Chapter 9 Notes

Legal Rights of Shareholders

- Elect Board of Directors
  - Indirectly control business
  - Can vote in person, often vote by proxy
- Proxy Fight
  - Soliciting enough shareholder proxy votes to oust management and replace them is called a proxyfight
- Takeover
  - When a corperation takes over another corperation by buying a majority of outstanding shares and forcing a "take-all" clause
- Ways to Prevent takeovers
  - Managers with less than 50% of ownership want to prevent takeovers
  - They may push for election cycles of electing 1/3 of board memebers each year to prevent a full takeover in a single year
  - They may vote to require 75% of shareholders to trigger the takeall clause
  - They may put a poison pill provision that allows managers to buy an aquiring companies shares at bargain price to avoid mergers
- Preemptive Right
  - Right to purchase shares to be issued at a preemtive rate
  - Reasons for Preemptive right
    - Prevents corperation for making tons of shares and buying them up for itself
    - Protect stockholders from a dilution of share value by the minting of new shares

Types of Stock

- Classified Stock
  - Class A,B,...,Z\
  - Different classes have different rules and voting rights
  - Class A is typically common stock
  - Class B is typically priority voting stock (aka founders shares)
    - Doesn't require you to own a majority of $ in the company to still retain control

Stock Valuation

Discounted Dividend Model:

- $D_t =$ Dividend Expected to be recieved at the end of year t. $D_0, ..., D_t$
- $P_0 =$ actual market price of stock today
- $\hat{P}_t =$ both the expected price and expected intrinsic value of the stock at year t
- $g =$ expected growth rate g in dividends predicted by an investor
- $r_s =$ required rate of return on the stock based on expected risk, inflation, and other factors from chap. 8.
- $\hat{r}_s =$ actual rate of return after it is known
- $\frac{D_1}{P_0} =$ dividend Yield expected during the coming year
- $\frac{(\hat{P}_1 - P_0)}{P_0} =$ expected capital gains yeild on the stock during the coming year.
- Expected Total Return
  - $\hat{r}_s =$ expected dividend yeild + expected capital gains yeild
  - $\hat{r}_s = \frac{D_1}{P_0} + \frac{(\hat{P}_1 - P_0)}{P_0}$

Expected Dividends as a basis for Stock Value

- Value of stock $= \hat{P}_0 =$ PV of expected future dividends
  - $= \frac{D_1}{(1+r_s)^1} + \frac{D_2}{(1+r_s)^2} + ... + \frac{D_\infty}{(1+r_s)^\infty}$
  - $= \sum_{t=1}^{\infty} \frac{D_t}{(1+r_s)^t}$
- Zero Growth Stock
  - $\hat{P}_0 = \frac{D}{r_s}$

Corperate Valuation Model
Free Cash Flow:

- FCF = [EBIT(1-T)+ Dep. and Amortizaiton] -[Cap. Expenditures + Net Operating Working Capital]
- Market Value of Companys Operations
  - $= V_{company's operations} =$ PV of expected future cash flows
  - $= \frac{FCF_1}{(1+WACC)^1} + \frac{FCF_2}{(1+WACC)^2} + ... + \frac{FCF_\infty}{(1+WACC)^\infty}$
- Horizon Value
  - $= V_{companies operations at t=N} = \frac{FCF_{N+1}}{(WACC - g_{FCF})}$
- Market Value of Company
  - Market Value of company operations + Market Value of company's non-operating assets

- $= \frac{FCF_1}{(1+WACC)^1} + \frac{FCF_2}{(1+WACC)^2} + ... + \frac{FCF_\infty}{(1+WACC)^\infty}$ + Market Value of company's non-operating assets

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