

Preface

This book aims to cover the full scope of corporate finance as it is practised today worldwide.

A way of thinking about finance

We are very pleased with the success of the first edition of the book. It has encouraged us to retain the approach in order to explain corporate finance to students and professionals. There are four key features that distinguish this book from the many other corporate finance text books available on the market today:

- Our strong belief that financial analysis is part of corporate finance. Pierre Vernimmen, who was mentor and partner to some of us in the practice of corporate finance, understood very early on that a good financial manager must first be able to analyse a company's economic, financial and strategic situation, and then value it, while at the same time mastering the conceptual underpinnings of all financial decisions.
- *Corporate Finance* is neither a theoretical textbook nor a practical workbook. It is a book in which theory and practice are constantly set off against each other, in the same way as in our daily practice as investment bankers at BNP Paribas, DGPA and Mediobanca, as board members of several listed and unlisted companies, and as teachers at the Bocconi and HEC Paris business schools.
- Emphasis is placed on concepts, intended to give you an understanding of situations, rather than on techniques, which tend to shift and change over time. We confess to believing that the former will still be valid in 20 years' time, whereas the latter will for the most part be long forgotten!
- Financial concepts are international, but they are much easier to grasp when they are set in a familiar context. We have tried to give examples and statistics from all around the world to illustrate the concepts.

The four sections

This book starts with an introductory chapter reiterating the idea that corporate financiers are the bridge between the economy and the realm of finance. Increasingly, they must play the role of marketing managers and negotiators. Their products are financial securities that represent rights to the firm's cash flows. Their customers are bankers and investors. A good financial manager listens to customers and sells them good products at high

prices. A good financial manager always thinks in terms of value rather than costs or earnings.

Section I goes over the basics of financial analysis, i.e. understanding the company based on a detailed analysis of its financial statements. We are amazed at the extent to which large numbers of investors neglected this approach during the latest stockmarket euphoria. When share prices everywhere are rising, why stick to a rigorous approach? For one thing, to avoid being caught in the crash that inevitably follows.

We are convinced that a return to reason will also return financial analysis to its rightful place as a cornerstone of economic decision-making. To perform financial analysis, you must first understand the firm's basic financial mechanics (Chapters 2–5). Next you must master the basic techniques of accounting, including accounting principles, consolidation techniques and certain complexities (Chapters 6–7), based on international (IFRS) standards now mandatory in over 80 countries, including EU (for listed companies), Australia, South Africa and accepted by SEC for US listing. In order to make things easier for the newcomer to finance, we have structured the presentation of financial analysis itself around its guiding principle: in the long run, a company can survive only if it is solvent and creates value for its shareholders. To do so, it must generate wealth (Chapters 9 and 10), invest (Chapter 11), finance its investments (Chapter 12) and generate a sufficient return (Chapter 13). The illustrative financial analysis of Indesit will guide you throughout this section of the book.

Section II reviews the basic theoretical knowledge you will need to make an assessment of the value of the firm. Here again, the emphasis is on reasoning, which in many cases will become automatic (Chapters 15–24): efficient capital markets, the time value of money, the price of risk, volatility, arbitrage, return, portfolio theory, present value and future value, market risk, beta, etc. Then we review the major types of financial securities: equity, debt and options, for the purposes of valuation, along with the techniques for issuing and placing them (Chapters 25–30).

In Section III, “Corporate financial policies”, we analyse each financial decision in terms of:

- value in the context of the theory of efficient capital markets;
- balance of power between owners and managers, shareholders and debtholders (agency theory);
- communication (signal theory).

Such decisions include choosing a capital structure, investment decisions, cost of capital, dividend policy, share repurchases, capital increases, hybrid security issues, etc.

During this section, we call your attention to today's obsession with earnings per share, return on equity and other measures whose underlying basis we have a tendency to forget and which may, in some cases, be only distantly related to value creation. We have devoted considerable space to the use of options (as a technique or a type of reasoning) in each financial decision (Chapters 31–39).

When you start reading **Section IV**, “Financial management”, you will be ready to examine and take the remaining decisions: how to organise a company's equity capital, buying and selling companies, mergers, demergers, LBOs, bankruptcy and restructuring (Chapters 40–45). Lastly, this section presents cash flow management, and the management of the firm's financial risks (Chapters 46–47).

Suggestions for the reader

To make sure that you get the most out of your book, each chapter ends with a summary, a series of problems and questions (a total of 798, with the solutions provided). We've used the last page to provide a crib sheet (the nearly 1000 pages of this book summarised on one page!). For those interested in exploring the topics in greater depth, there is an end-of-chapter bibliography and suggestions for further reading, covering fundamental research papers, articles in the press and published books. A large number of graphs and tables (over 100!) have been included in the body of the text which can be used for comparative analyses. Finally, there is a fully comprehensive index.

An Internet site with huge and diversified content

www.vernimmen.com provides free access to tools (formulas, tables, statistics, lexicons, glossaries), resources that supplement the book (articles, prospectuses of financial transactions, financial figures for over 16,000 European, North American and emerging countries listed companies, thesis topics, thematic links, a list of must-have books for your bookshelf, an Excel file providing detailed solutions to all of the problems set in the book), plus problems, case studies, and quizzes for testing and improving your knowledge. There is a letterbox for your questions to the authors (we reply within 72 hours, unless of course you manage to stump us!). There are questions and answers and much more. The site has its own internal search engine, and new services are added regularly. The Internet site is already visited by over 1000 single visitors a day.

A teacher's area gives teachers free access to case studies, slides and an Instructor's Manual, which gives advice and ideas on how to teach all of the topics discussed in the *Vernimmen*.

A free monthly newsletter on corporate finance

Since (unfortunately) we can't bring out a new edition of the *Vernimmen* every month, we have set up the *Vernimmen.com Newsletter*, which is sent out free of charge to subscribers by Internet. It contains:

- A conceptual look at a topical corporate finance problem (*e.g. behavioural finance, finance in China, carbon trading.*)
- Statistics or tables that you are likely to find useful in the day-to-day practice of corporate finance (*e.g. share ownership structure in Europe, debt ratios in LBOs.*)
- A critical review of a financial research paper with a concrete dimension (*e.g. business collateral in SME lendings, the impact of pension plans on betas.*)
- A question left on the [vernimmen.com](http://www.vernimmen.com) site by a visitor plus a response (*e.g. what is a debt push down? What is a subprime loan? What are economic and regulatory capital?*).

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We hope that you will gain as much enjoyment from your Vernimmen – whether you are a new student of corporate finance or are using it to revise and hone your financial skills – as we have had in editing this edition and in expanding the services and products that go with the book.

We wish you well in your studies!

Milan and Paris, January 2009

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