



## PROFESSIONAL 2 – STRATEGIC CORPORATE FINANCE

### EDUCATORS BRIEFING 2018/19

#### **Comment on 2018 Examination Performance**

April 2018 – 100% pass rate. All candidates performed well.

August 2018 - 100% pass rate. All candidates performed well.

The importance of DCF valuation techniques has been mentioned in previous educators' briefings and it appears that students are well prepared for critically evaluating the value of businesses in project proposals using the above mentioned techniques.

Students are also well prepared for critically appraising a company's exposure to foreign exchange risks which are very significant issues facing companies in the world of strategic corporate finance.

#### **Syllabus Objectives**

The aim of this subject is to develop students' critical understanding of the key responsibilities and financing decisions facing today's strategic financial manager. Students should be able to develop detailed business plans, to assess potential financial risks, and to advise on suitable risk management strategies for entrepreneurial activities and established organisations. Detailed learning outcomes can be found in the syllabus available from [www.cpaireland.ie](http://www.cpaireland.ie).

#### **Syllabus Changes**

There are no significant syllabus changes for 2019.

The following syllabus clarifications arose from past Educators' Conferences:

- Answers to questions based on case studies require that students engage with the material contained in the case. There should be no off-the-shelf templates for answers or styles of answer. What is required is a clear understanding of the concepts of Corporate Finance and how they can be applied in practice. Students must be able to determine the appropriate quantitative analyses to be undertaken to address the salient issues in a case. Having undertaken appropriate computations students are expected to justify, interpret and explain their significance and limitations in the context of the case.
- An assessment of value creation/destruction should underpin the evaluation of projects and strategies and any advice given in relation to same, while at the same time taking into account other relevant objectives of the firm in the given context.

- Investment Appraisal, valuation especially with particular emphasis on DCF techniques, capital rationing, agency theory, corporate governance and leverage are all examinable topics. This may involve the valuation of a business or the assessment of whether a merger creates or destroys value.
- The specific investment appraisal topic concerning the determination of optimum asset replacement cycles will not be examined.
- **Detailed** Interest Rate Risk related **calculations** involving futures and swaptions will not be required though candidates should be familiar with how to use such instruments to achieve financial risk management goals.
- **Detailed** Foreign Currency Risk related **calculations** involving futures and swaps will not be required though candidates should be familiar with how to use such instruments to achieve financial risk management goals.
- More generally, **detailed calculations** relating to derivative positions will not be required though candidates should be familiar with how to use such instruments to achieve financial risk management goals.
- Valuation issues which constitute the core of Corporate Finance can, at least partly, be addressed by accounting analyses. Students should be able to apply financial ratio analysis and understand the links between accounting information and strategic financial decision making. The ability of candidates to bring their accounting expertise to bear on financial decisions maintained, in 2018, the improvement demonstrated in recent prior years.
- Capital structure theories and their application in informing corporate financial policy advice are examinable topics. Students should be able to evaluate whether a client has the repayment capacity for any borrowing it may wish to undertake.
- For students to score well they must be able to identify the major factors that affect valuation in the case. A lack of knowledge of how to compute free cash flow or residual income (either will suffice) in order to establish the discounted cash flow valuation of a company will severely hinder a student's prospects for doing well in the SCF examination. In terms of foreign currency exposure the cases don't generally look for textbook type hedging solutions. Rather they look for long-term solutions to address the particular type of economic exposure relevant to the case. More detailed discussion and justification of the position taken regarding the case is required. While the cases can be complex and attention must be paid to each complexity it is important to identify the crucial issues that require attention. These issues must then be appraised in appropriate detail. An ability to use the accounting data given in the case to understand the corporate finance issues facing a company is essential when attempting the SCF examination.

- Students should be able to advise clients appropriately with respect to their business plans and their banking relationships.

### **Style of Examination**

The examination will be case study based. The case study will include considerable narrative and relevant financial/quantitative detail. Students will be expected to critically apply their knowledge of each syllabus area to analyse the scenarios presented with a view of addressing specific decision making or valuation problems, focusing on strategically important financial considerations. In doing so, they should demonstrate an ability to produce an appropriate synthesis by formulating well motivated and relevant advice for key stakeholders and decision-makers identified by the case study.

### **Format of Examination Paper**

The format of the papers for 2019 will be as follows:

**Section A** - Q 1 – Compulsory (50 Marks)

**Section B** - Q 2, Q3 and Q4 – Choice of two of these three questions (25 Marks each)

The initial question, carrying 50 marks, will usually involve some detailed financial analysis typically requiring the appraisal of a project or the valuation of a business/company in order to address a given financial strategy problem. The other questions will cover a broader range of examinable topics and may take a variety of formats. In any case, the analysis required to answer the first question will typically come useful in answering the other questions. Therefore, the candidate is advised to go through the first question before attempting the other ones, as the former will set the stage (especially in terms of detailed calculations and analysis) for answering the latter.