**LECTURE 1 – Introduction to** Business Finance

**Module Title:** Business Finance

**Module Description:**

This module considers cost information (both current and future) aligned to financial management and business performance.

The management of business finance can be crucial to the success or failure of the business.

Mismanagement of business finances can be detrimental to the business and can also impact on the impression customers have of that business. This module considers financial management within a business context and explores the interpretation of financial information to assess the performance of a business. Concepts covered within this module complete the development of financial information within Entrepreneurship.

**Module Aim:**

This module aims to help students understand a variety of financial strategies that are used by businesses. They will learn about budgeting, financial management and accounting and its importance in the monitoring and management of financial performance. Students will be provided with the opportunity to use cost data to produce financial records that can be analysed, to assess and evaluate the performance of a business. Students will explore different costing and budgetary systems and will discuss the causes of resulting variances and their impact on financial management. Students will be able to translate and measure business performance through the presentation of financial information for a range of businesses.

**Module Learning Outcomes:**

1. **LO1:**Examine cost information within a business
2. **LO2:**Critically analyse methods to reduce costs and enhance value within a business
3. **LO3:**Prepare forecasts and budgets for a business
4. **LO4:**Evaluate performance against budgets within a business

**Module Skills:**

* Interpret contrasting information.
* Apply theory to organisational practice.
* Contribute effectively and ethically in providing advice or making judgements that would inform or benefit management practice.
* Ability to apply and analyse financial data.

**Reading Lists** page111image2187712

Atrill, P. and McLaney, E., 2018. Accounting and finance for non-specialists. Harlow: Pearson Education Limited

Cinnamon, B. and Hellweg-Larsen, B., 2010 *How to Understand Business Finance (Creating Success)*. 2nd ed. London: Kogan Page.

Davies, D., 2005. *Managing Financial Information* 2nd Ed. London: Chartered Institute of Personnel and Development

Dyson, J.R., 2017. *Accounting for non-accounting students* 8th Ed. London: Financial Times/Prentice Hall.

**E Learning Resources**

http://www.managers.org.uk  
Money Week. http://moneyweek.com/  
Money Facts http://moneyfacts.co.uk/  
Bloomberg http://www.bloomberg.com/news/world Reuters http://uk.reuters.com/business  
MSN Money http://www.msn.com/en-gb/money

**Journal**

The Journal of Finance  
Journal of Business Finance and Accounting

**Assessment Details**

Report (3000 words) --- 75 %

Practical Assignment (1000 words) – 25 %

**BUSINESS FINANCE**

**LECTURE SEQUENCE**

1. Overview of Business Finance

2. Corporate financial statements

* Income statement
* Statement of financial position
* Cash flow statement.

3. Analysis & interpretation of financial performance

* Profitability
* Liquidity
* Working capital management / Efficiency
* Capital structure analysis
* Stock market performance

4. Investment Appraisal / Long term decision-making

* Traditional and DCF techniques
* Relevant cash flows

5. Sources of finance

* Long term Vs Short term
* Equity Vs Debt

6. Introduction to Management Accounting

* Cost classification; cost behaviour; product/service costing

7. Decisions making scenarios (short-term)

8. Budgeting and cash budgets.

9. Standard costing and variance analysis

**Revision & conclusion**

*All students must keep up with the weekly work in order to*

*progress well and benefit from the lectures.* ***This is a practical***

***module and requires application on your part****. Students may*

*contact me on:* [*sa.palan@lsclondon*](mailto:sa.palan@lsclondon)*.co.uk with your questions*

*and I will do my best to respond asap or within a day. Be*

*consistent with your work and success will follow. Thank YOU.*

**An introduction to Corporate Financial Statements**

**1. Influences upon financial accounting/reporting/financial statements:**

These can be grouped into the following:

* National law – the form and content of accounts may be regulated by national legislation. ‘Fair presentation’
* Accounting standards – The International Accounting Standards Board (IASB) produces accounting standards. These helps tackle issues/interpretation of standards.
* Accounting concepts and individual judgement – Accounting policies have developed over the centuries. These are based on generally accepted concepts: business entity concept, going concern, accruals, prudence, consistency, materiality, substance over form and more.
* GAAP – Drawn from local company law, accounting standards, statutory requirements in other countries and the stock exchanges (e.g. LSE)

**2. The main financial statements are:**

* **Income Statement and**
* **Statement of Financial Position (SOFP);**

**Sometimes they are also collectively referred to as the**

**‘final accounts’**

Be aware of old and new terminology used in various published materials in financial accounting - texts, articles etc

|  |  |
| --- | --- |
| **Old terminology** | **New terminology** |
| Profit statement | Income statement |
| Balance sheet | Statement of financial position (SOFP) |
| Stock | Inventory |
| Debtors | Receivables |
| Creditors | Payables |
| Fixed assets | Non-current assets |
| Long term liabilities | Non-current liabilities |

**3. Conceptual framework** - **Accounting concepts/principles:**

* These are principles/rules used in the preparation, use and interpretation of financial statements.
* Evolved over time; adopted for practical rather than theoretical purposes
* Not a rigid code – application of these concepts (via the choice of alternative accounting policies) are often subjective; a question of individual judgement/choice.
* Hence financial accounting/reporting/preparing financial statements is not an exact science?
* There are several accounting concepts. the **first (and not the most important)** of these is the **business** **entity concept:** The entity is treated as separate from its owners.

**4. Some accounting terminology used in financial accounting**

* **Asset:** Something valuable which an entity **owns** or has use of e.g. a factory, motor vehicles, inventory for resale, receivables (amounts owed by customers), bank and cash balances.
* **Liability:** What the entity **owes** somebody else (other than the owner/owners) e.g. bank loan; payables (amounts owed to the suppliers);
* **Capital:** What the entity **owes** (cash/assets) the sole trader/owners. (for companies the owners are the shareholders)

**5. Accounting equation:** (based on the business entity concept)

* What the business owns = What the business owes at any point in time of the business.
* Assets (owns) = Liabilities + Capital (both are what the business owes)

**6. Other accounting concepts**: There are several other accounting concepts and these will be brought together as we progress through the preparation of final accounts: going concern, accruals, prudence, consistency, materiality, substance over form and more.

Please research these before the next lecture. (your homework, please)

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**Requirements for preparing the financial statements / final accounts**

In order to prepare the final accounts (an Income Statement and a Statement of Financial Position) the following are required:

* A **trial balance** - a list of accounts with their balances at the end of an accounting period.
* **Year-end additional information -** required to adjust some of these accounts in the trial balance provided.

**A trial balance**

**1.** In a trial balance there are several accounts with their balances - some of these accounts have debit balances and others have credit balances.

**2**. Why do these accounts have either debit or credit balances? This is the result of applying the double entry system in recording business transactions (or double entry bookkeeping).

* Each business transaction has a dual effect on the accounts (or every business transaction has two equal but opposite effects)
* All business transactions must be entered in the accounts using the double entry system: a debit entry in one account and an equal but opposite credit entry in another account.
* Periodically (monthly or yearly) the accounts are balanced off. Balancing of all these accounts periodically will result in each of these accounts having a either a debit or a credit balance. A listing of these accounts and their balances (debit or credit) is called the **trial** **balance**.

**3.** The correct application of the double entry system should enable the trial balance to balance (i.e. mathematically the total of debit balances = total of credit balances; since for each debit entry there is a corresponding credit entry in the ledger accounts).

**4.** Sometimes mistakes/errors are made in the application of the double entry system and this may produce one of these two effects on the trial balance:

* Errors that affect the trial balance (resulting in the trial balance totals not being equal or balancing). For example, posting a single entry (instead of double entries) for a transaction will affect the trial balance totals.
* there are also errors that will not affect the trial balance totals. For example, a simple case in point is the complete omission (i.e. not accounted for) of a business transaction; this omission will still enable the trial balance to balance (i.e. trial balance totals will agree).

**5.** The trial balance needs to balance before the final accounts can be prepared. However, bear in mind that a balancing trial balance does not mean it is free of errors as explained in (4) above.

**6.** There are 5 types of accounts within the trial balance:

* **Incomes** e.g. Sales, rental income, interest received etc
* **Expenses** e.g. Wages and salaries, purchases (of goods for resale), rent, rates, insurance etc
* **Assets** (what the business **owns**) e.g. Machinery, shop fittings, inventory, bank and cash balances, trade receivables etc
* **Liabilities** (what the business **owes** others) e.g. Bank loan, trade payables, accruals etc
* **Capital** (what the business **owes** the owner)

**7.** All assets and liabilities can be classified into non-current or current

* **Non- current assets** are owned and used by the entity for more than one year (i.e. they are fixed financially for more than one year). Examples: Land, buildings, factories, plant and machinery, motor vehicles, fixtures & fittings
* **Current assets** are owned by the entity and change financially within a period of one year. Examples: inventory, trade receivables, prepayments, bank and cash balances.
* **Non-current liabilities** are what the business owes and require settlement beyond a year (owed for more than one year). Examples: long term bank loan, debentures or bonds (in the case of companies).
* **Current liabilities** are what the business owes and require settlement within a year. Examples: trade payables, short term bank loans, bank overdraft, accruals, taxation (for companies).

**How are financial statements prepared?**

1. Business transactions are recorded in the Books of Prime Entry [Sales Day book, Purchases Day book, Cash Book & the Journal].

2. From the Books of Prime Entry these are recorded in the Ledger Accounts using the double entry system (for everyone of them there most be debit entry in one a/c = a credit entry in another a/c.]

3. Periodically the ledger accounts are balanced. The resulting balances in the accounts are then used to produce a listing of these account balances.

4. This listing of balances is called a Trial Balance.

5. The Trial Balance with some additional information is the used to produce the Financial Statements.