

LE Paper 11 Corporate Finance

Syllabus (Effective from 1 February 2024)

Topic 1: Overview of the corporate finance industry

- 1 What is corporate finance?
 - Intermediation
 - Characteristics of financial markets
 - Securities
 - Equity and debt
 - Hybrids
 - Derivatives
 - Types of financial markets
 - Trading systems
 - Quality control in international securities markets
 - Liquidity in securities markets
 - Globalisation of financial markets
- 2 Types of organisation
 - Sole proprietor
 - Partnership
 - Unincorporated joint venture
 - Companies
 - Government and semi-government agencies
 - Other exotic types of incorporated entity
- 3 Problems faced by the finance industry
 - Problems and pitfalls in the finance industry
 - Ethics
 - Corporate governance
 - The finance industry, auditing and accounting

Topic 2: Accounting and financial statement analysis

- 1 Background
 - Accounting assumptions and principles

- Accrual accounting – working examples
 - Accounting standards – local and international
 - Accounting guidelines
 - Risk disclosure
- 2 Reading and understanding financial statements
- What is the reader looking for?
 - Statement of accounting principles
 - Statement of financial position
 - Current versus non-current
 - Classification of non-current assets
 - Spreading non-current assets over their useful life
 - Income statement
 - Cash flow statement
 - Notes to the financial statements
 - Creditors, accruals, provisions and contingencies
 - Shareholders' equity: capital, reserves and retained earnings
 - Segment reporting
 - Related-party transactions
- 3 Are financial statements and financial accounts adequate?
- Cosmetic accounting
 - Context
- 4 Using this information
- Ratio analysis
 - Cash-flow analysis
- 5 Special topics in accounting
- Accounting for business combinations
 - Accounting for asset securitisation
 - Accounting for derivatives and hedging activities
 - Foreign currency translation
- 6 Putting it all together: financial analysis

Topic 3: Principles of corporate finance

- 1 Basic principles
 - Uncertainty and risk
 - The time value of money
 - Risk and return
 - Interest and discount
 - Cost of capital
 - Alternative methods of calculating the cost of equity
 - Financial leverage and capital structure
 - Taxation
- 2 Capital budgeting
 - The decision process
 - Generation of investment proposals
 - Initial screening of proposals
 - Capital budgeting process
 - Detailed analysis of projects under consideration
 - Working capital
 - Selection and approval
- 3 Application of these principles
 - Alternative methods and considerations in evaluating investment proposals
 - Structuring the finance
 - Building a corporate finance structure to suit a company's needs
- 4 Corporate collapse
 - Causes of corporate collapse
 - Warning signals of failure
 - Trajectories of failure
 - Identifying the appropriate strategy for dealing with collapse
 - Implementing strategies for management of non-performing equities and non-performing loans
- 5 Infrastructure finance
 - Assessing potential infrastructure projects
 - Project participants

- Types of infrastructure financing risks and their allocation or mitigation
 - Structuring infrastructure finance
- 6 General principles of conduct in a corporate finance office

Topic 4: Equity financing

- 1 Capital needs of companies
 - The financing cycle of a company
- 2 Forms of equity financing
 - Ordinary shares
 - Special features of Hong Kong and PRC markets
 - Preference shares
 - Non-voting shares
 - Other products
 - Options
 - Concerns about stock options
 - Warrants
 - Hybrids
- 3 Considerations in devising equity structures
 - Taxation
 - Family shareholdings
 - Maintenance of control
 - Financing considerations
 - Rights issues
 - Incentives
- 4 The capital-raising process
 - Prospectus
 - Advisers to issuers
 - Underwriting
 - Vetting and approval by SEHK
 - Marketing the float
 - Allocation of shares
 - Listing date and thereafter

- ESG matters
- 5 Venture capital
 - Start-up and early-stage financing
 - Key characteristics
 - Linkages between cash flow analysis and venture capital financing
 - Other types of venture capital financing
 - Sources of repayment
 - Alternative capital raising methods for venture capital or private equity
- 6 Corporate governance and its role in equity financing
 - Definition of corporate governance
 - Asian corporate governance
 - Strengthening corporate governance

Topic 5: Debt financing

- 1 Characteristics of debt
 - Short-term versus long-term
 - Secured versus unsecured
 - Credit foncier versus bullet repayment
 - Intermediation versus debt securities
- 2 Types of debt financing
 - Conventional bilateral loans
 - Multilateral facilities
 - Commercial paper
 - Medium-term lending
 - Bonds
 - Convertible bonds
 - Asset-based finance
 - Securitisation
- 3 Process of approval of loans
- 4 Determining the appropriate debt structure
 - Debt service capacity
 - Fixed or floating

- Drawn or stand-by
 - Taxation
 - On-balance sheet or off-balance sheet
 - Domestic or international sources of funding
 - Public or private funding
- 5 International debt markets
- What international markets are available?
 - Why use international markets?
 - Who are the investors?
- 6 Securitisation
- Benefits of securitisation
 - Potential pitfalls of securitisation
 - Development of securitisation markets
 - Range of assets capable of being securitised
- 7 Managing debt
- Monitoring and management
 - Annual review

Topic 6: Business valuation

- 1 Essential principles
- Purpose of valuation
 - Investment objectives of clients
 - Professional valuation versus ad hoc/kerbside valuations
 - Disclosure of valuation methodology and assumptions
 - Valuation at a point in time
- 2 Valuation techniques
- Undiscounted valuation
 - Discount valuation with internal data
- 3 The company and its industry
- Understanding the industry in which a company operates
 - Understanding the business environment
 - Understanding the industry-specific competitive pressures

- Identifying changes to the competitive environment
 - Assessing sustainability
 - Focus of management team
- 4 Pricing issues of “new economy” companies
 - Implications of “new economy” multiples
 - 5 Valuation of business under special situations
 - Takeovers
 - Mergers
 - Liquidations
 - Market downturns
 - Divestiture
 - Boom valuations, bubble valuations and changed bases of valuation

Topic 7: Mergers and acquisitions

- 1 Overview of mergers and acquisitions
 - Motives
 - Social and economic implications
 - The players
 - Ethical issues
- 2 Structuring a takeover
 - The mechanics of a takeover
 - Takeover strategies
 - Legal issues
- 3 The target
 - Choosing the appropriate strategy
 - Pre-emptive versus reactive defensive strategies
- 4 Directors’ duties in a takeover

Expected Learning Outcomes (“ELOs”)

Topic 1: Overview of the corporate finance industry

The candidates should demonstrate a good understanding of the corporate finance industry, including its role, participants, and financial instruments involved.

The candidates are expected to:

- (a) describe the roles and functions of financial intermediaries and differentiate between direct and indirect financing, including their associated risks;
- (b) explain the implication of funding the needs of corporations through equity and debt;
- (c) differentiate between financial instruments used in corporate finance market;
- (d) explain how globalisation is affecting financial markets;
- (e) describe the interrelationship between regulations and efficient financial markets;
- (f) differentiate between various types of market participants by assessing their legal structure, liability implications, and regulatory considerations;
- (g) describe the causes and consequences of major failures in the finance industry and the approaches adopted to deal with them.

Topic 2: Accounting and financial statement analysis

The candidates should demonstrate a good understanding of accounting principles and key concepts, as well as the ability to analyse financial statements through structured approach.

The candidates are expected to:

- (a) apply a structured approach to financial analysis, focusing the need for a deep understanding of the company, its industry, and its competitive environment;
- (b) describe and apply the fundamental accounting assumptions and principles;
- (c) describe the role of accounting standards and risk disclosure requirements in shaping the content and comparability of financial statements;

- (d) explain the components and interrelationships of the statement of financial position, income statement, and cash flow statement, and evaluate a company's financial position and performance;
- (e) explain how to assess a company's financial position based on the key financial disclosure;
- (f) assess a company's overall financial position and performance relative to its peers, to investor's expectations, and its risk profile;
- (g) explain cosmetic accounting techniques and their impact on the reliability of financial statements;
- (h) explain the accounting treatments and financial statement implications of complex transactions, including business combinations, asset securitisation, etc.

Topic 3: Principles of corporate finance

The candidates should demonstrate solid understanding of corporate finance principles, including capital budgeting, investment proposal evaluation, and the analysis of corporate failure, as well as key concepts in infrastructure finance.

The candidates are expected to:

- (a) explain the nature of risk and return and assess their relevance to financial markets;
- (b) explain the concept of the time value of money and evaluate its impact on financial transactions;
- (c) differentiate between debt and equity;
- (d) evaluate investment proposals and different sources of financing;
- (e) assess alternative means of evaluating investment proposals;
- (f) describe the principles of corporate finance and apply them to specific areas of corporate finance;
- (g) describe the nature, causes, warning signals and responses to corporate collapse;
- (h) describe the features of infrastructure finance;
- (i) cite the essential principles of conduct required to maintain a professional corporate finance business.

Topic 4: Equity financing

The candidates should demonstrate a solid understanding of concepts related to equity financing, including its characteristics, types, processes and considerations.

The candidates are expected to:

- (a) describe the features of various forms of equity financing;
- (b) describe the special features and restrictions that apply to some shares in the Hong Kong and Chinese Mainland markets;
- (c) differentiate between types of preference shares;
- (d) describe dual-class shares;
- (e) evaluate the use of options in equity markets;
- (f) describe the tax-driven financing arrangements that can be achieved using hybrid securities;
- (g) explain the taxation considerations in devising equity structures;
- (h) explain the considerations which need to be assessed when structuring equity;
- (i) evaluate the factors influencing a company's decision to raise funds through equity or debt;
- (j) describe the capital-raising process;
- (k) describe venture capital ("VC") and its key characteristics;
- (l) describe the particular funding requirements of start-up companies;
- (m) differentiate between leveraged buy-outs, management buy-outs and management buy-ins, as well as their application;
- (n) describe alternative capital raising methods for venture capitals or private equity;
- (o) explain corporate governance and its key issues;
- (p) describe the steps being taken in Hong Kong to strengthen corporate governance.

Topic 5: Debt financing

The candidates should demonstrate a solid understanding of concepts related to debt financing, including its characteristics, types, processes and structures.

The candidates are expected to:

- (a) evaluate the considerations that determine the structure of debt available for transactions;
- (b) describe and evaluate the types of debt in the domestic and international markets;
- (c) assess the relationship between debt structure and the nature, size and domicile of the borrower;
- (d) assess the appropriate level of debt for a borrower or group of borrowers;
- (e) evaluate the considerations that apply when pricing a loan transaction;
- (f) describe the overview of various international debt markets available to borrowers;
- (g) describe the features, benefits and pitfalls of securitisation;
- (h) assess how lenders manage loan exposures (both direct and indirect) over the life of a loan transaction.

Topic 6: Business valuation

The candidates should demonstrate a solid understanding of the principles and techniques of business valuation, including pricing and valuation of different types of companies or in special situations.

The candidates are expected to:

- (a) assess the varying valuation requirements of different situations in financial markets;
- (b) describe the need for an objective, professional approach in addressing the valuation requirements;
- (c) assess the range of fundamental valuation approaches that are used in financial markets;
- (d) explain the relationship between a company's sustainable competitive position and the business environment it operates, the influence of industry-specific factors, its own capabilities and corporate governance;
- (e) assess the valuation models of "new economy" companies;
- (f) describe the principles of business valuation in special situations.

Topic 7: Mergers and acquisitions

The candidates should demonstrate a solid understanding of the parties, structuring, and considerations involved in mergers and acquisitions ("M&A").

The candidates are expected to:

- (a) explain various motivations that prompt companies to launch takeovers;
- (b) explain the economic and social impact of takeovers, and the interrelationship between corporate failure and M&A theories;
- (c) assess the structure of takeovers;
- (d) describe the roles of the key players in the process, the bidder, the potential target and other participants;
- (e) apply takeover strategies from the perspectives of both the bidder and the target respectively;
- (f) describe general legal issues to be considered by all parties;
- (g) describe the duties of directors in takeovers.