

Part D

Corporate Finance

I. Review of Valuation

We have learned at the outset of the course that:

- Corporate financial decisions often reduce to valuing CFs.
- Values of CFs are determined in financial markets.

We have learned the following about valuation:

1. Two characteristics of a CF: timing and risk
2. A CF can be valued by arbitrage:
 - Find a matching CF using traded assets
 - The given CF has the same value as the matching CF.
3. Market prices reflect available information.
4. Time value of money:
 - Term structure of interest rates
5. Risk premium:
 - CAPM
 - APT.

Now we apply what we know to corporate financial decisions.

II. Issues in Corporate Finance

1. Investment Decisions (capital budgeting):

- Which investments should the firm take?
- How should its assets be used?

2. Financing Decisions:

- How should the firm finance its investments?
 - Internal funds vs. external funds
 - Debt vs. equity
 - Public vs. private equity
 - Bonds vs. bank debt . . .

3. Payout Decisions (dividend policy)

- What to pay out vs. retain inside the firm?
 - Level of Dividends
 - Cash vs. share repurchases
 - Acquisitions . . .

4. Risk Management Decisions (hedging policies)

- Which risks should the firm hedge?
- How much should the firm hedge?
- How should the firm hedge these risks?