Collegedunia Handwritten Notes

Quick-Revision Notes for Class 12 Business Studies

Chapter 9: Financial Management

1. Two Definitions to Memorise

Lock Them In

Business finance = money needed for business activity.
Financial management = *optimal procurement* + *usage* of funds.

2. Primary Objective – Wealth Max

Why Not Profit Max?

Profit max ignores: **T**ime value of money · **R**isk · **A**ccounting manipulation · **S**hort-term focus (T-R-A-S). Wealth max = maximise *market price* of equity share.

3. Three Financial Decisions – I-F-D

Memorise the Trio

Investment (capital budgeting – *where* to invest)
Financing (capital structure – *how* to raise)
Dividend (*how much* to distribute)

4. Financial Planning – Two Objectives

Exact NCERT Wording

(a) To ensure *availability of funds whenever required*.
(b) To ensure the firm does not raise resources *unnecessarily*.

Definition spotter: "*Financial blueprint of an organisation's future operations*" $\Rightarrow$ Financial Planning.

5. Capital Structure – Debt-Equity Mix

Trading on Equity Rule

Trading on equity benefits equity holders *only if*
$\boxed{\text{ROI} > \text{Cost of Debt}}$

Always compute ROI first in numerical case: $\text{ROI} = \text{EBIT / Total Capital} \times 100$.

5.1 Capital Structure – 14 Factors

1. Cash flow position · **2.** ICR · **3.** DSCR
2. ROI · **5.** Cost of debt · **6.** Tax rate
3. Cost of equity · **8.** Floatation cost
4. Risk consideration · **10.** Flexibility · **11.** Control
5. Regulatory framework · **13.** Stock market conditions
6. Capital structure of peers

6. Fixed Capital (Capital Budgeting)

Four reasons capital budgeting decisions are special:

1. Long-term growth.
2. Large amount of funds.
3. High risk.
4. Irreversible.

8 factors: Nature of business · Scale · Choice of technique · Technology upgradation · Growth prospects · Diversification · Financing alternatives · Level of collaboration.

7. Working Capital – NWC Formula

Memorise

$$\boxed{\text{NWC} = \text{Current Assets} - \text{Current Liabilities}}$$

Liquidity-Profitability trade-off: more WC = safer but less profitable; less WC = profitable but risky.

7.1 12 Factors (One Letter Each)

Nature of business · **S**cale · **B**usiness cycle · **S**easonal factor · **P**roduction cycle · Credit **A**llowed · Credit av**a**iled · **O**perating efficiency · **R**aw material availability · **G**rowth prospects · **C**ompetition · **I**nflation.

8. Dividend Decision – 11 Factors

Group	Factors
Profitability	Earnings, Stability of earnings, Stability of dividend
Cash availability	Cash flow position, Access to capital markets
Future need	Growth opportunities
External	Shareholder preference, Taxation, Stock market reaction
Constraints	Legal (Companies Act), Contractual (loan covenants)

9. Last-Minute Spotters (CBSE Pattern)

Map the Keyword to the Answer

- *"Financial blueprint of future operations"* ⇒ **Financial Planning**.
- *"Increases return to equity due to fixed financial charges"* ⇒ **Trading on Equity**.
- *"Transport service / leather trader"* ⇒ **Less working capital** (service/trading < manufacturing).
- *"Buy on 3-month credit, sell for cash"* ⇒ Working capital **decreases**.
- *"ROI 8%, cost of debt 10%"* ⇒ **Do not raise debt** – ROI < cost of debt.
- *"No restriction on dividend"* ⇒ **Wrong – legal + contractual constraints exist**.

- "*Capital structure decision is risk-return optimisation*" $\Rightarrow$ **True** – min WACC at optimum debt-equity mix.

10. Numerical Quick-Solve Recipe

Sunrises Ltd. trap:

1. ROI $=$ EBIT / Total Capital $\times$ 100 $=$ 8,00,000 / 1,00,00,000 $\times$ 100 $=$ **8%**.
2. Cost of debt $=$ **10%**.
3. ROI $<$ Cost of debt $\Rightarrow$ **Do not issue debentures**.

Related Collegedunia Resources

Same chapter: NCERT Solutions | Revision Notes | NCERT Book PDF
Continue learning: Ch 8: Controlling | Ch 10: Financial Markets | All Class 12 Business Studies