A

Seminar report

On

Financial Management

Submitted in partial fulfillment of the requirement for the award of degree of MBA

SUBMITTED TO:

www.studymafia.org

SUBMITTED BY:

www.studymafia.org

Acknowledgement

I would like to thank respected Mr…….. and Mr. ……..for giving me such a wonderful opportunity to expand my knowledge for my own branch and giving me guidelines to present a seminar report. It helped me a lot to realize of what we study for.

Secondly, I would like to thank my parents who patiently helped me as i went through my work and helped to modify and eliminate some of the irrelevant or un-necessary stuffs.

Thirdly, I would like to thank my friends who helped me to make my work more organized and well-stacked till the end.

Next, I would thank Microsoft for developing such a wonderful tool like MS Word. It helped my work a lot to remain error-free.

Last but clearly not the least, I would thank The Almighty for giving me strength to complete my report on time.

Preface

I have made this report file on the topic **Financial Management**; I have tried my best to elucidate all the relevant detail to the topic to be included in the report. While in the beginning I have tried to give a general view about this topic.

My efforts and wholehearted co-corporation of each and everyone has ended on a successful note. I express my sincere gratitude to …………..who assisting me throughout the preparation of this topic. I thank him for providing me the reinforcement, confidence and most importantly the track for the topic whenever I needed it.

Introduction

Financial management refers to the efficient and effective management of money (funds) in such a manner as to accomplish the objectives of the organization. It is the specialized function directly associated with the top management. The significance of this function is not seen in the 'Line' but also in the capacity of 'Staff' in overall of a company. It has been defined differently by different experts in the field.

It includes how to raise the capital, how to allocate it i.e. capital budgeting. Not only about long term budgeting but also how to allocate the short term resources like current liabilities. It also deals with the dividend policies of the share holders.

Definitions of Financial Management

- “Financial Management is the Operational Activity of a business that is responsible for obtaining and effectively utilizing the funds necessary for efficient operation.” by Joseph Massie
- “Business finance deals primarily with rising administering and disbursing funds by privately owned business units operating in non-financial fields of industry.” – by Kuldeep Roy
- “Financial Management is an area of financial decision making, harmonizing individual motives and enterprise goals.” By Weston and Brigham
- “Financial management is the area of business management devoted to a judicious use of capital and a careful selection of sources of capital in order to enable a business firm to move in the direction of reaching its goals.” – by J.F.Bradlery
- “Financial management is the application of the planning and control function to the finance function.” – by K.D. Willson
- “Financial management may be defined as that area or set of administrative function in an organization which relate with arrangement of cash and credit so that organization may have the means to carry out its objective as satisfactorily as possible .“ - by Howard & Opton.
- Business finance can be broadly defined as the activity concerned with planning, raising, controlling and administering of funds and in the business. “ by H.G Gathman & H.E Dougall

Financial management is a body of business concerned with the efficient and effective use of either equity capital, borrowed cash or any other business funds as well as taking the right decision for profit maximization and value addition of an entity.- Kepher Petra; Kisii University.

Scope/Elements

1. Investment decisions includes investment in fixed assets (called as capital budgeting). Investment in current assets are also a part of investment decisions called as working capital decisions.
2. Financial decisions - They relate to the raising of finance from various resources which will depend upon decision on type of source, period of financing, cost of financing and the returns thereby.
3. Dividend decision - The finance manager has to take decision with regards to the net profit distribution. Net profits are generally divided into two:

   Dividend for shareholders- Dividend and the rate of it has to be decided.

   Retained profits- Amount of retained profits has to be finalized which will depend upon expansion and diversification plans of the enterprise.

Approaches of Financial Management

The scope and functions of financial management are divided into two broad categories:

Traditional approach.
Modern approach.

Traditional Approach

The traditional approach to the scope of financial management refers to its subject matter in the academic literature in the initial stages of its evolution as a separate branch of study. According to this approach, the scope of financial management is confined to the raising of funds. Hence, the scope of finance was treated by the traditional approach in the narrow sense of procurement of funds by corporate enterprise to meet their financial needs. Since the main emphasis of finance function at that period was on the procurement of funds, the subject was called corporation finance till the mid-1950's and covered discussion on the financial instruments, institutions and practices through which funds are obtained. Further, as the problem of raising funds is more intensely felt at certain episodic events such as merger, liquidation, consolidation, reorganisation and so on. These are the broad features of the subject matter of corporation finance, which has no concern with the decisions of allocating firm's funds. But the scope of finance function in the traditional approach has now been discarded as it suffers from serious criticisms. Again, the limitations of this approach fall into the following categories.

The emphasis in the traditional approach is on the procurement of funds by the corporate enterprises, which was woven around the viewpoint of the suppliers of funds such as investors, financial institutions, investment bankers, etc, i.e. outsiders. It implies that the traditional approach was the outsider-looking-in approach. Another limitation was that internal financial decision-making was completely ignored in this approach.

The second criticism leveled against this traditional approach was that the scope of financial management was confined only to the episodic events such as mergers, acquisitions, reorganizations, consolation, etc. The scope of finance function in this approach was confined to a description of these infrequent happenings in the life of an enterprise. Thus, it places over emphasis on the topics of securities and its markets, without paying any attention on the day to day financial aspects.

Another serious lacuna in the traditional approach was that the focus was on the long-term financial problems thus ignoring the importance of the working capital management. Thus, this approach has failed to consider the routine managerial problems relating to finance of the firm.

During the initial stages of development, financial management was dominated by the traditional approach as is evident from the finance books of early days. The tradi-tional approach was found in the first manifestation by Green's book written in 1897, Meades on Corporation Finance, in 1910; Doing's on Corporate Promotion and Reorganisation, in 1914, etc.

As stated earlier, in this traditional approach all these writings emphasized the finan-cial problems from the outsiders' point of view instead of looking into the problems from managements, point of view. It over emphasized long-term financing lacked in analytical content and placed heavy emphasis on descriptive material. Thus, the traditional approach omits the discussion on the important aspects like cost of the capital, optimum capital structure, valuation of firm, etc. In the absence of these crucial aspects in the finance function, the traditional approach implied a very narrow scope of financial management. The modern or new approach provides a solution to all these aspects of financial management.

Modern Approach

After the 1950's, a number of economic and environmental factors, such as the technological innovations, industrialization, intense competition, interference of government, growth of population, necessitated efficient and effective utilisation of financial resources. In this context, the optimum allocation of the firm's resources is the order of the day to the management. Then the emphasis shifted from episodic financing to the managerial financial problems, from raising of funds to efficient and effective use of funds. Thus, the broader view of the modern approach of the finance function is the wise use of funds. Since the financial decisions have a great impact on all other business activities, the financial manager should be concerned about deter-mining the size and natuʳe of the technology, setting the direction and growth of the business, shaping the profitability, amount of risk taking, selecting the asset mix, determination of optimum capital structure, etc. The new approach is thus an analyti-cal way of viewing the financial problems of a firm. According to the new approach, the financial management is concerned with the solution of the major areas relating to the financial operations of a firm, viz., investment, and financing and dividend decisions. The modern financial manager has to take financial decisions in the most rational way. These decisions have to be made in such a way that the funds of the firm are used optimally. These decisions are referred to as managerial finance functions since they require special care with extraordinary administrative ability, management skills and decision - making techniques, etc.

Objectives of Financial Management

The financial management is generally concerned with procurement, allocation and control of financial resources of a concern. The objectives can be-

1. To ensure regular and adequate supply of funds to the concern.
2. To ensure adequate returns to the shareholders which will depend upon the earning capacity, market price of the share, expectations of the shareholders.
3. To ensure optimum funds utilization. Once the funds are procured, they should be utilized in maximum possible way at least cost.
4. To ensure safety on investment, i.e, funds should be invested in safe ventures so that adequate rate of return can be achieved.
5. To plan a sound capital structure-There should be sound and fair composition of capital so that a balance is maintained between debt and equity capital.

Goals Of Financial Management

All businesses aim to maximize their profits, minimize their expenses and maximize their market share. Here is a look at each of these goals.

Maximize Profits A company's most important goal is to make money and keep it. Profit-margin ratios are one way to measure how much money a company squeezes from its total revenue or total sales.

There are three key profit-margin ratios: gross profit margin, operating profit margin and net profit margin.

1. Gross Profit Margin

The gross profit margin tells us the profit a company makes on its cost of sales or cost of goods sold. In other words, it indicates how efficiently management uses labor and supplies in the production process.

Gross Profit Margin = (Sales - Cost of Goods Sold)/Sales

Suppose that a company has $1 million in sales and the cost of its labor and materials amounts to $600,000. Its gross margin rate would be 40% ($1 million - $600,000/$1 million).

The gross profit margin is used to analyze how efficiently a company is using its raw materials, labor and manufacturing-related fixed assets to generate profits. A higher margin percentage is a favorable profit indicator.

Gross profit margins can vary drastically from business to business and from industry to industry. For instance, the airline industry has a gross margin of about 5%, while the software industry has a gross margin of about 90%.

2. Operating Profit Margin

By comparing earnings before interest and taxes (EBIT) to sales, operating profit margins show how successful a company's management has been at generating income from the operation of the business:

Operating Profit Margin = EBIT/Sales

If EBIT amounted to $200,000 and sales equaled $1 million, the operating profit margin would be 20%.

This ratio is a rough measure of the operating leverage a company can achieve in the conduct of the operational part of its business. It indicates how much EBIT is generated per dollar of sales. High operating profits can mean the company has effective control of costs, or that sales are increasing faster than operating costs. Positive and negative trends in this ratio are, for the most part, directly attributable to management decisions.

Because the operating profit margin accounts for not only costs of materials and labor, but also administration and selling costs, it should be a much smaller figure than the gross margin.

3. Net Profit Margin

Net profit margins are those generated from all phases of a business, including taxes. In other words, this ratio compares net income with sales. It comes as close as possible to summing up in a single figure how effectively managers run the business:

Net Profit Margins = Net Profits after Taxes/Sales

If a company generates after-tax earnings of $100,000 on its $1 million of sales, then its net margin amounts to 10%.

Often referred to simply as a company's profit margin, the so-called bottom line is the most often mentioned when discussing a company's profitability.

Again, just like gross and operating profit margins, net margins vary between industries. By comparing a company's gross and net margins, we can get a good sense of its non-production and non-direct costs like administration, finance and marketing costs.

For example, the international airline industry has a gross margin of just 5%. Its net margin is just a tad lower, at about 4%. On the other hand, discount airline companies have much higher gross and net margin numbers. These differences provide some insight into these industries' distinct cost structures: compared to its bigger, international cousins, the discount airline industry spends proportionately more on things like finance, administration and marketing, and proportionately less on items such as fuel and flight crew salaries.

In the software business, gross margins are very high, while net profit margins are considerably lower. This shows that marketing and administration costs in this industry are very high, while cost of sales and operating costs are relatively low.

When a company has a high profit margin, it usually means that it also has one or more advantages over its competition. Companies with high net profit margins have a bigger cushion to protect themselves during the hard times. Companies with low profit margins can get wiped out in a downturn. And companies with profit margins reflecting a competitive advantage are able to improve their market share during the hard times, leaving them even better positioned when things improve again.

Like all ratios, margin ratios never offer perfect information. They are only as good as the timeliness and accuracy of the financial data that gets fed into them, and analyzing them also depends on a consideration of the company's industry and its position in the business cycle. Margins tell us a lot about a company's prospects, but not the whole story.

Minimize Costs

Companies use cost controls to manage and/or reduce their business expenses. By identifying and evaluating all of the business's expenses, management can determine whether those costs are reasonable and affordable. Then, if necessary, they can look for ways to reduce costs through methods such as cutting back, moving to a less expensive plan or changing service providers. The cost-control process seeks to manage expenses ranging from phone, internet and utility bills to employee payroll and outside professional services.

To be profitable, companies must not only earn revenues, but also control costs. If costs are too high, profit margins will be too low, making it difficult for a company to succeed against its competitors. In the case of a public company, if costs are too high, the company may find that its share price is depressed and that it is difficult to attract investors.

When examining whether costs are reasonable or unreasonable, it's important to consider industry standards. Many firms examine their costs during the drafting of their annual budgets.

Maximize Market Share

Market share is calculated by taking a company's sales over a given period and dividing it by the total sales of its industry over the same period. This metric provides a general idea of a company's size relative to its market and its competitors. Companies are always looking to expand their share of the market, in addition to trying to grow the size of the total market by appealing to larger demographics, lowering prices or through advertising. Market share increases can allow a company to achieve greater scale in its operations and improve profitability.

The size of a market is always in flux, but the rate of change depends on whether the market is growing or mature. Market share increases and decreases can be a sign of the relative competitiveness of the company's products or services. As the total market for a product or service grows, a company that is maintaining its market share is growing revenues at the same rate as the total market. A company that is growing its market share will be growing its revenues faster than its competitors. Technology companies often operate in a growth market, while consumer goods companies generally operate in a mature market.

New companies that are starting from scratch can experience fast gains in market share. Once a company achieves a large market share, however, it will have a more difficult time growing its sales because there aren't as many potential customers available.

Next we'll take a look at the potential conflicts of interest that can arise in the management of a business's finances.

Profit Maximization or Wealth Maximization

We know that the goals of financial management are profit maximization and wealth maximization. These are the important objectives of business firms. Now the question arises of the choices,

i.e. which should be the goal of decision making be profit maximization or which strengthen the case for wealth maximization as the goal of the business enterprise.

Argument and Counter Argument:

Profits cannot be ascertained well in advance to express the profitability of return as future is uncertain. It is not at possible to maximize what cannot be known.

The executive or the decision maker may not have enough confidence in the estimates of future returns so that he does not attempt future to maximize. It is argued that firm's goal cannot be maximize profits but attain a certain level of profit holding certain shares of the market or certain level of sales.

There must be a balance between the expected return and risk. The possibility of higher expected yields are associated with greater risk to recognize such a balance and wealth maximization is brought in to the analysis. In such cases, higher capitalization rate involves. Such combination of expected returns with risk variations and related capitalization rate cannot be considered in the concept of profit maximization.

The goal of profit maximization is consider being a narrow outlook. Evidently when profit maximization becomes the basis of financial decision of the concern, it ignores the interest of the community on one hand and that of the Govt., workers and other concerned persons in the enterprise on the other hand.

Keeping the above objection in view, most of the thinkers on the subject have come to the conclusion that the aim of an enterprise should be wealth maximization not the profit maximization.

Prof. Solomon of Stanford University has handled the issue very logically. He argues that it is useful to make a distinction between profit and profitability maximization of profit with a view to maximizing the wealth of shares holders is clearly an unreal motive. On the other hand, profitability maximization with a view to using resources to yield economic value higher than the joint values of inputs required is useful goal.

Thus the proper goal of financial management is wealth maximization.

Functions of Financial Management

1. **Estimation of capital requirements:** A finance manager has to make estimation with regards to capital requirements of the company. This will depend upon expected costs and profits and future programmes and policies of a concern. Estimations have to be made in an adequate manner which increases earning capacity of enterprise.
2. **Determination of capital composition:** Once the estimation have been made, the capital structure have to be decided. This involves short- term and long- term debt equity analysis. This will depend upon the proportion of equity capital a company is possessing and additional funds which have to be raised from outside parties.
3. **Choice of sources of funds:** For additional funds to be procured, a company has many choices like-
    a. Issue of shares and debentures
    b. Loans to be taken from banks and financial institutions
    c. Public deposits to be drawn like in form of bonds.

    Choice of factor will depend on relative merits and demerits of each source and period of financing.

4. **Investment of funds:** The finance manager has to decide to allocate funds into profitable ventures so that there is safety on investment and regular returns is possible.
5. **Disposal of surplus:** The net profits decision have to be made by the finance manager. This can be done in two ways:
    a. Dividend declaration - It includes identifying the rate of dividends and other benefits like bonus.
    b. Retained profits - The volume has to be decided which will depend upon expansional, innovational, diversification plans of the company.
6. **Management of cash:** Finance manager has to make decisions with regards to cash management. Cash is required for many purposes like payment of wages and salaries, payment of electricity and water bills, payment to creditors, meeting current liabilities, maintainance of enough stock, purchase of raw materials, etc.
7. **Financial controls:** The finance manager has not only to plan, procure and utilize the funds but he also has to exercise control over finances. This can be done through many techniques like ratio analysis, financial forecasting, cost and profit control, etc.

RELATIONSHIP OF FINANCIAL MANAGEMENT WITH OTHER BRANCHES

Financial management is one of the important parts of overall management, which is directly related with various functional departments like personnel, marketing and production.

Financial management covers wide area with multidimensional approaches.

1. Financial Management and Economics

Economic concepts like micro and macroeconomics are directly applied with the financial management approaches. Investment decisions, micro and macro environmental factors are closely associated with the functions of financial manager. Financial management also uses the economic equations like money value discount factor, economic order quantity etc. Financial economics is one of the emerging area, which provides immense opportunities to finance, and economical areas.

2. Financial Management and Accounting

Accounting records includes the financial information of the business concern.Hence, we can easily understand the relationship between the financial management and accounting. In the olden periods, both financial management and accounting are treated as a same discipline and then it has been merged as Management Accounting because this part is very much helpful to finance manager to take decisions. But nowaday's financial management and accounting discipline are separate and interrelated.

3. Financial Management or Mathematics

Modern approaches of the financial management applied large number of mathematical and statistical tools and techniques. They are also called as econometrics. Economic order quantity, discount factor, time value of money,present value of money, cost of capital, capital structure theories, dividend theories,ratio analysis and working capital analysis are used as mathematical and statistical tools and techniques in the field of financial management.

4. Financial Management and Production Management

Production management is the operational part of the business concern, which helps to multiple the money into profit. Profit of the concern depends upon the production performance. Production performance needs finance, because production department requires raw material, machinery, wages, operating expenses etc. These expenditures are decided and estimated by the financial department and the finance manager allocates the appropriate finance to production department.The financial manager must be aware of the operational process and finance required for each process of production activities.

5. Financial Management and Marketing

Produced goods are sold in the market with innovative and modern approaches.For this, the marketing department needs finance to meet their requirements.The financial manager or finance department is responsible to allocate the adequate finance to the marketing department. Hence, marketing and financial management are interrelated and depends on each other.

6. Financial Management and Human Resource

Financial management is also related with human resource department, which provides manpower to all the functional areas of the management. Financial manager should carefully evaluate the requirement of manpower to each department and allocate the finance to the human resource department as wages,salary, remuneration, commission, bonus, pension and other monetary benefits to the human resource department. Hence, financial management is directly related with human resource management.

Conclusion

The aim of the course is to develop necessary skills and understanding needed to apply appropriate concepts, techniques and approaches for sound decision-making in financial management:To enable students to analyse financial situations and offer solutions to financial management problems.

To understand and apply theoretical concepts to a range of investment and financing decisions.

Learning Outcomes:

On completing this course students should be able to:

Knowledge and understanding of:

How shareholder wealth is created, and the role of financial management in this process.

Investment and valuation process and techniques.

Relationship between risk and return.

Investment and financing decision making process in relation to the role of capital markets and their efficiency.

How to value different sources of long term finance.

Alternative capital structure policies and dividend policies.

Reference

- www.google.com
- www.wikipedia.com
- www.studymafia.org