Corporate Finance I

Academic Year: (2022 / 2023) **Review date: 09-05-2022**

Department assigned to the subject: Business Administration Department

Coordinating teacher: TOLDRA SIMATS, ANNA

Type: Electives ECTS Credits : 5.0

Year : 1 Semester : 2

REQUIREMENTS (SUBJECTS THAT ARE ASSUMED TO BE KNOWN)

To have followed a course of microeconomics, some basic notions of econometrics and some notions of financial economics.

OBJECTIVES

The objective is to give a comprehensive picture of the modern literature of corporate finance. The classes will combine theoretical and empirical models. Also the students will use a database to replicate the results of some important papers on the literature of corporate finance.

DESCRIPTION OF CONTENTS: PROGRAMME

PART 1

TOPIC 1. Corporate financing under moral hazard
1.1/ Outside financing capacity with limited liability and risk neutrality
a) The fixed investment model and credit rationing
b) The continuous investment model
c) The problem of debt overhang and the renegotiation solution
1.2/ Determinants of borrowing capacity
a) Diversification
b) Collateral
c) Group lending
1.3/ Exercises:
a) Choosing one contract in the optimal set
b) Relaxing limited liability and risk neutrality
b) Reputational capital

References: Tirole book, chapters 3, 4 and 5

TOPIC 2. Corporate financing under asymmetric information
2.1/ Introduction
2.2/ The lemons problem and the market breakdown
a) Privately-known prospects model
b) Market breakdown and cross-subsidization
c) Application: The negative stock price reaction to SEO's
2.3/ Dissipative signals
a) Application 1: Payout policy
b) Application 2: IPO underpricing
2.4/ Exercises:
a) Signalling

References: Tirole book, chapter 6

TOPIC 3. Passive and active monitoring
3.1/ Introduction

3.2/ The benefits and costs of monitoring:
a) The reduction of credit rationing
b) Over-monitoring and managerial initiative
c) Other costs: illiquidity and collusion
3.3/ Monitoring vs advising
3.4/ Exercises:
a) Choosing the optimal monitoring intensity
b) The monitor as a third party vs the monitor as an investor.

PART 2:

Topic 1. Liquidity and risk management
- Maturity of liabilities
- Liquidity-scale tradeoff
- Hedging risk

Topic 2. Product markets
- Impact of competition on financial choices
- Profit destruction and benchmarking effects
- Commitment through financial structure

Topic 3. Credit rationing and economic activity
- Moral hazard
- Adverse selection
- Loanable funds and the credit crunch

SUMMARY:
The corporate finance course can be divided into two parts. The first part covers financial contracting decisions under the two well-known agency problems: moral hazard and asymmetric information. The second part covers the role of monitors and advisors in corporate decisions. This course covers mainly theoretical models. The objective is to give you, through theoretical modeling, a basic set-up to understand the trade-offs present in agency problems in financial contracting. Also, how different mechanisms help in the resolution of those problems.

The current fashion in corporate finance research is mainly empirically driven. But you need to know theory to do good empirical research. This course provides the theory behind most of the empirical contributions and also some insight on empirical evidence.

LEARNING ACTIVITIES AND METHODOLOGY

4 problem sets

ASSESSMENT SYSTEM

% end-of-term-examination:	60
% of continuous assessment (assigments, laboratory, practicals…):	40

Final grade is 60% the grade of the exam and 40% problem sets. A minimum score of 4.00 is required in the final exam to pass the subject

Students that do not meet the minimum passing grade should retake the subject. If the resit is taken, the above grade criteria also apply

BASIC BIBLIOGRAPHY

- Jean Tirole The theory of corporate finance, Princeton University Press, 2010

- João Amaro de Matos Theoretical Foundations of Corporate Finance , Princenton University Press, 2001

- Oliver Hart Firms, Contracts, and Financial Structure , Clarendon Press, 1993