in raising capital efficiently
→ CG positive impact on share price
→ provides proper incentives to the manager to achieve corporate objectives
→ minimize wastage, corruption, risk & mismanagement
→ brand formation

Financial Management
→ deals with procurement of funds & effective utilisation
→ planning, organising, directing & controlling financial activities
→ financial decision making

Why is it req?
→ needs finance to meet their requirement
→ lifeblood of business organisations

finance
→ art & science of managing money
→ provision of money at the time when it is needed.

Public finance → individual private company
Private finance

Objectives of FM:
→ adequate return to shareholders

→ optimum fund utilisation
→ safety on investment
→ sound capital structure.
↳ debt & equity balance.

Evolution of FM
→ three phases
⇒ traditional phase.
⇒ transitional.
→ modern

Traditional phase.
→ upto 1950
→ focus was on certain activities like issuance of capital, expansion, liquidation
→

Transitional phase
→ started in mid 50
→ rational matching of fun is required
→ emphasis on daily to day activities

Modern phase
→ management decision making dominant
→ role of FM widens to include product dev, market expansion, procurement

Funcn of fm
→ procure funds
→ Look at financial impacts of firms' services
→ coordinate with all activities

→ Procure fund.
→ optimal source of funds
→ max return to shareholders.

→ Key decisions to be made by fin mangers.
→ Size of firm
→ assets are equired
→ pattern of funds to be raised

→ Investment decis
→ financing
→ Dividend

Investment decis
→ determination of total assets
→ bearing risk.
→ composition of assets
→ proper utilisation of resources.

↳ Long-term investment decis
↳ Short term investment decis
↳ capital budgeting
↳ working capital mgmt

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→ Long term investment decision / Capital budgeting decision

Impact → (benefit) to the firm over a long period of time exceeding one year

→ setting up new plant
→ expansion of current plant
→ replacement of existing machinery
→ reallocation of funds in case investments do not fetch results as per expectation
→ acquisition of another firm
→ merger of firm with group compan.
→ producing a new product
→ buy an asset.

→ Investment projects are worth more than their cost

$$NPV > 0$$

Net Present value > 0

Adopting such projects increase the value of firms

→ Capital budgeting decision involves

Project evaluation →
- → determining size of benefit
- → Timing of benefit
- → Risk associated with benefits

→ Case Study
→ (SWOT Analysis of a company)

→ Boeing 757-767 in 1992
→ (3) bn $
1997 → (8) $bn $
↓ proje

→ Walt Disney
1992 → Disneyland in Paris for 2bn $
1994, loss - $200 m

Importance of capital budgeting
→ Huge Investments.
→ large amount of funds, fund avl are limited.
→ long term
→ permanent in nature, financial risk in the investment decision are more.
→ Irreversible
→ they can be change
→ reversing will result in huge losses
→ long-term effect
→ increases the revenue in the long run.

Capital Budgeting Process

1→ Identification of investment proposals
→ various investment Proposals
2→ Screening the proposals
→ avl resources VS investment cost
3→ Evaluation
→ Payback Period, NPV, Accounting rate of return, IRR.
4→ Final Project

→ Independent → dependent → Exclusive
→ which projects will give more profit

4→ Final Approval -
→ profitability, viability, market condition

5→ Implementing

6→ Performance review of feedback

7→ Methods of Capital Budgeting Evaluation

Traditional method.	Modern method.
└ Accounting rate of return.	→ Net present val
└ Payback period	→ Internal rate of return.
	→ Profitability Index

Payback Period
→ Time required to cover initial investment in a project

Payback Period = Initial Investment / Annual Cash flows

Accept / reject criteria
actual payback period is less than pre-determined pay back period, project would be accepted, would be rejected

Demerits
→ ignores true value of money
→ ignores cash inflow after payback period

100 cr → Initial Investment

25 cr → Annual cash inflow

⇒ Payback Period = $\frac{\text{Initial Invest.}}{\text{Annual cash inflow}}$

0 | 1 2 3 4
100 | 25, 25, 25, 25
cr

$= 4$

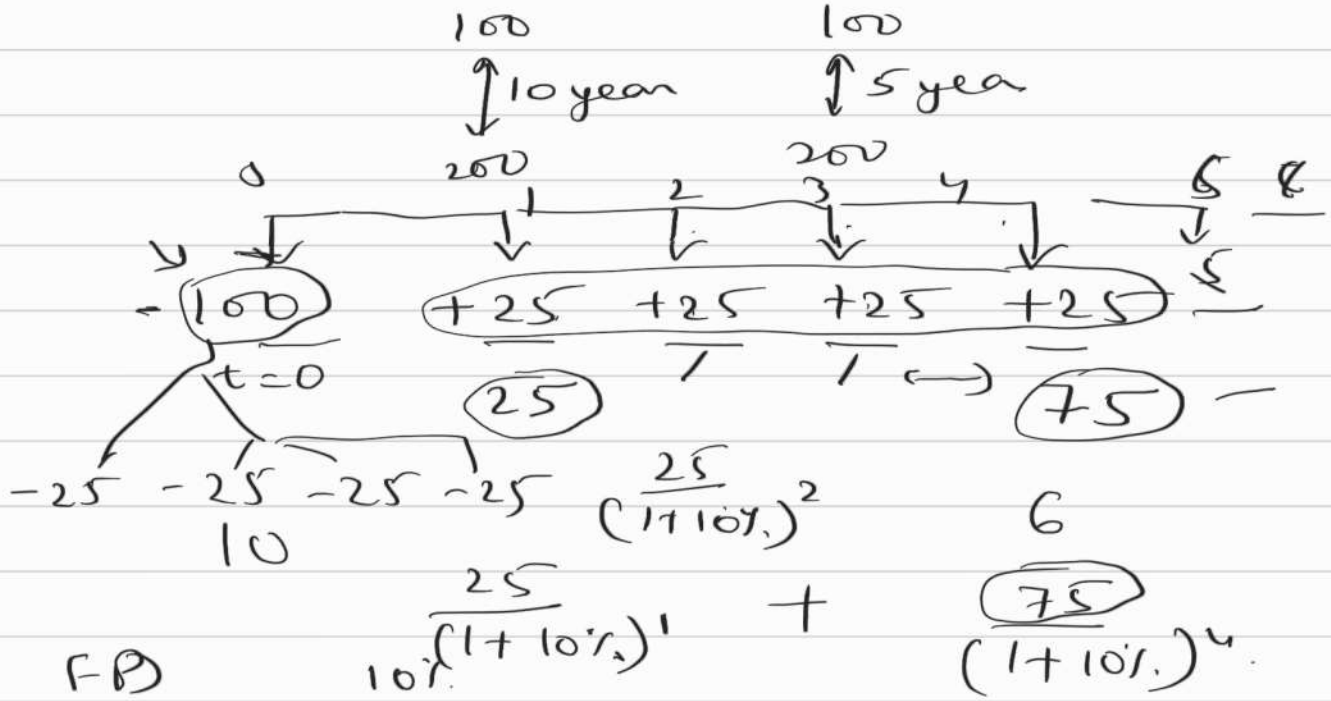
3 | 5

⇒ time value of money.

↳ 100 ↕ 10 year → 200

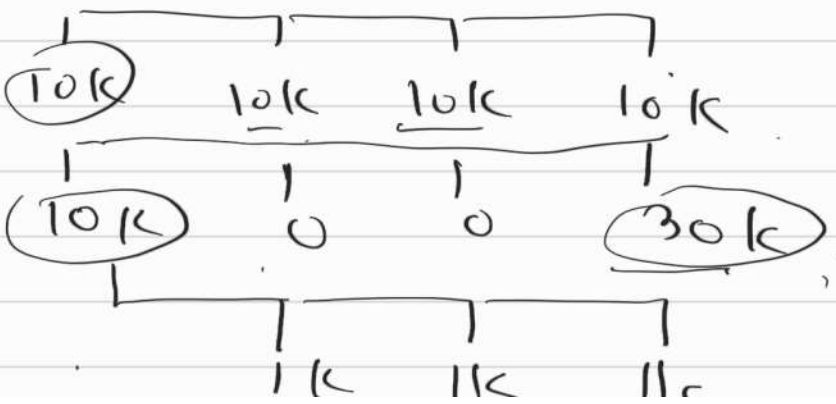
100 ↕ 5 year → 200

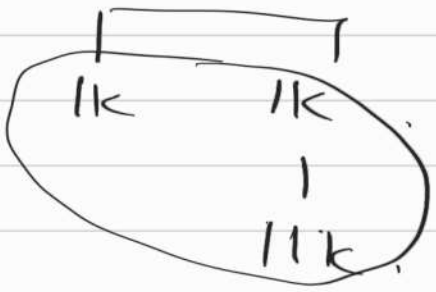
⇒ each cash flow after 4 years.



FD

1 Lakh.





→ Cumulative →
→ Non-cumulative

→ ignores cash flow after payback period

Accounting rate of return.

= PBT / original investment
↓
Profit before tax

Accept/reject 20%

Project ARR > 20% Accepted Rejected

→ ignores + ive value of money
→ ignores reinvestment potential of project.
→ accounting treatment could be diff

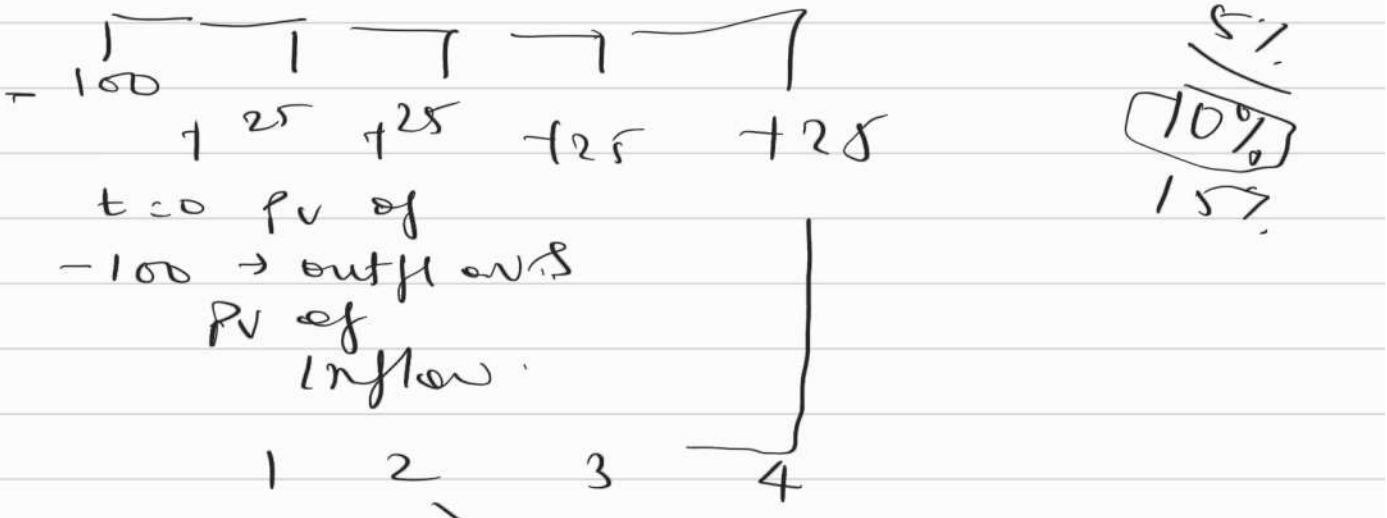
Net Present value. (NPV)

→ difference b/w total present value of future cash inflows & total PV of futm cash outflows
→ Time value of money is being consider.
→ total cash flow of the project
→ for mutualy exclusive project it is the best method

→ gives idea abt total benefit to shareholders

Demerits

→ different to understand & calculate
→ need discount factor for calculation of PV.
→ Return on the project

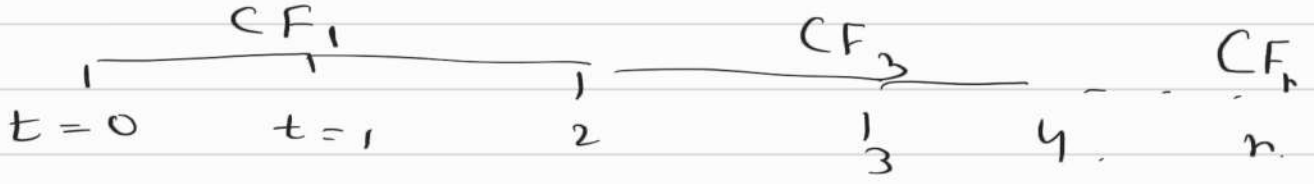


$$\frac{25}{(1+10\%)} \quad \frac{25}{(1+10\%)^2} \quad \frac{25}{(1+10\%)^3} \quad \frac{25}{(1+10\%)^4}$$

$\left(\frac{25}{1.1}\right)$

20 18 16 13

PV of 62 cr → outflow at 1
-100 → PV of out
-38



PV of cash flow at time n

$$= \frac{CF_n}{(1+D.f)^n}$$

total PV of cash flow

$$= \sum_{i=1}^{n} \frac{CF_n}{(1+D.f.)^n} - I_{nvt}$$

Investment

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Internal Rate of Return

→ IRR.

→ it is the rate at which when you discount cash flows the NPV of cash flows becomes zero.

Benefits

→ It incorporates the value of money

→ it gives you the rate of return on investment.

→ it takes into account total cash flow.

	PR1	PR2	PR3
⇒ NPV	100	200	500
Initial Investment	1000	3000	10000
	10%	6%	5%

Disadvantages

→ Calculation is difficult.

→ assumes that all intermediate cash flows are being invested at IRR

Working Capital Management

→ concerned mgm short term finance of the business

→ improvement in the operating performance of business & helps in meeting short ter fund requirem

→ planning, agauing & controlling the components of WC like cash, inventory, debtors, payables ST loans

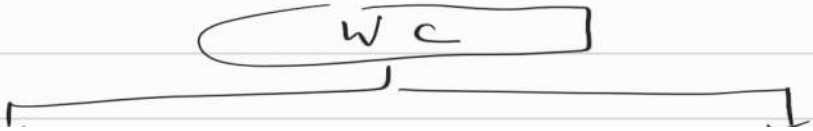
Working capital / short-term capital

→ as part of the funds which is used to meet day to day requirem. of the business.

→ paying salaries
→ purchasing RM.
→ Paying to suppliers

⇒ WC requirement of business
→ WC capital → Sales
↳ factors

→ Gross WC → total capital invested in total current assets of business
→ Net WC → excess of current asset over current liability



current Assets
↳ Cash.
↳ customer bills
↓
Bills receivable
↳ Debtors.
↳ Inventory
↳ Prepaid Expenses.

Current liability
↳ Bills payable
→ creditors
→ Bank OD
→ outstanding Expenses

Need for WC
→ Purchase of RM & spares
→ cash
→ RM & Spares in Stock
↳ Inventory.

→ Payment of wages & salary
→ periodical payment to worker

→ Day to Day Expenses
→ power, fuel, office expenses

→ Provide credit obligation
→ credit facilities to the cust
→ short term obligation / loan

→ causes & effects.
→ Excess WC
→ unnecessary accumulation of RM, component spers
→ creation of bad debts,
→ Inadequate WC.
→ efficiently utilize its assets.
→ risk of return

→ reduce the profit reduce.

Profitability Index = Present discounted value of future cash flows / Initial investment

Profitability Index = $\frac{\text{PV of FCF}}{\text{Initial Investment}} > 1$ (t = 1)

PI is > 1, then it is a good investment

higher the PI, better is the project

Factors determining WC requirements

→ Nature of business
  → Credit period offered
    → WC req will get impacted

→ Production cycle.
  → Production cycle is high, WC req will be high

→ Business cycle.
  → Boom, Contraction
  → when demand is less WC req will reduce.

→ credit Policy

→ if time taken to pay to suppliers increase, WC req. will decrease.

→ if time given to customers to pay increase, WC req will increase

→ Growth & Expansion

→ If growth is high, WC req is high.

→ Avl of RM: If RM is seasonal in nature, WC req will be high

→ Inventory mgmt.

→ Inventory is essential for smooth running of business

→ Proper planning of RM, handling, storing.

→ Kind of Inventories

→ Raw Material (RM)

→ basic form of inventory

→ through the production process is converted into final product.

→ Work in Progress (WIP)

→ which has been used in production, but not converted into FGs

→ Consumables

→ oil, grease

→ Finished Goods (FGs)
→ Final output of the production process.

→ Spares
→ machinery parts.

→ Receivables Management
→ Receivable is the payment/debt owned by Customers to the company arising for Sale of goods & services
→ main obj of receivable managmnt is to promote Sales & profit until that point where return from funding receivable is less that cost of funds.

→ Cost Associated with receivable management
→ collection cost
→ Capital cost
→ Administrative cost
→ Default cost

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FACTORS affecting the receivable size
→ sales level.
→ Credit Policy
→ Credit terms
→ Mangement of Receivables

factors determine size of payables

→ Bargaing Power of firm over Supplier
→ Importance of supplier
→ Supplier credit Policy

→ Financing Decision
→ arrangement of required finance

Quantum of finance
→ nature of business concern.
→ Situation of business concern.

Requirement of finance
→ Long term financial req.

→ Short term " "

Sources of finance
→ Based on the duration / tenure.
→ Long term sources
→ Large amount & repayable over 5 yr period.
Long term sources.
→ Equity, Preference share, Debenture, LT loan
→ short term sources

Short term sources.
→ meet the operation exp of the company.
ST source of finance include.
→ Bank credit, Trade credit,
Money Market Instrument.

→ Based on ownership

→ Share capital,
→ Retained earning
→ Surplus & Profit
} company or shareholder owned.

Borrowed capital
→ Debenture, Bonds

⇒ Based on Source of Generation
Internal sources of finance
→ Retained earning
→ Profit & Surplus.
→ Depreciation.

External.
→ Share capital
→ Debenture.
→ loans.

Features of sources of finance
share
⇒ Equity or Equity shares or common Equity or stock.
⇒ Maturity → no maturity period; cannot be redeemed.
⇒ Residual claim on Income:
→ right to get income left after paying debt holders & preference share holders.
⇒ Residual claim of assets
⇒ Right to control (voting rights)
→ real owners of the company
→ control the mgmt.
→ control operations & take decision

→ Pre-emptive right
→ Limited liability

→ Preference shares.
→ preferential right to get dividend
→ " " at the time of winding up of company
→ may not have voting rights

→ Debentures / loans
→ Maturity → fixed maturity period

→ Claim on Income. → fixed rate of interest in every year.
→ priority on income over equity & preference shareholder.

→ claim on assets

→ No voting rights → no control over the performance of business concern.

Adv of debenture.
→ Long term sources.
→ paid over 10 - 20 year.
→ fixed rate of interest
→ -
→ Income tax deduction
→ Int paid can be deducted from total profit.
→ Tax burden reduces

→ Protective measures

Div →
no. ownership of the company.

⇒ Internal finance

→ Depreciation funds.
→ Retained earning

→ Depreciation funds
→ depreciation of assets over usable life
→ reducing tax burden.
→ Cash in the hands of the company.

Retained Earning
→ part of the total profit after payment of dividend

Loans
→ Long term loans → Fixed deposits, Bank loan
→ Short term loans → Cash credit

⇒ Determine the finance Mix
→ LT source & ST sources of finance
→ Debt & equity

→ Hedging approach
→ Conservative approach
→ Aggressive approach

↳ LT sources → LT assets
ST sources → ST assets

Conservative approach.
→ LT sources → LT, ST assets
ST sources → emergencies
Lower profit, Low risk

Aggressive approach.
→ ST sources → LT, ST assets
↓ Higher profit
Higher risk

⇒ Leverage:
financial leverage.
operating leverage

financial leverage.
⇒ Operating profit / Profit Before tax
(mixx of
→ debt & equity company is using)

⇒ ability of firm to magnify effect of changes in EBIT on EPS

⇒ OP → Earning before Interest & Tax

PBT → OP − Interest.

OP → 100
Interest → 20
PBT → 80

Fin lev = 100/80 = 5/4 = 1.25

200/180 = 10/9 = 1.11

Fin = 100/100 = 1

80/60 = 1.33

OP. $= \frac{200-100}{100} \Rightarrow 100\%$

PBT $= \frac{180-80}{80} = \frac{100}{80} = 125\%$

OP $= \frac{180-100}{100} = \frac{20}{100} = 20\%$

PBT $= \frac{60-80}{20} = \frac{20}{80} = 25\%$

operating leverage:

⇒ percentage change in profit
" Change in sales

$= \frac{\%\text{ change in Profit}}{\%\text{ change in sales}}$

⇒ Dividend Decision

→ How profits of the company will be used.

→ pay dividend from profit
→ reinvest money in busines

Frequency of Decision FM

LT → capital budgeting → Occasional
ST → WC decision → Regular → Daily
→ Dividend → Regular → Half Annual

Relevant groups for financial decision making

→ Shareholders
→ Debt Investors
→ Employees
→ Custom / Suppliers
→ Public
→ Govt.

Goals of Financial Decision Making
→ defined goal.
→ Target oriented goal.
→ Maximizing or minimizing
profit, sales, Return on Inv
cost,

Key objectives of FM
→ Profit Maximization
→ increase profitability.
→ profit focus.
→ ST focus.
→ does not consider risk
→ Wealth Maximization
→ maximize the value of wealth
of shareholders.
→ share price focus.
→ LT focus.
→ consider risk

Risk & Return
Risk → variability of expected return
Return → total gain or loss expected over
a particular period
more certain the return less is

the risk

Risk return tradeoff:

return increase, risk increases

balance between return & risk

Financial system:

- Financial Market
- borrower.
- Investors.
- Intermediaries
- financial assets

Marketing

→ moving goods & services from concept to customer.

marketing mix

4P's → coordination

Product → identification, selection & development

Price → determining price

Place → distribution channel

Promotion → promotional strategy

→ business should be thought of in terms of customer needs & satisfaction.

→ marketing deals with developing demand for product & fulfilling customer needs