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Comparative Study of Decision Areas in Modern Financial Management

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ABSTRACT:-

This paper consisted how decision areas in financial management are interconnected and how much these areas influenced any business. Traditionally **Finance** involves arrangement of funds required by the business enterprise from and through financial institutions ('from' signifies procurement of loan capital, and 'through' implies the selling of securities by financial institutions). Hence, the traditional approach of financial management focused on 'arrangement of finance' for meeting various financial needs of an **enterprise**. In the modern sense, **financial management** encompasses wider applications, viz., assessment of funds required, effective procurement of those funds through most economical means, and efficient utilization of those funds through profitable investments, as well as cash and liquidity management. The key questions in financial management of a business enterprise happen to be: "(i) what is the total volume of funds an enterprise should commit? (ii) What specific assets should an enterprise acquire? (iii) How should the funds required be financed?" These questions, if answered properly, lead to four broad **decision areas** of financial management, viz., financing decision, investment decision, and dividend decision, Financial Analysis, Planning and Control Decisions. The efficient management of finance is vitally important to the success or failure of an organisation. The influence of the financial function is important because it has to: A) ensure that there are adequate funds available to acquire the resources needed to help the organization achieve its objectives; B) ensure costs are controlled; C) ensure adequate cash flow; D) establish and control profitability levels. As objective of the Financial Management is to maximize the value (i.e. wealth of shareholders).the firm should strive for an optimal combination of the four **interrelated** decisions solved jointly .The decisions to invest in a new capital project, for example, necessities financing the investment. The financing decisions in turn, influences and is influenced by the dividend decision. The retained earnings used in internal financing represents dividends foregone by the shareholders. In this paper has studied that how organizations can take joint decisions that tend to be optimal can be reached, with a proper conceptual frame work.

Keywords: - Finance, Enterprise, Financial Management, Decision Areas, Interrelation

2. INTRODUCTION:

Financial Management is concerned with the solutions of the three major decisions a firm must make the investment decision, the financing decision and the dividend decision. A firm wants to earn the profit because the founders of the firm believe that there is an opportunity to make profitable investment. This profitable investment need to be financed and profit distributed amongst those who have contributed the capital. Hence, there is need for decisions such as how to finance investment? How to distribute profit among shareholders?

it is a specialized functional field, dealing with the management of finance right from estimation and procurement till its effective utilization in the business. It is an area looked after by the finance manager who deals with the following issues:

I Which new proposals for employing capital should be accepted by the firm?
II How much working capital will be needed to support the firm's operations?
III Where should the firm go to raise long term capital and how much will it cost?
V Should the firm declare dividend on its equity capital and if so, how large a dividend should be declared?
VI What steps can be taken to increase the value of firm's equity capital?

The above issues are solved by taking four major decisions (1) Investment decision (2) Financing decision (3) Dividend decision (4) Planning and control decision area

2.1 FINANCING DECISION AREA:

It is the next step in financial management for executing the investment decisions once taken a look at the balance - sheet of a company indicates that it obtains finance from shareholders ordinary, preference, debenture holders, or long - term loans from the institutions, bank and other sources. There are variations in the provisions contained in preference shares, debentures, loans papers etc. Thus financing decisions i.e. The financing mix of capital structure. Efforts are made to obtain an optimal financing mix for a particular company. This necessitates study of capital structure as also the short and intermediate term financing plans of the company. In more advanced companies financing decision today , has become fully -integrated with top - management policy formulation via capital budgeting, long - range planning , evaluation of alternate uses of funds and establishment of measurable standards of performance in financial terms.

2.2 INVESTMENT DECISION AREA:

These involve the allocation of resources among various type of assets. What portion of the firm's fund should be invested in various current assets such as cash. Marketable securities and receivable and what portion in fixed assets, such as inventories and plant and equipment. The assets mix affects the amount of income the firm can earn. For example, a manufacturer is in business to earn income with fixed assets such as machinery and not with current assets. However, placing too high a percentage of its assets in new building or new machinery may leave the firm short of cash to meet an unexpected need or exploit sudden opportunity. The firm’s financial manager must invest in fixed assets. but not too much. Besides determining the assets mix financial manager must also decide what type of fixed and current assets to acquire. All this covers area pertaining to capital budgeting and working capital management.

2.3 DIVIDEND DECISION AREA:

The third major decision of financial management is the decision relating to the dividend policy. The dividend decision should be analyzed in relation to the financing decision of a firm. Two alternatives are available in dealing with the profits of a firm; they can be retained in the business. Which courses should be followed - dividend or retention? One significant factor is that the dividend payout ratio i.e. what proportion of net profits should be paid out to the shareholders. The decision will depend upon the preference of the shareholders and investment opportunities available within the firm. The second major aspect of the dividend decision is the factors determining dividend policy of a firm in practice

2.4 PLANNING AND CONTROL DECISION AREA:

There are two crucial aspects to the management of any project – 'planning' and 'control'. These are essential functions for every successful manager – without them, projects are generally not successful, not completed on time, or cost more than they should! The successful manager must always ensure that projects are based on excellent plans and followed by good control during implementation. 'Planning' is the setting of realistic goals and choosing effective ways to achieve these goals. Goals must be understandable, achievable and able to be assessed! If a goal is not clear, it cannot be assessed and, hence, it cannot be managed. If a goal is unrealistic, any plan will also be unrealistic and, therefore, unlikely to succeed. The successful manager must ensure that a project's plan is clearly defined and realistic. 'Control' is the process by which the manager ensures that all actions are consistent with the plan – all actions are, therefore, directed at achieving the stated goals. 'Control' is the systematic effort of comparing performance to plans.

2.5 OBJECTIVES OF STUDY

1. The main objective of this proposed research is the study of different –different decision areas in modern financial management and establishes the relationship between all areas.
2. Set the priority order that which one is the important in decision areas like financial, investment and dividend.
3. Check the performance of the companies on the behalf of decision areas.
4. The secondary objective of this research is comparison between traditional and modern approach of financial management.
5. Evaluate that which one is the best "profit maximization and wealth maximization of the shareholders view.
6. Comparative study between investment, financial, and dividend decisions.
7. To analyse that which company follows which decision areas in financial management?

3. RESEARCH METHODOLOGY:

Research in common parlance refers to a search for knowledge. Once can also define research as a scientific and systematic search for pertinent information on a specific topic. In fact, research is an art of scientific investigation. It's "a careful investigation or inquiry especially through search for new facts in any branch of knowledge."

3.1 SOURCE OF DATA:-

- **Primary data** –From four different Companies.
- **Secondary data** – It will been collected from library of College of Management Studies, different-different researchers points of view, magazines & from different web sites of companies.

3.2 Research method: -

The survey method was used to be able to come up with descriptions of the variables that are of interest and related to the topic of the study. The descriptions of each variable lead to the investigation of their possible relationship with each other as well as how each of them may influence the outcome of the other concepts of the study. The data to be utilized in the research will be both primary data (also known as the first-hand data) and secondary data. While the primary data are collected straight from the sources and are gathered through the survey which will be the key research tool, the secondary data are collected from current related literatures. The secondary analysis method involves the use of existing data, collected for the purposes of a prior study, in order to pursue a research interest which is distinct from that of the original work. Secondary data analysis is composed of the reviews of references and sources in this study to either support or rebut the claims and findings of this particular research endeavour.

3.3 HYPHOTHESIS:

NULL HYPOTHESIS:- Ho: $I_1 = I_2 = I_3 = I_4$ i.e., all decisions are interconnected for company's point of view where I_1 is the importance of financing decision, I_2 is the importance of the investment decisions and I_3 is the importance of dividend decisions and I_4 is the Planning and Control decision area.

Or

Ho: $\mu_1 = \mu_2 = \mu_3 = \mu_4$ i.e. there is no difference in the importance of decisions in organization performance and all are dependent to each other.

ALTERNATIVE HYPOTHESIS:- 1. H_1: $I_1 = I_2 \neq I_3 \neq I_4$

2. H_2: $I_1 \neq I_2 = I_3 \neq I_3$

3. H_2: $I_1 \neq I_2 \neq I_3 \neq I_3$

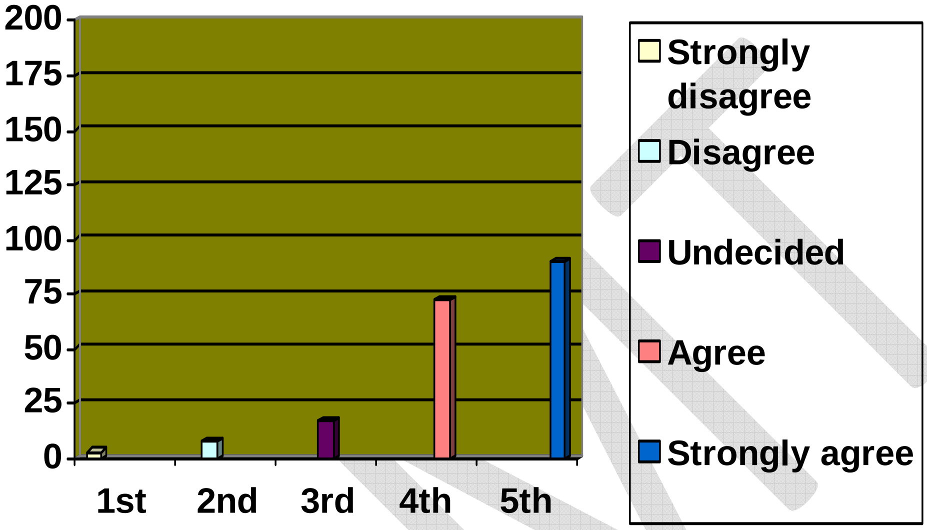
4. H_2: $I_1 \neq I_2 \neq I_3 = I_3$

i.e. if there is any difference between two or more in decision they will affect the organization performance. The observations recorded in an experiment may vary in respect of different decisions for example , in testing the hypothesis that Four decisions gives equal performance or importance , we may conduct an experiment in which four decisions and performance of the organization will plotted on the graph. In this basis observations are classified on the basis of a single criterion, the decisions areas.

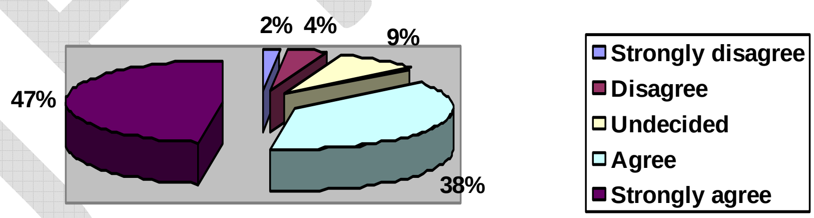
4. ANALYSIS AND INTERPRETATION:

In modern finance all decisions like Investment, Dividend, and Financial and Planning & Control Decisions are interdependent.

Ranking Given By Employee:-



→ 3 Employee was strongly disagree.
→ 8 Employee was disagreeing.
→17 Employee was in dilemma.
→ 72 Employee was agree that companies should focuses on all type of decisions.
→90 Employee was strongly agree that companies should focuses on all type of decisions.
Here null hypothesis is acceptable due to maximum percentage of equality in all areas.

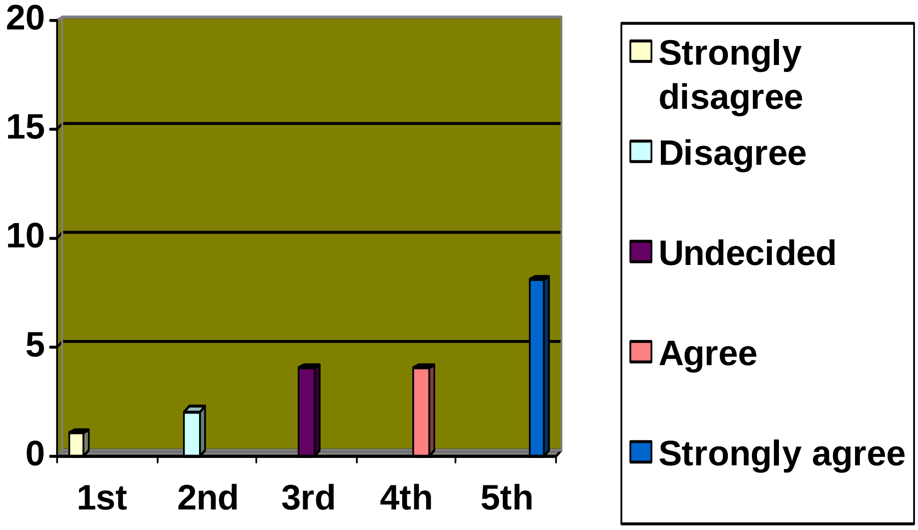


→ 2% Employee was strongly disagreeing.
→ 4% Employee was disagreeing.
→9% Employee was in dilemma.
→ 38% Employee was agreed that companies should focuses on all type of decisions.
→47% Employee was strongly agreed that companies should focuses on all type of decisions.

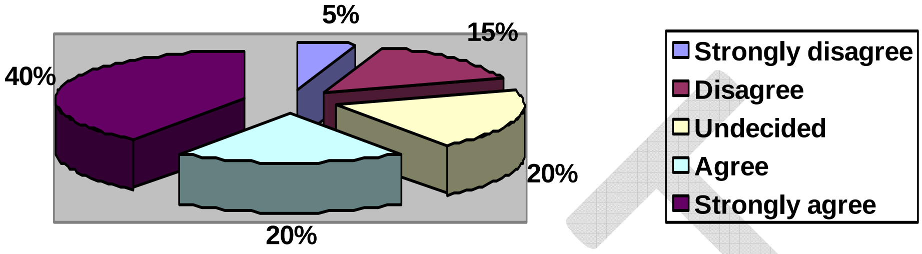
Here null hypothesis is acceptable due to maximum percentage of equality in all areas.

Decision	Ist	IInd	IIIrd	IVth	Vth
Investment	105	45	22	18	10
Dividend	28	70	39	40	23
Financing	27	52	51	45	35

Ranking Given By Finance Managers:-

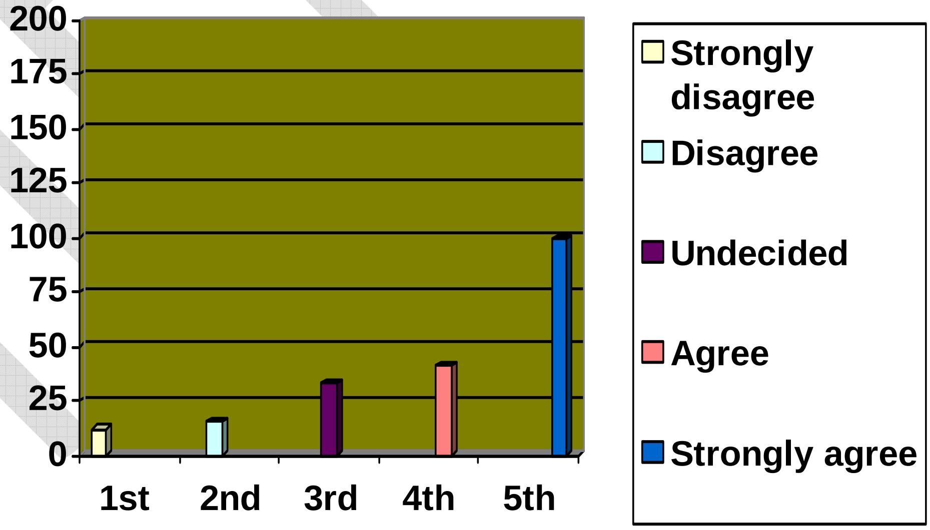


→ 1 Finance Manager was strongly disagree.
→ 3 Finance Manager was disagreeing.
→4 Finance Manager was in dilemma.
→4 Finance Manager was agree that companies should focuses on all type of decisions.
→8 Finance Manager was strongly agree that companies should focuses on all type of decisions.
Here null hypothesis is acceptable due to maximum percentage of equality in all areas.



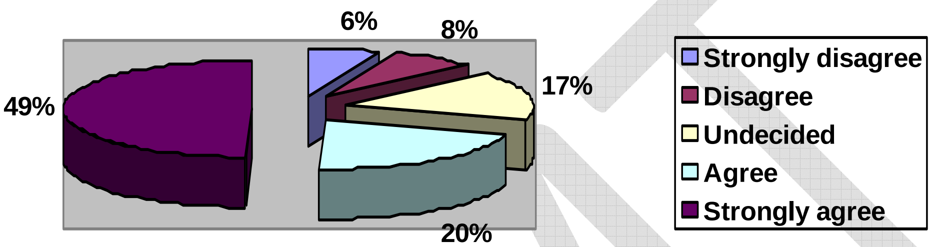
→ 5% Finance Manager was strongly disagreeing.
→ 15% Finance Manager was disagreeing.
→20% Finance Manager was in dilemma.
→20% Finance Manager was agreed that companies should focuses on all type of decisions.
→40% Finance Manager was strongly agreed that companies should focuses on all type of decisions.

Decision	Ist	IInd	IIIrd	IVth	Vth
Investment	12	3	1	2	2
Dividend	7	5	3	2	3
Financing	9	5	1	3	2



→ 3 Shareholders was strongly disagree.

→ 8 Shareholders was disagreeing.
→17 Shareholders was in dilemma.
→ 72 Shareholders was agree that companies should focuses on all type of decisions.
→90 Shareholders was strongly agree that companies should focuses on all type of decisions.



→6% Shareholders was strongly disagreeing.
→ 8% Shareholders was disagreeing.
→17% Shareholders was in dilemma.
→ 20% Shareholders was agreed that companies should focuses on all type of decisions.
→49% Shareholders was strongly agreed that companies should focuses on all type of decisions.

Ranking Given By Sharehoders:-

Decision	Ist	IInd	IIIrd	IVth	Vth
Investment	105	58	25	3	9
Dividend	103	54	12	14	17
Financing	98	51	25	18	8

Modern Approach to corporate finance in an improvement on the Traditional Approach: company finance is identified with rising of funds in meeting financial needs and fulfilling the set objectives of a company. At the outset in the early years corporate finance was confined to : 1) arrangement of funds from financial institutions.2) mobilizing funds through financial institutions.3) looking after the legal and accounting relationship between a corporate unit and its sources of funds. The traditional approach to corporate finance laid emphasis on the external und. But the subject or corporate finance spreads itself wider and wider. In the changed scenario the scope and importance of corporate finance has been greatly widened. Now it not only includes the traditional and conventional role of taking decision viz, investment, financing and dividend but also covers the area of reviewing and controlling decision to commit funds to new and ongoing uses. The field underwent a number of significant changes - new financial instrument and transactions like options on future contracts, foreign currency swaps, and interest rate swaps, GDR (Global Depository Receipts), globalization of capital market, liberalization measures taken by various government - all these have emphasized the need for effective and efficient modern approach to corporate finance. The modern approach to corporate finance lay emphasis that the corporate unit must make the best and most efficient use of finances available to it. Accordingly the central theme of financial policy is the wise use of funds and a rational matching of advantage of potential uses against the cost of alternative potential used with a desire to reach the set financial goals. It facilitates the key - how large should an undertaking be, in what form assets should be held with capital market. Given the existing legal, political and economic environment the modern approach entails a conceptual framework and is concerned with issues like -(a) - financial goals or corporate unit;(b) - adequacy of capita - maintaining minimum levels of capital to support the perceived risks ;(c) - controls of client's money.(d) - measuring the performance of the company.(e) - position of the firm within the group. Thus it is quite obvious that the modern approach to corporate finance is an extension as well as an improvement on the traditional approach.

Inter-relationship between Investments, Financing And Dividend: Three major functions of finance department are:

Financing Decision:

This function is mainly concerned with determination of optimum capital structure of the company keeping in mind cost , control and risk. It is also known as Procurement of Fund.

Investment Decision:

It is also known as Effective Utilization of Fund. In this respect finance department has to identify the investment opportunities and to choice the best one, after a proper evaluation.

Dividend Decision:

The finance manager is also concerned with the decisions to pay or declare dividend. He assists the top management to decide the portion of profit to be declared as dividend.

Planning & Control Decision:

Finally after evaluating above areas finance manager do the planning and take the corrective measure for controlling the cost and other factors.

So far the objective is concerned; the above stated three functions are same i.e. maximizing shareholders wealth. As their objectives are same the decisions are interrelated. A company having profitable investment opportunities, generally prefer lower dividend payout ratio. On the other hand having a good investment means profit of the company would be more and more dividend can be paid to shareholders. Similarly, finance function and investment functions are also highly correlated. Cost of capital play a major role whether to accept or not an investment opportunities. Financing decisions also dependent on amount of to be retained in the profit.

5. CONCLUSION:

All the above decisions of finance are inter - related with one another. Any decision undertaken by the firm in one area has its impact on other areas as well. For example acceptance of an investment proposal by a firm affects its capital structure and dividend decision as well. So these decisions are inter -related and should be

taken jointly so that financial decision is optimal. All the financial decision has ultimately to achieve the firm's goal of maximization of shareholders wealth.
For proper coordination of these decision areas finance manager can use some financial tools (Financial tools are the techniques that can be employed by the finance manager to solve the problem properly effectively and efficiently) like: 1) Ratio analysis, 2) Fund flow and cash flow analysis, 3) Cash budget, 4) ABC analysis, 5) EOQ model, 6) Ageing schedule, 7) Projected financial statements, 8) Long - term investment appraisal tools - payback period, net present value, profitability index internal rate of return. etc., 9) Cost of capital, 10) Leverages, 11) Hedging, These tools help the management in decision making and using resources effectively.

6. FUTURE STUDY:

1). Find out the best alternative out of three areas.
2). Provide one solution for all areas.
3). Find out relation of these areas with other disciplines like HR.

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