### SESSION PLAN

**COURSE:** ABE Level 6 Corporate Finance

**ELEMENT:** Element 2 – Equity and debt financing

## **LEARNING OUTCOME 2**

**2 Critically evaluate alternative sources of finance to ensure that financing decisions reflect the strategic objectives and strategic circumstances of the business (Weighting 20%)**

2.1 Compare alternative approaches to sources of equity and debt in relation to the strategic objectives and strategic environment of the business

2.2 Critically evaluate the impact of the use of a range of equity and debt financing on business’s financing structure

2.3 Apply criteria and decision-making frameworks in equity and debt financing

**NUMBER OF SESSIONS** Three - approximately twelve hours in total (plus self-study)

**SESSION TOPICS:** Session 1: Compare alternative approaches to sources of equity and debt in relation to the strategic objectives and strategic environment of the business

Session 2: Critically evaluate the impact of the use of a range of equity and debt financing on a business’s financing structure

Session 3: Apply criteria and decision-making frameworks in equity and debt financing

**Note to tutors: this is the recommended session plan for learning outcome 2, element 2 of ABE Level 6 Corporate Finance. You should follow the plan, using the resources (referenced as ‘slides’ here) and activities provided. It is important to enhance all sessions with local examples and case studies, involving the learners ACTIVELY wherever possible.**

### SESSION 1: Compare alternative approaches to sources of equity and debt in relation to the strategic objectives and strategic environment of the business

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| **Approx.**  **Duration** | **Topic** | **Tutor Activity** | **Slides** | **Learner Activity** | **Formative Assessment** |
| 3-4 hours | Alternative approaches to sources of equity and debt | Use filename: **6UCF Presentation E2**  Explain the unit, and what is going to be covered.  Assessment criterion 2.1  Explain how sources of finance can be grouped into two broad categories: equity and debt. Explain how equity and debt finance have different key features. Outline how different types of finance relate to the business’s strategic objectives and environment. Explain how businesses must take care to select sources of finance that are appropriate.  Play this to help to explain the concept of the need to decide how best to meet the financing needs of the business:  <https://www.youtube.com/watch?v=MrupJdMrpaE> | 1-5 | In small groups, learners should identify the importance of sources of finance to businesses.  Using the organisations that they identified and analysed as part of the activity in the previous session. Consider each of the businesses and the relative importance of equity and debt finance to each. | **6UCF E2 LO2 Activity 1 –** Alternative approaches to sources of equity and debt |
| The matching principle of finance | Outline the matching principle of finance. The matching principle of finance means that short term investment needs should be financed with short term sources of finance. Long term investment needs should be financed with long term sources of finance.  Look at the study guide for an explanation of the matching principle of finance and its importance in the selection of sources of debt and equity. | 6-7 | Learners try to identify and explain examples of different types of equity and debt finance.  Ask learners to consider the organisations that they identified and analysed as part of the activity in the previous session. Consider the particular types of equity and debt finance that are used by each of these organisations.  Allow them 30 minutes to discuss this in small groups, and then 30 minutes to present back to each other in one large group. | **6UCF E2 LO2 Activity 2** –Source of finance |
| The cost of capital | Explain how the mix of equity and debt financing represents a business’s financial structure. Hence, the cost to a business of raising finance is referred to as the cost of capital.  The mix of equity and debt financing in a business comprises its financial structure. Any imbalance in this financial structure will cause profits to be lower than they would otherwise be. The cost to a business of raising finance is referred to as its cost of capital.  Use this film to explain this in more detail: <http://www.investopedia.com/video/play/cost-capital/> | 8 | Ask learners to consider the Edmonton plc case study in the study guide. Ask learners to consider the actions that the board of directors of Edmonton plc might need to take in each of the short-term, the medium-term and the longer-term. Ask learners to explain how the company’s finances might be restructured as a basis for longer-term stability.  Allow them 30 minutes to discuss this in small groups, and then 30 minutes to present back to each other in one large group. |  |
|  | Review of session and learning outcomes | Ask students to read the second section of the study guide prior to the next session. |  | Pre-session preparation |  |

### SESSION 2: Critically evaluate the impact of the use of a range of equity and debt financing on a business’s financing structure

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| **Approx.**  **Duration** | **Topic** | **Tutor Activity** | **Slides** | **Learner Activity** | **Formative assessment** |
| 3-4 hours | Introduction to session and learning outcomes | Use file: **6UCF Presentation E2**  Assessment criterion 2.2 | 9 |  |  |
|  | Sources of finance and how they relate to strategic objectives and strategic environment | Distinguish between internal and external sources of finance. Outline the defining characteristics of internal and external sources of finance. | 10-11 | Ask learners to identify the key distinguishing characteristics of internal and external sources of finance.  Learners to identify the key characteristics of internal and external sources of finance.  Allow them 30 minutes to discuss this in small groups, and then 30 minutes to present back to each other in one large group. |  |
|  | Internal and external sources of finance | Outline how sources of finance can be categorised as internal or external and as either long-term or short-term in nature. Review the concepts of equity and debt finance that were introduced earlier in the session.  Use the following questions as discussion points:   * Are retained profits a ‘free’ source of finance? * How might shareholders feel if a business consistently uses retained profit as a source of finance, rather than distributed to shareholders in the form of a dividend? * In which industries might working capital represent a significant proportion of a business’s net asset base?   Identify and discuss the costs of holding (a) too little cash and (b) too much cash | 12  13 | Ask learners to consider the financial statements of the organisation that they identified in the previous session (alternatively, distribute examples of financial statements from businesses with which they might be familiar).  Learners to use the data in the financial statements to identify and discuss the sources of finance that are used by their chosen organisations.  Allow them 30 minutes to discuss this in small groups, and then 30 minutes to present back to each other in one large group. | **6UCF E2 LO2 Activity 3**- Types of external financing |
|  | Types of debt financing | Review the results of the activity on internal and external sources of finance that was used earlier in the session.  Outline each of the types of debt finance that were identified. Ensure that at least the following types of debt finance are considered: subordinated loan, term loans, loan notes, mortgages and bonds.  Play this to help to explain the cost of capital:  <https://www.youtube.com/watch?v=23Cg4X0caq8> | 14-15 | Ask learners to return to the activity they completed earlier in the session. Consider each of the types of debt finance that were identified. Explain the advantages and disadvantages of each.  Allow them 30 minutes to discuss this in small groups, and then 30 minutes to present back to each other in one large group, | **6UCF E2 LO2 Activity 4** – Loan financing  **6UCF E2 LO2 Activity 5** – Bond financing |
|  | Advantages and disadvantages of different sources of equity and debt financing | Review the concepts of debt and equity financing and of how the mix of equity and debt financing combines to comprise a business’s financial structure.  Play this to help to explain the concept of the need to decide how best to meet the financing needs of the business:  <https://www.youtube.com/watch?v=MrupJdMrpaE>  Explain the concept of tax shields in the concept of the use of equity or debt finance.  When they have done the activity ask them to present back their findings to the whole group. | 16-18 | Ask learners to return to the organisations that they selected for use in the previous activities.  Learners to consider the relative use of equity and debt finance in the organisations that they have selected. Ask learners to evaluate the financial structures of their selected business in the context of the financial structure of those businesses.  Allow them 30 minutes to discuss this in small groups, and then 30 minutes to present back to each other in one large group, | **6UCF E2 LO2 Activity 6 –** Equity or debt |
|  | Review of session and learning outcomes | Ask students to read the next section of the study guide prior to the next session. |  | Pre-session preparation. |  |

**Session 3: Apply criteria and decision-making frameworks in equity and debt financing**

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| **Approx.**  **Duration** | **Topic** | **Tutor Activity** | **Slides** | **Learner Activity** | **Formative Assessment** |
| 3 hours | Introduction to session and learning outcomes | Use file: **6UCF Presentation E2**  Assessment criterion 2.3 | 19 |  |  |
| Pecking order theory | Outline pecking order theory, its key characteristics and the key suggestions that are offered by pecking order theory. | 20-22 |  |  |
| Models of financial distress | Explain the nature of models of financial distress. Discuss the importance of financial ratios in these models.  Outline Altman’s Z-score model in this context.  Use this YouTube film to explain this in more detail:  <http://www.investopedia.com/terms/a/altman.asp> | 23 | Use the study guide. Ask learners to read the paper by Grice and Ingram (2001).  Ask learners to critically evaluate then usefulness of Altman’s model in the prediction of bankruptcy. | **6UCF E2 LO2 Activity 7 –** Different types of risk |
| Review of session and learning outcomes | Ask students to prepare for the next session by reading the first section of the next chapter in the study guide. |  | Pre-session preparation. |  |

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