Credit Risk Analysis I  
FIN 242f (1)  
Fall 2016  
Mondays and Wednesdays, 11:00 am – 12:20 pm  
Lemberg 55  

Edward Bayone  
Earle W. Kazis Professor of the Practice of Finance and International Real Estate  
Lemberg 259  
(781) 736-4874  
ebayone@brandeis.edu  

OVERVIEW  
In this course, we examine credit risk (i.e., the possibility that an obligor will fail to perform as agreed) from the perspective of the commercial banker. Based on a sound understanding of the firm and its business plan, the banker constructs the appropriate structure for the senior loan. Topics include asset-based, cash flow, and syndicated lending. All cases take place in the U.S.  

NOTE: The workload is high. If you are taking more than 16 credits, I recommend you drop this course.  

LEARNING GOALS & OUTCOMES  
✓ You will learn how commercial bankers in the US  
  ✓ think about credit risk  
  ✓ value qualitative as well as quantitative analysis  
  ✓ structure and syndicate loans  
  ✓ identify problems early and assess viability  

✓ You will also learn how “the story” shapes the banker’s perception of risk/return  

✓ If you fully apply yourself, by the end of the course you will be able to:  
  ✓ orally present a lending opportunity and key issues in 30 seconds!  
  ✓ write a 2-page memo highlighting a lending opportunity and key issues  
  ✓ write a full-blown credit analysis  

COURSE REQUIREMENTS  
Prerequisite: FIN 212a, ideally with a grade of B+ or better.  

Required Reading  
I have created a course area on the Harvard Business Online website where you can order the required materials for this course. Click on the link to order: http://cb.hbsp.harvard.edu/cbmp/access/51135358 If you have not registered with Harvard Business Online, you will be required to do so.  

Recommended Reading  
I have posted on LATTE 3 readings that you may wish to read (or skim) to gain a deeper insight into how US rating agencies, regulators and bankers think about credit risk. From Standard & Poors, you will find the 2012 edition of “A Guide to the U.S. Loan Market”; from the Office of the Comptroller of the Currency (the principal regulator of US banks), you will find the handbook, “Rating Credit Risk”; and from a former JP Morgan Chase commercial banker and credit officer, you will find, “A Primer on Deals for Middle Market Bankers.”
**Class Participation**
Lively class participation is expected of everyone in this course, and **class attendance is required**. In 8 of the classes, there will be a case assigned and you are expected to be prepared to discuss the case in detail, including a thorough analysis of the financial statements. To facilitate participation, place a name card on your desk.

**Written Assignments**
Team assignments must be done in groups of 3 students. Grades on each assignment are assigned to all members of the team (**although I reserve the right to alter individual grades** when it is clear to me that an individual did not contribute to the assignment in a consistent and meaningful way). Students may form different teams at any point in the course, so long as the affected students are given at least 4 days to find a new team.

**Grading** (55% individual, 45% team)

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<tr>
<th>Class Participation*</th>
<th>Hampton Machine Tool</th>
<th>Clarkson Lumber</th>
<th>Advanced Medical Technology</th>
<th>Blaine Kitchenware</th>
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*Class (attendance and) participation rules*
- You are permitted one absence for any reason for **classes 3-13**.
- **Each** additional absence, or an absence in either class 1 or 2, results in a reduction in this grading element (B+ to B, and so on).
- If you come to every class (or miss one of classes 3-13) but do **not** participate, your participation grade will be **C-**.
- Generally, I look for volunteers to speak, but sometimes I “cold call.” (If I “cold call” when there is a team assignment, I expect you to be able to answer for any part of the assignment, **not** just the section you may have worked on.)
- Class participation is not expected, **nor will it be graded**, in the 5 classes where I give a lecture
- Keep an accurate record of your participation, as I will ask for a self-evaluation at the end of the course in order to justify a participation grade of B+ or better. Quality is far more important than quantity, though always try to contribute something useful in each of the 8 case classes – **especially in those without written assignments!**

**Office Hours:** Students can meet with me individually during my office hours or by appointment.

**Academic Honesty**
You are expected to be honest in all of your academic work. Please consult **Rights and Responsibilities** for all policies and procedures related to academic integrity. You may be required to submit work to TurnItIn.com software to verify originality. Allegations of alleged academic dishonesty will be forwarded to the Director of Academic Integrity. Sanctions for academic dishonesty can include failing grades and/or suspension from the university. Citation and research assistance can be found at **LTS - Library guides**. **Under no circumstance may you search the internet, or turn to any other outside source, for any information regarding these cases without my permission. Failure to comply with this directive is cheating.**

**Special Accommodation**
If you are a student with a documented disability on record at Brandeis and wish to have a reasonable accommodation made for you in this class, please see me immediately. Please keep in mind that reasonable accommodations are not provided retroactively.
COURSE OUTLINE

CLASSES ONE and TWO
Monday, 8/29 and Wednesday, 8/31

“Salesperson or analyst?” Successful commercial bankers are both first-rate salespeople and excellent credit analysts. They must convince their prospect that they understand the company, can structure financings that meet its needs, and can “deliver” their bank. The marketing effort must be two-pronged: to the client and to bank management. Make a misstep along the way, and the deal is lost to another bank. What does the credit analysis involve? How is a loan structured?

Course introduction: syllabus review. This should take about 20 minutes of the first class.
Lecture: loan purpose and structure, financial ratio analysis, template for short- and long-form assignments

CLASS THREE
Wednesday, 9/7

“Purpose of the loan”. Sometimes it’s clear, often it’s not. Let’s look at a successful owner-manager of an established company who realizes that he cannot repay his loan on time and needs more money. To solve this case, think cash (vs. accrual accounting).

READING: Hampton Machine Tool Co. (280-103) + spreadsheet supplement
+ the cash flow template on LATTE
Note on Bank Loans (291-026)

Please consult LATTE for the specifics of this assignment. Please submit at the beginning of class a short-form analysis. Be sure to propose a loan structure that meets the needs of the firm. Please use (and include as an attachment) the template on LATTE to present the near-term cash flow. This is an individual assignment; as such, you may not discuss your cash flow or analysis with anyone. I will “cold call” often today on students to discuss various aspects of the case.

CLASS FOUR
Thursday, 9/8
Lecture on asset-based lending

CLASS FIVE
Wednesday, 9/12

“Financing Growth.” As companies grow, their working capital requirements can outpace their ability to generate cash from internal sources.

READING: Clarkson Lumber Company (297-028) + spreadsheet supplement
M. Porter, “The Five Competitive Forces That Shape Strategy,” HBR #R0801E

Please consult LATTE for the specifics of this assignment. Please submit at the beginning of class a long-form analysis in which you propose a loan structure that meets the needs of the firm. This is a team assignment. Be sure to incorporate Porter’s Five Forces analysis into your Business + Strategy section, and in every assignment from now on. Do not use the 90-day note structure mentioned in the case; instead propose a one (or more) year working capital line of credit.
CLASS SIX
Wednesday, 9/14
Lectures on problem loan identification and cash flow lending

CLASS SEVEN
Monday, 9/19
“Dreaming the dream.” The US economy is powered by the creativity and drive of entrepreneurs. Those same visionaries can be a challenge for the banker who prefers to operate in a more predictable environment.

READING: Advanced Medical Technology Corporation (287-028) + spreadsheet supplement

Please consult LATTE for the specifics of this team assignment.

CLASS EIGHT
Wednesday, 9/21
“It’s the Economy, Stupid.” (So went a phrase from a past US presidential campaign.) The recession has hit our borrower. Timing may not be everything but it does matter.

READING: Classic Fixtures & Hardware Company (915-523) + adjusted spreadsheet supplement

There is no written assignment. Consult LATTE for study questions and the adjusted spreadsheet. (I have adjusted the financial profile to make it more applicable to the course.) I will “cold call” today to discuss your analysis.

CLASS NINE
Monday, 9/26
“Time to sell?” There are several times in a company’s life cycle when the owners should consider selling; in this case, the owner has an offer on the table which he really doesn’t want to accept. Does he have an alternative, especially on such short notice?

READING: Owens Precision Machining (813-036)

There is no written assignment. Consult LATTE for study questions. (I have “updated” the story to make it very applicable to the course.) I will “cold call” today to discuss your analysis.

Time permitting, I will give a lecture on leveraged finance.

CLASS TEN
Wednesday, 9/28
“When in doubt, acquire!” Many firms explore M+A possibilities, especially when organic growth is difficult to achieve. Sometimes, a firm will even consider “bulking up” by acquiring an even larger company, which often would be financed through an injection of fresh equity (often from an outside firm to help validate the transaction and, indeed, value the equity) and a large amount of high-yielding debt (both senior and junior).

READINGS: Landmark Facility Solutions (915-528)
How to Negotiate a Term Loan (82201) - recommended (not required)

There is no written assignment. Consult LATTE for study questions. (I have adjusted the story to make it more applicable to the course.) I will “cold call” often today to discuss your analysis.
“Managing private wealth.” Sometimes long-term investors will want to achieve liquidity, perhaps to diversify their holdings. In this case, the bank considers extending a nine-figure loan to help finance a very large dividend (which is different from what the case considers). This type of transaction can be called a “leveraged recap."

READING: Blaine Kitchenware, Inc.: Capital Structure (#40-40) + spreadsheet supplement

Please consult LATTE for the specifics of this team assignment. Please submit at the beginning of class a long-form analysis in which you propose a loan structure that meets the needs of the firm.

CLASS TWELVE
Monday, 10/10
Lecture on syndicated lending and leveraged finance.

READINGS:  Note on LBO Capital Structure (214-039)
The High-Yield Debt Market (UV6756) – recommended (not required)

CLASS THIRTEEN
Wednesday, 10/19
“Leveraged Buy Outs can unlock value!” Enter a local hands-on PE (private equity) firm to buy out the position of a more passive PE firm through a combination of senior debt, high yield notes, and equity. How is the LBO justified? How is it structured, in particular, what will the senior debt look like?

READING: Berkshire Partners: Bidding for Carter’s (205-058) + courseware + spreadsheet supplement

There is no written assignment. Consult LATTE for study questions. I will “cold call” today to discuss your analysis

syllabus date: 7/25/16