Finance
Role of Financial Management

- Strategic role of financial management

A strategic plan encompass a long-term view of where the business is going, the strategies it will use to achieve its goals and a monitoring process to keep track of progress along the way.
Financial management is the planning and monitoring of a business's financial resources to enable the business to achieve its financial goals.
Financial management is crucial if a business is to achieve its financial goals. The mismanagement of financial resources can lead to
problems such as business failure.
Strategies for monitoring the financial resources of a business must be incorporated into its strategic plan.

- Objectives of financial management

The objectives of financial management are to maximize the businesses

- Profitability
- Liquidity
- Efficiency
- Growth
- Solvency

- Short-term and long-term

The financial objectives of a business are based on the goals of its strategic plan, which can be translated into:

  - ***Short-term financial objectives*** are the tactical (one to two years) and operational (day-to-day) plans of a business. These would be reviewed regularly to see if targets are being met and if resources are being used to the best advantage to achieve the objectives.
  - ***Long-term financial objectives*** are the strategic plans of a business. They are determined for a set period of time, generally more than five years. The business would review their progress annually to determine if changes need to be implemented.

- Interdependence with Other Key Business Functions

Interdependence of the key business functions means that each function is not able to operate in isolation successfully – it relies on the others to perform its role in achieving the broader goals of a business.
Marketing →
Human resource →
Operation →

Financial Management Strategies

Cash Flow Management:
cash flow statements

- Cash flow statements indicate the movement of cash receipts and cash payments resulting from transactions over a period of time.
- They can help identify trends and can be a useful predictor of change.

Distribution of payments, discounts for early payment, factoring

- Management must implement strategies to ensure that cash is available to make payments when they are due.
- Three strategies to manage cash flow are:
  - Distribution of payments
  - Discounts for early payment
  - Factoring

Working Capital Management

- Working capital is the term used to describe the funds available for the short-term financial commitments of a business.

Net working capital is the difference between current assets and current liabilities i.e. **Net working capital = CA – CL**

- It represents those funds that are needed for the day-to-day operations of a business to produce profits and provide cash for short-term liquidity.
- Working capital is a major asset of a business and the management of it requires planning and constant monitoring otherwise business failure can result.
- Working capital management involves determining the best mix of current assets and current liabilities needed to achieve the objectives of the business.

The formula that can be used for working capital is the current ratio (with the rule of thumb of 2:1).

Control of current assets – cash, receivables, inventories

- Management of CAs is important for monitoring working capital.
- Control of CAs requires management to select the optimal amount of each CA held. The costs and benefits of holding too much or too little of each asset must be assessed.
- Current assets that need to be managed include:
  - Cash: need to have enough to guard against sudden shortages and to enable business to take advantage of opportunities.
  - Receivables: collection is important. Must ensure timing allows the business to maintain adequate cash resources (the quicker they pay the better). Need to have procedures for managing receivables e.g. check credit ratings, send monthly statements, follow up overdue accounts, policies for bad debts
  - Inventories: levels must be monitored. Too much could lead to cash shortages and too little can lead to loss of customers