

PRINCIPLES OF FINANCE 2





LEARNING JOURNAL UNIT 5

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Obtaining financing is an essential process that makes economic growth possible by allowing businesses and individuals to access capital to fund operations, make purchases, or invest beyond their current means. Financial institutions like banks play a crucial role in providing money to companies, consumers, and investors so they can acquire goods and services that would otherwise be out of reach. This system of financing fuels business activities and consumer spending, enabling organizations to expand and individuals to afford large purchases they could not immediately pay for with cash on hand. Overall, access to outside funds acts as a catalyst that drives economic activity and development across all sectors (Hayes, 2023).

Working capital financing is critical for companies to support investments in short-term assets like inventory and accounts receivable. Common sources include revolving credit facilities, accounts receivable financing, inventory financing arrangements, and short-term loans or lines of credit. These allow flexibility in funding operating asset needs on a dynamic basis. Banks often provide such short-term secured lending based on strength of receivables and inventory. Additionally, fintech platforms now offer quick working capital loans by digitally assessing sales and collateral. These financing options can be tapped on-demand to manage daily cash flow needs related to short-term assets.

In contrast, long-term assets like technology systems, factories, machinery, and equipment have multi-year productive lives. Their substantial capital costs require appropriate long-term financing sources. Businesses often issue corporate bonds or take out long-term installment loans from banks to fund such expensive, long-lived assets while matching the financing tenure. Also, they may lease long-term assets rather than owning them outright. Leasing provides alternative financing as rental installments efficiently align with the assets'

useful lives. Moreover, equity offerings allow businesses to raise expansion and modernization capital which delivers gains over extended periods. Hence, long-term debt and equity instruments suit the longevity of physical and strategic capital assets.

In summary, working capital financing through short-term credit sources appropriately funds fluctuating short-term operating assets. Meanwhile, long-term assets warrant financing via instruments like bonds, term loans, leases and equity which align with multi-year capital investment horizons. Structuring finance tenures based on asset lifetimes ensures stability. Businesses must strategically optimize such financing blends to support asset mixes tailored to growth strategies.

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Reference:

Hayes, A. (2023, June 8). Financing: What it means and why it matters. Investopedia.
<https://www.investopedia.com/terms/f/financing.asp>