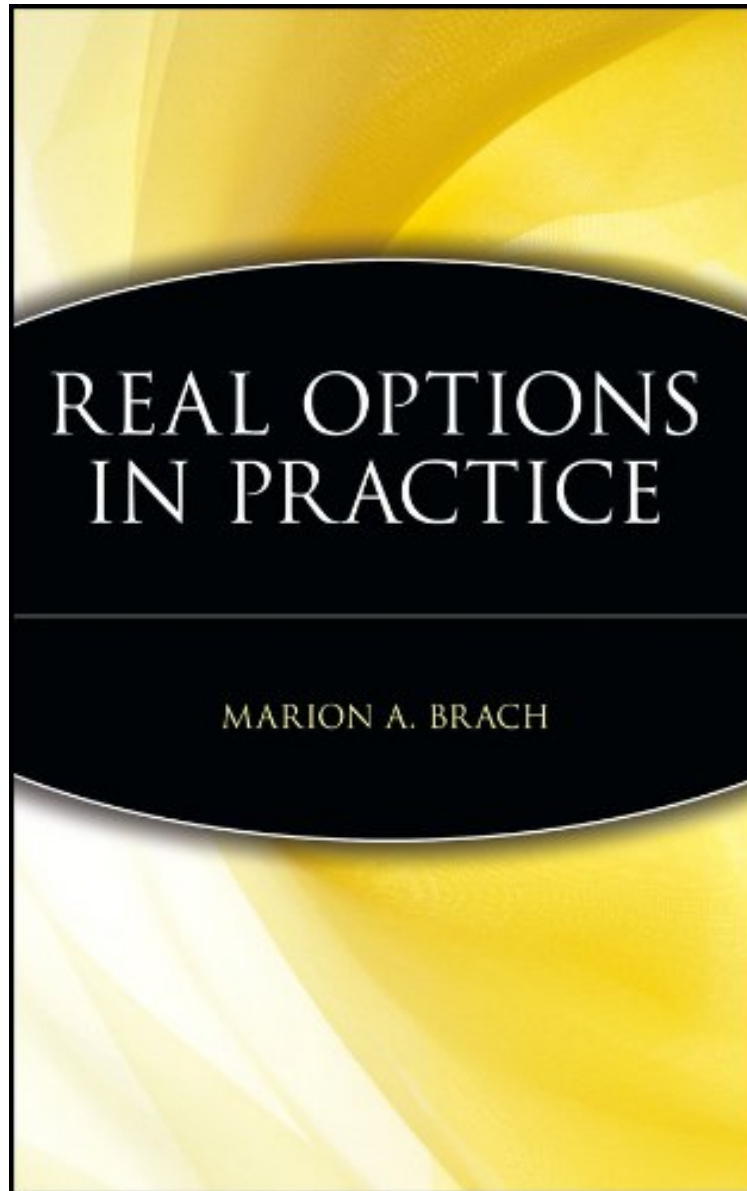


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Real Options in Practice (Wiley Finance)

Marion A. Brach

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Marion A. Brach : Real Options in Practice (Wiley Finance) before purchasing it in order to gage whether or not it would be worth my time, and all praised Real Options in Practice (Wiley Finance):

1 of 2 people found the following review helpful. A good text on real options for intermediate practitioners. By Abacus This book builds a solid foundation on corporate applications of real options. The author is an MD and has worked many years as a medical researcher. Thus, she has a first hand knowledge in health care and pharmaceutical research. She builds on this wealth of experience to develop many interesting examples of real options related to

pharmaceutical drug development. However, she is perfectly comfortable developing excellent examples across industries such as oil explorations, new product developments, and other traditional real option corporate applications. The strengths of the book include an excellent foundation in financial option theory, a good explanation of the Black Scholes option model and the binomial option pricing model. There is also an excellent section on the history of options which date back to the age of the Pharaohs and the Greeks. The author does also a good job at outlining the weakness of the Discounted Cash Flow (DCF) analysis method of valuing projects. DCF does not handle well uncertainty of projects outcome, and flexibility in management decision and investing schedule. These weaknesses are just where real options excel. One counterintuitive variable is that uncertainty, that corporate managers traditionally dislike, lowers the value of a project in DCF, but actually increases it in a real options framework. This is not so strange when you consider that volatility is the main driver of options values within the Black Scholes model. The overall weakness of this book is that many examples are not so well explained from a mathematical standpoint. You are often left wanting more explanations to truly become comfortable using these techniques. The experienced real option practitioner will find this book very interesting. The novice who wants to build a practical foundation better turn to "Real Options" written by Martha Amram and Nalin Kulatilaka which does a better job at explaining the underlying basic calculations behind each examples.

3 of 3 people found the following review helpful.
Disappointment
By Jakub Valkoun
I was really excited when I bought this book since I needed a guide on "real" approach in evaluating real options. This book is definitely different from any other book on the issue of real options on the market. It deals with some very interesting concepts such as that volatility is not always profitable in real options. There, Brach bases her work on Huchzermeier and Loch but unfortunately is rather unconvincing in her explanation. However I got really frustrated, when I tried solving some of her examples of valuating options. They are marred by numerous simple algebraic errors, making the whole example useless. (e.g. p. 99 fig. 3.21 - values of the stage options are incorrect) As one of the previous reviewers had noted, Brach doesn't seem very confident with her maths and many of her examples are incomplete and hard to follow. In short, if you want to read something "easy" and interesting about real options then this is your choice. However, don't expect this book to be a real guide in your everyday dealing with real options.

2 of 2 people found the following review helpful. Good overview but the editor was asleep
By Donald Harer
Brach covers the theory sufficiently; however, her attempts to apply the theory to practical examples is weak at best. Three problems became major distractions for me and ultimately led to my not completing the book. First, examples cited within the book are very difficult to follow. Fairly important components of example equations fall from the sky with little explanation as to how they were determined. Second, there are inconsistencies between stated assumptions and mathematical examples. This particular distraction is evident in the discount rates cited and used for calculations. Third, (I may be mistaken) but there may be variations in option valuing approaches that contradict Brach's methodology. By not addressing these variations ultimately leads the attentive reader to numerous unanswered questions. Overall, it is a nice book that addresses the overall mechanics in an understandable fashion...even considering the problems with the examples. However, for those wishing the end-all-be-all real option reference book...Keep Looking.

Explores real option theory applied in practice Real options are quickly becoming the valuation and decision-making method of choice for many companies, including oil and gas companies, utilities and natural resource companies, pharmaceutical and biotech companies, Internet companies, and many others. Real Options in Practice allows readers to view the world of real options from the vantage point of a corporate practitioner applying real option valuation techniques on a regular basis. Expert Marion Brach describes the challenges of implementing a real option framework in practice within a corporate setting. Touching on the real options most firms care about, Real Options in Practice identifies the classic types of real options-deferral, abandonment, switching, expansion, and compound-and explores the main concepts critical to understanding real option theory. Through Brach's own three-step real option valuation method readers will learn how the theory of real options is now being applied to drive better, more profitable corporate decision-making. Marion A. Brach, MD, MBA (Hagen, Germany), has undertaken financial valuation of business opportunities and acquisitions using scenario and real option valuation in the biotech industry. A recognized expert on real option theory and practice, Brach received her MBA from the Manchester Business School and frequently speaks at real option seminars.

Rarely, a book of immense breadth comes along so little understood by its publisher that it is launched as a technical manual for industry insiders when, in fact, it is a seminal work in many fields. Marion A. Brach, a physician with a background in medical research and a deep understanding of mathematics, migrated to finance. She took an interest in real options, which is the field of valuation of choices in the real as opposed to the financial world and in due course produced her book. Dr. Brach's interest is, at its core, whether X corporation should buy Y corporation or invest a known amount of money in a project. This sort of thing has usually been handled by discounted cash flow analysis. If Y can add a known amount of money to X's business, then the purchase price of Y must not exceed the discounted cash flow it brings in. What's wrong with discounted cash flow is that it ignores risk, as Dr. Brach points out. That's a

huge gap and one which real options can fix. The corrective value of real options pricing is obvious. The downside of real options is that it takes a good deal of math, usually partial differential equations, to do it. Financial calculators are already available at modest prices to handle the Black-Scholes model of options pricing, but real options that involve corporate planning require a deeper sense of what the math is about. As Dr. Brach points out, a model for a deterministic solution, such as how much to pay for a right to buy a what contract that will expire at a known price, zero, at a given time, is different from the situation of a process that has a stochastic or even randomized outcome. Dr. Brach moves her story and analysis from biblical accounts of grain trading and a developing and parallel options market and Joseph's choice of whether to save grain to guard against seven years of famine. Thales, the Greek philosopher, bought call options on olive presses well before a harvest and was able to raise press rents at the small cost of the options he bought. The story of the development of real options moves from Greek olives to Dutch tulips and then to theories of thermodynamics. Dr. Brach mentions the roots of real options analysis in Russian and French investigations of probability theory, the use of Brownian motion as a foundation for stochastic theories of where prices will be in successive periods, and assumptions about market clearing and interest rates. There are investigations of the value of learning and the reduction of noise, the applications of game theory to outcome analysis, and a consideration of where real options is going and where its usefulness may end. The strength of the book is its sweeping view of the field of the valuation of events, the clarity of Dr. Brach's writing, a fine 19 page bibliography, and her ability to tell her story without delving into mathematical physics - the source of much of the analytic power of real options analysis. For the investor, this value of this book about the analysis of non-financial options is what it says about the limitations of conventional investigations of future financial events. For thoughtful folks not concerned about figuring out the price of a financial options, Dr. Brach provides a glimpse of analysis as it will likely be in a decade or two. This reviewer cannot recommend this book too highly. For a reader with a little calculus and some statistics, it's not hard reading. For anyone, it is an adventure with a very bright mind-- Toronto Globe Mail

From the Inside Flap Real options are useful tools that can guide a firm's strategic planning and can create or enhance a firm's value. That's why real options are quickly becoming the valuation and decision-making method of choice for companies in competitive industries. The fact is that no matter what field you're in-financial, pharmaceutical, energy, or technology-if you're a corporate decision-maker, real options can help you make the right decisions at the most critical times. In *Real Options in Practice*, Marion Brach presents the world of real options from the vantage point of a corporate practitioner applying real option valuation techniques on a regular basis. Through in-depth insights, detailed formulas, charts, and case studies, you'll receive an executive education on real options that cannot be found anywhere else. To bring you up to speed on this topic, *Real Options in Practice* opens with a unique and comprehensive history of real options, from their earliest beginnings to the present. From here, you'll learn how to transform real option theory into a real-world framework that will produce tangible results. *Real Options in Practice* touches on only the most important issues. It discusses the relevance of Black-Scholes and Binomial Option Pricing models in relationship to real options, explains the basic managerial options you must know-deferral, abandonment, expansion, switching, and compounding-and explores the value of uncertainty within a real options environment. You'll also gain a firm understanding of new trends in real option theory, including the intersection of game theory with real options, and real options in preemption and technology positioning. Rounding out this comprehensive guide to real options are further discussions of real option analysis as a corporate strategy. You'll see how real option analysis can be implemented in contractual relationships; the shortcomings of the real option method that must be taken into consideration to ensure the best use of the paradigm; as well as the organizational challenges, in implementing real option concepts. By exploring the fascinating world of real options, where and why they are applied to corporate decision-making, and, most importantly, the challenges of implementing a real option framework in practice, *Real Options in Practice* offers you the most accurate and informative guide to using real options in a corporate setting.

From the Back Cover How much should a pharmaceutical company invest in RD for a new drug? At what point do the costs outweigh the benefits of a new technology? When should you abandon that oil-drilling project? "Real options is an exciting but very challenging subject for many strategy and corporate finance practitioners. *Real Options in Practice* is an excellent book to get a structured and accurate overview of real options, their use and computation. Marion Brach has succeeded in striking a difficult balance between theoretical firmness and practical actionability: her book is easy to read without sacrificing the richness of a subject that is more and more important for investment decision-making." -Remy Schosmann, Partner, Corporate Finance, and global head of strategic options management at Ernst Young "Marion Brach makes applied option theory accessible to the practitioner without neglecting technical rigor. Any manager seeking a solid foundation in option concepts-and how to profit by them-should start with this book." -John L. McCormack, Senior Vice President Stern Stewart Company