UNIT - I

CONTENTS

Introduction to finance- Financial Management – Nature, scope and functions of Finance, organization of financial functions, objectives of Financial management, Major financial decisions – Time value of money – features and valuation of shares and bonds – Concept of risk and return – single asset and of a portfolio.

Financial Management

Financial Management may be defined as planning, organizing, directing and controlling of financial activities in an organization.

Financial management is concerned with optimal procurement and effective utilization of funds in a manner that the risk, cost and control considerations are properly balanced in a given situation.

Nature & Scope of Financial Management

Financial management, as an academic discipline, has undergone significant changes over the years as regards its scope and coverage. In order to have a better exposition to these changes it will be appropriate to study both the traditional approach and the modern approach to the finance function

Traditional Approach:

The finance manager had a limited role to perform. He was expected to keep accurate financial records, prepare reports on the corporation's status and performance and manage cash in a way that the corporation was in a position to pay its bill in time.

The traditional approach evolved during 1920 continued to dominate academic thinking during the forties and through the early fifties. However, in the later fifties it started to be severely criticized and later abandoned on account of the following reasons.

a) Outside-looking-in approach

In thus treated the subject of finance from the viewpoint of suppliers of funds, i.e., outsiders, viz., bankers, investors, etc, it followed and outsider-looking-in approach and not the insider-looking-out approach since it completely ignored the viewpoint of those who had to take internal financing decisions.

b) Ignored Routine Problems

The subject did not give any importance to day-to-day financial problems of business undertaking.

c) Ignored Non-corporate Enterprise

The approach focused attention only on the financial problems of corporate enterprises. Non-corproate industrial organizations remained outside its scope.

d) Ignored working capital Financing

The approach laid overemphasis on the problem of long-term financing. The problems relation to financing short-terms or working capital were ignored.

e). No Emphasis of Allocation of funds

The approach confined financial management to issues involving procurement of funds. It did not emphasize on allocation of funds.

II. Modern Approach:

Under modern approach outlining scope of financial management are being discussed below.

1. Funds requirement Decision

A careful estimate has to be made about the total funds required by the enterprise taking into account both the fixed and working capital requirement

2. Financing Decision

Every business activity requires funds and hence every financial manager is confronted with this problem. He has to identify the sources from which the funds can be raised, the amount that can be raised from each source and the cost and other consequences involved.

3. Investment Decision:

This comprises decision relation to investment in both capital and current assets.

4. Dividend Decision

The dividend decision involves the determination of the percentage of profits earned by the enterprises when is to be paid to its shareholders.

5. To ensure supply of funds to All parts of the organization
6. Evaluation of the financial performance
7. To Negotiate with bankers, financial Institutions and other suppliers of credit.
8. To keep track of Stock Exchange Quotations and Behaviour of stock market.

Key Elements of Financial Management

Objectives of Financial Management

1. To maximize Profit
2. To Maximize earning per share
3. To minimize Costs
4. To Maximize Market Share
5. To Maximize the current value of the company's stock
6. To wealth maximization

Functions of a Financial Manager

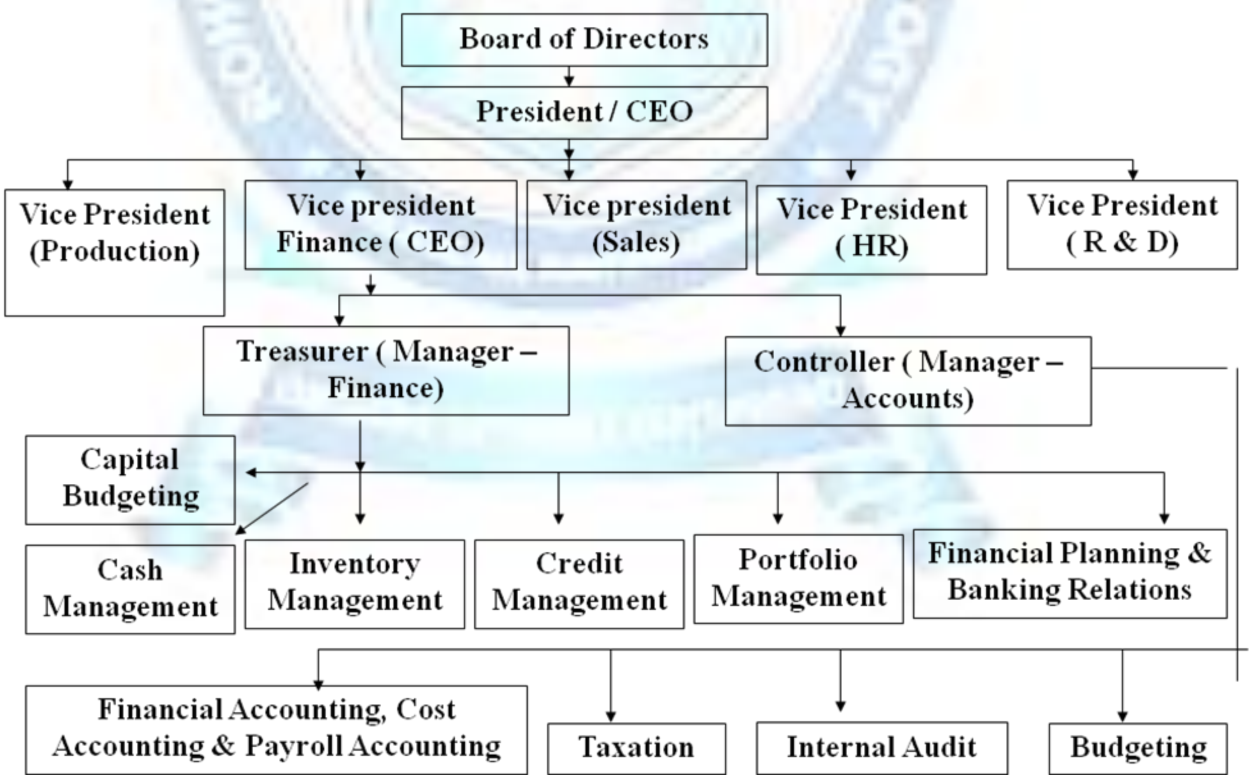
Primary Functions:

1. Estimating Capital Requirements
2. Financing or Capital Structure
3. Utilization of funds or Investment Decision
4. Disposal of surplus or Dividend Decision
5. Management of Cash
6. Financial Control

. **Subsidiary Functions:**

1. Ensuring the optimum level of inventory and receivables
2. Supplying funds to all the parts of the organization
3. Evaluating financial performance of various units of the organization.
4. Carrying out financial negotiations with financial institutions, banks underwriters, inter-corporate depositors.
5. Keeping track of stock exchange quotations and behavior of share prices

Finance Function in a Corporate Business Enterprise



Role of Financial Management in the Organization

1. Estimating Financial Requirements

2. Deciding Capital Structure
3. Selecting source of finance
4. Selecting a pattern of investment
5. Proper cash management
6. Implementing financial controls
7. Proper use of surpluses