

Financial Management Decisions

In organizations, managers in an effort to minimize the costs of procuring finance and using it in the most profitable manner, take the following decisions:

Investment Decisions: Managers need to decide on the amount of investment available out of the existing finance, on a long-term and short-term basis. They are of two types:

- Long-term investment decisions or Capital Budgeting mean committing funds for a long period of time like fixed assets. These decisions are irreversible and usually include the ones pertaining to investing in a building and/or land, acquiring new plants/machinery or replacing the old ones, etc. These decisions determine the financial pursuits and performance of a business.
- Short-term investment decisions or Working Capital Management means committing funds for a short period of time like current assets. These involve decisions pertaining to the investment of funds in the inventory, cash, bank deposits, and other short-term investments. They directly affect the liquidity and performance of the business.

Financing Decisions: Managers also make decisions pertaining to raising finance from long-term sources (called Capital Structure) and short-term sources (called Working Capital). They are of two types:

- **Financial Planning decisions** which relate to estimating the sources and application of funds. It means pre-estimating financial needs of an organization to ensure the availability of adequate finance. The primary objective of financial planning is to plan and ensure that the funds are available as and when required.
- **Capital Structure decisions** which involve identifying sources of funds. They also involve decisions with respect to choosing external sources like issuing shares, bonds, borrowing from banks or internal sources like retained earnings for raising funds.

Dividend Decisions: These involve decisions related to the portion of profits that will be distributed as dividend. Shareholders always demand a higher dividend,

while the management would want to retain profits for business needs. Hence, this is a complex managerial decision.