Business Valuation and Analysis Using Financial Statements (15.535)
Who?

• Professor Peter Wysocki – “Peter”
• Office Hours:
  – Anytime … Make appointment by e-mail.
When?

- Section “A”
- Section “B”

- Attending Other Sections:
  - Check with me first …. Usually “No Problem”
What?

• Primary Objectives
  – Provide knowledge to help you get a great job.
  – Provide information for job interview questions.
  – Promote you as MIT students – website.
  – Learn how to use financial information to Value and Analyze firms.
  – Apply your economics/accounting/finance skills to issues in today’s news to help understand:
    • What is contained in financial reports
    • Why firms report certain information
    • How to be a sophisticated user of this information.
What … My objectives

• My objective is not to make your life miserable.
• My objective is not to overload you with irrelevant assignments or make-work tasks.
• My objective is to make this class relevant, useful, stimulating, fun and enjoyable.
  – You have many commitments … But, the lowest-cost, lowest effort approach to benefit from and “cruise” through this class is to attend class.
  – Basically, I am serving it to you on “silver platter.”
Why?

• Provide up-to-date applied knowledge of:
  – Fundamental valuation techniques
  – Pitfalls of accounting reports
  – “Reading between-the-lines” of financial reports.

• Very useful for your career as:
  – Financial analyst, I-banker, consultant, etc.

• Discuss up-to-date and “hot” topics that companies face today.
  – This information will be extremely useful for your job interviews and your job.
How?

• Coursepack
  – There is no required coursepack! I will provide handouts and lecture notes during each class.

• Lecture Notes & Class Handouts
  – Also accessible through the class server prior to each class. If you are missing material for a particular class, please obtain them from the Web to make sure you do not fall behind.
How … Prep for Class

• Short reading assignments from the text and handouts will be provided at the end of each class.
• The textbook chapters to be covered in the next class will be listed in the class handouts.
• We will not cover every part of each chapter in the text! Concentrate your efforts on the short assigned readings.
How … Grading

- 6 "e-assignments" (count best 5) 50 pts
- 2 Quizzes (in class) 200 pts
- Analyst Reports/Presentation (Team) 150 pts
- Class Contribution (Particip/other) 100 pts
- Total 500 pts
How … Assignments

• These _short_ applied assignments will be assigned about 1 week before each due date.
• You may work alone or in a team of up to 4 students.
• Be prepared to discuss and defend your (or your team’s) analysis during the class discussion on the due date!
How … Analyst Reports

• Student teams (up to 4 students) will be responsible for creating and presenting an analyst report on a company of their choice.
• This comprehensive analysis is similar to the reports generated by Wall Street analysts.
How … Classroom Approach

- The classes will be casual, fun and informal.
- I think the best way to learn is through numerous examples. Therefore, we will examine many interesting “cases” from the today’s financial press on topics of current importance.
- To keep things lively, I will ask questions and get your input during class. My questions are not intended to put you on the spot … I am a very easygoing and forgiving person 😊!
Financial Statement Information

• Used extensively by internal users
  – Management at various levels
    • Performance evaluation
    • Competitive analysis
    • Investment decisions
    • Valuation of targets
  – Current and future employees
    • Is this firm going to meet its payroll and will the stock options be worth anything?
Financial Statement Information

• Used primarily by external users
  – Financial intermediaries (analysts)
    • Stock recommendations
  – Lenders
    • Loan decisions
    • Monitoring
  – Investment bankers
    • Valuation for M&A and IPO
    • Top management performance evaluation
Financial Statement Analysis

• Financial statement analysis and business analysis applications
  – Focus is more than a mechanical analysis of financial statements.
  – Draw heavily on your understanding of finance, economics, marketing, and strategy.
    • Combine that understanding with financial statement information to diagnose problems and come up with solutions/recommendations
What the course is **NOT** about

- Extreme details of financial reporting rules and financial statement preparation.
- T-accounts and journal entries.
Market Efficiency and the Role of Financial Statement Analysis

• Implications of stock market efficiency:
  • Many profit-maximizing, actively competing traders
  • Information almost freely available to all participants
  • Competition means that the full effects of new information on intrinsic values are reflected instantaneously in prices
  • Stock prices rapidly adjust to new information such that the new price promises only a normal rate of return to an investor

• If markets are efficient, then what’s the use of “Fundamental Analysis” and Valuation?
Market Efficiency and the Role of Financial Statement Analysis

• Conflicting evidence on market efficiency
  – Markets are Efficient:
    • Market’s reaction to news events is instantaneous.
    • Mutual funds have on average been unable to outperform broad indexes; in fact, generally under-performed.
    • Why publish “secrets” instead of making money yourself?.
  – Markets are Inefficient:
    • Growing evidence of “easy ways” to beat market.
    • Greater acceptance of “Behavioral Explanations” for stock market fluctuations.
Market Efficiency: What is My View?

- I am not dogmatic about efficiency.
  - Let the evidence accumulate and speak for itself.
  - Then you can decide.
- On the other hand, financial (stock) markets are very competitive.
  - It is **not** easy to make money above the expected rate for return for a given level of (beta) risk.
  - Trading strategies are not free of risk (Long Term Capital).
- Regardless of your allegiance, knowing state-of-the-art techniques and lingo from the “The Street” (post-earnings announcement drift, PEG ratio, B/M effect) will certainly help get you a great job!
Where Next? .. Prep for next week

1) Make sure you register on class server!

2) Form teams for assignments and the Analyst Project (maximum of 4 people). Submit the names of your team members (and e-mails) to me on a piece of paper by end of Next Class.

3) Next Class … Valuation Basics.
   - Preparation: Review your Finance Notes on DCF (or skim section in Brealy and Myers)