas J., Shan He, and Debarshi K. Nandy, "The Going-Public Decision and the Product Market," *Review of Financial Studies*, 23 (2010) 1855-1908.

Chemmanur, Thomas J., Gang Hu, and Jiekun Huang, "The Role of Institutional Investors in Initial Public Offerings," *Review of Financial Studies*, 23 (2010) 4496-4540.

Chemmanur, Thomas J., Karthik Krishnan, and Debarshi K. Nandy, "How Does Venture Capital Financing Improve Efficiency in Private Firms? A Look Beneath the Surface," *Review of Financial Studies*, 24 (2011) 4037-4090.

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Cornelli, Francesca, and David Goldreich, "Bookbuilding: How Informative Is the Order Book?," *Journal of Finance*, 58 (August 2003) 1415–1443.

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Cronqvist, Henrik, and Mattias Nilsson, "The choice between rights offerings and private equity placements," *Journal of Financial Economics*, 78 (November 2005) 375-407.

Cumming, Douglas, "Contracts and Exits in Venture Capital Finance," *Review of Financial Studies*, 21 (2008) 1947-1982.

Da, Zhi, Joseph Engelberg, and Pengjie Gao, "In Search of Attention," *Journal of Finance*, 66 (October 2011) 1461–1499.

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Demers, Elizabeth and Katharina Lewellen, "The Marketing Role of IPOs: Evidence from Internet Stocks," *Journal of Financial Economics,* 68 (June 2003) 413-437.

Degeorge, François, François Derrien, and Kent L. Womack, "Analyst Hype in IPOs: Explaining the Popularity of Bookbuilding," *Review of Financial Studies,* 20 (2007) 1021-1058.

Degeorge, François, François Derrien, and Kent L. Womack, "Auctioned IPOs: The US evidence," *Journal of Financial Economics*, 98 (November 2010) 177-194.

Derrien, François, IPO Pricing in "Hot" Market Conditions: Who Leaves Money on the Table?," *Journal of Finance*, 60 (February 2005) 487–521.

Derrien, François, and Ambrus Kecskés, The Initial Public Offerings of Listed Firms," *Journal of Finance*, 62 (February 2007) 447–479.

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Dewenter, Kathryn L., and Paul H. Malatesta, Public Offerings of State-Owned And Privately-Owned Enterprises: An International Comparison," *Journal of Finance*, 52 (September 1997) 1659–1679.

Dunbar, Craig G., "The Use of Warrants as Underwriter Compensation in Initial Public Offerings," *Journal of Financial Economics*, 38 (May 1995) 59-78.

Dunbar, Craig G., "Factors Affecting Investment Bank Initial Public Offering Market Share," *Journal of Financial Economics*, 55 (January 2000) 3-41.

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Edwards, Amy K. and Kathleen Weiss Hanley, "Short selling in initial public offerings," *Journal of Financial Economics* s, 98 (October 2010) 21-39.

Ellis, Katrina, "Who Trades IPOs? A Close Look at the First Days of Trading," *Journal of Financial Economics*, 79 (February 2006) 339-363.

Ellis, Katrina, Roni Michaely, and Maureen O'Hara, "When the Underwriter Is the Market Maker: An Examination of Trading in the IPO Aftermarket," *Journal of Finance*, 55 (June 2000) 1039–1074.

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Field, Laura Casares, and Gordon Hanka, "The Expiration of IPO Share Lockups," *Journal of Finance*, 56 (April 2001) 471–500.

Field, Laura Casares, and Jonathan M. Karpoff, "Takeover Defenses of IPO Firms," *Journal of Finance*, 57 (October 2002) 1857–1889.

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Hanley, Kathleen Weiss and Gerard Hoberg, "Litigation risk, strategic disclosure and the underpricing of initial public offerings," *Journal of Financial Economics*, 103 (February 2012) 235-254.

Hanley, Kathleen Weiss and William J. Wilhelm, "Evidence on the Strategic Allocation of Initial Public Offerings," *Journal of Financial Economics*, 37 (February 1995) 239-257.

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Hao, Qing, "Laddering in initial public offerings," *Journal of Financial Economics*, 85 (July 2007) 102-122.

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