INTERNATIONAL MANAGEMENT INSTITUTE, BHUBANESWAR
PROGRAMME NAME: PGDM
FN 620: Business Valuation
CREDIT: 3
SESSION DURATION: 90Minutes

TERM: IV
YEAR: 2014
BATCH: 2012-14

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Course Overview

Valuation plays a key role in many areas of finance -- in corporate finance, in mergers and acquisitions and in portfolio management. This course gives detailed insights about the valuation process. The premise of this course is that we can make reasonable estimates of value for most assets, and that the same fundamental principles determine the values of all types of assets, real as well as financial. Some assets are easier to value than others, the details of valuation vary from asset to asset, and the uncertainty associated with value estimates is different for different assets, but the core principles remain the same. The course is also geared towards enabling students to determine the factors which drive corporate value and to develop strategies to enhance company's value.

The course examines the three basic valuation approaches that can be used to value an asset. The first, discounted cashflow valuation, relates the value of an asset to the present value of expected future cashflows on that asset. The basis of this approach is that we buy most assets because we expect them to generate cash flows for us in the future. There are three inputs that are required to value any asset in this approach – the *expected cash flow*, the *timing* of the cash flow and the *discount rate* that is appropriate given the riskiness of these cash flows. The second, relative valuation, estimates the value of an asset by looking at the pricing of 'comparable' assets relative to a common variable like earnings, cashflows, book value or sales. The basis of this approach is that we essentially put our trust in markets getting the values right, at least on average. The third, contingent claim valuation, uses option pricing models to measure the value of assets that share option characteristics. A contingent claim or option is an asset which pays off only under certain contingencies - if the value of the underlying asset exceeds a pre-specified value for a call option, or is less than a pre-specified value for a put option. The basis of this approach is that discounted cash flow models understate the value of assets with option characteristics. The understatement occurs because DCF models value assets based upon a set of expected cash flows and do not fully consider the possibility that firms can learn from real time developments and respond to that learning. For example, an oil company can observe what the oil price is each year and adjust its development of new reserves and production in existing reserves accordingly rather than be locked into a fixed production schedule.

While they can yield different estimates of value, one of the objectives of this course is to explain the reasons for such differences, and to help in picking the right model to use for a specific task. The models

discussed under various approaches provide a range of tools that analysts/valuers will find of use, but the cautionary note is - valuation is not an objective exercise, and any preconceptions and biases that an analyst brings to the process will find their way into the value.

Learning Outcomes

After undergoing this course, the participants will be able to:

- Explain the role and need for valuation
- Describe various approaches to valuation
- Compute the value of a company
- Differentiate between various approaches of valuation in different context, examination of quality of earnings and other balance sheet related items
- Determine the value drivers for a company
- Criticize the valuation of other analysts

Evaluation Criteria

Component	Description	Weight(%)
Mid term	It will be based on the syllabus covered till date. The question paper will be designed in a manner to evaluate the understanding of concepts and application of concepts taught in the course.	20
End term	It will be based on entire syllabus. The question paper will be designed in a manner to evaluate the understanding of concepts and application of concepts taught in the course.	40
Quizes	There shall be four quizzes (equally weighted), two before and two after mid-term examinations.	20
Project	It will be on group (group of 2-3 students) basis. Project will involve ascertainment of earnings quality and its implications for corporate value.	20

Text Book

- Chandra, Prasanna., *Corporate Valuation and Value Creation*, TMH (PC)

References-

- Palepu, Healy, Bernard, Business Analysis & Valuation, CENGAGE Learning, Indian 3rd Edition, 2010
- Copeland, Koller & Murrin, Valuation : Measuring and Managing the Values of Companies, Wiely & Sons, USA, 3rd Edition, 2009
- Chandra Prasanna, Corporate Valuation and Value Creation, TMH

Session Wise Schedule

Session	Topic	Requirements: Reading/Cases	Learning Outcomes
Module 1: Introduction			
1	Introduction of Course (course overview, assessment scheme, instructor's expectations) Approaches to valuation	PC: Chapter 1	Understanding in principal, DCF approach, Relative Valuation approach and Option Valuation approach
Module 2: Discounted Cash Flow Valuation			
2	Estimation of Cost of Equity	PC: Chapter 3 Excel based exercise	Capability to analyze equity risk and measure it.
3	Estimation of fundamental Betas	PC: Chapter 3 Exercise: Calculate Beta of Nifty 50 companies	Understanding of fundamental determinants of beta
4	Estimation of Cost of Debt	PC: Chapter 3	Measurement of default risk and default spread
5	Estimation of WACC/Hurdle rate	PC: Chapter 3	Capability to measure overall cost of capital
6-7	Forecasting Cash Flows, Continuing Value	PC: Chapter 2	To develop the capability to ascertain growth drivers in an industry and a company and forecast the company's future growth chart.
8	Practice session on forecasting cash flows	Exercises	To develop the capability to forecast cash flows.
9	Dividend-Discount Model	PC: Chapter 3 Numerical Exercises	Using the model for valuation of equity; awareness about strengths and weaknesses of the model
10	Free-Cash-Flow-To-Equity Discount model	PC: Chapter 3 Numerical Exercises	Using the model for valuation of equity; awareness about strengths and weaknesses of the

			model
11-12	Valuing a Firm: The Free-Cash-Flow-To-Firm Approach	PC: Chapter 4 Numerical Exercises	Capability to use the model for valuation of firm ; awareness about strengths and weaknesses of the model
13	Adjusted Present Value Approach to Firm Valuation	PC: Chapter 4	Capability to use the model for valuation of firm.
Module 3: Relative Valuation			
14	Basic principles of relative valuation	PC: Chapter 5	Understanding of the process of relative valuation technique; capability to use relative valuation multiples wisely
15	Equity multiples	PC: Chapter 5	Ability to determine fundamental equity multiples and use them in relative valuation
16	Value multiples	PC: Chapter 5	Fundamental derivation of enterprise value multiples and their usage.
17	Introduction to mergers & acquisitions		To understand basics of M&A
18	Valuation issues in M&A		To apply the concept of valuations in M&A valuations
19	Group Presentations on valuation projects	Project 1: ITC Project 2: HPCL Project 3: L&T	To discuss the issues in valuation through their projects
20	Group Presentations on valuation projects	Project 4: Asian Paints Project 5 : Apollo Tyres	To discuss the issues in valuation through their projects