

Lec 1 Orientation

Four basic areas of finance

- Corporate finance: basis theories and ideas of finance
- Investments: financial assets such as shares and bonds
- Financial institutions: firms dealing in financial matters
- International finance: covers the above areas in global context

Balance sheet

<ul style="list-style-type: none">• What the firm owns• Current assets<ul style="list-style-type: none">• Cash• Accounts receivable• Inventory• Non-current assets<ul style="list-style-type: none">• Tangible assets• Intangible assets	<ul style="list-style-type: none">• What the firms owes• Current liabilities<ul style="list-style-type: none">• Accounts payable• Non-current liabilities• Shareholders funds<ul style="list-style-type: none">• Equity/capital
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Market values and book values

- Balance sheet is historical accounting
- Real or productive assets
 - Product the cash flows over time
- Financial or paper assets
 - Claim on cash flows of productive assets
- Balance sheet for finance
 - Not concerned with past
 - Market value (what is value of the assets today)

Income statement

Sales
+Other income
-COGS
-Administration expenses
-Other expenses
-Depreciation
=Operating income (Earnings before interest and tax EBIT)
-Interest expense
-taxes
=net income or profit after tax

Lec 2 Introduction

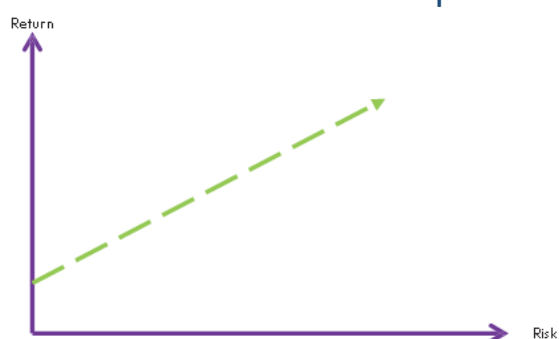
Goal of Financial Management

- **Maximise shareholder wealth**
 - Maximisation of share price
- Profit maximisation is not an appropriate goal
 - No time frame
 - What measure of profit? (depends on accounting standards)
- Other goals are also not appropriate

Factors in any financial decisions

- Dollar amount
- Time (time value of money)
- Risk (uncertainty -> higher return -> higher risk)

The trade-off between expected return and risk



Financial manager's responsibilities

- Investment decisions: what assets to buy (capital budgeting)
 - The most **important** decision
 - Determine the value of **long-term** asset
 - Evaluate size, time, risk of cash flows
 - Select assets that create most shareholder wealth
- Financing decisions: where does the money come from (capital structure)
 - Determine **the best mix** between debt and equity
 - Trade-off between return and risk
- Working capital decisions
 - Managing **short-term** assets and liabilities
 - Forms part of the investment decision

Forms of business

- **Sole trader/ proprietorship**:
 - Single owner
 - **Unlimited liability**
 - Lasts as long as the owner is alive or sells
 - Easy and inexpensive
 - Minimal reporting requirements
- **Partnership**:
 - Similar to sole trader
 - All share in gains and losses
 - **Unlimited liability**
 - If one leaves, partnership ends
- **Company**:

- Separate legal entity
- Unlimited life
- Formal and legal requirements
- Limited liability for shareholders
- Easy to raise capital

Agency problem

- Managers run the firm for the owners
 - To increase the shareholders wealth
 - The shareholders cannot influence managers

Primary market

- Security or instrument issued to an investor **for the first time**
- Public offering or private placement
- Can be debt or equity funding

Secondary market

- Financial securities that are **already issued are bought and sold**
- Way of transferring ownership
- i.e. securities exchange
- Investor-to-investor trading
- Non additional funds are raised by the firm