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## Introduction

# What is this course all about?

This course introduces the student to the basic concepts of corporate finance, and some advanced elements of cost accounting, developing further those aspects more relevant to engineering. This course goes through the fundamentals of financial management and budgeting, bringing together skills and techniques previously learnt in the degree.

During the course, students will learn about the time value of money, how to interpret and analyse financial statements, to value investment projects, to compromise between risk and return, to produce budgets and to manage the firm's networking capital.



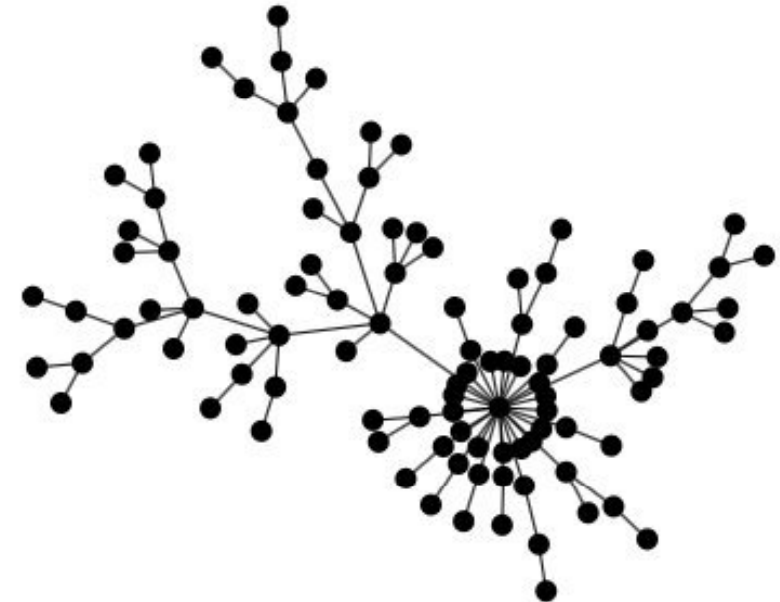
# Why should you care?

- It is one of the main 3 functions of the company (+ operations, + sales), and one that can cause the most problems for young companies.
- Preferential attachment you should be next to the core activities of your company if you want to be safe, you should be next to money if you want to make money.
- You should pass your subjects...

## Why Small Businesses Fail

(from Jessie Hagen of U.S. Bank, cited on the SCORE/Counselors to America's Small Business website <http://www.score.org>)

- 82% – Poor cash flow management skills/poor understanding of cash flow
- 79% – Starting out with too little money
- 78% – Lack of well-developed business plan, including insufficient research on the business before starting it
- 77% – Not pricing properly or failure to include all necessary items when setting prices
- 73% – Being overly optimistic about achievable sales, money required, and about what needs to be done to be successful
- 70% – Not recognizing or ignoring what they don't do well and not seeking help from those who do



# What do you know already?

Let's assess what you know already with a quick quizz.



# Time Value of Money

True or false? A dollar today is worth more than a dollar in the future



Pick the right answer!

☐ False

☐ True

Answer



# Time Value of Money

If your bank is paying you 1% on your savings deposits and the rate of inflation is 1.5%:



**Check the correct answer!**

- ☐ Your real rate of interest is 2.5%
- ☐ Your real rate of interest is 0.5%
- ☐ Your real rate of interest is -0.5%

**Answer**



# Financial Statements

The balance sheet heading will specify a



**Pick the right answer!**

- ☐ Period of time
- ☐ Point in time

**Answer**



# Financial Statements

Which financial statement displays the revenues and expenses of a company for a period of time?



**Pick the right answer!**

**Answer**

- ☐ Balance sheet
- ☐ Income statement
- ☐ Cash flow statement
- ☐ Statement of shareholder's Equity





# Financial Statements

Which of the following is a category or element of the balance sheet?



**Pick the right answer!**

**Answer**

- ☐ Expenses
- ☐ Gains
- ☐ Liabilities
- ☐ Losses



# Financial Statements

Which of the following would not be a current asset?



**Pick the right answer!**

- ☐ Accounts Receivable
- ☐ Land
- ☐ Prepaid Insurance
- ☐ Supplies



**Answer**

# What is a firm?

**Aggregation of capital and labor to produce goods and services, to create value**

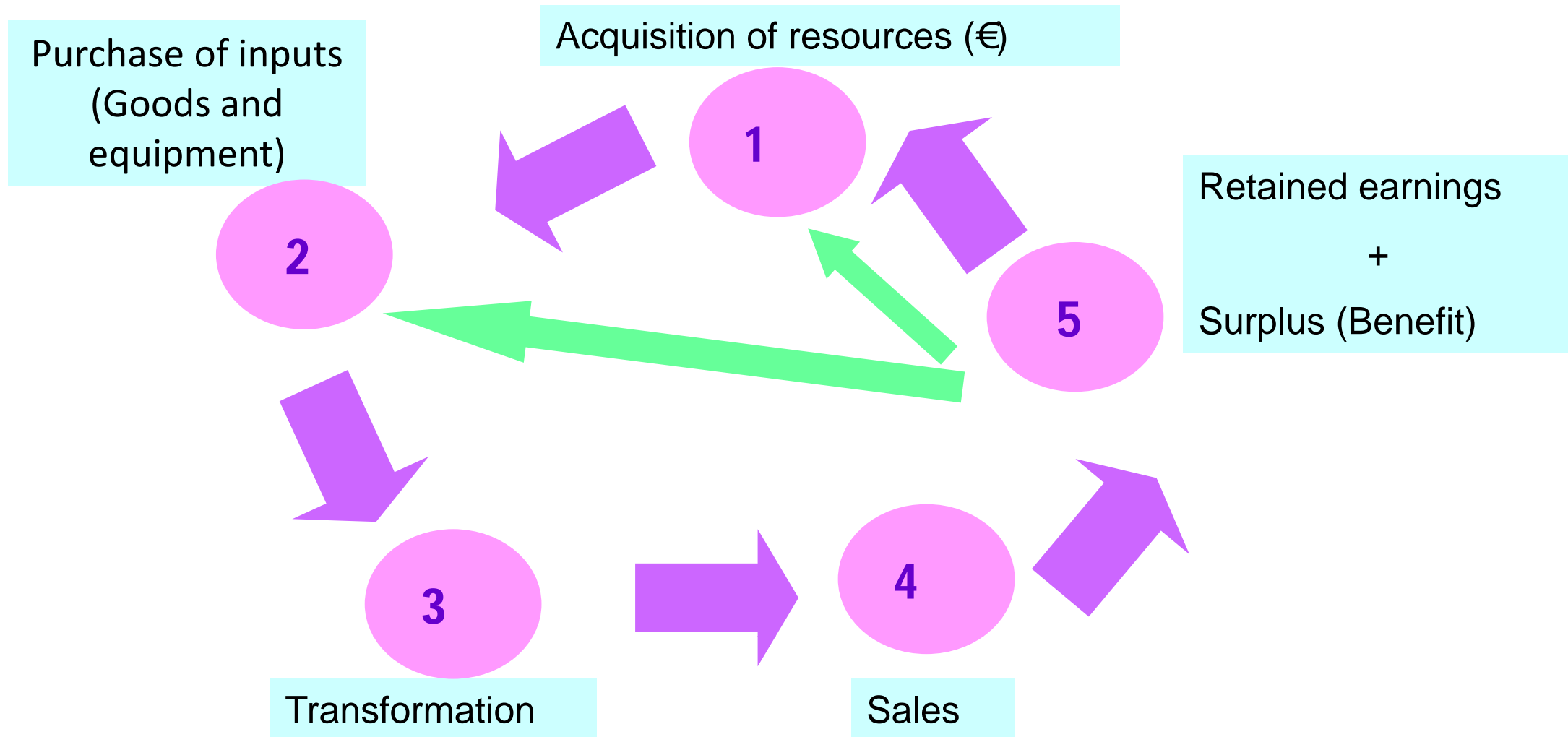
**Basic economic unit**

**Why are there firms?**

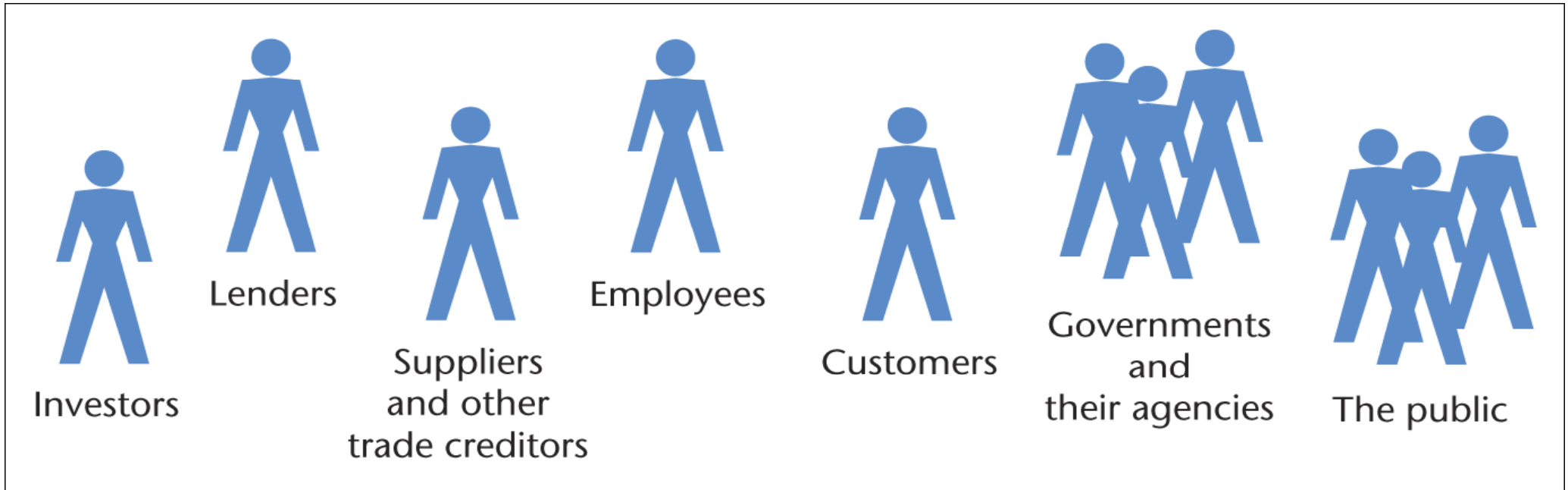
- To reduce transaction costs
- To accumulate capital



# Running a business

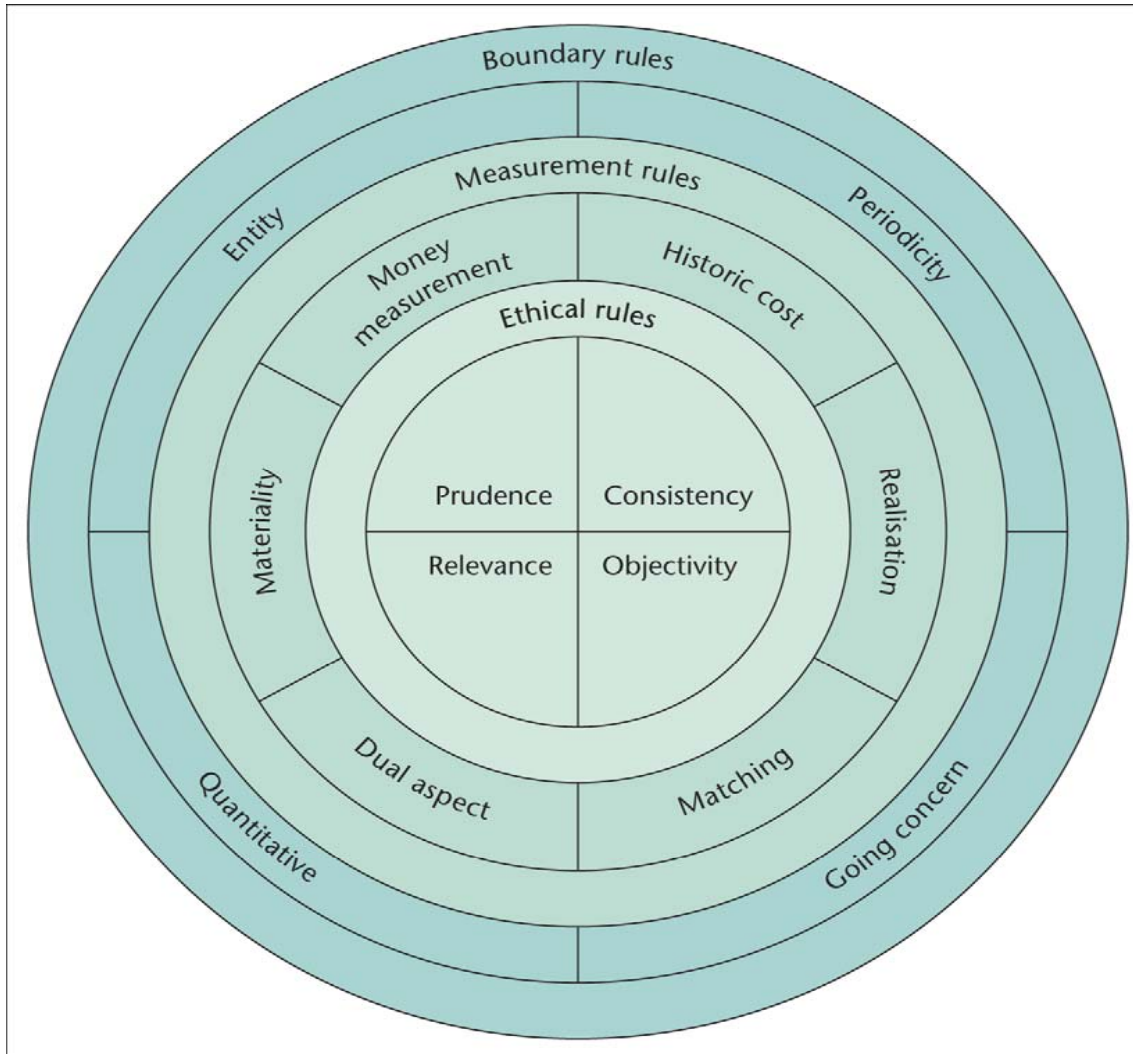


# Nature and purpose



Accounting is a service provided for those who need information about an entity's financial performance, its assets and liabilities

# Rules and regulations



Spanish regulations:  
(according to IAS)

- Plan General Contable
- Código de Comercio
- Leyes de S.A., S.R.L. y cooperativas
- Ley del Impuesto de Sociedades

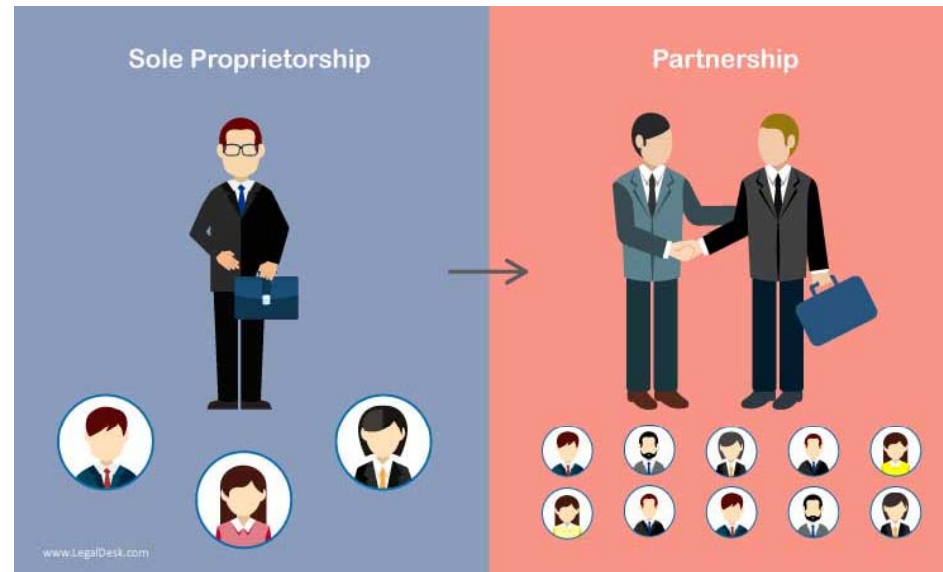
Official Accountancy Body:  
Instituto de Contabilidad y  
Auditoría de Cuentas-ICAC

# Types of firms according to their legal basis

## Sole proprietorship

## Partnerships / Corporations

- Different types depending on the country
- Usually differ in the liability of the partners and their legal entity



# Sole proprietorship

## Advantages

- Simplicity
- No minimum capital

## Disadvantages

- Unlimited liability
  - Some types have limited liability
- Tax arrangements





# Partnerships / Corporations

Based on a contract by which individuals agree to join resources and share profits

## Advantages:

- Bigger size: economies of scale
- Easier access to finance

## Three basic types

- Partnership
- Limited Liability Company
- Corporation



# Type of firms according to the ownership

**Private**

**Public**

**Cooperatives**

# Government based companies

**Their goal is to achieve the public good**

- Correction of market failures
- Monopolies
- Stimulate demand

**Their objective is not necessarily monetary profits**



# Cooperative

**Capital is owned by the workers**

**The objective is not to maximize profit**

**Democratic: one person, one vote**

**There are no capitalists**

## **Advantages**

- Fiscal
- Limited liability

## **Disadvantages**

- Minimum number of partners



# Objectives of the firm

## Maximization vs. Satisfaction

- Profitability
- Sales
- Shareholder value
- Competitive prices
- Market share
- Social benefits

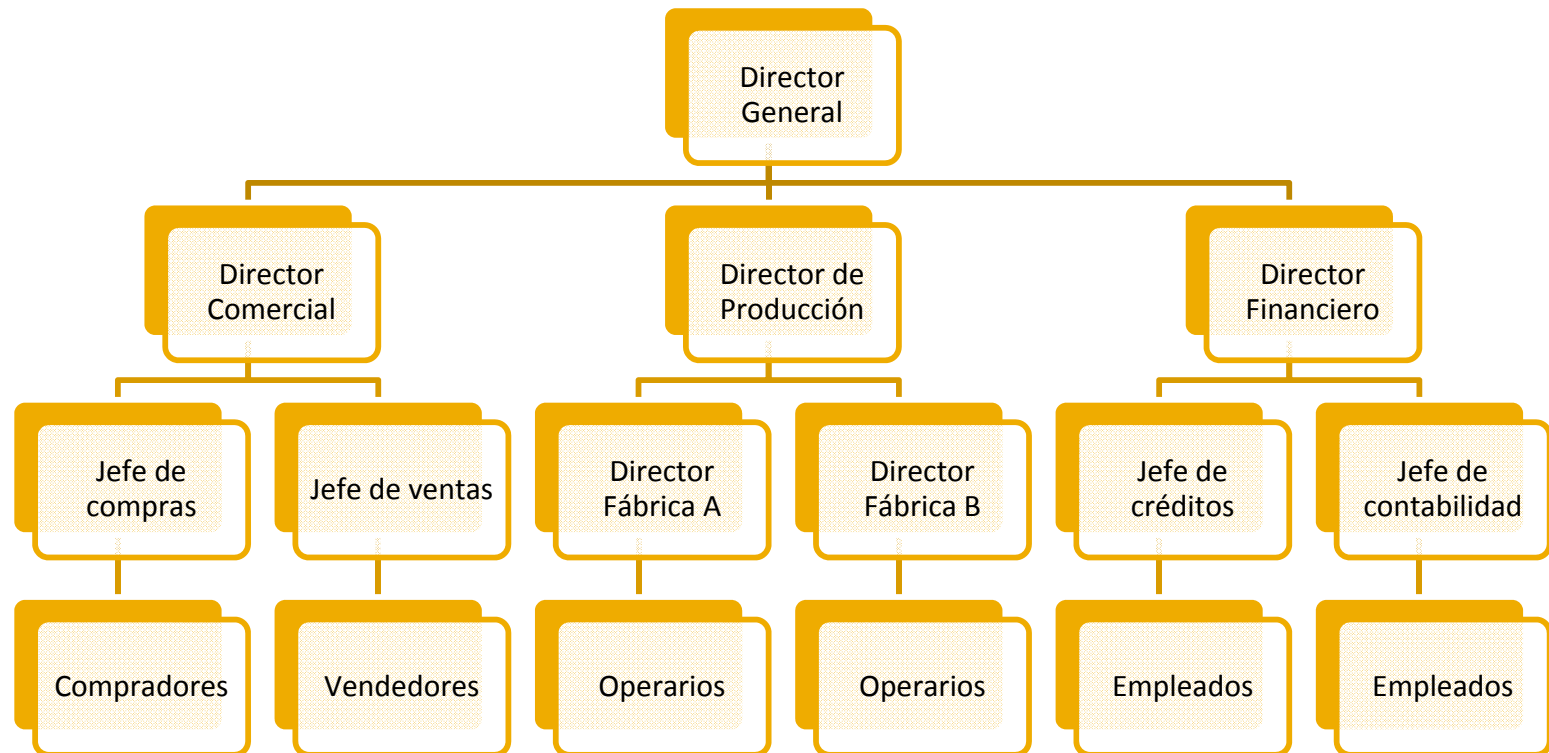


# Linear

Strong hierarchy

Clarity in command

Slowness and bureaucratization



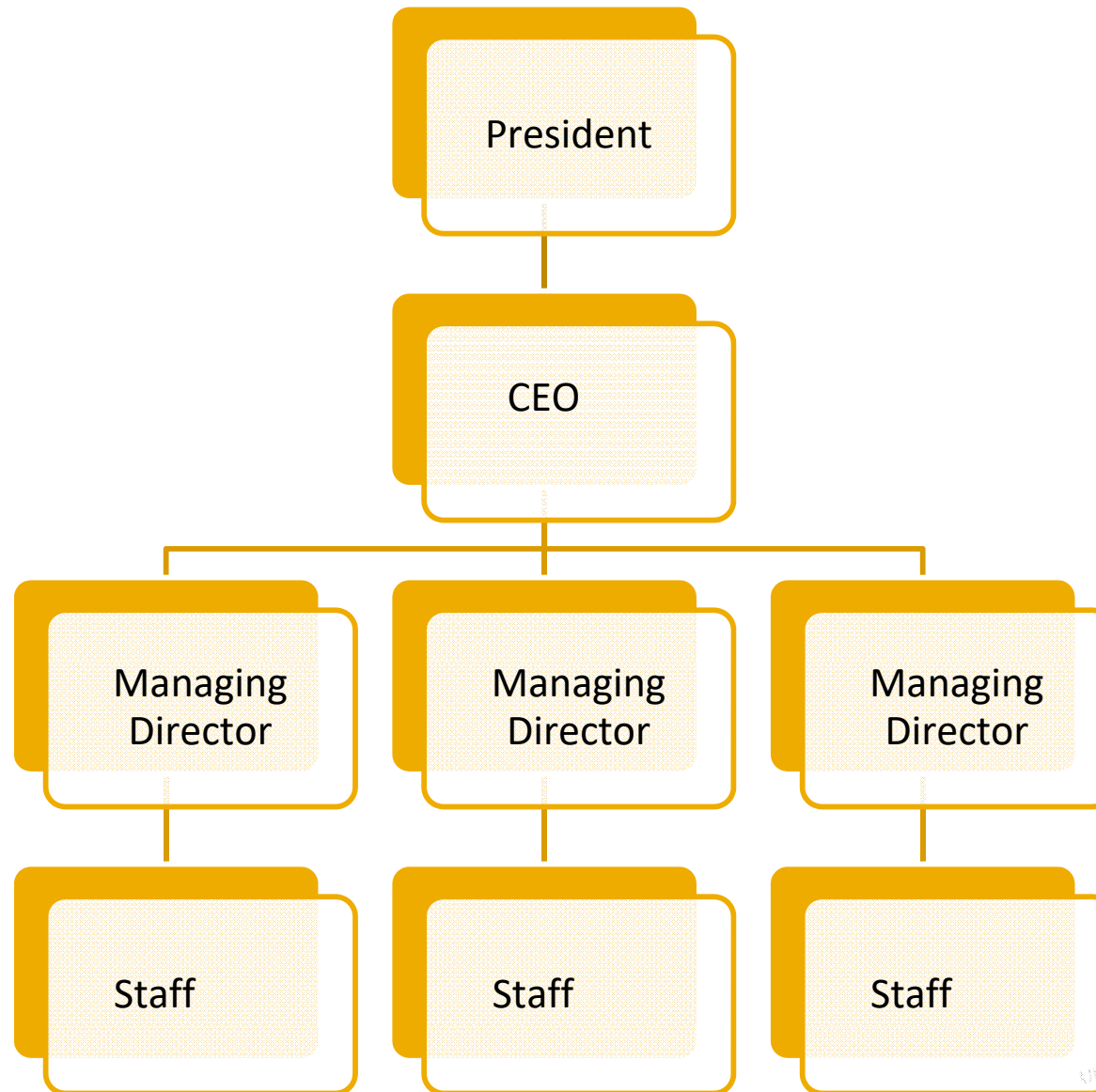


# Functional

Division by activities

Division of labor

Complex structure



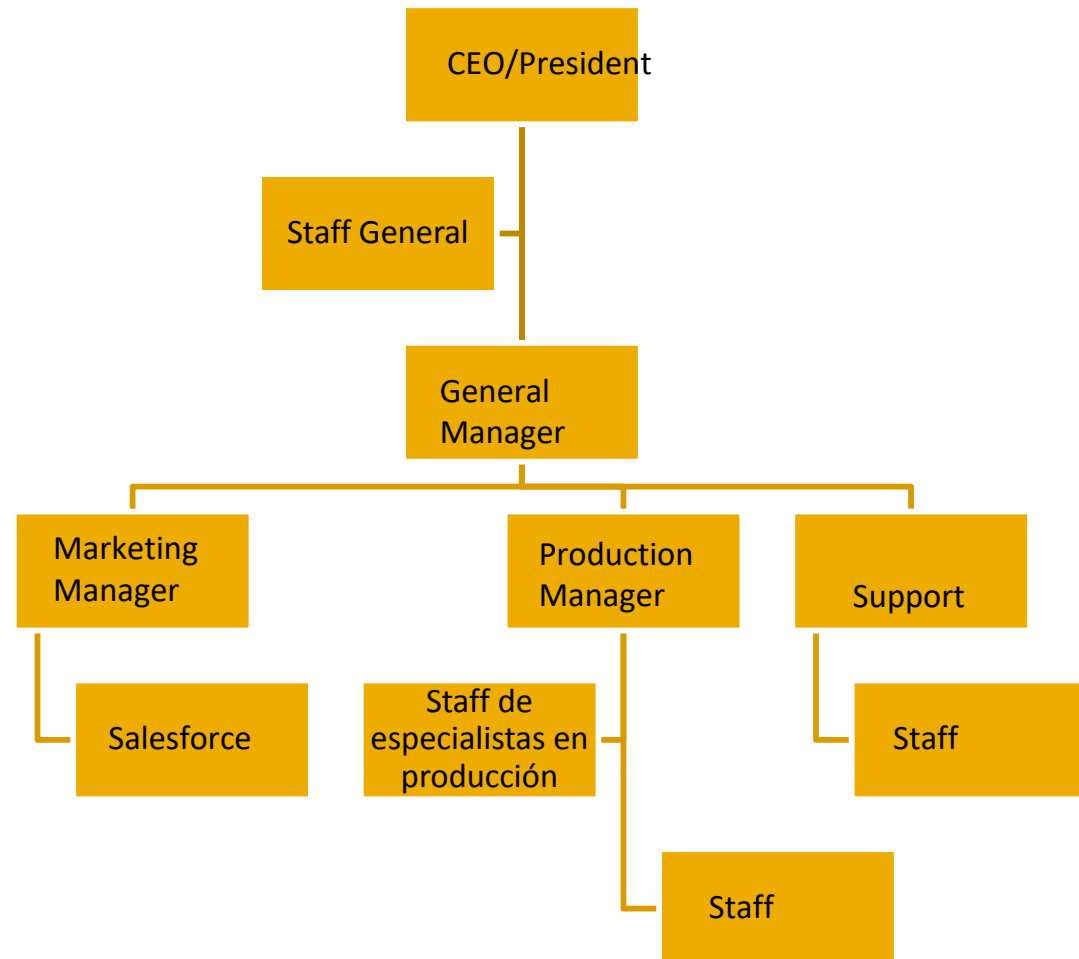


# Mixed

Combines line (hierarchy) / staff (advising)

Quick communications

Lack of authority of staff



# Committees

Group decisions

Compliance with decisions is higher

Loss of time, dilution of responsibilities

Never “pure”, combined with others

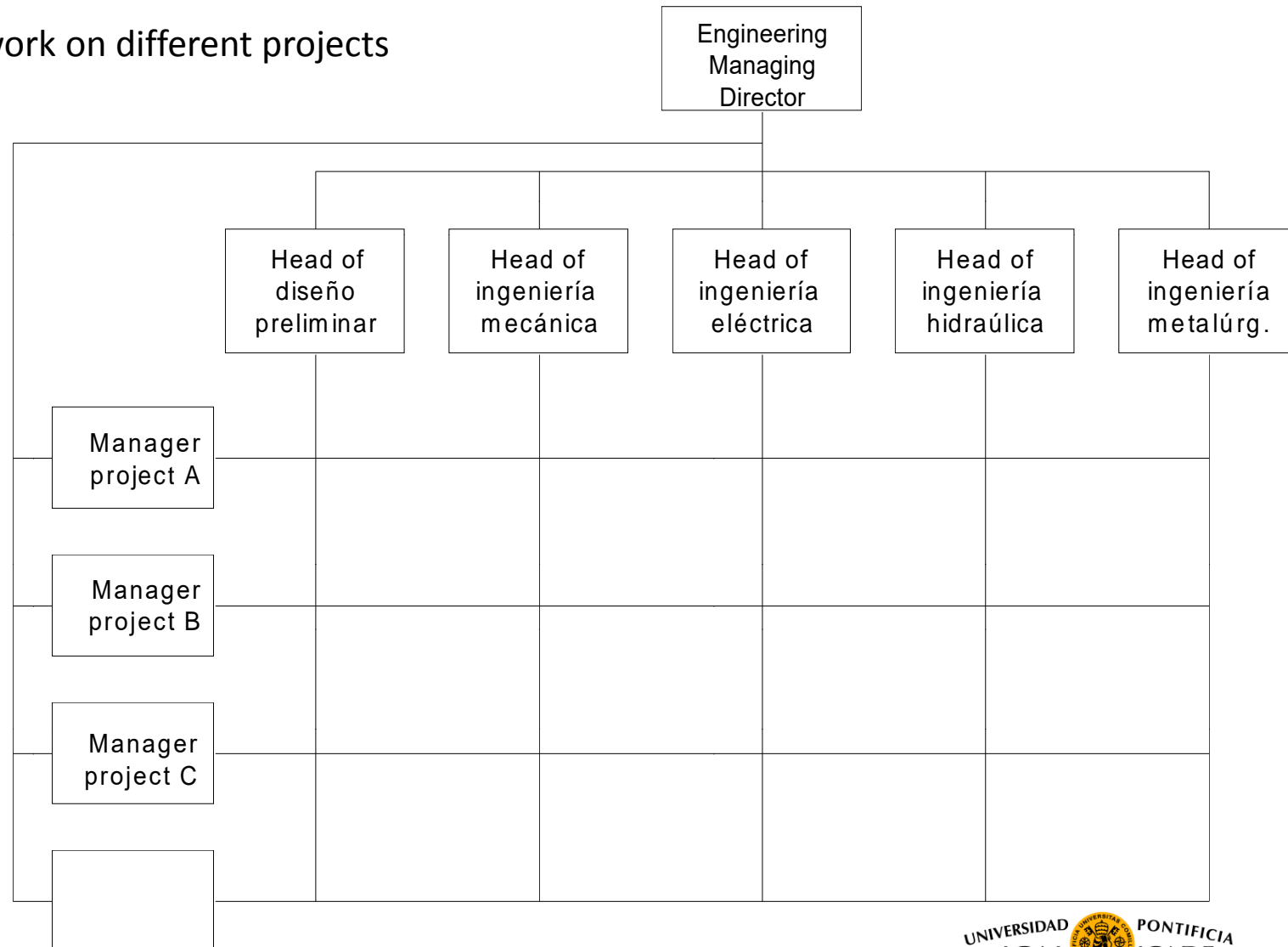


# Matrix

Specialists in different parts work on different projects

Flexibility

Lack of integration



# Functions of the firm

Production

Commercial

Financial

Others

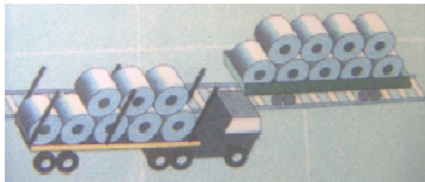
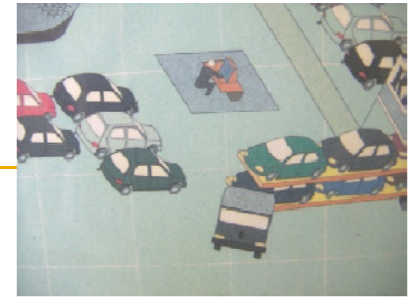


# Production function

## Creating value added

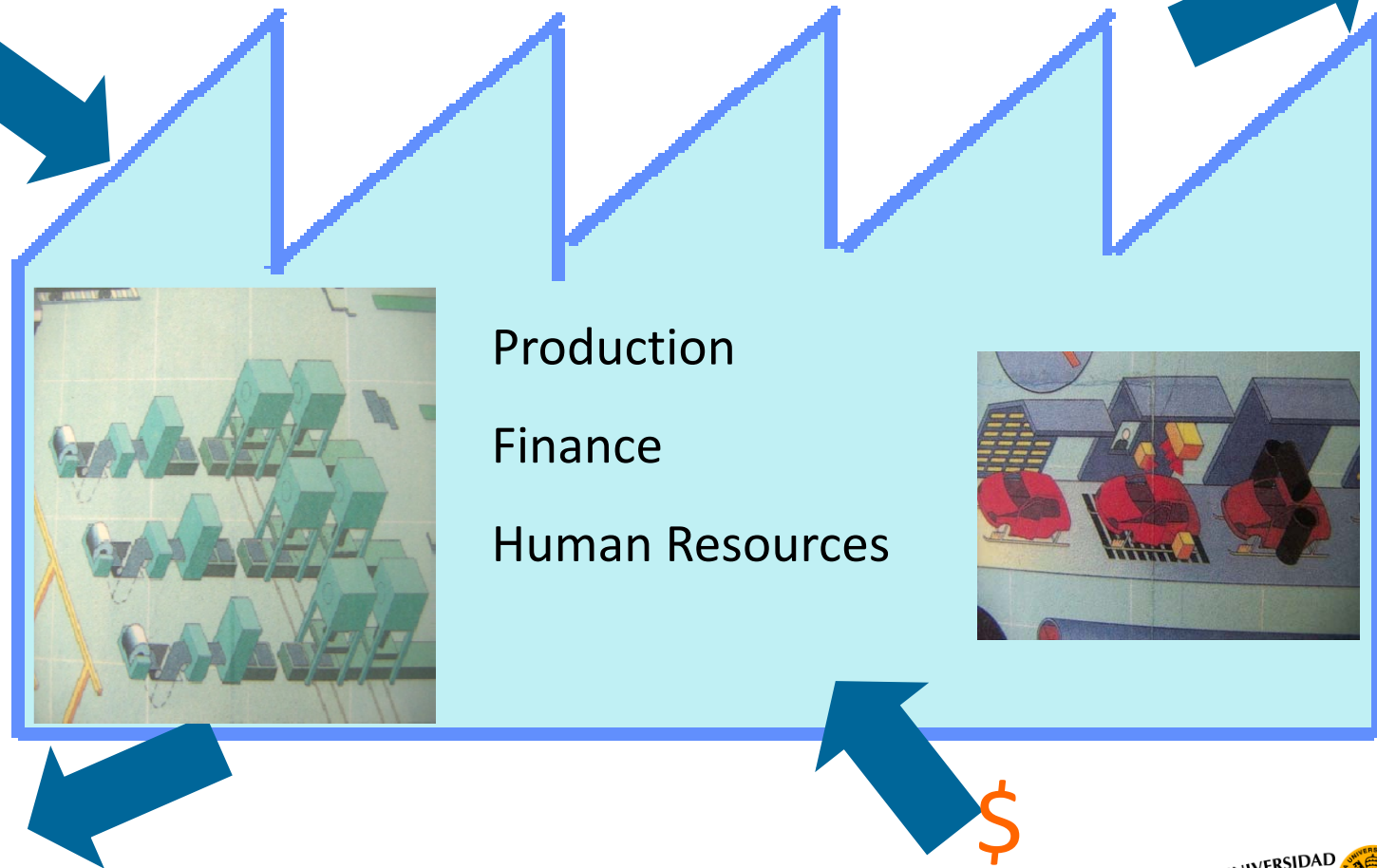


# The firm: an open system of production



Supply

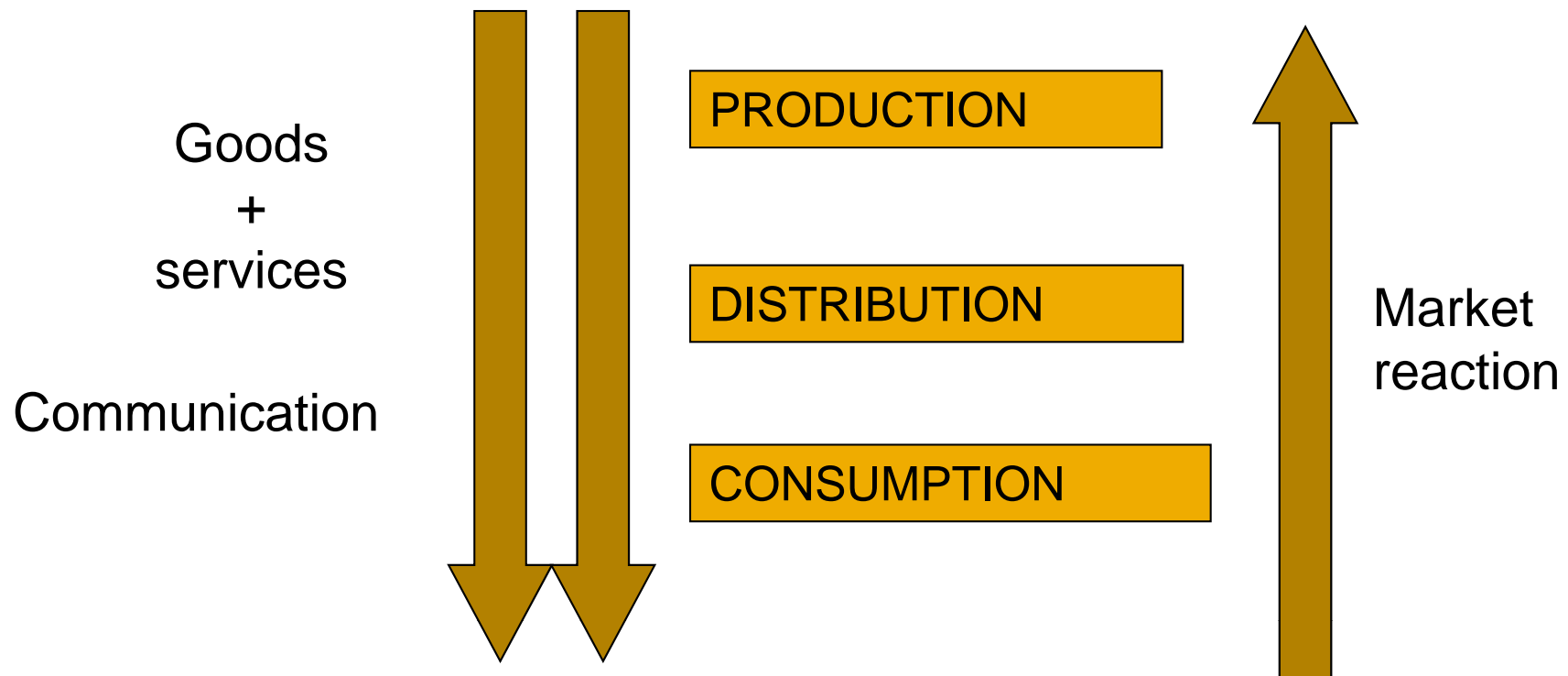
Distribution



# Sales function

Key issue in a market economy

Links productive system and consumers



# Basic areas of finance

Finance department is a key enabler of a Business

1

## Corporate finance = Business Finance

- What long-term investments should the firm take on?
- Where will we get the long-term financing to pay for the investments?
- How will we manage the everyday financial activities of the firm?

2

## Investments

- Work with financial assets such as stocks and bonds
- Value of financial assets, risk versus return, and asset allocation

3

## Financial institutions (companies that specialize in financial matters)

- Banks—commercial and investment, credit unions, savings and loans
- Insurance companies
- Brokerage firms

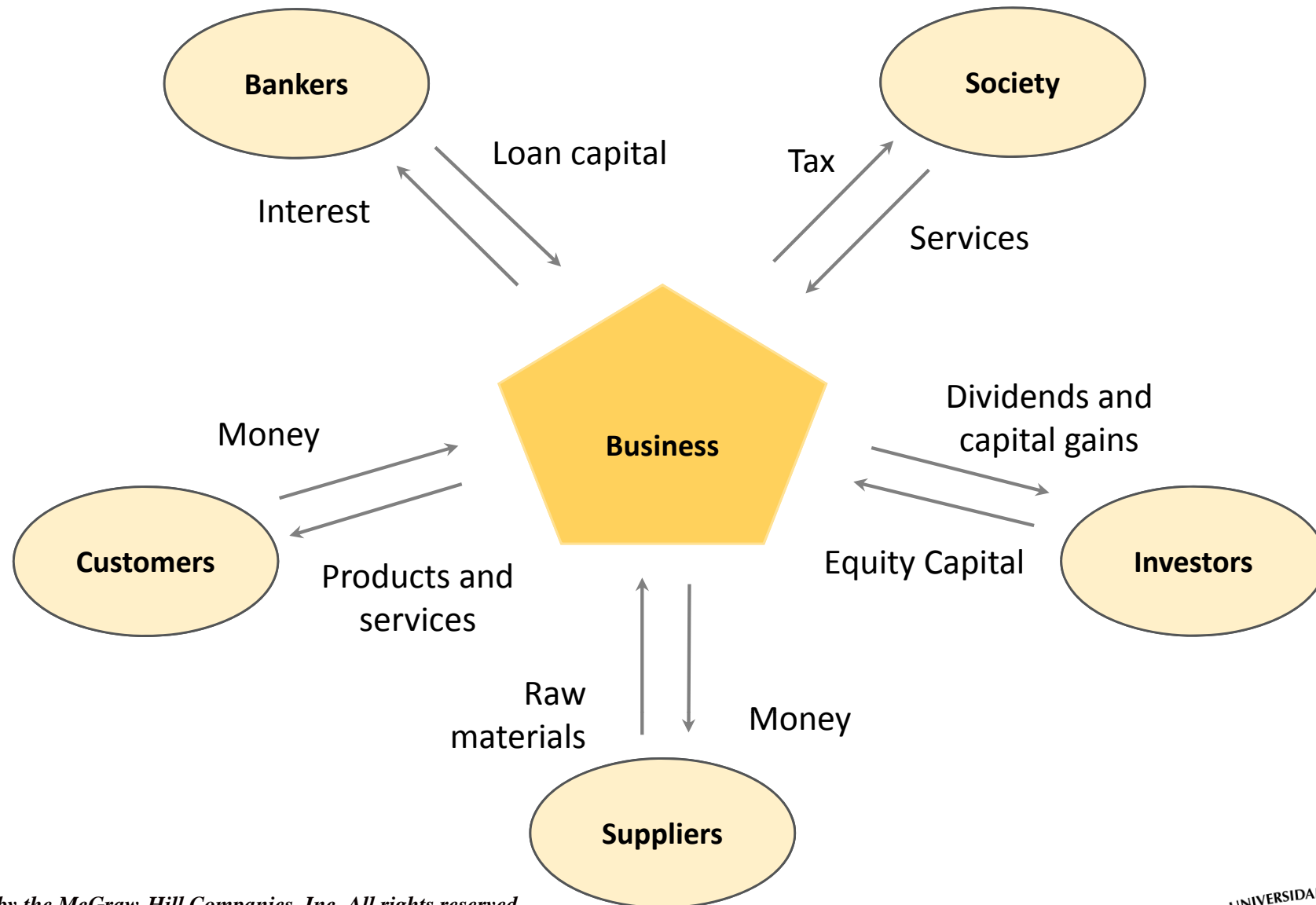
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## International finance

- Need to be familiar with exchange rates and political risk
- Need to understand the customs of other countries



# Businesses operate in an ecosystem in which they make exchanges with different players

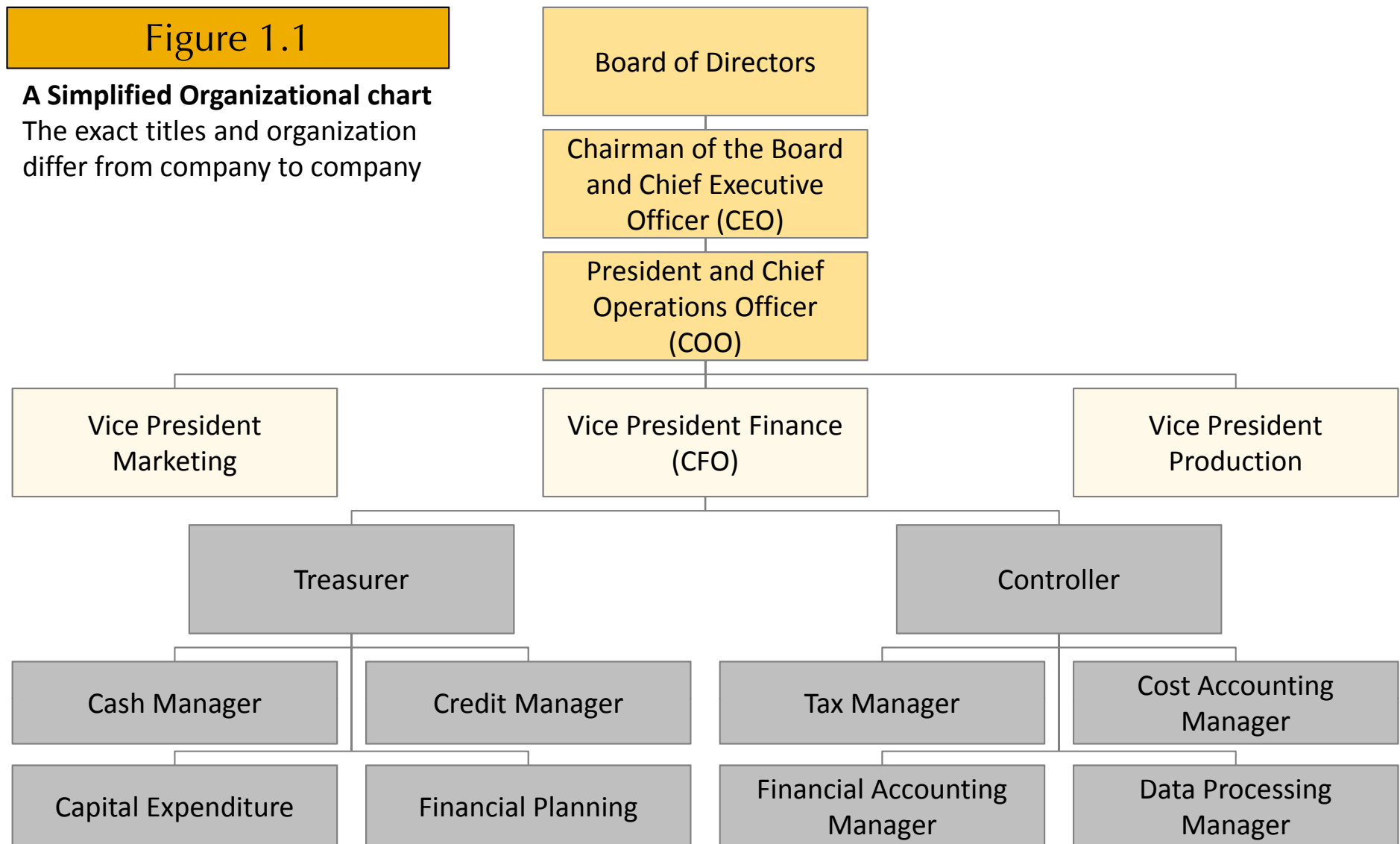


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# Business finance and the financial manager

**Figure 1.1**

**A Simplified Organizational chart**  
The exact titles and organization differ from company to company



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# The financial manager

## The Chief Financial Officer (CFO)

- Treasurer— oversees cash management, credit management, capital expenditures, and financial planning
- Controller—oversees taxes, cost accounting, financial accounting, and data processing

## Financial management decisions

- Capital budgeting: Long-term investments or projects to be taken on
- Capital structure: Pay for our assets and use debt or equity
- Working capital management: The day-to-day finances of the firm

# The goal of financial management

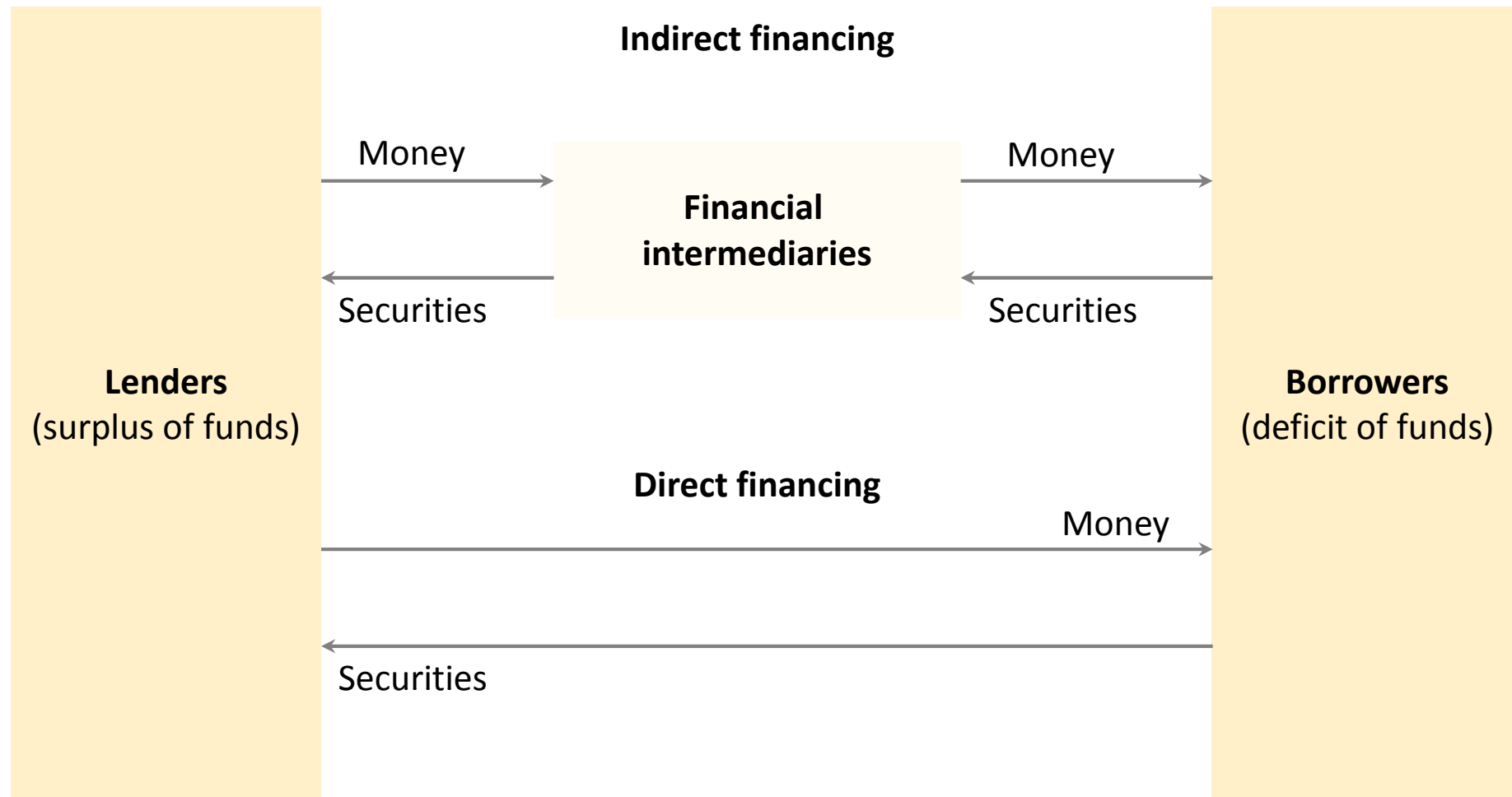
## The goal of a corporation

- Maximize profit?
- Minimize costs?
- Maximize market share?
- Maximize the current value per share of the company's existing stock
- Maximize the market value of the existing owner's equity

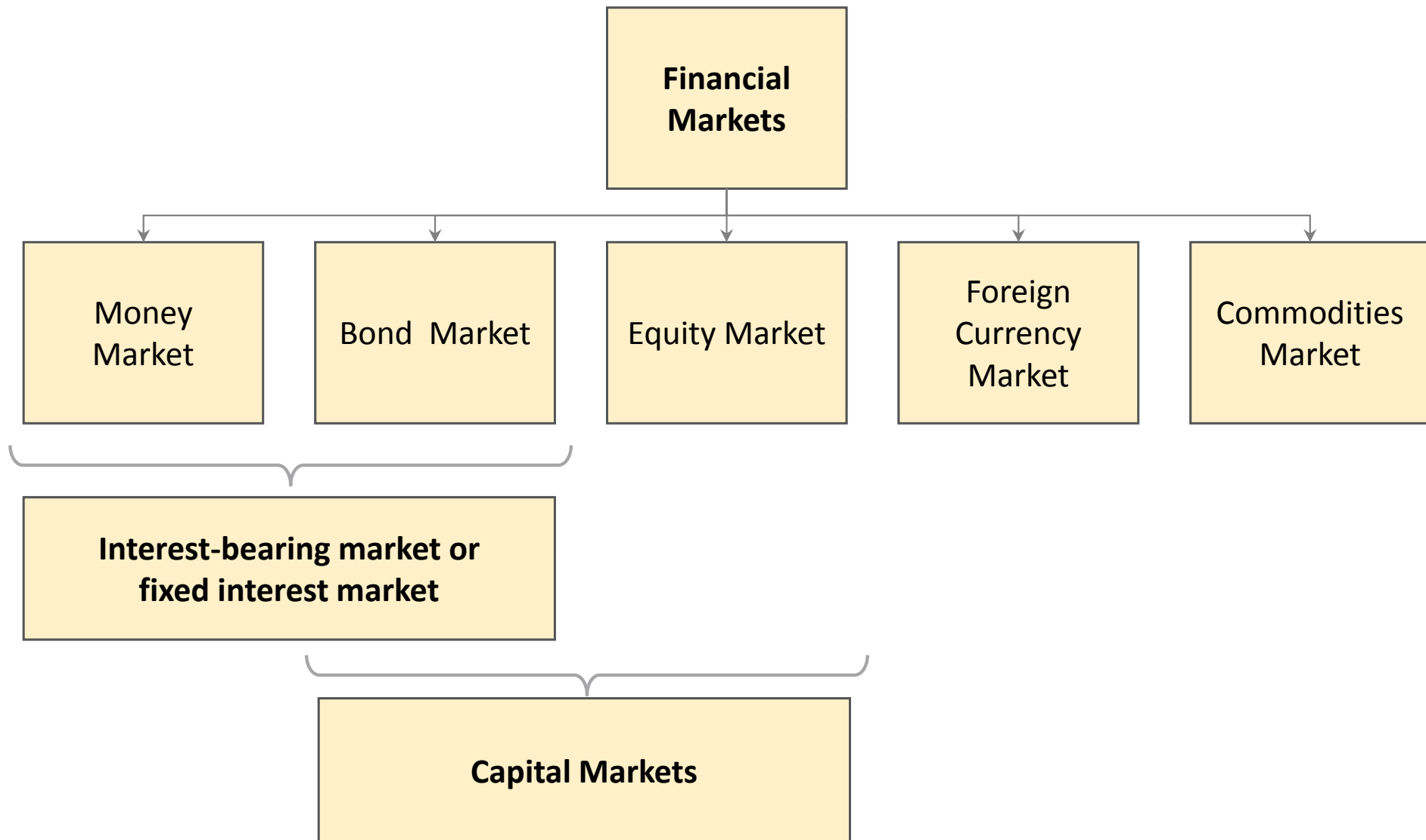
**This does not mean we should do anything and everything to maximize owner wealth**

- Outsourcing?
- Off-shoring?
- Enron?
- Corporate support of charities?

# Lenders, borrowers and financial institutions



# Financial markets



# Thank you

**Escuela Técnica Superior de Ingeniería ICAI**

Alberto Aguilera, 25  
28015 Madrid  
Tel +34 91 542 28 00  
info@icai.upcomillas.es

[www.upcomillas.es](http://www.upcomillas.es)

