

FINANCIAL MANAGEMENT

A Complete Study and Revision Guide



SYNAPSE
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FINANCIAL MANAGEMENT

A Complete Study and Revision Guide

Professional Accounting Studies

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This book is designed as a structured learning and revision resource in Financial Management. It supports conceptual understanding, numerical technique, professional judgement and examination readiness. Readers should apply current professional standards, laws and regulatory requirements where these are relevant to practice.

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Preface

Financial Management is best learned as an integrated decision discipline rather than as a collection of isolated formulas. This book therefore develops the subject progressively: from the financial-management framework and financing choices, through time value, valuation, capital structure, investment appraisal and financial analysis, to working-capital decisions, dividend policy, risk, contemporary finance and final integrated revision.

Each chapter combines explanation, decision logic, professional mathematical notation, worked applications, examination technique and structured practice. The emphasis is on understanding why a method is appropriate, setting out complete workings, interpreting the result and communicating a defensible financial decision.

The book is suitable for guided teaching, independent study and intensive revision. Readers are encouraged to work through examples actively, reproduce calculations independently and use the chapter recaps and practice sections as diagnostic tools.

How to Use This Book

Read the learning outcomes first so that the purpose of each chapter is clear. Work through the conceptual framework before attempting numerical questions, because correct technique selection depends on understanding the decision being made.

For calculation topics, reproduce the financial timeline, formula, substitution, workings and interpretation rather than reading the solution passively. For discussion topics, practise concise, distinct points that explain both the principle and its financial implication.

Use the recap, formula and practice sections at the end of chapters to identify weak areas. The final chapter should be attempted under timed conditions after the earlier chapters have been revised.

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Chapter 1

Financial Management Framework and the Financial System

Chapter Overview

This handbook is designed for live class use, independent revision and professional examination preparation. It follows the Chapter One sequence in the SGI Financial Management course framework while highlighting areas that recur in Financial Management examinations. The aim is not to memorise isolated definitions, but to build the ability to identify the issue, choose the relevant principle, present distinct points, and link each point to a financial-management decision.

Exam principle

A strong Financial Management answer combines technical accuracy with decision relevance. For a theory question, each mark should normally correspond to a distinct, properly explained point. For a computation, the method, workings, interpretation and recommendation all matter.

Learning Outcomes

- Explain the nature, scope and theoretical framework of financial management.
- Describe the role and responsibilities of the finance manager towards shareholders, employees, government, society and other stakeholders.
- Analyse financial and non-financial objectives, their overlaps and potential conflicts, and their connection to corporate strategy.
- Explain agency theory, stakeholder theory, corporate governance, managerial performance, compensation and incentive mechanisms.
- Identify and explain ethical issues that arise in financial management.
- Describe the structure of the financial system and distinguish major financial market classifications.
- Explain the role and operation of a securities exchange, including listing, cross-border listing, central depository systems, automated trading and demutualisation.
- Interpret the purpose and basic construction of stock-market indices and apply clean professional financial notation.
- Answer recent-exam-style questions using marker-friendly structure and disciplined financial language.

Chapter Road Map

Part	Focus	What you should be able to do
A	Financial management foundations	Nature, scope, finance-manager role, stakeholders and strategic context.
B	Objectives and governance	Financial/non-financial objectives, agency, stakeholder theory, incentives, governance and ethics.
C	The financial system	Markets, institutions, instruments and flow of funds.
D	Financial markets and the securities exchange	Market classifications, exchange operations, listing, CDS, ATS and demutualisation.
E	Stock-market indices	Purpose, interpretation and basic formula discipline.

Part	Focus	What you should be able to do
F	Exam application	Examination signals, answer technique, worked drills, practice questions and marking guide.

Examination Focus Areas

The pattern below shows that Chapter One is not “introductory” in the sense of being low priority. Recent papers repeatedly examine finance-manager responsibilities, objectives, agency/governance, ethics and market structure. The precise wording changes, but the underlying competencies recur.

Sitting	Chapter One signal	Marks	What the examiner is testing
Apr 2024	Agency-related conflicts and remedies	6	Identify a conflict clearly, connect it to stakeholder interests and propose a practical control or alignment mechanism.
Aug 2024	Fundamental ethical principles	6	State distinct principles and explain how each guides finance decisions.
Dec 2024	Limitations of profit maximisation	4	Critique a financial objective by showing what it ignores or may encourage.
Apr 2025	Financial vs non-financial objectives: overlaps and conflicts	6	Analyse interaction between objectives rather than merely defining them.
Apr 2025	Organised markets vs over-the-counter markets	4	Use paired distinctions based on trading venue, standardisation, transparency and counterparty structure.
Aug 2025	Functions of finance manager; mechanisms aligning managers and shareholders	8	Combine role knowledge with agency-control mechanisms.
Aug 2025	Disadvantages of securities-exchange listing	4	Explain practical costs and constraints of public listing.
Apr 2026	Principles of good corporate governance	4	Give governance principles with concise explanation and organisational relevance.

Revision note: these themes guide emphasis and should not be read as a prediction of future examination content.

Foundations of Financial Management

Nature and Scope of Financial Management

Financial management is the planning, acquisition, allocation, control and monitoring of financial resources in order to achieve the organisation’s objectives while balancing return, risk, liquidity and stakeholder obligations. The finance function therefore goes beyond accounting for historical transactions. It is forward-looking and decision-oriented: it asks where funds should come from, where they should be invested, how risk should be managed, how liquidity should be maintained and how value should be created and distributed.

Core decision frame

Nearly every major Financial Management topic fits into one of four connected decisions: investment, financing, liquidity and distribution. Chapter One provides the conceptual foundation for all four.

Decision area	Financial-management meaning
Investment decision	Determines which assets, projects or opportunities should receive scarce funds and what return/risk trade-off is acceptable.
Financing decision	Determines the mix and sources of funds, including equity, debt, internally generated funds and other financing instruments.
Liquidity decision	Ensures the firm can meet obligations as they fall due without holding excessive idle resources.
Distribution decision	Determines how earnings and cash resources are divided between retention for growth and distributions to investors.
Risk-control decision	Identifies financial exposures and designs controls, governance and policies that protect value and continuity.

The Finance Manager as a Value-Centred Decision Maker

A finance manager should not be described merely as a person who “handles money.” In examination answers, the stronger approach is to state the specific financial responsibility and then explain the decision consequence. The role is integrative: it connects strategy, capital, risk, performance, cash flows and stakeholder expectations.

Finance-manager responsibility	Exam-ready explanation
Financial planning and forecasting	Translate strategy into expected cash flows, financing needs, budgets and funding gaps.
Investment appraisal	Evaluate long-term and short-term uses of funds and recommend opportunities whose expected benefits justify their cost and risk.
Financing and capital structure	Select appropriate sources of funds and maintain a financing mix that supports value, flexibility and risk tolerance.
Working-capital and liquidity management	Manage cash, receivables, inventory and short-term obligations so that operations remain solvent and efficient.
Risk management	Identify financial risks, assess their potential effect and recommend mitigation, hedging or control mechanisms where appropriate.
Financial performance analysis	Interpret financial and market information, compare actual results with targets and support corrective decisions.
Investor and lender communication	Support reliable disclosure and communicate financing, performance and risk information needed by capital providers.
Governance, ethics and compliance	Ensure financial decisions respect delegated authority, internal controls, professional ethics and applicable governance requirements.

Exam Drill 1 | 4 marks

State and explain four functions of a finance manager in an organisation.

Marker-friendly answer framework

- Use four distinct functions; do not repeat “planning” in different words.
- For each function, give a short explanation of the financial decision involved.
- Good answers may draw from investment appraisal, financing, liquidity, risk management, planning/forecasting, performance analysis, investor communication or governance.

Responsibilities to Key Stakeholders

Financial decisions create effects beyond shareholders. An exam-quality stakeholder answer should identify the stakeholder, the financial interest involved and the finance manager’s responsibility. This avoids vague phrases such as “treat stakeholders well.”

Stakeholder	Finance manager’s responsibility
Shareholders / owners	Protect invested capital, pursue sustainable value creation, provide transparent reporting and make financing/investment decisions consistent with an acceptable risk-return profile.
Employees	Support continuity of employment through sound financial planning, honour contractual obligations and avoid decisions that create avoidable solvency or payroll risk.
Government and regulators	Comply with tax, reporting, securities, prudential and other legal requirements; provide truthful information and avoid financial practices designed to evade lawful obligations.
Customers	Support continuity, fair dealing and dependable service by maintaining a financially sustainable organisation rather than pursuing short-term gains that undermine delivery.
Suppliers and lenders	Respect credit terms, provide reliable information where required and manage liquidity so obligations are met as they fall due.
Society and communities	Consider lawful, ethical, environmental and social consequences of financial decisions, including external costs that may not immediately appear in accounting profit.

Exam distinction

Shareholder wealth maximisation remains a central financial objective, but stakeholder responsibilities affect the constraints, risks and sustainability within which that objective is pursued. A good answer does not treat stakeholder interests as automatically identical.

Objectives, Agency, Governance and Ethics

Goals of the Firm and Corporate Strategy

Corporate strategy identifies where the organisation intends to compete and how it intends to create sustainable advantage. Financial management converts that strategy into funding, investment, risk and performance decisions. A strategy that cannot be financed, cannot generate acceptable cash flows or exposes the organisation to unmanageable risk is not financially sustainable.

Profit Maximisation

Profit maximisation seeks the highest possible accounting profit. It is easy to understand and can be useful as an operating target, but it is an incomplete overarching financial objective because accounting profit does not fully capture timing, cash flow, risk, required investment or the sustainability of the result.

- It may ignore the timing of benefits: one shilling received earlier can be more valuable than one shilling received later.
- It may ignore risk: two strategies with the same expected accounting profit may expose owners to very different levels of uncertainty.
- It can encourage short-term decisions, such as cutting maintenance, training or research expenditure merely to improve current-period profit.
- It may not reflect cash flow and liquidity; a profitable firm can still experience cash difficulties.
- It does not directly indicate whether returns are adequate relative to the capital committed.

Shareholder Wealth Maximisation

Shareholder wealth maximisation focuses on increasing the economic value of shareholders' investment. Market value incorporates expectations about future cash flows, timing and risk more directly than accounting profit. In a listed company, this is commonly reflected in the market value of equity, although the finance manager must avoid assuming that short-term price movements always equal long-term intrinsic value.

Basic shareholder-wealth expression

$$\text{Shareholder wealth} = \text{Number of shares} \times \text{Market price per share}$$

Use this as a conceptual expression, not as a substitute for valuation analysis.

Total shareholder return (TSR)

$$TSR = [(P_1 - P_0 + D_1) / P_0] \times 100\%$$

P_0 = beginning share price; P_1 = ending share price; D_1 = dividend received during the period.

Financial and Non-Financial Objectives

Objective category	Meaning and examples
Financial objectives	Examples include profitability, cash generation, growth in shareholder value, liquidity, target returns, gearing limits and cost control.
Non-financial objectives	Examples include product/service quality, employee development, innovation, customer satisfaction, market reputation, environmental responsibility and operational resilience.

Financial and non-financial objectives can reinforce one another. Training may initially increase cost but improve productivity and service quality; stronger governance may increase compliance cost but reduce loss and reputational risk; innovation may reduce current profit while improving future cash flows. They can also conflict, particularly where a short-term financial target encourages actions that weaken longer-term capability.

Relationship	Financial-management interpretation
Overlap: quality and profitability	Better quality may reduce returns, rework and customer loss, improving long-term margins and cash flows.
Overlap: employee development and value	Training may improve productivity, retention and innovation, supporting future profitability.
Conflict: short-term profit vs maintenance	Deferring necessary maintenance can improve current-period profit but increase operational and safety risk.
Conflict: cost reduction vs service quality	Aggressive cost cuts may improve margins while reducing customer experience and future sales.
Conflict: dividends vs growth investment	Higher immediate distributions may satisfy income-seeking investors but reduce funds available for positive-NPV growth opportunities.

Exam Drill 2 | 6 marks

A company is pursuing rapid earnings growth while also committing to employee development, product quality and environmental targets. Examine three overlaps and three conflicts that may arise among these objectives.

Marker-friendly answer framework

- An overlap must show how two objectives can support one another.
- A conflict must show a trade-off: improving one objective can worsen another, at least in the short run.
- Use finance language: cost, cash flow, risk, investment, profitability, reputation or long-term value.

Agency Theory

Agency theory examines relationships in which one party, the principal, delegates decision authority to another party, the agent. In a company, the classic relationship is between shareholders and managers. Because managers control day-to-day decisions while shareholders provide capital, differences in objectives and information can create agency problems and agency costs.

Principal: The party that delegates authority and expects the agent to act on its behalf. **Exam cue:** *In the classic company setting, shareholders are principals.*

Agent: The party given authority to make decisions or perform tasks for the principal. **Exam cue:** *Managers are agents when they manage shareholders' capital.*

Agency problem: A conflict arising when the agent's interests or actions differ from the principal's interests. **Exam cue:** *Do not confuse the conflict itself with the cost of controlling it.*

Agency cost: The value lost or expenditure incurred because of agency problems, including monitoring, bonding and residual loss. **Exam cue:** *A control mechanism may reduce agency loss but itself has a cost.*

Common Sources of Agency Conflict

- Managerial perquisites: managers may consume benefits that raise their utility without proportionate shareholder benefit.

- Risk preference differences: managers may avoid risky positive-value projects because their employment and reputation are concentrated in one firm, while diversified shareholders may tolerate more risk.
- Short-termism: managers may favour actions that improve current reported performance even if they reduce long-term value.
- Empire building: managers may pursue growth, acquisitions or larger budgets because size increases status or influence even where expected returns are inadequate.
- Information asymmetry: managers possess more information than dispersed shareholders, making it difficult for owners to assess decisions promptly.

Mechanisms for Reducing Agency Problems

Mechanism	How it aligns interests
Performance-linked remuneration	Connect part of managerial compensation to well-designed financial and non-financial performance measures, while avoiding incentives that reward excessive short-term risk-taking.
Board oversight	Use an effective board and committees to scrutinise strategy, risk, remuneration and financial reporting.
Audit and internal controls	Strengthen the reliability of information and reduce opportunities for misappropriation, manipulation or unauthorised decisions.
Disclosure and transparency	Reduce information asymmetry by providing timely, understandable and credible information to investors and other stakeholders.
Share ownership / long-term incentives	Give managers a meaningful long-term interest in value creation, provided vesting and performance conditions are well designed.
Debt and covenant discipline	Borrowing can impose cash-flow discipline and contractual restrictions, although excessive debt creates financial risk and its own agency conflicts.
Market discipline	Poorly governed firms may face higher financing costs, investor exit, takeover pressure or difficulty attracting capital.

Exam Drill 3 | 6 marks

Explain three agency conflicts that could arise between an organisation's owners and another stakeholder group, and propose one practical response to each conflict.

Marker-friendly answer framework

- Identify the parties first.
- State the competing interests or incentives clearly.
- Give a remedy that directly addresses that conflict: governance, contract design, disclosure, monitoring, regulation or incentive alignment.

Stakeholder Theory

Stakeholder theory views the firm as having relationships with multiple groups that contribute to, depend on or are affected by its activities. The finance manager must therefore consider how decisions affect investors, employees, customers, suppliers, government, lenders and society. The theory does not eliminate financial discipline. Instead, it broadens the decision frame by recognising that stakeholder relationships can affect cash flows, risk, legitimacy and long-term organisational survival.

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