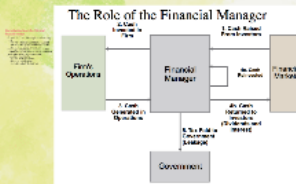


Corporate Finance Harvard Case Solution & Analysis



Role of financial manager

Capital budgeting decisions

- How to invest?
- Which projects to accept? (What assets should we buy?)
- How to raise the money to finance the investment?
- How to manage the risk of the investment?
- How to estimate the value of the investment?
- How to estimate the risk of the investment?

Capital structure decisions

- How to raise the money?
- How to choose between debt and equity?
- How to estimate the value of the investment?
- How to estimate the risk of the investment?

Working capital management decisions

- How to manage the day-to-day operations?
- How to estimate the value of the investment?
- How to estimate the risk of the investment?

Corporate Finance and the Financial Manager

- owners are not usually involved in the day to day management activities
- too many owners- consensus for decisions?
- run by managers- agent of shareholders-represent shareholders' interests.
- Shareholders electing a board of directors
- a group of people who have the final decision-making ability in the corporation.
- the board of directors set rules on how the corporation should be run, lay down policy, and keeps an eye on the performance of the corporation.
- They hire/fire the chief executive officer (CEO) - charged with running the corporation by instituting the rules and policies set by the board of directors

Goal of Financial Management

maximize value for the owners of profit making businesses.

- Objectives:
 - Maximize Sales
 - Minimize Costs
 - Be competitive-increase market share
 - Control risks
 - Survival
 - Asset Liquidity
 - Maintain stable profits or earnings

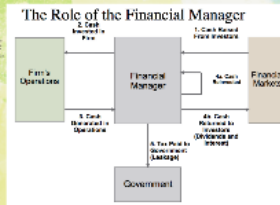
Value and Financial Goals

Value is the present value of the expected future cash flows from the investment.

Financial Goals

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Goal of Financial Management

- maximize value for the owners of profit making businesses.
- Objectives
 - Maximize Sales
 - Minimize Costs
 - Be competitive-increase market share
 - Control risks
 - Survive
 - Avoid Bankruptcy
 - Maximize stable profits or earnings

Values and Financial Goals

- Shareholder wealth creation is the primary objective of the firm.
- The firm's financial goals are derived from its strategic goals.
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Role of financial manager

- capital budgeting decisions
- investment decisions: what assets should we buy?
 - planning and managing a firm's long-term investment strategy
 - invest in risky versus safer assets.
 - What amount of the firm's cash flow should be distributed to investors and how much to hold as cash?
- capital structure decisions
- how to finance investments?
 - choose between debt and equity
 - what is the best way to raise capital?
- working capital management decisions
- what are the firm's assets and liabilities?
 - how much inventory to hold? how much sold on credit?
 - how much money used to support the firm's operations?
 - dividend payout decisions? when or how often?

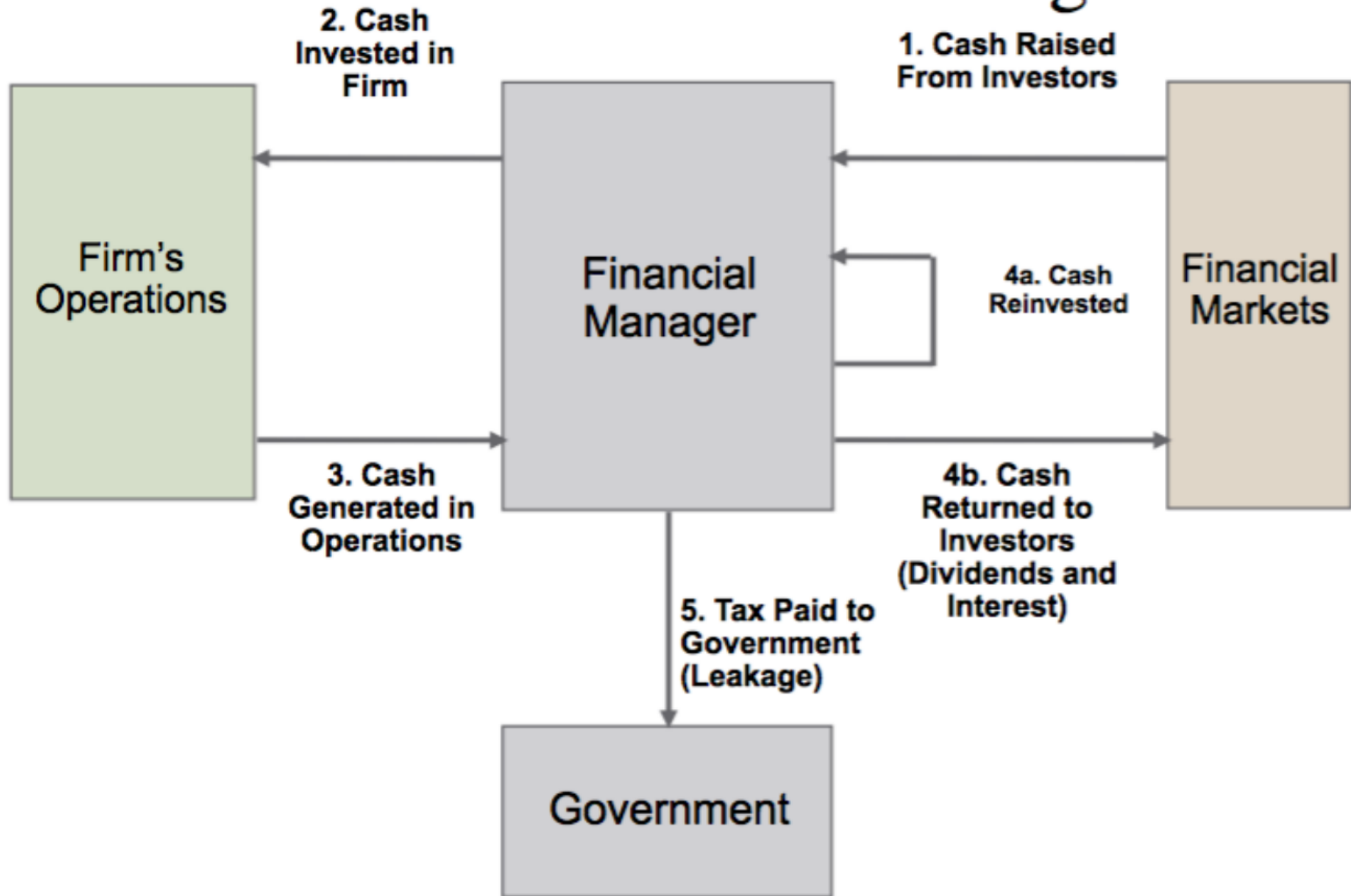
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Role of financial manager

- **capital budgeting decisions**
 - investment decisions? What assets should we buy?
 - planning and managing of a firm's long term investment namely in non-current assets
 - Must assessing the size of future cash flows, the timing of future cash flows and the risk to future cash flows.
- **capital structure decisions**
 - How to finance investment?
 - choose between debt and equity mix
 - all debt? all equity? or a mix?
 - which is the least costly?
- **working capital management decisions.**
 - short term assets and liabilities?
 - how much inventory to hold? how much sold on credit?
 - how much money owed to suppliers? bought on credit?
 - dividend payout decisions? retain or give out?

The Role of the Financial Manager



Interaction between the firm and financial market

- Firm will raise finance by issuing shares or borrowing cash
 - financial markets are also funded by households: put savings in financial institutions which in turn provide funds to the financial markets
- Assuming that the firm use both equities and debt securities to finance its activities- use cash to invest on assets which will generate returns or cash.
- The cash generated used to :
 - pay taxes to the government
 - pay dividends and creditors
 - reinvest: retained in the business.

Goal of Financial Management

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- Objectives:
 - Maximize Sales
 - Minimize Costs
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 - Control risks:
 - Survive
 - Avoid Bankruptcy
 - Maintain stable profits or earnings

Problems with the goals?

- maximize sales by reducing prices
- minimize costs by reducing staffs or reducing expenditure on research and development.
- avoid bankruptcy: do not borrowing at all/do not taking any risks
- maximize profits- maximize current against future profits? Should our profit maximization strategy be long term or short term?
- for the interests of shareholders? NO
 - profit maximization will involve some element of risks

THE GOAL

- shareholder buys shares from a company for a return
- financial manager decisions must increase the value of equity.
- goal of financial management: maximize the current value per share of the existing equity
- identify the investment and financing arrangements which will have a positive impact on the value of equity
- corporate finance as the study of relationship between business decisions and the equity value of the firm.

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