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ACCA F9

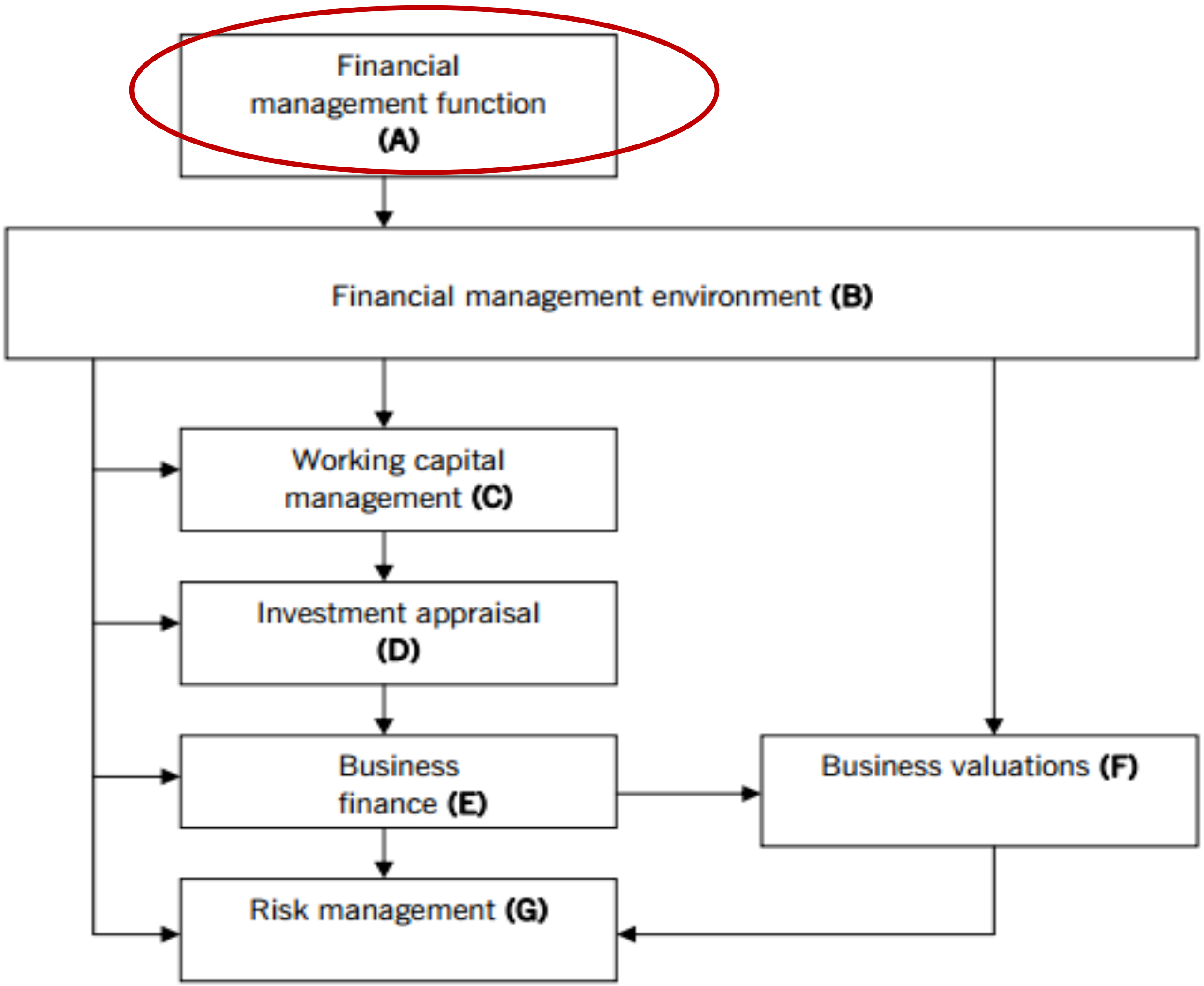
Financial Management（FM）

财务管理

ACCA Lecturer: Jerry Lin

Part A. Financial management function

RELATIONAL DIAGRAM OF MAIN CAPABILITIES



Part A. Financial management function

1. The nature and purpose of financial management
2. Corporate strategy and financial objective
3. Stakeholders
4. Encouraging shareholder wealth maximization
5. Ratio analysis for stakeholders
6. Not for profit organization

1. The nature and purpose of financial management

What is financial management?

Financial management can be defined as the management of the finances of an organization in order to achieve the financial objectives of the organization. The usual assumption in financial management for the private sector is that the **objective of the company is to maximize shareholders' wealth.**

Financial management decisions cover **investment** decisions (part D), **financing** decisions (part E), **dividend** decisions and **risk** management(part G).

1. The nature and purpose of financial management

1. Shareholder wealth maximisation （12/11，12/13）

- 股东获利的组成部分：dividends & capital gain
- 企业更加倾向于保留资金进行再投资以获取更多利润，股东 希望能够拿到分红——trade off
- **total return =（P_1 - P_0 + D）/P_0 (全收益公式)**
  - P_1 minus P_0为资本利得（capital gain）
  - P_0 为购买价格
  - D 为股利分红

1. **Profit maximasation**：Accounting profits can be manipulated to some extent by choices of accounting policies； Profit does not take account of risk；Profits on their own take no account of the volume of investment

2. **The growth of EPS**

   - Earnings per share is calculated by dividing the net profit or loss attributable to **ordinary** shareholders by the weighted average number of ordinary shares.
   - Relevant items for EPS： widely used to measure a company's performance and is of particular importance in comparing results over a period of several years

Other financial target

Risk——profit retention, operating profitability, etc

2. Corporate strategy and financial objective

- Strategy is a course of action to achieve an objective.

There are three main levels of strategy in an organization.

- Strategy may be defined as a course of action, including the specification of resources required, to achieve a specific objective. （short term or long term, depending on the time horizon of the objective it is intended to achieve）.
- Corporate: the general direction of the whole organization
- Business: how the organization or its business units tackle particular markets
- Operational/functional: specific strategies for different departments of the business

2. Corporate strategy and financial objective

Corporate objectives are relevant for the organization as a whole, relating to key factors for business success.

- Profitability (return on investment)
- Market share
- Growth
- Cash flow
- Customer satisfaction
- The quality of the firm's products
- Industrial relations
- Added value

Financial targets may include targets for: earnings; earnings per share; dividend per share; gearing level; profit retention; operating profitability.

The usual assumption in financial management for the private sector is that the primary financial objective of the company is to maximize shareholders' wealth.

3. Stakeholders

1. Stakeholder mapping (will study in P1 andP3)
2. Stakeholder group
   - Internal, external, and connected 要会举例
3. Agency theory
   - Agency relationship means the relationship between management and shareholders expressing the idea that managers act as agents for the shareholder, using delegated powers to run the company in the shareholders' best interests.

3. Stakeholders

- 引起agency problem 的原因主要是：

the separation of ownership and management

- 如何解决？

1. Managerial reward schemes——目标一致性（goal congruence）

1.1performance related pay

1.2 Executive share options plans（ESOPs)

2. Regulatory requirements

4. Encouraging shareholder wealth maximization

1. Managerial reward schemes

Encouraging to increase or maximize shareholder wealth by managerial reward schemes such as performance- related pay and share option schemes. Through these methods, the goals of shareholders and directors may increase in congruence.

• Performance-related pay links part of the remuneration of directors to some aspect of corporate performance, such as levels of profit or earnings per share. (problem : possibility of managers influencing corporate affairs for their own benefit rather than the benefit of shareholders, for example, focusing on short-term performance while neglecting the longer term).

• Share option schemes bring the goals of shareholders and directors closer together to the extent that directors become shareholders themselves. It allow directors to purchase shares at a specified price on a specified future date, encouraging them to make decisions which exert an upward pressure on share prices.

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4. Encouraging shareholder wealth maximization

2. Regulatory requirements

Regulatory requirements can be imposed through corporate governance codes of best practice and stock market listing regulations.

- Corporate governance codes of best practice, such as the UK Corporate Governance Code, seek to reduce corporate risk and increase corporate accountability.
- An independent perspective is brought to directors' decisions by appointing non-executive directors to create a balanced board of directors, and by appointing non-executive directors to remuneration committees and audit committees.

Stock exchange listing regulations can place obligations on directors to manage companies in ways which support the achievement of objectives such as the maximization of shareholder wealth.

5. Ratio analysis for stakeholders

Ratio analysis is often used by stakeholders to assess the performance of a company. Ratios are normally split into 4 categories :

a) Profitability – important to assess managerial performance

$$ROCE = \frac{\text{Profit from operations}}{\text{Capital employed}} \%$$

$$ROCE = \frac{\text{Profit from operations}}{\text{Revenue}} \times \frac{\text{Revenue}}{\text{Capital employed}}$$

$$\text{Profit margin} \times \text{Asset turnover}$$

b) Debt – important to banks

$$\text{Gearing} = \frac{\text{Book value of debt}}{\text{Book value of equity}}$$

$$\text{Interest cover} = \frac{\text{Profit from operations}}{\text{Interest}}$$

5. Ratio analysis for stakeholders

c) Liquidity – important to suppliers and customers

Liquidity ratios include:

Current ratio = Current assets : Current liabilities

Acid Test ratio = Current assets- inventory) : Current liabilities

d) Shareholder investor ratios – important to shareholders

$$\text{Dividend yield} = \frac{\text{Dividend per share}}{\text{Market price per share}} \times 100$$

$$\text{Earnings per share} = \frac{\text{Profits distributable to ordinary shareholders}}{\text{Number of ordinary shares issued}}$$

$$\text{Price earnings (P/E) ratio} = \frac{\text{Market price per share}}{\text{EPS}}$$

6. Not for profit organization

Many organizations are not for profit, in this case a more appropriate objective is to make sure that the organization is getting good value for money; economy, efficiency, effectiveness.(3E)

a) Economy – purchase of inputs of appropriate quality at minimum cost

b) Efficiency – use of these inputs to maximise output

c) Effectiveness – use of these inputs to achieves it goals (quality, speed of response)

Economy Efficiency Effectiveness

Input Input/output output

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