Tennessee
TECH

What is finance?

- Finance is a discipline resulting from the application of economic theory to accounting data.

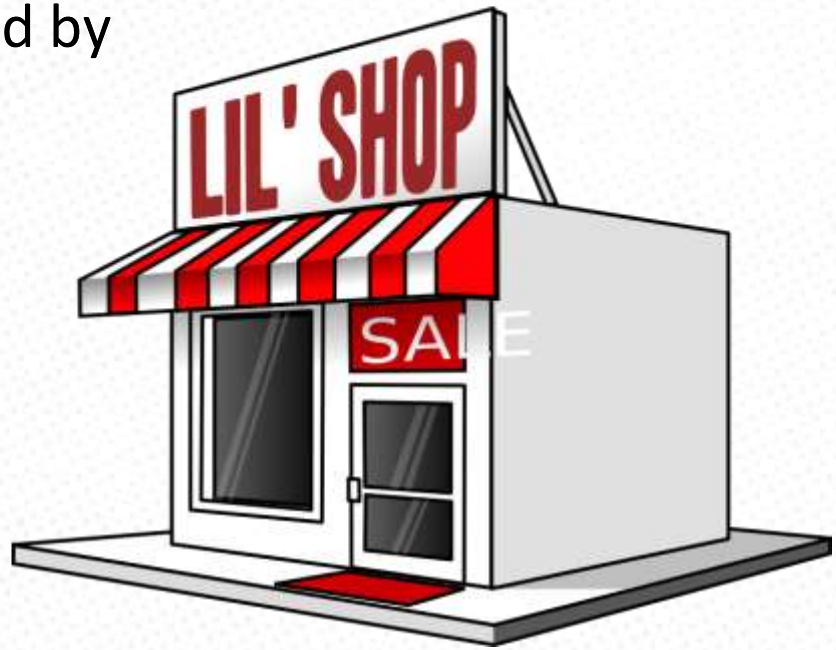
- It deals with the allocation of resources-including acquiring, investing and managing resources.

Fundamental Decisions in Financial Management

- 1. Capital Budgeting decisions: Planning, evaluating, comparing and selecting the long long-term projects of the company
- 2: Financing Decisions: Determine how the firm should pay for its business activities
- 3. Working Capital Management: Determine how the day-to-day will be managed to keep the firm in business

Forms of Business Organization: Sole Proprietorship/Partnership

- Unincorporated business owned by
  - 1 individual (sole proprietor)
  - More than 1 individual (partnership)
- Advantages
  - Easy and independent
  - Few government regulations
  - Lower taxes
- Disadvantages
  - Unlimited personal liability
  - Firm's life=owner's life
  - Difficult to obtain capital



Forms of Business Organization: Corporation

- Legal entity created by a state, separate and distinct from its owners and managers

- Advantages
  - Limits losses to initial investment
  - Unlimited life
  - Easy to transfer shares
  - Easier to raise capital
- Disadvantages
  - Higher taxes-subject to double taxation

From here on, corporations only

The goal of the financial manager

- The primary goal for managers of publicly owned companies is to maximize shareholder value/wealth
- Therefore, the manager's goal should be to maximize the long-run value of a firm's stock
- The long-run value of a firm's stock depends on managerial actions, the economic environment, taxes and the political environment

Intrinsic value versus stock price

- Intrinsic value: estimate of a stock's "true" value using "true" cash flows and "true" risk

- However, no one knows the "true" value or "true" risk.

- A stock's market price is the actual market price which is based on perceived but possibly incorrect cash flow and risk information

- Therefore, **theoretically, the manager's goal is to maximize a firm's intrinsic value but practically the manager's goal is to maximize the stock's long-run market price.**