
PRESCRIPTION: 203 BUSINESS FINANCE

Last date for assessing this prescription is 31 December 2008

INTRODUCED 1990
UPDATED 1999 (Implemented Semester Two 2000)

AIM OF SUBJECT

To provide students with the necessary knowledge and skills of business finance so that they may function effectively in association with the financial management decision-makers. Emphasis is given to modern accounting practice in New Zealand, particularly as it relates to small to medium businesses.

ASSUMED PRIOR KNOWLEDGE

A level of knowledge as provided in the NZDipBus paper 100 Accounting Principles or the equivalent.

An understanding of mathematics and statistics as provided in the NZDipBus paper 160 Quantitative Business Methods.

COURSE LENGTH

The equivalent of 20 National Qualifications Framework credits, with a minimum of 60 class contact hours or the equivalent for open learning/distance tuition.

RESOURCES

Suggested Student References

One or more of the following

Gitman, Lawrence J. Foundations of managerial finance. New York: HarperCollins College Publishers. Latest edition.

Gitman, Lawrence J. Principles of managerial finance. Reading, MASS: Addison Wesley. Latest edition.

Gitman, Lawrence J. and others. Principles of managerial finance in Australia. Melbourne: Addison Wesley. Latest edition.

Peare, Paula. (1999) An introduction to the New Zealand financial system. Auckland: Longman.

Peterson, Pamela P. Financial management and analysis. New York: McGraw-Hill. Latest edition.

Additional Student References

Brealey, Richard A., Myers, Stewart C. and Marcus, Alan J. Fundamentals of corporate finance. London: Irwin/McGraw Hill. Latest edition.

Besley, Scott and Brigham, Eugene F. (1999) Principles of finance. Fort Worth, TX: Dryden Press.

Brigham, Eugene F. and Houston, Joel F. Fundamentals of financial management. Fort Worth, TX: Dryden Press. Latest edition.

Osteryoung, Jerome S., Newman, Derek L. and Davies, Leslie G. (1997) Small firm finance: an entrepreneurial perspective. Fort Worth, TX: Dryden Press.

Petty, J. William and others. (1996) Basic financial management. Sydney: Prentice Hall.

Weston, J Fred., Besley, Scott and Brigham, Eugene F. Essentials of managerial finance. Fort Worth, TX: Dryden Press. Latest edition.

Additional References

Financial and accounting periodicals, such as:

- Abacus. Sydney: Sydney University Press. 2 issues per year
- The Accountant. Dublin: Lafferty Publications. Monthly
- Accounting and business research. London: Institute of Chartered Accountants in England and Wales. Quarterly
- Australian CPA. Melbourne: Australian Society of Certified Practising Accountants. Monthly
- CA magazine. Edinburgh: Institute of Chartered Accountants of Scotland. Monthly
- Charter. Sydney: Institute of Chartered Accountants in Australia. Monthly
- Chartered accountants journal of New Zealand. Wellington: Institute of Chartered Accountants of New Zealand. 11 issues per year
- Journal of accountancy. New York: American Institute of Certified Public Accountants. Monthly
- Pacific accounting review. Palmerston North: Pacific Accounting Review Trust. 2 issues per year.
- The Independent. Auckland. 48 issues per year

The financial section of:

- National business review. Auckland. 48 issues per year
- The main centre daily newspapers

Note: Many of the above texts and periodicals treat the subject in much greater depth than is required for this course. Students are therefore recommended to first check with their tutor as to which texts they should obtain.

TIME AND ASSESSMENT SCHEDULE

The prescription assumes a RCAP model of assessment (R = recall, C = comprehension, A = application, P = problem solving). In assessing to the prescription, it is expected that, in general, assessment will be of the ability of students to apply the learning outcomes and to undertake problem solving within the course material. Assessment of comprehension should be undertaken only where it is appropriate. Assessment of recall is implicit.

TOPICS	Time in hours	Assessment Weightings (%)	
		min	max
1 The Environment of Business Finance	2	2	5
2 Financial Planning and Control	5	5	10
3 Working Capital Management	10	15	20
4 Investment Decisions	16	25	30
5 Capital Structure	9	10	15
6 Sources of Finance	9	10	15
7 Integrated Case Study	9	15	20
	TOTAL	60	100%

This schedule is a recommendation and guide for lecturers/tutors, examiners and students. It gives:

- 1 an approximate allocation of time in hours, by topic
- 2 an approximate allocation of assessment in percentages, by topic.

The order of the topics presented here should only be taken as a guideline. The effects of taxations on business finance decisions should be included and considered at each stage as appropriate.

TOPICS

1 THE ENVIRONMENT OF BUSINESS FINANCE

Learning Outcome

Students who have fulfilled all requirements for this topic understand the environment of business finance.

Assessment Criteria

Students will be expected to:

- 1.1 Explain the theory and objectives of business finance, and explain the basic function of corporate finance:
 - profit motive - maximise profit
 - maximise earnings per share
 - maximise shareholder wealth.
- 1.2 Evaluate and justify maximisation of wealth in terms of:
 - investment decision
 - financing decision
 - dividend decision.
- 1.3 Explain the relationship between the corporate, financial and general objectives of shareholders, managers, and other interested groups.
- 1.4 Explain the following types of business organisation and the extent to which each is able to raise finance:
 - sole traders
 - partnerships (including special partnerships, syndicates, and joint ventures)
 - corporations.

2 FINANCIAL PLANNING AND CONTROL

Learning Outcome

Students who have fulfilled all requirements for this topic can undertake financial planning and control.

Assessment Criteria

Students will be expected to:

- 2.1 Explain the role of financial management.
- 2.2 Explain the role of financial planning and control.
 - What is financial planning?
 - Why a company may need extra finance.
 - Funds flow cycle and forecasting the flow of funds.
- 2.3 Explain the relationships between financial planning and control, the efficient allocation of funds, and the acquisition of funds on favourable terms.

- 2.4 Prepare cash budgets, and analyse the relationships among various budgets and cash flow statements.
- Percentage-of-sales method and sales forecasting are to be used.
- 2.5 Apply and interpret financial ratio analysis to financial management, and explain relationships between financial ratios.
- 2.6 Explain the effects of risk in financial planning decisions by
- evaluating risk
 - making risk comparisons
 - evaluating the impact of international financial markets.

3 WORKING CAPITAL MANAGEMENT

Learning Outcome

Students who have fulfilled all requirements for this topic can carry out cash and other forms of capital management.

Assessment Criteria

Students will be expected to:

- 3.1 Explain working capital management
- basic concepts
 - operating cycle
 - risk-return trade-offs
 - current assets and current liabilities
 - managing the company's use of current liabilities
- and recommend an appropriate level of working capital and liquidity.
- 3.2 Explain cash management:
- why businesses hold liquid assets
 - how liquidity is measured
 - how the cash assets can be managed efficiently.
- 3.3 Explain the processes used in managing accounts receivable:
- recommend credit standards
 - design a plan for control of receivables, incentives for early payment, use of trade credit, collection policy
 - evaluate the credit application.
- 3.4 Explain the process of managing inventories:
- recommend an optimum investment level in inventory
 - evaluate inventory control
 - evaluate the impact of inflation on inventories.

4 INVESTMENT DECISIONS

Learning Outcome

Students who have fulfilled all requirements for this topic can apply a knowledge of the major capital budgeting techniques to evaluate and recommend investment projects (including identifying and using the appropriate formulae and tables).

Assessment Criteria

Students will be expected to:

- 4.1 Apply capital expenditure decisions to
 - the capital budgeting process
 - estimated cash flows.
- 4.2 Explain the time value of money, calculate compound value of lump sums and annuities, calculate present values of future lump sums and annuities, calculate perpetuities and make applications of present values.
- 4.3 Explain the following:
 - the principles of capital budgeting under certainty
 - methods of capital budgeting
 - the required rate of return
 - establishment of cash flow from investment.
- 4.4 Apply and explain unsophisticated capital budgeting techniques such as:
 - calculating payback
 - calculating accounting rate of return.
- 4.5 Apply and interpret the output of sophisticated methods of capital budgeting:
 - discounted cash flow approaches
 - calculating net present value
 - calculating profitability index
 - calculating internal rate of return
 - using discount factors
 - using market capitalisation rate.
- 4.6 Critically evaluate the techniques of unsophisticated and sophisticated methods of capital budgeting in terms of:
 - net present value compared with internal rate of return
 - capital rationing
 - multiple rates of return
 - business and financial risk
 - inflation.

- 4.7 Briefly explain how risk in investments may be evaluated using computer simulation. Explain and four of the following:
- simple rules of thumb such as ignoring risk, payback period and conservative estimates
 - risk-adjusted discount rates
 - certainty equivalents
 - sensitivity and scenario analysis
 - portfolio theory and the concepts of standard deviation, correlation, systematic and unsystematic risk
 - progress reports and post audit.

5 CAPITAL STRUCTURE AND COST OF CAPITAL

Learning Outcome

Students who have fulfilled all requirements for this topic understand, and can calculate and apply the concepts of cost of capital and capital structure.

Assessment Criteria

Students will be expected to:

- 5.1 In relation to capital structure and cost of capital:
- define the cost of capital
 - list sources of finance
 - specify requirements for calculating the cost of capital
 - explain factors determining the cost of capital
 - give rationales for using weighted average cost of capital.
- 5.2 Calculate the components of cost of capital:
- cost of debt
 - cost of equity
 - cost of preference share capital
 - cost of retained earnings
 - weighted average cost of capital (Gordon model).
- 5.3 Apply the principles of the capital asset pricing model including:
- main purpose
 - assumptions (for example, efficient market hypothesis)
 - the relationship between risk and return
 - the cost of equity.

- 5.4 Apply the principles of optimal capital structure to financial management:
- use of operating and financial leverage
 - breakeven analysis
 - combined effect of operating and financial leverage
 - operating, financial, and total risk
 - financial risk and business failure.

6 SOURCES OF FINANCE

Learning Outcome

Students who have fulfilled all requirements for this topic can explain the difference between short-term and long-term financing and the quality of credit, and recommend a plan of action.

Assessment Criteria

Students will be expected to:

- 6.1 Explain short-term financing principles with reference to:
- composition of short-term financing
 - trade credit, terms of trade credit, advantages and disadvantages of trade credit, who bears the cost of trade credit and accrual accounts
 - bank loans, the banking system, bank credit, transaction loans, interest rates on bank loans
 - money market credit, commercial bills, accommodation bills, acceptance credits, promissory notes, security for bills, inter-company lending
 - secured lending arrangements, collateral value, accounts receivable financing and factoring, credit cards
 - inventory financing.
- 6.2 Give reasons for long-term financing, compare and contrast
- debentures
 - mortgages
 - leases
- and make a lease v buy decision.
- 6.3 Discuss the types of equity finance including:
- capital structures
 - financial leverage
 - the rights of ordinary shareholders and calculation of the value of these rights
 - reasons for using equity funds
 - principles of convertible notes and bonus issues
- and analyse their effect on control and earnings.

- 6.4 Explain options, preferentials, and subordinated debt.
- 6.5 Discuss theories of dividend policy and the effect different policies have on retained earnings.

7 CASE STUDY

Learning Outcome

Students who have fulfilled all requirements for this topic can apply finance techniques to resolve business problems.

Assessment Criteria

Students will be expected to:

- 7.1 Apply (on an integrated basis) the various techniques learned in the individual topics of this paper to a business finance case study, and put forward suitable recommendations and suggestions, including:
- the viability of the project
 - the financing of the project
 - the implications of the project on working capital management.

TEACHING NOTES

Throughout this paper, lecturers/tutors should stress that business finance problem solving underpins good business practice.

Financial risk management is a recurrent theme which should be addressed within each topic as appropriate.

Lecturers/tutors should take opportunities, as time allows, to include other topics within the area of business finance while ensuring that the requirements of the prescription are still met. In particular, some introduction to international finance may be appropriate. The case study (topic 7) offers particular opportunity for further material to be developed.

The use of computer simulation is encouraged where appropriate.