Corporate Value

Corporate Value

- What is the goal of the firm?
- Operating Assets vs. Nonoperating Assets

The Corporate Valuation Model

- The Value of the Firm's Operations:
  = ______________________________
  Discounted at __________________

- Recall:
  - FCF = NOPAT – Net Investment in Operating Capital
  - Non-constant Growth Stock Valuation

The Corporate Valuation Model

- The Value of a Firm
  = Value of the Firm's Operations + Value of the Firm's Nonoperating Assets

  - Includes Value of Current Assets-in-place

    and

  - Present Value of Growth Opportunities

Corporate Valuation: Example #1

- Consider a firm that just finished the year with $20 million in free cash flows. The firm has a WACC of 10 percent and you expect cash flows to grow at 5 percent for the foreseeable future. In addition, the firm has $100 million in marketable securities, $200 million in debt, $50 million in preferred stock. The book value of equity is $210 million. What is the value of the firm? What is the value of common equity?

Corporate Valuation: Example #2

- Consider a firm that plans to expand by borrowing $40 million and using internal funds. The firm has a 10 percent WACC, 10 million shares outstanding, and currently does not have any debt or pay dividends. Free cash flows are forecast to be -$5 million next year, $10 million and $20 million the following two years, respectively, and grow at 6 percent thereafter. What is the value per share?

What determines firm value?

Corporate Governance

- The Goal of the Firm:
- The Goal of Corporate Governance:
- 3 Elements of Corporate Governance:
  - Managerial Entrenchment
  - Compensation
  - Effective Monitoring by the Board of Directors

Managerial Entrenchment

- What is managerial entrenchment?
- Preventing hostile takeovers:
  - Targeted Share Repurchases (Greenmail)
  - Shareholder Rights Provisions (Poison Pills)
  - Restricted Voting Rights

Compensation

- Stock Options
  - What are they?
  - Why are they good?
  - Why might they be bad?
- ESOPs
  - What are they?
  - Why are they good?
  - Why might they be bad?

Effective Monitoring by the Board of Directors

- Inside vs. Outside Directors
- Chairman vs. CEO Titles
- Interlocking Boards
- Institutional Investors/Blockholders
- Compensation Through Shares/Options
- Staggered Boards

Chapter 10 Suggested Problems

- Questions:
  - 10-3 and 10-4