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Financial Management

Syllabus

Unit I Introduction:

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Unit II Capital Structures:

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Unit III Capital Budjeting

Capital Budjeting: ARR, Payback Period, Net Present value, IRR, Capital Rationing, simple Problems on Capital Budjeting Methods.

Unit IV Dividend policies:

Dividend Policies - Factors affecting dividend Payment - Company Law Provision on dividend, Payment - Various Dividend Methods (Walter's Gordons - MM Hypothesis.

Unit V Working capital:

Working capital - Components of working Capital - Operating cycle - Factors influencing Working capital - Determining (or) forcasting of working capital requirements

Unit I

Introduction.

Meaning of Finance:
Finance May be defined as the art and science of Managing money.
it includes financial services and financial institutions.

Definition:
Finance is also refered as the provision of Money at the time when is needed.

Function:
Procurement of funds and their effective Utilization in business concerns.

Objectives of finance:
(1) Profit Maximization:
Increase the financial gains of the business.
(2) Wealth Maximization:
Maximize the value of shareholders investments over time.
(3) Optimal Utilization of Resources:
Use financial resources efficiently to achieve the best posible output.
(4) Ensuring Liquidity:
Maintain sufficient Cash flow to meet short term obligations.
(5) Risk Management:
Identify, asses, and mitigate financial risk.
(6) Sustainable Growth:
Achieve growth that can be maintained over the long Period./term.

7. Cost Control: Monitor and reduce Expenses to improve Profitability

8. Financial Planning and Forecasting:
Develop Strategies for future financial needs and Potential scenarios.

9. Capital Structure Optimization:
Balance debt and equity to minimize the cost of Capital

10. Compliance and Legal considerations:
Adhere to financial Regulations and legal requirements.

11. Stakeholder Value:
Consider the interests of all Stakeholders including employees customers and the Community.

12. Innovation and Competitive Advantage:
Invest in new technologies and ~~pro~~ Processes to Stay ahead of competitors.

Importance of finance

* Finance is regarded as the life blood of a business Enterprise
* Finance is one of the basic foundations of all kinds of economic activities.
* It is the Master key which Provides access to all the Sources for being employed in Manufacturing and Merchandising activities.
* It has rightly been said that business needs money to make more money.

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* It turn that money begets more money only when it is Properly Managed.
* Efficient Management of every business enterprise is closely linked with efficient Management of its finances.

Sources of Finance

- Based on Period
  - Long term Sources
  - Medium term Sources.
  - Short term Sources.
- Based on Ownership
  - Owners Funds
  - Borrowed Funds.
- Based on the Source of Generation
  - Internal Sources.
  - External Sources.

I. Basis of Time Period.

(1) Long term Sources.

These are the Sources of finance that fulfill the financial Requirements of the business for a longer Period which is more than 5 years.

it includes:
* Equity shares. (ordinary shares)
* Retained earnings.
* Preference shares (Divident are paid before to the ins shares of common stock)
* Debentures (debt instrument)
* ~~Long te~~ Loan from financial Institution

ii) Medium term Sources:

These are the sources that are required for a period of more than one year but less than five years.

Example:
* Loan from Banks.
* Public Deposits
* Loan from financial Institutions

(iii) Short term loan:

These are the funds that are required for less than a year.

Example:
* Trade Credit
* Factoring
* Commercial Paper

II Basis of Ownership:

(i) Owners fund:

These are those Funds that are raised by the owners of the business.

It can be raised by the sole person or the partners or by the shareholders.
Sources : 1) Equity Shares
2) Retained Earnings.

(ii) Borrowed Fund :
Commonly used source of funds Borrowed fund for a specific period, on certain terms and conditions.
It has repaid after the expiry of the Period with interest. it includes.
Source : 1) Debentures,
2) Loan from banks
3) Public deposits
4) Loan from financial Institution.

III Basis of Sources of Generation.
(i) Internal Sources :
Internal Sources of finance are those funds that are within an organization.
These sources fulfil the short and limited needs of a business.
Example : (a) Equity shares.
(b) Retained Earnings.
II External Sources :
These refer to those Sources which involve raising funds outside of an Organisation.
It is useful when large amount of money is needed. Example :

(1) Financial institution
(2) Banks
(3) Public Deposit
(4) Debentures.
(5) Trade Credit

Financial Management

Financial Management is the Management of Monetary resources.
It involves (i) Planing accurarely
(ii) directing monetary resources at correct time
(iii) Controlling the financial activities of a firm

Functions of Financial Management!
The Modern approach to the financial Management is concerned with the Solution of major problems Like investment, financing and dividend decisions.

a) Investment Decisions!
The investment decision is concerned with the selection of assets in which funds will be invested by a firm.
The assets of a business firm include Long term Assets - Fixed Assets and Short term Assets - Current Assets

Long term assets will yield a return over a period of time in future.

Short term assets which are easily convertible into cash within an accounting period, i.e., year.

The longterm Investment decision - is known as Capital Budgeting

Short term Investment decision is known as Working Capital Management.

Capital Budgeting:

Capital Budgeting decision is the analysis of risk and Uncertainity

It means the long range planning of allocation of funds among the various investment proposals.

Working Capital Management:

The capital which is required to finance current assets is called working capital.

It is the capital of a business which is used to carry out day to day business operations of a firm.

The Finance Manager must equip himself with sound techniques of managing the current assets like cash receivable and inventories etc.,

(ii) Financing Decision:

This deals with deciding optimum proportion of equity and debt capital. The financial manager should get the optimal capital structures to maximize the shareholders return with a minimum risk.

(a) Cost of Capital:

It can be defined as the minimum rate of return that a firm must earn on its investment, to keep the value (of equity shares) of a firm intact.

(b) Capital Structure Decision

Capital structure includes only long term debt and total stakeholders investment.

This refers to the makeup of a firm's capitalization.

It refers to the mix of debt, preference shares and equity share capital.

Dividend Decision:

Dividend policy decisions are concerned with the distribution of profits of a firm to the shareholders. How much of the profits should be paid as dividend? ie, divident payout ratio.

The optimum dividend policy is one which maximizes the market value of the share. It includes 2 decisions

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(1) Profit Maximization
(2). Wealth Maximization

(1) Profit Maximization:
It is one of the objectives of the firm to earn higher returns on its resources. Which means higher dividends to the investors.
This Concept works on bigger the better, Principle.
It ignores quantitative and Qualitative aspects.
It also Ignors the time value of money Concept.

(2) Wealth Maximization:
Shareholder wealth maximization Means maximizing the Net Present Value of a course of action to Shareholders.

E_{P_2} = (intensity due to Smaller shell) + (intensity due to larger shell)

$$\left(\text{Shareholders Wealth}\right) = \left(\text{Number of Shares Held}\right) \times \left(\text{Market Value Per share}\right)$$

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Role of Financial Manager in Financial Management :

Financial activity of a firm is one of the most important and complex activities of a firm.

Therefore in order to take care of these activities a financial Manager performs all the requisite financial activities.

Main Functions of a financial Manager.

(1) Raising of funds
(2) Allocation of Funds
(3) Profit Planning
(4) Understanding Capital Markets.

(1) Raising of funds :

In order to meet the obligation of the business, it is important to have enough cash and liquidity. A firm can raise the ~~for~~ fund ~~from~~ by the way of equity and debt.

It is the responsibility of the financial Manager to decide the ratio between debt and equity.

It is important to maintain a good balance between equity and debt.

(2) Allocation of funds:
The Next important function of financial Manager is to allocate the funds.
The fund Should be allocared in the below manner optimally used.
(1) The Size of the firm and its growth capability.
(2) Status of assets whether they are long team or short term.
(3) Mode by which the funds are raised.

(3) Profit Planning:
* Profit earning is one of the Prime functions of any business organisation.
* Profit planning: It refers to Proper usage of the Profit generated by the firm.
* Profit raises due to many factors such as. (a) Pricing b) industry competition
c) State of the Economy
d) Mechanism of demand and Supply
e) Cost and Output
A healthy mix of variable and fixed factors of production can lead to an increase in the Profitability of the firm.

(H) Understanding Capital Markets:

A Clear understanding of Capital Market is an important function of financial Manager.

When Securities are traded on stock market there involves a huge amount of risk involved. The financial Manager understands and Calculates the risk involved in this trading of Shares and debentures.

Its on the discretion of a financial Manager as to how to distribute the Profits. The practices of a financial Manager directly impact the operation in Capital Market.