

S5 - STRATEGIC FINANCIAL MANAGEMENT
STRATEGIC LEVEL-2
INTRODUCTION

This course is designed to focus on the theoretical and practical aspects of financial management. The course contains tools and techniques of financial management, which can be applied in the specific area of business, to manage operating, financing and investing activities.

OBJECTIVE

To provide the students with an in-depth knowledge of strategic financial management enabling them to:

- Understand and apply strategic approach of financial management,
- Formulating financial strategy considering economic and financial constraints,
- Examine the financial goals and policy of the business for proper application, and
- Develop financial plan to manage various financial activities of business.

LEARNING OUTCOMES

On completion of this course, students will be able to:

- Understand the potential strategic financial objectives of an organization;
- Realize the impact of internal and external constraints on financial strategy, including the impact of regulation on business combinations;
- Evaluate investment projects (domestic and international), including their financial and strategic implications, taking account of potential variations in business and economic factors;

- Realize the constraints on financial strategy;
- Understand the working capital management and dividend policy;
- Comprehend the capital markets, rights issue, scrip dividends, bonus issues and share splits, share prices and investment returns and efficient market hypothesis;
- Understand the medium, long-term debt, convertible securities warrants and international debt finance;
- Perform the investment decisions, financing and cost of capital, dividend valuation model, CAPM, cost of debt;
- Make capital structure decision and explicate the effect of capital structure on ratios, theories of capital structure, project specific cost of capital and leverage;
- Perform treasury functions, risk and reward analysis and hedging financial risk;
- Perform investment appraisal technique including capital investment appraisal;
- Understand investment and projects, feasibility study and project control;
- Get acquainted with the reasons for valuations, asset valuation bases, earning valuation bases;
- Learn how to manage financial risks of proposals for mergers and acquisitions along with the various steps involved in mergers, acquisitions and corporate restructuring;
- Apply the procedures for foreign exchange control in business;

INDICATIVE GRID

PART	SYLLABUS CONTENT AREA	WEIGHTAGE
A	FORMULATION OF FINANCIAL STRATEGY	10%
	1. Objectives of organizations	
	2. Constraints on Financial Strategy	
	3. Forecasting and Analysis	
B	FINANCING DECISIONS	45%
	4. Financial Strategies	
	5. Equity finance	
	6. Debt finance	
	7. Leasing	
	8. The cost of capital	
	9. The capital structures	
	10. Operating and Financial Leverage	
C	INVESTMENT DECISIONS AND PROJECT CONTROL	45%
	11. Treasury Management	
	12. Investment appraisal techniques	
	13. International investment	
	14. Specific investment appraisal scenarios	
	15. Control of investment projects	
	16. Business valuations	
17. Amalgamations and restructuring		
TOTAL		100%

Note: The weightage shown against each section indicates, study time required for the topics in that section. This weightage does not necessarily specify the number of marks to be allocated to that section in the examination.

DETAILED CONTENTS
PART - A
FORMULATION OF FINANCIAL STRATEGY
1. Objectives of organizations

- Objectives of Companies
- Stakeholders and Objectives
- Objectives of public owned
- Objectives of non-commercial bodies

2. Constraints on Financial Strategy

- Constraint Factors
- Economic Constraints
- International Constraints

- Regulatory bodies

3. Forecasting and Analysis

- Performance Analysis
 - Calculation of ratios including DuPont approach and Z-Score.
- Cash Forecasts
 - Preparation of Cash Budget only
- Financial Statements Forecast
 - Budgeted Income statement
 - Budgeted Balance sheet
- Sensitivity Analysis and Changes in variables

- Concept of sensitivity Analysis in all of the above Forecasted statements and calculation of revised cash budget.

4. Financial Strategies

- Working Capital Management
 - Working capital needs (temporary and permanent need) and working capital financing strategies (aggressive, conservative and moderate strategy)
- Dividend Policy
 - Traditional theory of dividend Policy
 - MM theory of Dividend Policy
 - Dividend irrelevancy theory
 - Factors affecting dividend policy
 - Dividend signaling
 - Dividend stability
 - Other Dividend Policies: constant D/P, constant DPS, residual, zero etc
 - Stock Dividend and Stock Splits
 - Share buy back

PART - B FINANCING DECISIONS

5. Equity finance

- Capital Markets
 - Primary and Secondary market
 - Concept of Initial Public offer, underwriting, tender offering and placing
- Rights Issues
 - Concept of right issue and its impact of right issue on wealth of shareholder
- Calculation of Theoretical Ex right Price (TERP)
- Valuation of common stock and preferred stock including:
 - Dividend discount models
 - Earning multiplier models
- Scrip Dividends, Bonus Issues and Share Splits
- Share Prices and Investment Returns
- Calculation of required return on equity:
 - Dividend discount model
 - CAPM
- Concept and calculation of risk and return including:
 - Expected return and risk
 - Coefficient of variation
 - Certainty equivalents
 - Portfolio return and risk
 - Diversification
 - Concept of Beta
 - Characteristics line and capital market lines
 - Over and undervalued securities etc
- Efficient Market Hypothesis (types of market efficiency i.e., weak, semi strong and strong)

6. Debt finance

- Medium Term Finance
- Long Term Debt
- Convertible Securities
- Warrants
- International Debt Finance
- valuation of Perpetual bonds, Zero coupon bonds, Bonds with definite maturity, Deep discount bonds
- concept of KIBOR and LIBOR
- Treasury securities
- Yield curve (Term structure of interest rates)
- Bond price behavior such as price/yield relationship
- Callable and put able bonds

7. Leasing

- Operating VS financial lease
- Amortization
- Leasing as a Source of Finance
- Lease or Buy decision

8. The cost of capital

- Concept of Cost of capital, optimum cost of capital and its theories
- Cost of Equity
 - Dividend Valuation Model Without growth and with growth
 - CAPM
- Cost of debt (All types of Debts)
- Cost of preference shares (redeemable, irredeemable, convertible)
- Weighted average cost of capital
 - Calculation of weighted average cost of capital (WACC)
- Project Specific Cost of Capital
 - Concept of leverage, Business Risk and financial Risk and calculation of Asset beta and Equity beta.
 - Calculation of Risk adjusted WACC of a single business
 - Calculation of Risk adjusted WACC of a combined business (Only two businesses combined)

9. The capital Structure

- Capital Structure decision
 - Concept of capital structure and optimum capital structure
- Effect of Capital Structure on ratios
- Theories of Capital Structure
 - Traditional theory of capital structure
 - MM theory without tax
 - MM theory with tax

10. Operating and Financial Leverage

- Operating leverage
- Degree of Operating Leverage (DOL) & business risk
- Operating BEP (Break Even Point)
- Financial leverage
- Financial BEP
- Point of indifference
- Degree of Financial Leverage (DFL) & financial risk
- Degree of Total Leverage (DTL)
- Optimal financing option

11. Treasury Management

- Treasury Functions
 - Roles and responsibilities of a treasury department
- Concepts of Foreign currency and domestic currency, FX exchange rate understanding Bid/Buying rates and Ask/Offer/Selling rates in Direct and Indirect Quoting.
- Risk and Reward
 - Assessment of Risk associated with dealings in foreign currency
- Hedging for foreign currency Risk
 - Invoice in home currency
 - Leading and lagging
 - Netting / Matching assets and liabilities
 - Forward rate agreement and contracts
 - Money market hedging
 - Currency options (Basic concept and basic calculations)
 - Currency futures (Basic concept and basic calculations)

- Currency swaps (Basic concept and basic calculations)

PART - C
INVESTMENT DECISIONS AND PROJECT CONTROL

12. Investment appraisal techniques

- Capital Investment Appraisal
 - Concept of Capital investment and its appraisal
 - Non-Discounted Techniques
- Accounting rate of return
- Payback period
 - Discounted Techniques
- NPV Calculation of NPV by preparing operating cash flows and adjusting for inflation and taxation.
- IRR /MIRR
- Discounted payback period
- Profitability index
- Dealing with assets of unequal lives
 - Equivalent Annual Benefit (EAB)
 - Equivalent annual Cost (EAC)
- Risk and Uncertainty
 - Sensitivity analysis in Capital investment appraisal
 - Concept and application of expected values in calculation of NPV

13. International investment

- International Investment: Basis and Risk
- International Investment: Appraisal
 - Calculation of NPV for international projects
- Purchasing power parity
- International fisher effect
- Interest rate parity
- Appreciation and depreciation of currency
- Further risks / exposure in international investment

14. Specific investment appraisal scenarios

- Capital Rationing
- De-merger including exit strategies
 - Single period capital Rationing. Calculation of optimum investment mix under both assumptions that projects can be divisible and indivisible.

- Concept of soft and hard capital rationing and reasons of these.
- Dealing with assets of unequal lives and Asset replacement cycle decision
 - Calculation of Equivalent Annual Benefit (EAB)
 - Calculation of Equivalent Annual Cost (EAC)
- Real Options Black Scholes Model -Introduction
- Adjusted Present Value
 - Concept of APV and when to calculate APV in capital investment appraisal
 - Calculation of APV
 - APV in case of Subsidized or cheap loan

15. Control of investment projects

- Investments and Projects
- Feasibility Study
- Project Control
- Investment Performance
- Post-Completion Audits

16. Business valuations

- Reasons for Valuations
- Asset Valuation bases
- Earning Valuation bases
- Dividend Valuation bases
- Cash Flow Valuation Method
- Calculation of Economic value added (EVA) and Market value added (MVA)
- Valuation of intangible assets CIV approach
- Valuation issues

17. Amalgamations and restructuring

- Mergers and Acquisitions (Types of mergers / integration, Types of synergies in merges)
- Conduct of a takeover
- Payment Methods
- Valuation of Mergers and Amalgamations
- Regulation of Acquisitions
- Post-acquisition integration
- Impact of mergers and acquisition on stakeholders
- Bootstrapping
- Impact on combined EPS after merger
- LBO/MBO
- Defense mechanisms