



# Financial Management & Business Financing

## Meeting 12

# Balance Sheet (000 per month)

## ASSETS

Cash  
Accounts  
Receivable  
Stock

Equipment  
Vehicle

Total assets

## LIABILITY

? Account payable  
Financial Institution  
? Debt

? owner's capital  
?

? Total Liability

# Working capital & Profit level of invested capital

- Working capital = Current Assets related to Operations – Current Liabilities related to Operations + Fixed assets
- Working capital = ?
- Rate of return on investment = Working Capital / NOPAT (Net Operating After Tax) = ?

# Profit / Loss (000 per month)

Sales	?
Cost of goods sold (-)	?
initial stock (+)	?
Purchase (+)	?
Direct labor costs (+)	?
Last stock (-)	?
Gross Profit	?
Sales and administration costs (-)	?
Operating profit	?
Interest expense (-)	?
Profit before tax	?
Tax (-)	?
Net profit	?

# Profit Margin, ROA, ROE

- Margin = Net Income / Sales

=

- ROA = Net Income / Total Assets

=

- ROE = Net Income / Total Own Capital

=

# Gross Profit, Net Profit, Debt Repayment Ability

- Gross profit =
- Net Income =
- Debt Pay Ability =  
= Operating profit / interest expense

# Effectiveness of Asset Management & Financial Liquidity Conditions

- Inventory Turnover = Sales / Supplies  
=
- Asset Turnover = Sales / Total Assets  
=
- Liquidity = Current Assets / Current Liabilities  
=

# Concept

## Financial Management for Business Start-ups

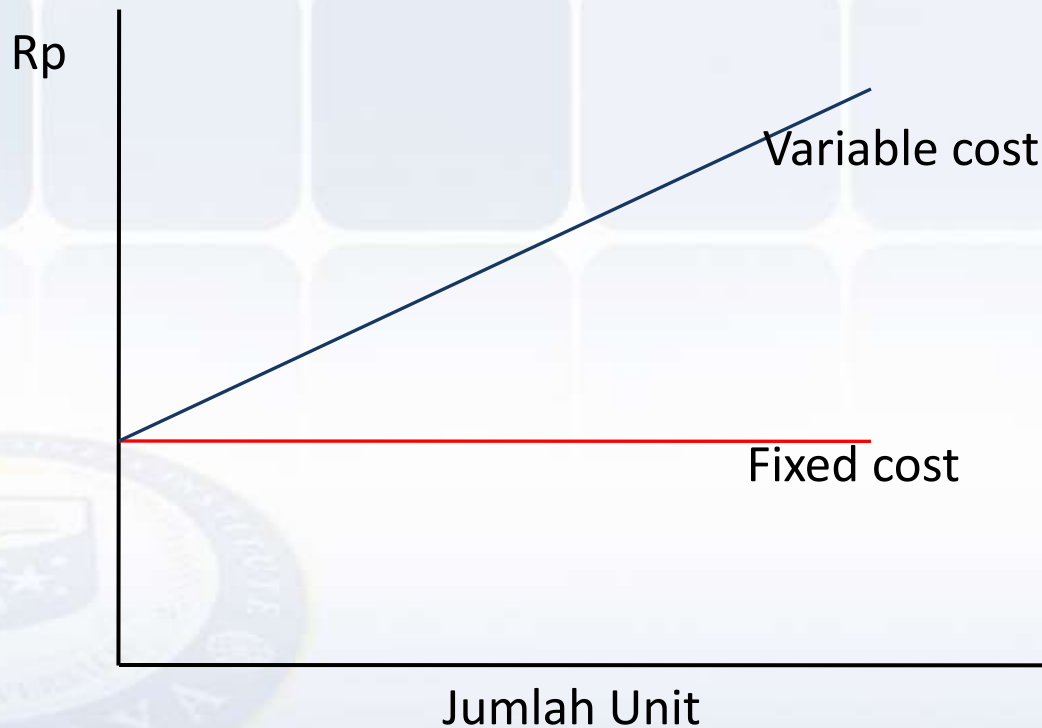




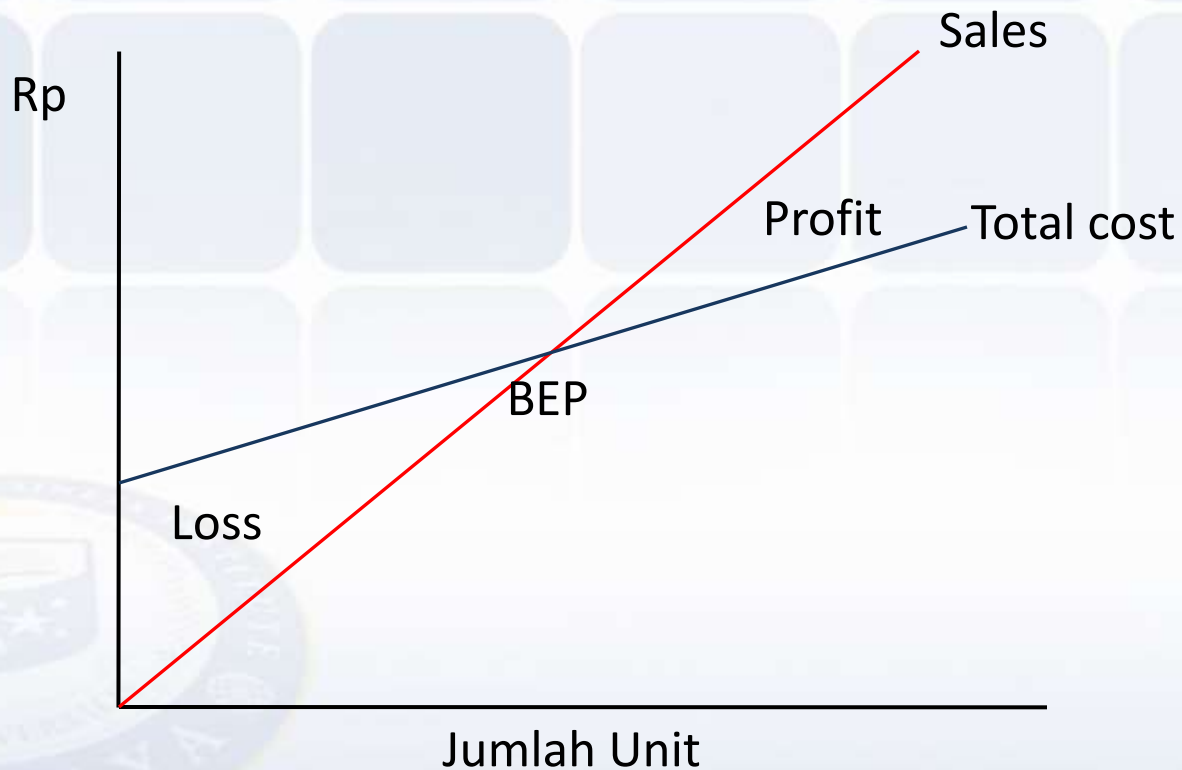
# Agenda

- Basic Financial Management for Start-Up Business Owner
- Financial Feasibility Analysis
- Managing Working Capital
- Managing Debt
- Managing Cash Flow
- Managing Financial Performance

# Fixed Cost vs Variable Cost



# Break Even Point



**NPV:** Sum of the PVs of inflows and outflows.

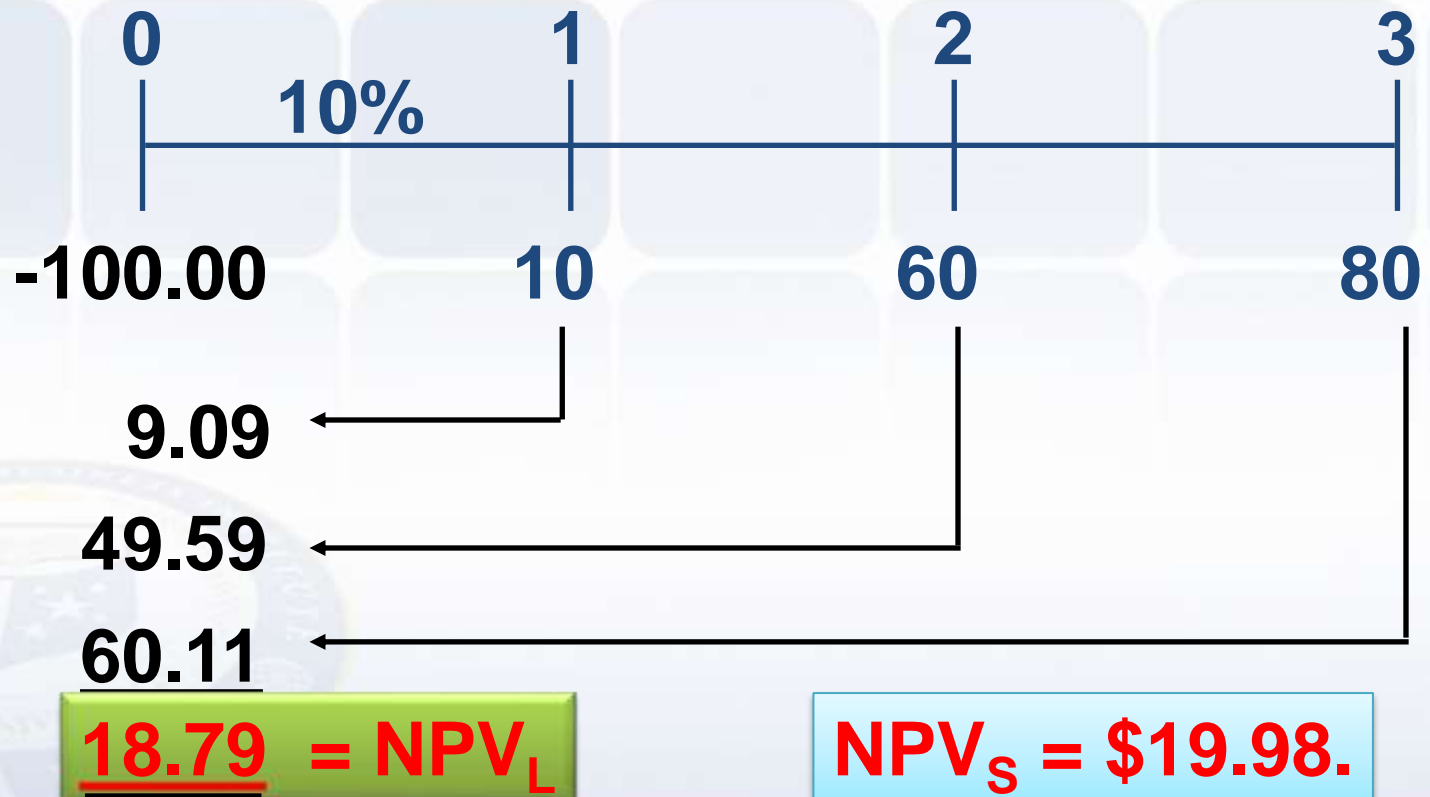
$$NPV = \sum_{t=0}^n \frac{CF_t}{(1+r)^t}.$$

Cost often is  $CF_0$  and is negative.

$$NPV = \sum_{t=1}^n \frac{CF_t}{(1+r)^t} - CF_0.$$

# What's Project L's NPV?

Project L:



# Calculator Solution

Enter in CFLO for L:

-100	<b>CF<sub>0</sub></b>		
10	<b>CF<sub>1</sub></b>		
60	<b>CF<sub>2</sub></b>		
80	<b>CF<sub>3</sub></b>		
10	<b>I</b>	<b>NPV</b>	<b>= 18.78 = NPV<sub>L</sub></b>

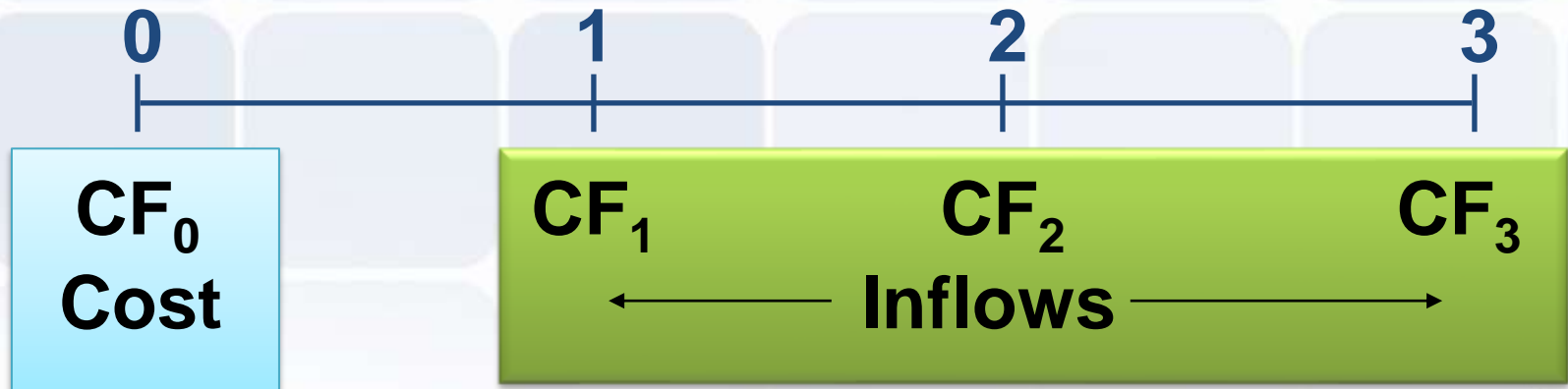
# Rationale for the NPV Method

$$\begin{aligned}\text{NPV} &= \text{PV inflows} - \text{Cost} \\ &= \text{Net gain in wealth.}\end{aligned}$$

Accept project if  $\text{NPV} > 0$ .

Choose between mutually exclusive projects on basis of **higher NPV.** Adds most value.

# Internal Rate of Return: IRR



**IRR is the discount rate that forces PV inflows = cost. This is the same as forcing NPV = 0.**



**NPV:** Enter  $r$ , solve for NPV.

$$\sum_{t=0}^n \frac{CF_t}{(1+r)^t} = NPV.$$

**IRR:** Enter  $NPV = 0$ , solve for IRR.

$$\sum_{t=0}^n \frac{CF_t}{(1+IRR)^t} = 0.$$

# Find IRR if CFs are constant:



<b>INPUTS</b>	3	-100	40	0	
	<b>N</b>	<b>I/YR</b>	<b>PV</b>	<b>PMT</b>	<b>FV</b>
<b>OUTPUT</b>	9.70%				

Or, with CFLO, enter CFs and press  
**IRR = 9.70%.**



*Bogor Palace, Bogor, West Java*

*"Keep smiling,  
because life is a  
beautiful thing and  
there's so much to  
smile about." -  
Marilyn Monroe*

# Money Management Strategies

- ❑ Effective money management strategies include organizing and maintaining personal financial records, overseeing the household budget, handling the checkbook, and achieving financial goals based on careful planning through the balance sheet and cash flow statements.
- ✓ A **balance sheet**, also known as the net worth statement, lists all items of value and all amounts owed. These are referred to as assets and liabilities, respectively. The balance sheet illustrates projected savings and expenses.
- ✓ A **statement of income**, showed company financial performance over specific period.
- ✓ A **cash-flow statement** summarizes all cash receipts and payments for a given time frame. The cash flow statement provides information on income and spending behavior.
- ✓ A **budget** assesses the current financial situation, provides direction for achieving financial goals, creates budget allowances, and provides feedback for evaluating planned objectives.

# Balance Sheet

## Asset

- Current Asset
  - Cash
  - Account Receivables
  - Inventory
- Fixed Asset
  - Equipment
  - Land
  - Building

## Liability & Equity

- Liability
  - Account Payable
  - Notes Payable
  - Accruals
  - Long-term debt
- Equity
  - Common stock
  - Retained Earnings

# Income Statement (P&L)

- Net Sales
  - (-) COGS
  - (-) Selling & GA expenses
- EBITDA
  - (-) Depreciation
  - (-) Amortization
- EBIT
  - (-) Tax
- Net Income

# Working Capital

- also known as **net working capital**, is a financial metric which represents operating liquidity available to a business
- *Net operating working capital*  
= *Operating CA – Operating CL*  
= *(cash, receivables, inventory) – (account payable, accruals)*
- *Net operating capital*  
= *Net Operating Working Capital + Fixed Asset*

# Working Capital Management

- Ensuring that the firm is able to continue its operations and that it has sufficient cash flow to satisfy both maturing short-term debt and upcoming operational expenses.
- Considerations:
  - Cash conversion cycle
  - ROIC (Return on Invested Capital) and CoC (Cost of Capital)
- Areas:
  - Cash Management
  - Inventory Management
  - AR Management
  - AP Management



# Debt Management

- **Leverage and the Use of Credit:**
- ✓ The degree to which borrowed capital is used to supplement and extend equity capital:
  - Leverage increases with increases in the debt/asset ratio.
  - Leverage can be a powerful tool, but use with caution.
- ✓ Should I borrow capital and use leverage to increase my profits?
  - Only if  $ROA > i$
- ✓ If  $ROA < i$ :
  - Equity capital has to be used to help pay the interest.

# Types of loan

By Length of repayment:

**Short-Term Loans**  
**Intermediate-Term Loans**  
**Long-Term Loans**

By Use of funds:

**Real Estate Loans**  
**Non-Real Estate Loans**  
**Personal Loans**

By Type of security:

**Secured**  
**Unsecured**

By type of Rate:

**Fixed Rate**  
**Variable Rate**

By Type of Repayment Plan:

**Single Payment Loan**  
**Line of Credit**  
**Amortized Loan**  
**Balloon Payment Loan**

# The Cost of Borrowing

## ✓ Interest Rates:

- (APR) Annual Percentage Rate/ Nominal Rate.
- Periodic Rate
  - Periodic rate =  $APR/m$
- Effective Rate
  - $Eff = (1 + \text{Periodic rate})^m - 1$

## ✓ Other cost:

- Loan closing fees or “points.”
- Appraisal fees.
- Other fees.

## Comparing the cost of different plans:

1. Calculate the dollar amount to be repaid in each time period:  
Principal, interest, other fees.
2. Find the discounted present value of the series of payments:  
Use the same discount rate for each alternative.
3. Find the NPV, or true cost, of the loan:  
IRR to the lender if want in percentage terms.

# Sources of Funds

- Individual Deposits & Savings
- Loan:
  - Family loan
  - Neighbors loan
  - “Pegadaian” (Pawnshop)
  - Bank loan (commercial bank, BPR, Syariah bank, etc)
  - Venture capital
  - Leasing
  - Etc.
- Suppliers
- Customers

# Cash flow statement

- A **cash-flow statement** summarizes all cash receipts and payments for a given time frame. The cash flow statement provides information on income and spending behavior
- Cash basis
- Exclude depreciation, amortization & accruals

# Statement of Cash Flow

- (+) Cash flow from operation
  - (+) Inflow (all receipt from production, sales, delivery, procurement, advertising, inventory, etc)
  - (-) Outflow (all payment for production, sales, delivery, procurement, advertising, inventory, etc)
- (+) Cash flow from investing
  - (+) Inflow (all receipt from investment result)
  - (-) Outflow (all payment for investment, such as: buy assets, make loan to customer, etc.)
- (+) Cash flow from financing
  - (+) Outflow (such as: new debt, new fund from equity)
  - (-) Outflow (such as: dividend payment)
- Net increase (decrease) in cash

# Financial Performance Indicators (1)

- **Liquidity:** Can we make required payments as they fall due?
  - $CR = CA/CL$
  - $QR = (CA-Inv)/CL$
- **Asset management:** Do we have the right amount of assets for the level of sales?
  - $Inv. TO = Sales/Inv$
  - $DSO = Receivables/Average\ sales\ per\ day$
  - $FATO = Sales/TFixedAsset$
  - $TATO = Sales/TA$



# Financial Performance Indicators (2)

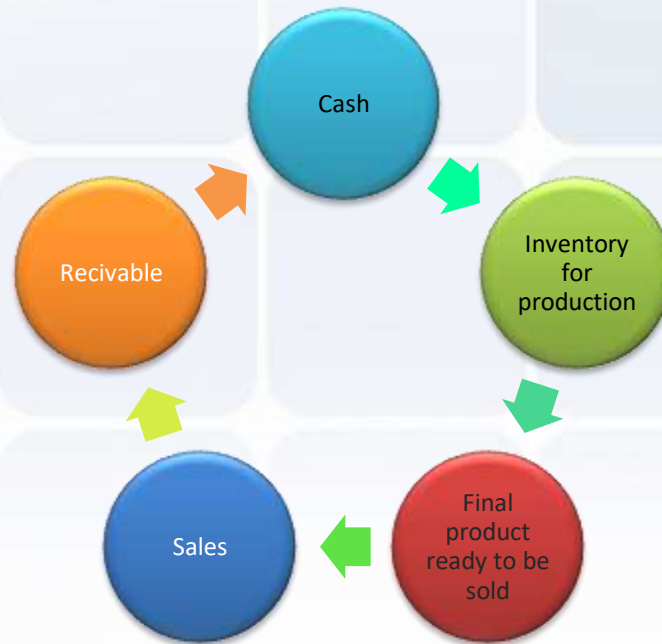
- **Debt management:** Do we have the right mix of debt and equity?
  - Debt ratio =  $TL/TA$
  - TIE =  $EBIT/\text{interest charges}$
- **Profitability:** Do sales prices exceed unit costs, and are sales high enough as reflected in PM, ROE, and ROA?
  - $PM = NI/\text{Sales}$
  - $BEP = EBIT/TA$
  - $ROA = NI/TA$
  - $ROE = NI/CE$

# Tips & Tricks



# Tips for Managing Working Capital

- Define cash conversion cycle



- Use cash management policy
- Use inventory management policy
- Use AR management policy
- Use AP management policy

# Tips for Asking a Loan Funds

- Knowing your business characteristics
- Knowing how much rupiah you need
- Asses payment capacity
- Asses interest and maturity of loan
- Asking more explanation & simulation
- Preparation for loan proposals



**end**

