INTERESTED IN CORPORATE FINANCE

WHAT YOU NEED TO KNOW FOR YOUR FINAL ROUND INTERVIEWS

SMITH HOWARD

ABOUT SMITH HOWARD

Smith Howard was set-up by a former investment banker to educate candidates about their career options, in particular the range of options in investment banking. It also helps organisations with smaller graduate recruitment targets to access the highest calibre candidates.

If you would like more information about Smith Howard and how we can be of help to you in your career, please contact us:

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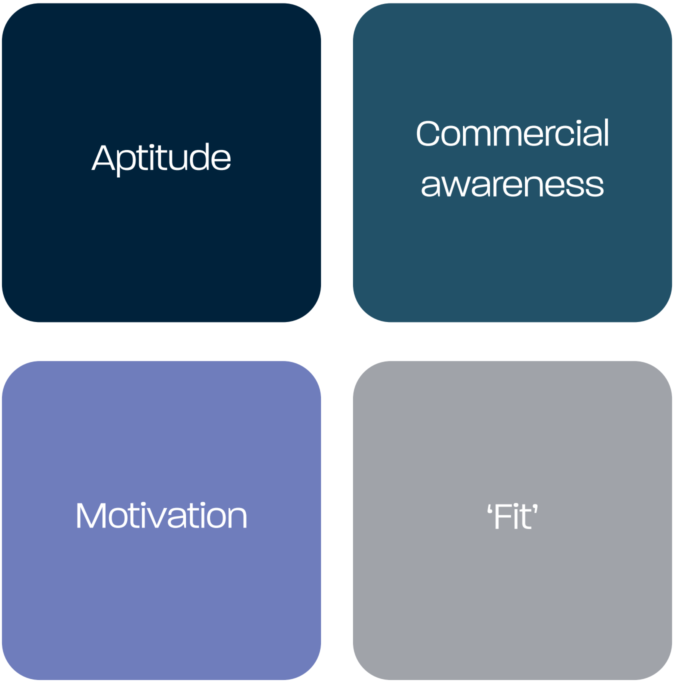
1. INTRODUCTION

The most difficult thing about interviewing for a job in corporate finance, is knowing what you need to know! Interviewing is an art rather than a science, but being prepared will increase your chances of success. Think about this document as a curriculum for corporate finance interviews. Its aim is to give you a framework for your interview preparations.
In Section 5, we have listed a number of resources that will help provide the 'meat' for the framework, plus a few books that provide a useful background to life as a banker.

In order to succeed, you need to understand what the interviewers are trying to gauge.



1. INTRODUCTION cont.

It goes without saying that all the investment banks want intelligent, motivated individuals, but importantly they also require them to be commercially aware and to 'fit' within their organisation. What most people don't realise is that these four qualities are interlinked. For example, an interviewer tests a candidate's knowledge of corporate finance not only to measure their aptitude, but also to gauge how motivated they are to achieve a graduate position.

This document is divided into two main sections:

- **What you need to know** – hard facts that will demonstrate your aptitude, motivation and commercial awareness
- **How to present yourself and your background** – answers that you can prepare in advance to best demonstrate your aptitude, motivation and 'fit' with the organisation you have applied to

2. WHAT YOU NEED TO KNOW

There are a number of theories and facts you need to understand ahead of your interviews. Think about it as learning a common language that will allow you to communicate with the interviewer. This is necessary as the interviewer wants to get a sense of what it will be like to work with you on a day-to-day basis; understanding corporate finance theory and being able to have a discussion about it will help him to do this.

Naturally, the amount of knowledge you are assumed to have is dependent on the position you are applying for, and your academic background. A candidate studying a finance-based degree is assumed to have more knowledge than one studying History. Similarly, candidates applying for graduate positions will be expect to know more about corporate finance than candidates applying for internships.

CORPORATE FINANCE

The first question that you should know the answer to is 'What is corporate finance?'.

What we call corporate finance, some call the investment banking division. It is important not to confuse an investment bank with the investment banking division of an investment bank.

An investment bank is an organisation which generally comprises of at least a corporate finance and a financial markets division. An investment bank can, however, also include private equity, asset management and private banking operations. Some of the larger investment banks also have retail banking operations, for example Citi or Deutsche Bank.

CORPORATE FINANCE cont.

The investment banking division refers to a particular set of activities also known as corporate finance or advisory. Corporate finance is advisory services which assist companies in raising capital and acquiring and disposing of businesses. It includes divisions referred to as M&A, ECM, DCM and corporate broking:

- **Mergers and acquisitions (M&A)** – an advisory function which helps companies buy and dispose of businesses
- **Capital markets** – the collective term for ECM and DCM (described below)
- **Equity capital markets (ECM)** – an advisory function which helps companies list their equity on a stock exchange or raise additional equity funding
- **Debt capital markets (DCM)** – an advisory function which helps companies raise debt funding
- **Corporate broking** – another advisory function which focuses more on a company's relationship with the market and its shareholders

You should know how an investment bank works and the difference between corporate finance and the other departments in an investment bank. Think about which departments work together and how they can effectively combine forces.

Some departments aren't allowed to work together and are separated by a 'Chinese Wall'. This Chinese Wall, is an ethical boundary which exists to separate the investment banking operations from other operations in an investment bank. Investment bankers are often privy to non-public information, as the accuracy of their advice relies on using up-to-date company forecasts. This non-public information could be used by other divisions in the bank to make illegal profits, a Chinese Wall exists to ensure that this doesn't happen.

A good place to start finding out about the divisions of an investment bank is our helpsheet **'Starting Your Career Search: What is Investment Banking?'.**

THE WORK THAT IS CARRIED OUT

As you have probably guessed by now, the business of corporate finance is advice. As such, corporate financiers are engaged in three main types of work:

- **Pitching** – seeing potential clients and talking to them about their company, their industry and giving the company ideas for their next strategic move
- **Advisory** – seeing clients (long-term or recently engaged) to provide advice about the strategic direction of the business
- **Project management** – once a transaction has been agreed upon, the bankers then act as project managers to ensure that all the teams involved (lawyers, accountants, PR) are working together to an agreed timetable

The way in which a corporate finance department is divided, varies from bank to bank. Some banks have what are called sector coverage teams. These teams will focus on one or a collection of sectors. They will pitch to win business and advise all the bank's clients in this sector about M&A opportunities or issues surrounding equity or debt funding. Execution teams support these sector coverage teams which handle the project management for all the different types of transactions. Some banks do not separate their corporate finance departments; bankers who work in these departments are involved in pitching, advisory and project management.

Pitching and advisory are all about valuation. In order to formulate the best advice for their clients, bankers have to assess the value of the company given the different strategic alternatives. Project management is about co-ordination and ensuring that the transaction adheres to the different rules that regulate the way in which companies operate, the most common being **'The Listing Rules'** and **'The Takeover Code'.**

It sounds obvious, but it is important that you have fully researched what you will be doing on a daily basis once you have the job. Make sure that you talk to friends or family that you know in the industry, or quiz the investment banking representatives that come on campus. If you don't know what your responsibilities will be, an interviewer will assume that you were not motivated enough to find out and therefore a riskier hire. Our helpsheet **'Investment Banking Initiation: Corporate Finance Intern Helpsheet'** gives a reasonably detailed view of the entry-level tasks, but you will also be expected to know how this work fits into the bigger picture.

FINANCIAL STATEMENTS

The knowledge assumed in this area, along with the debt vs equity and valuation sections varies depending on the degree subject you have studied. If you have studied an accounting degree, you will be expected to have a sound grasp of the financial statements, if you have studied something less financial you will be expected to have a basic understanding of the financial statements, what they show and what they are used for in corporate finance.

The three main financial statements are:

- **Profit and loss (income statement)** - presents the income and expenditure of a company over a stated time period, for example an annual report will show a profit and loss statement for one year
- **Cash flow statement** – describes the cash inflows and outflows of the company over a stated time period
- **Balance sheet** - this statement shows the assets and liabilities of a company – what the company owns and what it owes, at a snapshot in time (for example a company's year end)

A company listed on the London Stock Exchange, has to publish these three statements every six months. A corporate financier uses them to help forecast the financials for a company in order to derive a valuation and consider the implications of potential strategic moves.

DEBT VS EQUITY

Investment banks help companies raise debt and equity financing. It is therefore important that you understand the differences between debt and equity funding. The main differences are:

- Equity confers ownership, debt does not
- Debt is always repaid, equity is generally never repaid
- Debt is often secured on the companies assets, equity is unsecured
- If a company becomes insolvent, debt ranks higher than equity (i.e. the debt is repaid from an insolvent company's assets before any money is given to equity holders)

VALUATION

As described above, valuation is key to a corporate financiers work. It is therefore important that you understand the following valuation techniques.

Comparable companies' analysis

Commonly referred to as 'the comps'. This is the calculation of various ratios based on the valuation of similar listed companies. The ratios calculated vary between sectors, most valuation multiples involve denominators derived from the profit and loss statement. The most common multiples are enterprise value compared to EBITDA (earnings before interest, tax, depreciation and amortisation) and share price compared to earnings per share, these ratios are abbreviated to EV / EBITDA and P/E.

Comparable transaction analysis

This is similar to the comparable companies analysis described above, the only difference is that the ratios are calculated based on the value of a historic transaction.

Market valuation

All companies that are listed on the stock exchange are valued by their investors. The share price of a company is multiplied by the number of shares outstanding to give an equity value for the company. The equity value of a company is then added to the debt (net of any cash) outstanding to derive an enterprise valuation.

Discounted cash flow analysis (DCF)

The DCF gives the enterprise valuation of the company and is used to assess the fundamental value of a company. A discounted cash flow is based on two principles: cash flow and the time value of money. Find out:

- How to derive free cash flows
- What forecast periods are commonly used
- What the term 'terminal value' refers to
- How the cash flows are discounted for the time value of money
- How CAPM and beta are used to calculate the discount rate

In order to derive a DCF valuation for a company, a number of formulas are used. It is more important to have a sense of how a DCF valuation works, rather than knowing the formulas. For example, does a higher discount rate give a higher or lower valuation, assuming everything remains the same?

When studying the different valuation techniques, it is important to consider the advantages and disadvantages of each one and the way in which the values derived from each technique would compare when valuing the same company.

VALUATION cont.

Normally (beware there are exceptions), the DCF will give you the highest valuation as it assumes perfect execution of the financial forecasts and normally assumes growth around inflation for the time beyond the forecast period. A comparable transaction analysis would give the next highest valuation – as you pay a premium over the market valuation for control of a business. Market valuation and the comparable companies' analysis will give the lowest valuations, assuming that the company you are valuing is trading in line with its sector.

SYNERGIES

If you are interviewing for an M&A position, or one within a sector coverage team, you should have an idea of what synergies are. When companies merge or one company acquires another company, a rationale will be given for the transaction. This rationale will normally centre on the availability of 'substantial synergies'. 'Synergies' is the term used to represent the fact that often two companies can be more profitable together than as separate entities.

There are three different types of synergies, revenue synergies, cost synergies and financing synergies.

Revenue synergies

Revenue synergies can be generated in two ways:

- **Horizontal** – these synergies are available when two companies combine that are at the same level in the production cycle. In general these synergies are available because the combination allows the companies products/services to be marketed to a larger network. For example, a UK based company buys a US based company and is able to market its products to the new geographical customer base
- **Vertical** – these synergies are available when a company acquires a company that is either higher up or further down the production cycle, e.g. an oil refinery buying an oil well

Cost synergies

Cost synergies are available because a combined company can normally reduce its overall cost base.

- **Economies of scale** – this is based on the concept that the more a company buys of a raw material the cheaper the company's supply. This reduces a company's cost of goods sold and makes the company more profitable
- **Head office costs** – when companies combine, they have a number of duplicate 'head office' functions. These duplicate functions are slimmed down, for example all head office employers may move into one head office and in doing so reduce the property costs of the combined company

Financing synergies

Financing synergies are another type of synergy that is available as a result of economies of scale. The larger a company is, the larger the amount of debt it requires and in general the more credit worthy the company becomes. If this is the case, the combined entity becomes cheaper to finance.

THE ORGANISATION YOU ARE APPLYING TO

It goes without saying that you need to know about the company that you are applying to. Some candidates take this to the extreme, for example by memorising their recent results and trying (but not succeeding) to seamlessly drop it into conversation. The interviewer is more concerned whether you have shown an appropriate level of interest in their company and that you have done enough homework to work out how and why you would 'fit' with their organisation.

The guidance on the question 'Why this organisation?' is answered in the next section as we consider it more aligned with personal background. However there are a few things that you should know about the company you are interviewing with:

- The background of the company
- How they were formed
- Their business model – how do they stand out from their competition?
- The divisions within the organisation
- Their geographic focus
- Recent financial performance
- If appropriate, the deals they have done recently (study in detail at least one, but know about the other high profile deals)

COMMERCIAL AWARENESS

Commercial awareness is talked about a lot, but is difficult to define and is something that candidates often have a natural aptitude for. In short, it is the ability to apply business concepts to real word scenarios. Are you the type of person that sits in a busy restaurant, and works out 'the spend' per head, and then estimates the initial investment to try to work out just how much money they are making?

Something that is very important in corporate finance is that you can use the theories and apply them in different scenarios. In your interview, resist the temptation to recite the textbook; this is easy to see through. Demonstrate to the interviewer that you can apply them in different scenarios, merely reciting the textbook will give them the sense that you can't apply what you have learnt, and are not commercially aware.

You should spend some time thinking about how corporate finance theory applies to different companies and industries. You may be asked to talk about the drivers and any past or potential M&A transactions in a particular industry. Make sure that you have a couple of examples of industries that you can talk about and how they work. Smith Howard's tip is to choose a consumer type industry, for example high street retail. You should also know about the big M&A deals that are hitting the headlines and any companies that are listing on the stock exchange for the first time also called an IPO (an initial public offer).

You should also be fairly up to speed with the general economic conditions, for example what is the current thinking on inflation, interest rates, house prices etc.

3. HOW TO PRESENT YOURSELF AND YOUR BACKGROUND

All banks want to employ people that are hard working, honest and reliable, not too arrogant, but super bright and incredibly keen on business and finance. But every bank is looking for a slightly different mix of these qualities and therefore it is difficult to know if you are the type of candidate an organisation is looking for.

Every corporate financier thinks they are the model candidate and will naturally look for a candidate who is similar to themselves at the start of their career. However, it is very difficult to guess what they were like as a graduate, so it is important to be yourself. The interviewer is trying to get a sense of who you are; if you try to be who you think he wants you to be, you may not convince the interviewer you are genuine.

Looking for a job is a two-way process. It is not just about getting the job, but more about actually having the job - enjoying and succeeding in what you do. If you 'fit' within an organisation, there is a greater chance of succeeding in your career.

On the day, be smart – a smart suit and tie for the men is a must, and for women a smart suit and appropriate shirt. Be on time... This actually means, be early! Allow plenty of spare time; the ideal situation is to plan to have a coffee in the area before your interview so that you are on time. If you are late because of an unavoidable circumstance, advise the company's point of contact as soon as you become aware that you will be late. Give them the reason for your delay, an indication of your new time of arrival, and keep them up dated if this changes. Do not make excuses, remember they are busy organising a day of interviews, they just need to be informed as to what has happened.

On the interview day, be as confident as you can. Nerves are a natural part of the process and accepting this will help reduce any negative impact they may have. If appropriate, try to engage the interviewer in conversation but don't do all the talking. Maintain a reasonable degree of eye contact, not looking at the interviewer enough will show a lack of confidence or in the worst case disinterest and looking at him too much will seem too aggressive. Most of all think before the interview how you are going to relay to the interviewer how committed and enthusiastic you are about the opportunity and how you can demonstrate that you have what it takes.

COMPETENCY BASED QUESTIONS

Competency based questions have now become a regular part of the corporate finance interview. From the initial application to the final interview, you will be asked to demonstrate that you are a team player and that you can succeed against the odds.

You should have a small number of situations rehearsed that can be appropriately tailored to demonstrate the below:

- Attention to detail
- Hard worker
- Time management
- Creative solutions
- Logical (mathematical)
- Team player
- Leadership
- Strengths
- Weaknesses
- Successes
- Failures
- Ability to work on a number of projects at once
- Work under pressure

One of the key things that the interviewer will want to know is how and why you will be able to cope with the long hours that are often required of a junior banker. This is a difficult question to answer, it is important that you acknowledge that the time commitment will be one of the greatest challenges of the job. If you are too keen, you may be viewed as naïve. Do not try to give examples of how you will be suited to the time commitment, unless they are directly comparable. Candidates often give the response 'I worked hard at university so I am ready for a job'. Work is different to university, you have to do it all day every day, and there are no summer holidays!!

WHY M&A?

This is another important question which candidates are often ill prepared for. Think about your own reasons for applying to M&A – and think about how to present it to show the interviewer that it was a logical and rational decision that was well researched.

Implicit in this question is also the reason why you are suited to the job – we've all watched X-Factor enough times to know that you won't be successful as a singer if you can't sing. Make sure you know what corporate finance entails in the short-term and long-term, and show how your skills will ensure that you will succeed.

WHY THIS ORGANISATION?

This question may also be asked at the same time as the 'Why M&A?' question. The previous section on the organisation you are applying to tells you what you should know about the organisation you are applying to. In order to answer this question, you have to understand the organisation's strategic positioning and their culture. Think about your skills and your personality and the reasons why you think that you will succeed in this organisation. Make sure that you don't answer this question in a one sided way, it is about both what you can contribute to the organisation, and what the organisation can contribute to you.

CV STORY

You may be asked questions about the decisions you made about your A-Levels, university location or degree subject. The interviewer is just testing that you make rational decisions and show commitment to what you have decided to do.

WHAT OTHER JOB OFFERS DO YOU HAVE?

The reason the interviewer asks you about this, is because when they are making their decisions about who to offer jobs to, they want to make sure that they don't miss out on someone they want because they have an offer which is about to expire. Be honest, if you have no job offers, say so, but do state if you are expecting to hear from another organisation imminently.

WHAT QUESTIONS TO ASK WHEN YOU ARE GIVEN THE OPPORTUNITY

Each interviewer will usually give you an opportunity to ask them questions. Have a few genuine questions prepared that will help you in your career choice and help you to understand the organisation you are interviewing with. If you are struggling for a question to ask, you can always ask them about their own career development and why they chose and continue to choose to stay in their job.

This part of the interview is not your chance to stand out by asking a smart question about the market or about a particular corporate finance theory – you will stand out for the wrong reasons. This time is for you to glean useful information about the organisation – don't waste it.

HOW TO HANDLE THOSE AWKWARD QUESTIONS

During your interview, make sure that you listen to, and understand the questions you are being asked. Be clear, concise and logical in your answers and be quiet if you have answered the question. Candidates can sometimes get themselves into trouble when they don't stop talking. Take time to think about the answers to the questions – this will ensure that you don't make an error because you are talking faster than you can think. If you don't know the answer to a question, the mature thing to do is to say that you don't know. If you think that you should know the answer to the question, but you can't remember the answer, tell the interviewer. This will show that at least you know the framework of the corporate finance theories.

FIT

Hopefully by being well prepared and being yourself, you will 'fit' with at least one organisation. There is not much more that we can say about 'fit' other than remember that throughout all of your interviews you will be meeting new people. When it gets to your 10th interview, remember that this interviewer is meeting you for the first time, continue to be enthusiastic and present yourself as you did to the first interviewer.

4. AFTER THE INTERVIEW

It is important that you make the right moves after the interview.

FOLLOW-UPS

After the interviews, candidates will often send a follow-up email to thank the interviewer for their time during the interview. This is only appropriate if the interviewer has given you their business card or contact details. If you do not have their contact details, do not try to guess their email address – investment bankers are busy people and will not respond well to getting 20 unsolicited emails from all the candidates they interviewed.

If you do feel that a follow-up would be appropriate, keep the email short and to the point. You should thank them for their time and reiterate how impressed you are by their company and how eager you are to be considered for their graduate program.

ACCEPTING AND DECLINING

The way in which you present yourself should continue through to accepting and declining an offer. Once you receive the phone call that offers you the job, you should express how pleased you are to be offered the job, and that you would like time to think about their offer. If you are offered drinks or dinner with some of their employees, do take up the offer. This is your chance to find out a bit more about the culture and what is expected of an analyst. Remember that you can ask most of the questions you want to, now that you have the offer. Investment banks will give you at least a couple of weeks to think about their offer, take your time, but do inform the investment bank of your decision as soon as you have made it. When you inform the investment bank of your decision, whether you are accepting the offer or declining the offer, the etiquette is to call the person who extended the offer to you and anyone that helped you to make the decision. Do not email, leave a message or any such impersonal method of communication. You want to show, if you are accepting the offer, how honoured you are to be joining their organisation, or make sure that you don't close any doors if you are declining their offer.

IF YOU DON'T GET THE JOB

There is a little 'je ne sais pas' about getting a job, it is dependent on 'fit' and the other candidates applying for the positions. Apply to enough organisations with the right qualifications and you will find the one where you fit in. When you find the organisation where you fit in, the interviews will be easy and you won't understand exactly why you got the job!

5. RESOURCES

Careers services

Although some of you might not think that these careers services are at the cutting edge of careers, they do have a lot of useful resources for students and are the first port of call for all employers wanting to recruit on campus. You can also glean a lot from careers events be it meeting company representatives in person or attending careers workshops.

Careers services also subscribe to some of the most useful information sources. For example, Factiva, a news aggregator, which will help you to find out the latest news about a company you have an interview with.

Third party resources

There are a number of guides and websites that can be used to find information about the investment banking industry and the organisations to apply to. The most useful for corporate finance are:

- Vault (European Edition)
- Target
- Inside Careers

Academic texts

These are useful for the pure theory, but make sure you are always thinking about how it applies to real companies.

- **Arnold Corporate Financial Management** – Glen Arnold
- **Principles of Corporate Finance** – Richard Brearley and Stuart Myers
- **Valuation: Measuring and Managing the Value of Companies** – Tom Copeland

5. RESOURCES cont.

Accounts of investment banking true stories

These books give an insight into the way in which corporate finance is carried out and what life is like within an investment bank.

- **Big Deal** – Bruce Wasserstein
- **Barbarians at the Gate** – Bryan Burrough and John Helyar
- **Monkey Business: Swinging Through the Wall Street Jungle** - John Rolfe

There are other sources that you can use to research a deal that is in the press or find out more information about the company that you are applying to.

- **Companies websites**
- **Online newspapers**
- **Investegate** – a one-stop shop for official press releases issued by listed companies
- **Google alerts** – Google will email you news stories about specified topics, useful if you want to keep track of a deal in the press

6. THE 10 QUESTIONS YOU SHOULD KNOW THE ANSWER TO

1. What is corporate finance? What services do we offer to our clients?

2. What do you think you will be doing as an analyst at this organisation?

3. What are the main differences between debt and equity funding?

4. How do you value a company? Which valuation techniques would you use for a company with no revenues?

5. Choose an industry, what are the drivers and current trends in this industry?

6. If you could advise on any M&A transaction, which two companies would you combine and why?

7. Why do you wish to pursue a career in corporate finance?

8. Why did you apply to this organisation?

9. Why do you think we should hire you?

10. Have you any questions for me (the interviewer)?

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