



## Course Syllabus (Spring Semester)

**FNCE 4303: Advanced Issues in Asset Allocation and Portfolio Management --- 3 Credits**  
**Instructor:** Patrick A. Terrion **Office:** Finance Dept. **Office Hours:** Tue, Thurs 4pm to 5pm  
& by appointment

**Pre-requisites:** FNCE 3101 and FNCE 3302

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**Course Description:** In this course, we study and interpret methodologies used to value a business, including models such as Discounted Cash Flow (DCF), Relative metrics including business and transaction comparables, Contingent Claim Valuation and Liquidation Value to assess the worth of a business. We also evaluate specific business models that companies pursue to create competitive advantage – including toll gate positioning, segregation vs. integration, and organic vs. mechanistic strategies.

### **Text:**

Koller, Goedhart, and Wessels (2010) **Valuation: Measuring and Managing the Value of Companies,** (Fifth Edition); John Wiley & Sons

### **Required Cases:**

**Stonewall Kitchen** 805006-PDF-ENG

**Cola Wars Continue: Coke and Pepsi in 2010** 711462-PDF-ENG

**Nantucket Nectars** 898171-PDF-ENG

**McDonald's Corporation (Abridged)** 603041-PDF-ENG

**Acquisition of Consolidated Rail Corp. (A)** 298006-PDF-ENG

**Acquisition of Consolidated Rail Corp. (B)** 298095-PDF-ENG

**Microsoft in 2005** 705505-PDF-ENG

**John D. Rockefeller and the Creation of Standard Oil** 807110-PDF-ENG

**IBM in the 21<sup>st</sup> Century – Evolution or Revolution** 9308105-PDF-ENG

**Harley-Davidson: Preparing for the Next Century** 906410-PDF-ENG

**Henry Heinz: Making Markets for Processed Foods** 801289-PDF-ENG

**Boston Beer Co., Inc.** 196138-PDF-ENG

**Kodak and the Digital Revolution (A)** 705448-PDF-ENG

**The Southeast Bank of Texas in the Financial Crisis** 310141-PDF-ENG

**Kohler Company (A)** 205034-PDF-ENG

**Facebook** 808128-PDF-ENG

**Knight the King: The Founding of Nike** 9810077-PDF-ENG

**Coursepack link:** <https://cb.hbsp.harvard.edu/cbmp/access/32113652>

### **Course Objectives:**

- (1) To recognize the business models that influence the success and achievement of a company. (The term “business” refers to the dynamic nature of Finance, Marketing, Operations, Human Resources and Technology; and how these interact to create a business model to maximize shareholder wealth.)
- (2) To become aware of various business models and the approach to diagnosing the drivers that create business value.
- (3) To examine and critique various valuation tools that measures the value of a business and an investment.
- (4) To develop proficiency in the analysis, administration, and interpretation of a business and its valuation.
- (5) To demonstrate the strong correlation between business and investing skills that are needed to succeed in the business and investment world---using case studies, team discussions, and group presentations.



## **Topical Outline: Business and Investing Strategy – Business Valuation**

**Course Introduction: Second Semester** (week 1)

**Business Valuation---Quantitative** (week 2)

Evaluating key approaches to business valuation---Discounted Cashflow Valuation, Relative Valuation, Contingent Claim Valuation, Liquidation Value)

### ***BUSINESS VALUATION & MIND MAP LECTURES***

**Discussion on Valuing a Business---Qualitative & Quantitative**

Evaluating key qualitative attributes that create value in a business---(Achieving competitive advantage, Toll gate strategy, Segregation vs. Integration, Organic vs. Mechanistic)

**Stonewall Kitchen Case** (week 3)

Jonathan King and Jim Stott, the founders of Stonewall Kitchen, started out in 1992 with a simple business selling jams and jellies at local farmers' markets. By 2004, they had grown the company into a \$25 million organization with 250 employees. They expanded their range of services to include high-end specialty food manufacturing and wholesaling, as well as retailing through free-standing stores and catalogs. King, who serves as president and CEO, set an aggressive growth goal: to quadruple the business to \$100 million within the next five years.

#### **Case questions:**

- **If you were a private equity firm interested in Stonewall Kitchen, what is your value of the company?**
- **How did you arrive at this valuation?**
- **What would you look for from Jonathan King in order to meet his proposed value of Stonewall Kitchen?**
- **How would you construct the deal with Jonathan King as a private capital investor?**

**Cola Wars Continue: Coke and Pepsi in 2010** (week 4)  
**Complete Valuations of Coca-Cola and PepsiCo**

This case examines the industry structure and competitive strategy of Coca-Cola and Pepsi over 100 years of rivalry. Coca-Cola and Pepsi-Cola had vied for the "throat share" of the world's beverage market. The most intense battles of the cola wars were fought over the \$74 billion CSD industry in the United States, where the average American consumes 46 gallons of CSD per year. In a "carefully waged competitive struggle," from 1975 to the mid-1990s, both Coke and Pepsi had achieved average annual growth of around 10%, as both U.S. and worldwide CSD consumption consistently rose. Coke and Pepsi look to continue this growth into the next century.

#### **Case questions:**

- **When analyzing the beverage industry and its competitors, specifically Coca-Cola and PepsiCo during the past 100 years – why has Coke not achieved complete dominance of this industry when they had several opportunities over the past century?**
- **What are the key factors for Coca-Cola's and PepsiCo's success that led to their industry dominance?**
- **What is the value of Coca-Cola? PepsiCo?**

**Nantucket Nectars** (week 5)

The founders of Nantucket Nectars are trying to decide whether to sell their company. This case describes how the founders started the company and grew the Nantucket Nectars brand name. We examine guerilla marketing in a difficult industry, and the development of a brand. We also discuss the analysis when thinking about selling a brand.

**Case questions:**

- What are the key relationships that have helped Tom and Tom build Nantucket Nectars to date?
- What relationships do they need to develop in order to continue to thrive in this business?
- What are the pros and cons of remaining independent? Going public? Selling the company?
- What do you think management should do?
- As an advisor to Tom and Tom, what do you propose as the minimum bid they should accept for Nantucket Nectars?

**McDonald's Corp. (Abridged)**

(weeks 5 & 6)

**Complete Valuation of McDonald's**

McDonald's has, over many years, built a strategy based on consistency and quality through a limited product range. Competitive forces have drawn the company into a much wider variety of foods and services to maintain growth. Now, new competitors threaten to beat McDonald's at its own, original game. We evaluate the approaches and dangers arising from business dominance and the identification of capabilities that create a long-term competitive advantage.

**Case questions:**

- During the 1950's and 1960's there were many fast food hamburger restaurants competing in America - McDonald's, Burger King, Carrols, Wendy's, Jack-in-the-Box, White Castle, Hardees, Sandy's, etc. However, McDonald's emerged as the absolute dominant force in the fast food business. What areas can you cite throughout this case that led to McDonald's gaining such a tremendous competitive advantage in their industry, and permanently neutralizing their competitors?
- What is the value of McDonald's?

**Acquisition of Consolidated Rail Corp. (A)**

(week 6)

On October 15, 1996, Virginia-based CSX and Pennsylvania-based Consolidated Rail (Conrail), the first and third largest railroads in the eastern United States, announced their intent to merge in a friendly deal worth \$8.3 billion. This deal was part of an industry-wide trend toward consolidation and promised to change the competitive dynamics of the Eastern rail market. Shareholders must decide whether to tender shares into the front-end of a two-tiered acquisition offer. To make this decision, they must value Conrail as an acquisition target and understand the structure of CSX's offer.

**Case questions:**

- What do you think as a shareholder you should do – accept or reject the CSX offer?
- What is your value of Conrail?
- What qualitative and quantitative evidence can you use to support your valuation of Conrail?

**Acquisition of Consolidated Rail Corp. (B)**

(week 7)

Eight days after CSX announced it was going to buy Consolidated Rail (Conrail) for \$88.65 per share, Norfolk Southern made a hostile bid for Conrail. Over the next several months, the potential acquirers upped their bids while exchanging criticism in the popular press, prompting analysts to call this one of the nastiest takeover battles of the 1990s.

**Case questions:**

- What are your thoughts on Norfolk Southern's hostile bid approach for Conrail?
- How would you have approached a potential offer for Conrail?
- What do you think Norfolk Southern sees that supports their value for Conrail?

**Microsoft in 2005; John D. Rockefeller and the Creation of Standard Oil**

(week 8)

This case focuses on Bill Gates' strategy for sustaining competitive advantage in the global software industry. We also explore Microsoft's history and its current position, as the company attempts to diversify its product and service revenue streams. We learn the strategic aspects of company positioning and achieving long-term sustainability.

In comparison to Bill Gates, we reconstruct the entrepreneurial journey of John D. Rockefeller, founder of Standard Oil and one of the most famous business figures in history. This case traces his early career as a retailer in Cleveland through his decision to enter the oil industry in the early 1860s to his creation of Standard Oil. We emphasize the critical decades of the 1870s and 1880s when Standard Oil and the larger oil business were growing at white-hot speed. We also examine Rockefeller's (controversial) strategy for securing and maintaining Standard Oil's market dominance, his organizational innovations within the company, and his responses to a myriad of competitive threats.

#### **Case questions:**

- **Microsoft Windows was copied from Apple, who took the Graphic User Interface code from the Xerox. What led to Microsoft's dominance in the software industry? What is Bill Gates' business genius?**
- **What are the similarities between Bill Gates' and John D. Rockefeller's business strategy?**
- **Why is Microsoft's dominance being threatened today?**
- **What do you think Microsoft can do to regain its dominance in the software industry?**
- **What is the value of Microsoft?**

#### **IBM in the 21<sup>st</sup> Century – Evolution or Revolution**

(week 9)

Members of IBM's fifth Integration and Values Team (IVT5) were close to finishing their deliberations. Convened by Sam Palmisano, Chairman and CEO, and sponsored by Jon Iwata, Senior VP of Corporate Communications and Marketing, and John E. Kelly III, Senior VP and Director of Research, the IVT5's focus was on "the global IBMer"-define and develop global leaders; make the "globally integrated enterprise" relevant to all employees through corporate citizenship initiatives reflective of the company's values; and help IBM compete globally by ensuring market access. The scope was all 170 countries in which IBM operated. As leaders who had risen to their positions as systems thinkers committed to innovation, the team knew it was necessary to stand back and look at the big picture-to see how IBM worked now and operate at its best in order to understand the gaps, dilemmas, and opportunities.

#### **Case questions:**

- **In 1990 IBM experienced a shake-up that brought the company to an inflection point, necessitating a turnaround. What led to IBM's complacency and loss of competitive advantage in the late 1980s?**
- **What could IBM have done differently to avoid a revolutionary turnaround under Lou Gerstner?**
- **Under Lou Gerstner, what did IBM do to become relevant in the technology industry?**
- **What did Palmisano's team do to ensure IBM did not meet another disruptive inflection point?**
- **Why do you think their strategic plan has faltered? What should Ginni Rometty do to put IBM on track?**
- **What is the value of IBM?**

#### **Harley-Davidson: Preparing for the Next Century** (week 9)

Harley-Davidson Co. exemplifies a remarkable management-led business transformation of a long standing manufacturing company. The company successfully met global competition and continues to innovate to maintain its market position. Given the company's past success, you will need to evaluate the opportunities for Harley-Davidson to build value into the future.

#### **Case questions:**

- **What has contributed to Harley-Davidson being viewed by consumers as "different and unmatched" compared to competitors?**
- **How has Harley-Davidson been able to achieve their "brand status"?**
- **What can Harley-Davidson do to strengthen their brand and market position in the future?**
- **What is the value of Harley-Davidson?**

#### **Henry Heinz: Making Markets for Processed Foods** (week 10)

This case outlines many of the supply-side innovations, such as improved transportation, communication, and technological developments that greatly expanded the productive capacity of the United States in the late 19th century. This case also explores a range of demand -side shifts, including rising incomes,

population growth, and urbanization, that changed consumers' wants and needs in the past century, leading up to the present Berkshire Hathaway and 3G Capital purchase of Heinz.

**Case questions:**

- It is 1865, and you are analyzing investment opportunities for J.P. Morgan. How would you evaluate the size and potential profit opportunities of the market for processed food?
- How did Henry Heinz view Emerging markets?
- Why did Henry Heinz fail at food processing in 1875, yet succeed five years later?
- It is 2013, and you are analyzing investment opportunities for Warren Buffett. How would you evaluate the size and potential profit opportunities of the global market for processed food?
- What do you think is the value of Heinz today? How would you support this value?

**Boston Beer Co., Inc.**

(week 11)

The capital markets may have overcapitalized the craft brewing industry during a flurry of new IPOs. In the context of a "hot" IPO market each individual company's valuation may seem reasonable. However, after careful analysis of each company's financial statement and upon consideration of analysts' forecasts of the industry's growth prospects, it is unclear whether the craft brewing industry is overcapitalized.

**Case questions:**

- What are your thoughts about the valuations of the public craft brewing companies?
- How does Boston Beer's market position compare to other craft brewing companies?
- If you were hired as an investment banker by Boston Beer, what would you advise? Why?
- What do you think is the value of Boston Beer as they consider their IPO?
- Looking back, how did the craft brewing IPO's work out for investors?

**Kodak and the Digital Revolution (A)**

(week 11)

The introduction of digital imaging in the late 1980s had a disruptive effect on Kodak's traditional business model. This case examines Kodak's strategic efforts and challenges as the photography industry evolves. After discussing Kodak's history and its past strategic moves in the new landscape, the case questions how CEO Daniel Carp can use digital imaging to revitalize Kodak. We review the results of Kodak's strategy to create value, and its eventual demise.

**Case questions:**

- What contributed to Kodak's eventual demise as a dominant company in the film business?
- What business do you think Kodak was in?
- What could management have done differently in the 1990's to position Kodak for the future?
- What could management do today to ensure Kodak's survival?
- What is the value of Kodak?

**The Southeast Bank of Texas in the Financial Crisis** (week 12)

The Southeast Bank of Texas, like most other financial institutions in the US, had fallen on hard times during the financial crisis of 2008. Now, in March 2009, the bank is faced with several choices as a result of the new reforms spawned from the financial crisis: The FDIC's Temporary Liquidity Guarantee Program and the US Treasury's Capital Purchase Program. Additionally, the implementation of BASEL II has left new regulations in place for capital requirements for banks. Irwin Greff, President and CEO of the Southeast Bank, faces several decisions on how to proceed with these new policies that will surely shape the future of the bank.

**Case questions:**

- What factors contributed to the financial crisis of 2008?
- Do you think the financial crisis could have been avoided? How?
- What do you think are the capital needs for the Southeast Bank of Texas?
- What should Irwin Greff and the Southeast Bank of Texas do? Why?

**Kohler Co. (A)**

(week 12)

Kohler Co., best known for its plumbing fixtures, is a large, private family firm. As part of a recapitalization aimed at preserving family ownership of Kohler Co., nonfamily shareholders, who held 4% of common stock, were required to sell their shares to the company. A group of dissenting shareholders filed a lawsuit claiming that the buyout price undervalued their shares by a factor of five. In April 2000, Herbert V. Kohler, Jr., chairman and CEO, had to decide whether to settle with the dissenters and, if so, at what share price.

**Case questions:**

- **Why is there such a disparity between the Kohler family valuation of the company vs. the dissenting shareholders?**
- **What do you think is the value of Kohler Company?**
- **If you were Mr. Kohler, what would you do?**

**“The Social Network”**

(week 13)

This film case focuses on Mark Zuckerberg's entrepreneurial challenges in bringing Facebook from a bootstrap startup to social network dominance – our discussion includes business ownership, financial backing, along with the personal and legal issues that resulted in bringing Facebook to fruition.

**Facebook**

In September 2011, Facebook registered its 800 millionth user, cementing its position as the largest online social network in the world. Facebook was cash-flow positive and its revenue was estimated to be \$4.27 billion in 2011. Despite these successes many observers believed that the current business model, which relied on advertising, offered limited growth opportunities. The emergence of Google+ and Twitter as a serious competitors provided additional challenges. On the verge of the company's initial public offering (IPO), it was critical for Facebook to find solutions to these problems.

**Case questions:**

- **Why do people use Facebook and what do they do when they are there?**
- **How successful is advertising on Facebook? Can this revenue stream be annuitized? Why, or why not?**
- **How successful is Facebook fan pages?**
- **What are your thoughts on Facebook Platform and Facebook for Websites?**
- **What is Facebook's business model? How sustainable is their business model?**
- **What is the value of Facebook?**

**FINAL EXAM - Knight the King: The Founding of Nike**

It had taken Phil Knight sixteen long years to build Nike into the number one athletic-shoe company in the country. When Knight had first conceived of the company for an MBA class project, Adidas had had more than 80% market share, but Knight's marketing approach had revolutionized the industry, his company had developed several ground-breaking shoe technologies, and Nike's brand had become one of the most recognizable in the world. In 1980, the same year that Nike had knocked Adidas off its throne, Nike had gone public and Knight, its founder-CEO, still owned close to half of the company. He had led the company through dramatic changes as it evolved from a scrappy start-up to a large public company. However, now, barely half a decade later, Knight had just received the news that Nike itself had been dethroned by Reebok, an upstart competitor. Knight closeted himself in his office, faced the wall, and sat there, weak and sick and devastated for hours.

**Case questions:**

- **Was Nike's success due to the business skills of Phil Knight, or by luck and circumstance? Explain.**
- **How did Nike change the athletic apparel industry, and what other companies have successfully duplicated their business model? Unsuccessfully? Why?**
- **How has Nike's business model impacted global labor practices and the socio-economic environment?**
- **How could Knight have avoided the crisis posed by Reebok's growth?**
- **What was the value of Nike in 1981, their first year after going public in 1980? What is the value of Nike today?**



**Chapter coverage-- Valuation: Measuring and Managing the Value of Companies**

<b>Topic: Value metrics:</b>	<b>chapters 2-5</b>
<b>Frameworks for valuation &amp; free cash flow:</b>	<b>chapters 6 &amp; 7</b>
<b>Analyzing and Forecasting performance:</b>	<b>chapter 8 &amp; 9</b>
<b>Estimating continuing value:</b>	<b>chapter 10</b>
<b>Estimating the cost of capital:</b>	<b>chapter 11</b>
<b>Calculating and interpreting results:</b>	<b>chapter 12 &amp; 13</b>

**GRADING:**

<b>Class Participation/Case Preparation:</b>	<b>90%</b>
<b>Final Exam</b>	<b>10%</b>

**Class Participation & Case Summaries**

Class Participation & Case Summaries will involve your ability to isolate and interpret key case factors, and reach conclusions regarding the case to be reviewed in class. Prior to the class discussion on each case, you will be asked to hand in your “two-page” summary/conclusions, along with a valuation for the assigned case. Each written summary will count toward 3% of the final grade, along with class participation in each case of 3%, for a total 90% possibility of the class grade generated between written summaries and participation.

**Final Exam**

*The final exam will be a case study that will be completed within the allotted final exam timeframe. You will be required to provide a complete in-depth analysis of the case, and answer the case questions with a breakdown of your personal thoughts and perspective. You will also be required to complete a valuation using the various valuation methodologies learned throughout the semester as part of the final case analysis.*