

**Final Course**  
(Revised Scheme of Education and Training)  
**Study Material**

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**PAPER 2**

**Strategic Financial  
Management**



**BOARD OF STUDIES**  
**THE INSTITUTE OF CHARTERED ACCOUNTANTS OF INDIA**

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## BEFORE WE BEGIN...

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Strategic Financial Management (SFM) is one of the core papers for students appearing in Final Level of Chartered Accountancy Course.

As you all are aware that SFM is a blend of Strategic Management and Financial Management. Recently, it has gained significance due to growing globalization and continuous cross border flow of capital.

Some corrections have been carried in the Study Material of this edition vis-à-vis the previous edition of October 2020. Though some additions/ deletions have also been carried out at some places, the details of notable changes have been separately outlined in separate pages titled “Significant Changes”. Accordingly, student who has referred October 2020 Edition for his/her preparation can continue to refer the same by referring to these Significant Changes.

The other characteristics of this study material which are outlined as below:

- (i) It comprehensively covers the course requirements of students preparing for SFM paper.
- (ii) It is written in a very simple and lucid manner to make the subject understandable to the students.
- (iii) At the beginning of each chapter, learning outcomes have been given so that the students know in advance as to what he will learn after going through the chapter.
- (iv) At the end of each chapter, under the caption, “Test your Knowledge” is given. Basically, the purpose of the same is to motivate the students to recapitulate what they have learnt in the chapter.
- (v) While preparing the study material, every effort has been made to keep the chapters concise, giving appropriate headings, sub-headings and examples, at suitable places.

We are confident that this study material will prove to be extremely useful to the students.

Although, sincere efforts have been made to keep the study material error free, it is possible that some error might have inadvertently crept in. In this respect, students are encouraged to highlight any mistake they may notice while going through the study material by sending an e-mail at: [sfm-final@icai.in](mailto:sfm-final@icai.in) or write to the Director of Studies, The Institute of Chartered Accountants of India, A-29, Sector-62, Noida-201309.

**Happy Reading and Best Wishes!**

# SYLLABUS

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## PAPER 2: STRATEGIC FINANCIAL MANAGEMENT

*(One paper – Three hours – 100 marks)*

### **Objective:**

To acquire the ability to apply financial management theories and techniques in strategic decision making.

### **Contents:**

#### **(1) Financial Policy and Corporate Strategy**

- (i) Strategic decision making framework
- (ii) Interface of Financial Policy and strategic management
- (iii) Balancing financial goals vis-à-vis sustainable growth.

#### **(2) Risk Management**

- (i) Identification of types of Risk faced by an organisation
- (ii) Evaluation of Financial Risks
- (iii) Value at Risk (VAR)
- (iv) Evaluation of appropriate method for the identification and management of financial risk.

#### **(3) Security Analysis**

- (i) Fundamental Analysis
- (ii) Technical Analysis
  - a) Meaning
  - b) Assumptions
  - c) Theories and Principles

- d) Charting Techniques
- e) Efficient Market Hypothesis (EMH) Analysis

#### **(4) Security Valuation**

- (i) Theory of Valuation
- (ii) Return Concepts
- (iii) Equity Risk Premium
- (iv) Required Return on Equity
- (v) Discount Rate Selection in Relation to Cash Flows
- (vi) Approaches to Valuation of Equity Shares
- (vii) Valuation of Preference Shares
- (viii) Valuation of Debentures/ Bonds

#### **(5) Portfolio Management**

- (i) Portfolio Analysis
- (ii) Portfolio Selection
- (iii) Capital Market Theory
- (iv) Portfolio Revision
- (v) Portfolio Evaluation
- (vi) Asset Allocation
- (vii) Fixed Income Portfolio
- (viii) Risk Analysis of Investment in Distressed Securities
- (ix) Alternative Investment Strategies in context of Portfolio Management

**(6) Securitization**

- (i) Introduction
- (ii) Concept and Definition
- (iii) Benefits of Securitization
- (iv) Participants in Securitization
- (v) Mechanism of Securitization
- (vi) Problems in Securitization
- (vii) Securitization Instruments
- (viii) Pricing of Securitization Instruments
- (ix) Securitization in India

**(7) Mutual Fund**

- (i) Meaning
- (ii) Evolution
- (iii) Types
- (iv) Advantages and Disadvantages of Mutual Funds

**(8) Derivatives Analysis and Valuation**

- (i) Forward/ Future Contract
- (ii) Options
- (iii) Swaps
- (iv) Commodity Derivatives

**(9) Foreign Exchange Exposure and Risk Management**

- (i) Exchange rate determination

- (ii) Foreign currency market
- (iii) Management of transaction, translation and economic exposures
- (iv)** Hedging currency risk
- (v) Foreign exchange derivatives – Forward, futures, options and swaps

#### **(10) International Financial Management**

- (i) International Capital Budgeting
- (ii) International Working Capital Management
  - a) Multinational Cash Management
    - Objectives of Effective Cash Management
    - Optimization of Cash Flows/ Needs
    - Investment of Surplus Cash
  - b) Multinational Receivable Management
  - c) Multinational Inventory Management

#### **(11) Interest Rate Risk Management**

- (i) Interest Rate Risk
- (ii) Hedging Interest Rate Risk
  - a) Traditional Methods
  - b) Modern Methods including Interest Rate Derivatives

#### **(12) Corporate Valuation**

- (i) Conceptual Framework of Valuation
- (ii) Approaches/ Methods of Valuation
  - a) Assets Based Valuation Model

- b) Earning Based Models
- c) Cash Flow Based Models
- d) Measuring Cost of Equity
  - Capital Asset Pricing Model (CAPM)
  - Arbitrage Pricing Theory
  - Estimating Beta of an unlisted company
- e) Relative Valuation
  - Steps involved in Relative Valuation
  - Equity Valuation Multiples
  - Enterprise Valuation Multiple
- f) Other Approaches to Value Measurement
  - Economic Value Added (EVA)
  - Market Value Added (MVA)
  - Shareholder Value Analysis (SVA)
- g) Arriving at Fair Value

### **(13) Mergers, Acquisitions and Corporate Restructuring**

- (i) Conceptual Framework
- (ii) Rationale
- (iii) Forms
- (iv) Mergers and Acquisitions
  - a) Financial Framework
  - b) Takeover Defensive Tactics



- c) Reverse Merger
- (v) Divestitures
  - a) Partial Sell off
  - b) Demerger
  - c) Equity Carve outs
- (vi) Ownership Restructuring
  - a) Going Private
  - b) Management/ Leveraged Buyouts
- (vii) Cross Border Mergers

**(14) Startup Finance**

- (i) Introduction including Pitch Presentation
- (ii) Sources of Funding
- (iii) Startup India Initiative

## SIGNIFICANT CHANGES

<b>Significant changes in this Study Material <i>vis-à-vis</i> Study Material of November 2020 edition of the Study Material</b>		
<b>Chapter</b>	<b>Chapter Name</b>	<b>Details</b>
1	Financial Policy and Corporate Strategy	<ul style="list-style-type: none"> <li>• Insertion of Sub-Heading '1.1 Meaning of Strategic Financial Management' including small change in the language of the contents.</li> <li>• Insertion of Sub-Heading 'Sustainable Growth Rate' including small change in the language and formatting of the contents.</li> </ul>
4	Security Valuation	<ul style="list-style-type: none"> <li>• On Page No. 4.9 please read '<math>H_1</math>= Half-life of high growth period' as '<math>H_1</math>= Half of duration of the transition period'.</li> <li>• On Page No. 4.14 changed presentation of formula for calculation of Theoretical Value of Right.</li> <li>• Insertion of new para 8.16 – Refunding of Bonds</li> <li>• Corrections in the alternative solution of Question No. 15.</li> <li>• In the solution of Question No. 27 in last table under Bond X please consider value 972.73 as 972.63 and also the answer as 51.80 instead of 51.79.</li> </ul>
5	Portfolio Management	<ul style="list-style-type: none"> <li>• Insertion of some material in the end of para 10.3 – Jensen Alpha.</li> <li>• Solution of Question No. 15 has been revised.</li> <li>• Answer to part (i) of Question No. 17 as per alternative approach has been included.</li> <li>• Answer to part (iii) of Question No. 32 as per alternative approach has been included.</li> <li>• Answer to parts (ii) and (iii) of Question No. 36 as per alternative approach has been included.</li> <li>• Solution of Question No. 39 has been revised.</li> </ul>
7	Mutual Funds	<ul style="list-style-type: none"> <li>• Insertion of some material on Quant Fund under the heading Special Funds.</li> <li>• Minor changes in the language of first two lines of para 4.9.</li> </ul>

		<ul style="list-style-type: none"> <li>• In the Question No. 19 please read second last sentence 'At the end of the year equity shares and 10% debentures are quoted at 175% and 90% respectively' as 'At the end of the year equity shares and 10% debentures are quoted at 175% and 90% respectively of face value.'</li> <li>• Insertion of alternative answer of Question No. 12.</li> <li>• Insertion of a note in the end of the solution to Question No. 7.36.</li> <li>• Insertion of note in the solution of Question No. 17 under Plan B.</li> </ul>
8	Derivatives Analysis and Valuation	<ul style="list-style-type: none"> <li>• Some values have been inserted in the end of Illustration 3 and minor change in the solution of sub-part (iii).</li> <li>• Topic of Embedded Derivatives have been removed and therefore question on the same in Test Your Knowledge section been removed.</li> <li>• Small change in the language of Question No. 4.</li> <li>• In part (ii) of Question No. 12 please ignore the Rupee symbol before 8125.</li> <li>• In the end of Question No. 19 please read the line 'Assume the size option is 100 shares of Delta Corporation.' as 'Assume the option size is 100 shares of Delta Corporation.'</li> </ul>
9	Foreign Exchange Exposure and Risk Management	<ul style="list-style-type: none"> <li>• In the Illustration No. 8, a note for sounding off rates has been inserted and hence solution stands modified. Further in solution in part (b) please ignore the phrase 'Net Amount payable by customer per US\$'</li> <li>• On page No. 9.33 language of Swap Loss has been modified.</li> <li>• In Illustration 9 the answer of sub-part (ii) and (vi) has been modified.</li> <li>• In the Question No. 16 please insert 5 before paisa.</li> <li>• Solution of part (ii) of Question No. 1 has been slightly changed.</li> <li>• In the solution of Question no. 38 in second last line 3 months has been replaced with 4 months.</li> </ul>

		<ul style="list-style-type: none"> <li>In the solution of Question No. 41 in part (b) while calculating forward rate please add 0.0060 to €1.1770 instead of 0.0055 and accordingly the answer will change to £ 3381234 instead of £ 3382664.</li> </ul>
10	International Financial Management	<ul style="list-style-type: none"> <li>Illustration 1 and its solution has been slightly revised.</li> </ul>
11	Interest Rate Risk Management	<ul style="list-style-type: none"> <li>In the second para of heading 1.3.1 please read last line as 'Conversely, a negative or liability sensitive Gap implies that the banks' NII could increase as a result of decrease in market interest rates.'</li> <li>In Question No. 3 for calculation of figures please consider 3 decimal points instead of 4 and accordingly solution stands slightly revised.</li> <li>In the second last line of Question No. 7 please ignore '9.0% and'.</li> <li>Minor changes in (ii) part of the solution of Question No. 4.</li> </ul>
12	Corporate Valuation	<ul style="list-style-type: none"> <li>In the Illustration No. please read term 'Reserves &amp; Surplus' as 'Surplus Fund'. Further in the answer in second table ignore term 'Enterprise Value' after Equity Value.</li> <li>On page No. 12.25 in the table of Step a(2) please read 'Forecasted Net Working Capital' as 'Forecasted Increase in Working Capital'.</li> <li>In Question No. 3 please read the line 'From 4<sup>th</sup> year onward it will stabilize.' as 'From 4<sup>th</sup> year onward cash flow will be stabilized.'</li> </ul>
13	Mergers, Acquisitions & Corporate Restructuring	<ul style="list-style-type: none"> <li>Under the sub-heading 4.2 please ignore the last para.</li> <li>Case Studies under the heading 11 have been removed.</li> <li>In Question No. 19 in last line of para below the table please consider '(EPS)' after 'earnings'.</li> <li>In Question No. 30 missing value of Equity Capital i.e. ₹ 70,00,000 has been inserted.</li> </ul>
14	Startup Finance	<ul style="list-style-type: none"> <li>In Bootstrapping, please ignore the last para as already covered earlier.</li> </ul>

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