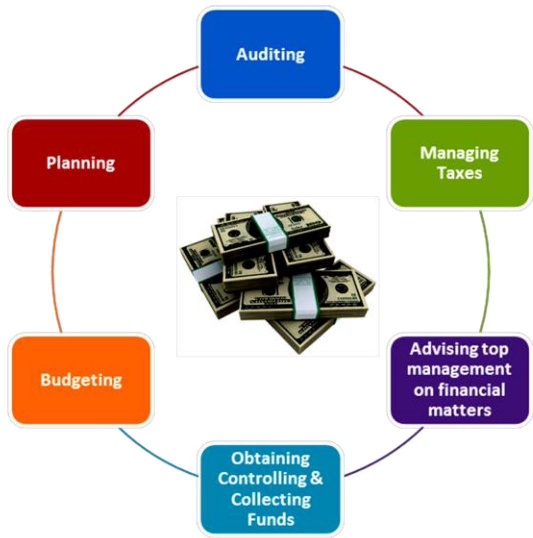
What is Finance?

Finance is the ways in which a company acquires funds for the firm and manages those funds within the firm.

What do Financial Managers Do?

Financial management refers to the management of a firm's resources so it can meet its goals and objectives. Basically, this is the allocation of money (a scarce resource) to different departments to finance the operations of the business. The financial manager analyzes the financial data from the accountants and recommends strategies for improving the financial performance of the company.



The Value of Understanding Finance

Without an understanding of finance, businesses often fail within the first few years of operation. The three most common reasons are: ***undercapitalization*** *(starting a business without sufficient funds to support it),* ***poor control of cash,*** *and* ***inadequate control of expenses.***

Financial Planning

Financial planning means analyzing short-term and long-term money flows to and from the firm.
Its overall objective is to optimize the firm's profitability and make the best use of its money. It has three steps:
(1) forecasting the firm's short-term and long-term financial needs
(2) developing budgets to meet those needs
(3) establishing financial controls to see whether the company is achieving its goals

Short-Term Forecast

This attempts to predict revenues, costs, and expenses for a period of one year or less.

- ***Projected Cash Flows*** *projects the inflows and outflows of cash, usually in months or quarters.*
- ***Sales Forecast*** *projects the expected sales, usually in months or quarters.*

Long-Term Forecasting

Involves forecasting for longer periods such as 5-10 years.

Part of the company's long-term strategic plan and used to answer the following:

- *What business are we in?*
- *Should we be in it five years from now?*
- *How much money should we invest in technology and new plants and equipment over the next decade?*
- *Will we have cash available to meet long-term obligations?*

Budgets and the Budgeting Process

A financial plan that sets forth management's expectations and, on the basis of those expectations, allocates the use of specific resources throughout the firm.

3 MAIN BUDGETS ARE

Capital Budget	**Cash Budget**	**Operating (or master) Budget**
A budget that highlights a firm's spending plans for major asset purchases that often require large sums of money *Ex. Property, Buildings, Equipment*	*A budget that estimates cash inflows and outflows during a particular period like a month or a quarter.* *Ex. Anticipating borrowing needs, debt repayment, operating expenses, and short term investments*	*The budget that ties together the firm's other budgets and summarizes its proposed financial activities. The most detailed report a firm prepares* *Ex. Estimates costs and expenses to run the business, given projected revenues.*

Why the Need to Establish Financial Controls

A company practices this procedure to periodically compare its actual revenues, costs, and expenses with its budgets. They want to make sure everything is running according to plan and determine if they need to make any corrective action to the overall budget. Finally, the financial controls help reveal which specific accounts, departments, and people, if any, are varying from the financial plan.

THE NEED FOR OPERATING FUNDS

4 Key Areas

Managing day-by-day needs of the business	**Controlling Credit Operations**	**Acquiring Needed Inventory**	**Making Capital Expenditures**
-Collect money that is owed to a business as quickly as possible to pay its employees, invest in interest-bearing accounts, and maximize the investment potential of the firm's funds. *-Paying bills as late as possible, so a business can keep on maximizing their funds before their bills are due.*	*-Allows current customers to be happy and attract new ones because when selling a product the customer can pay the firm over an agreed period of time (monthly, yearly) without having to pay the whole cost up front.* *-A firm will offer cash or quantity discounts to customers who pay their accounts by a certain time, which motivates customers to pay off their debts. Money owed to a company from a customer is put into an account called Accounts Receivable.*	*-A carefully constructed inventory policy allows the firm to manage its available funds and maximize profitability.* *-If a firm has too much inventory in stock with no customers to buy the goods, then a company has wasted money.* *-If the company is low on inventory with a high customer demand, the firm is missing out on chances to make revenue.*	*- Major investments in tangible long-term assets such as land, buildings, and equipment or intangible assets such as patents, trademarks, and copyrights.* *-This allows a firm to possibly expand into new markets and take risks to grow the company.* *-Examples of capital expenditures include land for future expansion, manufacturing plants, or research development*

Alternative Sources of Funds

Debt Financing	**Short-Term Funds**	**Long-Term Funds**
Debt Financing are funds raised through various forms of borrowing that must be repaid **Equity Financing** is money raised within the firm, from operations or through the sale of ownership in the firm (stock)	Needed for a year or less • Monthly expenses • Unanticipated expenses • Cash Flow problems • Expansion of current inventory • Temporary promotional programs	Needed for more than a year (2 to 10 years) • New-product development • Replacement of Capital equipment • Mergers or acquisitions • Expansion into new markets • New Facilities