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THEORETICAL ASPECTS OF FINANCIAL MANAGEMENT

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Abstract
Finance is considered as the life blood of any business. In fact, the term, finance has to be understood clearly as it has different meaning and interpretation in various contexts. The time and extent of the availability of finance in any organization indicates the health of a concern. Every organization, may it be a company, firm, college, school, bank or university requires finance for running day to day affairs. As every organization previews stiff competition, it requires finance not only for survival but also for strengthening themselves. Finance is said to be the circulatory system of the economy body, making possible the required cooperation between the innumerable units of activity. The present study focuses on the conceptual understanding of the financial management.

Keywords: Finance, Organisation, Economy Body.

Introduction

Finance is the provision of money at the time when it is required. Every enterprise whether it may be large, medium of small, needs finance to carry on its operations and to achieve its targets. In fact, finance is so indispensable that it is the lifeblood of an enterprise. Without adequate finance, no enterprise can possibly accomplish its objectives. Finance is the life blood and nerve system of any business organization. Just as circulation of blood, is necessary in the human body to maintain life. Finance is necessary in the business organisation for smooth running of the business.

Definition of Finance

According to F.W.Paish, Finance may be defined as the position of money at the time it is wanted. In the words of John J. Hampton, the term finance can be defined as the management of the flows of money through an organization, whether it will be a corporation, school, bank or government agency. According to Howard and Upton, "finance may be defined as that administrative area or set of administrative functions in an organization which relates with the arrangement of each and credit so that the organization may have the means to carry out the objectives as satisfactorily as possible.

In the words of Bonneville and Dewey, Financing consists in the raising, providing, managing of all the money, capital or funds of any kind to be used in connection with the business. As put forth by Hurband and Dockery in his book 'Modern Corporation Finance', finance is defined as "an organism composed of a myriad of separate enterprise, each working for its own ends but simultaneously making a contribution to the system as a whole, some force is necessary to bring about direction and co-ordination. Something must direct the flow of economic activity and facilitate its smooth operation. Finance is the agent that produces this result".

The Encyclopedia Britannica defines finance as "the act of providing the means of payment." It is thus the financial aspect of corporate planning which may be described as the management of money. An analysis of the aforesaid definition, makes it clear that finance directs the flow of economic activity and facilitates the smooth operation. Finance provides the required stimulus for continued business operations of all categories. Finance is essential for expansion, diversification, modernization, establishment, of new projects and so on. The financial policy of any organization to a greater extent, determines not only its existence, and survival but also the performance and success of that organization. Finance is required for investment, purposes as well as to meet substantial capital expenditure projects.

Importance of Finance Function

In general, the term "Finance" is understood as provision of funds as and when needed. Finance is the essential requirement of every organisation. The following points expresses the importance of finance function.

Required Everywhere: All activities, be it production, marketing, human resources development, purchases and even research and development, depend on the adequate and timely availability of finance both for commencement and their smooth continuation to completion. Finance is regarded as the life-blood of every business enterprise.

Efficient Utilisation More Important: Finance function is the most important function of all business activities. The efficient management of business enterprise is closely linked with the efficient management of its finances. The need of finance starts with the setting up of business. Its growth and expansion require more funds. The funds have to be raised from

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various sources. The sources have to be selected keeping in relation to the implications, in particular, risk attached. Raising of money, alone, is not important. Terms and conditions while raising money are more important. Cost of funds is an important element. Its utilisation is rather more important. If funds are utilised properly, repayment would be possible and easier, too. Care has to be exercised to match the inflow and outflow of funds. Needless to say, profitability of any firm is dependent on its cost as well as its efficient utilisation.

Concept of Financial Management

As already discussed, the general meaning of finance refers to providing funds, as and when needed. However, as management function, the term 'Financial Management' has a distinct meaning. Financial management deals with the study of procuring funds and its effective and judicious utilisation, in terms of the overall objectives of the firm, and expectations of the providers of funds. The basic objective is to maximise the value of the firm. The purpose is to achieve maximisation of share value to the owners i.e. equity shareholders.

The term financial management has been defined, differently, by various authors. Some of the authoritative definitions are given below:

- "Financial Management is concerned with the efficient use of an important economic resource, namely, Capital Funds" **—Solomon**
- "Financial Management is concerned with the managerial decisions that result in the acquisition and financing of short-term and long-term credits for the firm" **—Phillioppatus**
- "Business finance is that business activity which is concerned with the conservation and acquisition of capital funds in meeting financial needs and overall objectives of a business enterprise" **—Wheeler**
- "Financial Management deals with procurement of funds and their effective utilisation in the business" **—S.C. Kuchhal**
- The definition provided by Kuchhal is most acceptable as it focuses, clearly, the Basic requirements of financial management. From his definition, two basic aspects emerge:
  - a) Procurement of funds.
  - b) Effective and judicious utilisation of funds.

Financial management has become so important that it has given birth to Financial Management as a separate subject.

Nature of Financial Management

Financial management refers to that part of management activity, which is concerned with the planning and controlling of firm's financial resources. Financial management is a part of overall management. All business decisions involve finance. Where finance is needed, role of finance manager is inevitable. Financial management deals with raising of funds from various sources, dependant on availability and existing capital structure of the organisation. The sources must be suitable and economical to the organisation. Emphasis of financial management is more on its efficient utilisation, rather than raising of funds, alone. The scope and complexity of financial management has been widening, with the growth of business in different diverse directions. As business competition has been increasing, with a greater pace, support of financial management is more needed, in a more innovative way, to make the business grow, ahead of others.

Scope of Financial Management

Financial management is concerned with optimum utilisation of resources. Resources are limited, particularly in developing countries like India. So, the focus, everywhere, is to take maximum benefit, in the form of output, from the limited inputs. Financial management is needed in every type of organisation, be it public or private sector. Equally, its importance exists in both profit oriented and non-profit organisations. In fact, need of financial management is more in loss-making organisations to turn them to profitable enterprises. Study reveals many organisations have sustained losses, due to absence of professional financial management. Financial management has undergone significant changes, over the years in its scope and coverage.

Traditional Approach

The scope of finance function was treated, in the narrow sense of procurement or arrangement of funds. The finance manager was treated as just provider of funds, when organisation was in need of them. The utilisation or administering resources was considered outside the purview of the finance function. It was felt that the finance manager had no role to play in decision making for its utilisation. Others used to take decisions regarding its application in the organisation, without the involvement of finance personnel. Finance manager had been treated, in fact, as an outsider with a very specific and limited function, supplier of funds, to perform when the need of funds was felt by the organisation. As per this approach, the following aspects only were included in the scope of financial management:

- Estimation of requirements of finance,
- Arrangement of funds from financial institutions,

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- Arrangement of funds through financial instruments such as shares, debentures, loans etc
- Looking after the accounting and legal work connected with the raising of funds.

Modern Approach
Since 1950s, the approach and utility of financial management has started changing in a revolutionary manner. Financial management is considered as vital and an integral part of overall management. The emphasis of Financial Management has been shifted from raising of funds to the effective and judicious utilisation of funds. The modern approach is analytical way of looking into the financial problems of the firm. Advice of finance manager is required at every moment, whenever any decision with involvement of funds is taken. Hardly, there is an activity that does not involve funds. In the words of Solomon "The central issue of financial policy is the use of funds. It is helpful in achieving the broad financial goals which an enterprise sets for itself". Nowadays, the finance manger is required to look into the financial implications of every decision to be taken by the firm. His Involvement of finance manager has been before taking the decision, during its review and, finally, when the final outcome is judged. In other words, his association has been continuous in every decision-making process from the inception till its end.

Aims of Financial Management
The following are the aims of finance function:
1. Acquiring Sufficient and Suitable Funds: The primary aim of finance function is to assess the needs of the enterprise, properly, and procure funds, in time. Time is also an important element in meeting the needs of the organisation. If the funds are not available as and when required, the firm may become sick or, at least, the profitability of the firm would be, definitely, affected. It is necessary that the funds should be, reasonably, adequate to the demands of the firm. The funds should be raised from different sources, commensurate to the nature of business and risk profile of the organisation. When the nature of business is such that the production does not commence, immediately, and requires long gestation period, it is necessary to have the long-term sources like share capital, debentures and long term loan etc. A concern with longer gestation period does not have profits for some years. So, the firm should rely more on the permanent capital like share capital to avoid interest burden on the borrowing component.

2. Proper Utilisation of Funds: Raising funds is important, more than that is its proper utilisation. If proper utilisation of funds were not made, there would be no revenue generation. Benefits should always exceed cost of funds so that the organisation can be profitable. Beneficial projects only are to be undertaken. So, it is all the more necessary that careful planning and cost-benefit analysis should be made before the actual commencement of projects.

3. Increasing Profitability: Profitability is necessary for every organisation. The planning and control functions of finance aim at increasing profitability of the firm. To achieve profitability, the cost of funds should be low. Idle funds do not yield any return, but incur cost. So, the organisation should avoid idle funds. Finance function also requires matching of cost and returns of funds. If funds are used efficiently, profitability gets a boost.

4. Maximising Firm's Value: The ultimate aim of finance function is maximising the value of the firm, which is reflected in wealth maximisation of shareholders. The market value of the equity shares is an indicator of the wealth maximisation.

Functions of Finance
According to Paul G. Hasings, "finance" is the management of the monetary affairs of a company. It includes determining what has to be paid for and when, raising the money on the best terms available, and devoting the available funds to the best uses. Kenneth Midgley and Ronald Burns state: "Financing is the process of organising the flow of funds so that a business can carry out its objectives in the most efficient manner and meet its obligations as they fall due." Finance squeezes the most out of every available rupee. To get the best out of the available funds is the major task of finance, and the finance manager performs this task most effectively if he is to be successful. In the words of Mr.A.L.Kingshott, "Finance is the common denominator for a vast range of corporate objectives, and the major part of any corporate plan must be expressed in financial terms."

The description of finance may be applied to money management provided that the following three objectives are properly noted:
Many activities associated with finance such as saving, payment of things, giving or getting credit, do not necessarily require the use of money. In the first place, the conduct of international trade has been facilitated. The development of the pecuniary unit in the various commercial nations has given rise to an international denominator of values. The pecuniary unit makes possible a fairly accurate directing of capital to those parts of the world where it will be most productive. Within any given country, the flow of capital from one region to another is guided in a similar manner.

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The term ‘finance’ refers to the financial system in a rudimentary or traditional economy, that is, an economy in which the per capita output is low and declining over a period of time. The financial organisation in rudimentary finance is characterized by the absence of any financial instruments of the saving deficit units of their own which they can issue and attract savings. There will not be any inducement for higher savings by offering different kinds of financial assets to suit the varied interests and preferences of the investing public. The other characteristic of such a financial system is that there are no markets where firms can compete for private savings.

Finance Function – Objectives

The objective of finance function is to arrange as much funds for the business as are required from time to time. This function has the following objectives.

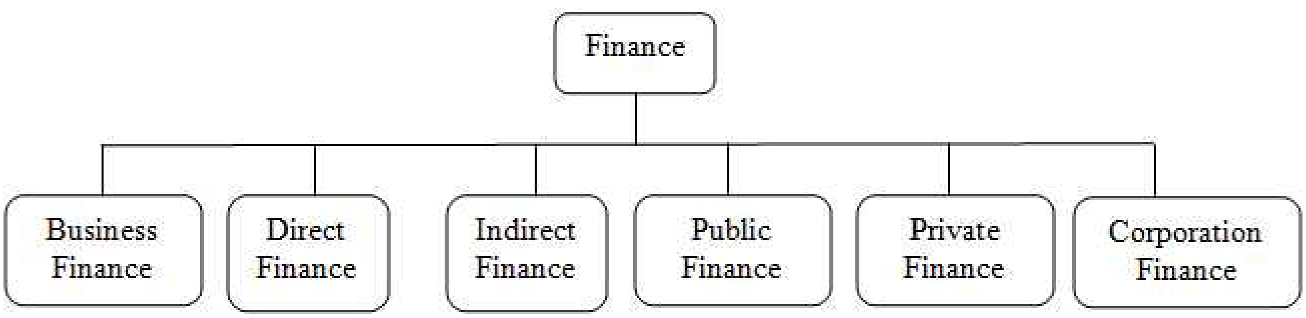
1. Assessing the Financial Requirements: The main objective of finance function is to assess the financial needs of an organization and then finding out suitable sources for raising them. The sources should be commensurate with the needs of the business. If funds are needed for longer periods then long-term sources like share capital, debentures, term loans may be explored.

2. Proper Utilisation of Funds: Though raising of funds is important but their effective utilisation is more important. The funds should be used in such a way that maximum benefit is derived from them. The returns from their use should be more than their cost. It should be ensured that funds do not remain idle at any point of time. The funds committed to various operations should be effectively utilised. Those projects should be preferred which are beneficial to the business.

3. Increasing Profitability: The planning and control of finance function aims at increasing profitability of the concern. It is true that money generates money. To increase profitability, sufficient funds will have to be invested. Finance function should be so planned that the concern neither suffers from inadequacy of funds nor wastes more funds than required. A proper control should also be exercised so that scarce resources are not frittered away on uneconomical operations. The cost of acquiring funds also influences profitability of the business.

4. Maximising Value of Firm: Finance function also aims at maximizing the value of the firm. It is generally said that a concern's value is linked with its profitability.

Types of Finance



Business Finance

The term ‘business finance’ is very comprehensive. It implies finances of business activities. The term, ‘business’ can be categorized into three groups: commerce, industry and service. It is a process of raising, providing and managing of all the money to be used in connection with business activities. It encompasses finance of sole proprietary organizations, partnership firms and corporate organizations. No doubt, the aforesaid organizations have different characteristics, features, distinct regulations and rules. And financial problems faced by them vary depending upon the nature of business and scale of operations. However, it should be remembered that the same principles of finance are applicable to large and small organizations, proprietary and nonproprietary organizations.

According to Guthmann & Dougall, business finance can be broadly defined as the activity concerned with planning, raising, controlling and administering of funds used in the business. Business finance deals with a broad spectrum of the financial activities of a business firm. It refers to the raising and procurement of funds and their appropriate utilisation. It includes within its scope commercial finance, industrial finance, proprietary finance corporation finance and even agricultural finance. The subject of business finance is much wider than that of corporation finance. However, since corporation finance forms the

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lion's share in the business activity, it is considered almost inter-changeable with business finance. Business finance, apart from the financial environment and strategies of financial planning, covers detailed problems of company promotion, growth and pattern. These problems of the corporate sector go a long way in widening the horizon of business finance. The finance manager has to assume the new responsibility of managing the total funds committed to total assets and allocating funds to individual assets in consonance with the overall objectives of the business enterprise.

Direct Finance
The term 'direct', as applied to the financial organisation, signifies that savings are effected directly from the saving-surplus units without the intervention of financial institutions such as investment companies, insurance companies, unit trusts, and so on.

Indirect Finance
The term 'indirect finance' refers to the flow of savings from the savers to the entrepreneurs through intermediary financial institutions such as investment companies, unit trusts and insurance companies, and so on. Finance administers economic activities. The scope of finance is vast and determined by the financial needs of the business enterprise, which have to be identified before any corporate plan is formulated. This eventually means that financial data must be obtained and scrutinised. The main purpose behind such scrutiny is to determine how to maintain financial stability.

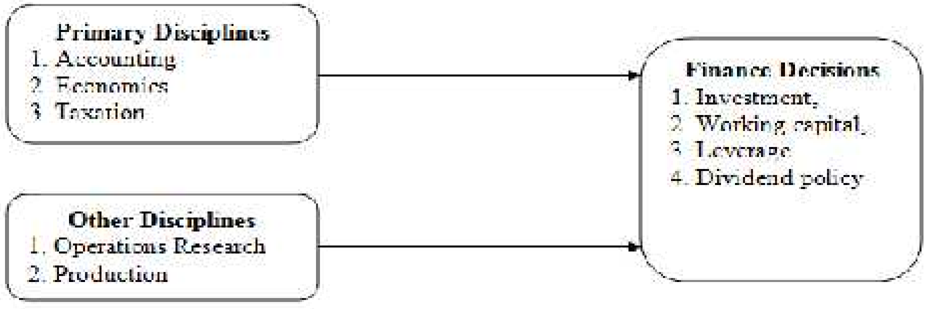
Public Finance
It is the study of principles and practices pertaining to acquisition of funds for meeting the requirements of government bodies and administration of these funds by the government.

Private Finance
It is concerned with procuring money for private organization and management of the money by individuals, voluntary associations and corporations. It seeks to analyse the principles and practices of managing one’s own daily affairs. The finance of non-profit organization deals with the practices, procedures and problems involved in the financial management of educational chartable and religions and the like organizations.

Corporation Finance
Corporation finance deals with the financial problems of a corporate enterprise. These problems include the financial aspects of the promotion of new enterprises and their administration during their early period ; the accounting problems connected with the distinction between capital and income, the administrative problems arising out of growth and expansion, and, finally, the financial' adjustments which are necessary to bolster up to rehabilitate a corporation which has run into financial difficulties. The term ‘corporation finance’ includes, apart from the financial environment, the different strategies of financial planning. It includes problems of public deposits, inter-company loans and investments, organised markets such as the stock exchange, the capital market, the money market and the bill market. Corporation finance also covers capital formation and foreign capital and collaborations.

Finance in Relation to other Allied Disciplines
The finance function cannot work effectively unless it draws on the-disciplines which are closely associated with it. Management is heavily dependent on accounting for operating facts. Accounting' has been described by Richard M. Lynch and Robert W. Williamson as "the - measurement and communication of financial and economical data. In fact, accounting information relates to the production, sales, expenses, investments, losses and gains of the business. Accounting has three branches namely, financial accounting, cost accounting and management accounting.

Relationships between Finance and other Disciplines



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Financial Accounting

It is concerned with the preparation of reports which provide information to users outside the firm. The most common reports are the financial statements included in the annual reports of stock-holders and potential investors. The main objective of these-reports is to inform stockholders, creditors and other investors how assets are controlled by a firm. In the light of the financial statements and certain other information, the accountant prepares funds film statement, cash flow statement and budgets. A master plan (Budget) of the organization includes and coordinates the plans of every department in financial terms. According to Guthmann and Dougall, "Problems of finance are intimately connected while problems of purchasing, production and marketing".

Cost Accounting

It deals primarily with cost data. It is the process of classifying, recording, allocating and reporting the various costs incurred in the operation of an enterprise. It includes a detailed system of control for material, labour and overheads. Budgetary control and standard casting are integral part of cost accounting. The purpose of cost accounting is to provide information to the management for decision making, planning and control. It facilitates cost reduction and cost control. It involves reporting of cost data to the management.

Management Accounting

It refers to accounting for the management. It provides necessary information to assist the management in the creation of policy and in the day to day operations. It enables the management to discharge all its functions, namely, planning, organizing, staffing, direction and control efficiently with the help of accounting information. Functions of management accounting include all activities connected with collecting, processing, interpreting and presenting information to the management. According to J. Batty, 'management accounting' is the term used to describe the accounting methods, systems and technique which coupled with special knowledge and ability, assist management in its task of maximizing profits or minimizing losses. Management accounting is related to the establishment of cost centres, preparation of budgets, preparation of cost control accounts and fixing of responsibility for different functions.

Conclusion

Finance is the life blood of business. It may be defined as the position of money at the time it is wanted. Financing consists in the raising, providing, managing of all the money, capital or funds of any kind to be used in connection with the business. The term 'business finance' is very comprehensive. It implies finances of business activities. The term, 'business' can be categorized into three groups: commerce, industry and service. It is a process of raising, providing and managing of all the money to be used in connection with business activities. The term 'corporation finance' includes, apart from the financial environment, the different strategies of financial planning. It includes problems of public deposits, inter-company loans and investments, organised markets such as the stock exchange, the capital market, the money market and the bill market. The finance function cannot work effectively unless it draws on the disciplines which are closely associated with it. Management is heavily dependent on Accounting, Economics, Taxation, Operations research, Production and Marketing.

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