



NATIONAL OPEN UNIVERSITY OF NIGERIA

91, Cadastral Zone, University Village Jabi, Abuja

FACULTY OF MANAGEMENT SCIENCES

COURSE CODE: BFN209

COURSE TITLE: INTRODUCTION TO FINANCE

Course Code BFN209

Code Title: Introduction to Finance

Course Editor: Dr. I.D. Idrisu (Dept of Financial Studies, NOUN)

Course Coordinator: Mrs. Kunbi Lawal (Dept. of Financial Studies)

COURSE GUIDE

1.0 INTRODUCTION

This course is designed to give you self -instruction on the Introduction to Finance- 100 level students of Bachelors' degree of Banking and Finance of the School of Management Sciences.

2.0 COURSE AIMS

The aim of this course is to introduce Finance to first year undergraduate students of Banking and Finance to understand business finance in a firm, enterprise or business organization.

3.0 COURSE OBJECTIVES

By the end of this course, the student should be able to:

Explain finance- Nature, Scope, Function, Risk, Role;

Identify financial statements as the basis for financial analysis of an enterprise;

Plan for profit

Introduce working capital management

4.0 WORKING THROUGH THE COURSE

This course, BFN209 Introduction to Finance expects you to do a lot of reading in order to cover the materials in the course material. It implies that you should devote much time to this course by reading through this material and getting more information from numerous texts and journals in research. The course material has been made easy to read and user-friendly.

5.0 COURSE MATERIALS

The National Open University of Nigeria provides you with the following items:

Course Guide

Study Units

TMA Assignment file

In addition, at the end of every unit is a list of texts for your references and for further reading. It is not compulsory for you to read all of them. They are only essential supplements to this course material.

I

5.0 STUDY UNITS

The study units in this course are located under Modules as follows:

MODULE 1

Unit 1	Nature of Finance
Unit 2	Scope of Finance
Unit 3	Function of Finance
Unit 4	Risk of Finance
Unit 5	Key Role of Finance

MODULE 2

Unit 1	Finance Goals and Objectives in a Firm
Unit 2	The Role of Financial Managers
Unit 3	Introduction of Financial Analysis
Unit 4	Profit planning and Pricing
Unit 5	Introduction to Working Capital Management

MODULE 3

Unit 1	Basic forms of business organization
Unit 2	Sources of Business Finance
Unit 3	Financial planning and forecasting
Unit 4	Finance in the Firm's organization structure
Unit 5	Finance and related disciplines

COURSE DESCRIPTION AS IN THE OPP

The modules and units are self explanatory as they summarize **INTRODUCTION TO FINANCE - 100** level students of Bachelors' degree of Banking and Finance. You will need to work in groups with other students in this course and program in order to discuss, compare notes and thoughts and to exchange and share ideas.

6.0 ASSESSMENTS

There are two aspects to the assessment of the course: first are the tutor-marked assignments (TMA); and the end of course examination. Within each unit are self assessment exercises which are aimed at helping you check your assimilation as you proceed. Try to attempt each of the exercises before finding out the expected answer from lecture.

8.0 TUTOR-MARKED ASSIGNMENT (TMA)

This is your continuous assessment and accounts for 30% of your total score. You are expected to answer at least four TMA's, three of which must be answered and submitted before you sit for the end of course examination. Your Facilitator will give you the TMA's and you must submit to your Centre your responses.

9.0 FINAL EXAMINATION AND GRADING

With this examination written successfully, you have completed your course in Basic Research and one believes you would apply your knowledge (new or up-graded) in your project. The ‘end of course examinations’ would earn you 70% which would be added to your TMA score (30%). The time for this examination would be communicated to you.

Table 1: Course Marking Scheme

ASSESSMENT	MARKS
Assignment (TMAs) 1 – 4	Four (4) assignments, best three (3) marks of the four account at 10% each = 10 x 3 = 30%
End of course examination	70% of overall course marks
Total	100% of course marks

10.0 HOW TO GET THE MOST FROM THIS COURSE

In distance learning, the study units are specially developed and designed to replace the conventional lectures. Hence, you can work through these materials at your own pace, and at a time and place that suits you best.

Visualize it as reading the lecture.

Each of the study units follows a common format. The first item is an introduction to the subject matter of the unit, and how a particular unit is integrated with the other units and the course as a whole. Next is a set of learning objectives. These objectives let you know what you should be able to do by the time you have completed the unit. You should use these objectives to guide your study. When you have finished the unit, you must go back and check whether you have achieved the objectives. If you make a habit of doing this, you will significantly improve your chances of passing the course.

The main body of the unit guides you through the required reading from other sources.

This will usually be either from your set books or from a *Reading Section*.

Activities are interspersed throughout the units, and answers are given at the end of the units.

Practice these self-assessment exercises to help you to achieve the objectives of the units and prepare you for the assignments and the examinations. Keep tap with your facilitator for assistance.

In summary,

- (1) Try to read this course guide.
- (2) Organize a study schedule.
- (3) Do everything you can to stick to the schedule.

- (4) Assemble the study materials.
- (5) Work through the unit. The content of the unit itself has been arranged to provide a sequence for you to follow. As you work through this unit, you will be instructed to read sections from your set books or other articles.
- (6) Review the objectives for each study unit confirms that you have achieved them. If you feel unsure about any of the objectives, review the study material or consult.
- (7) When you are sure of having achieved a unit's objectives, you can then start on the next unit.
- (8) After completing the last unit, review the course and prepare yourself for the final examination. Check that you have achieved the unit objectives and the course objectives.

To gain the maximum benefit from course tutorials, prepare a question list before attempting them.

11.0 SUMMARY

This course BFN209 is designed to introduce you to Finance to give you some knowledge which would help you to understand the role of finance in business enterprise Endeavour to go through this course successfully and you would be in a good position to pass your examination at the end of the semester

We wish you success in this interesting course. GOOD LUCK.

MODULE 1

Unit 1	Nature of Finance
Unit 2	Scope of Finance
Unit 3	Function of Finance
Unit 4	Risk of Finance
Unit 5	Key Role of Finance

UNIT 1 NATURE AND SCOPE OF FINANCE**CONTENTS**

1.0	Introduction
2.0	Objectives
3.0	Main Content
3.1	Nature of Finance
3.1.1	Finance Defined
3.2	Evolution of Finance
3.3	Field of Finance
3.4	Role of Finance
3.5	Common Denominator of Finance
3.6	Interrelationship and Transaction
3.7	Funds Flow
4.0	Conclusion
5.0	Summary
6.0	Tutor-Marked Assignment
7.0	References/Further Reading

1.0 INTRODUCTION

Finance plays a very important role in any business activities, whether public or private sector. Its management is the pillar upon which all economic activities stand. No business can survive or be sustained without finance.

In this first unit of this course, we will you will be introduce the nature of finance in a buy & sell enterprise, define finance; explain the role and field of finance.

2.0 OBJECTIVES

At the end of this unit, you should be able to:

discuss the nature of finance
define finance

Identify the role finance.

3.0 MAIN CONTENT

3.1 Nature of Finance

Finance may be defined as the provision of money at the time it is required. Every person responsible for finance, whether it is for a corporate organization or private household, money is confronted with prospects of inflow receipts on the one hand, and outflow payments on the other. The inflows are expected to be arranged in such a way that fund (money) is always available to make necessary payments as they arise.

3.1.1 Finance Defined

Oyekanmi (2003) defined finance “as money affairs or money matters”. All forms of money or near money e.g. debt, cash equity certificates would be implied. In certain usage, however, not only are liquid funds subsumed in the term finance, but all forms of assets, which are capable of being expressed in monetary terms.

On the other hand, Anao (1993) defined finance as money affairs or money matters. All forms of money or near-money such as debt, cash equity, certificates of deposits would be implied. In certain usage, however, not only are liquid funds subsumed in the term finance, but all forms of assets, which are capable of being expressed in money terms.

According to Hornby (2001), finance is the money need or needed to support an activity, project, programme etc. and or the management of money.

3.2 Brief Evolution of Finance

Finance evolved from economics as its branch in the early part of the 20th century; but later became a separate discipline. It graduated in response to the complexity of business from sole proprietorship to corporate organisation. Finance was initially concerned mainly with the keeping of records of receipts and payments; dealings simply on bonds, debentures, banks.

Nowadays, it has extended the ‘coast’ to various aspect or aspects of company survival, introduction of new technologies in operation, the application of computers and its closeness to economy.

SELF ASSESSMENT EXERCISE 1

Define of Finance.

3.3 Field of Finance

The field of finance originally covered mainly:

Instruments of finance (e.g. bonds, debentures etc.)

Institutions / intermediaries (e.g. banks, finance coys etc.)

Capital markets (e.g. exchange etc.)

The finance is related to economics as every individual, organizations and government operate within the economy. So understanding economic setting is paramount to you.

You need the knowledge and alertness of each level of economic activity and the related consequences. It is associated with accounting as both are interested in cash flows and accounting and financial data necessary for taking basic decisions.

3.4 Role of Finance

Without money (finance), an enterprise cannot function; hence, understanding the role of finance and its ability to measure the progress of a business is essential for effective management.

Finance can be likened to a lubricant. Too little of it (finance) can make a business grind to a halt; while too much of it may lead the business having to grapple with all types of projects not minding their usefulness.

3.5 Common Denominator of Finance

Money is the common denominator for the full range of activities performed in the business.

Yes, there are other factors which are common to business like man-hours, which are all the same length but don't have the same value in term of quantity of work done or skill and expertise displayed.

Money also presents its problems, particularly when inflation sets in, resulting in changes in the purchasing power of a unit of currency.

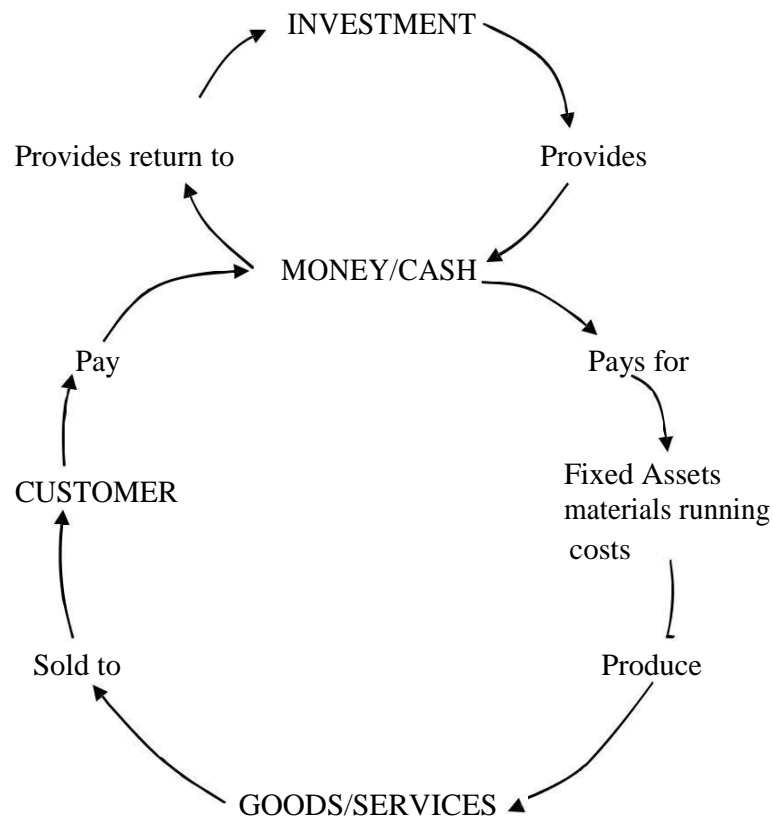
This notwithstanding, for the moment, this fact has not affected its role as a common denominator, so long as it remains the medium in which business is conducted.

3.6 Inter-relationship and Transaction

Money is the medium of exchange in business; the other two elements are production/operation and marketing. All these three must be held in balance to enable optimum utilization of the resources of the enterprise.

The interrelationship between the various elements is graphical represented below:

Figure 1: Business Cycle



SOURCE: Jones, G.L. (1976) Financial Measurement for Managers

According to Jones (1976), the initial investment of cash (money) in figure 1 above, is shown to provide the means whereby the entrepreneur or promoter of the business enterprise can purchase those assets which enable the business to have premises, equipment, transport and other items required before the activities of the organization can take-off.

The investment must also be sufficient to allow management to pay the running expenses of the business, such as wages, rent etc. and purchase the first quantities of goods or other basic commodities which are required before any income can be earned.

It is essential to realize that in most cases, money is paid out for these items before the receipt of cash can be expected.

Having acquired the assets and the materials needed to commence business, and paid the running costs for the first period of activity, goods and services become available to the potential customers, who in turn, purchase them and thus provide the cash to pay for further commodities and running costs.

Because the cash received from sales should be greater than the cash paid out for materials and running expenses, a reservoir of cash is built up from which funds can be drawn to pay the providers of the initial capital a return on their money in the form of interest or dividends.

SELF ASSESSMENT EXERCISE 2

Describe the role of Finance in an enterprise.

3.7 Funds Flow

The working cycle described in figure 1 above demonstrates the way funds flow through business. There are a number of linked transactions.

Note: First, that every time funds flow in a business, there is a source of funds and a use of funds. That is, each transaction has two aspects:

1. The generation or supply of funds
2. The utilization of these funds.

4.0 CONCLUSION

The nature as well as the vital role played by finance in any business enterprise has been discussed and illustrated in this unit.

5.0 SUMMARY

In this unit, we have discussed the nature of evolution, field and role of Finance. Also, we have introduced finance as a common denominator in

business and attempted to explain its interrelationship in business transaction and illustrated the flow of funds in business cycle.

6.0 TUTOR-MARKED ASSIGNMENT

1. Identify the role of Finance in a business enterprise.
2. Discuss the nature of Finance in a business organisation.

7.0 REFERENCES/FURTHER READING

Anao, A.R. et. al. (1993) ‘ *Investment Analysis and Management*’ Lagos
The Chartered Institute of Bankers of Nigeria (CIBN)

Hornby, A.S. (2000) *Oxford Advanced Learner’s Dictionary of Current English* (6th edition) Oxford: Oxford University Press

Jones, G.L. (1976). *Financial Measurement for Managers* London:
Edward Arnold (Publishers) Ltd.

Oyekan, A. (2003). *Basic Concepts and Applications in Business Finance*
Ibadan TL-PEAKLINE Publishers

Paish, F.W. (1975) *Business Finance*. Pitman Publishing PVT Ltd New
York USA

Pandey, I.M. (2005). *Financial Management* (9th edition). New Delhi
India: VIKAS Publishing House PVT Ltd.

UNIT 2 SCOPE OF FINANCE

CONTENTS

- 1.0 Introduction
- 2.0 Objectives
- 3.0 Main Content
 - 3.1 Scope of Finance
 - 3.2 Internal and External Finance
 - 3.3 Real and Financial Asset Markets
 - 3.3.1 Real Market
 - 3.3.2 Financial Asset Market
 - 3.4 Finance and Management Functions
- 4.0 Conclusion
- 5.0 Summary
- 6.0 Tutor-Marked Assignment
- 7.0 References/Further Reading

1.0 INTRODUCTION

In this unit of the course, we will discuss the scope of finance to be reached, emphasizing on the relevant areas of concern because finance is a wide area of studies with much interrelationship in business. It is part of management.

2.0 OBJECTIVES

At the end of this unit, you should be able to:

- discuss the scope of finance
- explain the financial and real asset market
- identify types of financing
- Discuss finance as part of management.

3.0 MAIN CONTENT

3.1 Scope of Finance

In Unit 1 of this Module, money (finance) was presented as a common denominator in doing business (trading). The other two elements that will combine to strike a balance in order to enhance the optimum utilization of resources of the business are: production and marketing.

The business cycle in Unit 1 explains financial (fund) activities and how they are related to the enterprise's other activities. Manufacturing / operation activities provide goods/services to customers. They sell their

goods or services to earn profit. They raise funds to acquire manufacturing and other facilities.

A firm generates whatever capital it needs and utilises it (finance activity) in activities which generate returns on invested capital (production and marketing activities) as indicated in figure 1, Unit 1 earlier.

3.2 Internal and External Finance

There are two types of financing an enterprise can apply.

Internal Finance – also known to as equity fund/finance is referred to as Equity. This is solely owned/contributed by the stakeholders (within) and is referred to as an internally-generated fund.

External Finance – This is called borrowed fund/finance and referred to also as debt. The stakeholders source this from outside. This could be through direct loan, shares, etc. A firm/business can sell shares to acquire equity funds.

Shares represent ownership rights of their holders. Buyers of shares are called shareholders/stockholders and they are the legal-owners of the business whose shares they hold. For example, recruitment and promotion of employees in an organization, payment of their wages and salaries etc. involves finance. The evolvement of sales promotion/advertisement policies is within marketing preview. All these activities require cash budgeting, hence they affect financial resources.

Shareholders invest their money in the shares of a company in the expectation of a return on their invested capital. The return consists of dividend and capital gain.

Shareholders can be of two types

Ordinary and
Preference.

3.3 Financial and Real Assets Markets

There are two kinds of markets, namely:

- 1) Financial Market
- 2) Real Assets Market

3.3.1 Real Markets

Real markets are for physical or tangible assets such as plant, machinery, wheat, office, gold, buildings etc. Intangible real assets include copyrights, patent, technical know-how.

3.3.2 Financial Markets

Financial market trades on financial assets. This asset promises future benefits in the form of cash payments such as is applicable to bonds, certificate of deposits, treasury bills, etc.

SELF ASSESSMENT EXERCISE 1

Give examples each of financial and real assets

3.4 Finance and Management Function

There is a relationship between finance and other functions in business enterprises. You should know that all business activities, directly or indirectly, involve the acquisition and utilization of funds. All the activities and decisions undertaken in respect of the day-to-day financing of a business make finance and management functions interrelated. For example, decisions on the following finance issues are taken by management upon recommendation of the Financial Controller:

Preference shareholders receive dividend at a fixed rate and they enjoy a priority over ordinary shareholders.

The dividend rate for ordinary shareholders is not fixed and can vary from year to year depending on the board of directors.

A company can also obtain equity funds by retaining earnings available for shareholders. This is known as retained earnings (an internal equity) undistributed profits of equity capital.

Rights Shares – after a company distributes all earnings to shareholders, it can re-acquire new capital from the same source (existing shareholders) by issuing new shares.

Public Issue – may be made to attract new (and the existing) shareholders to contribute equity capital.

Creditors/Lenders (External Finance) – They are not owners of the company. They provide money to enterprises as loan which are debt.

The loans are furnished for a specific period of time at a fixed rate of interest.

Payment of the interests is a legal obligation. The business can borrow fund from many sources like banks, financial companies, public or issuing bonds or debentures.

A bond/debenture is a certificate stating the amount of money lent by a bond holder to the company.

SELF ASSESSMENT EXERCISE 2

What is dividend?

4.0 CONCLUSION

The unit concludes that the scope of financing a business entity is from internally and externally generated fund. This keeps the business cycle turning to produce earnings (profits).

5.0 SUMMARY

In this unit, the scope of finance is summarized along with types of financing, real and financing market and finance as part of management.

6.0 TUTOR-MARKED ASSIGNMENT

1. Discuss the scope of finance
2. Identify types of financing in business enterprises.

7.0 REFERENCES/FURTHER READING

Jones, G.L. (1976). *Financial Measurement for Managers* London Edward Arnold (Publishers) Ltd

Pandey, I.M. (2005). *Financial Management* 9th edition New Delhi VIKAS Publishing House PVT Ltd

UNIT 3 THE FINANCE FUNCTIONS

CONTENTS

- 1.0 Introduction
- 2.0 Objectives
- 3.0 Main Content
 - 3.1 Investment Function
 - 3.2 Financing Function
 - 3.3 Dividend Function
 - 3.4 Liquidity Function
 - 3.5 Financial Procedures
- 4.0 Conclusion
- 5.0 Summary
- 6.0 Tutor-Marked Assignment
- 7.0 References/Further Reading

1.0 INTRODUCTION

In this unit, you will be introduced to finance functions in the various stages of activities of a business organization. You may recapitulate that in the business cycle figure drawn in Unit 1, you were shown the functional movement of funds/financial activities through investment to cash, production of goods and services, given their marketing thereof.

2.0 OBJECTIVES

At the end of this unit, you should be able to:

- identify the functions of finance
- apply these functions of finance
- Establish effective execution of finance functions.

3.0 MAIN CONTENT

Finance functions have been acknowledged as major in most organisations. They are identified as raising funds, investing them in assets and distributing returns earned from assets to shareholder/owners. This exercise is known as financing decision, investment decision and dividend decision.

These finance phenomena which will be treated extensively later; were expressed in figure 1, Unit 1, Module 1 of this course. When a firm endeavours to balance the cash inflows and outflows while performing the above functions, it is called liquidity decision. Hence, the list of important finance functions includes:

Long term asset-mix or investment function
Capital-mix or financing function
Profit allocation or dividend function
Short-term asset-mix or liquidity function

A business organization performs finance functions simultaneously and continuously in the normal course of its activities. The occurrence may, however, not be in sequence. Finance functions require skill and professional planning, control and execution of an organization's activities.

SELF ASSESSMENT EXERCISE 1

List the important finance functions in a firm

3.1 Investment Function

Investment decisions involve capital expenditures which are referred to as capital budgeting decision. This is the decision of allocating capital to long-term assets that will bring in beneficial yield (cash inflow) in the future.

There are two important aspects of investment decisions:

- a) The evaluation of the prospective profitability of new investment;
and
- b) The measurement of a rate against the prospective return of new investments could be compared.

Risk in investment, as would be explained in the next unit, arises because of uncertainty in returns. Investment proposals should, therefore, be analysed and evaluated in terms of both expected return and risk.

SELF ASSESSMENT EXERCISE 2

What are the two important aspects of investment decisions?

3.2 Financing Function

This is another vital function in an enterprise. The financial manager has to identify the time, place and the technique for acquiring adequate funds to meet the enterprise's investment needs. The central issue here is the determination of appropriate proportion of internal (equity) and

external (debt) finance required by the enterprise. The mix of the two is known as the **capital structure** of the business organization.

The Financial Manager strives to obtain and sustain the best financing mix, to optimize the capital structure, which forms the base of financing. The capital structure is said to be optimum when the market value of shares is maximized.

SELF ASSESSMENT EXERCISE 3

What is capital structure of an enterprise?

3.3 Dividend Function

This is the other major financial decision which affects the shareholders and the business as a whole – the decision to distribute all profits or retain same. The proportion of distribution of profit and the balance retained is subject to the firm's policy, decision of the board of director or economic situation as applied. The proportion of profits distributed as dividend is called the **dividend-payout ratio**.

The **retention ratio** is the retained portion of profits. The dividend policy is determined by its impact on the shareholder's value.

SELF ASSESSMENT EXERCISE 4

What is retention ratio in finance?

3.4 Liquidity Function

Liquidity and profitability affect investment in current assets in business organizations. Liquidity of an enterprise is affected by the level of management of current asset. Risk of illiquidity (lack of liquidity), in extreme situations, can lead to a business insolvency.

Current assets if properly/efficiently managed would safeguard the business organization against risk of illiquidity. The firm needs to invest sufficient funds in current assets in order to become liquid.

It would lose profitability, if more of available current assets are not utilized to earn any revenue.

To sum it up, financial decisions is concerned with the acquisition or disposal of assets through commitment or recommitment of funds on a continuous basis.

This is why finance function affects the size, growth, profitability and risk of the firm, and ultimately, the value of the business/enterprise.

SELF ASSESSMENT EXERCISE 5

Liquidity of a business is affected by _____.

3.5 Financial Procedures

Financial procedures involve a lot of measures to achieve effective execution of finance function. Some important routine finance functions are:

Supervision of cash receipts and payments and cash balances safeguarding.

Custody and safeguarding of securities, insurance policies and other valuable papers.

Taking care of the mechanical details of new outside financing.

Record keeping and reporting.

In recent years, the scope of finance function as stated in Unit 1 of this Module indicates that it has widened. This will be discussed more in the next unit.

4.0 CONCLUSION

The various finance functions have been identified and discussed showing they are applied at each stage of cash to investment as they affect production of goods and services and the marketing of these product.

5.0 SUMMARY

In this unit, we have identified the finance function of a business enterprise are identified based on investment, financing, dividend and liquidity decisions. The effective procedure for the execution finance function was also established.

6.0 TUTOR-MARKED ASSIGNMENT

1. State some financial procedures for effective execution of finance function.
2. Explain in short note: investment decision and liquidity decision of a business concern.

7.0 REFERENCES/FURTHER READING

Pandey, I.M. (2005). *Financial Management* (9th edition). New Delhi
India VIKAS Publishing House PVT Ltd.

Jones, G.L. (1976). *Financial Measurement for Managers* London
Edward Arnold (Publishers) Ltd

UNIT 4 RISKS OF FINANCE

CONTENTS

- 1.0 Introduction
- 2.0 Objectives
- 3.0 Main Content
 - 3.1 Investor's Dilemma
 - 3.2 Physical Risks and Finance
 - 3.3 Technical Risks and Finance
 - 3.4 Economic Risks and Finance
 - 3.5 Political Risks and Finance
 - 3.6 Avoidance of Risk
 - 3.7 Distribution of Risks
- 4.0 Conclusion
- 5.0 Summary
- 6.0 Tutor-Marked Assignment
- 7.0 References/Further Reading

1.0 INTRODUCTION

To function properly in business, you should consider the risk taken; especially in the sourcing and usage of fund.

In this unit, you would be led to the investor's dilemma, especially in the developing economy like Nigeria, where risk taking is much dreaded and one has to "look before one leaps" in financial venture.

2.0 OBJECTIVES

At the end of this unit, you should be able to:

discuss the risks of finance
state category of risks in finance
Identify how to avoid finance risks.

3.0 MAIN CONTENT

3.1 Investor's Dilemma

If the investor believes that there is some chance, however small, that in the long run he may earn a small return (profit), he would extra effort than he could obtain on a riskless investment. He will not invest unless he can expect a higher return if the investment does succeed. Though in

the course of event, he will not necessarily expect this higher return to become available at once.

This allowance for risk, in greater or less degree, is made whenever the yield of the investment is anywhere dependent on the satisfactory result of the undertaking of work for which the full fruits are reaped only after a delay.

It is pertinent to note that there can never be a certainty that the fruits, when reaped would be commensurate with the cost of resources (labour, capital etc) expended in the production/marketing.

Hence, there is always some chance that part or all of the resources employed may prove to have been wasted.

The risk that threatens the complete or partial loss of the postponed fruits of effort can be classified under four main headings:

Physical risks
 Technical risks
 Economic risks
 Political risks

3.2 Physical Risks and Finance

These are risks that some accident may destroy or spoil some physical goods created by the work financed.

For example:

A stock of food may go bad or be eaten up by insects or animals
 A house (premises) may be destroyed by fire
 A ship may be wrecked or sunk.

Dangers from fire, flood, storm, theft etc. have always threatened and still threaten the benefit of the fruits of business enterprise.

3.3 Technical Risks and Finance

These are those risks that arise from the fact that the producer's skill or that of the subordinates may not be up to the expected level for the plan, hence it may fall short of achieving the intention. If at all it is achieved, it may fall below the standard; i.e. the end -product, at disposal may consume, in its construction, more resources than permitted in making the plans.

For example, a farm entrepreneur in a new environment may try to grow crops unsuited to the soil or climate. A new technical process, successful in the laboratory or in small-scale plant, may encounter unforeseen difficulties when tried in large-scale production. Wherever experience of the exact process is lacking, whether because the process itself is only newly developed or because of the lack of experience of the people using it, a high degree of technical risk is always present. This is one of the reasons why the early stage of enterprise venturing into new areas of producing goods/services, using newly processes are nearly always less satisfactory than anticipated.

Experience (know-how) gained by the organization of its particular technical process which often constitutes its most valuable possession. Thus, unforeseen technical risk in finance renders the whole months of intensive work completely wasteful; except for the obtaining of valuable experience.

3.4 Economic Risks and Finance

This category of risks is usually the greatest and closely related to finance. They remain; even though the physical object created suffer no unexpected damage. It is found possible to construct these physical objects with the resources assumed to be available. There are **four** main kinds of this risk:

The risk of an inadequate supply of the resources needed to make the product planned so that it costs more to make than had been expected or even cannot be made at all; and

The risk of fall in demand for the product once it has been made.

The risk of a failure of the demand for a product is increased when that product is itself highly durable, for them to the other risk.

The risk that potential purchasers may be prevented from buying by a shortage of finance.

3.5 Political Risk and Finance

These are risks of losses as the result of unforeseen intervention by governments. These risks may particularly affect the enterprise operating in or exporting to, a foreign country, where government laws discriminate. This may have untold frustration in the quest for achievement of the expected return on capital investment. Example includes Rent Act, which can affect the status of workers who are

tenants if it is not favourable; corporate tax can affect the profit margin of an enterprise and this may in turn have effect on the finances of the organization.

SELF ASSESSMENT EXERCISE 1

List the different types of risk associated with the finance of an enterprise.

3.6 Avoidance of Risk

There are three ways of avoiding or reducing risk. These are as follows:

Appropriate measures involving additional expenditure;

Turn into regular costs by pooling them with large numbers of similar risks; and

Combing them with other risks operating in the opposite direction.

Almost every kind of risk can be reduced, to some extent, by increasing expenditure on precautions as follows:

A building can be made more resistant to fire if more fund is expended on it to add value to it.

The risk of financial failure of a new method of production can be reduced at the cost of increased expenditure of time and money; if a thorough testing in a small-scale plant is made before being introduced into large-scale production (project).

The risk of production being held up for lack of an important component can be removed and the cost of an immediate loss of output avoided; if adequate reserve stocks are built up.

Even the risk of miscalculating consumers' demand can be reduced by expenditure on market research, advertisement and sales promotion.

The great difficulty is usually to determine how large an increase in costs is justified in order to achieve an uncertain degree of reduction in an uncertain risk.

SELF ASSESSMENT EXERCISE 2

Name ways of avoiding risk in a business concern.

3.7 Distribution of Risks

After eliminating all the risks which can be reduced by taking precautions, pooled by insurance or offset by hedging (the term used for reducing risk by using derivatives – debt capacity enhancement, increased focus on operations and isolating managerial performance which we tried to explain earlier).

There remain a very large number of risks that must be borne by whoever provides the finance for a productive operation. It is with these various methods of sharing such risks among various classes of providers of capital that this unit is mainly concerned with.

The simplest form of finance is where the whole of finance required by a particular enterprise is provided by an Entrepreneur (a single person). In this business, the person pays all expenses, takes all receipts and makes the whole of any profit or loss which results from the activities of the business. When the business requires more assets than he can afford to provide personally (expansion) then, there arises the problem of how to distribute the risk inherent in the business. Hence, different contributors to the finance of the business will be required to share the risk as shareholders.

The number of possible ways in which the risks and profits can be shared between the different people who jointly contribute to the finance of a business is also infinite. The following ways are frequently adopted.

1. A full share of all risk and profits.
2. A prior claim on any profits the enterprise can earn up to a certain limited amount, with or without some share in the remainder.
3. A loan of money on payment of a fixed amount of interest which must be paid whether the concern is earning a profit or not.
4. The renting of land or other durable good is return for fixed money (rent), payable whether or not the enterprise is able to earn a profit (leasing).

Partnership and Limited Liability Company are two main institutional forms under which people join together on equal terms to provide the finance needed for an enterprise, sharing fully in both risks and profits.

SELF ASSESSMENT EXERCISE 3

Name two structures of sharing finance risks.

4.0 CONCLUSION

The categories of risk of finance in a business organization were identified and discussed. The manners or ways on how to minimize risks among investors were suggested as well as the means of distributing the risk.

5.0 SUMMARY

In this unit, attempts have been made to discuss risk of finance and business, types of risk (physical, technical, economic, political), the avoidance and distribution of risk.

6.0 TUTOR-MARKED ASSIGNMENT

1. Discuss the finance dilemma of an entrepreneur.
2. Explain how finance risks affect technical risk.

7.0 REFERENCES/FURTHER READING

Kolb, R.W & Rodriguez, R.S (1994) *Essential Financial Management* Florida USA: Kolb Publishing Company Inc.

Paish, F.W. (1975) 'Business Finance' *Pitman Publishing* New York USA

Pandey, I.M. (2005). *Financial Management* (9th edition). New Delhi India.

UNIT 5 KEY ROLE OF FINANCE AND RELATED DISCIPLINE

CONTENTS

- 1.0 Introduction
- 2.0 Objectives
- 3.0 Main Content
 - 3.1 Central Role of Finance Manager
 - 3.2 Crucial Role Played by Staff
 - 3.3 Corporate Organisation
 - 3.4 Finance Functions in an Enterprise
- 4.0 Conclusion
- 5.0 Summary
- 6.0 Tutor-Marked Assignment
- 7.0 References/Further Reading

1.0 INTRODUCTION

In this unit, you would identify the key role of finance as it is embedded in the functions of the Finance Manager. The central role of the finance manager will be explained to emphasis its utility as a pivot of management functions.

2.0 OBJECTIVES

At the end of this unit, you should be able to:

identify the key roles of finance in an enterprise

state the duties of a Finance Manager

Explain the interdependent relationship of finance with other sections of a business organisation.

3.0 MAIN CONTENT

3.1 Central Role of Finance Manager

As could be deduced from Unit 1 of this Module, the finance manager's duties include:

Budgeting

Raising funds

Selecting and evaluating projects

Planning the marketing and pricing strategies.

The finance manager is always supposed to be a specialist/professional, with knowledge of many areas of finance. The breadth of finance

function is vast that in many business organisations, it includes human resources from several departments of management.

3.2 Crucial Role Played by Finance Staff

As has been spelt out in Unit 1 of this Module, Finance is concerned with the flow of fund, which is the life blood of the business. The crucial role played by finance staff is recognised as vital and they are rewarded accordingly.

Clearly, skill is an extremely valued asset in managing an enterprise. It entails the techniques through which an organisation obtains finance for the business and the usage of the finance to assure the business as a going concern and successful. The use of the finance to establish the enterprise successfully, maintain, sustain and enable it grow into a colossus requires financial dexterity which the finance manager and the staff are at the centre.

SELF ASSESSMENT EXERCISE 1

State the key roles of a finance manager.

3.3 Corporate Organisation

The finance function to staff and departments will be dependent upon the size and magnitude of the business organisation. The larger the organisation, the greater is the degree/level of specialization of tasks and duties required.

The smaller business consolidates many duties in fewer sections and units. Generally however, the head of finance – Director of Finance, Chief Finance Officer, as it may apply, is the treasurer or any other designation like the controller of finance or general manager finance etc.

As expressed in the highlighted functions of an enterprise, the treasurer supervises or participates in the functions of finance. The treasurer oversees or manages the enterprise's liquid assets, liabilities, payroll and cashier activities, credits and collections, forecasting, capital budgeting and investment and financing. (All these will be discussed later in other units and other financial management courses in the programme as appropriate).

The Treasurer is an active participant in long -range financial planning. Practically, the task of finance is specifically assigned to finance staff, but non-finance staff frequently partakes in the decision-making process.

For example:

- i) Cost recording and control are accounting and finance function, whereas the determination of standard costs and the responsibility for correcting any variation(s) from realizable standards is with operations department.
- ii) In the same state, sales department in collaboration with marketing consultant (hired by the enterprise) estimate the level of sales for various pricing/costing policies. This data is then utilized in financial planning to estimate profit levels for each price structure.

The framework and responsibility for pricing/costing policy are jointly determined by the marketing/sales department and financial planning staff.

Planning funds for operations and capital budgeting is also a joint decision-making process conducted by the production, sales and finance personnel.

- iii) The need for a new machine might be determined by the production department which makes its request to the head of division/department etc, (who is a part of financial management team).

If the expenditure is not greater than the estimated value example N20,000 the decision as to whether to acquire the machine would be made at this point. If the outlay is above that amount, the requisition would be submitted for approval to business organisation with head of finance recommendation and supporting information as onus of proof.

This will then follow the laid-down policy of the enterprise – to approve or disapprove the proposal; based upon data relating to projected production/sales and the available funds to finance the investment.

SELF ASSESSMENT EXERCISE 2

Give one example of how finance inter-dependes on other sections/units for implementation of a business.

3.4 Finance Functions in an Enterprise

The functions of finance manager are condensed into the following:

- 1) Financing and investment;

- 2) Accounting and control;
- 3) Forecasting and long-run planning;
- 4) Pricing, and
- 5) Others.

They are discussed below.

1. **Financing and Investments:** Supervising the firm's cash and other liquid holdings, raising additional funds when required and investing funds in projects for adequate returns to keep the enterprise going as a concern.
2. **Accounting and Control:** Maintaining financial records, controlling financial activities; identifying deviations from planned and efficient performance and managing payroll, tax matters, inventories, fixed assets and computer operations.
3. **Forecasting and Long-Run Planning:** Forecasting costs, technological changes, capital market conditions, funds needed for investment purposes, returns on proposed investment projects and demand for the organisation's product etc.
4. **Pricing:** Determining the impact of pricing/costing policies on profitability.
5. **Other Functions:** Credit and collection, insurance and incentive planning (pension, etc.)

4.0 CONCLUSION

In this unit, we have attempted to establish the financial manager as a key person in the business organisation, frequently rising to the top in an enterprise as his role is central, dynamic and important.

5.0 SUMMARY

In summary, this unit is made up of the central role of the finance manager in a business organisation, the crucial role of finance staff, and the interdependence of finance unit/department with others in a corporate organisation and the highlights of finance function in an enterprise.

6.0 TUTOR-MARKED ASSIGNMENT

1. What are the central roles of finance manager in a business organisation?
2. Discuss briefly the duties of a treasurer in an enterprise.

7.0 REFERENCES/FURTHER READING

Jones, G. L. (1976). *Financial Measurement for Managers* London Edward Arnold (Publishers) Ltd

Pandey, I. M. (2005) *Financial Management* (9th edition) India, New Delhi: VIKAS Publishing House PVT Ltd

Schall, L. G. & Haley, C.W. (2002) *Introduction to Financial Management*. New Delhi: TATA McGraw-Hill Publishing Co Ltd.

Oyekanmi, Abiodun (2003). *Basic Concepts and Applications in Business Finance* Lagos Nookia Ventures Ltd

MODULE 2

Unit 1	Finance Goals and Objectives in a Firm
Unit 2	The Role of Financial Managers
Unit 3	Introduction to Financial Analysis
Unit 4	Profit Planning and Pricing
Unit 5	Introduction to Working Capital Management

UNIT 1 FINANCE GOALS AND OBJECTIVES OF A FIRM**CONTENTS**

1.0	Introduction
2.0	Objectives
3.0	Main Content
3.1	Profit Maximization
3.2	Wealth Maximization
3.3	Financial Goal, Firms Mission and Objectives
4.0	Conclusion
5.0	Summary
6.0	Tutor-Marked Assignment
7.0	References/Further Reading

1.0 INTRODUCTION

In this unit, we will be shown the financial goal of a firm which is shareholders' wealth maximization as reflected in the market value of business equity - owners' contributions/shares.

2.0 OBJECTIVES

At the end of this unit, you should be able to:

identify financial goal of a business firm
discuss profit maximization
Explain wealth maximization.

3.0 MAIN CONTENT

3.1 Profit Maximization

In the market economy of a country, prices of goods and services are determined by the forces of demand and supply. Firms produce goods and services desired by the community in which they serve as efficiently as possible.

It is worthy of note that a business organisation's financing and investment decisions remain continuous in response to the business activities and circumstances around them.

Price mechanism (system) is a vital organ of a market economy, showing the goods and services required in the community. When the goods and services are in high demand, their prices will rise. This will give rise to higher profit margin. Other Firm with similar or complementary goods and services will intensify competition in order to have a share of the market. The equilibrium price will eventually be reached where demand and supply match.

Business firms are frequently profit oriented with maximization of profit as the proper objective.

What is Profit?

It may be expressed as the amount a business can spend in a period and be as "well off" at the end of the period than as at the beginning. In this statement, there are limitations and complications like:

What determines the "well off" of a business (the size and magnitude of activities)?

Is it maximising total profit or rate of profit?

Other problems are risk associated with a project

Profit maximization neglects differences in the degree of risk associated with different income streams.

Risk is the expected variability of the income flow.

This is why Pandey (2005) summarised profit maximization limitations as follows:

It is vague

It ignores the timing of returns

It ignores risk.

Profit maximization objective is not always clear. It may not specify period – short, medium or long term profit – profit before or after tax; total or relative profit; total operating profit or accruing profit.

SELF ASSESSMENT EXERCISE 1

What is profit maximization limitation?

3.2 Wealth Maximization

This is one of the financial goals of a business enterprise. Yes! You should recall in our previous study that Firm's management controls the firm, but the shareholders/entrepreneur are the owners of the business Firm. It is then incumbent on the owners to specify the business concern's primary objective to maximize the utility of the entrepreneurs/owners.

Apart from profit making and maximization, the investors (the contributors to the capital base) wealth should be maximized through the manner of profit sharing.

The finance manager should use it as a basis for making decisions concerning:

Survival

Growth of the business and the owners' delight too.

The financial thrust should correspond with business owners / entrepreneurs primary goal. It is pertinent, at this point, to note that the best primary financial goal to meet the above stated criteria is to maximise the business organisation's value to the existing owners/entrepreneurs.

Market value assessment of the appropriate prices of a business is considered thus:

Current and expected income

Uncertainty and timing of income streams

Dividend policy

Other factors the market considers relevant

The market price hereby reflects the markets' view of management's activity record of business investment, financing and dividend decisions. Invariably, the market's view is largely based upon information provided by management in the business's annual and other reports.

A brief consideration of whether the goal of maximizing the business's value to existing shareholders meets the three criteria earlier specified.

1. **Consider if the objective is operational:** Finance Officer can evaluate alternative courses of action and choose which will increase the business value to the owners by the largest amount.
2. This objective overcomes the problems inherent in the profit maximization objective in that the market price of a business's contribution/shares is an unambiguous concept and its determination takes account of the time value of money and risk.
3. Finally, it is reasonable to assume that the objective is reasonable and consistent with owners/entrepreneurs' interests.

To sum it up then, we should note that the goal of the firm and that of managers and employees are to maximize the wealth of the owners for whom the business is being managed, which in turn, is measured by the value of contribution by owner(s). Therefore, when the finance manager is considering each financial decision, alternative or realistic action, in the light of impact on the firm's contribution, value/ price, he should accept only those actions that are expected to increase contributor's price.

SELF ASSESSMENT EXERCISE 2

In your own words, highlight the limitations of profit maximization.

3.3 Financial Goal and firm's Mission/Objectives

Pandey (2005) stated that the basis of the theory of financial management is the same as that of maximisation of owners' welfare (classical theory of the firm). Every corporate business Firm states categorically their vision, mission and values in broad terms and is also concerned about technology, leadership, productivity, market standing, image, profitability, financial resources, employee satisfaction etc.

Objectives and decision criteria should be distinct.

Goals or objectives are missions or basic purposes of a business's existence. They direct the firm's actions.

The strategies are designed on these basic objectives.

Defines its markets, products and technology.

Policies are laid down in areas of production, purchase, marketing, technology, finance etc.

SELF ASSESSMENT EXERCISE 3

Picture yourself as an entrepreneur.

On this basis, develop a typical mission and objectives of your business.

4.0 CONCLUSION

We have attempted a simplified approach to understanding financial goal of a business firm which we have seen as not being simply profit maximization but considering the well being of the investors too. The two have to be balance by the finance officer in-charge to impact positively on the society.

5.0 SUMMARY

This unit is summarized thus:

The identification of financial goals of a firm seen through profit maximization and wealth maximization.

The blend of the two effectively and efficiently by the financial manager gives the society a good turnaround of the business performance.

Each firm produces a mission and objectives to synchronize with the financial goals to produce goal befitting the entrepreneurs own.

6.0 TUTOR-MARKED ASSIGNMENT

1. Identify main financial goal of a business concern.
2. Explain financial goal based on firm mission and objectives fulfilment.

7.0 REFERENCES/FURTHER READING

Pandey, I.M. (2005). *Financial Management* New Delhi: India: VIKAS Publishing House PVT Ltd. (9th ed).

University of Southern Queens Land, Business Finance I Study Book.

UNIT 2 THE ROLE FINANCIAL MANAGERS

CONTENTS

- 1.0 Introduction
- 2.0 Objectives
- 3.0 Main Content
 - 3.1 Financial Manager
 - 3.2 Fund Raising
 - 3.3 Funds Allocation
 - 3.4 Profit Planning
 - 3.5 Capital Markets
- 4.0 Conclusion
- 5.0 Summary
- 6.0 Tutor-Marked Assignment
- 7.0 References/Further Reading

1.0 INTRODUCTION

In this unit, you will be able to know who a Finance Manager is and identify his role in the financial management ‘mix’ of a firm.

Among other things, he coordinates the flow in the working cycle and makes the correct ‘dose’ of investment to be at the proper place in order to avoid “too much or too little of fund”.

2.0 OBJECTIVES

At the end of this unit, you should be able to:

explain who a Financial Manager is
identify the role of Financial Manager
plan profit of a Business firm
Describe Capital Market.

3.0 MAIN CONTENT

3.1 Financial Manager

This is the person responsible for performing finance functions. In a modern firm, finance manager’s position is significant. He is recognised

as a member of the top management team. He maintains records, prepares progressive financial report through auditing, financial/managerial accounting and assists in raising funds when required.

As an adviser, the finance manager now shapes the fortunes of the firm and he is involved in the most vital decision of allocation of capital.

Finance Manager must be broad in knowledge and far-sighted in outlook, to ensure that the funds of the business outfit are utilized in an efficient and effective way.

Finance decisions influence the size, profitability, growth, risk and survival of the firm; and these in turn, affect the overall value of the firm. Hence, a finance manager must have clear understanding and professional grasp of the nature and scope of the finance functions.

SELF ASSESSMENT EXERCISE 1

Describe a financial manager

3.2 Funds Raising

The scope of financial management includes fund raising in the modern approach to financing. This was not the case in the past because raising funds was always done during major events in the life of the firm like:

Promotion
Re-organization
Expansion
Diversification.

As a cardinal duty, the finance manager sees that a firm is well funded to be able to meet its obligation. This had already been discussed previous unit of this course.

3.3 Funds Allocation

The modern approach to finance is an analytical way of looking at the financial problems of the business. Financial management is therefore considered as a vital and an integral part of overall management.

In a modern firm, the basic function of finance department is to decide about the expenditure decisions and to determine the demand for capital to meet these expenditures. That means, the finance manager is duty bound to allocate funds in an efficient and effective manner.

The finance manager should be able to find answers to the following questions:

How large should the firm be?

How fast should it grow?

What form of assets should it hold?

How should the funds be raised?

3.4 Profit Planning

Profit-planning function is one of the acquired roles of the Finance Manager. Profit planning is the operating decisions in the areas of pricing, costing of the volume of output and the firm's product lines selection.

It is, therefore, a pre-requisite for optimising investment and financing decisions. The cost structure of the business organization (the mix of fixed and variable costs) has a significant influence on a firm's profitability.

Fixed costs remain constant while variable costs change in direct proportion to changes in volume of goods. The fixed costs enhance profit fluctuation at a higher degree than the fluctuations in sales. The change in profits due to the change in sales is an operating leverage.

Profit planning is an aid to anticipating the relationships between volume, costs and profits. It is from here that an action plan emanates.

SELF ASSESSMENT EXERCISE 2

Discuss the different roles of a finance manager.

3.5 Capital Markets

Capital market is the meeting point for investors (lenders) and firms (borrowers), hence, the understanding of the operations of the capital markets and the way in which the capital markets value securities.

In Nigeria, it is known as the Nigeria Stock Exchange (NSE). The Exchange is the market that serves as an intermediary between fund-raisers and supplier of capital. The Nigerian Securities and Exchange Commission (SEC) is the regulator and monitor of activities in the Nigerian Capital Market in order to protect both the largely unaware investing public and issuers of securities.

The finance manager should know how risks are measured and how to cope with dynamism of investment and financing through the capital market.

It is worthy of note that, if a business organization uses excessive debt to finance growth, investors may perceive it as risky. The value of a firm share may shrink or decline. In the same vein, investors may not like the decision of a highly profitable, growing firm to distribute dividend. They may like the firm to plough back the profits into more lucrative and prospective opportunities (investments) that would enhance futuristic prospects of high capital gains.

These types of operations in capital markets are where investors continually assess the capability of the finance manager, after all investments involve risk and return.

SELF ASSESSMENT EXERCISE 3

Investment is about risk and return. Discuss.

4.0 CONCLUSION

We have explained who a financial manager is and also identify the role of the financial manager in a going concern (business organization). The financial manager coordinates the inflow and outflow of fund in the business cycle of a firm.

5.0 SUMMARY

In this unit, we have discussed the financial manager's role as follows:

- Financial Management
- fund raising
- fund allocation
- profit planning and
- The operation of capital markets.

6.0 TUTOR-MARKED ASSIGNMENT

1. What is Capital Market high-lighting its function in the economy?

2. What is profit planning in a firm?

7.0 REFERENCES/FURTHER READING

Anao, A.R et al, Ekundayo, J.O, Osaze, B.E. (1993) *Investment Analysis and Management* Lagos The Chartered Institute of Bankers of Nigeria

Pandey, I.M. (2005). *Financial Management* (9th edition). New Delhi: India: VIKAS Publishing House PVT Ltd.

UNIT 3 INTRODUCTION TO FINANCIAL ANALYSIS

CONTENT

- 1.0 Introduction
- 2.0 Objectives
- 3.0 Main Content
 - 3.1 Financial Analysis: An Overview
 - 3.2 Main Components of Financial Statement Analysis
- 4.0 Conclusion
- 5.0 Summary
- 6.0 Tutor Marked Assignment
- 7.0 References/Further Readings

1.0 INTRODUCTION

In this unit, you will be introduced to financial statement analysis and its main components. You will also be led through the discussion on how financial statement analysis aids management in decision-making process.

2.0 OBJECTIVES

At the end of this unit, you should be able to:

Explain financial statement analysis;

Identify the main components of financial statement and the analysis;

Discuss financial analysis as a tool for management decisions.

3.0 MAIN CONTENT

3.1 Financial Statement Analysis: An Overview

Financial statement is a statement that records financial activities of a particular business organisation (business enterprise). It is the book keeping and recording of source document from the early stage of business enterprise through journalizing to the ledger accounts, trial balance and then the final accounts.

In the early times, keeping financial statement analysis was not a priority because business transactions were undertaken by means of barter system where goods exchanged for goods. With the modern economy, all transactions were monetized and therefore there was the

need to keep records using money as a common denominator, hence financial recording known as financial statement.

Financial statement analysis is used for two purposes, namely: definitive purpose and information purpose. Where it is used for information purpose, it is for comparative analysis to be made within (intra) and between (inter) the industry.

Users of financial statement have further insight about financial strengths and weaknesses of the business enterprise if information (data) reported in the statement are properly analyzed. It is therefore incumbent on the management to have interest in knowing or developing enough passion for the state of the enterprise at any point in time. This shall be possible if management uses the financial report effectively to evaluate the performance of the business and ensure that the business is suitably organised along corrective measures.

Financial statement is also used for future plans of the enterprise. The present financial data of the business is compared with the past in order to project the likely outcome of activities in the future. It is also worthy of note that financial analysis is based on the data collected from financial statement which itself is the starting point (source) of making the plans before using same for forecasting. It is also good to note that the past financial record is a prerequisite for anticipating the future.

It therefore means that financial statement is the custodian of business activity from the beginning and the basis of financial analysis – which measures the business's progress and viability. It contains financial information required to predict, compare and evaluate an enterprise's earning ability. It is the basis for financial analysis, planning and decision-making. The financial statement analysis is used as managerial guide and aid. It is supported on the premise that money values provide a common denominator for the varied activities of an organisation. Financial statement is an accounting report.

Self Assessment Exercise 1

What is financial statement? Briefly explain its role in analysis of an enterprise.

Diagram of a Typical Financial Statement

The pro forma (typical) financial statement of an enterprise is shown below. It is made up of the following:

- (i) Balance sheet
- (ii) Income statement

(iii) Cash flow statement.

These are prepared as final accounts for users of financial reports of the business at the end of the year.

ROI Enterprises

Balance Sheet as at 31st December 20XX

N	N	N
NBV	Cost	Accumulated
Fixed Assets		
Land and buildings	X	X
X		
Plant and machinery	X	X
X		
Furniture and fittings	X	X
X		
Motor vehicles	<u>X</u>	<u>X</u>
<u>X</u>		
	<u>X</u>	<u>X</u>
<u>X</u>		
Long- term Investments		
X		
Current Assets		
Stock		X
Trade debtors	X	
Less: Provision for bad debt	<u>(X)</u>	
		X
Short-term Investments		X
Prepayments		X
Accrued income		X
Bank		X
Cash		<u>X</u>
		X
Less: Current Liabilities		
Trade creditors	X	
Accrued expenses	X	
Incomes received in advance	X	
Bank overdraft	<u>X</u>	
		<u>X</u>
Working capital		
<u>X</u>		

X
Long-term Liabilities

Bank loans

(X)

Net Assets

X

Financed By:

Owner's Equity

Capitals at 1st January 19X4

X

Additional capitals introduced

X

Net profit

X

Less: Drawings

(X)

ROI Enterprises

Income Statement for the Year Ended 31st December, 20XX

	N		N	
Sales			X	
Less: Sales Returns			<u>(X)</u>	
			X	
<u>Less: Cost of Sales</u>				
Opening stock	X			
Purchases	X			
Purchases returns	(X)			
Carriage inwards	<u>X</u>			
Cost of goods available for sale	<u>X</u>			
Closing stock	(X)			
Cost of goods sold	<u>X</u>			
Wages **	<u>X</u>			
Cost of sales			<u>X</u>	
Gross profit			X	
Add: Other Incomes				
Interest received		X		
Rent received		X		
Commission received		X		
Discount received		X		
Decrease in provision for bad/doubtful debt		<u>X</u>		
			<u>X</u>	
			X	

X

Trading Account

Profit and Loss Account

Less: Expenses		
Salaries **	X	
Rent and rates	X	
Carriage outwards	X	
Increases in provision for bad/doubtful debt	X	
Depreciation	X	
Printing and stationery	X	
Discount allowed	X	
Repairs	X	
Telephone	X	
Motor expenses	X	
Loan interest	X	
Advertising	<u>X</u>	
Net profit		<u>X</u>

** **Wages** should be charged in the trading account *only* if shown separately on the trial balance from **salaries**. In such circumstances, the assumption, unless you are otherwise told, is that the wage is a direct trading expense to be included in the trading account while the salary is an indirect (i.e. overhead) expense to be included in the profit and loss (P&L) account.

If only wages is shown on the trial balance, it should be charged to the P&L account unless you are otherwise told.

If both *salaries* and *wages* are combined as one item (i.e. *salaries and wages*) on the trial balance, it should be charged to the P&L account.

ROI Enterprises

Statement of cash flows for the Year Ended 31st December, 20XX

N

N

Operating Activities:

Operating profit

X

Adjustments for items not involving flow of cash: Depreciation charge for the year X (Profit)/loss on sale of fixed assets and long-term investments(X)

Increase/(decrease) in provision of bad debt, etc. X

X

Net cash flow before changes in working capital

X

Change in working capital

(Increase)/decrease in stock (X)

(Increase)/decrease in debtors and prepayments X

Increase/(decrease) in creditors and accruals

(X)

X

Net cash flow generated from operations

Z

VAT paid to government [excess of output VAT over input VAT (X)

VAT refund received from government [excess of input VAT over output VAT] X

Increase taxes paid (X)

X

Net cash flow from operating activities

X

Investing Activities:

Payment for purchase of fixed assets (X)

Proceeds from sale of fixed assets X

Interest received X

Dividend received X

Payment for investments acquired (X)

Proceeds from sale of investments X

Net cash flow from investing activities

X

Financing Activities:

Receipts from issue of shares and debenture X

Interest paid (X)

Dividend paid (X)

Long-term loans obtained X

Repayment of loans (X)

Redemption of debentures and preference shares (X)

Payment of finance lease rentals (X)

Payments relating to acquisition of own shares (X)

Drawdown on loans and overdraft facilities

(X)

Net cash flow from financing activities

(X)

Net increase/(decrease) in cash and cash equivalents

X

Cash and cash equivalents at opening date

X

Cash and cash equivalents at closing date

X

In actual practice, all these statements have notes to explain adjustment and operations where necessary.

Source: Igben, R.O. (2004)

3.2 Main Components of Financial Statement

There are three main components of financial statement used for financial analysis. They are as follows:

- (a) Balance Sheet
- (b) Income Statement
- (c) Cash flow Statement

(a) Balance Sheet

Balance sheet shows the present statement of a business. The business as a single entity shows the financial condition of an accounting entity as at a particular point in time.

Balance sheet consists of assets (probable future economic benefits obtained and controlled by an entity as a result of past transactions or events). They may be physical assets such as land, buildings, stocks, or inventory. Assets may also be intangible such as trademarks, goodwill, copyright, or patent. For instance, assets are normally categorized into current and long-term. This will be discussed in detail in subsequent units.

(b) Income Statement

Income statement is otherwise known as profit and loss account. Other scholars refer to it as statement of income, statement of earnings and statement of operations. It is a summary of income and expenses, gains and losses of a business organisation and ends with the determination of net income for a specific period.

Income statement reveals the revenue (income) and expense (disbursements); hence the profit and loss is expressed with the

true position of the net income. Management will have the profitability index and decision will be taken based on this.

The management can ask basic questions like “Can the present profit margin sustain the business?” “Should the business go for borrowing?” “Is the leverage position of the business alright?” “Should the company expand its operations?” “Can the business add to its human resource needs?”

The elements of income statement are:

- (i) Net sales (revenue/income)
- (ii) Cost of goods sold or cost of sales
- (iii) Other operating revenue
- (iv) Selling expenses
- (v) Administrative expenses

(c) **Cash flow Statement**

The analysis of cash flow benefits is for short-term planning with a view to generating enough cash to settle indebtedness maturing in the near future, to pay interest on borrowing and other expenses and to pay dividends to shareholders. The enterprises can make projects of cash inflows and outflows for the near future to determine the availability of cash. This cash balance can be matched with the needs of the business for the period and appropriate arrangement can be put in place to meet deficit or invest surplus cash temporarily. It should be noted that a historical analysis of cash flow provides an insight for the preparation of reliable cash projection for the immediate future.

On the other hand, the cash statement enables management to explain the changes in cash and cash equivalent production. Management can use cash flow statement for dividend posting, cash generated by operations, investing and financing policy.

Basic elements of cash flow include the following:

- (1) **Operating Activities:** consist of all transactions plus other events that are not investing or financing activities. Cash flows from operating activities are generally the cash effects of transactions and other events that are added to determine the net income.

- (2) **Investing Activities:** consist of lending money and collection of these loans and acquiring and selling investments and productive long-term assets.
- (3) **Financing Activities:** consist of cash flows relating to liability and owners' equity.

The details of these cash flow activities will be expressed in subsequent units with illustration to back them up.

3.3 Financial Statement as a Management Tool

Financial statement helps in presenting the financial to oversee the resources of the information and data of an organization. The statement will be meaningless if they are not appropriately utilized.

Users of financial statement include managers of business, financial analysts, consultants, researchers, trade creditors, suppliers of long-term debt, bankers, investors, etc. In this course, we will concentrate on its usefulness to management as a tool for decision making.

It is the overall responsibility of management to oversee the resources of the enterprise. Financial statement presents the accounting reports with dependable financial information to guide and aid management in evaluating the performance of the business outfit. This is done through the interpretation and analysis of the financial statement, either directly or through consulting experts, within or outside the management circle.

The financial statement properly prepared forms the basis for financial planning by management. The management will, at the end, take appropriate decision on how to run the business efficiently and effectively.

Financial statement analysis helps management predict, compare and evaluate the enterprise's activities and forecast the earning ability of the enterprise. It is the financial statement analysis that will direct management on the financial condition of the enterprise as well as the statement of affairs of the enterprise at a particular moment in time.

It should be noted that in modern management, the head of financial management belongs to the management team and is always a reference point of the top management on financial issues. His/her expertise is always sort before a financial decision is made. If this is ignored, the management will not have the true and fair picture of financial position and consequence is always a negative one.

With the balance sheet, the financial position of the assets and liabilities is known and management will always be informed. Hence, it is worth of note that financial statement position and its analysis/interpretation would enable management to respond to the challenges posed by this analysis appropriately.

Self Assessment Exercise 2

Discuss financial statement analysis as a tool for management decision making.

4.0 CONCLUSION

We hereby conclude that the financial statement is a record of financial activities of an organization which is used for financial analysis. When properly analyzed and utilised by management it can turn out to be a guide to the growth and development of the enterprise.

5.0 SUMMARY

In this unit, we have taken a brief overview of financial statement analysis, alongside the main components like balance sheet, income statement and cash flow statement. The unit concludes with the discussion of financial statement analysis as a tool for management decision making.

6.0 TUTOR MARKED ASSIGNMENT

1. Identify the main components of financial analysis.
2. Discuss financial statement analysis as a tool for management decision.

7.0 REFERENCE/FURTHER READINGS

Gibson, C.H. (1998). *Financial Statement Analysis using Financial Accounting Information*, 7th Edition, Ohio, USA: South-western College Publishing.

Igben, R.O. (2004). *Financial Accounting 1 & 2* Lagos: El-Toda Ventures Limited.

Jones, G.L. (1976). *Financial Measurement for Managers* London: Edward Arnold (Publication) Limited.

Pandey, I.M. (2005). *Financial Management* New Delhi: Vikas Publishing House PVT Limited.

UNIT4 PROFIT PLANNING AND PRICING

CONTENTS

- 1.0 Introduction
- 2.0 Objectives
- 3.0 Main Content
 - 3.1 Profit Planning
 - 3.2 Pricing
- 4.0 Conclusion
- 5.0 Summary
- 6.0 Tutor-Marked Assignment
- 7.0 References/Further Reading

1.0 INTRODUCTION

In this unit, you will learn how to discuss profit planning, explain pricing and how management applies them to the benefit of entrepreneurial growth and development.

2.0 OBJECTIVES

At the end of this unit, you should be able to:

- Discuss profit planning
- Explain pricing

3.0 MAIN CONTENT

3.1 Profit Planning

Budget is the profit plan base. A well managed enterprise usually produces a budget cycle planning the performance of the organisation as a whole including the profit projections.

Profit planning is related to considering four main factors – fixed costs, variable costs, selling price and sales volume. Any change in one or several of other factors, affect the planned profit.

The management has to develop strategies in making sure these factors are properly mixed regarding the term – short, medium or long for the enterprise and the competitions thereof.

Self Assessment Exercise 2

Budget is the profit plan base. Explain

3.2 Pricing

In our study of pricing, there are many factors critical to the success of an enterprise's short and long term plans. Importance is attached to cost control because of its susceptibility to control than other factors. In the concept of cost -volume-profit analysis is the centre of short-term planning, but in any given enterprise's cost structure, price changes could affect both the sales volume and the profit level. (Consideration of the purchasing power, task demand rate etc). In short, management ability to improve profits through price changes will depend on its knowledge of how the market will react to such changes.

Therefore, a well formulated pricing policy or strategy which considers the likely effects of price changes on the market's demand for the enterprises product, so as to plan a level of operation which, given the enterprise's cost structure will produce the required profit.

We may therefore associate in the study of pricing, the problem of management in the two-fold aspect

The problem of control-in-the-large and
That of control-in-the-small.

Pricing policy provides the means in which the enterprise can control to a degree, its relationship with its external environment (control-in-the-large) and at the same time, it is controlling its internal operations accordingly (control-in-the-small).

A further dimension to the problem of pricing: like if an enterprise formulates a pricing policy affecting its relationship with the market, such a policy has short term and long term implications (effect). Any alteration in the volume of demand for the enterprise's products which results directly from its own pricing policy will affect its capital budgeting programme.

Hence, in summation an enterprise's long- term projected plan should reflect its long-term pricing policy. Thus, short-term changes in that policy should be effected solely for providing that degree of flexibility which essential for effective long-range planning and control.

Self Assessment Exercise 1

Explain pricing and its implication, in an enterprise as a going concern.

3.0 CONCLUSION

Pricing in an enterprise has been shown as an integral decision form of an enterprise which aids in profit planning process and policy formulation.

4.0 SUMMARY

In the unit, pricing and profit planning were discussed in the line with the pricing policy and decision limitation of an enterprise.

5.0 TUTOR-MARKED ASSIGNMENT

- 1 What is pricing in an enterprise?
2. Discuss profit planning giving the main factors of consideration.

6.0 REFERENCES/FURTHER READING

Glantier MWE & Underdown B. (1978) *Accounting Theory and Practice*
PITMAN Publishing, London.

Horngren, C.J., Foster, G. Dta, S.M. (2000) *Cost Accounting – A
Managerial Emphasis* Prentice Hall, London

UNIT 5 INTRODUCTION TO WORKING CAPITAL MANAGEMENT

CONTENTS

- 1.0 Introduction
- 2.0 Objectives
- 3.0 Main Content
 - 3.1 Working capital management
 - 3.2 The main components of working capital management
 - 3.2.1 Cash Management
 - 3.2.2 Receivable management
 - 3.2.3 Inventory Management
- 4.0 Conclusion
- 5.0 Summary
- 6.0 Tutor-Marked Assignment
- 7.0 References/Further Reading

1.0 INTRODUCTION

This unit, you will be introduced to working capital management. In business, when sales arise not in cash, the immediate outlet is receivables – accounts receivables or trade debtors and current asset cash and receivables (debtors) which assist in the operation of a business enterprise. The management of these receivables is very vital to the business as a going concern. Organisations usually have claims to future inflows of cash. These claims are known as accounts receivables and note receivables expressed in financial statements.

Inventories are the balance of goods on hand (part of current assets). In a producing enterprise, they comprise raw materials, work-in-progress and finished products. These inventories need to be managed properly to avoid unnecessary cost. Management of inventory will be explained as part of working capital management.

2.0 OBJECTIVES

At the end of this unit, you should be able to:

- Explain working capital management
 - State the main components of working capital management
 - Explain receivable management
- List Steps to Cash Management
- Explain the process for managing inventory

3.0 MAIN CONTENT

3.1 Working capital management

Working capital management refers to the management of current or short-term assets and short-term liabilities. Components of short-term assets include inventories, loans and advances, debtors, investments, and cash and bank balances. Short-term liabilities include creditors, trade advances, borrowings and provisions. The major emphasis is, however, on short-term assets, since short-term liabilities arise in the context of short-term assets.

Working capital management is, therefore, concerned with the ways and means of making working capital adequate to meet the firm's short-term obligations. The effective working capital management involves the adoption of appropriate management policy.

3.2 The main components of Working capital management

Cash management

Receivables management

Inventory management

3.2.1 Cash management focuses on managing cash flows in and out of an enterprise i.e. cash flows within and cash balances held by an enterprise at a given point in time which is utilised either by financing the deficit gap or investing surplus cash. **Note:** Sales generate cash disbursed. Surplus cash is invested while deficit is borrowed to make-up.

Cash management attempts to control cash cycle at a minimum cost and tries to achieve liquidity. Cash management places cash as the most significant and at the same time the least productive asset at the disposed of an enterprise. It is a means of settling indebtedness of the enterprise. It is not easy to predict cash flows accurately, that means, it takes time and dexterity to achieve its ideal position. That means the aim of cash management is to maintain adequate control over cash position to be able to keep the enterprise sufficiently liquid and to use excess cash in some profitable way.

Cash management is concerned with the managing of:

Cash flows into and out of the enterprise

Cash flows within the enterprise

Cash balances held by the enterprise at a point of time by financing deficit or investing surplus cash.

Self Assessment Exercise 1

What is cash management?

Steps to Cash Management

This involves two paths of action – (i) having the right amount on hand to pay your bills (2) using any excess of that amount wisely. We will now consider an approach for a reliable cash management which involves four steps:

- 1) Keeping adequate records on cash book control
- 2) Identifying the cash flow pattern
- 3) Estimating future cash balances and
- 4) Utilizing excess cash to generate income.

Cash comes from:

Daily cash sales

Payments made by customers to their accounts

Loans acquired for short-term needs

Additional capital borrowed on long term basis.

Motives for holding cash

Business need to hold cash to achieve the following three motives:

Transactions, Precautionary and Speculative

Transaction Motive

This requires an enterprise to hold cash to perform its ordinary business activities. This cash is to pay for purchase, wages and salaries, other operational expenses, tax dividends etc. With effective management of cash receipts and cash payment will make the holding of cash not necessary as there will be enough cash when payment is to be made.

Precautionary Motive

This is for the enterprise to meet up contingencies as they arise in the future. Cash at this stage is used to provide a cushion or buffer to withstand some unexpected emergency. The precautionary amount of cash will depend upon the predictable nature of the cash flow of the business.

Speculative Motive

This is holding cash for investing in profit-making opportunities as and when the need arises. The opportunity to make profit by an enterprise may arise when the security prices change. This is an opportunity to hold cash and expect a rise in interest rates and security prices will fall.

Self Assessment Exercise 3

Explain the three principal motives for holding cash

3.2.2 Receivables Management

Trade credit make way for trade debtors otherwise known as account receivable which a business (an enterprise) expects to receive in form of cash in the near future (usually within a short period within the financial period e.g. a week, fortnight, month, quarter, half a year, a year). The customers benefiting from this gesture are known as trade debtors or generally listed as debtors (to be claimed as asset of the organisation).

Receivables are risk elements, meaning that management must identify some elementary facts (characteristics).

1. It involves the analysis of the implication of value of credit sales. Cash sales are riskless. Credit sales need to be carefully analysed as cash payment will be in future. The integrity of the beneficiary of the sales must not be in doubt judging by the track record of the trade business.
2. Based on economic value, the purchaser benefits at the time sales immediately while the owner of the sales expects an equivalent of the trade value in future time.
3. It connotes that the buyer will provide the cash payment for the good/services received in a future period.

The time lag is the risk which is borne by the seller. He need be sufficient and surplus in its cash holding, control and management to stay afloat till that aspect of account is received as a whole. Any hiccup in repayment by the customer (beneficiary) will negative affect the cash flow level at the expected time. You should note that debtors form a reasonable part of current assets of many enterprise especially where the customer need this service to enhance their being in business as a going concern.

Self Assessment Exercise 1

“Receivables expect cash in future”. Discuss

3.2.3 Inventory management

Inventory management is a tool to avoid excessive and inadequate levels of inventories and maintain sufficient inventory for the smooth operations of the enterprise in terms of production and sales output. The management should provide the enterprise with an order at the right time with the right source to acquire the right quantity at the right price and quality.

An effective inventory management ensures

A continuous supply of raw materials to facilitate functional production and distribution.

The maintenance of sufficient stocks of raw materials in short supply period and anticipate changes in price level

Sufficient finished goods inventory for smooth sales distribution in order to sustain efficient customer service.

Minimum carrying cost and time and

Investment control in inventories and optimum level of operation.

Self Assessment Exercise 2

Explain the effectiveness of inventory management in facilitating production.

Managing current assets generally require a great attention and inventory is inclusive.

Inventory is constantly being in use. Raw materials and work-in-progress inventories are used in production. Finished goods are sold, spare parts replace worn-out parts. The rate of usage, depend on the type of inventory.

Managing the level of inventory can be compared with maintaining the level of water in a bath tub with an open drain. The water flows out continuously. If it flows too slowly, the tub is soon empty. If it is let too fast, the tub overflows. Like the water tub the particular inventory items is dynamic, while the level may stay the same.

The fundamental financial decision problems are:

- to determine the proper level of investment in inventory and
- to decide how much inventory to be acquired at each period to maintain the required level.

Maintaining inventories means:

- Tying up the enterprise's funds and

- Incurrence of storage and
- Handling of costs.

4.0 CONCLUSION

We have identified cash management as a tool to maintain control over cash position which enhances the effectiveness of an enterprise to keep the required liquidity level and utilise the excess cash for profitable venture.

We conclusion is that the major factor of managing receivables is that the organisation expects to receive cash eventually in the future.

5.0 SUMMARY

In this unit, we have discussed cash management steps and control, sensitivity analysis and motives for holding cash. You have also learnt about receivables management. And In this unit, you have learnt about inventory management as part of working capital and the techniques there of.

6.0 TUTOR-MARKED ASSIGNMENT

1. Why is inventory management important?
2. Explain cash management in an enterprise.

7.0 REFERENCES/FURTHER READING

Gibson, C.H. (1997). *Financial Statement Analysis using Financial Accounting Information* South-Western College Publishing

Hand, H. H. & Hollingsworth, A. T. (1979) *Practical Readings in Small Business*, W.B. Sunders Coy

NOUN (2012) Course Material on *Managerial Finance (MBF 718)*

Ola, C.S. (1982). *Management Accounting: Theory and Application*. Bedfordshire Graham Burn

Pandey, I.M. (2005). *Financial Management* 9th Ed. VIKAS Publishing House – PVT New Delhi

MODULE 3

Unit 1	Basic forms of business organization
Unit 2	Sources of Business Finance
Unit 3	Financial planning and forecasting
Unit 4	Finance in the Firm's organization structure
Unit 5	Finance and related disciplines

BASIC FORMS OF BUSINESS ORGANISATION

CONTENTS

1.0	Introduction
2.0	Objectives
3.0	Main Content
	3.1 Sole Proprietorship
	3.2 Partnership
	3.3 Limited Liability Company
4.0	Conclusion
5.0	Summary
6.0	Tutor-Marked Assignment
7.0	References/Further Reading

1.0 INTRODUCTION

There are three main forms of business organizations- the Sole proprietorship, Partnership, and Limited Liability Company. Each of these has its own distinguishing features/characteristics, as well as merits and demerits.

2.0 OBJECTIVES

After studying this Unit, you should be able to:

- List the three basic forms of business organizations.
- Identify their features

3.0 MAIN CONTENT

3.1 Sole Proprietorship

A Sole proprietorship or one – man business, as the name implies, is a business concern owned by one person who often is also engaged actively in the running of the business. The sole owner subscribes to all of the equity capital of the business which in most cases are raised from personal savings or soft loans obtained from relations and friends. All incomes also accrue to the owner.

Other characteristics/features of one – man business include the following:

A sole proprietorship has no distinct legal entity.

The owner has freedom to deal with the organisation's assets without any restrictions;

it is often small and can be recognised easily;

Its capacity to borrow (especially from banks) is limited;

It has very high risk because of the inseparability of the owner with the business;

The structure is simplistic in nature.

3.2 Partnership

A partnership is generally defined as a legal relationship between two or more persons where each person contributes something in order to carry on a lawful business with a view of profit which is to be shared between the partners in a proportion agreed upon by them. Therefore, for a partnership to exist:

the association must be engaged in a business which may be a trade or a profession;

the trade or the profession must be carried on together, jointly, for the benefit of all the partners; and

there must be an intention to earn a profit.

The above description, therefore, distinguishes a partnership from a political, religious, social, or philanthropic club or association. A partnership agreement, which need not necessarily be in written form (although it is advisable or wiser that any agreements between the partners be reduced to writing as this will tend to lead to fewer possibilities of misunderstandings and disagreements between partners), will govern the relationships between the partners, including:

name of organisation, the type of business, and duration;

capital to be introduced by partners;
 sharing of profits between parties, including salaries since not all the partners may be employed by the partnership on a full-time basis. Such salaries will be normal operating expenses;
 drawings by partners;
 arrangements for dissolution, or on the death or retirement of partners;
 settling of disputes;
 preparation and audit of accounts.

At this juncture, it is necessary to note that, although the partnership agreement creates a legal relationship between the partners, the partnership itself is not a legal entity.

We can highlight the essential features of a partnership as follows:

- (i) Partnership is not separated from the partners.
- (ii) Setting-up cost is low and it is easy to form.
- (iii) Life of partnership is limited because it is a legal entity.
- (iv) Regarding liability, the partners must risk all their personal assets, even those not invested in the business, for under the partnership each partner is for the business' debts.
- (v) Partners share in the profits of the business according to their individual financial contribution to the business.
- (vi) The death of a partner can dissolve the partnership.

Self-assessment exercise

State the characteristics of a sole proprietorship.

3.3 Limited Liability Company

A limited liability company (or company) may be defined as an artificial creature, invisible, intangible, and existing only in contemplation of law. As a legal (artificial) person, it is separate from the owners. It can enter into a contract, sue and be sued in its name. Examples are First Bank, Julius Berger etc.

A company is legally formed by meeting the conditions stipulated in the Companies and Allied Matters Act (Decree), 1990. The promoters must apply for registration at the Corporate Affairs Commission together with both a Memorandum and Articles of Association.

The Memorandum of Association must contain the following information:

name of the company, with the term “Limited” as the last word of the name;

objects for which the company is formed;
 amount of the share capital with which the company proposes to be registered and the division into shares of a fixed amount;
 address of the registered office of the company; and
 a statement to the effect that the 'liability' of the members or shareholders is 'limited'.

The Articles of Association, on the other hand, setting out the regulations for internal organisation, and contains provisions relating to:

proceedings at meetings;
 alteration of capital;
 appointment of directors;
 borrowing powers of directors;
 transfer or transmission of shares;
 winding-up procedure, etc.

The Memorandum and Articles of Association, duly stamped for stamp duties and fees, and accompanied by certain other forms, are lodged with the Registrar-General, who if everything is in order, issues a Certificate of Incorporation. At that point, a Limited Liability Company is formed, and those who signed the memorandum are its "foundation members".

From the foregoing, let us highlight the following distinguishing features of a company as follows:

Separate legal entity, which is not affected by changes in its ownership;
 Can own assets and incur liabilities in its own right;
 Can sue or be sued in its own name;
 Has perpetual succession – does not cease to exist upon the death of any or all of the owners;
 Liability of owners/shareholders is limited to the amount paid for shares allocated;
 Has the right to borrow on its own account;
 External audit is compulsory;
 Profits are subject to Company Income Tax;
 Statutory annual returns to the Corporate Affairs Commission.

Self-assessment exercise

Define a Company

4.0 CONCLUSION

The knowledge of the distinguishing features/characteristics of the three basic forms of business organisations, as well as their strengths and weaknesses, is essential in the study of Managerial finance.

5.0 SUMMARY

In this unit, we have been able to consider that:

The three basic legal forms of business organisations are:
the Sole proprietorship (one – man business)
Partnership and
Limited Liability Company.

6.0 TUTOR – MARKED ASSIGNMENT

- 1 State the basic forms of business
- 2 List the characteristics of a limited liability company

7.0 REFERENCES/FURTHER READING

NOUN (2008) Course Material on *Financial Accounting (ENT 222)*

NOUN (2008) Course Material on *Financial Accounting (BHM 624)*

NOUN (2012) Course Material on *Managerial Finance (MBF 718)*

Pandey, I.M. (2005). *Financial Management* 9th Ed. VIKAS Publishing House – PVT New Delhi

Weston J. Fred and Brigham, Eugene F. (1990) *Essentials of Managerial*

Finance, 9th Edition Chicago: The Dryden Press.

UNIT 2 – SOURCES OF BUSINESS FINANCE

CONTENTS

- 1.0 Introduction
- 2.0 Objectives
- 3.0 Main Content
 - 3.1 Sources of Business Finance
 - 3.1.1 Short-Term Sources
 - 3.1.2 Long-Term Sources
- 4.0 Conclusion
- 5.0 Summary
- 6.0 Tutor-Marked Assignment
- 7.0 References/Further Reading

1.0 INTRODUCTION

Financial sources or funds available to a business organization could be classified into short-term, medium term, and long-term, or into short-term and long-term. Sources of funds available to business organizations could be classified into two main categories:

- Internal
- External

These categories have different types of sources, that is a firm can generate funds internally or externally to finance its activities. External sources could also be short-term or long-term. This unit will focus on how firms acquire funds in order to acquire assets.

2.0 OBJECTIVES

At the end of this unit, you should be able to:

- List and discuss the external sources of finance;
- Classify the sources of finance for a firm;

3.0 MAIN CONTENT

3.1 SOURCES OF FUNDS

3.1.1 Short-term sources

Short-term sources of funds represent current liabilities (funds owed). They represent short-term obligations. Since they are supposed to be settled by cash, they represent cash payments which must be settled as at when due. Examples of current liabilities and their sources are explained as follows:

Owner's Equity: The owner contributes as owner/shareholder who bears the risk of the business.

Bank Overdraft: The source of overdraft is commercial banks, and they grant this to creditworthy firms. Funds could be advanced to such firms within a period ranging between one day and one year. These loans are supposed to be repaid on self-liquidating basis.

Account Payable: This is trade credit. A firm can buy something on credit. Supplies could be made on credit, and they give rise to trade credits.

Bill Finance: This is bill is a promissory note. But there are different types of bills and complexity exists in their meanings. In our case, a bill is a trade bill of exchange which could be domestic or foreign. If a bill of exchange (inland) is accepted from discounting operations.

Deferred Tax Payment: Tax payment could be looked at from two perspectives: Self imposed (a firm will not pay when it is supposed to pay and that becomes a source) and Late assessment.

Factoring: Debt could be factored. This is another source of short-term funds. Factoring involves handing over of account receivable or any other debt to factors for collection with or without recourse.

Hire Purchase Finance Arrangement: Firms that engage in selling on installment basis can make arrangement with hire purchase firms to make credit facilities available to customers. Alternatively, a firm may make hire purchase agreement with its customers.

Stock Finance: Stocks could be used to raise short-term funds in a number of ways. They could be used as collaterals for secured loans from commercial or merchant banks. Raw materials could be financed en route by means of trade bills and/or warehouse receipt. This represents another type of secured loans on the value of stock of raw materials. The bill could become negotiable if endorsed by a reputable commercial house or bank, and could thereafter be sold outright or used as collateral for a loan.

SELF-ASSESSMENT EXERCISE

List and explain six short-term sources of finance for a firm.

LONG-TERM SOURCES

Two major external sources of long-term funds are: Financial institutions (including lease finance companies), and Capital market.

Capital market is classified into: Organized and Unorganized.

The organized capital market will be our focus because it is the capital market that will assess the performance of the firm.

Firms raise money from the capital market by: Issuing common stock (C/S); And Issuing instruments of debt (long-term liabilities).

Note that a firm cannot issue debt instruments if it has no common stock.

Common Stock: Equity shares, common stock and ordinary shares, all mean the same thing, but a stock is a group of shares, that is, a stock is made up of shares. Ordinary shares could be issued by firms which have been quoted on the stock exchange. Ordinary shares constitute the equity base of a firm, and represent ownership of the firm on pro-rata basis. This implies that an individual investment is a small proportion of total investment.

Each equity shareholder is entitled to a proportionate part of the firm's residual profit and asset. The capital contributed by the shareholders is, therefore, known as risk capital. But they have some compensation like voting rights.

Preference Shares: The next class of shares which ranks above equity shares are the preference shares. They are also known as preference stocks. Preference shares occupy an intermediate position between common stock and debenture stocks. Preference shareholders are entitled to fixed dividend payment as different from equity shareholders which are entitled to variable dividend payments. They are imperfect creditors because tax is paid before fixed dividend is paid to them; they are not creditors and they are not the owners of the firm. They do not normally have voting rights unless otherwise stipulated in the terms of the issue. There are various types of preference shares:

- (1) Cumulative preference shares
- (2) Participating Non-Cumulative shares
- (3) Participating Cumulative shares
- (4) Redeemable and irredeemable Preference shares
- (5) Convertible Preference shares

1. Cumulative Preference Shares

Preference shares could be cumulative or non-cumulative. Cumulative preference shares allow for dividend payment to be deferred if a firm does not make adequate profit to pay such dividend. Therefore, such firms are normally required to pay such dividends in arrears before dividend could be paid to common shareholders. Non-cumulative preference shares do not allow for any form of deferment of dividend payment.

2. Participating Non-Cumulative Preference Shares

This class of shareholders is entitled to a non-cumulative dividend at a fixed rate but without a right to participate in the residual profit of a firm after the equity shareholders has been paid.

3. Participating Cumulative Preference Shares

This class of shareholders is entitled to participate in the residual profit of a firm in addition to the cumulative fixed dividend rate (i.e. they combine the features of cumulative and participating).

4. Redeemable and Non-Redeemable/Irredeemable Preference Shares

Preference shares could be redeemable or irredeemable. Redeemable preference shares are normally redeemed after a fixed period of time. We can say that this class of preference shares has a definite maturity period while irredeemable preference shares do not have definite maturity period (but it could be sold at the security market – an artificial maturity period).

5. Convertible Preference Shares

Convertible preference shares convey upon the holders the right to convert these shares into equity shares in accordance with the terms of issues. This is an issue with speculative features. These shares are corporate fixed-income securities that the investor can choose to turn into a certain number of shares of the company's ordinary shares after a predetermined time span or on a specific date. The fixed income component offers a steady income stream and some protection of the investors' capital. However, the option to convert these securities into stock gives the investor the opportunity to gain from a rise in share price. It can be summarized that convertible preference shares give the assurance of a fixed rate of return plus the opportunity for capital appreciation.

Debenture Stocks: These are corporate bonds.

Two categories of debentures are:

All banks debentures

This involves one to one relationship between a bank and a firm, and lending is based on the assets.

Debenture Stocks – Debenture stocks or corporate bonds are normally issued under a firm's seal. This represents the legal evidence of a firm's indebtedness.

A debenture stock holder is a creditor to the firm, therefore, he is entitled to a fixed interest payment whether a firm makes profit or not. Debenture stock

holders do not have any voting right and their interest in the firm is limited to the fixed interest payment no matter how successful the firm may be.

Lease Financing: This is an important source of long-term funds. It may be used as a source of financing company expansion or for modernization of the productive apparatus of the firm. Thus, through leasing, a company may make use of an equipment without actually owning it. The main objective of leasing is to put at the disposal of a firm a plant or any fixed asset which serve the productive need of such a firm. The firm, in making use of that equipment, is obliged to pay to the lessor adequate sum of money which constitutes cost on the part of the firm. Three types of leases are:

Operating lease;
Financial lease;
Sale and leaseback.

Self-assessment exercise

Discuss the various types of debenture.

4.0 CONCLUSION

A firm can source for funds, internally or externally, to finance its activities. These sources could be short-term or long-term, and the funds so acquired are used in turn to acquire assets. The capital market is very important to the firm in the acquisition of long-term funds.

5.0 SUMMARY

In this Unit, we have been able to classify the sources of finance for a firm and enumerate and discuss the various short-term and long-term sources of finance;

6.0 TUTOR-MARKED ASSIGNMENT

List six short-term sources of finance for a firm.

7.0 REFERENCES/FURTHER READING

NOUN (2012) Course Material on *Managerial Finance (MBF 718)*

Pandey, I.M. (2005). *Financial Management* 9th Ed. VIKAS Publishing House – PVT New Delhi

Weston J. F and Brigham, E F. (1990) *Essentials of Managerial Finance, 9th Edition* Chicago: The Dryden Press.

UNIT 3 FINANCIAL PLANNING AND FORECASTING

CONTENTS

- 1.0 Introduction
- 2.0 Objectives
- 3.0 Main Content
 - 3.1 Financial Planning
 - 3.2 Process of Forecasting
- 4.0 Conclusion
- 5.0 Summary
- 6.0 Tutor-Marked Assignment
- 7.0 References/Further Reading

1.0 INTRODUCTION

Planning is a process of achieving specified objectives. Planning involves the selection of objectives and the means of achieving them. It presupposes that alternative procedures for achieving the same objective exist. Planning involves taking decisions in advance on the following:

- What should be done?
- How could it be done?
- When should it be done?
- By whom should it be done?

These are the basic questions a planner should answer and they are basic factors that should be taken into consideration in the planning process. There exists a gap between objective and achievement, and planning helps the planner to fill the gap.

In this unit, however, we shall be concerned with financial planning. We shall define financial planning; consider the process of financial forecasting.

2.0 OBJECTIVES

After a careful study of this unit, you should be able to:

- define financial planning;
- enumerate and discuss the steps in the forecasting process;

3.0 MAIN CONTENT

3.1 FINANCIAL PLANNING DEFINED

What is financial planning?

Financial planning is not just forecasting.

Financial planning does not attempt to minimise risk.

There is a relationship between planning and budgeting. Planning helps to identify the output desire but budgeting helps to identify the inputs required.

A financial plan is a budget. A budget, therefore, interprets all the elements of a plan in financial terms. In corporate financial planning, the first thing that is done is to set objectives and goals (an objective is broader than a goal; a goal is more specific).

3.2 PROCESS OF FORECASTING

We can use financial ratios to identify symptoms and look for remedial action. Ratios can also be used to forecast and predict the future of the business. The terms FORECASTING and PREDICTION are commonly used as synonyms (used interchangeably), but they refer to different things.

Forecasting is used to cast forward the past performance into the future. The forecasting is based merely on the historical experience of a single time series.

Prediction, on the other hand, is based on available information including economic condition. Prediction is frequently used in planning for funds. The objective of prediction is to increase accuracy and correct planning. The prediction process is usually divided into two, namely:

- (i) Forecasting (projecting) the past time patterns (historical patterns) into the future;
- (ii) Modification of the forecast, on the basis of new/current information (because the situation that existed in the past might have changed).

The process of forecasting and modification could be illustrated as follows:

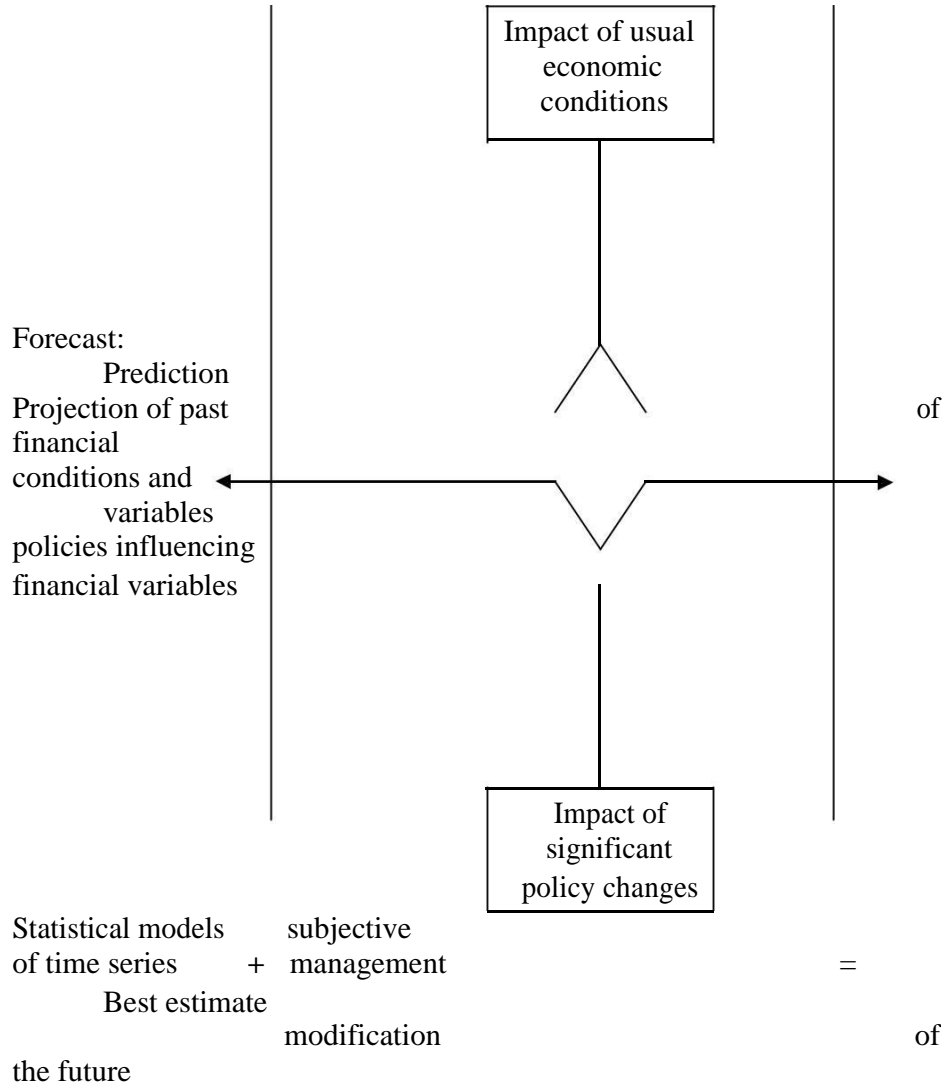


Figure 2.2: Process of Forecasting and Modification

From the above, the impact of significant policy changes will lead to modification of the forecasted future. Forecast is computed statistically from observations from the time series. The forecast, therefore, projects the historical behaviour of a variable directly without requiring the specification of individual influences. The second aspect is to modify the forecast based on the subjective estimate of the impact of changing management policies and economic conditions.

It is essential to modify the forecast because certain conditions which existed in the past may not persist in the future. Thus, a modified forecast is the best estimate of the future variable. The modified forecast is, therefore, known as prediction.

Thus, three (3) steps could be used in the forecasting process. They are:

- (i) Model identification (MI)
- (ii) Estimation of parameters (EP)
- (iii) Diagnostic check (DC) (i.e. test of accuracy and compliance with theoretical model).

Model identification (MI) involves graphing the variables to identify the pattern for a given number of years while Estimation of parameters is the determination of the functional relationship or algebraic expression.

It is important to compute the periodic changes known as the first difference (). This is a very common feature or procedure for time series analysis of financial data. This is because financial time series are not stationary but often trends (moves) upwards. The first difference, therefore, helps to transform the non-stationary series to stationary ones.

It should, therefore, be noted that a non-stationary time series has the tendency to move away from the main value towards infinity while a stationary time series value varies around its main value.

SELF-ASSESSMENT EXERCISE

Enumerate and discuss the steps in the forecasting process.

4.0 CONCLUSION

Sales forecasting usually combines various techniques. Opinions of the sales staff are sought. Statistical methods are often used. Correlation between sales and economic indicators help to make sales forecasts more reliable. In most cases, the quantitative analysis provided by economists and members of the research staff provide valuable help but not outright answers.

5.0 SUMMARY

In this unit, we have considered that:

- a financial plan is a budget;
- a budget interprets all the elements of a plan in financial terms;
- forecasting is used to cast forward the past performance into the future;

it is important to modify the forecast because certain conditions which existed in the past may not persist in the future; the modified forecast is known as prediction, and it is the best estimate of the future variable;

6.0 TUTOR-MARKED ASSIGNMENT

1. Diagrammatically explain the process of forecasting and modification.

7.0 REFERENCES/FURTHER READING

NOUN (2012) Course Material on *Managerial Finance (MBF 718)*

Pandey, I.M. (2005). *Financial Management* 9th Ed. VIKAS Publishing House – PVT New Delhi

Weston J. F. and Brigham, E. F. (1990) *Essentials of Managerial Finance, 9th Edition* Chicago: The Dryden Press.

UNIT 4 FINANCE IN THE FIRM'S ORGANIZATION STRUCTURE

CONTENTS

- 1.0 Introduction
- 2.0 Objectives
- 3.0 Main Content
 - 3.1 Definition of Finance
 - 3.2 The Finance Function
- 4.0 Conclusion
- 5.0 Summary
- 6.0 Tutor-Marked Assignment
- 7.0 References/Further Reading

1.0 INTRODUCTION

The subject of finance is not only discussed, but is part of all disciplines and all facets of socio- economic activities of humans. Finance has evolved to assume a very important position in the decisional process of households, businesses, governments and other non-business organisations. No financial decision can be efficiently and effectively implemented without financial structure.

In this introductory Unit, we shall attempt to answer the following questions:

- What is finance?
- How is finance related to other disciplines?
- Explain financial structure in an organization

2.0 OBJECTIVES

After studying this unit, you should be able to:

- define finance clearly;
- explain the concept of financial structure in an organization management;

3.0 MAIN CONTENT

3.1 Definition of Finance

The field of finance is broad and dynamic. It directly affects the lives of every person and every organisation. There are many areas for study and large number of career opportunities available in the field of finance.

Finance has been defined in different ways. Each definition however reflects the perception of finance relative to its role and scope. However, it may not be possible to give a precise and very comprehensive definition to such a wide, complex and important subject which is of interest to everybody.

Webster's third International Dictionary, for example, defines finance as "the system that includes the circulation of money, the granting of credit, the making of investments and the provision of banking facilities." This definition gives an indication to the fact that finance is a system by itself and thus a broad field of activities at the centre of economic operations or social activities with economic implication.

The Shorter Oxford English Dictionary defines finance as "to lend, to settle debt, pay ransom, furnish, and procure, etc. --- the management of money --- the science of levying revenue in a state, corporation --- the provision of capital." This definition looks at finance as a science which applies to both the public and private sectors.

The Encyclopedia of Banking and Finance has however given a broader definition of finance. Its definition is classified into three categories as follows:

- (i) to raise money necessary to organise, re-organise or expand an enterprise whether by sales of stocks, bonds, notes, etc.
- (ii) a general term to denote the theory and practice of monetary credit, banking and promotion of operations in the most comprehensive sense. It includes money, credit, banking, securities, investment, speculation, foreign exchange, promotion, underwriting brokerage trusts, etc.
- (iii) originally applied to raising money by taxes or bonds issues and the administration of revenues and expenditure by government.

Finance, as seen by the Encyclopaedia of Banking and Finance, is much more comprehensive than the concept of finance as reflected in earlier definitions. The above concepts of finance are synonymous with business finance, money and credit and public finance, international finance, investments, etc.

Christy and Roden (1973) tried to narrow the definition of finance by defining it as the study of the nature and use of the means of payment. This definition has tried to avoid the mention of money as the centrepiece of finance. This is because finance can equally take place without money as its main feature.

Lastly, Gitman (2000) defines finance as the art and science of managing money. In contrast with Christy and Roden (1973), money is mentioned here. Virtually all individuals and organisations earn or raise money and spend or invest money. Finance is concerned with the process, institutions, markets, and instruments involved in the transfer of money among and between individuals, businesses and governments.

What is now known as finance evolved as a branch of economics in the later part of the 19th Century. Since then, finance has exerted the most important influence on technological and industrial development, the turnaround of depression or recession, consumer behaviour, administrative strategies and styles of governments and research and development etc.

Finance can be classified into two broad categories, namely: micro and macro finance (see Figure 1.1).

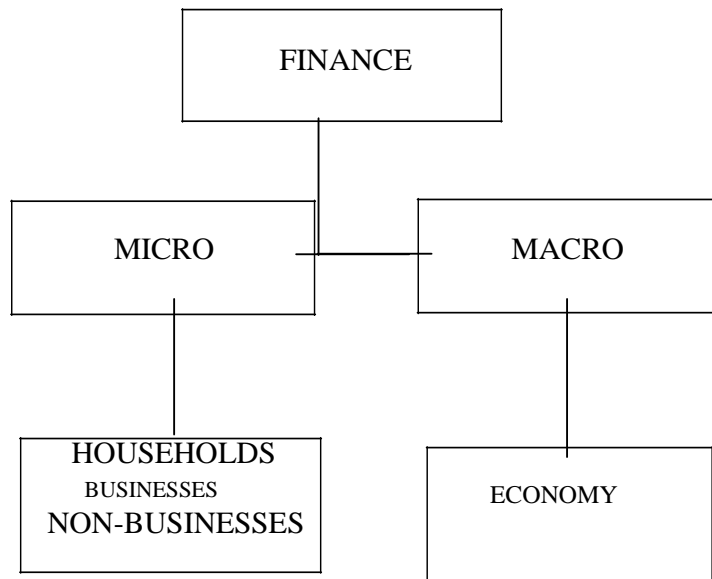


Figure 1.1 *Classification of Finance*

Micro finance relates to financing decisions and practices of individual households, businesses and non-business organisations. Macro finance relates to the financing decisions and practices of the entire economy. Finance has as its area of concentration the use and impact of money and money substitutes. Therefore, the principle of finance has brought about the concept of financial management which involves the management of instruments of finance. No decision involving finance can be efficiently and effectively implemented without financial management.

The functions of finance include sourcing and application of funds, and demands that money is used in the firm wisely, that is, when and where it is desired. Money sourced, for example, to improve on the production base of a firm should be appropriated wisely. It will be most inappropriate to use such funds to acquire assets unrelated to the course of production.

Self assessment exercise

Study this case and answer the question:

A plastic manufacturing company sourced for a loan of ₦15m from the bank to increase its production capacity but used the money in erecting structures for the provision of staff accommodation.

On the other hand, a packaged water manufacturing company sourced for a loan of ₦13m from the bank and used it to purchase raw materials for its production, bought some machinery, and expanded a bit of the factory.

Which of the companies stands a better chance of increasing its turnover and have the capacity to repay the loan in good time? Give reasons.

Finance is more or less technical economics in that its principles are derivatives of economic principles. It is also related to mathematics in that it adapts mathematical equations or relationships to formulate models and its systematic principles. Finance also provides the basis for accounting. In other words, without finance, accounting as a course may not be as extensive as it is today and may in fact not have existed. There are also financial laws showing the relationship between finance and law as a discipline (commercial law, law relating to banking etc). Laws are

normally used to regulate financial practices and such laws are normally incorporated in the law discipline.

Self assessment exercise

Explain the roles of finance in business administration.

4.0 CONCLUSION

The roles of a financial manager are played in every organisation, whether it is private or public, profit or not-for-profit making.

5.0 SUMMARY

In this unit, we have seen that:

the different definitions of finance reflect the perception of finance in respect of its role and scope;
finance pervades all disciplines and all facets of human and economic activities;
finance can act as a tool for decision making in many disciplines such as Economics, Management, Business Administration, etc, and each discipline makes use of the finance rules;

6.0 TUTOR-MARKED ASSIGNMENT

1. Explain the objectives of finance in the management structure of an organization.

7.0 REFERENCES/FURTHER READING

NOUN (2012) Course Material on *Managerial Finance (MBF 718)*

Pandey, I.M. (2005). *Financial Management* 9th Ed. VIKAS Publishing House – PVT New Delhi

Weston J. F. and Brigham, E. F. (1990) *Essentials of Managerial Finance*, 9th Edition Chicago: The Dryden Press.

UNIT 5 FINANCE AND RELATED DISCIPLINES

CONTENTS

- 1.0 Introduction
- 2.0 Objectives
- 3.0 Main Content
 - 3.1 Relationship between Finance and other Disciplines
- 4.0 Conclusion
- 5.0 Summary
- 6.0 Tutor-Marked Assignment
- 7.0 References/Further Reading

1.0 INTRODUCTION

The subject of finance is not only discussed, but is part of all disciplines and all facets of socio-economic activities of humans. Finance has evolved to assume a very important position in the decisional process of households, businesses, governments and other non-business organisations. No financial decision can be efficiently and effectively implemented without financial management.

In this introductory Unit, we shall attempt to answer the following questions:

- How is finance related to other disciplines?
- How do we explain financial management structure

2.0 OBJECTIVES

After studying this unit, you should be able to:

enumerate the roles of finance in other disciplines;
explain the concept of financial management structure

3.0 MAIN CONTENT

3.1 Definition of Finance

The field of finance is broad and dynamic. It directly affects the lives of every person and every organisation. There are many areas for study and large number of career opportunities available in the field of finance.

Finance has been defined in different ways. Each definition however reflects the perception of finance relative to its role and scope. However, it may not be possible to give a precise and very comprehensive definition to such a wide, complex and important subject which is of interest to everybody.

Webster's third International Dictionary, for example, defines finance as "the system that includes the circulation of money, the granting of credit, the making of investments and the provision of banking facilities." This definition gives an indication to the fact that finance is a system by itself and thus a broad field of activities at the centre of economic operations or social activities with economic implication.

The Shorter Oxford English Dictionary defines finance as "to lend, to settle debt, pay ransom, furnish, and procure, etc. --- the management of money --- the science of levying revenue in a state, corporation --- the provision of capital." This definition looks at finance as a science which applies to both the public and private sectors.

The Encyclopedia of Banking and Finance has however given a broader definition of finance. Its definition is classified into three categories as follows:

- (iv) to raise money necessary to organise, re-organise or expand an enterprise whether by sales of stocks, bonds, notes, etc.
- (v) a general term to denote the theory and practice of monetary credit, banking and promotion of operations in the most comprehensive sense. It includes money, credit, banking, securities, investment, speculation, foreign exchange, promotion, underwriting brokerage trusts, etc.

- (vi) originally applied to raising money by taxes or bonds issues and the administration of revenues and expenditure by government.

Finance, as seen by the Encyclopaedia of Banking and Finance, is much more comprehensive than the concept of finance as reflected in earlier definitions. The above concepts of finance are synonymous with business finance, money and credit and public finance, international finance, investments, etc.

Christy and Roden (1973) tried to narrow the definition of finance by defining it as the study of the nature and use of the means of payment. This definition has tried to avoid the mention of money as the centrepiece of finance. This is because finance can equally take place without money as its main feature.

Lastly, Gitman (2000) defines finance as the art and science of managing money. In contrast with Christy and Roden (1973), money is mentioned here. Virtually all individuals and organisations earn or raise money and spend or invest money. Finance is concerned with the process, institutions, markets, and instruments involved in the transfer of money among and between individuals, businesses and governments.

3.2 Relationship between Finance and Other Disciplines

Finance is related to many other disciplines in that it can act as a “tool” for decision making in disciplines like administration, management, educational administration, science and technology, law, economics, etc.

This is due to the fact that finance has evolved from a purely descriptive course to a normative one. That is, finance focuses on statements which enunciate rules that help to attain specified goals. Thus, each discipline makes use of the finance rules.

Finance is a special functional area of business administration. This could be shown in the diagram (Figure 1.2) below:

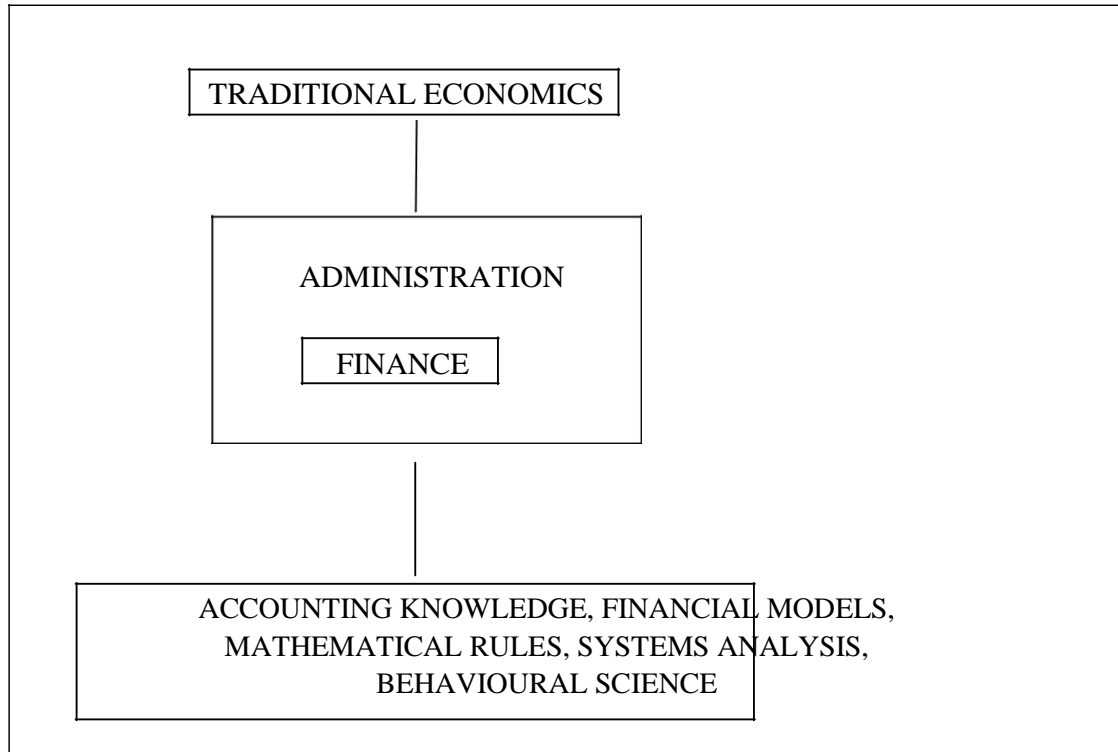


Figure 1.2 Relationships between Finance and other Disciplines

Finance is more or less technical economics in that its principles are derivatives of economic principles. It is also related to mathematics in that it adapts mathematical equations or relationships to formulate models and its systematic principles.

Finance also provides the basis for accounting. In other words, without finance, accounting as a course may not be as extensive as it is today and may in fact not have existed. There are also financial laws showing the relationship between finance and law as a discipline (commercial law, law relating to banking etc). Laws are normally used to regulate

financial practices and such laws are normally incorporated in the law discipline.

3.2 CONCEPT OF FINANCIAL MANAGEMENT

The activities of organisations whether business or non-business, have finance as their centrepiece. The role of finance however reflects the objectives of an organisation. Therefore, financial management is a reflection of the nature and objectives of the organisation. Financial management is thus a very important aspect of finance although it is not easy to separate financial management from the rest of other finance activities (Myres, 1976). However, an attempt to limit the areas of financial management can be made if one agrees with the fact that financial management itself requires the simultaneous consideration of three key financial decisions (Christy and Roden, 1973), namely:

anticipation of financial needs of the organisation;
acquisition of financial resources for the organisation; and
allocation of financial resources within the organisation.

These three key financial decisions provide the basis for periodic financial analysis and interpretation of historical financial practices. The control measures which may be contemplated by management or re-orientation of management strategies in turn depend on the analysis and interpretation of historical financial data.

Financial management is, therefore, a dynamic and evolving art of making daily financial decisions and control in households, businesses, non-business organisations and government. It is a managerial activity which is concerned with planning, providing and controlling the financial resources at the disposal of an organisation.

4.0 CONCLUSION

Although most organisations may not designate an official as a “Financial Manager,” the roles of a financial manager are played in every organisation, whether it is private or public, profit or not-for-profit making.

5.0 SUMMARY

In this unit, we have seen that:

the different definitions of finance reflect the perception of finance in respect of its role and scope;

finance pervades all disciplines and all facets of human and economic activities;

finance can act as a tool for decision making in many disciplines such as Economics, Management, Business Administration, etc, and each discipline makes use of the finance rules;

financial management involves the management of finances or the instruments of finance and it is important in the household finance, business finance, government and other business organisations;

the financial manager's functions/roles are enormous. Apart from the traditional function which includes the management of a firm's cash position to guarantee liquidity, the roles have broadened to include analytical aspects of an organisation finances.

6.0 TUTOR-MARKED ASSIGNMENT

1. Explain the objectives of financial management.

7.0 REFERENCES/FURTHER READING

NOUN (2012) Course Material on *Managerial Finance (MBF 718)*

Pandey, I.M. (2005). *Financial Management* 9th Ed. VIKAS Publishing House – PVT New Delhi

Weston J. F. and Brigham, E. F. (1990) *Essentials of Managerial Finance*, 9th Edition Chicago: The Dryden Press.