CIMA

Financial Strategy

Strategic level | Subject F3

CIMA official revision cards

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How to use Revision Cards

The concept

- Revision Cards are a new and different way of learning, based upon research into learning styles and effective recall.
- The cards are in full colour and have text supported by a range of images, making them far more effective for visual learners and easier to remember.
- Unlike a bound text, Revision Cards can be rearranged and reorganised to appeal to kinaesthetic learners who prefer to learn by doing.
- Being small enough to carry around means that you can take them anywhere. This gives the opportunity to keep going over what you need to learn and so helps with recall.
- The content has been reduced down to the most important areas, making it far easier to digest and identify the relationships between key topics.
- Revision Cards, however you learn, whoever you are, wherever you are.........

How to use them

Revision Cards are a pack of approximately 52 cards, slightly bigger than traditional playing cards but still very easy to carry and so convenient to use when travelling or moving around. They can be used during the tuition period or at revision.

They are broken up into 3 sections.

- An overview of the entire subject in a mind map form (orange).
- A mind map of each specific topic (blue).
- Content for each topic presented so that it is memorable (green).

Each one is a different colour, allowing you to sort them in many ways.

- Perhaps you want to get a more detailed feel for each topic, why not take all the green cards out of the pack and use those.
- You could create your own mind maps using the blue cards to explore how different topics fit together.
- And if there are some topics that you understand, take those out of the pack, leaving yourself only the ones you need to concentrate on.

There are just so many ways you can use them.

Contents

Core areas of the syllabus

A	Financial policy decisions	15%
B	Sources of long term funds	25%
C	Financial risks	20%
D	Business valuation	40%

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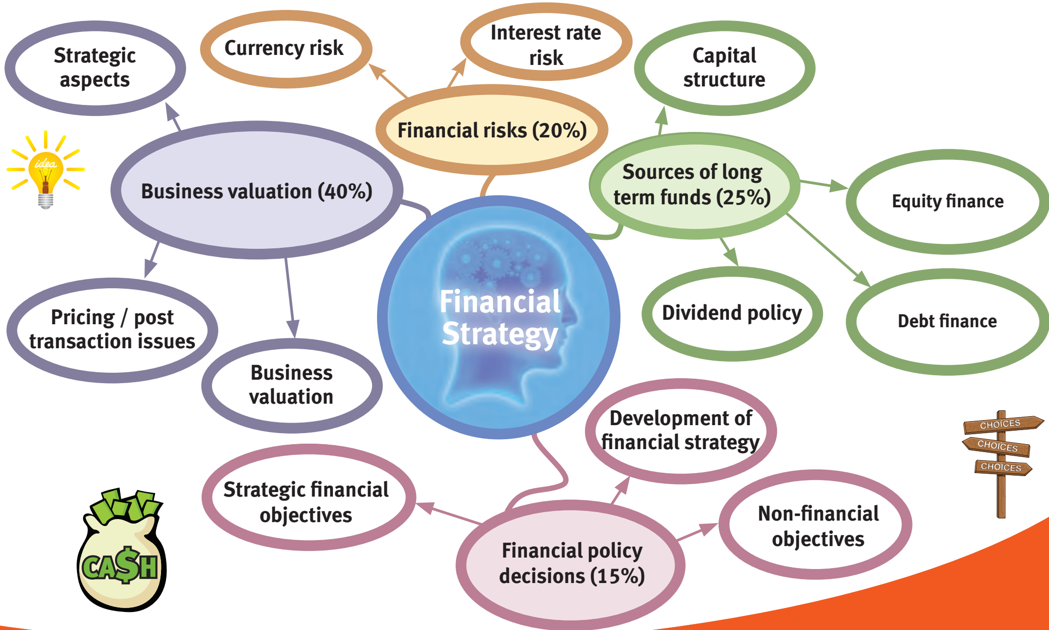
overview

financial strategy

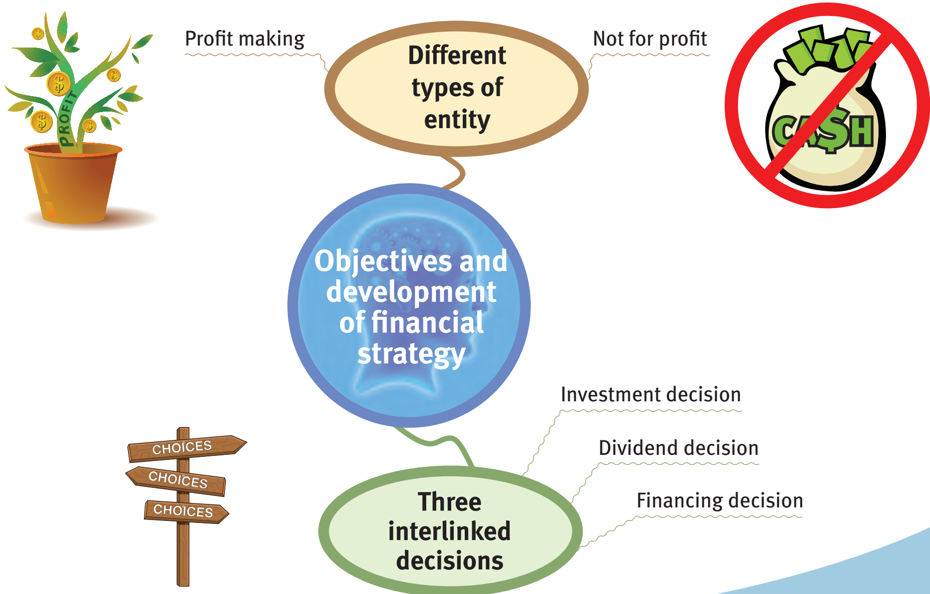
RevisionCards


Financial Strategy
Business valuation (40%)
Strategic aspects
Pricing / post transaction issues
Business valuation
Financial risks (20%)
Currency risk
Interest rate risk
Sources of long term funds (25%)
Capital structure
Equity finance
Dividend policy
Debt finance
Financial policy decisions (15%)
Strategic financial objectives
Development of financial strategy
Non-financial objectives
idea
CA$H
CHOICES
CHOICES
CHOICES

Objectives and development of financial strategy

financial strategy

RevisionCards



Profit making
PROFIT
Different types of entity
Not for profit
CA$H
Objectives and development of financial strategy
CHOICES
CHOICES
CHOICES
Three interlinked decisions
Investment decision
Dividend decision
Financing decision

Objectives: Profit making v not-for-profit organisations

Profit making organisations:

A company (profit making organisation) has shareholder wealth maximisation as its **primary objective**.

The needs of other stakeholders need to be considered too, since dissatisfied stakeholders in the short term may lead to an erosion of shareholder wealth in the long term.

Not-for-profit organisations:

The **primary objective** is to provide an acceptable level of service to its key stakeholders. Financial objectives will tend to focus on costs, and the efficient, effective and economic use of resources.

- Organisations set objectives which will satisfy key stakeholders, such as:
  - **Shareholders** – require returns (dividends and / or capital growth)
  - **Employees / managers** – require job security and pay increases
  - **Customers** – require good quality products / services and reasonable prices
  - **Suppliers / Lenders** – require payment when due
  - **Government** – require taxes to be paid and laws to be followed
  - **Local community** – require considerate / responsible behaviour
- The impact of external, economic forces (such as interest rates, inflation, exchange rates) needs to be considered before objectives can be set.
- Conflicts will often arise between different stakeholder groups (e.g. shareholders requiring dividends and employees requiring pay rises).

Performance appraisal

Investors (shareholders and lenders) will often appraise the performance of an entity, to assess whether it represents a good investment.

The most readily available source of information is the published accounts, but these have the following limitations:

- figures are historic records, not forward looking.
- the accruals concept means that the income statement will not relate to the entity's cash position.
- financial information might not give a full picture of the entity's position.

Profitability ratios

- Operating profit margin = (Profit before interest and tax (PBIT) / Turnover) x 100%.
- Gross profit margin = (Gross profit / Turnover) x 100%.

Return on Capital Employed (ROCE) and Return on Equity (ROE):

ROCE = (Operating profit / Capital employed) x 100%

This measures the underlying performance of the business before considering financing.

Capital employed = total funds (debt and equity) invested in the business.

ROE = (Profit after tax (PAT) / Equity value) x 100%

This measures the return which relates to the shareholders.

Note that ROE is post tax and ROCE is pre tax, so the ratios are not directly comparable.

Financial gearing ratios

Financial gearing can be analysed by looking at the balance sheet (statement of financial position) or the income statement. The risk is that if gearing is too high, the entity will not be able to afford to service its debts.

Balance sheet
(statement of financial position)

Financial gearing can be measured as either:

Debt value / Equity value, or

Debt value / (Value of equity +debt)

- Market values should be used if possible, or use book values if working from financial accounts.

Income statement

Key measure:

Interest cover

= Profit before interest and tax (PBIT) /

Interest (Finance charges)

- A high ratio indicates low risk.

Stock market ratios

For quoted companies, stock market ratios will give a market driven measure of performance.

P/E ratio

Share price / EPS

A high P/E ratio indicates that the market has confidence in the company

Dividend cover

EPS/Dividend per share (DPS)

High dividend cover will reassure investors that dividend levels are likely to be maintained even if profits fall

Dividend yield

DPS/Share price

A basic measure of yield to shareholders

Note that:

- EPS (earnings per share) = (Profit after tax and preference dividends) / No. of shares
- A better measure of shareholder return (taking account of capital gains as well as dividends, would be [(closing share price – opening share price) + dividend] / opening share price