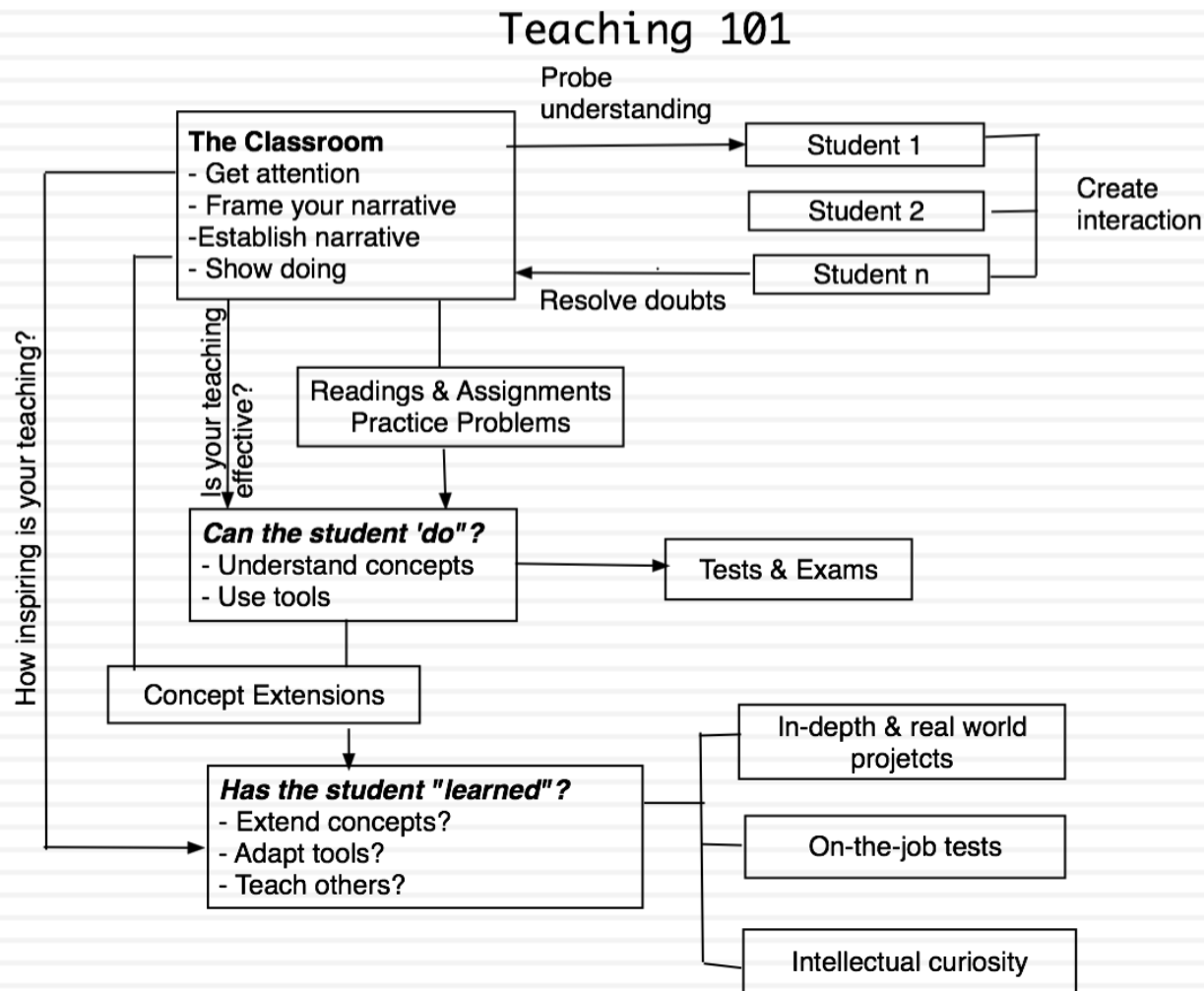


# TEACHING: ART, SCIENCE OR MAGIC?

Aswath Damodaran

<http://www.damodaran.com>

# Teaching: The Big Picture (and Questions)



*Impact factor: Did your class change your students' perspective/thinking/life?*



# The Perspiration Side of Teaching

Grading, Office Hours and Administration

# The importance of testing...

- Why do you give exams and quizzes?
  - a. Because I am required to...
  - b. Because it forces students to keep up with the material..
  - c. It is the basis for their grades..
  - d. All of the above
  - e. None of the above (Give me your reason then..)
- Which of the following best describes your exam writing/grading philosophy?
  - a. I give easy exams but grade tough
  - b. I give tough exams but grade easy
  - c. I give easy exams and grade easy
  - d. None of the above
- What are the characteristics a good grading system? Of a bad one?

# Exams and Grading

- Tie exams to your course objective: Structure exams around what you want students to learn and not from ease of grading or other objectives.
  - ▣ Corollary: Unless you plan to religiously follow a textbook, avoid test banks.
- Make it difficult to cheat: People cheat... and even a few cheaters can create the perception that the grading is not fair.
  - ▣ Assume that every past exam and its solutions are in the public domain
  - ▣ Create multiple versions of the same exam.
  - ▣ Have rules and enforce them.
- Speedy noisy feedback is better than perfect delayed feedback: Quick feedback is even more important for a large class than for a small one. Students have a much tougher time gauging how well or badly they are doing.
  - ▣ Give quizzes early and often in a class.
  - ▣ Grade and return exams as quickly as you can
- Be fair: Listen to grading grievances and admit your mistakes.

# Office hours and other delights...

- Do you enjoy having office hours?
  - a. Yes
  - b. No
  - c. Sometimes
  
- If you dislike office hours, why do you dislike them?
  - a. Being asked the same questions, over and over again.
  - b. Too many administrative questions.
  - c. Takes away time from more important things that I have to do (research, preparing for class)
  - d. They are boring.

# Interaction outside the class

- Minimize administrative issues: Be as clear and decisive as you can be about the administration of the class and how you will be grading students.
- Learn from doubts/questions: Reduce the proportion of your office hours you are spending answering the same question over and over.
  - ▣ If you are asked the same question more than three times by different students, either open a class by posing the question for the whole class and answering it (or)
  - ▣ Developing a help manual for the class, where you start listing the questions with your answers and make the manual available to all students (or)
  - ▣ Use technology. Put your help manual online. It makes searching easier
- Have an open-door policy. Being available does not mean that you will be inundated by students.

# Use technology to engage!

- Reinforcing lessons from class
  - ▣ [Short summary of class](#) right after class ends
  - ▣ [Newsletter](#) at the end of each week
  - ▣ Articles relating to the topic at hand (from business press...)
  - ▣ [Weekly challenges](#) extending the concepts (optional)
  - ▣ [Valuation \(CF analysis\) of the week](#) (optional)
- Reminders of cases and exams coming due.
- Keep track of your outliers...
  - ▣ The Good outliers, who are interesting in delving deeper into the subject than you will be able to cover in class.
  - ▣ The Neutral outliers, who hope to fade into the background.
  - ▣ The Bad outliers, who have given up on the class
- Email Rules
- Set aside time to answer email. Do not view it as an imposition.
- If you open email, answer it.





# The Inspiration side of teaching

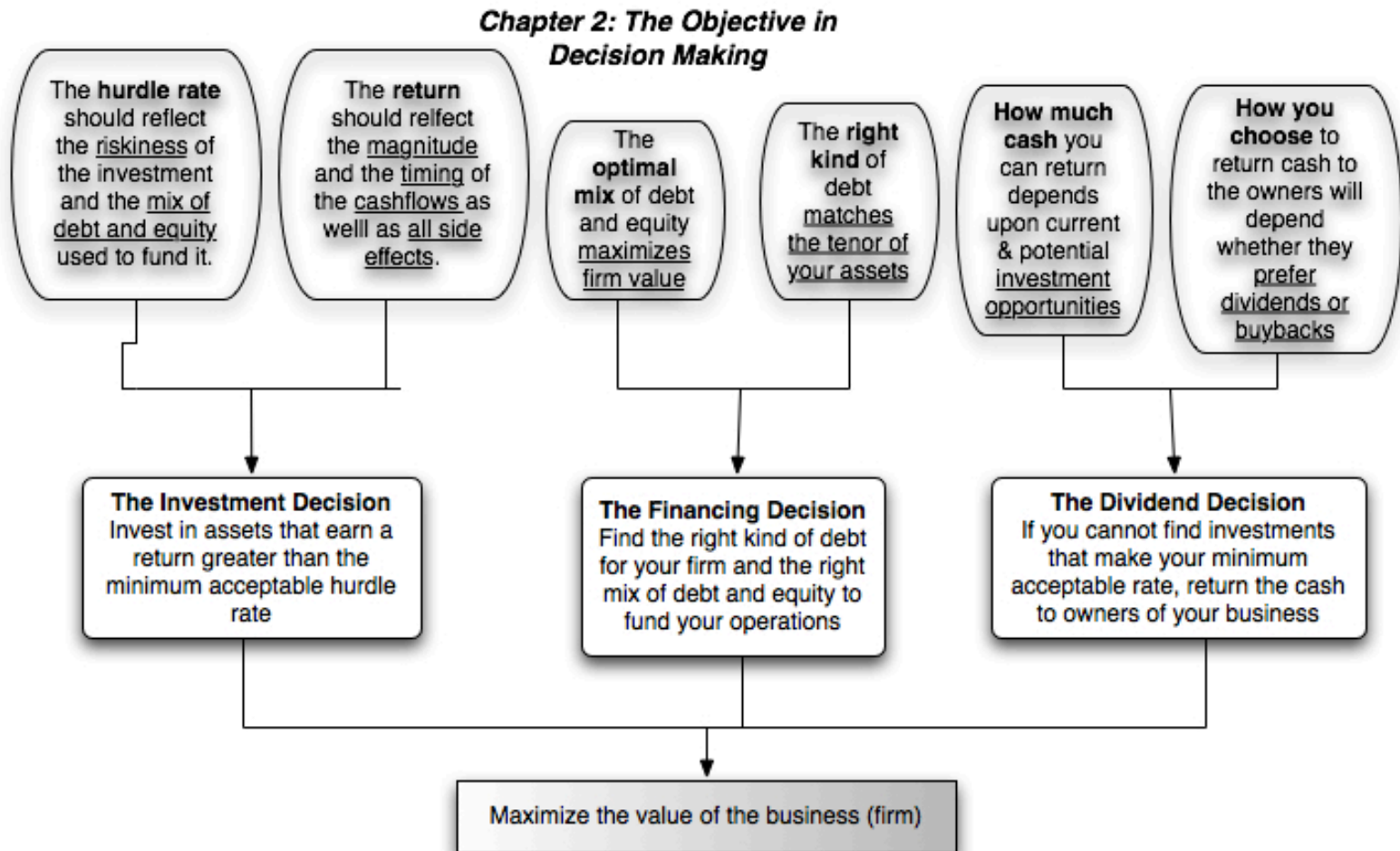
In the Classroom

# The Classroom

- ① Put it in context - provide the big picture and have a narrative.
- ② Be clear about where you are going before you take off.
- ③ Explain why your subject matter is relevant.
- ④ Frame topics to appeal to the widest audience
- ⑤ Make it real
  - ① Use real companies in real time
  - ② Connect to everyday life.
- ⑥ Keep people involved
  - ① Active versus Passive participation
  - ② Look for Aha! Moments
- ⑦ Manage your time, don't let the system beat you and trust your students.

# 1. Show them the big picture..

## Corporate Finance: First Principles



# Task 1: The Big Picture for the class you teach...

## Establishing a narrative

- Think about the big picture/ first principles that govern the class that you are teaching now. While doing this,
  - ▣ Avoid the jargon that is endemic to every discipline
  - ▣ Think in terms of the principles that govern how you think through problems in your discipline rather than on tactics or strategy.
  - ▣ Put first principles in common sense terms
  - ▣ Keep it compact (should fit on a page)
- Test it out by explaining what you are trying to do in your class to someone who does not know anything about your discipline and, better still, does not care.

## 2. Have a central question/theme for each class

### Session 16: The Financing Mix Question

- Background: This is session 16 of a 26-session corporate finance class. It follows sessions where we have analyzed the investment principle. This session is built around one question.
- In deciding to raise financing for a business, is there an optimal mix of debt and equity?
  - ▣ If yes, what is the trade off that lets us determine this optimal mix?
  - ▣ If not, why not?

## Task 2: The question of the day is....

- Take your conventional syllabus, which usually lists the topics for each session.
- For each session in your class, outline the key question or questions that you hope to answer. In doing so, keep in mind that
  - ▣ Most good lectures revolve around one question or perhaps two...
  - ▣ Framing the question correctly will make it easier for your students to follow the class.
  - ▣ Your lecture should revolve around answering the question.

### 3. Motivate the discussion

#### Why your debt ratio matters...

- Every business, small or large, private or public, has to choose a mix of debt and equity to fund its operations.
- It is possible that there exists a mix of debt and equity that is best for each business, and that the mix could be different for different businesses.
- If such a mix exists, we should try to find it even though we may be constrained by internal and external factors from moving to that mix.

## Task 3: Make it relevant

- For each lecture in your class, explain why answering the question you will be addressing in that session matters. In coming up with the motivation, remember that the following don't work:
  - ▣ You need to know it because it will be on the exam
  - ▣ Everyone in my discipline (finance, marketing ..;) believes that it is important to know this...
- If you cannot find a good reason why students should know the answer to a question, perhaps you should not ask it in the first place...



## 4. Generalize the discussion...

### The Choices in Financing

- There are only two ways in which a business can make money.
  - ▣ The first is debt. The essence of debt is that you promise to make fixed payments in the future (interest payments and repaying principal). If you fail to make those payments, you lose control of your business.
  - ▣ The other is equity. With equity, you do get whatever cash flows are left over after you have made debt payments.
- The equity can take different forms:
  - ▣ For very small businesses: it can be owners investing their savings
  - ▣ For slightly larger businesses: it can be venture capital
  - ▣ For publicly traded firms: it is common stock
- The debt can also take different forms
  - ▣ For private businesses: it is usually bank loans
  - ▣ For publicly traded firms: it can take the form of bonds

# Task 4: Generalize your discussion

- Take a typical lecture and go through it looking for ways to say things that appeal to those from
  - ▣ From other countries
  - ▣ From other backgrounds (not finance, in my case)
  - ▣ With other interests

## 5. Make it real

### Measuring a firm's financing mix

- The simplest measure of how much debt and equity a firm is using currently is to look at the proportion of debt in the total financing. This ratio is called the debt to capital ratio:
  - $\text{Debt to Capital Ratio} = \text{Debt} / (\text{Debt} + \text{Equity})$
- Debt includes all interest bearing liabilities, short term as well as long term.
- Equity can be defined either in accounting terms (as book value of equity) or in market value terms (based upon the current price)

# Bring in real companies

## Disney (US, entertainment)

Debt = \$13,028  
Equity = \$121,878  
D/E ratio = 13.1%

## Tata Motors (India, automobile)

Debt = Rs 477,268 m  
Equity = Rs 1,152,664 m  
D/E ratio = 41.4%

## Baidu (China, technology)

Debt = 15,403 m Yuan  
Equity = 334,345 m Yuan  
D/E ratio = 5.5%

Corporate Finance  
First principles

## Deutsche Bank (Germany, bank)

Debt = 143,800 m Euros  
Equity = 35,150 m Euros  
D/E ratio = 409.1%

## Vale (Brazil, mining)

Debt = \$R 99,132  
Equity = Rs 180,257 m  
D/E ratio = 55.0%

## Bookscape (US, bookstore)

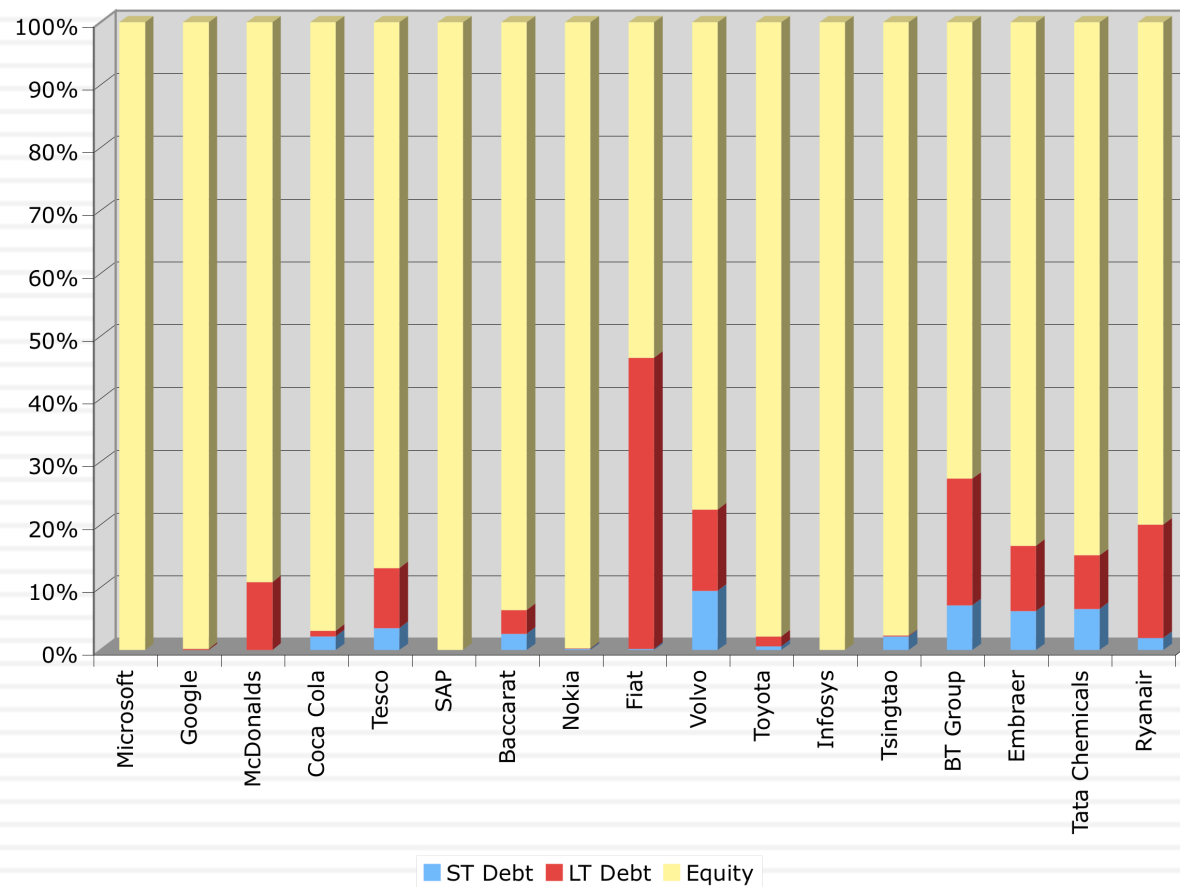
Debt = \$12,156  
Equity = \$31,500  
D/E ratio = 38.5%

## ▼ Application Test: What is your firm's debt ratio?

- Looking at the balance sheet of your firm, estimate the following:
  - ▣ Total interest bearing debt at your firm
  - ▣ The book value of equity
  - ▣ Book value debt to capital ratio
- Using the market value of equity in the firm, estimate the market value debt to capital ratio

# The Real World Intrudes...

Differing Financing Mixes



# Task 5: Make it real..

- When introducing a measure, a model or a proposition, follow it up by having students look at a real company. If possible,
  - ▣ Let them pick their own companies
  - ▣ Make it real time
  - ▣ Work with the companies in class
- If not, use a case... If you do, watch out for the following:
  - ▣ Don't make the case discussion too contrived or stage managed
  - ▣ Leave open the possibility that the “case solution” (offered by the case writer) may be wrong or incomplete
  - ▣ Watch out for hindsight bias

## 6. Set up roadmaps for discussions

### The Trade Off: Debt versus Equity

- Benefits of Debt
  - ▣ Tax Benefits
  - ▣ Adds discipline to management
- Costs of Debt
  - ▣ Bankruptcy Costs
  - ▣ Agency Costs
  - ▣ Loss of Future Flexibility



## 6a. And use anecdotes to bring home your point

### Debt adds discipline to management

- If you are managers of a firm with no debt, and you generate high income and cash flows each year, you tend to become complacent. The complacency can lead to inefficiency and investing in poor projects. There is little or no cost borne by the managers
- Forcing such a firm to borrow money can be an antidote to the complacency. The managers now have to ensure that the investments they make will earn at least enough return to cover the interest expenses. The cost of not doing so is bankruptcy and the loss of such a job.

## Task 6: Explain with every day occurrences...

- When explaining a concept, see if you can come up with something from everyday life that brings it home. If you can,
  - ▣ Make it personal
  - ▣ Make it funny
  - ▣ And keep it connected to what you are trying to explain
- Try it out on an audience. If it does not work, try modifying it. If it does, remember it and keep fine tuning it.



## 7. Allow for different types of participation Added Discipline...

- Assume that you buy into this argument that debt adds discipline to management. Which of the following types of companies will most benefit from debt adding this discipline?
  - a. Conservatively financed (very little debt), privately owned businesses
  - b. Conservatively financed, publicly traded companies, with stocks held by millions of investors, none of whom hold a large percent of the stock.
  - c. Conservatively financed, publicly traded companies, with an activist and primarily institutional holding.

## Task 7: Create active participation...

- Take a few open ended questions that you currently ask in class and see if you can convert them into a multiple choice questions, with each answer representing a feasible answer (albeit with a different assumption needed to get there).

# 8. Repeat, rinse, repeat

## Debt: Summarizing the Trade Off

### **Advantages of Borrowing**

#### *1. Tax Benefit:*

Higher tax rates --> Higher tax benefit

#### *2. Added Discipline:*

Greater the separation between managers and stockholders --> Greater the benefit

### **Disadvantages of Borrowing**

#### *1. Bankruptcy Cost:*

Higher business risk --> Higher Cost

#### *2. Agency Cost:*

Greater the separation between stockholders & lenders --> Higher Cost

#### *3. Loss of Future Financing Flexibility:*

Greater the uncertainty about future financing needs --> Higher Cost

## 8a. Let them figure it out

### A Hypothetical Scenario

- Assume you operate in an environment, where
  - ▣ (a) there are no taxes
  - ▣ (b) there is no separation between stockholders and managers.
  - ▣ (c) there is no default risk
  - ▣ (d) there is no separation between stockholders and bondholders
  - ▣ (e) firms know their future financing needs
  
- What are the costs and benefits of borrowing in this scenario? What are the implications for an optimal debt ratio?

## 8b. Look for Aha! moments

### The Miller-Modigliani Theorem

- In an environment, where there are no taxes, default risk or agency costs, capital structure is irrelevant.
- The value of a firm is independent of its debt ratio.

## 8c. Aha2: Build on confidence

### Application Test: Try it on your firm

- Considering, for your firm,
  - ▣ The potential tax benefits of borrowing
  - ▣ The benefits of using debt as a disciplinary mechanism
  - ▣ The potential for expected bankruptcy costs
  - ▣ The potential for agency costs
  - ▣ The need for financial flexibility
- Would you expect your firm to have a high debt ratio or a low debt ratio?
- Does the firm's current debt ratio meet your expectations?



# Task 8: Create aha moments!

- If you could do it, what part of your class would you want your students to have the aha moment on?  
How would you go about making it easier for them to get there?
  - ▣ A simple framework for thinking through problems
  - ▣ No extraneous issues and questions
  - ▣ No buzz words...
  - ▣ A non-threatening atmosphere
- The more important the proposition, the greater the payoff to letting them get there on their own...



# The Disruption of Teaching

The technology effect

# The World has changed.. Have you?

- Do you find yourself frustrated that your students don't learn the way you learned or communicate the way you did?
- Have you adapted the way you communicate to the way your students communicate?
  - Are there parts of your class that will lend themselves to any of the social media vehicles?
  - Do you incorporate Facebook or other social media into your class? If so, how do you do it? If not, why do you choose not to?

# 1. Technology: A tool

- The technology that we have available to teach has improved dramatically.
- Technology is great, but don't become its slave
  - Use technology to supplement and augment your teaching, but don't let it become the star of the show or a distraction. (Be careful how you use videos and other outside material in your classroom)
  - Assume that technology will always fail and have a backup. Always be ready to teach your class with no technology at all.
- Remember that your students will never be as dazzled by your use of technology as you are. They have grown up in a tech world, where YouTube videos and social media fireworks are part and parcel of every experience.


## 2. Use social media wisely

  Joe Mellet posted 3 months ago

An example of extreme bias when two parties are valuing a business. MS and Citi have been fighting over the value of their Smith Barney JV. MS is arguing the business is only worth \$9.5 Billion while Citi claims it is worth \$22.5 Billion. Huge disparity...  
[online.wsj.com/article/SB10000872396390444017504577645381587194956.html?mod=WSJ\\_hp\\_LEFTWhatsNewsCollection](https://online.wsj.com/article/SB10000872396390444017504577645381587194956.html?mod=WSJ_hp_LEFTWhatsNewsCollection)

 [Morgan Stanley Lands Victory Over Citigroup](#)  
Citigroup and Morgan Stanley agreed to value their Morgan Stanley...

1 LIKE 

 Leave a comment  

  Ankur Khandelia posted 3 months ago

The Facebook co-founder Dustin Moskowitz sold all of his remaining class A shares for \$108.4m, but he still holds all of his class B shares. Current share price is \$18.98. Interesting!

 [Dustin Moskowitz made another \\$108.4M from Facebook trades](#)

# 3. Harness the power of crowds



## Part IV: Closing presentation

This page will include the webcasts from the current class. The webcasts can be accessed in one of three ways:  
 Streaming video (The file will be streamed to your computer. This will work only if you have a good internet connection, but should be of the best quality)  
 Video podcast (The .m4v file will be downloaded to your computer and you can watch the video using Quicktime or video software or on your iPod)  
 Audio podcast (The .mp3 file will be downloaded as an audio file and can be played on any audio player). The AV system used to record the lectures has changed and I think it is much improved.  
 The prior semester's webcasts can be found [here](#).

Finally, you can read the emails that I send to the class by [this link](#), as well as the [newsletters](#) for the class.

Session Webcasts	Topics covered	Lecture notes
1 (9/5/12) <a href="#">Webcast, streamed (need a good internet connection)</a> <a href="#">Video podcast (downloadable)</a> <a href="#">Audio Podcast (downloadable)</a>	Introduction to Class	<a href="#">Syllabus for class</a> <a href="#">Project Description</a> <a href="#">Introduction to Valuation</a> (Page 1-4)
2 (9/10/12) <a href="#">Webcast, streamed (need a good internet connection)</a> <a href="#">Video podcast (downloadable)</a> <a href="#">Audio Podcast (downloadable)</a>	<a href="#">Valuation bias: A test and my solutions</a> Valuation: How much detail? Valuation approaches DCF: Valuation choices	<a href="#">Introduction to Valuation</a> (Page 4-End) Lecture note packet 1: Page 1-8
Valuation of the week (Facebook in August 2012)	<a href="#">My blog post on the Facebook IPO</a> <a href="#">My valuation of Facebook</a>	<a href="#">Google spreadsheet for your estimates</a>
3 (9/12/12) <a href="#">Webcast, streamed (need a good internet connection)</a> <a href="#">Video podcast (downloadable)</a> <a href="#">Audio Podcast (downloadable)</a>	<a href="#">Cash flow consistency: A test (Congoleum)</a> DCF: The consistency principles Dividend, FCFE and FCFE Models Inputs: The riskfree rate	Lecture note packet 1: 9-36  <a href="#">Default spreads: Ratings classes</a> <a href="#">CDS spreads: Mid-year 2012</a>
Weekly challenge # 1	Reconciling firm and equity valuation	<a href="#">Weekly challenge #1 Solution</a>
Valuation of the week: Valuing the iPhone 5 franchise	<a href="#">My valuation of the iPhone franchise</a>	<a href="#">Google spreadsheet for your estimates</a>

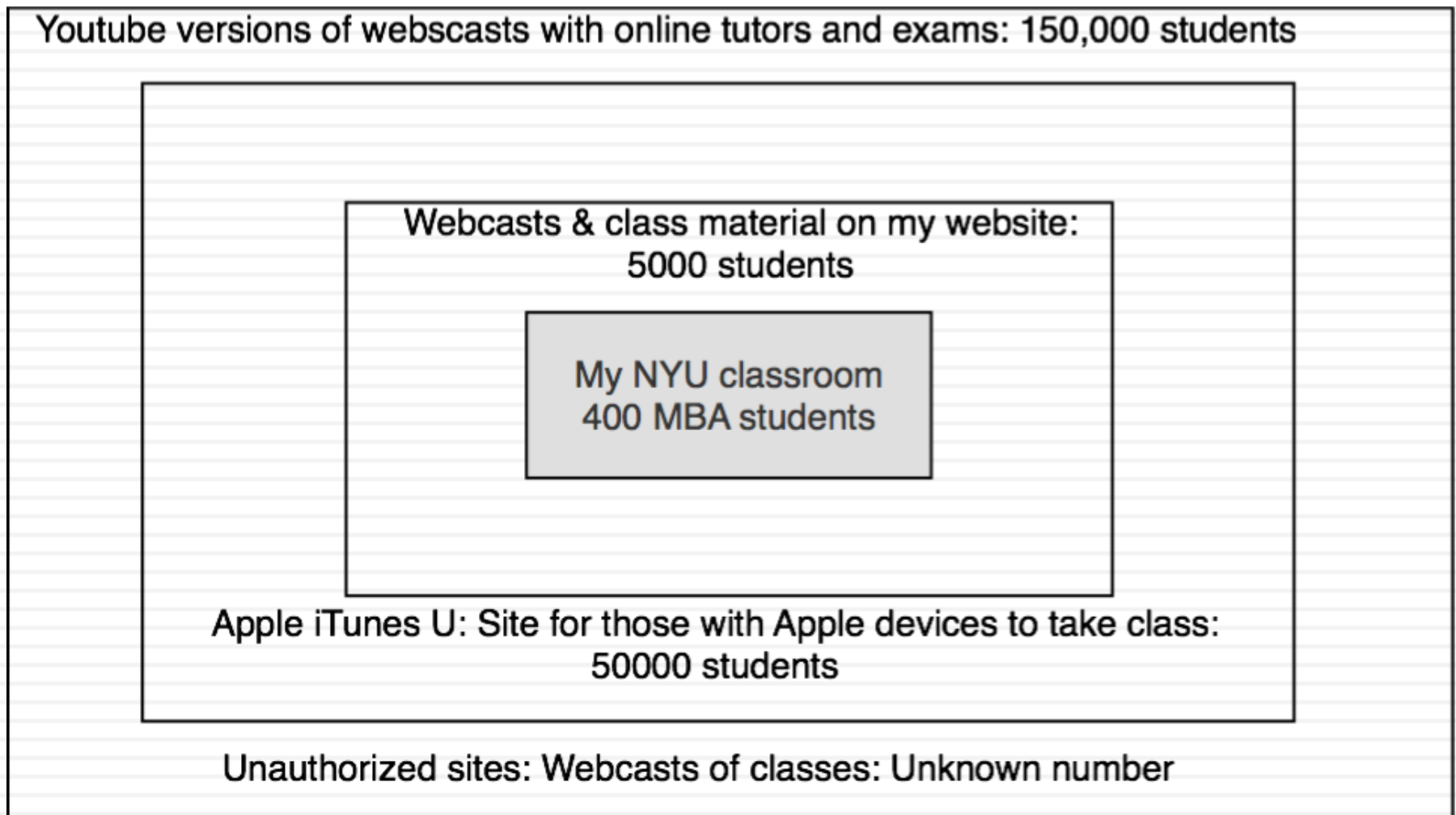
1 people online  
 they can help you right now

Get Live Help

Live Study Group

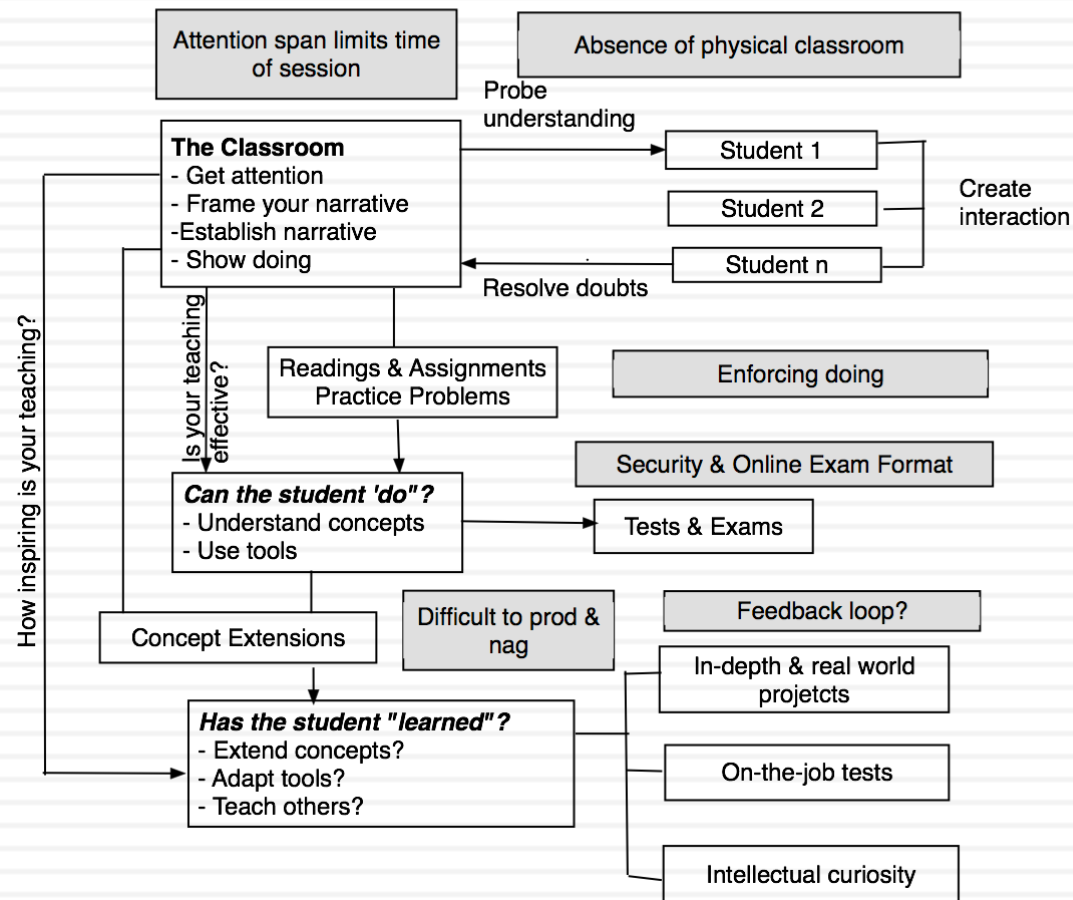
Your classmate is telling you how they plan to become financially successful. Which of the

# 4. Rise to the challenge of online teaching



# The barbarians are at the gate!

## The Online Teaching Challenge







# The Academic Trap

Publish & Perish!

# The system is rigged but you can beat it..

## Undermine the system...

### **If you teach at a research university**

- They tell you that teaching matters but make judgments about who to hire, who to tenure and who to reward based upon “quality” research.
- You should
  - a. Research what interests you and do not be driven by the “publish or perish” culture.
  - b. Stare into the abyss (of not getting tenure)
  - c. Preserve the option to abandon.

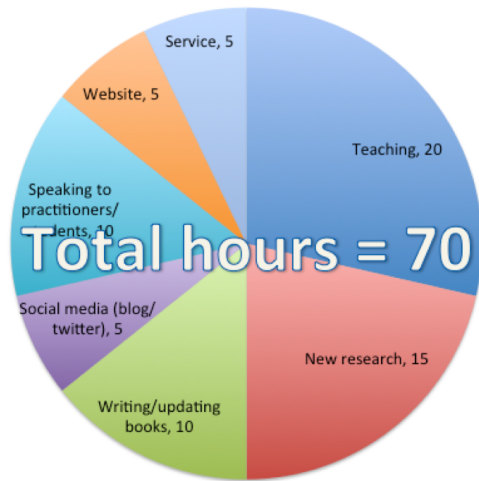
### **If you teach at a teaching college**

- They tell you that you should be a good teacher but don't give you the resources to back it up and give you a teaching load that causes burn out.
- You should view teaching well as your ultimate revenge. If you can pull this off, your power and affirmation will flow from below (the students) and not from above (the administration).

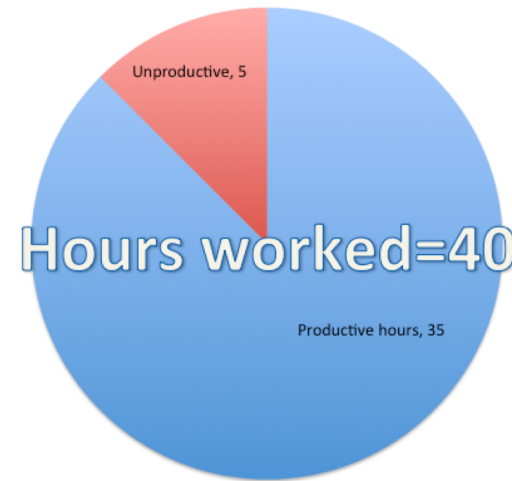
# Take a time audit and follow up...

- Take a typical workweek and keep track of the time you spend on activities, breaking down teaching into preparation, office hours, classroom hours, email hours etc. and the rest of the week into administrative and research time.
- Think about ways in which you can make one activity serve more than one purpose. For instance, when you are doing research, can you think of ways of incorporating into a classroom session. Alternatively, can you make your administrative time actually serve useful purposes?

# Don't compartmentalize.



Total hours = 70



Hours worked=40

# Look into the abyss... it may just be a ditch!

- If you are on the academic treadmill, doing research on topics that you don't much care about, trying to publish in journals where the game is fixed and trying to get papers published that few people will read, and doing all of this because you want to get tenure, I have two questions:
  - Assume that you succeed and get tenure, what do you see happening with the rest of your life?
  - Assume that you fail and don't get tenure, what do you see happening with the rest of your life?

# Assume the best about your students..

## Here is what I believe about mine!

- They want to learn: Learning is fun, a natural high and makes people feel good. So, learning opens the door to more learning...
- They want me to succeed (at teaching them): If I succeed at my job (teaching), it makes their job (learning and doing well on the class) easier.
- They are “good” people, but they are human: While there will always be exceptions, I have to start with the presumption that my students would prefer to do their assignments, not cheat and help their classmates.

# Closing Thoughts on Teaching...

- Remember the three Es of teaching
  - ▣ Enthusiasm: If you are not enthusiastic about what you teach, why would you expect your students to be?
  - ▣ Energy: There is a critical mass of energy that any class needs to sustain itself. It has to come from either your students or you (or preferably both). If one side is low energy, the other has to make up for it.
  - ▣ Empathy: Remember when you were a student.
- Its easy to teach when you are in the “zone”. The real test is whether you can teach when you are out of it.
- Be yourself.
- Have fun. It is infectious.