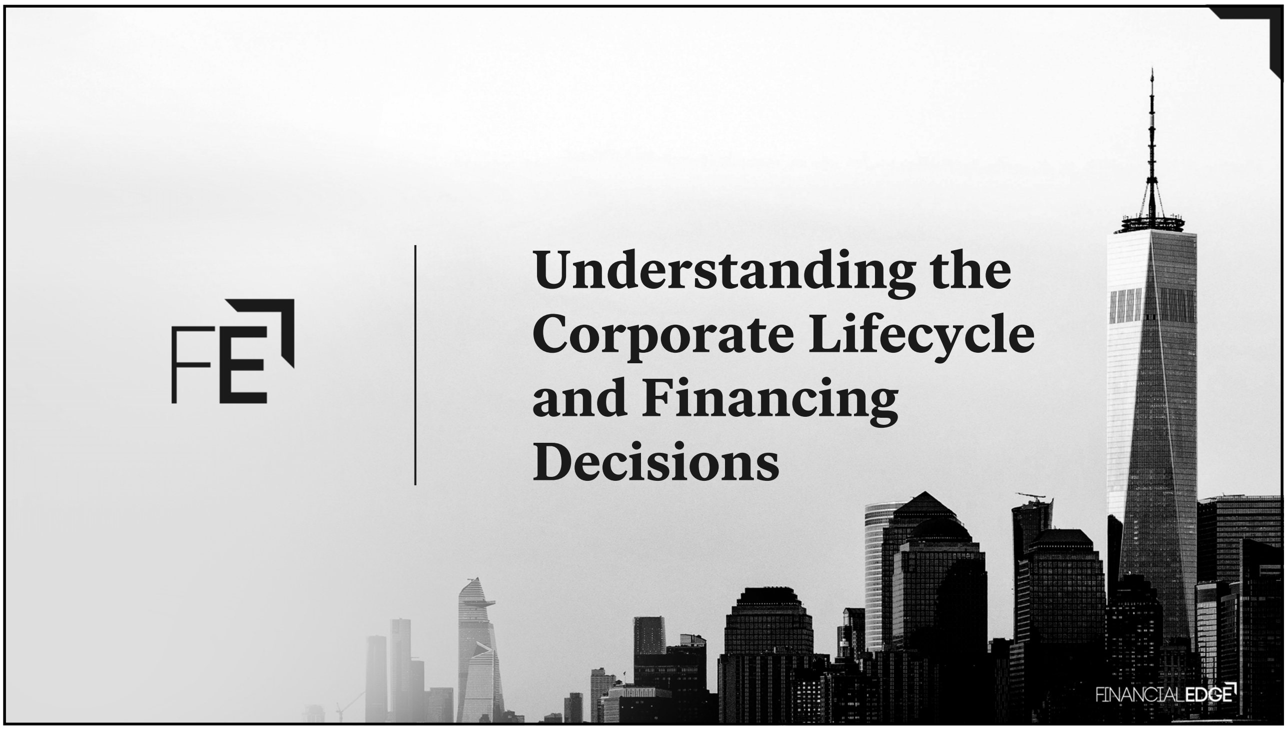
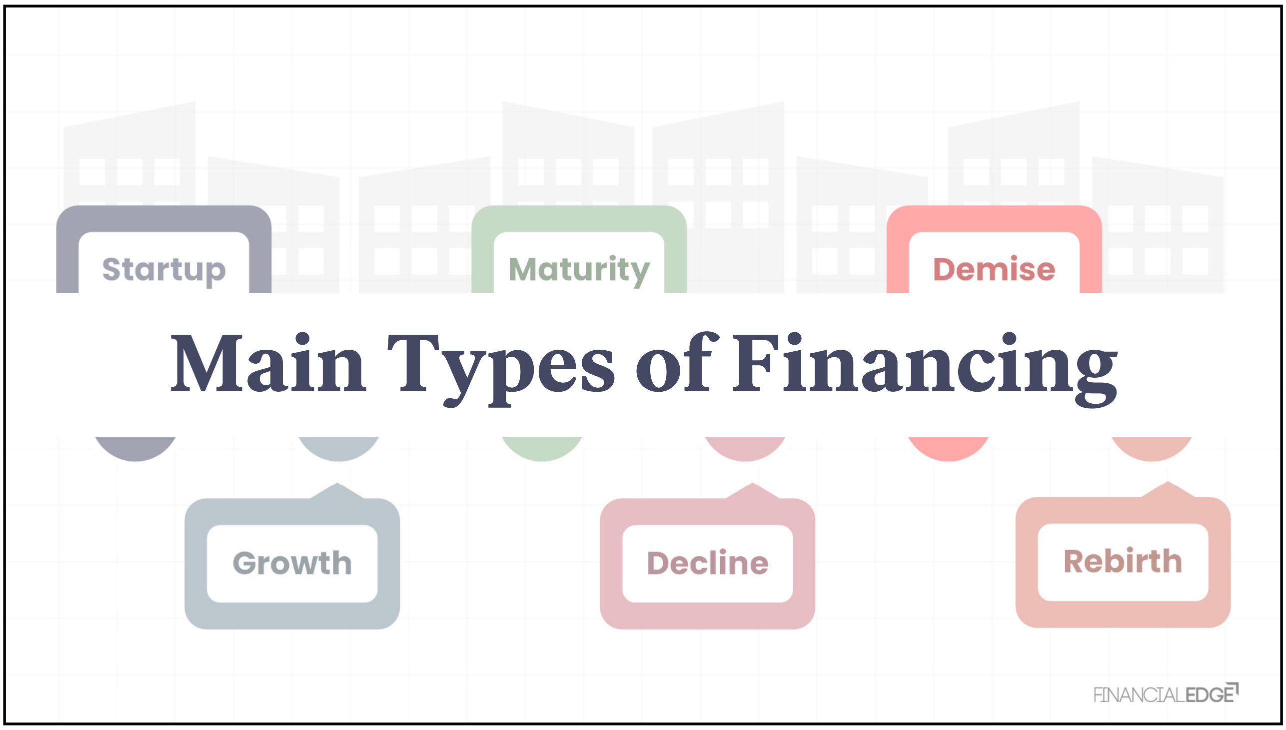

FE
Understanding the Corporate Lifecycle and Financing Decisions
FINANCIALEDGE


Startup
Maturity
Demise
Main Types of Financing
Growth
Decline
Rebirth
FINANCIALEDGE

Companies

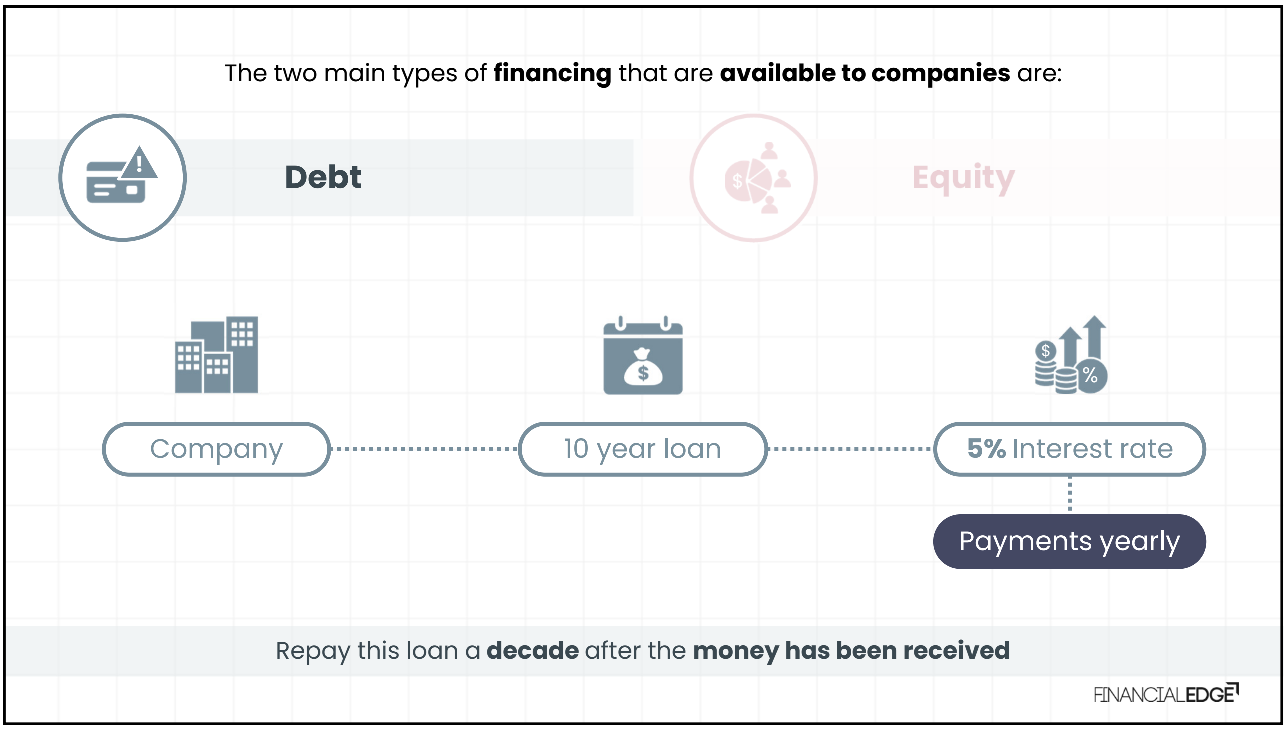
Need money to operate and grow:

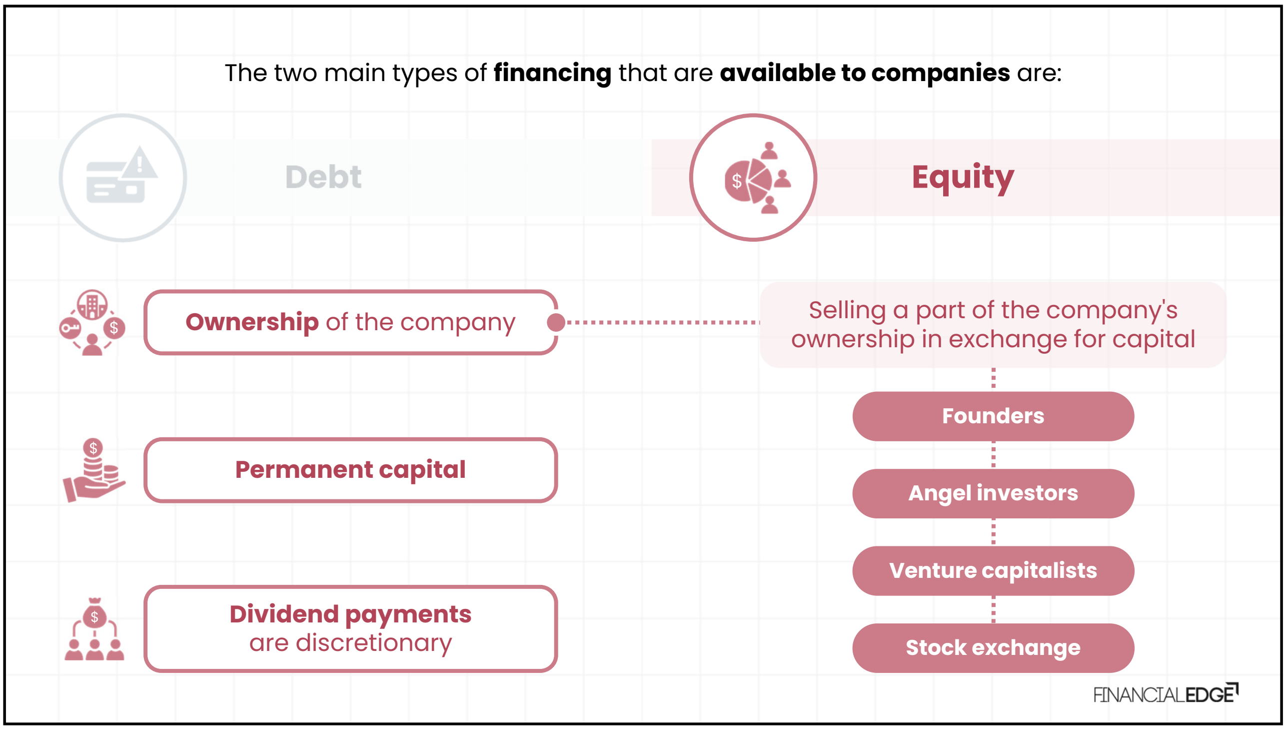
1. **Fund day to day operations**
2. **Invest in projects**
3. **Expand into new markets**

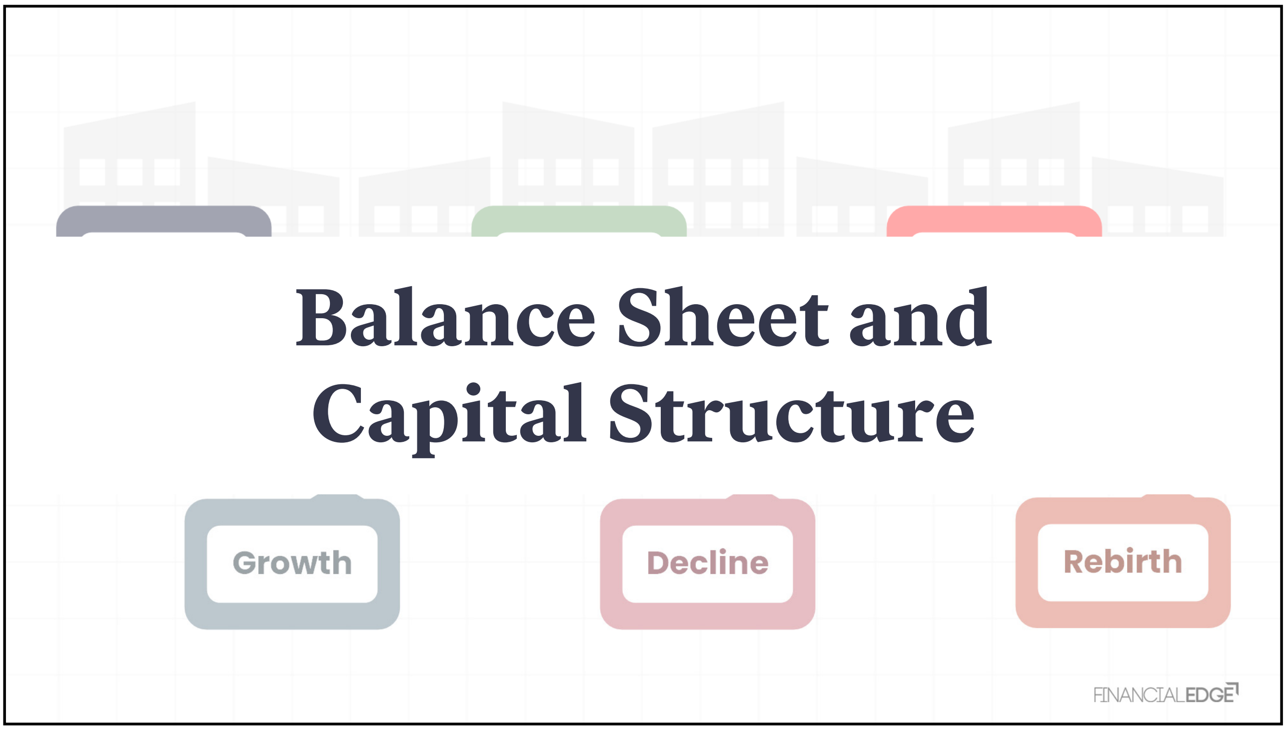
The two main types of **financing** that are **available to companies** are:

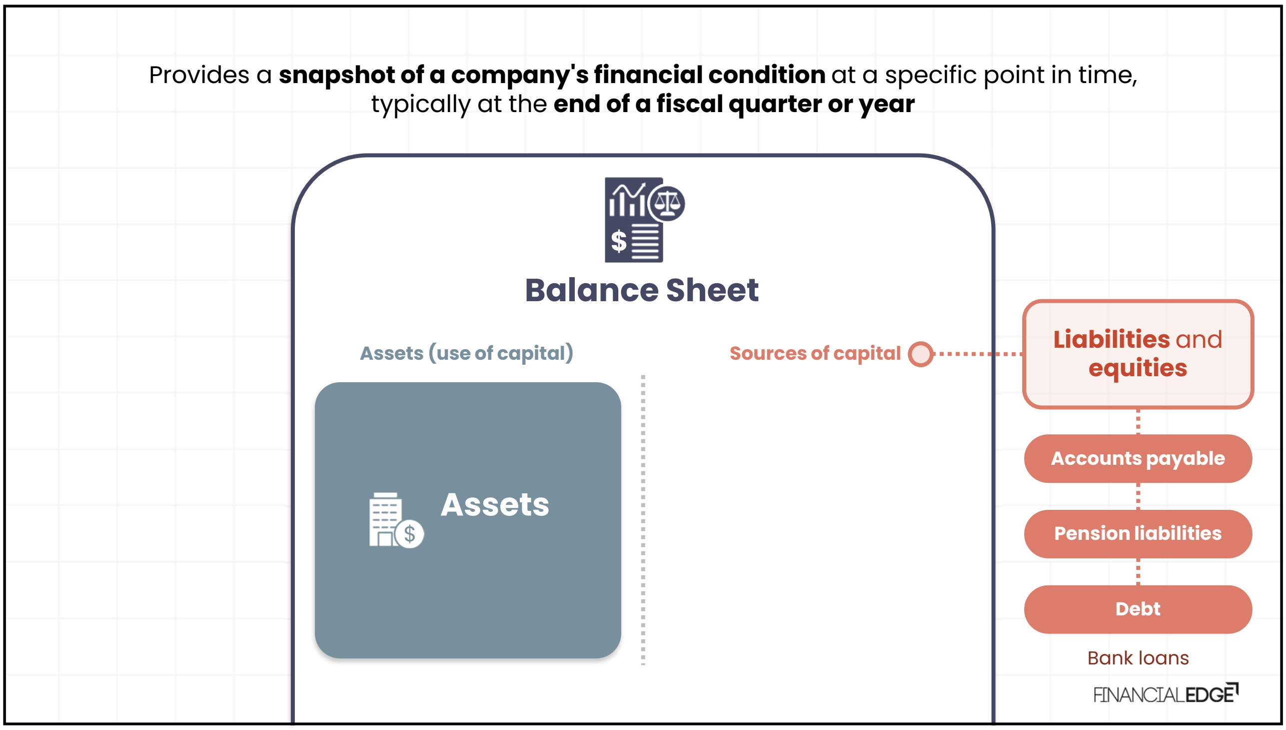
Debt | **Equity**

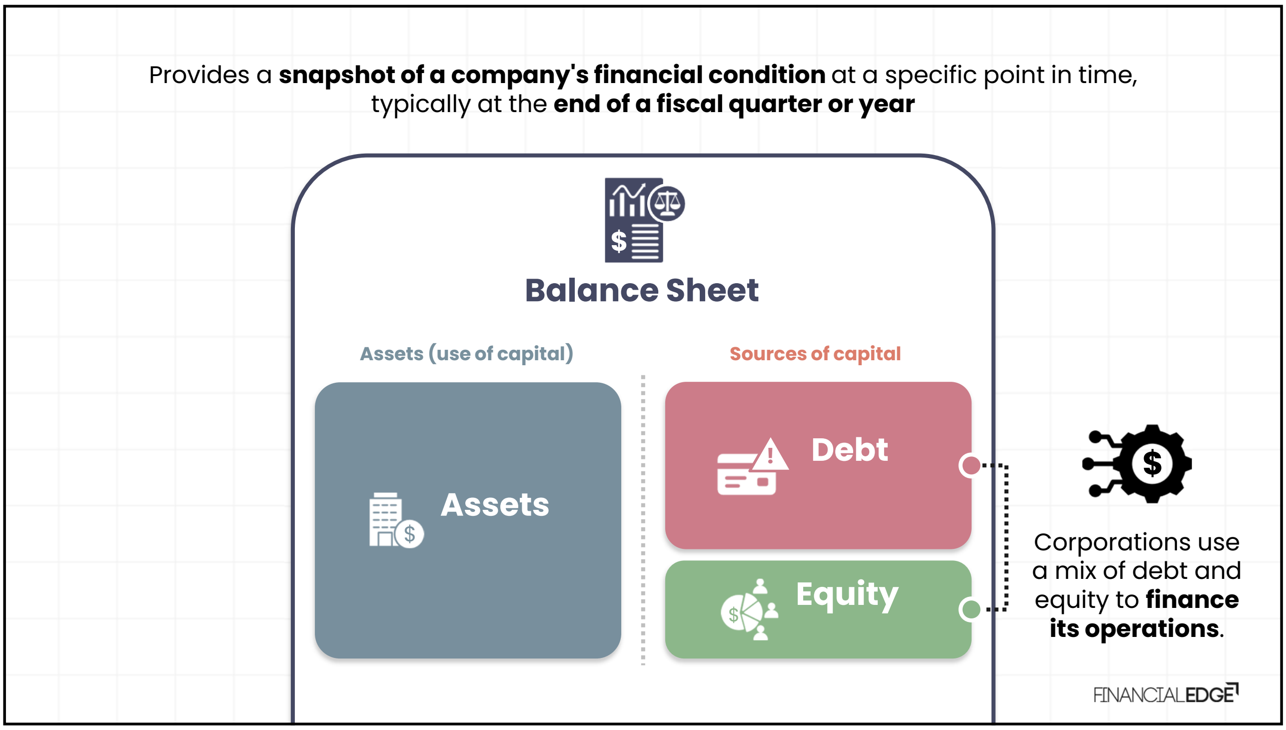
- **Borrowed money**
- **Paid back with interest**
- **Within a certain time frame**

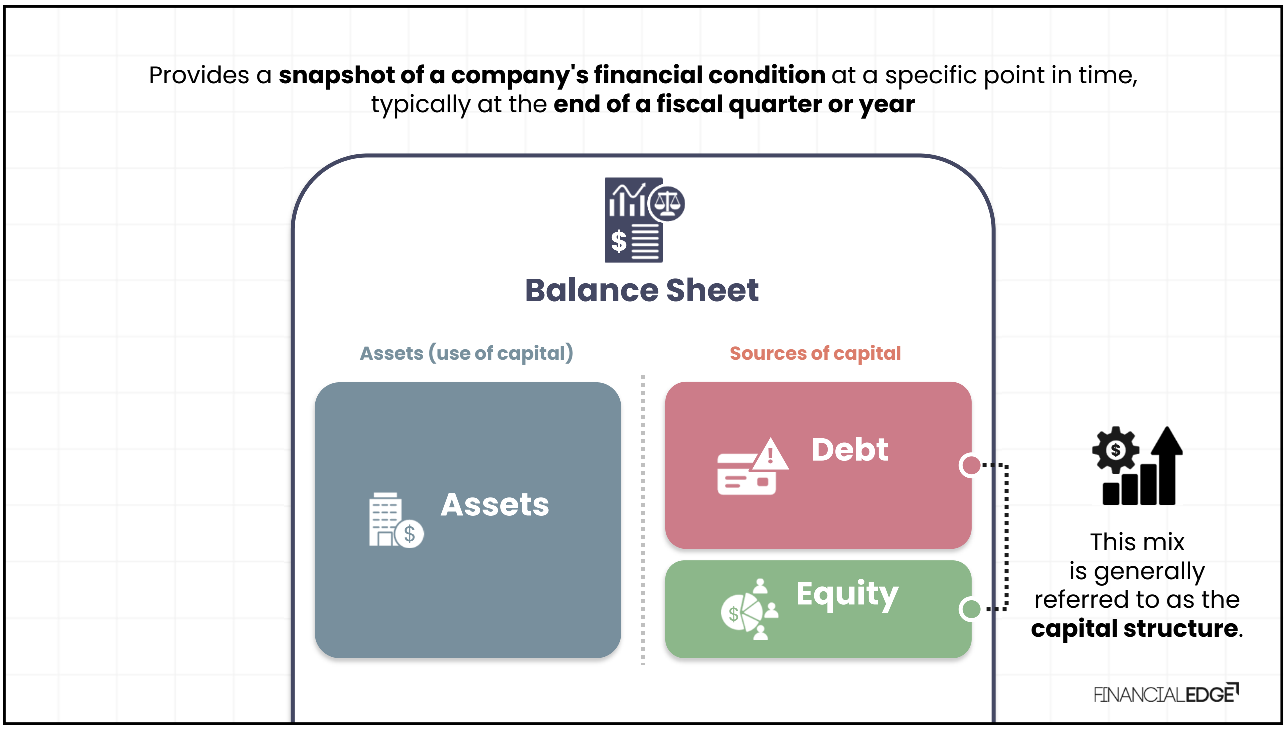

The two main types of financing that are available to companies are:
Debt
Equity
Company
10 year loan
5% Interest rate
Payments yearly
Repay this loan a decade after the money has been received
FINANCIALEDGE

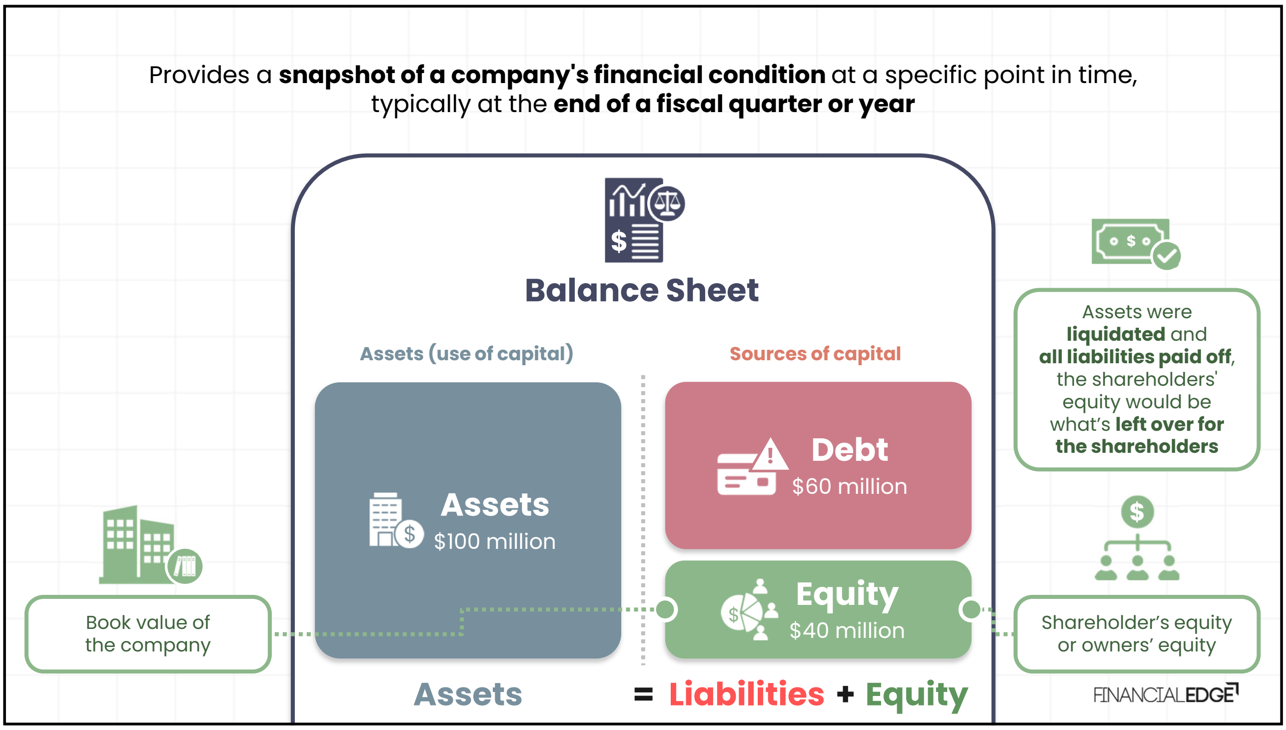

The two main types of financing that are available to companies are:
Debt
Equity
Ownership of the company
Selling a part of the company's ownership in exchange for capital
Permanent capital
Dividend payments are discretionary
Founders
Angel investors
Venture capitalists
Stock exchange
FINANCIALEDGE

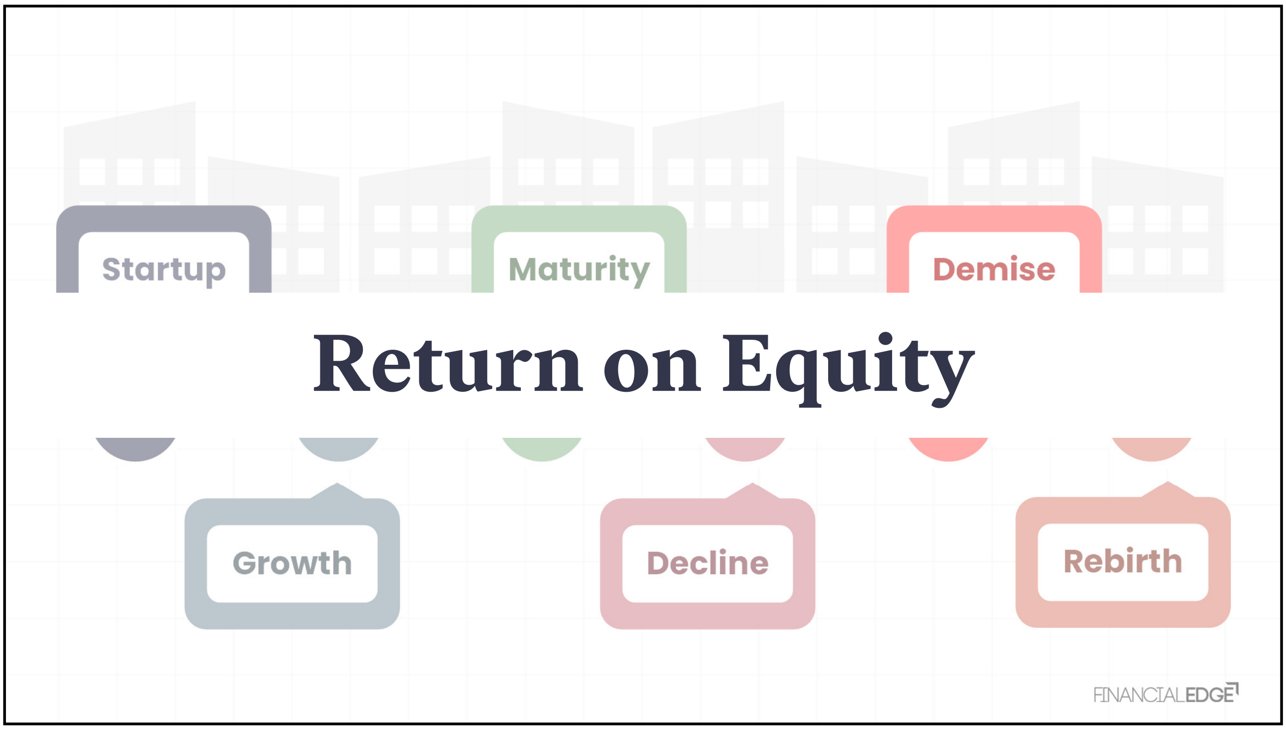

Balance Sheet and
Capital Structure
Growth
Decline
Rebirth
FINANCIALEDGE

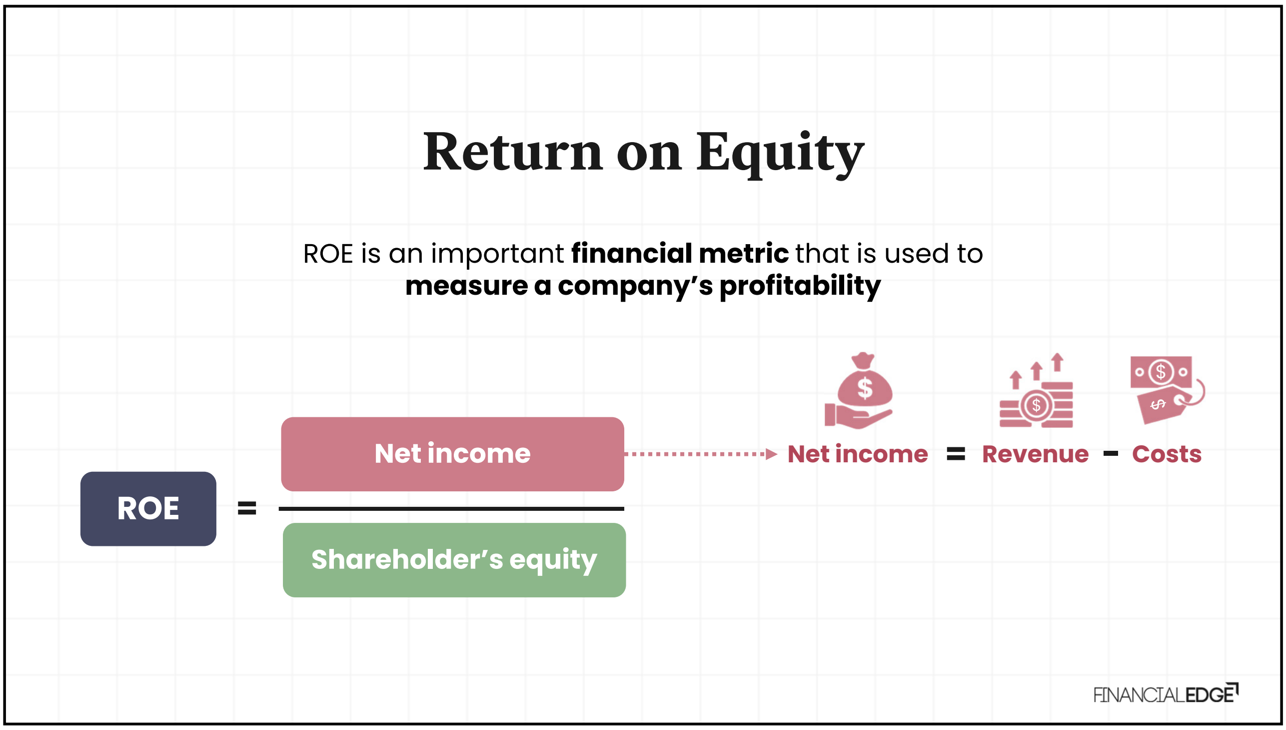

Provides a **snapshot of a company's financial condition** at a specific point in time, typically at the **end of a fiscal quarter or year**
Balance Sheet
Assets (use of capital)
Assets
Sources of capital
Liabilities and equities
Accounts payable
Pension liabilities
Debt
Bank loans
FINANCIALEDGE

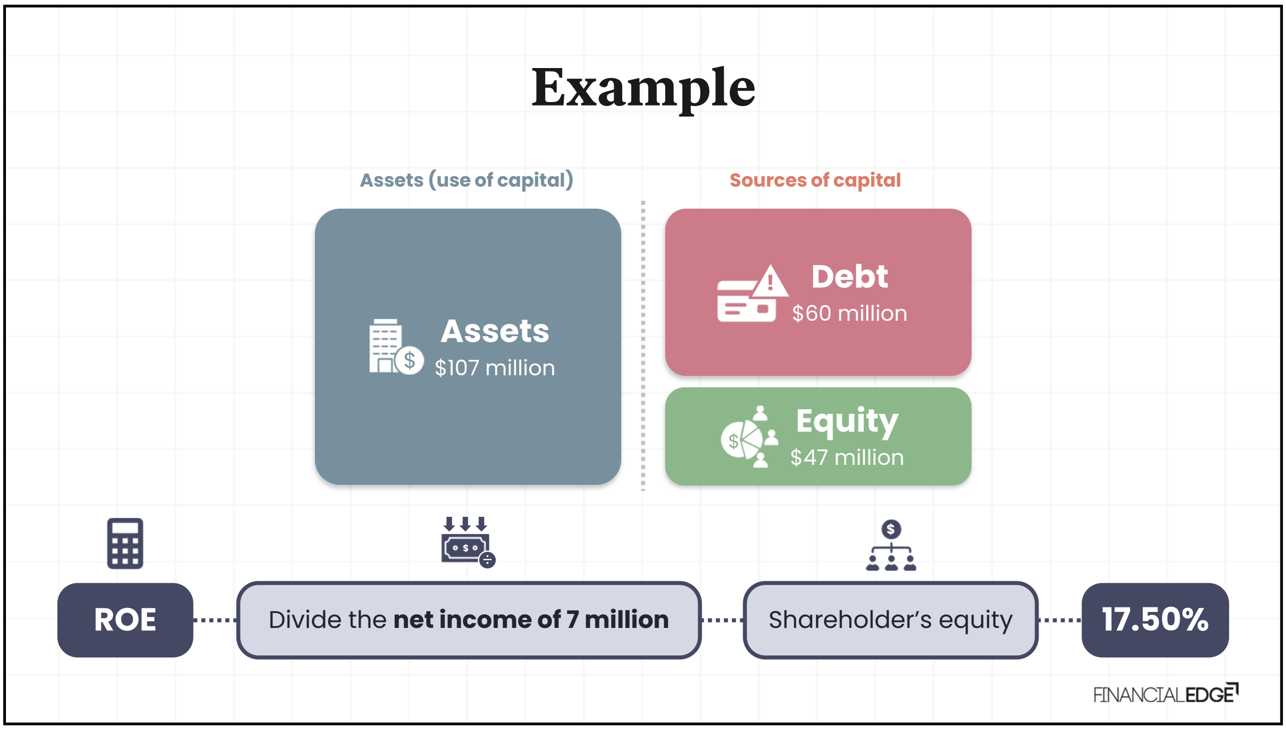

Provides a snapshot of a company's financial condition at a specific point in time, typically at the end of a fiscal quarter or year
Balance Sheet
Assets (use of capital)
Sources of capital
Assets
Debt
Equity
Corporations use a mix of debt and equity to finance its operations.
FINANCIALEDGE

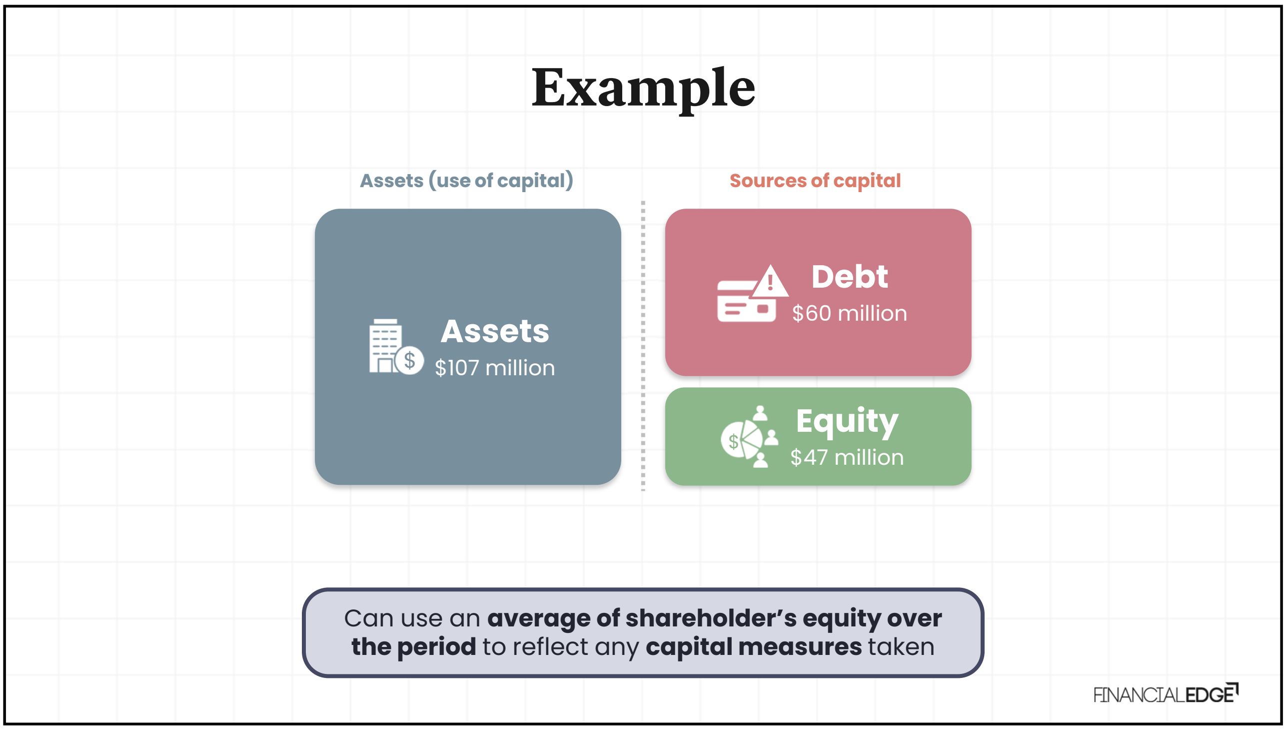

Provides a snapshot of a company's financial condition at a specific point in time, typically at the end of a fiscal quarter or year
Balance Sheet
Assets (use of capital)
Sources of capital
Assets
Debt
Equity
This mix is generally referred to as the capital structure.
FINANCIALEDGE

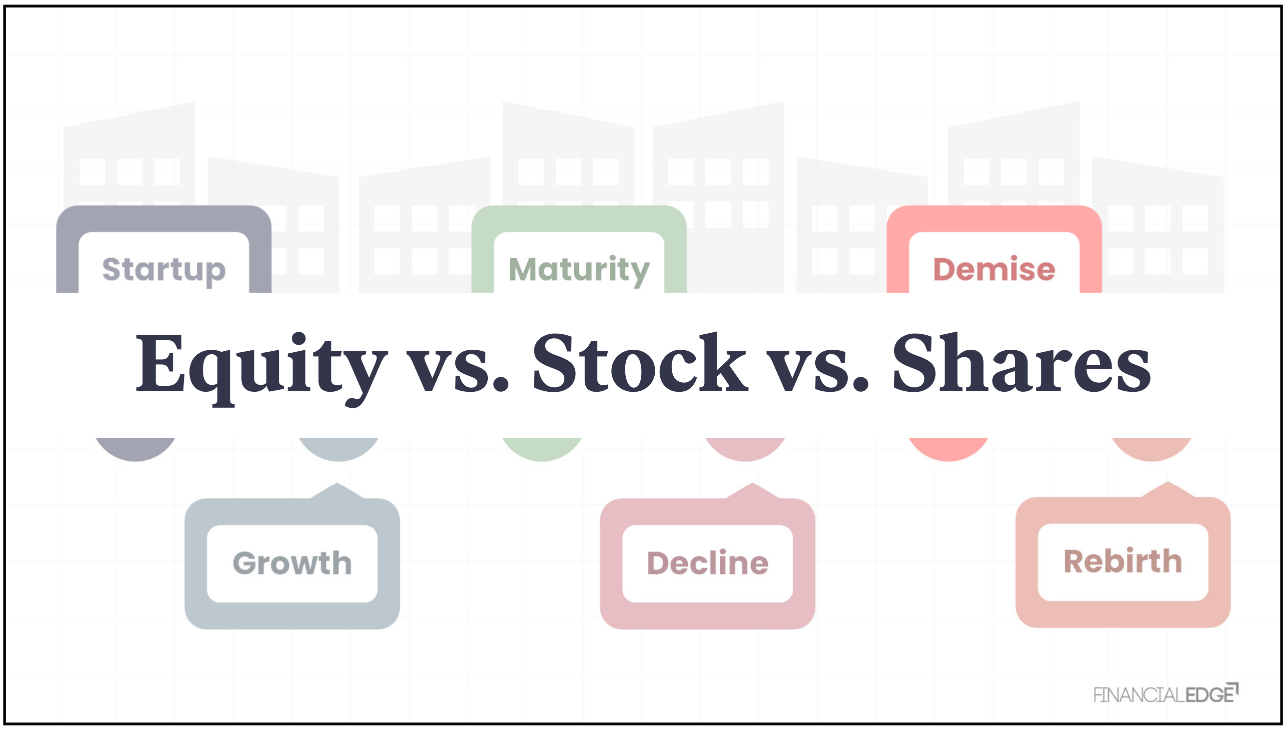

Provides a **snapshot of a company's financial condition** at a specific point in time, typically at the **end of a fiscal quarter or year**
Balance Sheet
Assets (use of capital)
Sources of capital
Assets
$100 million
Debt
$60 million
Equity
$40 million
Book value of the company
Assets were **liquidated** and **all liabilities paid off**, the shareholders' equity would be what's **left over for the shareholders**
Shareholder's equity or owners' equity
Assets = Liabilities + Equity
FINANCIALEDGE

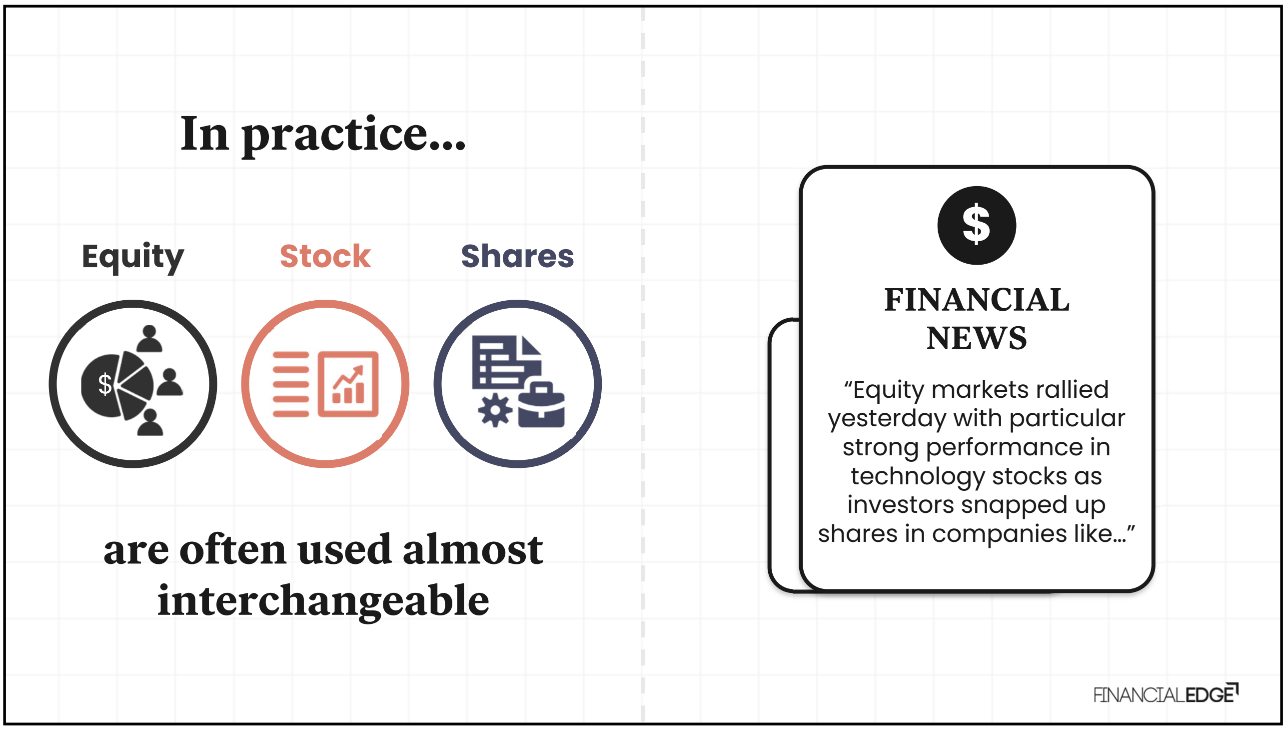

Startup
Maturity
Demise
Return on Equity
Growth
Decline
Rebirth
FINANCIALEDGE


Return on Equity
ROE is an important financial metric that is used to measure a company's profitability
ROE
=
Net income
Shareholder's equity
Net income = Revenue - Costs
FINANCIALEDGE


Example
Assets (use of capital)
Sources of capital
Assets
$107 million
Debt
$60 million
Equity
$47 million
ROE
Divide the net income of 7 million
Shareholder's equity
17.50%
FINANCIALEDGE

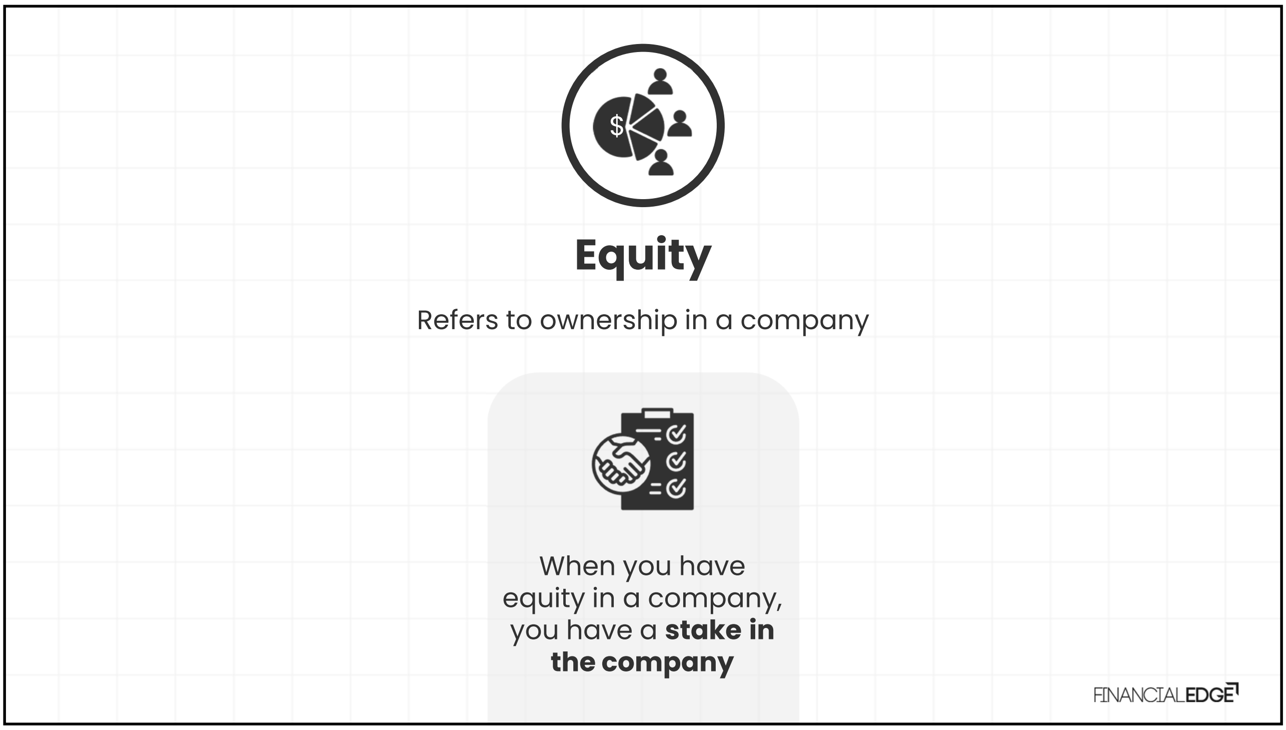

Example
Assets (use of capital)
Sources of capital
Assets
$107 million
Debt
$60 million
Equity
$47 million
Can use an **average of shareholder's equity over the period** to reflect any **capital measures** taken
FINANCIALEDGE


Startup
Maturity
Demise
Equity vs. Stock vs. Shares
Growth
Decline
Rebirth
FINANCIALEDGE


In practice...
Equity
Stock
Shares
are often used almost interchangeable
FINANCIAL NEWS
“Equity markets rallied yesterday with particular strong performance in technology stocks as investors snapped up shares in companies like...”
FINANCIALEDGE


Equity
Stock
Shares
FINANCIALEDGE

FINANCIALEDGE



Stock

Refers to ownership units or certificates that represent ownership in a corporation

Can be thought of as the **entire pool of ownership** in a company

A **subset of equity** and is often used when discussing ownership in **publicly traded companies**

FINANCIALEDGE

Equity	Stock	Shares

FINANCIALEDGE

Shares

The individual units or pieces that make up the stock of a company

When people **buy or sell shares**, they are dealing with the **individual units** of ownership

If a company has issued **1,000 shares** in total

Each share represents a **1/1,000th ownership stake** in the company

FINANCIALEDGE

Book Value Per Share

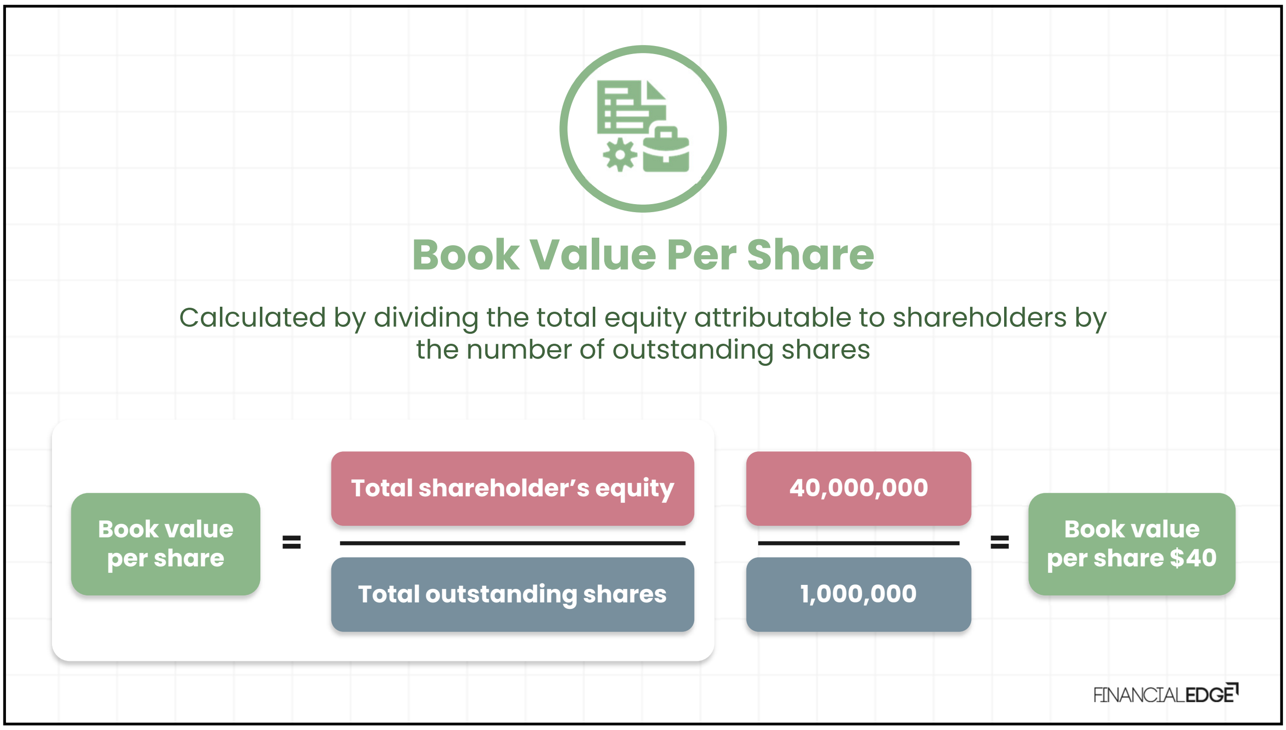
Calculated by dividing the total equity attributable to shareholders by the number of outstanding shares

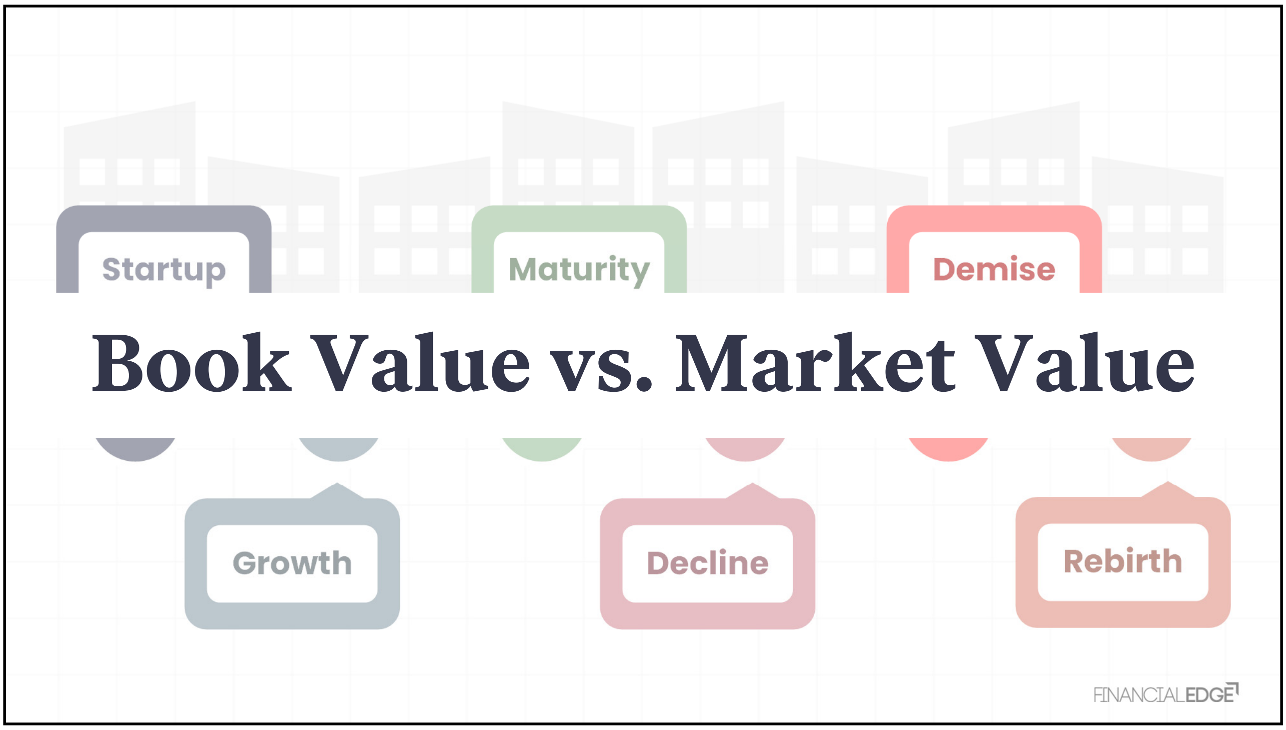
How much the **holder of one share should receive** if the company would be **unwound** in an orderly fashion

All the **assets** would be **sold** and **turned into cash**

All **debt repaid** and the remaining cash **equally distributed**

FINANCIALEDGE

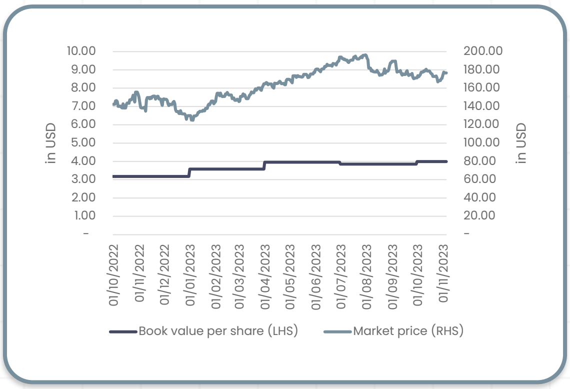

Book Value Per Share
Calculated by dividing the total equity attributable to shareholders by the number of outstanding shares
Book value per share
=
Total shareholder's equity
Total outstanding shares
40,000,000
1,000,000
=
Book value per share $40
FINANCIALEDGE


Startup
Maturity
Demise
Book Value vs. Market Value
Growth
Decline
Rebirth
FINANCIALEDGE

Market Price

The price at which a share can be bought or sold on the stock exchange

Apple book value vs. market price



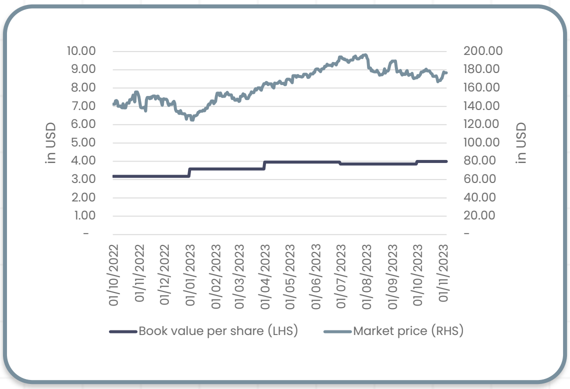
Apple price to book ratio

FINANCIALEDGE

Market Price

The price at which a share can be bought or sold on the stock exchange

Apple book value vs. market price



Last day:

Book value: $4

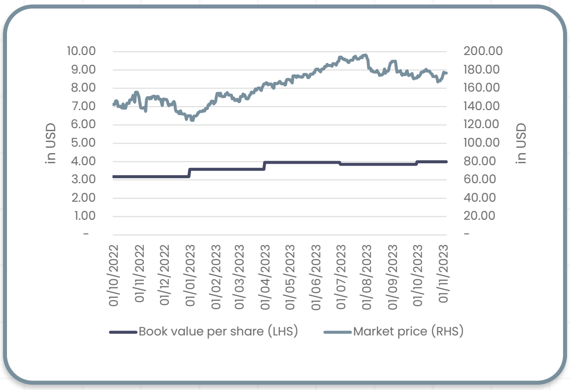
Market price: $176.65 per share

FINANCIALEDGE

Market Price

The price at which a share can be bought or sold on the stock exchange

Apple book value vs. market price



Apple price to book ratio

FINANCIALEDGE

Market Price

The price at which a share can be bought or sold on the stock exchange

Price to book ratio:
Divide the **share's current price** by its **book value per share**

Price to book ratio: 35x to 50x

Last day: Just under 45x

? Why is there a difference between the book value and the market value?

Apple price to book ratio

FINANCIALEDGE

1

Future Growth Expectations

Balance sheet is **backward looking** while markets are **forward looking**

If the market **expects future growth** and profitability this will be reflected in the **share price** but not in the **balance sheet values**

FINANCIALEDGE

1 Future Growth Expectations

2

Intangible Assets

The book value **might not fully account** for intangible assets

Brand reputation

Intellectual property

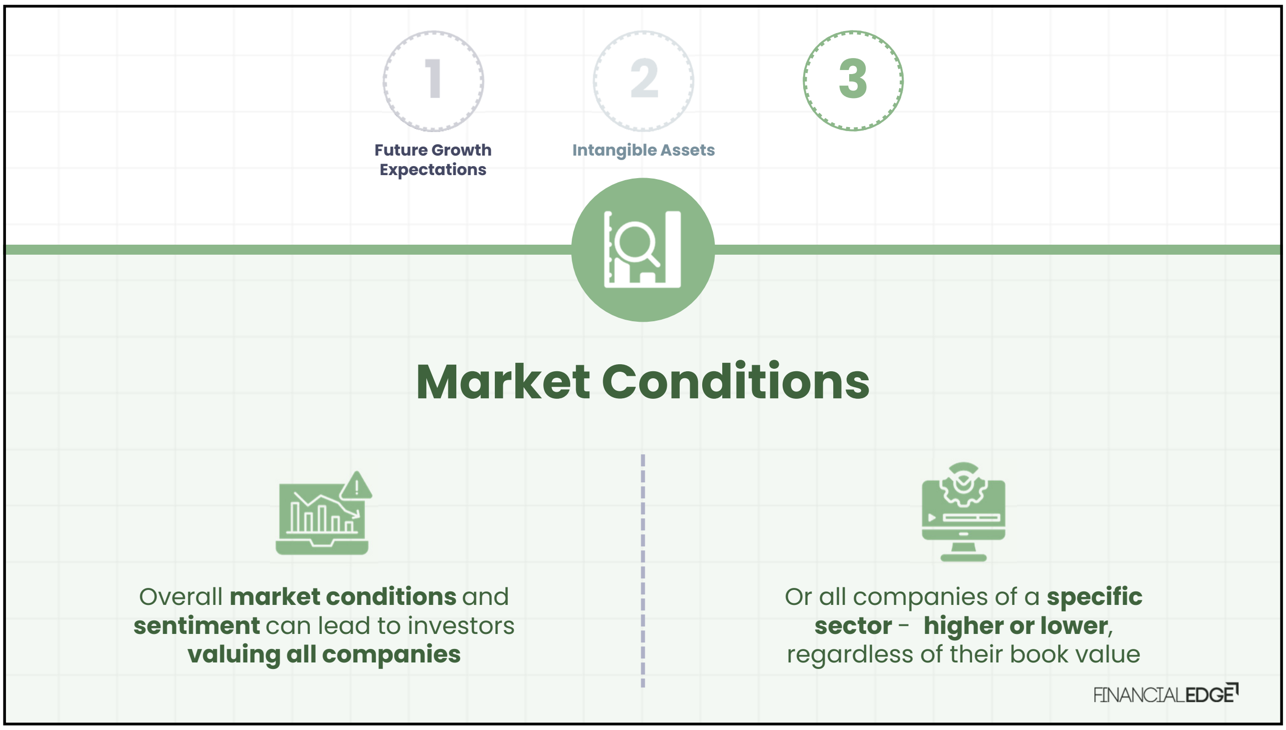
Customer loyalty

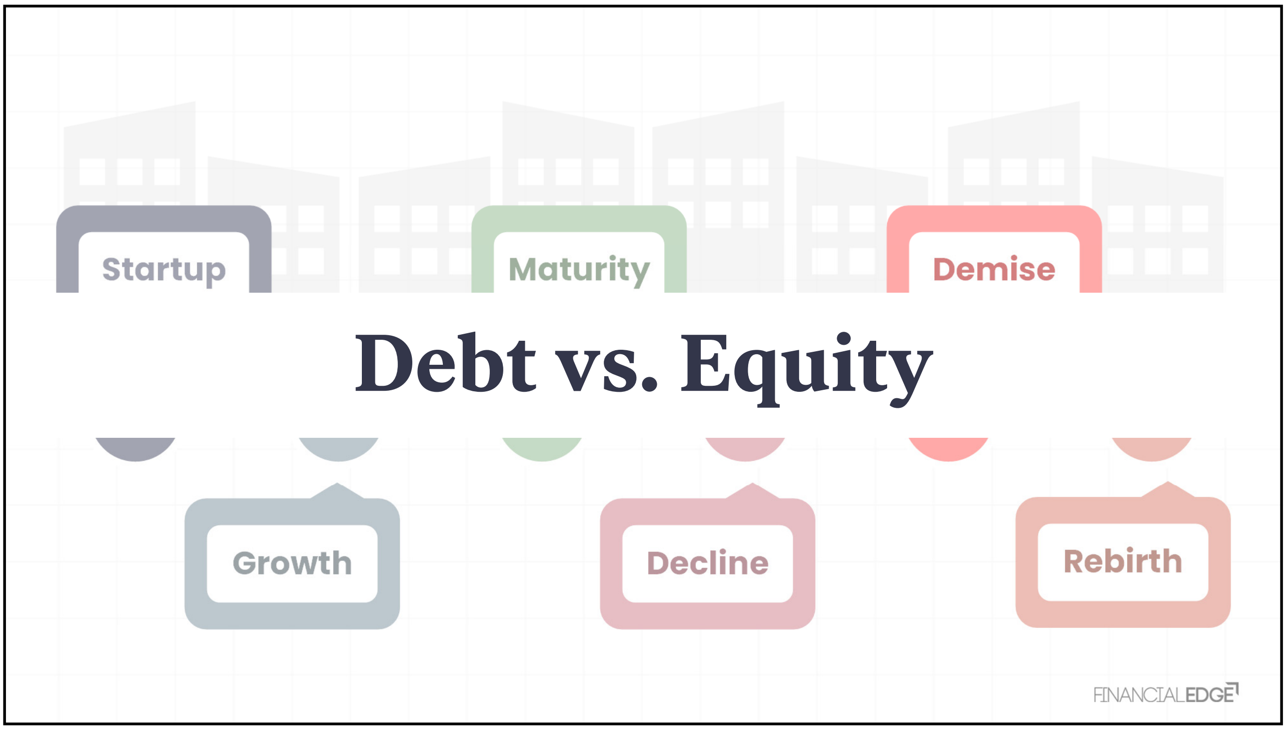
Generate revenue

Have **monetary value**

Factored into **market price**

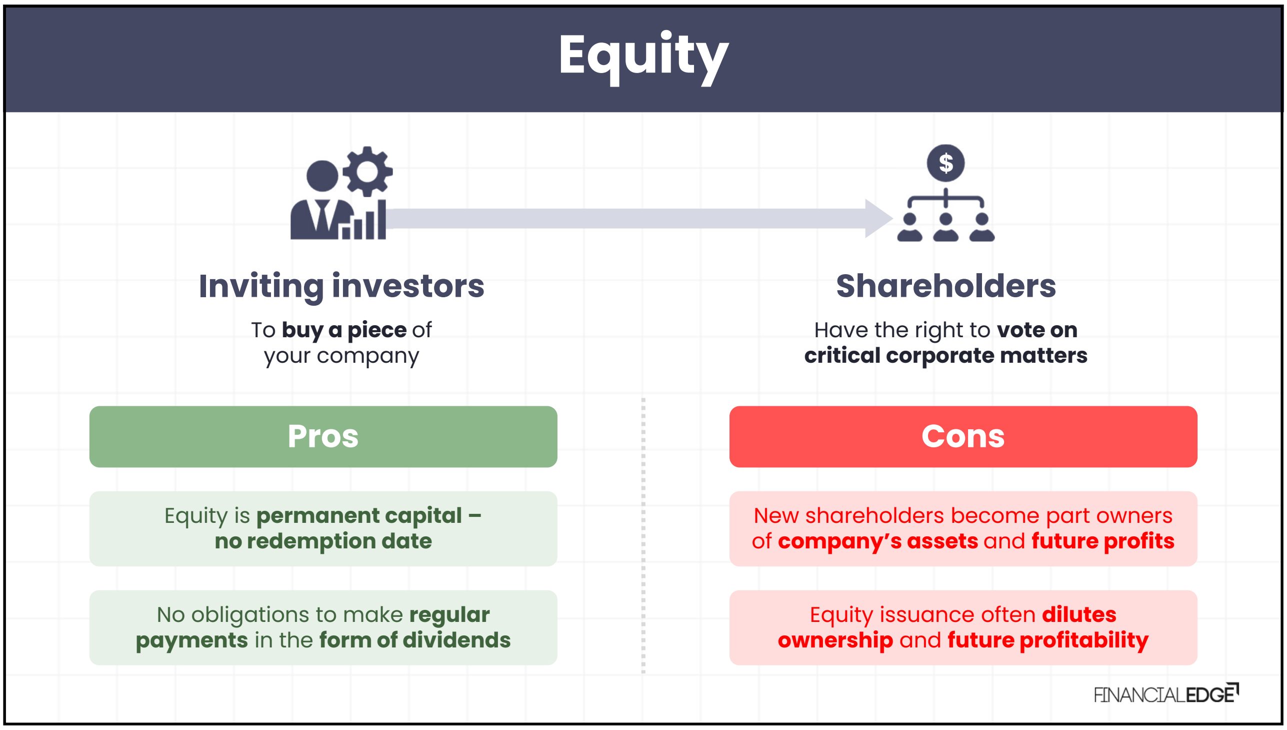
FINANCIALEDGE

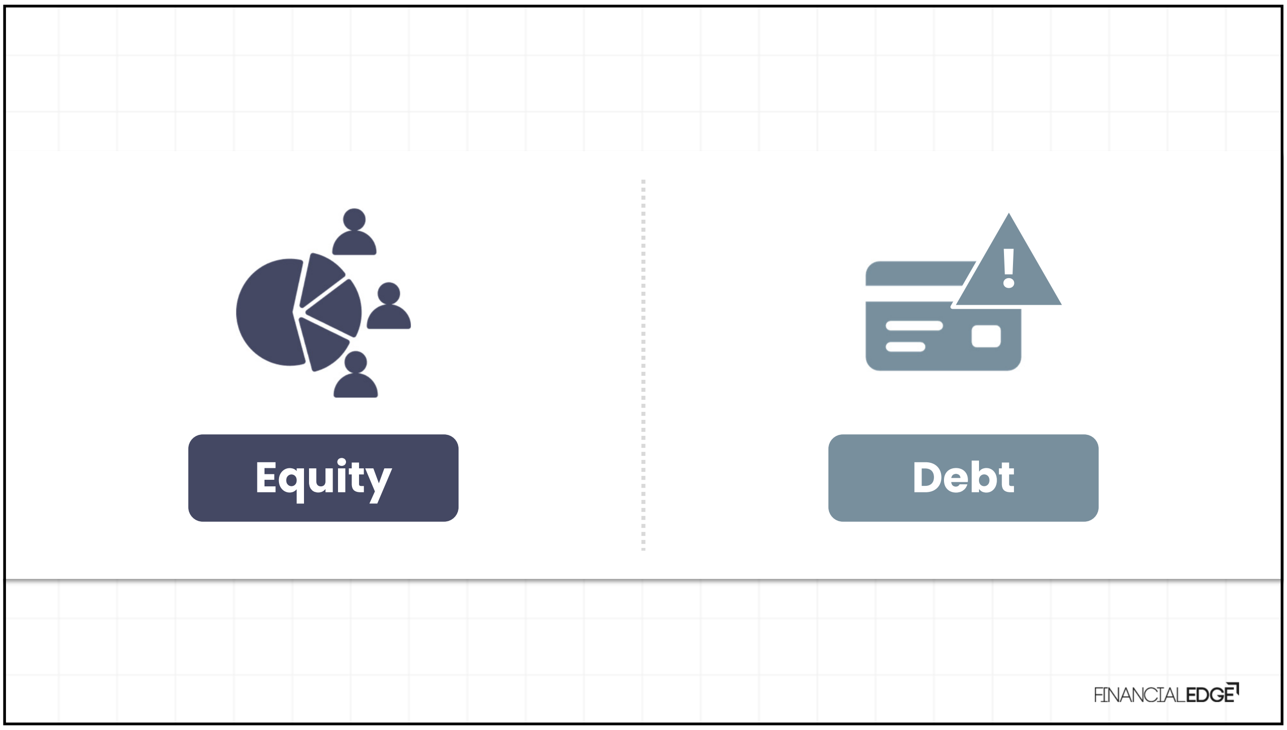

1
Future Growth Expectations
2
Intangible Assets
3
Market Conditions
Overall market conditions and sentiment can lead to investors valuing all companies
Or all companies of a specific sector - higher or lower, regardless of their book value
FINANCIALEDGE


Startup
Maturity
Demise
Debt vs. Equity
Growth
Decline
Rebirth
FINANCIALEDGE

Pros and Cons from the Issuer's Perspective

The company looking to raise financing


Equity
Inviting investors
To **buy a piece** of your company
Shareholders
Have the right to **vote on critical corporate matters**
Pros
Equity is **permanent capital – no redemption date**
No obligations to make **regular payments** in the **form of dividends**
Cons
New shareholders become part owners of **company's assets** and **future profits**
Equity issuance often **dilutes ownership** and **future profitability**
FINANCIALEDGE


Equity
Debt
FINANCIALEDGE

Debt

Issuing debt

Legal obligation to **repay the borrowed amount** with **interest**

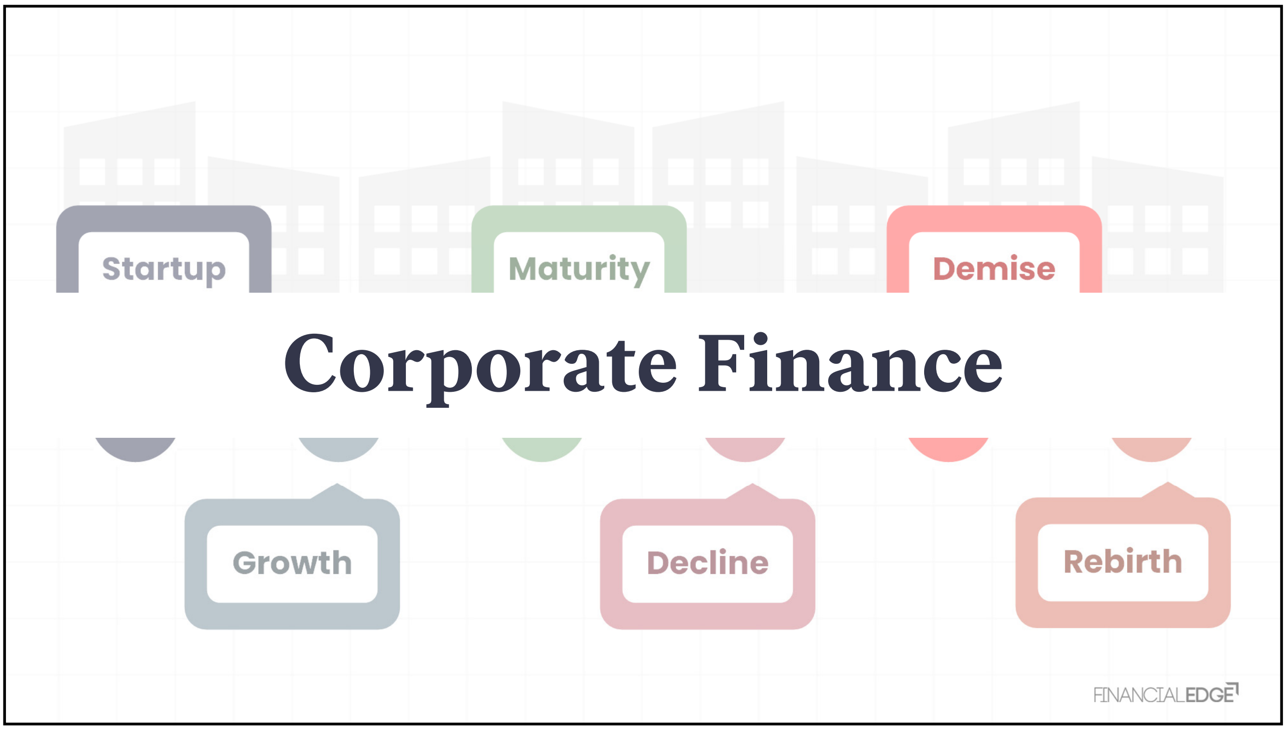
Pros	Cons
Lenders **do not receive ownership**	In the event of **liquidation, debt holders** are **repaid before equity investors**
Interest payments are **tax-deductible**	

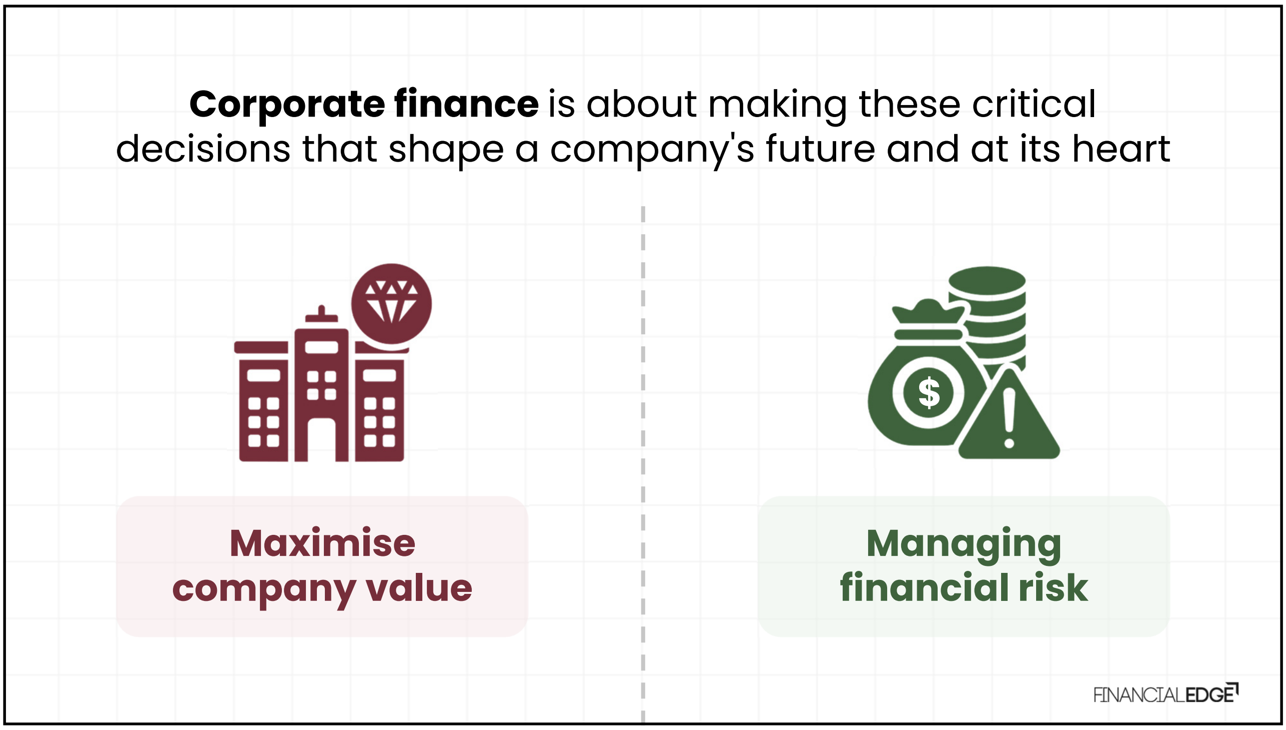
FINANCIALEDGE

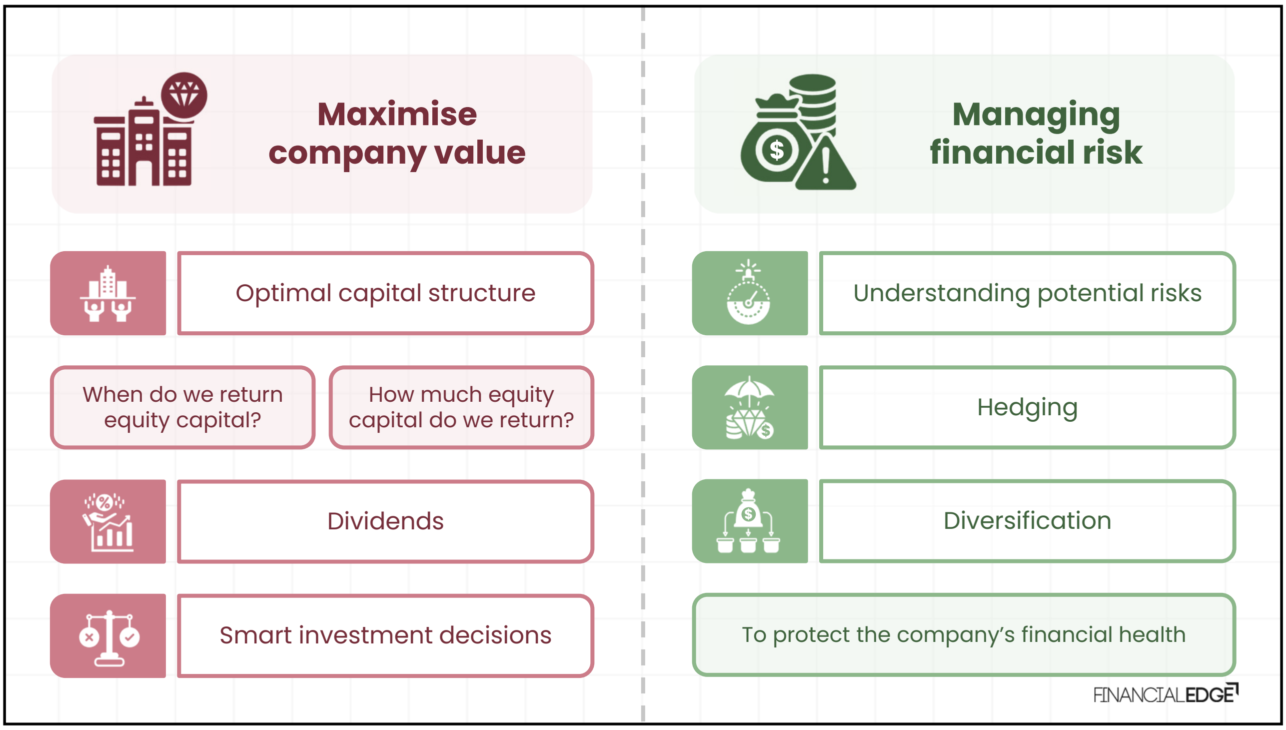
Debt VS Equity

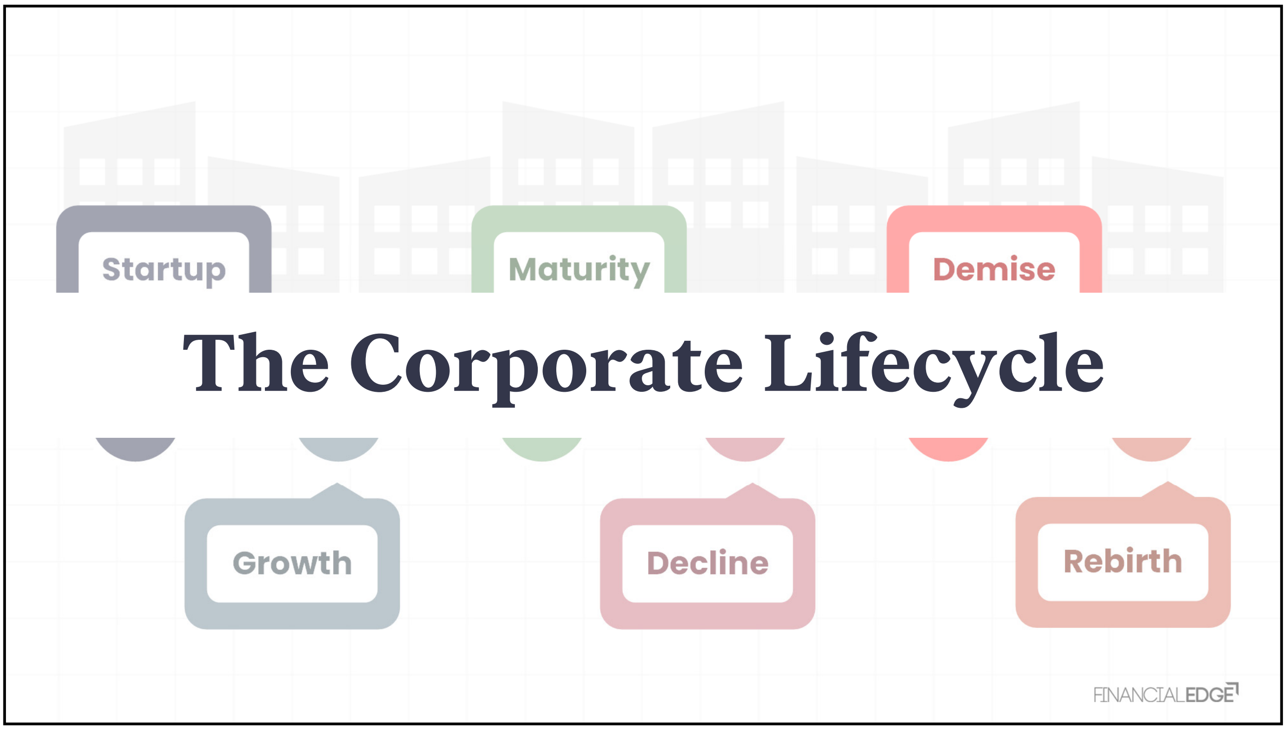
Debt	Equity
Allows for **retaining full control** while potentially **lowering taxable income**	**No payment obligations**
Requires adequate **revenue to cover interest** and **principal payments**	**Diluted ownership**
	Equity investors often **expect higher returns than debt holders**

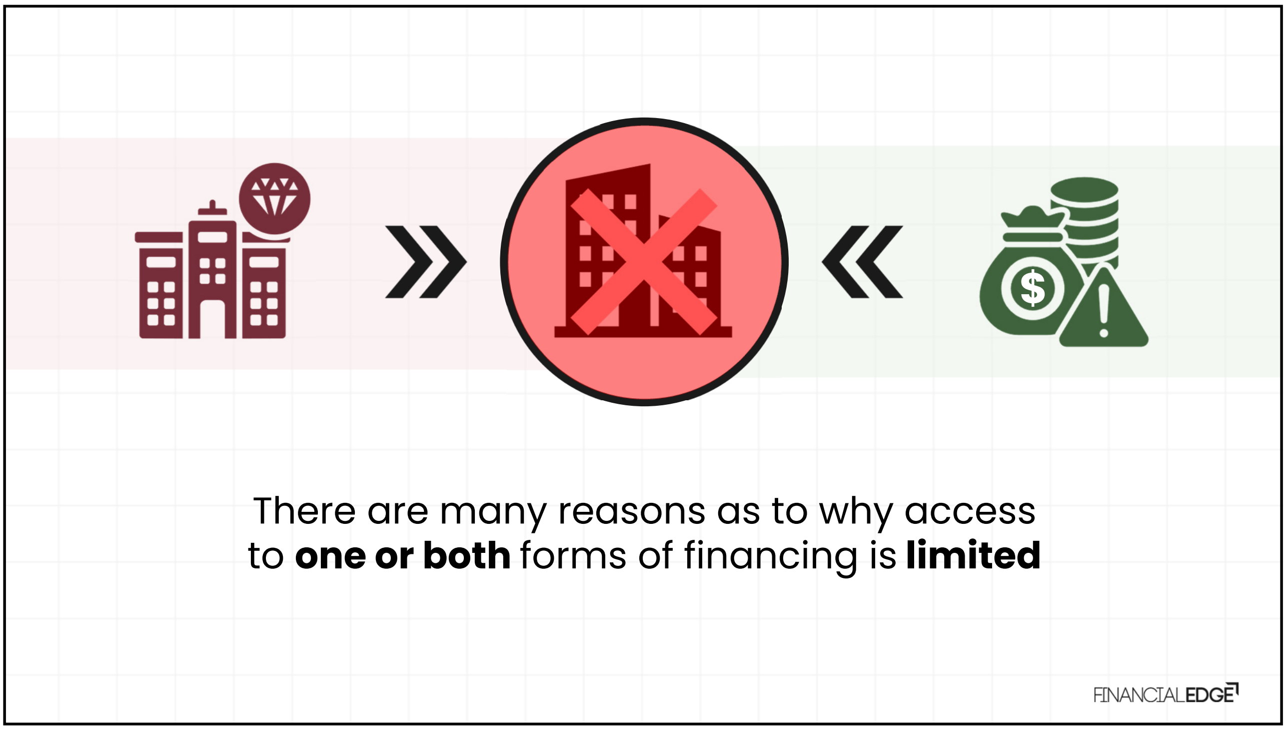
FINANCIALEDGE

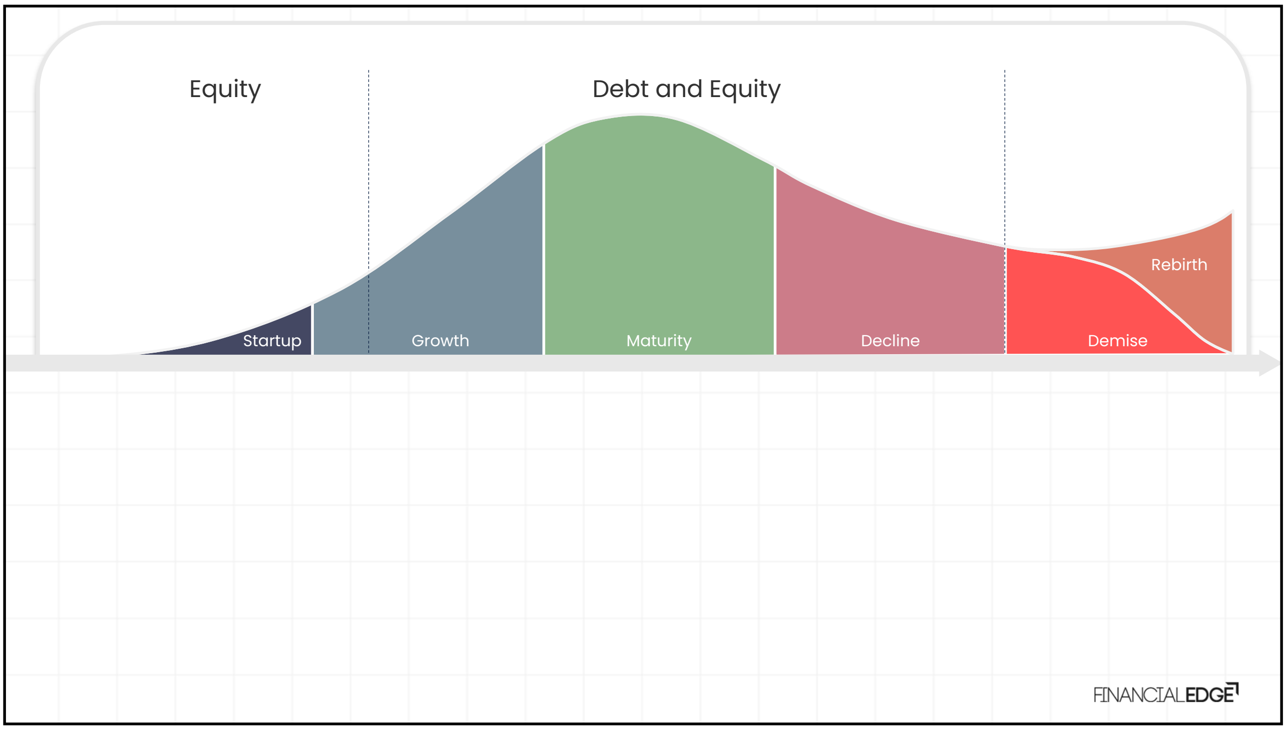

Startup
Maturity
Demise
Corporate Finance
Growth
Decline
Rebirth
FINANCIALEDGE

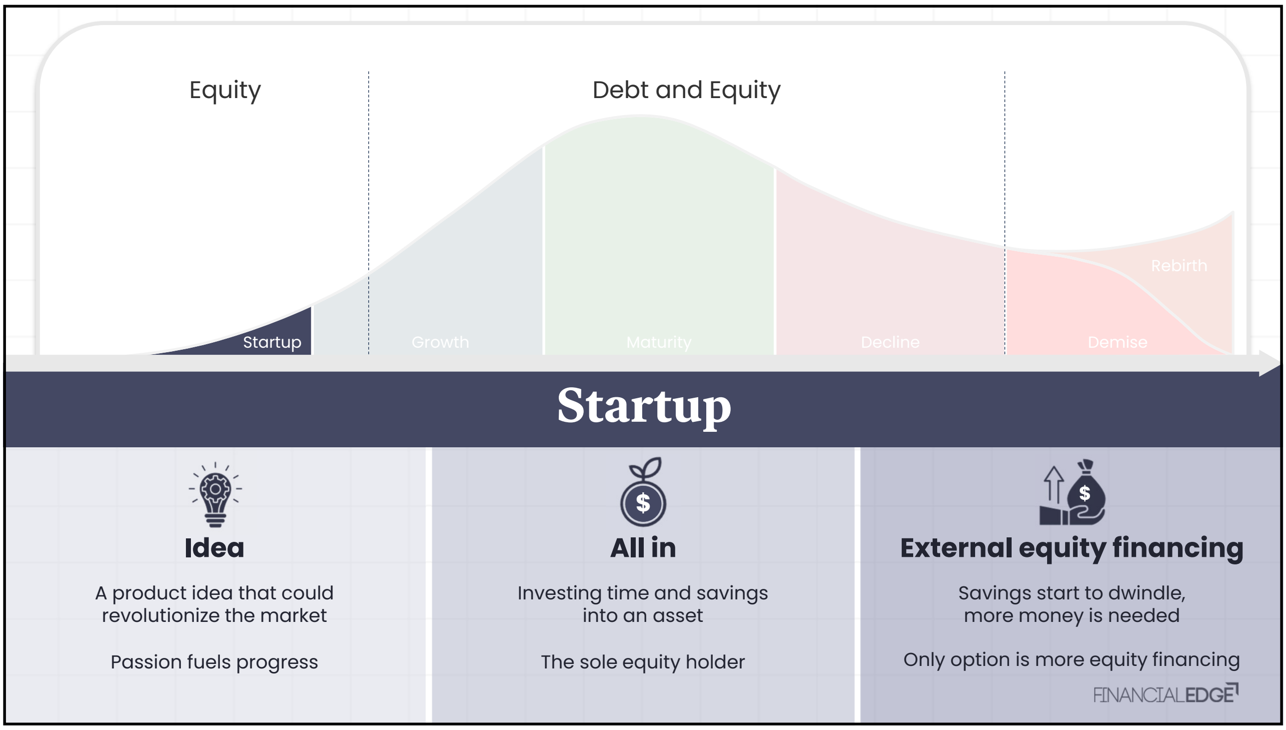

Corporate finance is about making these critical decisions that shape a company's future and at its heart
Maximise company value
Managing financial risk
FINANCIALEDGE

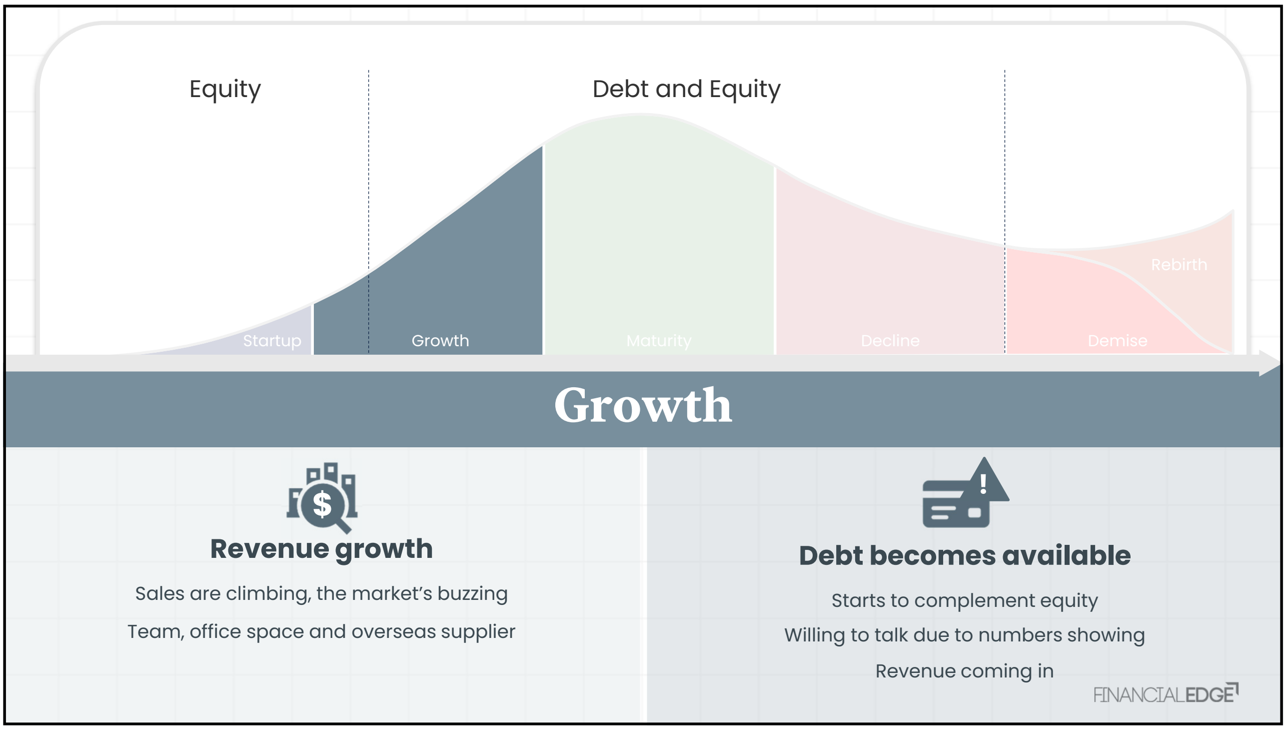

Maximise company value
Optimal capital structure
When do we return equity capital?
How much equity capital do we return?
Dividends
Smart investment decisions
Managing financial risk
Understanding potential risks
Hedging
Diversification
To protect the company's financial health
FINANCIALEDGE

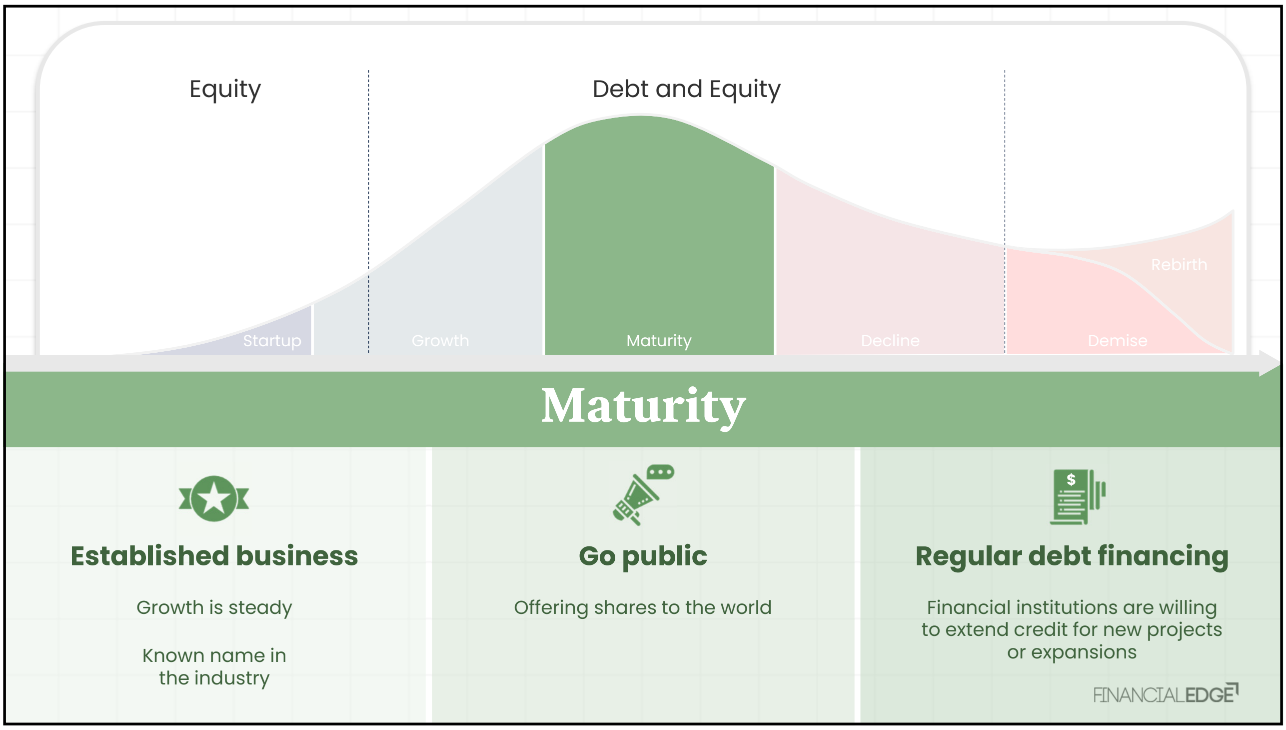

Startup
Maturity
Demise
The Corporate Lifecycle
Growth
Decline
Rebirth
FINANCIALEDGE

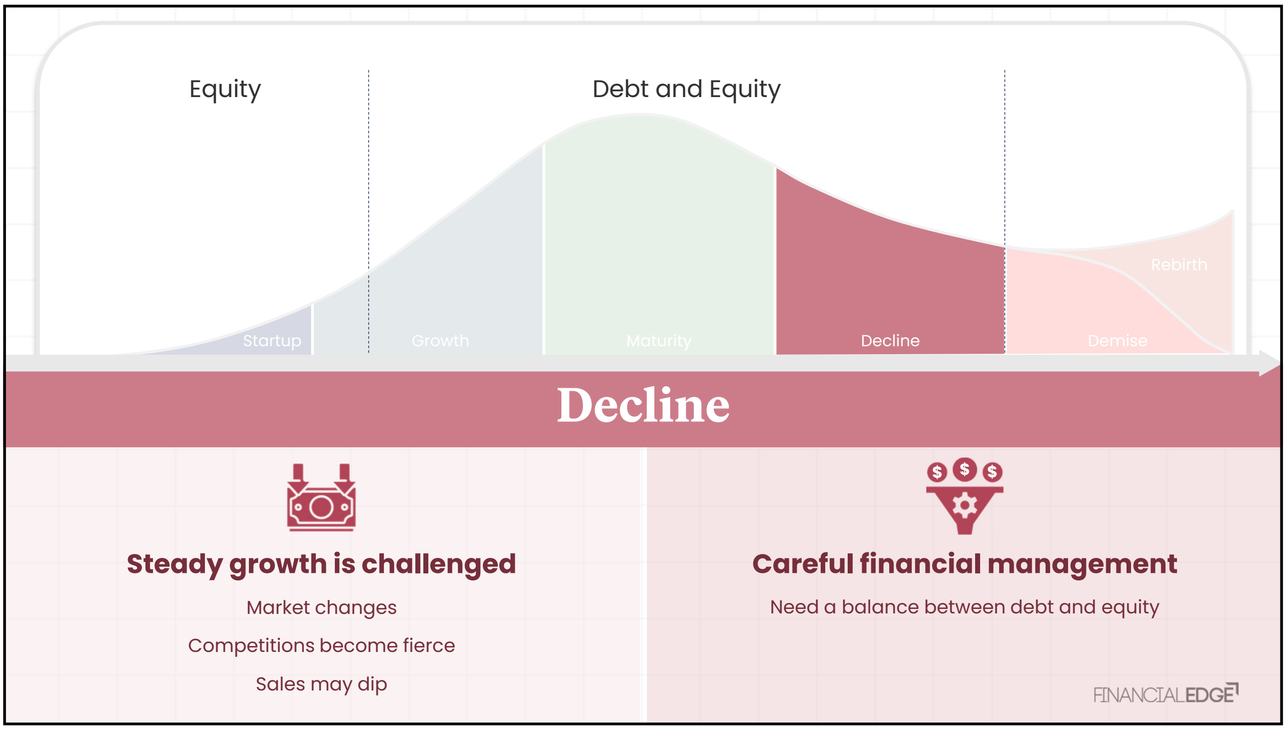

There are many reasons as to why access to **one or both** forms of financing is **limited**
FINANCIALEDGE

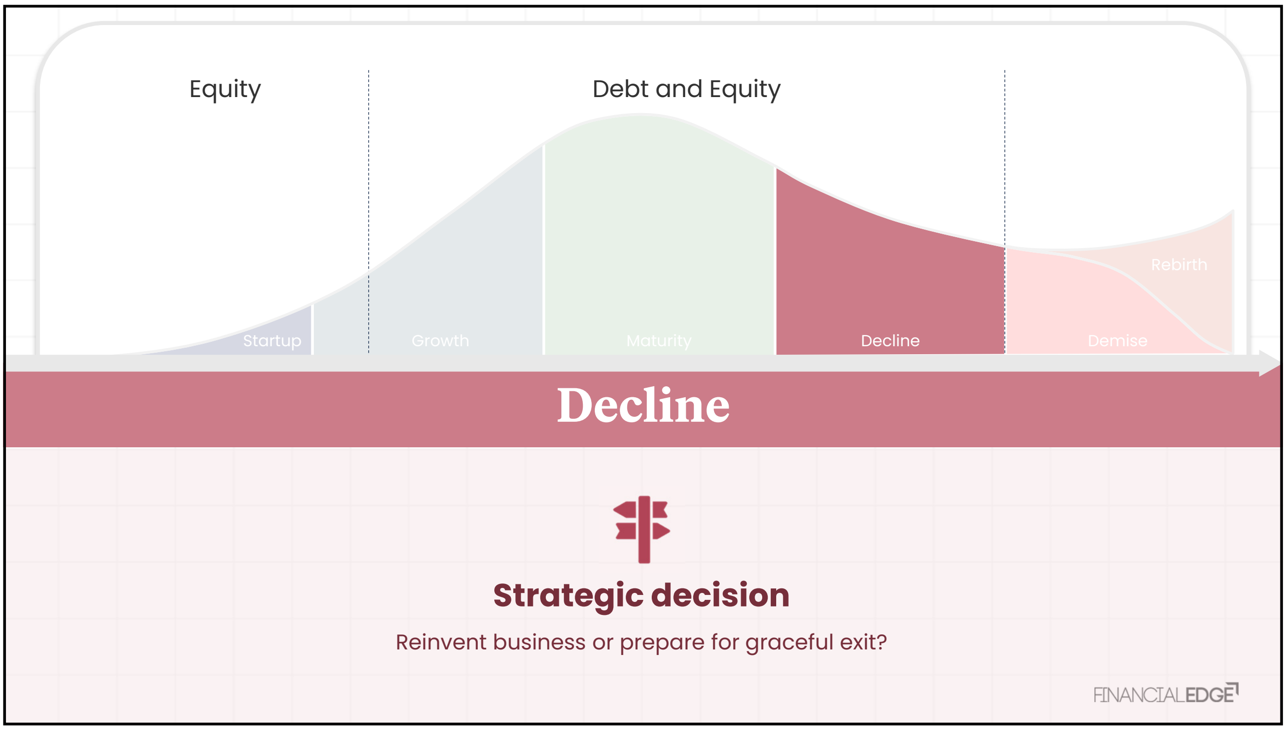

Equity
Debt and Equity
Startup
Growth
Maturity
Decline
Rebirth
Demise
FINANCIALEDGE

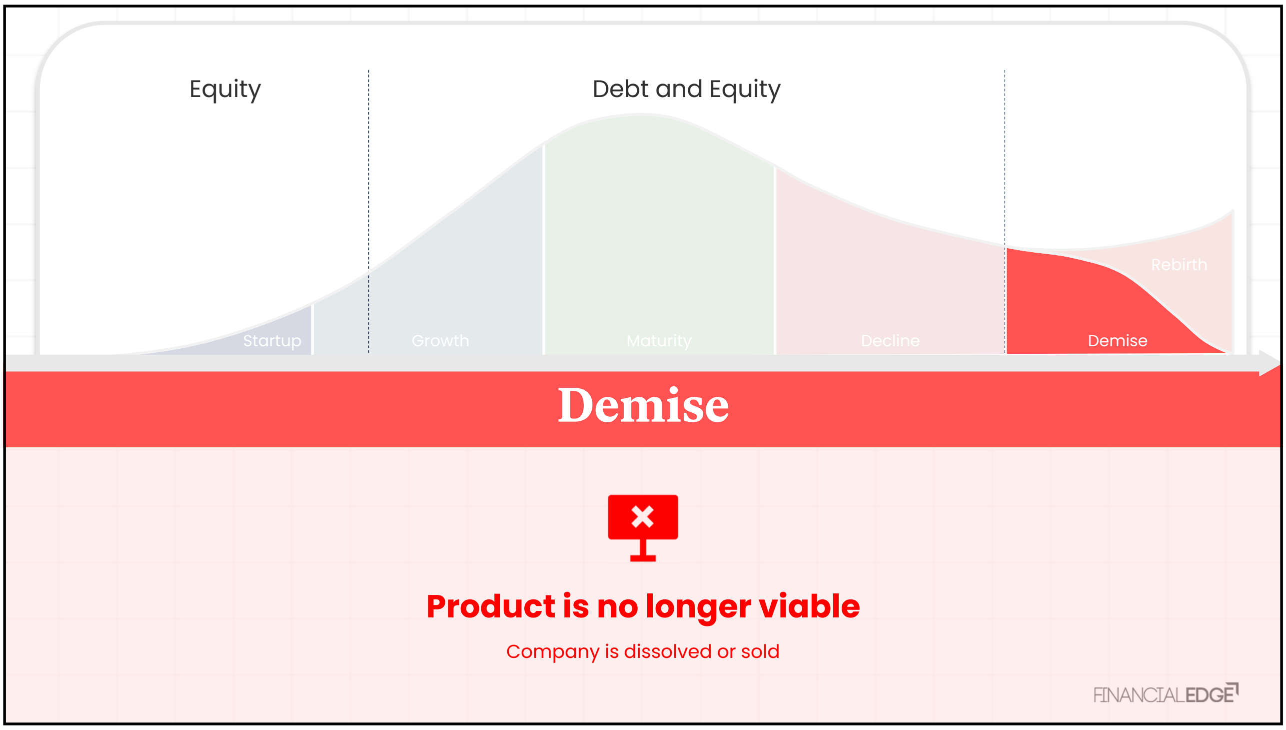

Equity
Debt and Equity
Startup
Growth
Maturity
Decline
Demise
Rebirth
Startup
Idea
A product idea that could revolutionize the market
Passion fuels progress
All in
Investing time and savings into an asset
The sole equity holder
External equity financing
Savings start to dwindle, more money is needed
Only option is more equity financing
FINANCIALEDGE

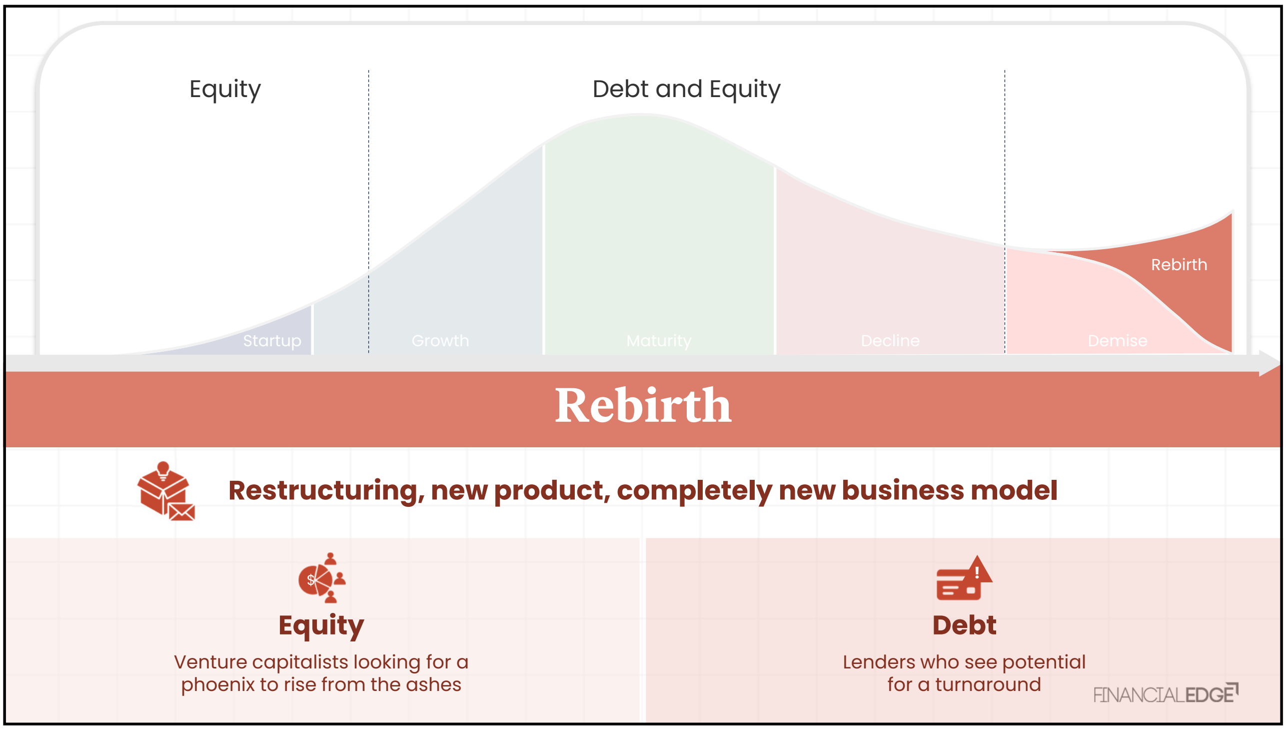

Equity
Debt and Equity
Startup
Growth
Maturity
Decline
Demise
Rebirth
Growth
Revenue growth
Sales are climbing, the market's buzzing
Team, office space and overseas supplier
Debt becomes available
Starts to complement equity
Willing to talk due to numbers showing
Revenue coming in
FINANCIALEDGE

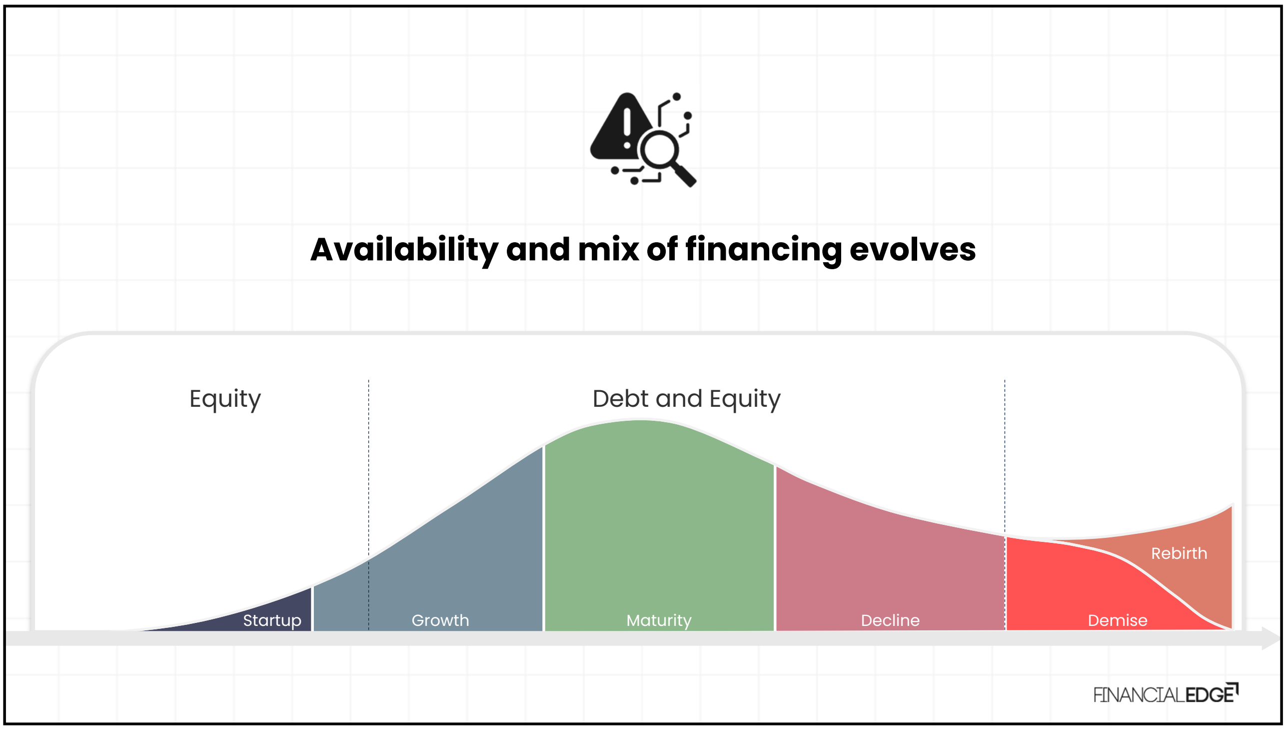

Equity
Debt and Equity
Startup
Growth
Maturity
Decline
Demise
Rebirth
Maturity
Established business
Growth is steady
Known name in the industry
Go public
Offering shares to the world
Regular debt financing
Financial institutions are willing to extend credit for new projects or expansions
FINANCIALEDGE

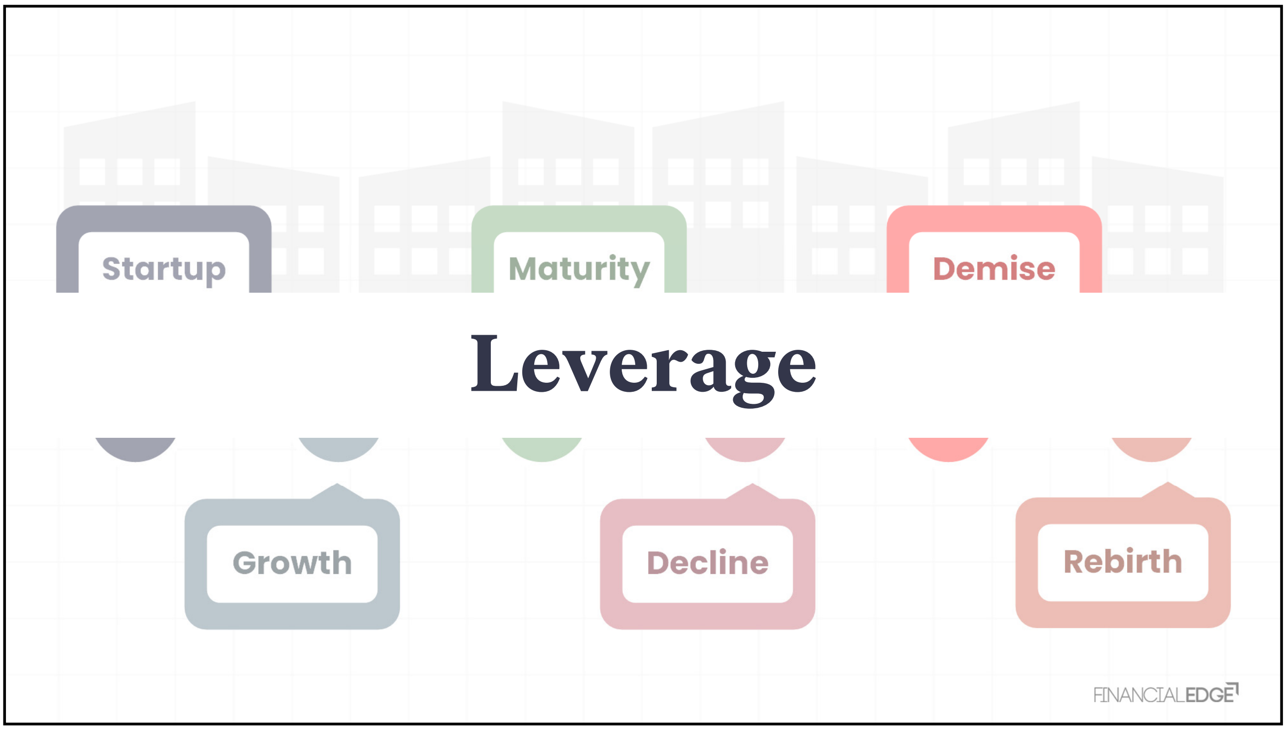

Equity
Debt and Equity
Startup
Growth
Maturity
Decline
Demise
Rebirth
Decline
Steady growth is challenged
Market changes
Competitions become fierce
Sales may dip
Careful financial management
Need a balance between debt and equity
FINANCIALEDGE

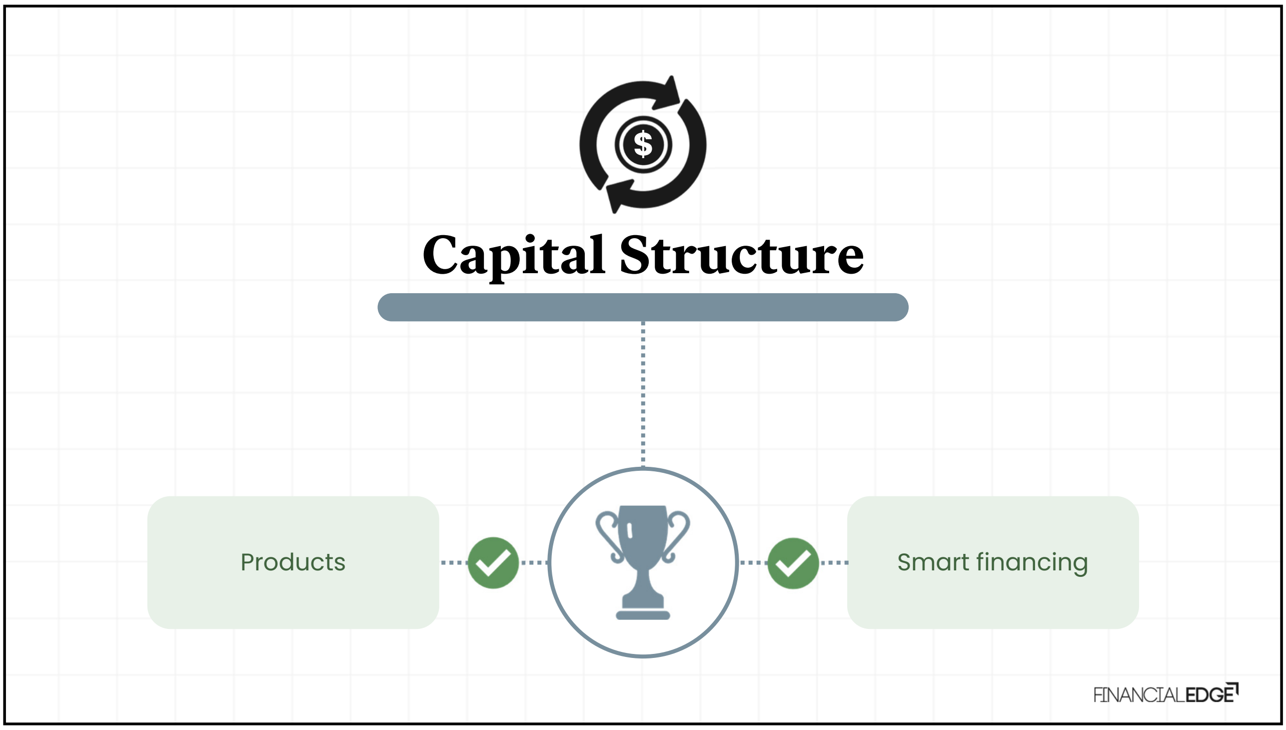

Equity
Debt and Equity
Startup
Growth
Maturity
Decline
Rebirth
Demise
Decline
Strategic decision
Reinvent business or prepare for graceful exit?
FINANCIALEDGE


Equity
Debt and Equity
Startup
Growth
Maturity
Decline
Rebirth
Demise
Demise
Product is no longer viable
Company is dissolved or sold
FINANCIALEDGE


Equity
Debt and Equity
Rebirth
Startup
Growth
Maturity
Decline
Demise
Rebirth
Restructuring, new product, completely new business model
Equity
Venture capitalists looking for a phoenix to rise from the ashes
Debt
Lenders who see potential for a turnaround
FINANCIALEDGE


Availability and mix of financing evolves
Equity
Debt and Equity
Rebirth
Startup
Growth
Maturity
Decline
Demise
FINANCIALEDGE


Startup
Maturity
Demise
Leverage
Growth
Decline
Rebirth
FINANCIALEDGE


Capital Structure
Products
Smart financing
FINANCIALEDGE

Leverage is using **borrowed money**, or **debt**, to amplify the **potential returns** of an investment

Companies use debt to fuel growth…

…betting that returns will outweigh the cost of borrowing

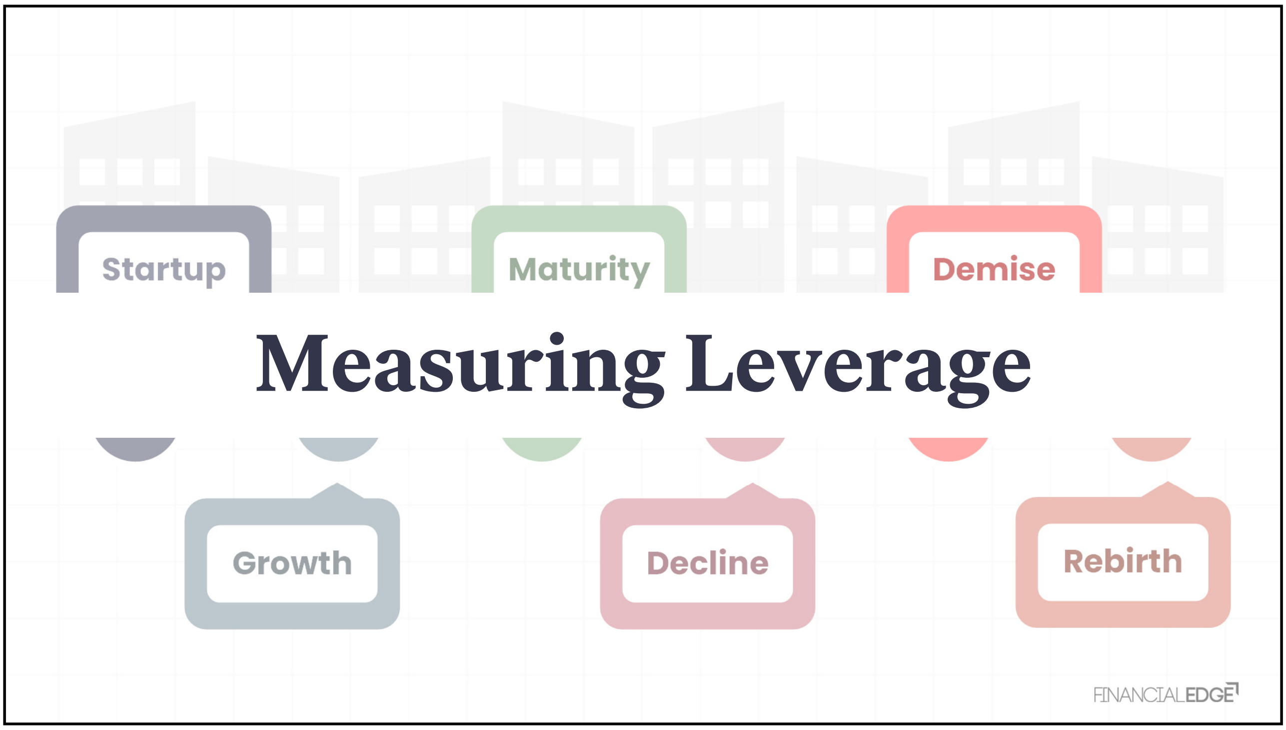
FINANCIALEDGE

It's a Balancing Act

Too little leverage = miss out on growth

FINANCIALEDGE


It's a Balancing Act
Too much leverage = can crush if things go south
FINANCIALEDGE


Startup
Maturity
Demise
Measuring Leverage
Growth
Decline
Rebirth
FINANCIALEDGE

How Do We Measure a Company's Leverage?

$$\text{Debt – equity ratio} = \frac{\text{Total debt of the company}}{\text{Shareholder's equity}}$$

This ratio tells us how much a **company** is **relying on:**

Debt to finance its assets

vs

Its **own funds**

FINANCIALEDGE

At the **maturity stage**, a company might be eyeing debt to **finance a new venture**

Debt is often cheaper than issuing new equity

Debt

Borrow more

Increases leverage

Equity

Sell additional shares

Decreases leverage

FINANCIALEDGE

What is Considered a "Good" Debt to Equity Ratio?

Industry

Economic Conditions

Individual Company Circumstances

FINANCIALEDGE

"Good" Debt-Equity Ratio Examples

Industry Benchmark

Different **industries** have different **average D/E ratios**

Capital-intensive industries like **utilities** or **telecommunications** might have **higher ratios**

Tech companies might have **lower ratios** as they require **less capital**

Growth Prospects

Companies with **high growth prospects** have **higher D/E ratio**

Take on **more debt** to fuel their **growth**

Expecting to **pay it back** with future earnings

Interest Rates

When rates are **low**, companies might **increase their debt** because it is cheaper to borrow

Could lead to a **higher D/E ratio**

FINANCIALEDGE

"Good" Debt-Equity Ratio Examples

Economic Conditions

During **economic downturns**, companies might have to **reduce debt** to lower their **risk**

Improving their **D/E ratio**

Company Age

Younger companies might have **higher D/E ratios** as they **borrow to grow**

Mature companies might have **lower ratios** as they've had time to **accumulate earnings** and **pay down debt**

FINANCIALEDGE