INTERNATIONAL JOURNAL OF ACADEMIC RESEARCH IN ECONOMICS & MANAGEMENT SCIENCES

OPEN ACCESS JOURNAL

Vol 13, Issue 4, (2024) E-ISSN: 2226-3624

Financial Management and its Importance within a Company

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To Link this Article: http://dx.doi.org/10.6007/IJAREMS/v13-i4/22350 DOI:10.6007/IJAREMS/v13-i4/22350

Published Online: 15 October 2024

Abstract

For many, financial management means: managing your bank accounts: paying your rent or mortgage, paying your utility bills, buying groceries, maybe even planning a monthly budget. But business financial management is a much more complex concept. It involves controlling and tracking all money coming in and out of the company, as well as taking steps to increase the profitability and financial security of the company.Financial management means controlling the flow of money in and out of the organization. Every business must sell products or services, pay expenses, balance the records and record taxes. Financial management includes all of these, along with more complex processes such as paying employees, purchasing materials, and submitting reports to government agencies to show compliance with applicable laws and regulations. The act of monitoring all these transactions is the financial management of a company. In general, the bigger the company its, the more complicated financial management becomes.

Keywords: Financial Management, Monitoring, Controlling, Protecting, Reporting.

Introduction

For many, financial management means: managing your bank accounts: paying your rent or mortgage, paying your utility bills, buying groceries, maybe even planning a monthly budget. But business financial management is a much more complex concept. It involves controlling and tracking all money coming in and out of the company, as well as taking steps to increase the profitability and financial security of the company. To get a clearer picture, we need to identify and analyze some of the important objectives and functions of financial management.

What is financial management?

Financial management means controlling the flow of money in and out of the organization. Every business must sell products or services, pay expenses, balance the records and record taxes. Financial management includes all of these, along with more complex processes such as paying employees, purchasing materials, and submitting reports to government agencies to show compliance with applicable laws and regulations. The act of monitoring all these transactions is the financial management of a company. In general, the bigger the company its, the more complicated financial management becomes.

Employees who specialize in financial management are responsible for all money coming in and out of the company. Smaller companies will have at least one accountant or bookkeeper who works with the bank to execute these transactions and track the flow of money. Large companies will often have entire finance teams led by a CFO, controller, head of finance or someone in a similar role.

The main task of the finance team is to ensure that the company remains solvent and does not run out of cash – but it is not its only duty. It is also responsible for managing loans and debt, balancing the books, overseeing investments, raising venture capital, and managing public offerings (namely, selling company shares on the open market). Basically, the finance team protects a company's financial resources, monitors and controls all transactions, and takes action to maximize the company's profitability.

Understanding financial management

Financial management includes business processes that cover every team and department in the company. Responsibilities of a finance team includes:

- *Billing and Accounts Receivable:* The money customers pay or have promised to pay. Finance teams are responsible for sending invoices and processing payments as they come in. Collections teams are responsible for tracking overdue accounts (this process is sometimes outsourced to third parties).
- Payment obligations: The money the company owes its traders and suppliers. Financial teams are responsible for paying these invoices and recording payments.
- *Bank transactions and reconciliations:* Financial teams work closely with banks to ensure all bank transactions are processed correctly. They must also ensure that the account statements correspond to their own records in the company's General Ledger and sub-ledgers. The financial team must track and correct any discrepancies between the bank statements and the books – a process known as reconciling the accounts.
- *Closing the records:* on a certain date, the company will make transactions in a certain period so that it can reconcile its accounts and report its financial position. Closing, as this process is called, usually occurs at the end of a month, quarter or year.
- *Reporting:* Companies must report regularly on financial performance, whether to an executive director, a board of directors, investors, shareholders or government regulators. The financial team is responsible for the clarity and accuracy of these reports.
- *Scenario modeling, planning, and budgeting: S*cenario modeling begins with making certain assumptions about a future period, for example, "In the next quarter, we expect to achieve revenues of between $10 and $15 million." The financial team will run several hypothetical best and worst case scenarios, estimating the amount of money the company will hold if those conditions become reality. Based on these models, the finance team will assess how best to respond and develop plans, forecasts and budgets. Often, the finance team will collaborate with other departments—such as sales, HR, project management, or procurement teams—to create models that include data from sales estimates, labor expenses, and inventory costs. This process is known as connected planning.

- *Payroll and Expenses:* Verification of individual payments to employees is usually the responsibility of the HR department. However, overall labor costs are transferred to the finance team so that they can take them into account when creating budgets and plans. Finance is also responsible for reimbursing employees for expenses such as work-related travel and meals.
- *Cash management and forecasting:* With money constantly flowing in and out of the company, it's important for finance teams to look ahead. They need to ensure that the company has enough cash to stay solvent for the next quarter, year – maybe even the next three to five. In most companies, cash forecasting is usually done once a month.
- *Tax strategies:* Every company has to file tax returns. And like anyone, they want to take advantage of as many deductions as possible to prevent paying extra. Some finance teams employ tax specialists to handle this. Companies that do not frequently perform these tax activities outsource them to an accounting firm.
- *Risks and compliance.* Every company has financial risks, from rising interest rates to global pandemics. The finance team is tasked with controlling such risks and reducing the company's exposure to them as much as possible. They must also ensure that the rules and regulations set by governments, regulatory authorities and other legal bodies are followed within the company to maintain compliance and avoid substantial fines.

Why is financial management important?

Financial management is important because it ensures the solvency of the company. Its basic purpose is to ensure that the business does not go bankrupt. Financial management addresses the most important issues a company may face, such as loss of revenue (as happened during the COVID-19 pandemic) or in the event of natural disasters, strikes, wars, etc.

Beyond basic profitability, financial management supported by appropriate software can help a company grow and prosper. Financial teams can use many tools within the company to drive development. In good market conditions, with a growing economy and low interest rates, finance teams can borrow money from banks, raise funds from investors, or list the company on the stock exchange (sell shares on the stock market). The company can invest these funds in development by opening new branches, expanding to other territories, modernizing equipment, etc. When market conditions are less favorable—for example, during a recession—financial management tactics might include cutting costs by laying off employees or closing unprofitable locations.

Improving profitability is an important component of financial management. Finance teams often work with sales and marketing teams to set prices for the company's products or services. They have to strike a balance to set the right prices. If prices are too high, customers may turn to competitors who sell cheaper. If they are too small, the company may not generate enough revenue to cover expenses. In the same way, cost control is also one of the important responsibilities of the financial team, regardless of whether it is employees, rents, electricity, raw materials or transportation expenses.

Reporting is an essential component of effective financial management. CFOs and other business leaders want to know how well the company is performing in order to make the best decisions about its profitability. They want to know that the business is performing as planned and that it is delivering the appropriate return for the company's investors. Effective financial management matters because it helps a company achieve or even exceed its goals.

Objectives of financial management in business

Financial teams have many objectives related to financial management. Their main objectives include:

1. Ensuring the solvency of the company by avoiding bankruptcy and producing the money needed to carry out the activity.
2. Maximizing profitability by setting the right price for existing products and services, discarding unprofitable products and services, and evaluating the potential profit of new products and services.
3. Minimizing costs by monitoring expenses and looking for new ways to reduce indirect costs.
4. Ensuring a good return on investment (ROI) for investors, shareholders and other stakeholders.
5. Capital growth by attracting more investment driven by a positive ROI.
6. Estimating cash to ensure the organization has enough cash – not just to operate, but to invest in development.
7. Reducing risks and avoiding fines by ensuring companies' compliance with the respective regulations. Increasingly, this also includes environmental, social and corporate governance planning and reporting.

Functions of financial management

1. *The function of forecasting* - represents the set of actions undertaken by the company's managers and their collaborators in order to establish the strategic and tactical objectives of the company, as well as the financial and other resources necessary to achieve them. In other words, through the materialization of the forecasting function, the company's future activities (for a given time horizon), the conditions under which they can be realized and the expected results are established.

2. *Financial organization* - within this function are included the activities necessary to fulfill the company's financial objectives, placing them, as tasks, on employees and organizational structures and determining all of them in a precisely outlined framework for making and following up decisions.

3. *Financial coordination* - includes the activities that harmonize the decisions and actions of the company's personnel and its subsystems within the adopted strategies, tactical procedures and organizational system. Viewed in evolution, coordination is basically, as most specialists say, the dynamic organization of the company.

4. *Training for the achievement of the company's financial objectives* - refers to the activities through which the company's personnel are determined to achieve the set objectives, under the established efficiency conditions. The essence, the engine of the training actions is the motivation of the staff, that is, the harmonious interweaving of the company's interests with those of the staff (understood in a broad sense: employees, shareholders, etc.).

- 5. *The control and evaluation of the achievement of the set objectives and financial performances* – the control and evaluation close a cycle of the managerial process and prepare the foundation and start of the next cycle. By performing this function, the finality of the way to achieve the other attributes of the managerial act (forecasting, organization, coordination and training) is quantified, and by comparing the results obtained with the predetermined parameters, the deviations are quantified and the causes that determined them, strengths and weaknesses of the company, as well as the measures that are required to correct things, prevent the repetition of negative phenomena and to stimulate the expansion of the area of manifestation of the effects of the positive phenomena that have appeared. Also, through the tools of this function, the evaluation of the company as a whole and on patrimonial elements is carried out.

Key Findings

- Financial management means monitoring, controlling, protecting and reporting a company's financial resources.
- Companies have accountants or finance teams responsible for managing their finances, including all banking transactions, loans, debts, investments and other sources of finance.
- Financial teams must also ensure that all legal regulations are met within the company, that it is solvent and as profitable as possible.

At the end of the paper I left some defining questions in understanding the concept of financial management, accompanied by concise answers.

1. What does financial management mean?

R: Financial management refers to the management of a company's finances, including all money coming in and out of the company, cash or all reserve assets.

2. What is the role of financial management?

R: The essential role of financial management is to ensure the solvency of the company. In addition to this, proper financial management can help a company grow and prosper.

3. What would be an example of financial management?

R: An example of financial management is when a financial management team determines the amount of money a company should borrow to invest in a new plant, product line, or service offering.

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