# MODULE 4 – PART 2

# Financial Plans ?

- A financial plan is a process a company lays out, typically broken down into a step-by-step format, for utilizing its available capital and other assets to meet its goals for growth or profit based on a reasonable financial forecast.
- A financial plan can be considered synonymous with a business plan in that it lays out what a company plans to do in terms of putting resources to work to generate maximum possible revenues.

**Financial Forecasts ?**

- ✓ Financial forecasting is critical for business success.
- ✓ To effectively manage working capital and cash flow, a company must have a reasonable **idea of how much revenue it plans to receive over a given time period and what its necessary expenses will be over that same period of time**.
- ✓ Financial forecasts are commonly reviewed and revised annually as new information regarding assets and costs becomes available.
- ✓ The new data enables an individual or business to **make more accurate financial projections.**
- ✓ It is easier for established companies that generate steady revenues to make accurate financial forecasts than it is for new businesses or companies whose revenue is subject to significant seasonal or cyclical fluctuations.

## What Is land, building, Plant, Equipment and Machinery?

- These are long-term assets vital to business operations.
- Property, plant, and equipment are tangible assets, meaning they are physical in nature or can be touched; as a result, they are not easily converted into cash.
- The overall value of a company's assets can range from very low to extremely high compared to its total assets.
- Property, plant, and equipment are also called fixed assets, meaning they are physical assets that a company cannot easily liquidate or sell.
- These assets fall under the category of noncurrent assets (the value of that investment does not recur within an accounting year), which are the long-term investments or assets of a company.
- Noncurrent assets have a useful life of more than one year, but usually, they last for many years.

## Noncurrent Assets?

- Noncurrent assets or long-term assets, not all noncurrent assets are land, plant, and equipment.
- Intangible assets are nonphysical assets, such as **patents and copyrights**.
- They are considered to be noncurrent assets because they provide value to a company but cannot be readily converted to cash within a year.
- Long-term investments, such as **bonds and notes**, are also considered noncurrent assets because a company usually holds these assets on its balance sheet for more than one fiscal year.
- This refers to specific fixed, tangible assets, whereas noncurrent assets are all of the long-term assets of a company.

## Significance of land, building, Plant, Equipment and machinery?

- Investment analysts and accountants use these assets of a company to determine if it is on a sound financial footing and utilizing funds in the most efficient and effective manner.
- A company investing in these assists is a good sign for investors.
- A fixed asset is a sizable investment in a company's future.
- Purchases of these assets are a signal that management has faith in the long-term outlook and profitability of its company.
- These are a company's physical assets that are expected to generate economic benefits and contribute to revenue for many years.
- Investment in this is also called a capital investment.

# Limitations of land, building, Plant, Equipment and machinery?

- PP&E are vital to the long-term success of many companies, but they are capital-intensive.
- Companies sometimes sell a portion of their assets to raise cash and boost their profit or net income.
- As a result, it's important to monitor a company's investments and any sale of its fixed assets.
- Since these are tangible assets, this analysis doesn't include intangible assets such as a company's trademark.
- For example, Coca-Cola's (KO) trademark and brand name represent sizable intangible assets.
- If investors were to only look at Coca-Cola they wouldn't see the true value of the company's assets.
- These assets only represent one portion of a company's assets.

## What Is Working Capital?

- Working capital, also known as net working capital (NWC), is the difference between a company’s **current assets**—such as cash, accounts receivable/customers’ unpaid bills, and inventories of raw materials and finished goods—and its **current liabilities**, such as accounts payable and debts.
- It's a commonly used measurement to gauge the short-term health of an organization.

**Working Capital = Company’s current assets - Current liabilities**

**What Is Working Capital?**

- Working capital is also a measure of a company’s operational efficiency and short-term financial health.
- If a company has substantial positive NWC, then it could have the potential to invest in expansion and grow the company.
- If a company’s current assets do not exceed its current liabilities, then it may have trouble growing or paying back creditors. It might even go bankrupt.

## Components of Working Capital?

- All components of working capital can be found in a company's balance sheet, though a company may not use all elements of working capital discussed below.
- For example, a service company that does not carry inventory will simply not factor inventory into its working capital calculation.
- Current assets listed include cash, accounts receivable, inventory, and other assets that are expected to be liquidated or turned into cash in less than one year.
- Current liabilities include accounts payable, wages, taxes payable, and the current portion of long-term debt that’s due within one year.

## Limitations of Working Capital?

- ✓ Working capital can be very insightful to determine a company's short-term health.
- ✓ However, there are some downsides to the calculation that make the metric sometimes misleading.
  - ✓ First, working capital is **always changing**.
    - ✓ If a company is fully operating, it's likely that several—if not most—current asset and current liability accounts will change.
    - ✓ Therefore, by the time financial information is accumulated, it's likely that the working capital position of the company has already changed.
  - ✓ Working capital **fails to consider the specific types of underlying accounts**.
    - ✓ For example, imagine a company whose current assets are 100% in accounts receivable.
    - ✓ Though the company may have positive working capital, its financial health depends on whether its customers will pay and whether the business can come up with short-term cash.