Corporate Finance and Financial Governance in the European Union

Challenges and Opportunities

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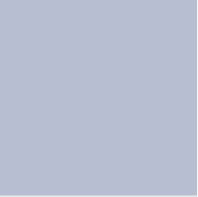
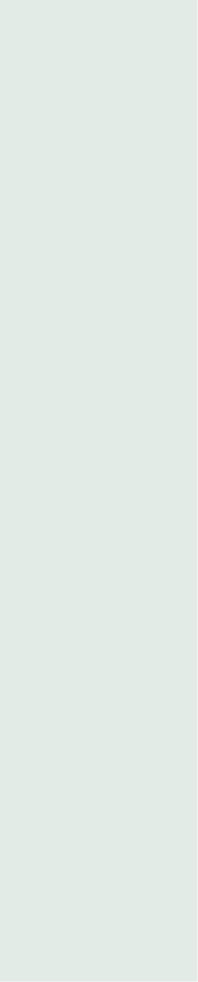

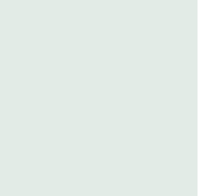

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Aleš Trunk

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Chapter One

Introduction to Corporate Finance and Financial Management in the European Union

Corporate finance and financial management are critical factors for the success of companies in the European Union (EU). We will introduce the basic concepts and methods for effectively managing the financial resources of companies in the EU. We aim to provide an understanding of the basic principles of corporate finance and how they are applied to strategic decision-making and achieving corporate objectives. We will then discuss basic concepts, financial planning, financial statement analysis, capital structure, valuation of businesses and investments, equity and debt financing, cash flow management, risk and return, and the role of EU regulations and policies in financial management.

Basic Concepts of Business Financing

First, we will introduce basic concepts such as financial planning, financial statement analysis, capital structure, business and investment valuation, equity and debt financing, and cash flow management. We will understand how these principles play a crucial role in ensuring the financial stability and growth of companies in the European Union.

Financial Planning

Financial planning is how companies define their financial needs, objectives and strategies. It involves assessing the business's current financial position, preparing budgets, forecasting future cash flows and determining the financial resources needed to achieve the objectives. Financial planning ensures companies have sufficient resources to finance their activities, growth, and development (Melicher & Norton, 2013). Financial planning is a process that helps companies and individuals define their financial goals and develop strategies to achieve them. This includes assessing the current financial situation, preparing a budget, identifying future income and expenditure, identifying investment

TABLE 1.1 Financial Planning

Setting financial targets	Companies must set clear and measurable financial targets that align with their business strategies and long-term plans. These objectives may include increasing revenues, reducing costs, improving return on investment, reducing debt, or increasing the business's market value.
Assessment of the current financial situation	Financial planning starts with assessing the company's current financial position, including an analysis of its financial statements, such as the balance sheet, income statement and cash flow statement.
Preparing the budget	A budget is a tool that helps companies plan their future income and expenditures and monitor their financial progress. It must be realistic and based on reliable data, considering all possible factors that may affect the company's financial performance.
Identifying investment needs	Based on their financial targets and current financial position, companies must determine how much they must invest in ongoing operations, growth, new product or service development, research and development, marketing and other strategic initiatives.
Risk analysis and preparation of risk management plans	Businesses face various financial risks, such as market, credit, liquidity, and operational risks. Financial planning involves analysing these risks and developing appropriate strategies to manage them, such as diversification of investments, insurance, hedging and building up adequate financial reserves.
Determining the optimal capital structure	Businesses need to implement the right mix of equity and debt to ensure financial stability, lower funding costs, and enable them to meet their growth and profitability targets. The optimal capital structure depends on company size, industry, market conditions, and business strategy.
Assessment of investment opportunities	Financial planning involves assessing the different investment opportunities available to the company and comparing them with the risks and expected returns. This may include analysing financial indicators such as the internal rate of return (IRR), net present value (NPV), and return on invested capital (ROIC).
Monitoring and adjusting financial plans	Financial planning is a dynamic process that requires regular monitoring and adjustment of plans in response to changes in the business environment, market conditions or internal company factors. Companies should regularly review and adjust their financial plans to stay on track and achieve their financial objectives.

needs and risk analysis, and developing risk management plans. In a business context, financial planning helps companies to achieve a wide range of objectives (table 1.1).

All of these activities are key to successful financial planning and cor-

porate governance. A well-designed financial plan allows a company to focus on its key business objectives, optimise its financial resources, reduce risks and maximise returns for owners and investors. Financial planning is also essential for managing a company's cash flow, liquidity, and debt and maintaining long-term financial stability and growth.

Analysis of the Financial Statements

Financial statement analysis examines a company's financial statements to assess its financial performance, stability and profitability. This includes an analysis of the balance sheet, income statement, cash flow statement and statement of changes in equity. Important ratios used in financial statement analysis include return on equity, liquidity, leverage, operating efficiency and return on investment. Financial statement analysis allows companies and stakeholders such as investors, creditors and regulators to assess a company's financial health and performance and monitor its progress (Gowthorpe, 2021).

Financial statement analysis is the process of reviewing and evaluating the financial information that an entity presents in its financial statements. This analysis assesses an entity's financial position, performance, and stability and gives insight into its financial prospects and risks. Financial statement analysis typically uses various tools and techniques to compare a company with competitors, industries, and periods.

The main financial statements to be analysed are:

1. *Balance sheet* shows an enterprise's financial position at a given date. It lists its assets, liabilities, and owner's equity, allowing an assessment of its liquidity, indebtedness, and financial stability.
2. *Income statement* shows an enterprise's income and expenditures over a given period, allowing an assessment of its profitability and performance.
3. *Cash flow statement* shows an entity's cash inflows and outflows over a specified period. It estimates cash flow from operating, investing, and financing activities and provides insight into the entity's liquidity and solvency.

Some of the main methods of analysing financial statements include three primary analyses (Fridson & Alvarez, 2022):

1. *Vertical analysis* compares items in the same financial statement.

For example, in the income statement, each expense item may be compared to revenue to determine the proportion of expense to revenue.

2. *Horizontal analysis* compares a company's financial data over several periods, assessing trends and changes in the company's financial performance.
3. *Indicator analysis* involves calculating financial ratios that assess a company's liquidity, indebtedness, profitability, efficiency, and market value. These indicators can be compared with competitors, industries, or periods to determine the company's relative performance.

Analysis of financial statements is crucial for all stakeholders, including owners, investors, managers, employees, suppliers, customers and regulators, as it enables them to understand better a company's financial performance, risks and opportunities. This analysis can lead to strategic decisions such as investments, new product development, expansion into new markets, cost reductions, debt refinancing, dividend payments or other actions that can affect the financial performance and value of the business.

To analyse the financial statements effectively, it is essential to consider the following factors:

1. *Context.* Financial statements should be analysed in the context of the industry, market conditions, and the company's business strategy. This allows a better understanding of the factors influencing a company's financial performance and the differences between companies in the same sector or geographical area.
2. *Information quality.* The analysis of the financial statements is based on the reliability and accuracy of the financial information presented in the company's accounts. Therefore, it is essential to check the quality of the financial information and consider any limitations or biases in its compilation.
3. *Comparability over time.* Financial statements must be analysed and compared to assess a company's financial performance trends and dynamics. This requires using uniform accounting policies and standards and adjusting financial data for the impact of extraordinary events such as mergers, auctions, reorganisations, or changes in accounting standards.

4. *Relative comparison.* The analysis of the financial statements must include comparing the entity with competitors, industries, or market benchmarks to assess its relative performance and competitive position. This requires using comparable financial indicators that allow comparisons between companies and sectors, regardless of their size, geographical location, or business model.

By analysing financial statements, companies and stakeholders can make better and more informed decisions, optimise their financial resources, reduce risks and improve their long-term competitiveness and performance. This analysis also allows companies to monitor their progress towards strategic and financial objectives and to adapt their business and financial strategies to changing market conditions, competitive pressures, technological developments, regulatory frameworks and other factors that may affect their performance and risks.

In addition, financial statement analysis plays a vital role in a company's external communication with investors, lenders, credit rating agencies, regulators and other stakeholders by providing transparency, reliability and comparability of the financial information needed to assess a company's creditworthiness, profitability and risk.

In practice, the analysis of financial statements can be carried out in different ways.

1. *Internal analysis.* Companies can internalise their financial statements through accounting, finance, and management teams. These teams can use various tools and methodologies to assess financial results, trends, and risks and produce internal reports and recommendations to improve business and financial strategies.
2. *External analysis.* External analysts, including investors, lenders, credit rating agencies, regulators, the media and other stakeholders, may carry out an independent analysis of a company's financial statements to obtain their insights, assessments and recommendations on its financial performance, risks and prospects. This external analysis may influence market assessments, credit ratings, investment decisions, regulatory actions and other factors that may affect the company's value, reputation and competitive position.
3. *Professional services.* Companies may hire external professionals such as financial advisors, auditors, business analysts or in-

vestment banks to provide specialised financial statement analysis, valuations, due diligence reviews, prospectus preparation or other documents and services needed to support strategic decisions, transactions, reorganisations, refinancing or other financial needs of the company. Financial advisors, auditors, business analysts or investment banks may provide specialised financial statement analysis, valuations, due diligence reviews, prospectus preparation or other documents and services needed to support the company's strategic decisions, transactions, reorganisations, refinancing, or other financial needs. These professionals may use advanced methods, models and tools to evaluate financial information, market parameters, competitive comparisons and other factors that may affect a company's financial performance and risks.

4. *Use of technology.* Modern technology enables the automation and improvement of financial statement analysis through the use of computer programs, algorithms, artificial intelligence, machine learning and other digital tools that can collect, process, analyse and present large volumes of financial data, market information, benchmarks and other relevant sources in a real-time, interactive and visual format. This technological support can improve the speed, accuracy, flexibility and efficiency of financial statement analysis and support better and more informed decisions based on credible, relevant and up-to-date financial information.

Financial statement analysis is essential for a company's successful management and optimising its financial position, profitability, and risks. By analysing financial statements, companies can monitor their progress, adjust their business and financial strategies, improve their competitiveness and value, and build trust and credibility with their stakeholders. Therefore, companies must understand, use and improve their financial statement analysis capabilities and invest in the necessary resources, experts and technologies to make better and more informed financial decisions.

Capital Structure

Capital structure refers to how an enterprise finances its assets and investments, particularly the equity-to-debt ratio. Companies must balance their capital structure to minimise financing costs and risks and

optimise returns to equity holders. A company's capital structure can affect its financial stability, growth, and valuation, so companies must be aware of their capital structure and adapt it to their needs and market conditions (Sari & Sedana, 2020).

The capital structure is how a company is financed, involving a combination of debt (loans and bonds) and equity (shares). The debt-equity ratio is vital in determining a company's risk and profitability.

Companies with a higher debt ratio tend to have a higher financial risk, as they have to pay interest and debt principal no matter how good or bad they are. On the other hand, if the business performs well, the use of debt increases the potential returns to owners, as more profits are left for the owners of the capital.

Companies with a higher equity share tend to have lower financial risk, as debt obligations do not burden them. However, the potential returns to shareholders may be reduced if the company does not take advantage of the opportunity to increase returns through debt.

The optimal capital structure depends on several factors, including the industry in which the firm operates, its age and growth, cash flows, and strategic objectives (Brusov & Filatova, 2023).

Valuation of Enterprises and Investments

Business and investment valuation is the process of estimating the value of a business or investment based on its financial data, market factors and expected future cash flows. Valuation is crucial for investors who want to assess whether a company or investment is attractive and fairly valued. There are several valuation methods, the most well-known of which are discounted cash flow (DCF), market value multiples and the net present value method.

Business and investment appraisal is critical in deciding on investments and strategic steps for a company. It involves assessing a business or investment's economic and financial aspects to determine its current and future value.

There are different methods of valuing companies and investments (Fernández, 2019):

1. *Discounted cash flow method (DCF).* This method is based on an estimate of the future cash flows to be generated by an entity or an investment and then discounts these flows to present value at a rate that reflects the risk of the investment.

2. *Benchmarking.* This method involves comparing a company or investment with similar ones. It may include multiples such as P/E (price to earnings), EV/EBITDA (enterprise value to EBITDA), etc.
3. *Asset valuation.* This valuation method estimates the value of the enterprise's net assets. It can be helpful for companies with many physical assets, such as real estate or production equipment.
4. *Return on equity (ROE) method.* This method evaluates a company based on the return it generates on its equity. A higher return on investment means greater efficiency in using equity capital.

When choosing a valuation method, it is essential to consider each company or investment's specific characteristics, such as industry, growth rate, asset type, and other factors. It is also helpful to use several methods and compare the results to get a more complete picture of the company or investment's value.

Equity and Debt Financing

Businesses can be financed by equity capital, which involves issuing shares and raising capital from owners, or by debt capital, which involves borrowing from creditors such as banks, bonds or other forms of loans. Equity financing allows companies to raise capital without repayment obligations but reduces ownership and potential profits among many shareholders. Debt financing increases the company's leverage, potentially increasing shareholder profitability, but increases the risk and the company's liabilities to creditors.

Equity financing is a form of capital raising in which an entity issues shares and offers them to public or institutional investors. A share represents an ownership interest in a company, which means that the shareholder becomes a shareholder and, thus, the company owner. Shareholders have the right to profit-sharing (in the form of dividends) and voting rights at company general meetings where important decisions are made. Share financing allows a company to raise capital without debt obligations, but means that the company shares its ownership structure and management with other investors.

Debt financing, on the other hand, refers to raising funds by borrowing or issuing bonds. In debt financing, a company borrows money from lenders or investors and commits to repay the borrowed asset plus interest over a specified period. The lenders or bondholders do not have an ownership interest in the company but are entitled to interest and

repayment of the principal. Debt financing is often linked to fixed interest rates, repayment terms and collateral. The company retains its ownership structure with debt financing but must make regular interest payments and repay the principal.

Businesses typically use a combination of equity and debt financing to raise the capital they need to carry out their activities. The decision between equity and debt financing depends on various factors, including the company's ability to repay the debt, the cost of raising the capital, the risks assumed by the company, and the objectives of the company's owners.

Cash Flow Management

Cash flow management is the process of monitoring, analysing, and adjusting a company's income and expenditures to ensure optimal liquidity and financial stability. Effective cash flow management involves optimising revenue collection, managing inventories, deferring expenses, and finding favourable financing terms. Cash flow is crucial to a company's financial health, ensuring it has sufficient cash to fund its current and long-term obligations.

Cash flow management, often called liquidity management, is how an entity manages its cash flows, income, and expenses to ensure that it has sufficient liquid funds to operate smoothly. It is crucial to a company's long-term financial health as it helps to prevent liquidity problems, shortages of funds, and unnecessary costs due to inadequate cash flow management. Some critical aspects of cash flow management are presented in table 1.2.

Cash flow management is crucial to a company's financial stability and performance. Effective liquidity management enables a company

TABLE 1.2 Critical Aspects of Cash Flow Management

Cash flow forecasting	An entity must monitor and forecast future cash flows based on expected income and expenditure. This allows better preparation for potential liquidity shortfalls or surpluses and enables timely action to maintain balance.
Revenue management	Effective cash flow management involves monitoring and managing a company's income. This includes proper invoicing, monitoring customer payment terms and taking measures to minimise defaults and debt collection.

Continued on the next page

TABLE 1.2 *Continued from the previous page*

Expenditure management	A company must pay attention to its costs and manage them in a way that is consistent with its financial capacity. This includes controlling costs, optimising processes, negotiating more favourable terms with suppliers and managing inventories rationally.
Short-term financing	In the event of a liquidity shortage, the company can use various sources of short-term funding, such as bank loans, bridge loans or factoring, to ensure sufficient liquidity to keep operations running smoothly.
Investment management	Cash flow management also includes efficiently managing the company's investments. This means selecting appropriate short-and long-term investments with adequate returns and liquidity.
Adapting to business cycles	The company considers business cycles and seasonal fluctuations in income and expenditure. This allows for adequate liquidity planning during periods of increased or reduced activity and for measures to rebalance cash flows.
Increasing the efficiency of payments	Cash flow management also involves optimising payment processes. This means shortening customer payment terms, improving supplier payment processes, and taking advantage of benefits such as early payment discounts.
Increasing liquidity	A company can take steps to increase its liquidity, such as selling redundant assets or using short-term investments with high liquidity. It can also improve its business processes to reduce the time between expenditures and payment receipts.
Monitoring and reporting	It is essential to monitor and report the company's cash flow regularly. This allows for early identification of potential problems and timely adjustment of cash flow management strategies.

NOTES Adapted from Robinson and Sensoy (2016).

to meet its obligations, operate without interruption, and take advantage of opportunities for growth and development.

Risk and Return

Risk and return are two fundamental concepts of business financing that relate to the probability of failure and success of an investment or business decision. Risk relates to the uncertainty of future events and their impact on an enterprise's financial performance. Return represents the financial reward that an entity or investor receives for taking a risk. Companies must carefully assess the risks and expected returns of their business decisions to optimise their investments and achieve long-term objectives.

Risk and return are two critical concepts in finance and investment.

The two are inextricably linked and vital to consider when making investment decisions.

The return is the profit or loss you make on an investment. It is usually expressed as a percentage of the initial investment. For example, if you invest €1000 in a share and its value increases to €1100, your return is 10%.

Risk refers to the possibility that actual returns may differ from expected returns. For example, if you invest in a share, there is a chance that its value will fall, and you will lose some or all of your investment. The higher the risk, the higher the probability of such fluctuations.

In finance, the general rule is that risk and return are linked. Higher potential returns usually mean higher risk. For example, investing in equities usually yields higher potential returns than investing in safe government bonds, but the risk is also higher.

Investors should consider risk tolerance when deciding on their investments. Some are more risk-averse and willing to accept more risk for potentially higher returns, while others are more conservative and prefer lower-risk investments.

In addition, it is essential to understand that there are different types of risks, including market risk (the risk that market prices will change), credit risk (the risk that the debtor will not be able to pay) and operational risk (the risk arising from the day-to-day running of the business). Understanding and managing these risks is critical to a successful investment.

EU Rules and Policies on Financial Management

The European Union plays a crucial role in shaping the regulatory framework and policies affecting corporate financial governance in the region. These policies and regulations relate to banking, securities, insurance, accounting, taxation, and competition. They aim to ensure financial markets' stability, integrity, and efficiency and promote fair and transparent business conduct.

The European Union (EU) has a range of financial governance rules and policies to ensure the financial system's stability and integrity and protect consumers' interests. Some of the key regulations and policies in this regard include:

1. *European Banking Union (EBU)* was set up to strengthen the banking sector's stability in the EU. It involves the supervision and reg-

ulation of the banking sector by the European Central Bank (ECB) and the creation of a Single Resolution Mechanism (SRM) to deal effectively with potential crises in the banking sector.

2. *Financial Instruments Regulation (MiFIR) and Markets in Financial Instruments Regulation (MiFID II)* are essential regulations governing the trading of financial instruments in the EU. They lay down rules on the functioning of financial markets, transparency of trading, reporting obligations and investor protection.
3. *CRA Regulation (CRA III)* supervises credit rating agencies that assess the credit risk of bond and other financial instrument issuers. It sets out transparency, interest management, and accountability requirements for credit rating agencies.
4. *Insurance Regulation (Solvency II)* concerns insurance companies and sets the framework for their capital adequacy, risk management, reporting, and supervision. It aims to ensure the stability and safety of the insurance sector.
5. *Payment Services Directive (PSD2)* is a vital directive regulating payment services in the EU. It brings more competition, innovation and payment security and opens banking data to third-party service providers through open-access interfaces.
6. *General Data Protection Regulation (GDPR)* does not explicitly address financial governance, however, it significantly impacts personal data protection in the financial sector. It sets out the EU's rules for collecting, processing and protecting personal data.

In addition, the EU is adopting policies that promote sustainable finance, such as the Sustainable Finance Act, the European Green Deal, and the Sustainable Finance Action Plan. These policies encourage investment in projects and businesses that contribute to reducing environmental impact, promoting clean energy, and using sustainable resources. At the same time, the European Central Bank (ECB) implements monetary policy, which influences financial governance in the EU. The ECB monitors price stability, manages monetary policy and monitors systemic risks in the banking sector.

In financial governance, the EU works with international organisations such as the International Monetary Fund (IMF), the G20 and the Basel Committee on Banking Supervision to harmonise regulations and policies globally (Viterbo, 2019).

All these rules and policies aim to ensure the financial system's stability, protect investors, and promote innovation and sustainable development in the financial sector. They also ensure uniform rules and standardisation across the EU, contributing to greater transparency and confidence in financial markets.

Banking and Financial Stability

The European Central Bank (ECB) and the national central banks of the EU Member States are responsible for formulating and implementing monetary policy, supervising the banking sector and maintaining financial stability (Micossi, 2015). The ECB monitors and regulates banking institutions to ensure their solvency, liquidity and compliance with legislation. It also implements measures to prevent financial crises and support economic growth.

Banking is crucial to ensuring economic and financial stability. It is a financial institution that accepts deposits from individuals and businesses and provides loans to those needing finance. Banks also play a crucial role in financial intermediation, converting savings into productive investments.

Financial stability refers to how the financial system – including banks, stock exchanges and financial markets – can channel funds efficiently from savers to those needing financing, even in economic difficulty.

Banking is crucial for financial stability for several reasons:

1. *Risk management.* Banks use different methods to assess and manage the risks associated with lending. This helps to ensure that borrowers can repay their loans, thereby reducing the risk to the financial system.
2. *Liquidity.* Banks provide liquidity by allowing depositors to withdraw their funds anytime. This helps maintain confidence in the financial system and prevents panics that could lead to a banking crisis.
3. *Monetary policy.* Central banks use banking to conduct monetary policy. Changing interest rates or reserve requirements can influence the amount of credit they lend, affecting overall economic activity.

However, banking can also pose risks to financial stability. For ex-

ample, if banks provide too much credit without proper risk assessment, this could lead to over-indebtedness and a potential financial crisis. Therefore, banks must act responsibly and be supervised by the appropriate regulators to ensure their stability and the financial system's health.

Securities and Capital Markets

The European Union regulates securities trading and the functioning of capital markets through directives and regulations such as the Markets in Financial Instruments Directive (MiFID II) and the Markets in Securities Regulation (MiFIR). These rules and policies ensure that securities trading is carried out transparently, fairly, and efficiently. They also protect investors' interests and reduce the risk of market abuse.

Securities and capital markets are critical financial system elements, enabling the trading of financial instruments such as shares, bonds, and derivatives. These instruments allow companies and other entities to raise finance and investors to invest and generate returns. The following is some background information on securities and capital markets (Christensen et al., 2016).

1. *Securities* are documents or electronic records representing an ownership or debt interest in a company or other organisation. The most common types of securities are shares and bonds. A share represents an ownership interest in a company, which means that the holder becomes a shareholder and has certain rights, such as participation in profits and voting at general meetings. A bond is a debt security where the issuer owes a certain amount of money to the bondholder plus interest.
2. *Capital markets* are financial markets where supply and demand for securities meet. These markets enable companies and other organisations to raise capital by issuing new securities and allow investors to trade in these securities. In capital markets, the prices of securities are based on supply and demand and other factors such as corporate profitability, macroeconomic indicators and investor expectations.
3. *Primary and secondary markets.* New securities are issued in the primary market. This means that a company is offering shares or bonds to investors for the first time. In the primary market, investors buy securities directly from issuers. On the other hand,

there is a secondary market where securities are traded between investors without the direct involvement of the issuer. In the secondary market, prices are formed based on supply and demand among investors.

4. *Stock exchanges* are regulated markets where securities are officially traded. Securities are bought and sold on stock exchanges through intermediaries. Exchanges provide an organised and regulated framework for trading securities, allowing for transparency, liquidity and market efficiency. Europe's most well-known stock exchanges are the London Stock Exchange, Euronext, Deutsche Börse, Borsa Italiana and Nasdaq Nordic.
5. *Capital markets are regulated and supervised* to ensure the market's fairness, integrity and stability. In the European Union, MiFID II (MiFID II) and MAR (Market Abuse Regulation) are designed to ensure transparency and investor protection and prevent abuse in capital markets. Regulatory authorities such as ESMA supervise and enforce these regulations at the EU level.
6. *The impact of capital markets.* Capital markets play an essential role in stimulating economic growth and development. They provide companies with access to capital for expansion and investment, stimulating innovation, job creation and economic activity. At the same time, they allow investors to invest their funds and generate returns. Capital markets contribute to the efficient transfer of capital from savers to investors and allow market risk and liquidity diversification.

Securities and capital markets are a complex and vital financial system. They enable the transfer of assets and the creation of investment opportunities. Their functioning is subject to regulation and supervision to ensure market fairness, transparency, and stability.

Insurance and Risk Management

The insurance sector in the EU is regulated by the Insurance Directive (Solvency II), which sets out requirements for capital, risk management and insurance supervision. This Directive aims to ensure the financial stability of the insurance sector, protect policyholders and promote competition in the market.

Insurance is an activity that involves the transfer of risks from individuals or companies to insurance companies. Insurance companies

collect premiums from policyholders and undertake to pay an agreed compensation or indemnity in the event of a loss. This allows policyholders to protect themselves against financial losses related to risks such as accidents, illness, natural disasters, or property losses.

Risk management is a vital part of the insurance industry. It involves identifying, assessing and managing the risks individuals and businesses face. Risks must be appropriately identified and assessed, and action must be taken to manage them.

The following are some key aspects of insurance and risk management (Hopkin, 2018):

1. *Identifying risks.* The first step is identifying the risks individuals or companies face. This involves identifying the risks that could lead to financial loss or damage and determining their likelihood and potential consequences.
2. *Risk assessment* uses various methods to determine the likelihood and impact of risks. These include quantitative and qualitative analysis, statistical models, expert judgment, and the use of data and information.
3. *Risk management* involves taking action to manage risks. This includes transferring risks to insurers by entering into insurance contracts, mitigating risk (e.g., precautionary measures, reducing risk exposure), transferring risks to other parties (e.g., liability contracts), and making risk management decisions.
4. *Insurance contracts.* The conclusion of an insurance contract is a critical component of risk management. An insurance contract defines insurers' and policyholders' coverage, terms, conditions, premiums, and obligations. Policyholders pay premiums to the insurer in return for a promise that the insurer will pay compensation or indemnity in case of a claim.
5. *Diversification of risks.* Diversification is essential in risk management. It reduces the concentration of risks and expands sources of wealth. For example, investors can diversify their portfolios by investing in different types of investments and different sectors. By diversifying their activities and locations, companies can reduce their risk exposure.
6. *Stress tests* are procedures used to assess the resilience of individuals or companies to unusual or extreme events. They include

simulating scenarios such as financial crises, natural disasters, or changes in the economic environment to assess how well individuals or companies respond to such events.

7. *Risk management in insurance undertakings.* Insurance undertakings also have internal risk management procedures. These include identifying, assessing and managing the risks they assume by issuing insurance contracts. Insurance undertakings carry out risk analyses, set premiums, establish indemnity provisions, and use other financial instruments to manage risks.

Risk management and insurance are closely linked, as insurance companies provide risk transfer and management for individuals and businesses. Risk management is essential for safe and sustainable operations, ensuring financial stability, and protecting against unforeseeable events and losses.

Accounting and Financial Reporting

EU companies must follow International Accounting Standards (IAS), which set out the principles and practices for preparing and presenting financial statements. These standards facilitate comparability and transparency of financial information and ensure that investors, creditors, regulators and other stakeholders receive accurate and relevant information about companies' financial position and performance.

Accounting and financial reporting are crucial elements of any company's management. Accounting is the process of recording, classifying, summarising, analysing, and reporting an enterprise's financial transactions. Accounting information is essential for understanding the business's current state, planning future activities, and making strategic decisions.

Financial reporting communicates this information to stakeholders, including investors, lenders, boards and regulators. Financial reports such as the balance sheet, income statement, cash flow statement and statement of changes in equity provide an overview of a company's financial position and performance.

Accounting and financial reporting are subject to various rules and standards, including International Financial Reporting Standards (IFRS) and the Accounting Act. These standards ensure that companies' financial information is presented in a standardised and fair way that allows comparison between companies.

Taxation

The EU is committed to harmonising business and personal taxation and preventing tax competition and avoidance. It is working with Member States to develop standard rules and policies on taxation, such as the Common Consolidated Corporate Tax System (CCCTB) Directive and the Savings Tax Directive. These policies ensure fair and efficient taxation and promote economic growth and competitiveness.

Taxation is an essential aspect of financing public spending and the functioning of government. Countries use taxation to raise funds to finance public services, infrastructure, social security and other needs of society. Taxation affects the economy, public finances and the behaviour of individuals and businesses. Let us look at some key aspects of taxation (Olbert & Spengel, 2017):

1. *Types of taxes.* Several types apply at different levels, such as national, regional, and local. The most common types of taxes are income taxes (taxes on personal income), corporate taxes, value-added taxes (VAT), excise duties, property levies, and other taxes.
2. *Fairness and progressivity.* Taxation is often based on the principle of fairness, whereby individuals and companies are taxed according to their ability to pay. The concept of progressivity means that higher incomes are taxed at higher rates, leading to a higher burden on those with higher incomes. This approach aims to reduce inequalities and ensure social justice.
3. *Tax breaks and exemptions.* Countries usually provide tax breaks and exemptions to encourage certain activities or investments. This can include incentives for research and development, investment in green technologies, incentives for small businesses and other measures to promote economic growth and development.
4. *Tax system and administration.* The tax system includes laws, regulations, and procedures for collecting taxes. Efficient administration is critical to ensuring its fairness and effectiveness. This includes tax collection, transparency, enforcement of tax rules, prevention of tax evasion, and the fight against tax fraud.
5. *The impact of taxation on the economy.* Taxation significantly impacts economic activity and the behaviour of individuals and businesses. Higher tax rates can reduce incentives to work, save and invest. They can also affect the competitiveness of firms and at-

tract foreign investment. Some tax measures can encourage or discourage economic activity and behaviour, such as tax breaks for research and development, while high tax rates on profits can reduce incentives for entrepreneurship.

6. *International taxation.* Taxation also has an international dimension, with companies and individuals facing taxation challenges in several countries. International tax treaties and bilateral double taxation agreements help to prevent tax duplication and promote international trade and investment.
7. *Taxation and public finances.* Taxes are an essential source of revenue for a country and help finance public spending on things like education, health, infrastructure, and social services. Proper tax planning and management are crucial to ensuring the stability of public finances and adequate financing of public needs.

Taxation is essential in managing public finances, stimulating economic growth, and fairly sharing the burden between individuals and businesses. The proper design and administration of the tax system are vital to ensuring efficient tax collection, stimulating economic activity, and ensuring societal fairness.

Competitiveness and State Aid

The EU monitors competition between companies and state aid to ensure a level playing field and prevent unfair competition. The European Commission monitors and regulates market practices such as agreements between undertakings, abuse of dominant positions and concentration of undertakings. It also monitors and regulates state aid granted by Member States to undertakings to avoid distortions of competition and adverse effects on the common market.

Competitiveness and State aid are essential aspects of the European economy and the European Union (EU) legal framework. Competitiveness refers to the ability of companies and economies to compete in the market, innovate and achieve efficiency gains. On the other hand, state aid refers to financial or other support governments provide to companies or sectors, which can affect competitiveness and distort the EU internal market.

The European Commission is responsible for monitoring competition in the EU and adopting rules on state aid. The main objective of these rules is to ensure fair competition between companies and Mem-

ber States and to prevent market abuses and distortions. Some key aspects of competition and state aid are (Jones & Sufrin, 2016):

1. *Competition rules.* The EU competition rules are laid down in the EU Treaties and the Competition Regulation. These rules prohibit agreements that restrict competition, abuses of dominant positions, and concentrations that may jeopardise competition in the internal market. They also support the promotion of innovation, efficiency, and consumer protection.
2. *State aid.* EU state aid rules determine when and under what conditions state aid is allowed. State aid may be granted to promote regional development, research and development, environmental protection, crisis management, or other public interest objectives. However, under EU rules, state aid must be proportionate and transparent and not distort internal market competition.
3. *Monitoring and decision-making.* The European Commission is responsible for monitoring and decision-making on competition and state aid. Generally, companies seeking state aid must register with the Commission, which assesses compliance with EU rules. The Commission can also recover unlawfully granted state aid and impose penalties for breaches of competition rules.
4. *Competitiveness and economic development.* Competitiveness is critical to the EU's economic development. Fostering competition boosts innovation, productivity and job creation. Competitiveness also promotes resource efficiency and improves the quality of products and services for the benefit of consumers. A healthy competitive framework encourages companies to continuously improve and adapt, leading to economic innovation and progress.
5. *State aid control.* EU state aid rules are essential in maintaining a level playing field for EU businesses. This prevents market distortions caused by the unfair advantages that state aid can bring. Strict rules and controls on state aid help to ensure a fair, competitive environment for all companies in the internal market.
6. *Regional development.* Competitiveness and state aid play essential roles in promoting regional development in the EU. Member States can use state aid to promote economic development in less developed regions and reduce regional disparities. This can include investment subsidies, tax breaks, regional funds, and other

incentives to attract investment in regions with lower economic activity.

EU competition and state aid rules play a crucial role in ensuring the fair and efficient functioning of the internal market. This promotes innovation, growth, and business development and protects consumers' interests. An appropriate balance between competitiveness and using State aid is essential for a sustainable and competitive European economy.

Corporate finance and financial management are critical factors for the success of businesses in the European Union. Understanding basic concepts such as financial planning, financial statement analysis, capital structure, business and investment valuation, equity and debt financing, cash flow management, risk and return, and the role of EU regulations and policies in financial management is essential for the effective management of EU companies' financial resources.

These concepts and methods will better equip EU companies to make strategic decisions, optimise their investments, and achieve their long-term goals. They will also better assess the risks and opportunities arising from EU financial markets, regulations, and policies and adapt to changes in the economic and business environment. This will also help increase businesses' financial stability, growth, and competitiveness in the European Union.

Chapter Two

The Time Value of Money: How Inflation and Other Factors Affect the Value of Money over Time

The time value of money is a concept that describes how money's value can change over time due to inflation and other factors. Understanding and considering the time value of money is crucial for financial planning, investing, and making decisions about future cash flows.

Inflation is one of the main factors affecting the value of money over time. Inflation is a general and sustained increase in the price level of goods and services in an economy. As inflation increases, the purchasing power of money decreases. This means that the same amount of money will not be able to buy as much in the future as it can today. For example, if you have €100 today and inflation is 3% in 2023, buying the same good or service will take more than €100.

In addition to inflation, other factors can affect the value of money over time, such as interest rates, investment returns, risks, and general economic conditions. Higher interest rates or yields may positively impact the value of money over time, while lower interest rates or investment opportunities may decrease its value.

Financial methods such as discounting cash flows calculate and reflect the time value of money. This method uses a discount rate that reflects the expected return or cost of equity to convert the value of the future cash flow back to its present value. This allows cash flows to be compared over different periods and decisions to be made on the acceptability of investments, business projects, or financial decisions.

It is essential to understand that the time value of money affects all areas of personal and business financial planning. Considering the impact of inflation and other factors on the value of money over time is crucial to properly planning savings, investments, debt management and other financial decisions.

Time Value of Money

Definition

The time value of money refers to the concept that money received or paid at a given moment is worth more than the same nominal value that will be received or paid in the future. This is due to factors such as inflation, the possibility of investment returns or the loss of value of money over time.

Time value is based on the idea that money can generate returns or losses in value over time. As a result, money received or paid in the future is worth less than money of the same nominal value received or paid today.

The reasons for this are multifaceted. Inflation, which increases the price level of goods and services in the economy, eventually reduces the purchasing power of money. In addition, the money available today has the potential for a return on investment, meaning we can earn more money by investing over time. However, there is also a risk that future cash flows will not materialise.

Understanding and considering the time value of money is crucial for financial planning, investing, and making decisions about future cash flows. Methods such as discounting cash flows convert the value of future cash flows back to a present value, allowing cash flows to be compared over different periods and making more informed financial decisions.

Relevance for Financial Planning, Investments and Decisions on Future Cash Flows

The time value of money plays a crucial role in financial planning, investing and deciding on future cash flows. Understanding this concept allows us to address financial issues more comprehensively and to estimate future cash flows more accurately.

It is essential to consider the time value of money in financial planning. This allows us to estimate the value of future inflows and outflows and plan appropriate actions to meet financial targets. Failure to consider the time value of money may result in underestimating or overestimating the required savings, the value of pension funds, or target investment returns.

Understanding the time value of money is crucial in assessing the return on investment. Money held today can be invested to generate

returns in the future. Comparing the value of these future returns with the value of the initial investment allows us to assess the return on investment and make better investment decisions.

When deciding on future cash flows, the concept of the time value of money allows us to assess the impact of inflation, interest rates, and other factors on the value of money over time. This helps us to compare different options and choose the one that will give us the most value in the future.

A comprehensive understanding of the time value of money allows us to plan our finances better, assess the return on our investments, and make more informed decisions about future cash flows. Applying this concept correctly allows us to maximise opportunities to grow wealth, reduce financial risks, and achieve our goals.

The Impact of Inflation on the Value of Money over Time

What Is Inflation?

Inflation is a general and sustained increase in the price level of an economy's goods and services over time. It means that the value of money decreases because the same amount of money cannot buy the same amount of goods or services in the future as it can today. Inflation is a natural economic phenomenon usually measured by the consumer price index.

Some of the main characteristics of inflation are (Nojiri et al., 2017):

1. *Price increases.* During inflation, the prices of goods and services gradually increase. This can include the prices of food, housing, fuel, education, health services, and other goods.
2. *Reduction in purchasing power.* Inflation reduces the purchasing power of money. More money is needed for the same amount of goods or services. This means that people with a fixed income or savings lose purchasing power.
3. *Impact on the economy.* Inflation can have significant economic consequences. High inflation can lead to uncertainty, reduced consumption, increased production costs, and reduced investment. Low inflation or deflation can also lead to negative consequences, such as economic stagnation and falling prices.
4. *Causes of inflation.* Inflation can arise from several factors, including demand growth, increases in production costs, central bank

monetary policy, commodity price fluctuations, changes in fiscal policies, changes in exchange rates and other economic changes.

Knowing inflation is essential for financial planning, investments, and decisions regarding future cash flows. The impact of inflation on the value of money over time should be considered when assessing investment returns, planning savings and adjusting personal and business financial goals.

Rising Prices and a Reduction in the Purchasing Power of Money

Inflation is reflected in an increase in the price level of goods and services in the economy, reducing the purchasing power of money. This means the same amount of money cannot buy the same goods or services. This phenomenon affects people's daily lives and the economic environment in several ways (Lorenzoni et al., 2018):

1. *Decrease in the value of money.* Inflation decreases the value of money as the prices of goods and services rise. This means more money must be spent to buy the same product or service. Money loses purchasing power, which affects the standard of living of individuals and households.
2. *Impact on consumption.* Inflation can make it difficult for consumers to maintain the same level of consumption. Higher prices can reduce purchasing power, leading to lower demand for goods and services. This can affect businesses which struggle with falling sales and profits.
3. *Random burden-sharing.* Inflation can also unevenly impact people and households. Lower-income and socially disadvantaged groups may be more exposed to inflation as they cannot adjust to higher prices. This can increase social inequality and widen the gap in purchasing power between populations.
4. *Impact on savings.* Inflation can negatively impact the value of savings. If interest rates on savings do not keep pace with inflation, the real value of savings decreases, which can threaten the financial security of individuals and pensioners.

The decline in money's purchasing power due to inflation underlines the importance of considering money's time value in financial planning, investments, and decisions about future cash flows. Understand-

ing and managing inflation's impact can help preserve money's purchasing power, adjust financial targets, and protect assets against loss of value.

An Example of the Effect of Inflation on the Value of Money

To get a better idea of the impact of inflation on the value of money, consider the following example:

> Suppose you have €100 today, and inflation is 3% yearly. That means that goods and services will rise by 3% every year.
> If inflation did not affect money, €100 could buy a certain amount of goods or services. However, inflation is expected to reduce the value of money, meaning that the same amount of goods or services will cost more in the future.
> So, assuming that inflation stays at 3% and we want to find out how much our €100 will be worth in ten years, we can use a simple calculation:
>
> $$€100 \times (1 + 0.03)^{10} = €134.39.$$
>
> This means that the value of €100 in ten years, assuming 3% inflation, will be around €134.39. In other words, buying the same amount of goods or services you can buy today for €100 will cost €134.39.

This example clearly shows how inflation erodes money's purchasing power over time. To avoid this loss of value, the time value of money must be considered in financial planning, investments, and decisions about future cash flows.

Other Factors Affecting the Value of Money over Time

Interest Rates and Return on Investment

Interest rates and investment returns significantly impact the value of money over time. Understanding this impact helps us plan investments, assess returns, and make better financial decisions. Here are some key considerations (Palepu et al., 2020).

1. *Interest rates* are the cost or return on money expressed as a percentage. Higher interest rates mean we will pay more for a loan or receive a higher return on an investment. Interest rates can affect the value of money in two ways:

  - *Impact on the value of future cash flow.* Higher interest rates can increase the value of future cash flow, as the returns or interest we receive will be higher. This means the future cash flow will be worth more if the interest rate is higher.
  - *Impact on the discount rate.* discounting is used to estimate the value of future cash flows, whereby the future cash flow is recalculated back to its present value. A higher discount rate reduces the present value of future cash flows.
2. *Return on investment* represents the profit or return that can be achieved by investing money. Returns can vary depending on the type of investment, the risks involved and market conditions. Investment returns affect the value of money over time in the following ways:
  - *Property appreciation.* Positive investment returns increase the value of our assets. The money we invest and earn above-inflation returns will be worth more, allowing us to maintain or increase our purchasing power.
  - *Decrease in property value.* Negative investment returns can reduce the value of our assets. If returns are not high enough to overcome inflation or investment costs, the value of assets will decrease in the future, leading to a loss of purchasing power.

When planning investments and making financial decisions, it is essential to consider the impact of interest rates and investment returns on the value of money over time. Here are some key considerations:

1. *Comparing interest rates and returns.* When choosing between different investment options, it is important to compare interest rates and expected returns. Higher interest rates or yields allow for an increase in wealth growth and maintain or increase the purchasing power of money over time, so it makes sense to look for investments with higher interest rates or expected returns to increase wealth growth.
2. *The impact of interest rates on borrowing costs.* Interest rates also affect borrowing costs. Higher interest rates increase the cost of borrowing, making financing more difficult and reducing the profitability of a project or investment. Therefore, interest rates should be considered when planning financing to avoid an excessive financial burden.

3. *The long-term effect of interest rates and yields.* Interest rates and investment returns can affect the value of money in the long term. Over time, a slight difference in interest rates or yields can widen significantly due to the compounding of returns. Long-term planning and selection of investments with appropriate interest rates or yields can contribute to long-term asset growth and preserve the purchasing power of money.

It is essential to remember that interest rates and investment returns depend on economic conditions, central bank policies, risks and global market conditions. Their value can change, so investment strategies and financial decisions should be regularly monitored and adjusted to current conditions. A comprehensive understanding of the impact of interest rates and investment returns on the value of money over time is crucial for successful financial planning, appropriate asset management and achieving financial goals.

Risks and General Economic Situation

Risks and general economic conditions can significantly impact the value of money over time. Understanding this impact helps us to plan investments, manage risks and adjust financial decisions. Key considerations include (Adrian et al., 2019):

1. *Risks and returns.* Every investment carries a particular risk. Higher risks usually mean potentially higher returns, volatility, and the possibility of asset value losses. Risks affect the value of money over time in the following ways:
   - *Increasing uncertainty.* If the market is precarious and uncertain, demand may decrease, leading to lower prices and asset values.
   - *Changes in profitability.* Risks and general economic conditions can affect an investment's profitability. An unstable economy, recession, or other adverse conditions can decrease investment returns, negatively affecting money's value.
2. *Inflation.* Risks and general economic conditions can also affect inflation rates. High-risk and volatile conditions can increase inflation and reduce the purchasing power of money and the value of assets.
3. *Diversification of investments.* To manage risks, it is essential to

implement an appropriate approach to diversification of investments. This reduces the risk of concentration and exposure to particular investments or sectors. Asset diversification allows us to reduce individual risks' impact on our assets' overall value over time.

4. *Risk management.* Appropriate measures are essential to manage risks and protect assets. This includes monitoring economic conditions, regularly reviewing and adjusting investment portfolios, and adequately insuring against potential losses.
5. *Adjusting financial decisions.* General economic conditions and risks can affect our financial decisions. In these circumstances, it is essential to adjust financial decisions to preserve the value of money over time. Some options for adjustment are:
   - *Adjusting the investment portfolio.* We can adjust the composition of our investment portfolio depending on the general economic situation and the expected risks. For example, in times of high risk and volatility, we may increase our exposure to more stable investments such as bonds or safe havens. Adjusting our portfolio helps us preserve the value of money in different economic environments.
   - *Risk management.* Effective risk management allows us to reduce exposure and protect assets against potential losses. This includes analysing risk, adopting an appropriate level of risk in line with our objectives and capabilities, and using instruments such as insurance or hedging strategies.
   - *Adapting consumption habits.* Adapting consumption habits is important in times of general economic conditions and increased risk. Lifestyle changes, savings, and innovative cost management help us maintain financial stability and the purchasing power of money.
   - *Monitoring inflation.* Monitoring inflation rates in an economic climate and in the presence of risks is crucial. If inflation is expected to increase, financial plans need to be adjusted, including adjustments to future revenues, costs, and investment strategies.

Proper risk management and adapting financial decisions to the general economic situation help preserve the value of money over time. Monitoring and adapting financial strategies to circumstances allows

us to maintain financial stability, reduce risk exposure, and achieve our financial goals.

The Impact of Spending and Investment on the Value of Money

The way we spend and invest has a significant impact on the value of money over time. Different approaches to spending and investing can affect our financial stability and ability to grow assets and maintain the purchasing power of money. Let us look at some key aspects (Van Duuren, Plantingain Scholtens, 2016):

1. *Spending and saving.* How we spend our money affects how much we have left for the future. If we spend all our money on our current needs and gratification, we risk financial insecurity in the future. However, if we can save a portion of our income and invest it wisely, we can create wealth that allows us to maintain or increase our purchasing power.
2. *Investments.* How you invest your money significantly impacts how your wealth grows and maintains its value. Smart investments allow us to generate returns over inflation, which maintains or increases the purchasing power of money over time. Diversifying the investment portfolio, considering risks and returns, and monitoring market trends are critical for appropriate investments.
3. *Long-term perspective.* The value of money is better expressed in a long-term perspective. Investing long-term and planning for the future allows us to reap the benefits of wealth growth and risk management. Having a long-term perspective on our financial goals allows us to make more informed spending and investment decisions, which in turn allows us to preserve and increase the value of our money over the long term.
4. *Inflation.* How we spend and invest also impacts how we manage the effects of inflation. If our spending and investment do not keep pace with inflation, the value of money can decrease, and our assets lose purchasing power. Adjusting how we spend and choosing investments that can beat inflation allows us to preserve the value of money and maintain financial stability.

The right way of spending and investing allows us to preserve and increase the value of money over time. By doing the right things, we can

achieve financial stability, save for the future, preserve the purchasing power of money and achieve our financial goals. Below are some fundamental principles to consider when spending and investing (Kidwell et al., 2016):

1. *Control over budget and costs.* Creating a budget gives us a clear overview of our income and expenditure and allows us to manage our money better. Tracking our costs helps us identify areas where we can save and optimise our spending. By cutting unnecessary costs, we can save more money for the future.
2. *Diversifying investments.* Diversifying investments is a critical way to reduce risk and increase returns. By dividing an investment portfolio into different investment classes, such as shares, bonds, and real estate, we can reduce exposure to particular risks and increase the possibility of achieving stable returns in different economic environments.
3. *Long-term investments.* Long-term investments allow us to reap the benefits of growing wealth over time. By continuously investing in investments with long-term growth potential, we can achieve our medium-and long-term financial goals. It is essential to be patient and persistent, recognising that investments can change in value and that short-term downturns can be part of a long-term recovery.
4. *Education and expert advice.* Continuously educating yourself on financial topics and understanding investment options and spending methods is essential. Advice from a financial professional can help us make more informed decisions that align with our goals and needs.

The right way of spending and investing allows us to manage our money better, grow our wealth, and preserve its value over time. Being aware of how we spend, diversifying our investments, investing for the long term, and educating ourselves help us achieve financial stability and reach our financial goals.

Financial Methods to Take into Account the Time Value of Money

Discounting Cash Flows

Discounting cash flows is a financial method for estimating the present value of future cash flows. This method is based on the time value of

money, which states that money received in the future is less valuable than the same amount received today. Discounting cash flows allows cash flows to be compared over different periods and helps make financial decisions, such as assessing the return on an investment or valuing a business.

The discounting process involves using a discount rate that reflects the required return or cost of capital. The discount rate represents the investor's expected return or cost regarding risk, liquidity, market conditions, and other factors. A higher discount rate reduces the present value of future cash flows, while a lower discount rate increases the present value.

The method of calculating the discounted value of cash flows is to apply the formula:

$$Discounted\ value = \frac{cash\ flow}{(1 + discount\ rate)^{time\ period}}$$

When future cash flows are discounted, they are converted to present value. This lets us estimate how much a future cash flow is worth today. Discounting cash flows can be used to perform a net present value (NPV) analysis, an internal rate of return (IRR) analysis, or to estimate the value of an investment.

Discounting cash flows is essential in financial planning, assessing return on investment, business valuation and cash flow management decisions. Proper application of this method allows a better estimate of the value of future cash flows and helps to choose the most profitable and sensible financial decisions.

Use the Discount Rate to Recalculate the Value of Future Cash Flows

Using a discount rate to recalculate the value of future cash flows is critical to implementing the discounting process. The discount rate represents the expected return or cost of capital and reflects risk, liquidity, market conditions and other factors.

When determining the appropriate discount rate, it is essential to consider the following factors (Hall, 2017):

1. *Risk.* A higher level of risk usually requires a higher discount rate. Different investments or projects have different levels of risk, so it is essential to assess the risk and adjust the discount rate accordingly.

2. *Alternative investments.* The discount rate can be linked to alternative investment options. If investments have a higher expected return, the discount rate will be higher, as the investor expects an appropriate return compared to alternative investments.
3. *Market conditions.* Market conditions such as interest rates, inflation, economic growth, and the general financial environment can affect the discount rate. In periods of high interest rates or market volatility, it is common to use a higher discount rate as the expected return or cost of capital is higher.
4. *Length of period.* The length of the period affects the discount rate. The time value of money concept is commonly used, stating that money received in the future is less valuable than the same amount received today. Therefore, a higher discount rate is used for extended periods to account for more significant uncertainty.

The correct application of the discount rate is crucial in converting the value of future cash flows into a present value. A higher discount rate reduces the present value of future cash flows, while a lower discount rate increases the present value. This allows cash flows to be compared over different periods and helps make financial decisions such as assessing the return on investment or valuing businesses.

Comparison of Cash Flows over Different Periods

When comparing cash flows over different periods, it is crucial to consider the time value of money. Money received in the future has a lower value than the same amount of money received today. The discounting method compares cash flows over different periods, allowing future cash flows to be converted into present value.

A net present value analysis may be helpful when comparing cash flows over different periods. This analysis uses a discount rate to convert the sum of future cash flows into a present value. The net present value represents the difference between the present value of the cash flows and the initial investment. A positive net present value indicates a positive return on investment, while a negative net present value indicates a negative return.

In addition to the net present value analysis, an internal rate of return (IRR) analysis can be used. The IRR is the discount rate at which the net present value is zero. The IRR represents the expected return on an investment and is used to compare different projects or investment

options. A higher IRR usually indicates a more profitable investment.

Other factors, such as risk, cost of capital, and expected returns, should also be considered when comparing cash flows over different periods. These factors should also be considered when determining the discount rate and converting cash flows to present value.

Comparing cash flows over different periods allows us to assess the return on investment, evaluate projects and make financial decisions. Using discounting methods, we can correctly calculate cash flows and consider the time value of money, which helps us choose the most profitable and sensible financial options.

The Importance of Considering the Time Value of Money in Financial Decisions

Taking into account the time value of money is crucial for financial decisions, as the value of money is not constant but changes over time. Understanding and considering the time value of money helps us plan, invest and make the right decisions about future cash flows. Some critical aspects of considering the time value of money include (Babashamsi et al., 2016):

1. *Discounting of cash flows.* The discounting method converts future cash flows into present value. This method is based on the idea that money received in the future is worth less than today's amount. Discounting cash flows considers the time value of money and allows cash flows to be compared over different periods.
2. *Valuation of investments.* When assessing the return on an investment, it is essential to consider the time value of money. Future investment returns are worth less today than the same amount of money. Therefore, when valuing investments, an appropriate discount rate should be used to reflect the expected return or cost of capital. Proper valuation of investments helps us to choose the most profitable options.
3. *Revenue and cost planning.* The time value of money must be considered when planning revenue and costs. Expected income in the future will be worth less than the same amount of money today, so it is essential to prepare for income and adjust it for inflation and expected changes.
4. *Debt management.* The time value of money is also essential in

debt management. The debt held today will have to be repaid in the future, taking interest into account. A proper understanding of the time value of money allows us to plan appropriately for debt repayment and avoid excessive costs in the future.

Savings and Investment Planning

Savings and investment planning are critical to achieving financial goals and creating stability and growth in wealth. Some essential aspects of savings and investment planning include (Brounen et al., 2016):

1. *Setting financial goals.* The first step is to define clear and measurable financial goals, such as setting up a safety fund, buying a home, funding children's education or preparing for retirement. Setting goals helps us plan the right amount of savings and choose the right investment strategies.
2. *Budgeting.* A budget lets you plan your monthly income and expenditures. Create a budget that covers all your expenses, including fixed costs such as housing bills, food, transport, and health insurance and discretionary expenses such as travel and entertainment. A budget also allows us to determine the amount we can spend on savings and investments.
3. *Savings automation.* You can achieve consistent savings by setting up an automated savings system. This system allows us to automatically transfer a certain amount of money into a separate savings or investment account before it is used for other purposes, ensuring regular and consistent savings.
4. *Diversification of investments.* When planning investments, diversification is essential. Diversifying the investment portfolio with different types of assets, such as shares, bonds, real estate, or funds, helps reduce risk and improve returns. Properly allocating resources aligned with our risk tolerances and objectives allows us to achieve long-term asset growth.
5. *Monitoring and adjusting.* Monitoring progress towards financial targets and reviewing investment performance regularly is crucial. Review your investment portfolios, monitor returns, and assess whether investment strategies must be adjusted to changing market conditions or objectives.

Savings and investment planning is a long-term process that re-

quires informed decisions and regular monitoring. With proper savings and investment planning, several benefits can be achieved, such as:

1. *Achieving financial targets.* Planning allows us to set and progressively achieve financial targets. By setting clear goals and planning appropriate savings and investments, we increase our chances of achieving them. For example, if you plan to buy a home, you set the amount you need to save and choose an investment strategy to achieve it.
2. *Financial security.* Regular savings and an appropriate investment strategy help us build financial security. By creating a savings fund, we reserve funds for unforeseen situations such as job loss, medical expenses or property repairs. Long-term investments also allow us to grow our wealth gradually and improve our financial stability.
3. *Wealth growth.* Planned savings and intelligent investments allow us to grow our wealth gradually. Over time and through the cumulative effect of returns, we can increase the value of our investments. Proper asset allocation across different investment classes allows us to reduce risk and improve returns over the long term.
4. *Financial independence.* Long-term savings and investment planning can lead to financial independence. By saving adequately and generating income from investments, we can achieve the financial freedom to achieve our goals without relying solely on a full-time job.
5. *Flexibility and opportunity.* Financial planning creates flexibility and the chance to take advantage of opportunities. Having an adequate reserve of funds allows us to cope with unexpected costs or take advantage of favourable investment opportunities in the market.

When planning your savings and investments, it is essential to consider your financial goals, the time value of money, risk and flexibility. Systematic planning allows us to manage our money better and improve our long-term economic well-being. Here are some steps that can help you plan your savings and investments:

1. *Setting objectives.* Explain which financial objectives you want to

achieve. This includes short-term goals, such as saving for a holiday or buying a car, and long-term goals, such as retirement preparation. Setting specific and measurable goals will allow you to plan more focusedly.

2. *Budgeting.* Make a budget that includes your income and expenses. Analyse your expenses and identify areas where you can save money. This will help you determine how much money you can spend on savings and investments.
3. *Determine your investment approach.* Consider your investment approach and the risk you will take. Depending on your objectives and the time horizon available, determine an appropriate asset allocation between different investment classes, such as shares, bonds, real estate, or funds.
4. *Regular savings.* Save money systematically and regularly every month. This will allow you to gradually build up your funds and take advantage of the time value of money. Use automatic transfers to special savings or investment accounts to simplify the savings process.
5. *Monitor and adapt.* Regularly monitor progress towards your financial goals and review the performance of your investments. Adapt your investment strategy to changing circumstances, market conditions, or objectives if necessary.

Savings and investment planning are dynamic and require commitment, consistency, and flexibility. These steps will better control your finances and create the foundations for long-term financial well-being.

Debt Management

Debt management is a crucial aspect of financial planning that helps us manage our debt obligations and achieve long-term economic stability (table 2.1).

TABLE 2.1 Fundamental Principles of Debt Management

Understanding debt	The first step in debt management is to understand your debt type and the conditions attached to it. Pay attention to interest rates, repayment terms, approval costs and any conditions in the contract. Understanding your debt allows you to plan your repayments better and reduce costs.

Continued on the next page

TABLE 2.1 *Continued from the previous page*

Proper repayment planning	Plan your debt repayments in a way that suits your financial situation. Create a budget that includes monthly debt repayment instalments and ensures you can meet your obligations regularly. Set repayment priorities where you can prioritise higher interest debt or debt with the shortest repayment term.
Reducing the cost of debt	Find ways to reduce the cost of your debt. For example, check your debt refinancing options and consider transferring your debt to another financial institution with more favourable terms. Also, consult your creditor to see if changes to the repayment terms can be negotiated, such as lowering the interest rate or extending the repayment period.
Avoiding further borrowing	While managing your current debt, avoid taking on further debt. Consider your needs and wants and whether some new debt commitments are necessary. This will help you better control your finances and reduce the risk of over-indebtedness.
Financial advice	If you are facing a big debt problem or need professional help with debt management, get financial help. Financial advisers can help you plan repayments, restructure debt, negotiate with creditors and develop a comprehensive debt management strategy.
Building a contingency reserve	During debt management, it is essential to build up a contingency reserve. Unexpected events such as job loss, emergency repairs or medical expenses can affect your ability to repay your debt. With an adequate emergency reserve, you can better cope with such situations without interfering with your existing debt.
Increasing financial literacy	Improving financial literacy is critical to effective debt management. Learn about the different aspects of personal finance, including understanding interest rates, loan terms, debt repayment strategies and how to manage your finances properly. This will enable you to make more informed decisions about debt and improve your long-term financial position.
Long-term planning	It is also essential to have a long-term plan when managing debt. Consider how your debt fits your long-term financial goals and plans, such as retirement or buying a property. With clearly defined goals and debt management strategies, you can focus on your long-term financial well-being.
Regular monitoring and adaptation	Keep regular track of your debt and its repayment. Be aware of any changes in your financial situation or life circumstances that may affect your ability to repay your debt. Adjust your repayment plan or consult a professional to find appropriate solutions.

NOTES Adapted from Brealey et al. (2020).

Debt management requires discipline, commitment, and informed decisions. Adopting a proper debt management, you can achieve finan-

cial stability, reduce stress, and move closer to your long-term financial goals.

Impact on Personal and Business Financial Goals

The impact of the time value of money on personal and business financial goals is an essential aspect of financial planning. Understanding this impact allows us to plan better, choose the right strategy and achieve the desired results. Let us look at some of how the time value of money affects personal and business financial goals:

1. *Personal financial goals*
    - *Saving for retirement.* Early planning and retirement savings are crucial to maximising long-term wealth growth. Thanks to the compounding effect, the money we save today for retirement can increase significantly over time.
    - *Buying property.* The time value of money affects the ability to save for property purchases. By planning and saving early, you can achieve more significant savings and have better financial opportunities to buy a flat or a house.
    - *Children's education.* Parents should plan for the future costs of their children's education. If we start saving early, we can provide the necessary resources for an expensive education.
2. *Business financial targets*
    - *Business growth.* the time value of money influences financing and investment decisions in a business. Understanding this effect allows us to assess the value of long-term investments and choose appropriate funding sources that provide adequate returns.
    - *Business projects.* When planning new business projects, the time value of money must be considered. Discounting allows us to estimate the value of future cash flows and select projects that add the most value.
    - *Repaying loans.* The time value of money is crucial for repaying loans. Early repayment allows us to reduce interest costs and improve the company's financial position faster.

The time value of money is essential for setting, planning and achieving personal and business financial goals. Understanding this concept allows us to adapt financial strategies better, optimise returns and re-

duce risks. Essential aspects of the impact of the time value of money on personal and business financial goals include (Lee & Lee, 2015):

1. *Budgeting.* The time value of money is crucial when budgeting at a personal and business level. Considering the time value of money allows us to allocate resources efficiently and ensures that we focus resources on the priorities that deliver the most value.
2. *Investment planning.* Understanding the time value of money helps us plan long-term investments. If we start saving or investing early, we have more time to grow our assets and can take advantage of interest rates. By adequately diversifying investments into different asset classes, we can achieve a balanced return and reduce risk.
3. *Funding decisions.* When deciding whether to fund personal or business projects, the money's time value must be considered. Borrowing or external financing means costs that have to be paid back in the future. By understanding the time value of money, we can estimate the cost of financing and choose the most favourable option.
4. *Retirement planning.* The time value of money is a crucial factor in retirement planning. Saving for early retirement allows us to take advantage of a long time horizon to grow wealth. Early retirement planning will enable us to enjoy a good quality of life without financial worries.
5. *Risk management.* Understanding the time value of money helps us manage risk. Investing in insurance products such as life insurance or health insurance allows us to manage unforeseen costs and ensure financial security in the future.
6. *Adjusting financial strategies.* Based on the time value of money, it is essential to regularly review and adjust financial strategy. This includes:
   - *Portfolio review.* Regularly monitor your investment portfolios, assess their performance and check whether they meet your financial goals. Adjust your asset allocation to take advantage of growth opportunities or reduce risks if necessary.
   - *Adapting to changing circumstances.* Life and business conditions change, and adapting your financial strategies is essential. If you face unforeseen events such as job loss or medical

expenses, adjust and review your financial plans and find appropriate solutions.

- *Portfolio diversification.* Monitoring the time value of money allows us to identify the need to diversify our portfolio. Diversifying investments across investment classes and sectors reduces risk and improves returns over the long term.
- *Increase your savings.* If your current savings are not enough to meet your financial goals, consider increasing your savings. An extra investment today, because of the time value of money, will bring more value in the future.
- *Continuing education.* It is critical to stay financially literate and constantly learn new approaches and strategies. Keeping up with current trends and news in the financial world allows you to better understand the time value of money and improve your investment and debt management decisions.

Knowing how the time value of money affects your personal and business financial goals allows you to plan better, manage, and adjust your financial strategies. This will enable you to take advantage of interest rates and achieve the results you want in the long term.

The time value of money is a crucial concept for understanding the impact of inflation and other factors on the value of money over time. It is essential for proper financial planning, investing, and making important decisions regarding future cash flows.

Chapter Three

Equity Crowdfunding: The Benefits and Challenges of Raising Capital through Equity Sales

Equity finance is a crucial strategy companies use to raise capital and promote growth and development. In this form of financing, a company raises funds by issuing equity or shares that allow investors to enter into the company's ownership structure. The sale of shares gives the company access to additional financial resources, expertise and a more comprehensive network of business partners. At the same time, investors become company owners by acquiring a particular stake.

In this chapter, we will examine the benefits and challenges of equity financing. We will start by analysing the benefits of equity sales, including the ability to raise more finance, flexibility in the capital structure, joining a network of experienced investors, risk sharing, and access to expertise. These advantages are vital in providing capital for expansion, R & D, innovation, and other business needs. The second part will focus on companies' raising capital through equity sales challenges. These include losing control over the company, the need for disclosure, potential conflicts between investors and existing owners, and the need to create long-term value for investors. Understanding these challenges is critical to properly planning and executing a capital raising through an equity sale and building successful investor relations.

This comprehensive overview of the benefits and challenges of equity financing for businesses will give readers a better understanding of this critical topic. Exploring these aspects will help companies make informed decisions on financing strategies, select the right investors and establish effective relationship management with their owners. This will contribute to the long-term success and sustainable growth of the business.

Benefits of Equity Financing

Equity finance is one of the critical ways for companies to raise capital. It brings several benefits companies can use to grow, develop, and suc-

ceed in the long term. Some of the essential benefits of equity financing include (Gompers, 2022):

1. *The ability to raise capital.* By selling equity stakes, a company raises funds from investors, allowing it to raise more capital than other forms of financing, such as debt financing. Higher capital gives the company greater financial resilience and the ability to invest more or grow.
2. *Sharing risks and responsibilities.* Integrating new owners into the company allows for sharing risks and responsibilities. The owners take on part of the risk associated with the business's success and operation, which reduces the financial pressure on the business and relieves the existing owners.
3. *Increased credibility and reputation of the company.* Attracting reputable and influential investors as business owners helps to increase the credibility and reputation of the company. This can positively impact the trust of customers, business partners and other stakeholders and help create better business opportunities.
4. *Access to expertise.* By selling equity stakes, a company can attract strategic partners and investors with expertise, experience, and business contacts. Such collaboration allows the company to benefit from the valuable know-how of partners, which can accelerate the company's growth, innovation, and development.
5. *Potential for long-term growth and expansion.* Equity finance empowers a company to obtain long-term financial resources for growth, business expansion, new product development, or entry into new markets. A company can achieve its long-term vision and goals with stable and sufficient capital.

These advantages of equity finance allow companies to raise more capital, share risk and responsibility, increase credibility and reputation, access expertise and the potential for long-term growth and expansion. Equity finance allows companies to raise the necessary funds for various needs, such as developing new products, expanding their business, acquiring other companies or carrying out innovative projects.

In addition to financial support, equity investors bring added value through their expertise, experience, and business contacts. Working with strategic partners can help a company accelerate its development,

attract new customers and exploit synergies between different businesses. In addition, a company with reputable and influential owners has greater credibility and trust in the eyes of customers, suppliers and other stakeholders, which can lead to better business opportunities and competitive advantages.

However, it is also essential to consider the challenges of equity financing, such as loss of complete control of the company, profit and benefit sharing with investors, and potential investor interference in business decisions. The complex process of raising equity capital, which involves preparing the relevant documentation, assessing the value of the business and negotiating with investors, must also be considered.

Despite these challenges, equity finance's benefits prevail. It enables companies to raise the capital they need and to develop and grow over the long term. Proper investor relations management, strategic planning, and equity fundraising implementation are essential to successfully reaping the benefits of equity finance.

The Challenges of Equity Financing

Equity finance also presents some challenges companies face in raising and managing equity capital. Some of the critical challenges of equity financing include (Brealey et al., 2020):

1. *Loss of complete control of the company.* A company may lose control of its business and business decisions by selling equity stakes. Investors who become owners may have some influence over the company's business strategy, management, and decisions.
2. *Sharing profits and benefits with investors.* By incorporating new owners, the company commits to sharing profits with its investors. This may affect the company's profitability and limit its freedom to use profits for purposes other than reinvestment or expansion.
3. *Potential investor interference in business decisions.* Equity investors may have some involvement in a company's business decisions. Their interests and priorities may differ from the company's, leading to tensions or conflicts in crucial decision-making.
4. *Raising equity is a more complex process that takes time, effort, and costs.* The company has to prepare for transparency, business plans, business valuations, negotiations, and contracts with investors.

5. *Proper investor relations management.* The company must establish effective management, including clear communication, regular reporting, consideration of investors' interests and expectations, and maintaining a long-term partnership.

Successfully meeting these challenges requires good planning, professionalism, and an open dialogue between the company and investors. The company must be aware of these challenges and adequately prepare for their impact, implementing adequate mechanisms to manage investor relations and resolve potential conflicts.

Strategic Aspects of Equity Capital Increases

Raising equity is crucial to corporate financial management and can have significant strategic implications. Let us look at some of the strategic considerations that need to be taken into account when raising capital (table 3.1).

Raising equity is an important strategic step for a company and requires a holistic approach. With proper planning, evaluation and im-

TABLE 3.1 Strategic Considerations That Need to Be Taken into Account When Raising Capital

Company objectives	A company must clearly define its objectives and strategy before approaching an equity acquisition. Does the company want to finance growth or fund new projects? Clearly defined goals will help determine appropriate strategies for raising capital.
Type of Equity	A company can choose to raise different types of equity, such as private equity, selling shares on the stock exchange, or raising venture capital. Each type of equity has advantages and disadvantages, so it is essential to consider the options and choose the one that best suits the business's needs.
Valuing the company	Before raising equity, the company must be valued. This will include an assessment of financial ratios, past performance, future expectations and market conditions. An accurate valuation will help determine the right level of capital to raise and the company's bargaining power when negotiating with potential investors.
Finding the right investors	Finding the right investor who brings financial resources and strategic value is essential when raising equity. An investor with the right experience, industry knowledge or market opportunity can help a company grow and develop. It is also essential to check the reputation and references of potential investors,

Continued on the next page

TABLE 3.1 *Continued from the previous page*

Negotiations and contractual relations	Raising equity capital involves negotiating with investors and building contracts and relationships. A company must devote sufficient time and energy to properly drafting contracts that set out the terms of the equity investment, the company's management, the distribution of profits and possible exit strategies.
Long-term consequences	Raising equity can have long-term consequences for the company. Equity investors bring new stakeholders to the company and can influence decisions, strategy and management. The company should be aware that raising equity may affect the ownership structure, control and autonomy. It is essential to assess whether
Intra-company compliance	When raising equity, the entire company's management and team must be aligned with the capital-raising strategy. This includes aligning with the company's objectives, communicating clearly with employees, ensuring everyone receives the correct information, and understanding the implications of raising capital.
Legal and regulatory compliance	Legal and regulatory requirements should also be considered when raising equity capital. This includes compliance with securities laws, stock exchange rules, and other regulations. Legal compliance is crucial to avoid future legal problems or consequences.
Changes in corporate culture	Increasing equity can also change a company's corporate culture. Investors can bring new ideas, practices, and expectations that may differ from the existing corporate culture. The company must adapt to ensure that the existing corporate culture is consistent with the expectations of new investors.

NOTES Adapted from Nambisan et al. (2018).

plementation, a company can achieve its financial objectives, drive growth and development and gain a strategic advantage in the market.

Legal and Regulatory Aspects of Equity Financing

Obtaining equity financing can be complex, requiring various legal and regulatory considerations. Table 3.2 presents some of the critical legal

TABLE 3.2 Critical Legal and Regulatory Considerations That Need to Be Taken into Account in the Context of Equity Financing

Securities legislation	Equity acquisition usually involves the issue of shares or other securities, which securities laws may govern. An entity shall carefully consider and comply with the requirements of the laws and regulations governing the procedures, disclosures, obligations and restrictions applicable to the issuance and sale of securities.

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TABLE 3.2 *Continued from the previous page*

Treaties and agreements	Acquiring equity involves entering into various contracts and agreements, such as investment, share sale, co-founder, or share management agreements. These agreements govern the rights, obligations, distribution of profits, control, and other important aspects between the company and the investors and must be drafted with due care.
Privacy and confidentiality	Sensitive information about a company's business may be exchanged during an equity purchase. Protecting the privacy and confidentiality of this information is crucial. The Company must manage this information carefully, comply with applicable data protection laws and enter into appropriate confidentiality agreements with investors and other participants.
Regulatory authorities	Equity capital raising may be subject to supervision and regulation by regulatory authorities such as financial market regulators, securities commissions, or other competent institutions. The Company must comply with these authorities' rules and requirements and, where applicable, obtain the necessary licences and approvals.
Transparency and disclosure	An entity shall ensure adequate transparency and disclosure of information relating to equity acquisition. This includes publishing correct and complete information about the company, its financial terms, its plans for using the capital raised, and the risks involved. This is important to protect investors' interests and ensure compliance with regulatory requirements.
Corporate governance	Raising equity can change a company's corporate structure and governance. The company should follow best corporate governance practices and establish clear procedures and policies for engaging new owners, making decisions and ensuring adequate oversight. This helps to ensure investor confidence and maintain effective corporate governance.
Competition law	It is also essential that the rules of competition law are respected when raising equity capital. In some cases, an undertaking's acquisition of equity capital may lead to market structure changes, which may trigger scrutiny and approval by the competition authorities. The Company must be alert to any restrictions and obligations under competition rules.
Tax aspects	An increase in equity can also have tax consequences for the company and investors. The company must comply with tax legislation and consider the tax liabilities and benefits associated with the equity acquisition. An appropriate tax structure can help minimise the tax burden and optimise tax benefits.

NOTES Adapted from Li (2010).

and regulatory considerations that need to be taken into account in the context of equity financing.

When raising equity, it is crucial to obtain legal and professional support to help the company understand and comply with the legal and regulatory aspects. This will ensure regulatory compliance, mitigate risks and enable the implementation of equity fundraising.

Analysis of the Effectiveness of Equity Financing

Analysing the effectiveness of equity financing is a complex process that involves assessing various aspects and outcomes of equity capital raising. Here are some of the critical factors that can be taken into account when analysing performance (Chadha & Sharma, 2015):

1. *Financial results.* An important point is to assess the company's financial performance after the equity acquisition. This includes comparing vital financial indicators such as profit, return on equity, return on assets, cash flow, revenue, and profit growth before and after the equity acquisition. Assessing whether the capital acquisition has improved the company's financial performance is also essential.
2. *Growth and development.* Analyzing the effectiveness of equity financing also includes assessing the company's growth and development after raising capital. It is essential to check whether the company has achieved its planned growth targets and milestones, successfully expanded into new markets, developed new products or services, and increased its market share. Growth and development are critical indicators of success in increasing equity.
3. *Strategic advantages.* The performance analysis should also include an assessment of the strategic advantages the equity acquisition has brought to the company. These may include access to new resources, investor expertise, market knowledge, an extended network of business partners, or other strategic benefits. It is essential to assess whether these benefits have given the company a competitive advantage and long-term value.
4. *Governance and influence of owners.* The analysis of the effectiveness of equity financing also includes an assessment of the company's governance after the acquisition of capital and the influence of the new owners. It is essential to consider whether effective governance mechanisms have been implemented, whether the new owners have added value, expertise and experience and whether positive synergies have been established between the

company and the owners. Effective governance and engagement with owners are critical to the long-term success of equity finance.

5. *Value for investors.* The investor perspective should also be considered when analysing the effectiveness of equity financing. This includes an analysis of the return on investment, an assessment of dividends or profit distributions, share or stock appreciation and other benefits accruing to investors. If the equity acquisition has created value for investors and met their expectations, it can be successful.
6. *Long-term effects.* Identifying the long-term effects of equity increases is essential. These may include the impact on the company's long-term strategy, competitive position, innovation, human resource development, acquisition of new business opportunities, and other long-term benefits. The effectiveness of equity fundraising can be assessed in terms of its positive long-term effects on the company.

It is important to remember that the analysis of equity financing's effectiveness focuses on financial results and strategic, operational, and long-term impacts. Each company is unique, and specific circumstances, objectives, and benchmarks must be considered to assess the effectiveness of equity capital raising correctly.

Alternative Financing Options

In addition to raising equity capital, there are other alternative financing options that companies can use. Some common alternatives include are presented in table 3.3.

TABLE 3.3 Alternative Financing Options

Long-term loan financing	Businesses can obtain long-term loans from banks, financial institutions or other lenders. Loans are usually repaid over several years at a fixed interest rate and often require collateral. Long-term loan financing suits projects with long-term returns, higher equipment, or real estate investments.
Short-term loan financing	Companies can use short-term loans to cover their liquidity needs in the short term. This includes bridging loans, working capital or opening credit lines with banks. Short-term loan financing helps cover short-term expenses such as inventories, payroll, and other operating costs.

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TABLE 3.3 *Continued from the previous page*

Bond financing	Companies can issue bonds, which are long-term debt instruments. Bonds can be issued publicly or privately, offering interest and principal repayment terms. This type of financing is suitable for companies with good creditworthiness and those wishing to expand their funding sources through the capital markets.
Long-term subordinated financing	Companies can obtain subordinated long-term financing through subordinated bonds or other subordinated instruments. This type of financing is subordinated to conventional loans and bonds and poses a higher risk to investors. Long-term subordinated financing is suitable for companies that want to expand their long-term funding sources and are willing to take on more risk.
Finance leases and leasing	Businesses can finance the purchase of equipment or real estate through finance leases or leasing. In the case of a finance lease, the entity pays monthly rental payments for the use of the equipment or property, but ownership is usually transferred to the entity at the end of the lease period. Leasing is similar but offers the option to purchase the equipment or property at the end of the lease period.
Crowdfunding	Crowdfunding is the raising of finance through crowds, usually through online platforms. Companies can use this funding model to raise funds for various purposes, such as product development, business expansion or the implementation of a specific project. Different forms of crowdfunding include product resales, donations, investment campaigns or interest-bearing loans.
Corporate Venture Capital (CVC)	Entrepreneurial venture capital (CVC) is a form of financing in which a large company invests directly in a start-up or growing business. This gives the company access to innovative technologies, business models, or market opportunities while simultaneously providing the start-up with a large company's financial resources and expertise. CVC can be a mutually beneficial way of financing and forming strategic partnerships.
Subsidies and public funding	Businesses can obtain funding through various grants, subsidies and other public sources. Governments, local authorities, and institutions can offer financial support for multiple purposes, such as research and development, employment, sustainable projects, and regional development. Obtaining public funding usually requires applying for and meeting specific criteria.
Business partnerships and strategic integrations	Instead of attracting finance through traditional forms of financing, companies may seek business partnerships or carry out strategic mergers. This allows sharing of costs, risks, and resources with other companies while creating synergies and expanding business opportunities. This type of financing is based on strategic objectives and long-term benefits for the parties involved.

NOTES Adapted from Bruton et al. (2015).

When selecting alternative financing options, the company's needs, objectives, and capabilities, as well as the industry's and the market's specificities, must be considered. The risks, costs, and legal aspects of each financing option must also be considered, and experts such as financial advisors and lawyers must be consulted to ensure that the right choice is made and implemented.

Chapter Four

Debt Financing for Business: The Pros and Pitfalls of Raising Capital through Debt

Debt financing is one of the key strategies companies use to raise capital and ensure financial stability. It is the process by which a company raises the necessary funds by issuing bonds, obtaining loans, or using other debt instruments. This form of financing allows companies to take advantage of external funding benefits while facing specific challenges and pitfalls.

This section details the advantages and pitfalls of debt financing for businesses. First, we analyse the benefits of borrowing, including retention of ownership control, tax advantages, fixed interest rates, payment flexibility, and diversification of funding sources. These benefits are crucial in providing capital for a company's development, expansion, and other financing needs.

In the second part, we will focus on companies' pitfalls regarding debt financing. These include increased financial risk, borrowing constraints, solvency, interest costs and dependence on lenders. Understanding these pitfalls is critical to proper debt planning and management, as companies need to carefully balance the benefits of raising capital with borrowing and identify the potential challenges and risks they pose.

By providing a thorough overview of the advantages and pitfalls of corporate debt financing, we will give readers a comprehensive insight into this critical topic. Understanding these aspects will help companies decide on the most appropriate financing strategy and debt management, contributing to their long-term financial stability and success.

Benefits of Debt Financing

Debt financing has several advantages that attract companies to raise capital. Here are some of the critical benefits of debt financing (Greenwood et al., 2015):

1. *Retaining ownership control.* Debt financing allows a company to raise the necessary capital without diluting its equity or sharing control of the company. The existing owners still own the company, giving them control over the business and its strategy.
2. *Tax benefits.* Interest rate liabilities related to debt financing are usually tax deductible. A company can reduce its tax base by paying interest and lowering tax liability, which is an essential lever for reducing the cost of borrowing.
3. *Fixed rate.* Debt financing allows a company to obtain a loan at a fixed interest rate. This ensures the predictability and stability of debt repayments, as interest rates are usually agreed upon when the loan is signed and remain unchanged throughout the repayment period.
4. *Payment flexibility.* Debt financing allows a company to adjust the repayment period and instalment amount according to its financial capacity. This allows for better liquidity and flexibility in managing the company's cash flow.
5. *Diversifying sources of finance.* Debt financing allows a company to diversify its sources of finance. In addition to bank loans, other forms of financing are available, such as issuing bonds or raising loans from direct investors. Diversifying the sources of financing reduces dependence on a single source and increases the company's financial stability.
6. *Ease of implementation.* Debt financing is usually less complex and faster than other forms of funding, such as equity fundraising. The process of obtaining a loan or issuing bonds is well-established and widely used, facilitating implementation and reducing administrative hurdles.

These advantages of debt financing make it an attractive option for companies. It allows companies to raise the necessary capital for various purposes, such as business expansion, investment in equipment, research and development, and short-term financing needs, without unnecessarily weakening the company's ownership structure.

However, it is important to stress that debt financing has challenges and limitations. Companies must be aware of these factors and consider them when making financing decisions. The difficulties of debt financing include:

1. *Repayment obligations.* Debt financing includes the obligation to repay the debt, including interest. The enterprise shall ensure sufficient cash flows to make regular instalments and interest payments at the specified times. Please meet these obligations to avoid financial difficulties affecting the entity's credit rating and ability to obtain future financing.
2. *Interest costs.* Debt financing includes interest payable to lenders. Interest costs depend on the interest rate, the company's credit risk, and other factors. Higher borrowing costs can reduce a company's profitability and affect its competitiveness.
3. *Debt limits.* Lenders impose limits and conditions on companies' borrowing, such as maximum loan amounts, debt-to-equity ratios and other financial ratios. These limits can restrict a company's flexibility to manage its capital and financing.
4. *Dependence on lenders.* With debt financing, the firm becomes dependent on lenders to raise capital. This may mean the firm loses some of its financial autonomy and becomes subject to the lenders' requirements and restrictions.

Despite the challenges and limitations of debt financing, this form of funding remains an attractive option for companies seeking to raise capital for development and growth. Appropriate debt management, choosing suitable financial instruments, and maintaining a solid debt-equity ratio can help address debt financing challenges. Companies can also adopt risk mitigation strategies, such as diversifying their sources of finance and reducing their reliance on individual lenders.

It is also essential to consider the company's overall financial picture, ability to repay debt, future profitability and cash flow projections. Effective communication with lenders and timely reporting on a company's financial performance can improve relations with lenders and reduce the risk of adverse consequences from potential debt repayment problems.

The key is to find the right balance between debt and equity financing and to choose the right mix according to the company's specific needs and objectives. Some companies may combine debt and equity financing to take advantage of both forms' benefits and reduce the risks involved. With an awareness of the benefits and challenges of debt financing and appropriate risk management, companies can achieve financial stability, support growth, and meet their business objectives.

The Pitfalls of Debt Financing

Debt financing has many advantages and pitfalls that must be considered when deciding on this form of funding. Let us look at some of the key pitfalls associated with debt financing (Brealey et al., 2020):

1. *The financial burden of the repayment obligation.* Debt financing includes debt repayment obligations in principal and interest. These financial burdens can be a significant cost for a company, especially when facing financial difficulties or reduced revenues. Failure to meet debt repayment obligations can lead to financial difficulties, late payments, and even loss of control of the company.
2. *Increase in financial risk.* An increase in indebtedness also increases a company's financial risk. High debt levels can make a company more vulnerable to changes in interest rates, economic conditions, or adverse events. Inadequate financial risk management can lead to severe problems, including difficulties obtaining additional financing or insolvency.
3. *Debt limits.* Lenders impose limits and conditions on borrowing from a company. These restrictions may include limits on debt-to-equity ratios, minimum credit ratings or specific financial ratios that must be met. If a company is within these limits or if certain conditions are met, it may avoid difficulties obtaining further financing or may have to take additional measures to resolve its financial problems.
4. *Dependence on lenders.* By acquiring debt, the firm becomes dependent on lenders to raise capital. This means that the firm is dependent and may lose some financial autonomy. Lenders may also have specific requirements regarding corporate governance or adherence to particular policies and procedures.
5. *Interest costs.* Interest on debt is a cost to the company. Higher interest rates can significantly impact a company's financial performance and reduce profitability. Interest costs can increase and negatively affect a company's cash flow, especially in periods of high interest rates or volatility in financial markets.
6. *Limited flexibility in corporate governance.* With debt financing, the company makes commitments to lenders and has to respect their conditions and restrictions. This can limit the company's flexibility and freedom to make critical decisions such as invest-

ment projects, dividend policies, or strategic changes. The company may need help adapting to its business plan or responding to rapid changes in the market.

Despite these pitfalls, companies can successfully manage debt financing through proper planning, risk management, and building solid relationships with lenders. Properly assessing the financial situation, managing debt, and maintaining an appropriate debt-to-equity ratio are vital steps to successfully managing the pitfalls of debt financing.

Businesses need to be aware of the challenges and risks associated with debt financing and carefully weigh all the benefits and pitfalls before choosing this form of funding. The right balance between debt and equity financing and adopting appropriate debt management measures will enable companies to successfully implement their financial strategy and achieve long-term financial stability.

Examples of Successful and Unsuccessful Examples of Debt Financing

Examples of successful and unsuccessful debt financing can vary depending on several factors, including the company's specific circumstances, the industry, the economic environment and debt management. The following are some examples that illustrate successful and unsuccessful debt financing cases.

Successful examples of debt financing:

1. Company A has successfully obtained a loan from a bank to finance its expansion plan. The capital injection enabled the company to increase its production capacity, expand its sales network and achieve high profitability. The debt was repaid on time, and interest rates were favourable, allowing the company to continue to grow and develop.
2. Company B issued bonds on the capital market and successfully raised funds to finance a significant infrastructure project. Investors received the bonds well, and the interest rates were competitive, allowing the company to manage its cash flows and complete the project.

Debt financing failures:

1. Company C obtained a high-interest loan to finance its expansion

plan but faced an unexpected drop in market demand. The company could not generate sufficient revenue to repay the loan on time, resulting in financial difficulties, late payments, and a weakening credit rating.

2. Company D has been heavily leveraged to finance investments in new technologies. Despite high expectations, the latest technology fell short of expected results, leading to lower revenues and increased financial risk. The company faced high-interest costs, difficulties repaying debt, and a loss of economic stability.

These examples show that the success of debt financing depends on various factors such as planning, implementation, risk management, economic conditions and the ability of the company to meet its obligations. It is essential that companies carefully consider their financial capacity, manage risks, and choose the appropriate debt structure that fits their needs and objectives. The success of debt financing depends on a company's ability to manage debt, maintain adequate liquidity, meet repayment obligations and adapt to changing market conditions.

It is also essential to remember that the success or failure of debt financing can be subjective and depend on the company's perspective and objectives. What may appear to be successful financing for one company may be insufficient for another. Each company has its specific circumstances, and it is, therefore, crucial that a company carries out a thorough analysis, assesses its risks, and carefully plans its financial strategy.

To avoid failures, it is essential that the company:

1. Carefully assess your ability to repay your debt and determine an appropriate debt structure in line with your financial capacity.
2. Thoroughly analyse the market and business environment to assess potential demand, competition, and risks associated with the project or investment.
3. Verify the quality and reliability of lenders and obtain favourable borrowing conditions such as competitive interest rates, flexible repayment terms and adequate collateral.
4. It manages debt prudently and regularly monitors the company's financial position and cash flow. This should include ensuring sufficient liquidity to repay debt on time.
5. Think about diversifying your sources of finance rather than be-

ing overburdened by one form of debt. Diversification of funding sources reduces dependence on individual lenders and reduces risk.

6. It considers the company's long-term strategy and the consistency of its financing with it. The long-term success of the financing depends on consistency in the company's overall strategy.

Proper debt financing planning, analysis, and implementation can help a company achieve successful results and financial stability. It is essential to be proactive, monitor market developments, and adjust the financial strategy in time to avoid unsuccessful scenarios.

Tips for Effective Debt Financing Management

Effective management of debt financing is critical to ensuring the stability and viability of a company. Some tips to help you manage your debt effectively are presented in table 4.1.

TABLE 4.1 Tips to Help You Manage Your Debt Effectively

Long-term plan	When planning debt financing, it is crucial to consider the company's long-term financing needs. Analyse your objectives, projects, and future needs and assess the appropriate debt structure, interest rates, and repayment periods consistent with your long-term strategy.
Diversifying sources of funding	Diversification of funding sources is essential to reducing risk. Do not limit yourself to a single lender or type of debt financing. Consider options such as bank loans, bond issues, asset finance, leasing, or alternative forms of debt financing.
Choose your lenders carefully	Before you decide to finance your debt, check the quality and reliability of the lenders. Consider their business reputation, financial stability, loan terms and interest rates. Choose lenders that are professional, reliable and offer good terms.
Liquidity management	Make sure you have enough liquidity to repay your debt on time. Monitor your cash flows carefully, manage your short-term liabilities and plan your inflows and outflows of funds. Use liquidity management tools such as credit lines or emergency reserves where necessary.
Take interest rates into account	Keep an eye on interest rates and take advantage of refinancing opportunities when conditions are favourable. Be alert to changes in interest rates so you can adjust your debt management strategies in time.

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TABLE 4.1 *Continued from the previous page*

Risk management	Be aware of the risks associated with debt financing and take appropriate measures to manage them. You must assess financial risk, carry out stress tests, implement risk management policies, and be prepared for adverse scenarios. Consider using collateral such as guarantees, mortgages, or sureties to mitigate risks and increase lenders' confidence.
Track and report	Regularly monitor your financial position, cash flows, debt repayment obligations, and other vital indicators. Be aware of any changes affecting your ability to repay your debt. Report your company's financial situation to lenders and investors promptly and be transparent about your financial performance.
Communicate with lenders	This open and proactive approach, where you plan and coordinate repayments, can improve trust between the company and the lenders. It is also beneficial to explain any changes in the business environment and present your debt management plans, which can facilitate any adjustment or reorganisation of the debt in case of difficulties.
Keep up to date with legislation and regulations	Familiarise yourself with the applicable laws and regulations on debt financing. Observe the obligations arising from these regulations, such as reporting requirements, interest rates, collateral or other restrictions. Adapt your procedures and policies to changes in legislation promptly.

NOTES Adapted from Brealey et al. (2020).

Effective debt financing management requires an integrated approach, including planning, monitoring, risk management, and communication. This advice will help you better manage debt, reduce risks, and achieve long-term financial stability for your business. Being proactive and flexible and assessing your financial needs and debt management strategies is essential.

Chapter Five

Investment Risks and Returns: The Relationship between Expected Gains and Losses

Considering the investment risks and returns is essential, as these two elements are vital in making investment decisions. The ratio of expected gains to losses helps us assess whether the potential return is adequately balanced by the risk we are taking.

In the introductory section, we will examine the concepts of investment risk and return and focus on their relationship. First, we will define investment risk as the possibility of losing or not meeting the expected return on a given investment. We will then focus on profitability, representing an investment's expected gains or returns.

Understanding the relationship between investment risks and returns is critical. High-risk investments tend to yield potentially higher returns, while lower-risk investments tend to produce lower returns. This risk-return relationship is essential for assessing investment opportunities and selecting an appropriate investment strategy.

Understanding your financial profile, risk tolerance, and investment objectives is crucial when making investment decisions. Portfolio diversity can also reduce overall risk.

Investment Risks

Investment risks refer to the possibility of a loss of value or return on an investment due to various factors. This uncertainty occurs when investing in different forms of assets, such as shares, bonds, real estate, commodities, etc. Investment risks come from various sources, including economic conditions, political instability, regulatory changes, natural disasters, and liquidity risks.

Investment risks are different and can be measured in various ways. The most common types of investment risk are market risk, which arises from changes in market prices; liquidity risk, which relates to the difficulty of selling an investment and converting it into cash; credit risk, which relates to the possibility of default by the debtor, and oper-

ational risk, which arises from factors associated with the operation of the business or the investment.

Investment risks are measured using various methods such as standard deviation, beta coefficient and value-at-risk (VaR). These methods allow us to estimate the probability of a loss or decline in the value of an investment over a given period.

Investment risk management is an essential aspect of the investment process. It involves assessing and managing risks and deciding on the allocation of assets in an investment portfolio. You can feel more secure about your investment decisions by actively managing risks. Portfolio diversification, which involves investing in different types of investments, is one strategy to reduce investment risks.

Investment decisions should also consider investment risks. Higher risks tend to yield potentially higher returns, but the risk of loss increases. Therefore, it is essential to understand and assess investment risks and integrate them into investment planning and decision-making.

Return on Investment

Return on investment refers to the expected profits or returns that investors can expect from their investments. It measures an investment's performance and is critical to investment decision-making. The return on investment depends on several factors, including the type of investment, market conditions, and investment management.

Different types of investments may have other ways of calculating and measuring returns. Equity investments often use dividends and capital gains returns, while bond investments consider interest rates and yields to maturity. For real estate investments, profitability is related to rents and potential capital gains on sale.

When assessing the return on an investment, it is also essential to consider the risk associated with the investment. Higher risks tend to have higher expected returns, while lower-risk investments tend to have lower expected returns. Investors need to strike a balance between expected return and an acceptable level of risk in line with their investment objectives, time horizon and financial capacity.

The return on investment also depends on market conditions, the economic environment and general macroeconomic factors. Market movements, interest rates, inflation, political instability and other financial changes can affect investment returns.

Monitoring portfolio returns and regularly assessing their performance is essential to manage investments successfully. Investors can use different methods to measure returns, such as return on investment (ROI), return on equity (ROE), internal rate of return (IRR), and discounted cash value (NPV).

Return on investment is critical in investment decisions and should be carefully considered and assessed throughout the investment process.

Impact of the Risk/Return Ratio

The risk/reward ratio is critical to assessing an investment's attractiveness. It is the ratio of the expected return on an investment to the risk taken. Understanding this relationship is crucial for investors as it allows them to make more informed investment decisions and appropriately balance expected returns and acceptable risk.

Higher risk usually means a higher risk of loss or instability in investment returns. Investors willing to take higher risks also expect higher returns to compensate for that risk. This means a positive correlation exists between risk and expected return – higher levels of risk mean potentially higher returns, while less risky investments offer lower expected returns.

However, it should be noted that not all higher-risk investments always yield higher returns. Investment returns depend on several factors, including economic conditions, market trends, investment management, and other macroeconomic factors. Therefore, conducting a thorough risk-return analysis of each investment and assessing its suitability for the investment objectives, time horizon, and risk tolerance is essential.

Investors can use various methods to assess the risk-return trade-off, such as calculating a beta coefficient, which measures the sensitivity of an investment's value to changes in the market. The expected value and standard deviation concept is often used to assess an investment's expected return and risk.

Balancing risk and return consistent with a company's financial objectives, investment strategy, and risk tolerance is essential. Some investors are more inclined to take more risk for potentially higher returns, while others prefer less risky investments with lower but more stable returns.

The impact of risk-return is a critical factor in the investment process

and can help investors make investment decisions. Understanding this impact allows them to (Lim et al., 2021):

1. *Determining the appropriate investment strategy.* Investors can choose an investment strategy that aligns with their expectations, depending on their investment objectives, financial capacity, and risk tolerance. If they are riskier investors, they may opt for a more aggressive strategy involving higher-risk investments with the potential for higher returns. Conversely, more conservative investors prefer less risky investments with lower but more stable returns.
2. *Portfolio diversification.* The risk-return trade-off is essential in diversifying portfolio investments. Diversification allows you to reduce risk by investing in different types of investments and sectors. This creates a balanced portfolio that can reduce the adverse effects of potential losses on one investment with good returns on other assets.
3. *Risk management.* The risk-return trade-off is critical to risk management. Investors can choose different risk management strategies, such as using protective measures like insurance or low-risk investments. It is essential that investors understand the link between risk and return and take appropriate risk management measures.
4. *Monitoring and adjusting investments.* The risk-return trade-off should be regularly monitored, and investment performance have to be checked against expected returns and risk tolerance. If the risk-performance ratio improves or deteriorates, the investment strategy should be adjusted accordingly.

The risk-return trade-off is a crucial aspect of the investment process and can help investors achieve their objectives. However, it is essential to understand that there is no optimal risk-return level, as this will vary according to the individual investor and their specific needs.

Portfolio Diversification to Reduce Risk

Portfolio diversification is an approach that includes a wide range of investments such as shares, bonds, real estate, commodities, currencies, etc. Diversification aims to reduce investment risks by allocating assets to different investments and sectors. This allows for a more balanced portfolio with less sensitivity to losses on a single investment.

Critical aspects of portfolio diversification to mitigate risk include:

1. *Diversification of investments.* Diversification is based on the principle that different investments react differently to changes in the market. Thus, a gain on another can offset a negative effect on one investment. Diversification of investments reduces the impact of a particular event or trend on the portfolio as a whole.
2. *Investing in different asset classes.* Diversification involves investing in different asset classes, such as shares, bonds, real estate, commodities, etc. Each asset class has its characteristics and market behaviour, leading to greater diversification and reduced dependence on a particular market segment.
3. *Geographical diversification.* Diversification also includes geographical diversification of investments. Investments in different regions and countries can help reduce the impact of regional economic or political developments on the overall portfolio, reducing the risk of concentration in one geographical area.
4. *Sectoral management.* Investing in different sectors of the economy is another aspect of diversification. Different sectors may behave differently depending on economic conditions and trends. Appropriate diversification of investments across sectors can reduce the impact of sector underperformance on the overall portfolio.
5. *Achieving financial objectives.* Portfolio diversification depends on each investor's specific financial objectives. Investment diversification should be consistent with the investor's defined objectives, risk, timing, and needs.
6. *Regular portfolio adjustment.* Diversification is not static but requires regular monitoring and portfolio adjustment. Investors should regularly review their portfolios, assess the performance of their investments, and check that they are still meeting their objectives and risk profiles. Possible adjustments, such as reallocating assets or including new investments, are necessary to maintain adequate diversification.

Portfolio diversification is a vital strategy to reduce investment risk, as it allows diversification of assets and reduces exposure to individual risks. It helps to reduce volatility and increase portfolio stability over the long term. However, diversification does not provide complete

protection against losses and does not always guarantee the highest returns. Therefore, investors must carefully consider their objectives, time horizon, risk tolerance and financial capacity and adapt their diversification strategy to these factors.

Risk and Return Analysis Before Investment

Risk and return analysis is essential before investing, as it allows investors to assess the likelihood of loss or gain and make informed decisions. Different steps and factors that need to be considered are presented in table 5.1.

Risk and return analysis are vital parts of the investment process. They enable investors to make more informed decisions and reduce the chance of unexpected losses. They help build a balanced portfolio that meets the investor's objectives and needs. At the same time, they allow

TABLE 5.1 Risk and return analysis

Estimation of potential returns	Investors need to assess the expected return on their investments. This includes an estimate of the expected appreciation in the value of the investment, the expected dividends or interest that the investment will generate, and any capital gains on the sale of the investment. Long- and short-term market trends and the possibility of achieving the expected returns should also be considered.
Risk assessment	In addition to the potential returns, the risks associated with the investment should also be assessed. This includes identifying and assessing different types of risk, such as market, liquidity, credit, operational, and political risks. Understanding how these risks may materialise and their impact on the investment's value is essential.
Determining the risk-return trade-off	Investors must assess the relationship between the expected return and the risk taken. This helps them determine whether an investment is proportionately profitable for the risk they are taking. Higher risk usually requires higher expected returns, while less risky investments yield lower returns.
Use of analytical tools	Analytical tools and models that help quantify potential returns and risks may be helpful when analysing risk and return. This includes statistical techniques such as standard deviation to measure risk or discounted cash flows to estimate the future value of an investment.
Assessing the plausibility of scenarios	Investors can assess the likelihood of different scenarios and their impact on investment returns. This includes analysing macroeconomic factors, market trends, competition, and other relevant factors affecting the investment.

Continued on the next page

TABLE 5.1 *Continued from the previous page*

Portfolio management	Risk and return analysis are critical to effective investment portfolio management. Based on the analysis results, investors can adjust the composition of their portfolios. For example, if an investment is too risky for the expected returns, they can reduce or exclude it from their portfolio. They can also identify opportunities with a good risk-return profile and add such investments to their portfolio.
Understanding constraints and personal goals	When analysing risk and return, it is also essential to consider the investor's objectives and constraints. This includes timeframe, financial capacity to take risks, lifestyle, and other factors. Each investor may have different priorities and needs, so the risk-return analysis must be based on these circumstances.
Monitoring and adaptation	Risk and profitability analysis is not a one-off activity but requires continuous monitoring and adjustment. Market conditions, economic conditions and other factors can change, so the analysis must be regularly reviewed and updated. Investors should be prepared to adapt their investments and strategies to new information and changing circumstances.

NOTES Adapted from Lim et al. (2021).

investors to identify opportunities to generate returns while considering risks.

Investment Risk Management

Investment risk management is identifying, analysing and managing the risks associated with investment activities. This process aims to reduce the adverse effects of risks on investments and achieve more stable and predictable outcomes. Understanding how risks arise and how they can be effectively managed is essential. Some key aspects of investment risk management include (Hopkin, 2018):

1. *Identifying risks.* The first step in risk management is identifying potential risks that may affect investments. This includes identifying internal and external factors that may affect investment returns, such as market risks, credit risks, liquidity risks, operational risks, political risks, etc. Understanding which risks are relevant for each investment and their implications is essential.
2. *Risk analysis and assessment.* Once risks have been identified, a detailed analysis and evaluation of these risks must be carried out. This includes quantitative and qualitative analysis, using various tools and techniques to assess the likelihood and impact of the

risks on the investment. Understanding how risks can affect the profitability, liquidity and value of investments is essential.

3. *Risk management strategies.* Following the risk assessment, strategies should be developed to manage these risks. This includes implementing risk mitigation measures, transferring the risk to other parties (e.g., insurance), adopting measures to reduce exposure to the risk, developing alternative scenarios, and designing safeguards.
4. *Portfolio diversification.* Diversification is one of the effective risk management strategies for investments. It involves investing over different asset classes, sectors, and regions, reducing the concentration of risk on individual investments. If one investment proves to be inefficient, other investments in the portfolio can offset the losses.
5. *Monitoring and control.* Investment risk management requires continuous monitoring and control of risks. Investors should regularly assess the performance of investments and monitor any risk changes. Monitoring includes tracking market trends, analysing financial data, and monitoring news and events that may affect investments. Based on this information, appropriate risk management measures and portfolio adjustments should be taken where necessary.
6. *Time horizon management.* Investment risk management also includes time horizon management. Different investments have different time horizons, and risks may occur over shorter or longer time horizons. It is essential to understand how risks may vary depending on the time horizon and to take appropriate action accordingly. This includes acceptable levels of risk, asset timing, and adapting investment strategies to changes in the time horizon.
7. *Ongoing education and knowledge.* Managing investment risk also requires ongoing education and learning about risks, risk management, and investment strategies. Investors should be aware of new trends, practices, and instruments related to investment risk management. In doing so, they will be better equipped to make informed decisions and reduce their risk exposure.

Managing investment risks is crucial for investors as it helps reduce risks' negative impact on investments and achieve more stable results.

Investors can minimise losses and maximise return opportunities by adequately identifying, analysing, managing, and monitoring risks.

Comparison of Different Types of Investment

When comparing different types of investments, it is essential to consider several factors, including risk, profitability, liquidity and benefits. Here are some critical aspects of comparing different types of investments:

1. *Risk.* Investments vary according to the level of risk they involve. On the one hand, higher-risk investments, such as shares or real estate, have the potential for higher returns but are also more exposed to market fluctuations. Alternatively, there are lower-risk investments, such as bonds or deposits, which offer more stable returns but may also be less profitable than riskier investments.
2. *Returns.* Returns are an essential factor when comparing investments. Investors must assess each investment's expected returns and compare them with the investment objectives and risks taken. They must consider both the current returns, the historical performance of the investment, and the potential for future growth and profitability.
3. *Liquidity.* Liquidity refers to the ability to convert an investment into cash. Some investments, such as shares, bonds or investment funds, are more liquid, meaning they can be sold quickly at the current market price. Other assets like real estate or alternative investments may require more time or procedures to sell. Liquidity is significant because it affects the investor's ability to adapt his portfolio to changing needs or opportunities.
4. *Benefits.* Other benefits of individual investments should also be considered when comparing investments. For example, some investments may bring tax benefits such as tax relief or tax deferral on profits. Other investments may bring different benefits, such as acquiring an equity stake in a company or influencing management.

When comparing different types of investments, it is essential to consider each investor's investment objectives, needs, and risk tolerance. There is no one-size-fits-all rule that applies to all investors. When choosing investments, individuals should consider their finan-

cial objectives, time horizon, risk tolerance, and other personal circumstances. They should also monitor market developments and adjust the portfolio in light of new information available.

When comparing different types of investments, it is also advisable to use other methods and analysis tools, such as statistical indicators, risk assessment, calculating returns, and researching historical trends. Considering different scenarios and options that could affect future investments is also important.

Finally, it should be noted that portfolio diversification can be an effective risk mitigation strategy. It involves combining different types of investments with different risks and returns. Investors must pay attention to their investment objectives and make informed decisions about asset allocation for different investments.

When choosing investments, consulting experts such as financial advisers or investment analysts with knowledge and experience in these areas is a good idea. This will help you better understand and compare different types of investments and select the ones that best suit your financial goals and needs.

Impact of Global and Macroeconomic Factors on Risks and Profitability

Global and macroeconomic factors significantly impact risk and return on investment. These factors may include (Dimic et al., 2016):

1. *Economic growth.* Economic growth affects the return on investment, as a more robust economic environment usually leads to higher returns. Rapid economic growth can increase corporate profits, which has a positive impact on share values. Conversely, slow economic growth or a recession can reduce profits and investment returns.
2. *Interest rates.* Changes in interest rates affect the return on investments, especially bonds and bank deposits. Higher interest rates tend to increase bond yields, while lower interest rates reduce yields. Interest rates can also affect the value of currencies, indirectly affecting the return on investment in foreign currencies.
3. *Inflation.* The inflation rate affects the actual value of investment returns. High inflation reduces the purchasing power of returns, which hurts their actual value. Investments that can keep up with or even outperform inflation are usually preferable.

4. *Geopolitical events.* Political and geopolitical events such as political instability, wars, terrorism, or trade tensions can cause significant uncertainty in financial markets. This can lead to higher fluctuations in the value of investments and increased risk. Investors should be alert to such events and their potential impact on their investments.
5. *Currency risks.* Currency movements can significantly impact investment returns, especially for foreign currency investments. Changes in exchange rates can increase or decrease the return on assets; therefore, currency risk needs to be considered and managed accordingly.

When managing investments, it is essential to consider the impact of global and macroeconomic factors on risks and profitability. Investors should pay attention to current market conditions and monitor economic indicators, political and geopolitical developments and changes in monetary policy. Understanding the interrelationships between different factors and their impact on investments is also important.

Effective risk and return management include:

1. *Monitoring and analysing global and macroeconomic trends.* Investors should monitor economic data such as GDP, inflation, unemployment, interest rates, and trade agreements. Understanding these trends can help predict investment returns and manage risks.
2. *Diversifying investments.* Diversifying portfolios is an effective way to reduce risks and increase return opportunities. Investing across different sectors, regions, and asset types can reduce exposure to risks associated with specific areas or regions.
3. *Use of hedging strategies.* In the event of uncertainty or volatility in financial markets, it makes sense to use hedging strategies such as options, currency hedging, or derivatives. These strategies can help minimise losses or limit the negative impact of certain events on investments.
4. *Adjusting the portfolio to changes.* The investment portfolio must be adjusted in response to global and macroeconomic changes. This may include reallocating assets to more promising sectors or regions and adjusting return expectations to changing conditions.
5. *Continuing education and updating knowledge.* Global and macroe-

conomic factors constantly change, so staying informed and educated about new trends and developments is essential. This includes monitoring the financial media, attending seminars and conferences, and consulting experts who can provide insights into the current situation.

The impact of global and macroeconomic factors on risk and profitability is complex and dynamic. Investors who are well-informed and able to adapt their investments to these factors are more likely to achieve successful outcomes.

Chapter Six

Cost of Capital: How to Calculate the Cost of Financing and Manage Financial Resources

The cost of capital is critical in a company's financial management. It refers to the price it pays to finance its business activities. Understanding the cost of capital is essential for successfully managing financial resources and investment and financing decisions.

In this section, we will focus on the importance of calculating the cost of capital and how it can be correctly calculated. We will also look at how companies can effectively manage their financial resources to reduce their cost of capital and optimise their capital structure.

The first step in calculating capital cost is understanding its components. The cost of capital consists of the interest rate on debt and the required return on equity. Both elements play important roles in pricing, financing, and managing financial resources.

In addition to understanding the components of the cost of capital, appropriate calculation methods should be used. This section will present three standard methods: discounted cash flow, equity, and comparable entities. Each method has advantages and limitations, so choosing the appropriate method according to the company's specific circumstances is essential.

Once we are familiar with the cost of capital calculation, we can focus on managing financial resources. This includes optimising the capital structure, managing risk, and diversifying funding sources. By adequately managing its financial resources, a company can reduce its cost of capital, increase its economic stability and improve its ability to invest and finance its business activities.

In the remainder of this chapter, we will examine in more detail the methods used to calculate the cost of capital. We will also examine financial resource management practices and present examples of good practice. Understanding the cost of capital and managing financial resources effectively are critical to a company's long-term success and achieving its economic objectives.

The Cost of Capital and Its Importance

The capital cost represents an enterprise's price to obtain the financial resources needed for business activities. This concept is critical to understanding the value of capital and a firm's economic performance. The relevance of the cost of capital is multifaceted and affects different areas of a company's business.

First, the cost of capital is essential when making investment decisions. Companies need to assess the expected returns on their investments and compare them with the cost of capital. If the expected return is higher than the cost of capital, the investment may make sense. Conversely, if the price of capital is higher than the expected returns, the company may prefer to seek alternative investment opportunities or reduce its investments.

Second, the cost of capital influences a company's financing decisions. Companies may choose different sources of financing, such as equity, debt or hybrid instruments. The cost of capital helps a company assess which financing source is the most economical and appropriately balances its capital structure. A higher cost of capital can lead to higher interest costs on borrowings, which can affect the company's profitability.

Third, the cost of capital is essential for assessing the value of a company. Using a reasonable cost of equity in the discounted cash flow (DCF) calculation helps to determine the present value of a company's future cash flows. A higher cost of capital will reduce the present value of future cash flows and vice versa. This valuation is important when valuing a business for a sale, merger, asset acquisition or assessing the company's viability.

In addition to the above, the cost of capital also influences other financial decisions, such as determining the appropriate rate of return for project appraisals, designing dividend policies, managing risks and setting targets for capital structures.

A comprehensive understanding of the cost of capital is crucial for the financial management of a company. Effective management of the cost of capital can increase profitability, optimise the capital structure, reduce financial risks and improve the business's overall value. It is essential to remember that the cost of capital is not static but can vary according to changes in financial markets, economic conditions, the riskiness of a company's business and other factors.

Companies need to accurately estimate the cost of capital, consider-

ing the different sources of financing and their specific conditions. In general, equity has a higher capital cost than debt, as investors demand a higher return on equity risk. Conversely, debt has a fixed interest rate, which is determined by market interest rates and the company's creditworthiness. When calculating the cost of capital, the company's specific characteristics, such as its industry, size, market position, business risk, and credit rating, must also be considered. In addition, the expected returns and risks associated with the company's investments must be assessed appropriately.

Managing the cost of capital requires constant monitoring of financial markets, interest rates, changes in the economic environment and the risks associated with the company's activities. Companies can also use strategies to reduce the cost of capital, such as improving creditworthiness, reducing risks, diversifying sources of financing, using financial instruments to hedge risks and optimising capital structure.

A complete understanding of the cost of capital and how to manage it effectively is crucial to a company's financial performance. This enables companies to achieve lower financing costs, optimise their investments and create value for their owners and stakeholders.

Components of the Cost of Capital

The cost of capital consists of two essential elements: the interest rate on debt and the required return on equity. These two elements reflect the costs and expected returns associated with using specific sources of financing.

1. *Interest rate on debt.* This component of the cost of capital refers to the interest rate paid by the enterprise on debt, such as bank loans, bonds, or other forms of borrowing. Market interest rates and the enterprise's creditworthiness and riskiness determine the interest rate. A higher risk for the company usually means a higher interest rate demanded by lenders.
2. *ROCE.* The ROCE represents the expected return an entity's owners require to bear the risks associated with ownership. This component of the cost of capital is related to the expected returns that owners can achieve from alternative investments with the same risk. The required return on equity is often expressed as a return in the capital market or as a premium over the risk-free interest rate.

There are several methods for calculating each component of the cost of capital based on different models and approaches. The interest rate calculation on debt is usually based on current market interest rates, the company's creditworthiness and other relevant factors. The required return on equity can be calculated using various models such as the equity premium, discounted cash flow or comparable entities method.

It is essential to understand that the interest rate on debt and the required return on equity can vary between companies, industries and financial conditions. Understanding and calculating these components correctly is vital in determining a company's total cost of capital and making financial decisions such as investments, project financing or setting capital structure targets.

Methods of Calculating the Cost of Capital

Several methods can be used to calculate the cost of capital, depending on the specific circumstances of the company and the information available. Some standard methods for calculating the cost of capital include (Brealey et al., 2020):

1. *Discounted cash flow (DCF).* This method involves estimating an entity's future cash flows and using discounting to calculate the present value of those cash flows. An appropriate discount rate calculates the discounted value and represents the required return to investors. The discount rate consists of two components: the interest rate on debt and the required return on equity. This method is most commonly used in business valuation and investment decision-making.
2. *Capital Asset Pricing Method (CAPM).* The CAPM uses systematic risk to determine the required return on equity. Here, a formula includes a free interest rate, a risk premium and a company beta factor. The risk-free interest rate represents the return on investments with minimal risk, while the risk premium reflects the additional return investors expect from taking on risk. The beta factor of a company measures the sensitivity of share prices to market changes. The CAPM method focuses on the estimation of the required return on equity.
3. *Comparable companies' method.* In this method, the cost of capital is estimated based on comparable companies in the market. The

required return on equity is determined based on the average return of companies in comparable sectors and with similar risks. This method assumes that companies with the same risk have the same required return on equity.

Other approaches, such as adjusted discounted cash flow, multiplier methods, risk arbitrage, and others, can be used in addition to these methods. The choice of method depends on the availability of data, the industry, the data's reliability, and the company's risk assessment.

When calculating the cost of capital, appropriate input parameters based on qualitative information and a reasonable assessment of the risk associated with the company's activities must be considered. Current market interest rates, the company's creditworthiness, and the specific conditions and requirements of lenders must also be considered in determining the interest rate on debt. However, the required return on equity requires an assessment of the systematic risk associated with the company's activities, including economic and industry risk.

Managing Financial Resources

Financial resource management is the process of planning, directing, and controlling money in an organisation or business. It aims to manage money effectively and responsibly and achieve the organisation's financial objectives.

Financial asset management involves several activities, such as:

1. *Budgeting* determines income, expenditure and investments over a given period. Budgeting is critical to planning and controlling financial resources and making sound decisions.
2. *Cash flow management* is managing cash flow in an organisation. It involves monitoring cash inflows and outflows, managing receivables and payables, and providing liquidity to the organisation.
3. *Investment management* involves setting the investment strategy, selecting eligible investment instruments and monitoring investment returns. The objective is to achieve an optimal balance between risk and return.
4. *Financial reporting.* Preparing and presenting financial reports that provide an overview and analysis of an organisation's finan-

cial position. Financial reports are essential for internal management and external reporting.

5. *Control and audit.* The control and audit of financial resources include monitoring and verifying financial transactions and compliance with financial standards and regulations. This helps detect possible errors, fraud, or irregularities and improves internal controls.

Managing financial resources is crucial to an organisation's success. By managing financial resources effectively, an organisation can avoid financial difficulties, optimise profitability, and achieve its objectives.

The Impact of the Cost of Capital on a Company's Decisions

The cost of capital is a crucial factor influencing a company's decisions, representing the required return for investors or business owners. The impact of the cost of capital on a company's decisions can be divided into the following aspects:

1. *Investment decisions.* The cost of capital influences investment decisions in new projects or business opportunities. If the cost of capital is high, the company will be more cautious in its choice of investments and require a higher expected return to justify the cost. This may lead to the rejection of some projects with lower expected returns, or the company may look at alternative sources of finance with lower capital costs.
2. *Financial structure.* The cost of capital is also closely linked to the company's financial structure choice. Suppose the cost of debt (interest rate) is lower than the cost of equity (expected return on equity). In that case, the company is likely to choose debt financing as this will help to reduce the cost of capital and improve the return to owners. However, if the price of capital for the debt is too high, the company may finance it by issuing equity.
3. *Reinvesting dividends and profits.* The cost of capital is also essential when deciding whether to pay dividends and reinvest profits. If the price of capital is high, a company may prefer to reinvest profits in new projects with higher expected returns rather than pay dividends to owners. However, if the cost of capital is low, the company may prefer to pay dividends to its owners, as their expected return will exceed the cost of capital.

4. *Valuation of the company.* The cost of capital is also a critical factor in valuing a company. A higher cost of equity means that the company's expected cash flows will be less valuable, which may affect its value and market price.

Together, the cost of capital significantly impacts a company's decisions on investment choices, financing, dividend payouts and closing the company's value. A company needs to be aware of the cost of capital and consider it in its financial decisions, as this will affect its profitability, value and long-term performance. Proper management of the cost of capital will enable a company to optimise its financial structure, select suitable projects and create value for its owners.

Financial Asset Management in Practice

Financial resource management involves several processes and activities that are key to efficient and effective money management. Some examples of financial resource management in practice include:

1. *Budgeting.* Planning income, expenditures, and investments for a period. The organisation sets objectives and priorities and prepares a budget that ensures consistency between expected income and expenditure and allows for efficient resource use.
2. *Cash flow management.* Cash flow management involves monitoring and managing an organisation's cash inflows and outflows. This includes careful monitoring of receivables and payables, implementing measures to increase liquidity, and using appropriate financial instruments to manage risks.
3. *Investment management.* Investment management is setting investment strategies, selecting appropriate investment instruments, and monitoring the return and riskiness of investments. The organisation focuses on selecting investments that are consistent with its objectives, risk profiles and profitability.
4. *Financial reporting.* Financial reporting is a vital part of financial resource management, involving preparing and presenting an organisation's financial reports. These reports enable internal and external stakeholders to understand the organisation's financial position, monitor performance and make informed decisions.
5. *Analysis and control.* Analysis and control of financial data are essential for monitoring and assessing the effectiveness of finan-

cial resource management. This includes comparing actual results with planned results, identifying discrepancies, seeking improvements and adjusting financial resource management strategies and policies.

In addition to these activities, it is also essential to consider the laws and regulations governing the management of financial resources in a particular country or industry. In practice, financial resource management requires expertise and analytical skills.

Chapter Seven

Capital Structure: How to Allocate Different Sources of Funding

Capital structure is a critical element of a company's financial management. It refers to the allocation of economic resources between different sources of funding. The proper allocation and management of these sources of financing significantly impact a company's stability, profitability, and long-term performance.

A company faces many challenges and decisions when choosing a capital structure. Should it be financed by debt or equity? What is the most appropriate debt-equity ratio? How do you decide between different types of debt or equity issuance?

Proper capital structure has advantages. For example, debt can provide favourable interest rates and tax advantages, while equity brings flexibility and less financial risk. Finding the optimal balance between debt and equity that suits the company's specific needs and objectives is essential. However, an incorrect capital structure can have negative consequences. Excessive debt can increase financial risk and interest costs, while excessive equity can limit a company's growth.

This chapter will examine how to properly allocate and manage the different funding sources to achieve an optimal capital structure. We will also examine the various sources of financing, such as debt and equity, and the benefits and challenges they bring. We will also focus on financial analysis, which is crucial in deciding on the capital structure and adapting it to the company's objectives and market conditions.

Together, we will explore best practices and case studies to help us understand how to properly allocate and manage different funding sources to achieve an optimal capital structure. Finally, we will gain insight into the importance and impact of the proper capital structure on a company's long-term success and growth.

The Importance of Capital Structure

Capital structure is essential for any business, directly affecting its financial stability, profitability, liquidity, and long-term viability. Capital

structure refers to the allocation of financial resources between different sources of financing, particularly debt and equity.

Some critical aspects of the importance of capital structure include (Jensen & Meckling, 2019):

1. *Financial stability.* An appropriate capital structure can increase a company's financial stability. Proper debt-equity timing reduces the risk of insolvency and increases a company's ability to meet its financial obligations.
2. *Profitability.* A company's capital structure can affect its profitability. A favourable mix of debt and equity allows an optimal balance to be struck between the cost of financing and the expected return for business owners. The proper capital structure can also increase the return on equity.
3. *Liquidity.* A company's capital structure can also affect its liquidity. Excessive indebtedness can make raising new debt or managing cash flow difficult, leading to liquidity problems. A proper capital structure allows for adequate liquidity and cash flow management within the company.
4. *Access to finance.* An appropriate capital structure is essential for access to finance. A company with a stable and balanced capital structure can obtain loans on more favourable terms and attract potential investors.
5. *Flexibility and resilience.* A flexible capital structure gives a company greater flexibility to adapt to changes in market conditions, develop new projects or finance growth. The proper capital structure allows a company to adapt to different financial and business challenges.

The proper capital structure depends on the company's specific needs and objectives, market conditions, risk profile, and industry. Careful planning, analysis, and capital structure management are crucial to achieving financial stability, profitability, and success.

Different Sources of Funding

The different sources of finance are how companies obtain the necessary funds for their operations, investments and growth. Using suitable sources of finance is crucial to the success and development of a business. The primary sources of finance include:

1. *Debt* is one of companies' primary sources of finance. It includes loans from banks, bond issues or the use of credit lines. Companies can borrow to finance business activities, expand, purchase assets or improve their liquidity. Debt is usually repaid by interest and principal payments.
2. *Equity* is capital invested by a business's owners. This includes money invested by the company's founders or external investors such as business partners, venture capitalists, or public share sales. In return for equity, owners can participate in the company's profits and voting rights.
3. *Internal resources* of finance are those a company generates from its activities and resources. This includes profits the business generates that can be reinvested to finance growth, development, or investment. Internal sources of finance can also include savings through efficiency gains and optimisation of business processes.
4. *Donations* are funds that a company receives from various sources, such as the government, non-profit organisations, or international institutions. These funds are often used to support specific projects, research, innovation, or corporate social responsibility activities.
5. *Leasing and renting.* Companies can use leasing and renting to finance necessary assets such as vehicles, equipment or real estate. In this case, the enterprise pays periodic rental payments for using these assets without long-term equity liabilities.

The appropriate source of finance depends on the company's specific needs and objectives, risk profile, market conditions, and industry.

Debt Management

Debt management ensures a company's financial stability, liquidity and profitability. By managing debt properly, a company can optimise its financing costs, maintain good creditworthiness and ensure sufficient liquidity to meet its financial obligations. Some critical aspects of debt management are presented in table 7.1.

Debt management requires careful planning, risk analysis and decisions that align with the company's objectives and needs. Proper debt management enables a company to optimise its financing costs, maintain financial stability and achieve its business objectives.

TABLE 7.1 Critical Aspects of Debt Management

Debt planning	A company should plan its debt based on its financial needs, objectives, repayment period, and available resources. It is essential to assess the risk associated with using debt and adjust the plan according to the company's financial capacity.
Diversifying sources of funding	Diversification of funding sources reduces concentration risk and increases flexibility in debt management. A company can raise debt from various sources, such as banks, market debt (bonds), state aid or public subsidies.
Choice of appropriate interest rates and terms	When choosing a debt, it is essential to consider interest rates, approval costs, contractual terms and maturity of the debt. The company should seek the most favourable interest rates and terms and consider whether a fixed or variable interest rate is more appropriate to the company's long-term objectives and risk profiling.
Risk management	Debt can be associated with risks such as interest rate risk, currency risk, refinancing risk and liquidity risk. An entity should manage these risks through appropriate analysis and the use of financial instruments such as option contracts, hedging clauses, currency instruments or default reserves.
Debt control	Debt control involves regular monitoring of financial commitments, interest payments, and principal repayment according to agreed-upon terms. The company must maintain a good relationship with its lenders to ensure that obligations are met on time and that there is adequate cash flow to pay the debt.
Debt refinancing	In some cases, a company decides to refinance debt to improve financing terms, reduce costs or extend the maturity of the debt. Debt refinancing can be done by issuing new debt with more favourable terms than a lower interest rate or by replacing existing debt with another form of financing, such as issuing shares or selling assets.
Monitoring the debt profile	An entity should regularly monitor its debt profile, including debt-to-equity ratio, total debt, interest-bearing liabilities and debt maturity. This allows for the timely detection of potential imbalances or risks and the adjustment of debt management strategies.
Managing relationships with lenders	Maintaining good relations with lenders is critical to debt management. This includes informing them regularly, providing timely information, and meeting agreed-upon terms and financial commitments. Good communication with lenders builds trust and facilitates access to finance in the future.

NOTES Adapted from Okpala et al. (2019).

Equity Management

Equity management ensures a company's financial stability, profitability and long-term viability. Proper equity management enables a com-

pany to reap the benefits of equity financing and create value for its owners. Some critical aspects of equity management are presented in table 7.2. Proper equity management requires careful analysis, planning and monitoring of financial data, communication with investors and compliance with legal and regulatory requirements. This ensures the company's long-term success, increases owners' satisfaction and strengthens their confidence.

TABLE 7.2 Critical Aspects of Equity Management

Acquisition of equity	A company may raise capital by issuing new shares or attracting external investment. In this context, it is essential to determine the appropriate share value and ownership structure and to provide attractive investment opportunities for potential investors.
Dividend management	Dividends represent the share of profits paid to shareholders. Dividend management involves setting the appropriate level of dividends, considering the company's profitability, the need to reinvest profits for growth, and shareholders' expectations and wishes.
Managing the share issue	It is essential to manage the process of issuing new shares, including properly assessing capital needs, setting the correct share prices, selecting suitable investors, and complying with legal and regulatory requirements.
Monitoring the market value of shares	The market value of shares is an essential indicator of a company's performance and the satisfaction of its owners. Managing the market value of shares involves monitoring market trends, communicating effectively with investors and implementing measures to improve shareholder value, such as growth strategies, optimising business processes or improving profitability.
Management of voting rights	Shareholders also have voting rights, which they can use to decide on essential matters in the company, such as the election of the board of directors, strategic decisions, or amendments to the company's articles of association. Managing voting rights involves establishing proper governance, communicating with owners, and respecting their rights.
Maintaining owner satisfaction	Satisfied owners are the key to a company's long-term success. Equity management also includes ensuring owner satisfaction through regular information, transparent financial reporting, transparent decision-making and participation in critical strategic decisions.
Managing capital structures	Proper equity management also requires analysing and optimising a company's capital structures. This includes assessing the equity/debt ratio, selecting the optimal mix of equity and debt according to the business's needs, and managing the risks associated with different capital structures.

Continued on the next page

TABLE 7.2 *Continued from the previous page*

Managing strategic investors	When a company attracts strategic investors, it is essential to manage the relationship carefully. This includes setting clear objectives and communicating and participating in strategic plans that contributing to the company's long-term success.
Risk management	Equity management also requires managing the risks associated with equity financing. This includes assessing and managing risks related to the impact on the ownership structure, volatility of the market value of shares, uncertainty of profitability, and potential changes in corporate governance.

NOTES Adapted from Mathuva (2015).

Mixed Capital Structure

A mixed capital structure combines debt and equity in a company's financial structure. This approach allows a company to take advantage of the benefits of both financing sources and achieve an optimal balance between risk, financing costs and profitability.

Some critical aspects of the mixed capital structure include:

1. *Risk diversification.* A blended capital structure allows a company to reduce risk by sharing it between different funding sources. Although debt is associated with interest rate obligations and financial constraints, equity can contribute to more excellent stability and flexibility in risk management.
2. *Optimising the cost of funding.* A mixed capital structure allows a company to achieve the optimal mix of funding sources and thus optimise the cost of funding. Debt is usually cheaper than equity due to lower interest rates, while equity provides a lower cost than issuing new debt or refinancing existing debt.
3. *Flexibility and liquidity.* A mixed capital structure gives the company greater flexibility and liquidity. Debt allows the company to access funding for short-or long-term needs, while equity provides greater flexibility to manage business activities and adapt to market changes.
4. *Impact on the company's value.* A mixed capital structure can impact a company's market value. A properly balanced capital structure can increase a company's value and the satisfaction of its owners by optimising capital, financing growth, and improving profitability.

5. *Investor acceptance.* A mixed capital structure can increase a company's attractiveness to potential investors. A diversity of funding sources and a balanced capital structure give investors greater confidence in the company's financial stability and long-term viability.

When designing a blended capital structure, it is essential to consider the company's specific needs, objectives and risk profiling. It is also essential to consider industry standards, legal and regulatory requirements and the ability to service financial commitments. Achieving an optimal blended capital structure requires a comprehensive analysis, including assessing financial ratios, risk management and consideration of long-term business plans.

Companies can use different approaches to create a mixed capital structure. For example, they may pool debt and issue new shares to raise funds for investment and growth. They can also use existing sources of finance, such as internal resources or grants, together with debt or equity.

When managing a mixed capital structure, it is essential to consider the company's long-term objectives, funding needs, funding costs, risks and liquidity. It is also crucial to monitor financial ratios, manage risks and adjust the capital structure to reflect market changes and the company's internal needs.

Managing a mixed capital structure also requires regular monitoring, evaluation and adjustment in response to changes in the business environment, financial objectives and corporate needs. Careful management of a mixed capital structure enables a company to achieve the optimal mix of funding sources, ensure stability, liquidity and profitability, and create long-term value for owners and other stakeholders.

Financial Analysis of the Capital Structure

Financial capital structure analysis assesses and understands the allocation of financial resources in an enterprise, particularly between debt and equity. This analysis provides insight into an enterprise's financial stability, risks, profitability, and liquidity and helps make informed capital management decisions.

The following key indicators are commonly used in financial capital structure analysis (Liang et al., 2016):

1. *Debt-to-equity ratio* measures a company's debt-to-equity ratio. A

higher debt-to-equity ratio indicates a higher proportion of debt in the capital structure, which may imply a higher financial risk. A lower debt-to-equity ratio, on the other hand, indicates a higher proportion of equity, which may imply more excellent financial stability.

2. *Debt-to-assets ratio* measures the proportion of the company's balance sheet total that is debt. A higher debt-to-assets ratio indicates a higher proportion of debt in the company's total value, which may indicate increased financial risk and reduced liquidity. On the other hand, a lower debt-to-assets ratio indicates a lower debt-to-total value ratio, which may indicate more excellent financial stability.
3. *Return on equity (ROE)* measures the return a company generates for its owners on the capital it invests. A higher ROE indicates a higher return on capital and a higher value the company creates for its owners. Return on capital depends on the company's performance in generating profits relative to the capital invested.
4. *Return on assets (ROA)* measures a company's efficiency in using its assets to generate profit. A higher ROA indicates greater efficiency, which means better capital management and higher profitability. *Interest cost structure.* The analysis assesses the relationship between interest costs and the company's earnings. A higher proportion of interest expense in earnings indicates a greater reliance on debt and may imply a higher financial risk. Companies with a high-interest cost structure are more sensitive to changes in interest rates and find it more challenging to manage their financial liabilities.
5. *Comparing the cost of debt with the return on capital.* It is also essential to compare the cost of debt with the expected return on capital. If the cost of debt is higher than the expected return on capital, the company may not have used debt efficiently and should consider optimising its capital structure.

A financial analysis of the equity capital structure enables a company to understand better the financial relationships, risks, and profitability of using debt and equity. These analyses enable the company to make informed decisions on optimising its capital structure, reducing risk, improving profitability, and managing its financial resources. A proper

financial analysis of the capital structure is crucial for the company's long-term financial stability and success.

Adjusting the Capital Structure

Capital structure adjustment is changing the allocation of financial resources in an entity, particularly between debt and equity, in response to changes in the entity's circumstances, objectives, and needs. Properly adjusting the capital structure is essential to ensure financial stability, optimise the cost of funding, manage risks, and achieve the firm's long-term objectives.

The following aspects are taken into account when adjusting the capital structure (Graham et al., 2015):

1. *Financial needs analysis.* A company needs to assess its financial needs, such as investing for growth, expanding its business, buying assets or reducing debt. Depending on these needs, it may decide to raise new debt or issue new shares to meet its financing needs.
2. *Assessment of financial resources.* An entity needs to assess its financial resources and their availability. This includes assessing financial capacity, access to credit, available internal resources, and the potential to attract external investment or subsidies.
3. *Financing cost analysis.* Estimating the financing costs associated with the different sources of capital is essential. This includes interest rates, debt repayment terms, fees, share issue costs, or dividends. Analysing financing costs helps determine the most efficient capital structure.
4. *Risk management.* Risk management should also be considered when adjusting the capital structure. This includes assessing debt and equity risks such as interest rate, currency, illiquidity, and profitability risks. Adjustments to the capital structure may include reducing debt to reduce financial risk or increasing equity for stability.
5. *Adaptation to regulatory requirements.* When adapting the capital structure, it is also essential to consider regulatory requirements and restrictions imposed by legislation or regulators. The company must be aware of and comply with requirements and regulations relating to capital requirements, debt-to-capital ratios, minimum capital requirements or other regulations that may affect

the capital structure. Adjustments to the capital structure must comply with applicable rules and ensure compliance with legal and regulatory requirements.

6. *Stakeholder communication.* When adjusting the capital structure, it is essential to establish communication with the various stakeholders, such as owners, lenders, investors and regulators. Transparency, clarity, and openness regarding capital structure adjustment help build stakeholder trust and support.
7. *Long-term perspective.* The capital structure adjustment must also consider the company's long-term perspective and objectives. The capital structure must be consistent with the company's strategy and long-term plans for growth, development, and value creation for owners.

Adjusting the capital structure is a dynamic process that requires analysis, reflection, and prudence. To achieve an optimal capital structure, a company must consider various factors such as financing needs, costs, risks, legal requirements, and objectives. The proper capital structure adjustment can contribute to a company's financial stability, profitability, and long-term success.

Chapter Eight

Financial Analysis of Investment Decisions: How to Calculate Return, Risk and Other Key Indicators

Financial analysis is vital for assessing profitability, risk, and other essential factors in investment decisions. Companies must thoroughly assess potential financial outcomes and associated risks before investing in new projects or assets. Financial analysis of investment decisions involves calculating various vital indicators to assess the project's profitability, compare it with alternative options and manage risk. Critical indicators include net present value (NPV), internal rate of return (IRR), payback period (payment period) and others. In addition, the financial analysis also considers specific factors such as the tax impact, the time value of money, inflation and the opportunity cost of capital. These factors should be considered to ensure an accurate profitability and risk assessment and to make informed investment decisions.

The objective of financial analysis of investment decisions is to provide companies with a basis for making decisions based on prudent financial performance and risk assessment. Properly calculated indicators and comprehensive analysis allow a better understanding of the expected return on investment, identification of potential risks, and optimisation of the portfolio.

This chapter will focus on critical aspects of financial analysis of investment decisions, including methods for calculating returns and assessing risk. It will present essential indicators to help you make informed decisions and examine specific factors that should be considered.

The Importance of Financial Analysis for Investment Decisions

Financial analysis of investment decisions plays a crucial role in making informed investment decisions in a company. Its importance can be described in the following terms (Lee & Shin, 2018):

1. *Assessing profitability.* Financial analysis of investment decisions

allows assessing the expected return on investment. Properly carried out, this analysis allows future cash flows to be forecast and the profitability of a project or investment to be determined. This is crucial as it allows companies to identify the most profitable investment opportunities and select the projects that will generate the most added value.

2. *Identifying risks.* Financial analysis of investment decisions also helps to identify and assess the associated risks. This includes assessing operational, financial, market, regulatory, and other risks affecting an investment's performance. Proper risk analysis can help companies better understand potential risks and take appropriate management measures.
3. *Comparison of alternatives.* Financial analysis of investment decisions allows you to compare alternatives. Benchmarking can be used to determine which option has the highest return and the lowest risk. This helps the company choose between several projects or financing options and identify which projects have the best chance of achieving its objectives.
4. *Managing scarce resources.* Financial analysis of investment decisions contributes to efficiently managing scarce resources such as money, time, labour, and materials. The analysis assesses which projects will make the most efficient use of available resources and bring the most value to the company, preventing inefficient and ineffective resource use.
5. *Support for obtaining funding.* Financial analysis of investment decisions is crucial in attracting external funding. Investors, lenders, and other financial partners often require detailed financial analysis to demonstrate an investment's return potential and risks. High-quality financial analysis helps a company gain the trust and support of its financial partners and increases the likelihood of successfully raising the necessary finances.
6. *A tool for strategic planning.* Financial analysis of investment decisions is vital for strategic planning. The analysis helps a company assess the long-term implications of its investment decisions, identify the critical success factors, and choose the strategy that best serves its long-term objectives. This allows better resource targeting, business model adaptation, and the company's long-term performance optimisation.

Financial analysis of investment decisions is vital in assessing profitability, risk and other important investment factors. It helps companies select the most profitable projects, identify and manage risks, compare alternatives, manage scarce resources efficiently, and support financing. Proper financial analysis of investment decisions enables companies to make informed and well-informed decisions, contributing to the business's long-term success and sustainable growth.

Methods for Calculating Return on Investment

Different methods are used to calculate the return on investment, depending on the nature of the investment and the specific requirements. Some standard methods for calculating ROI include (Fernández, 2019):

1. *Net present value (NPV).* The NPV method is one of the most commonly used methods for calculating the return on an investment. This method considers the time value of money and estimates the present value of future cash flows, considering the required rate of return. A positive net present value indicates the investment is profitable, while a negative net present value indicates an unsuitable investment.
2. *Internal rate of return (IRR).* The IRR is the rate of return at which the net present value of an investment is zero. This method allows for calculating the rate of return and investment yields. If the IRR is higher than the required rate of return, the investment is profitable.
3. *Payback period.* The payback period measures the time it takes to recover the initial investment from future cash flows. This method focuses on the period needed to recover the investment. A shorter payback period indicates a more profitable investment.
4. *Discounted cash flow (DCF).* The DCF method uses discounting of future cash flows to calculate their present value. This method considers the time value of money and estimates the return on investment according to the required rate of return.
5. *Profitability index.* The profitability index is the ratio between the present value of future cash flows and the initial investment. This indicator measures the return on investment relative to the asset invested. A higher profitability index indicates a more profitable investment.

6. *Return on investment (ROI).* ROI is the profit to capital invested ratio. This method allows you to calculate the return on investment as a percentage. A higher ROI indicates a more profitable investment.

It is essential to understand that each method has advantages and limitations and can be used in different situations. The correct method for calculating the return on investment depends on the investment's specific circumstances and the company's requirements.

Methods for Assessing Investment Risk

Different methods are used to identify and quantify risks when assessing the risk of investments. Some common methods for assessing investment risk include (Aharoni, 2015):

1. *Sensitivity analysis* assesses how the expected return on investments varies according to changes in critical variables such as future cash flows, costs, selling prices, interest rates, etc.
2. *Scenario analysis* generates scenarios that consider possible developments. Each scenario represents a particular combination of variables and conditions and assesses their impact on the return on investment. This helps to identify and assess the risks in different scenarios.
3. *Monte Carlo simulation* is a statistical method that generates random samples from probability distributions of key variables. This allows us to estimate the probability of different investment outcomes and the risk based on many possible combinations of variables.
4. *Geographical risk analysis* is used in international investments to assess the risks associated with different countries, such as political instability, currency risks, legal framework, etc.
5. *SWOT analysis* (Strengths, Weaknesses, Opportunities, Threats) is a method that identifies the strengths and weaknesses of an investment and identifies opportunities and threats. This assesses the risk of an investment of internal and external factors affecting its performance.
6. *Historical data analysis* uses historical data on similar investments or industries to assess risk. Historical returns, trends, volatility

and past behaviour of similar investments are examined to help predict risk and assess investment performance.

Combining these methods allows for a more comprehensive assessment of investment risk. It is essential to understand that while no method is perfect or predictive of future events, combining several methods allows for a better understanding and assessment of investment risk. In addition to using these methods, collecting and accurately analysing relevant information and investment data is crucial. This includes examining market trends, competition, the regulatory environment, macroeconomic factors and other relevant information that could affect the performance of investments. When assessing investment risk, it is also essential to consider a company's personal preferences and risk tolerance. Each company has its unique approach to risk and objectives, so these factors must be considered.

Proper risk assessment is critical to making informed decisions and managing a company's investment portfolio effectively. It helps identify risks, manage unknowns, and create a favourable balance between expected return and acceptable risk. By properly assessing risk, a business can minimise the potential negative consequences of investments and achieve better outcomes and long-term performance.

Key Indicators for Financial Analysis of Investment Decisions

In the financial analysis of investment decisions, it is crucial to use effective indicators that comprehensively assess profitability, risk and other relevant investment factors. These indicators are valuable tools for companies to objectively assess and compare different investment options and support them in making informed decisions.

Critical indicators for the financial analysis of investment decisions are designed to allow a quantitative assessment of different aspects of an investment. This includes an assessment of the return, risk, time value of money, liquidity, and other factors that affect an investment's performance. Each indicator has specificities and provides unique information to help understand and evaluate investment opportunities.

This section will focus on critical indicators for the financial analysis of investment decisions, their use, and interpretation. These indicators will allow us to assess the profitability, risk, liquidity, and other critical aspects of investments, which will help us make more informed decisions.

It is essential to understand that each indicator represents only one part of the picture and that a comprehensive financial analysis of investments depends on combining several indicators. Indicators are a decision-support tool; other factors such as company strategy, specific objectives, risk tolerance, and other qualitative aspects should also be considered.

Appropriate indicators for the financial analysis of investment decisions provide companies with the valuable information they need to manage their investment portfolio successfully. They can identify profitable opportunities, manage risks and optimise their investment strategies. Below, we will examine the key indicators that help us achieve these objectives.

Net Present Value

Net Present Value (NPV) is one of the most commonly used and basic methods for assessing the profitability of investments. NPV measures the difference between the present value of the future cash flows generated by an investment and the value of the initial investment.

The net present value calculation considers the time value of money, which states that the value received in the future is less than the value received today. This concept is based on the idea that money held today has more value because it can be invested or used to generate returns.

The calculation of the net present value involves the following steps:

1. *Determining the expected cash flows.* The first step is to estimate the expected cash flows that the investment will generate. This includes the sales revenue, costs, taxes, and other relevant cash flows the investment will generate over a specified period.
2. *Discounting of cash flows.* In calculating the net present value, each expected cash flow is discounted to its present value using an appropriate discount rate. The discount rate is usually determined based on the investment risk and considers alternative equity returns.
3. *Sum of discounted cash flows.* All discounted cash flows are added together to give the net present value. A positive net present value indicates that the investment is profitable, as the expected revenues exceed the initial costs. However, a negative net present value indicates an unsuitable investment, as the initial costs exceed the expected revenues.

When making investment decisions, investments are usually accepted if their net present value is positive, as this means that they will generate more value than their cost. Otherwise, they are rejected.

Net present value can be a handy indicator when comparing different investment options, as it allows an objective assessment of their profitability. However, other factors such as risk, liquidity and company strategy should also be considered when making investment decisions.

Internal Rate of Return

The internal rate of return (IRR) is critical for assessing investments' profitability. The IRR is the rate of return at which an investment's net present value (NPV) is zero.

The internal rate of return is the rate earned on an investment, often expressed as a percentage. This method allows the comparison of different investment options and the assessment of their profitability relative to the required rate of return or alternative return on capital.

An iterative approach is used to calculate the internal rate of return when a rate of return is required at which the net present value is zero. This rate of return makes the expected investment income equal to the initial cost, which means that the value of the investment is preserved. The IRR can be found using financial calculators, computer programs or iterative methods such as the hopeless search, decision, or Newton-Raphson methods.

Once the internal rate of return has been calculated, it can be compared with the required rate or the minimum acceptable rate of return. If the internal rate of return is higher than the required rate of return, the investment is considered profitable. If the IRR is lower than the required rate of return, the investment shall be rejected.

IRR has some advantages and limitations. Advantages include considering the time value of money, ease of understanding and use, and its comparative nature, which allows for comparing different investment options. However, IRR does not consider the size of the investment or the absolute amounts of cash flows, which may lead to some limitations in the estimation of returns.

Despite its limitations, the IRR is an essential indicator for assessing the return on investment and is widely used in practice. Together with other indicators such as net present value, it provides a more comprehensive picture of investment performance and helps companies to make informed investment decisions.

Repayment Period

A method for assessing the profitability of investments that focuses on the period needed to recover the initial investment from future cash flows.

When calculating the payback time, we only consider the cash flows generated by the investment and do not consider factors such as the time value of money or discounting. The idea is to analyse how long it takes to recover the initial investment through the investment proceeds. The process of calculating the refund period usually involves the following steps:

1. *Determining the expected cash flows.* The first step is estimating the turnover, costs, and other cash flows the investment will generate. These cash flows must be net, i.e. all costs and taxes have already been deducted.
2. *Sum of cash flows.* The cash flows are combined to give the total sum of the cash flows the investment will generate each year.
3. *Calculation of the payback period.* The initial investment is divided by the average annual cash flow to give the payback period. This means calculating how many years it takes to recover the initial investment.

The payback period is often expressed in years but can also be expressed in months or other units, depending on the nature of the investment.

A commonly used guideline for investment decisions is that the return period is appropriate if it is shorter than a certain period acceptable for the return on the investment. A period that is specific to the industry or company is usually used.

The payback period is a simple method that allows companies to assess the return on their investment quickly. However, it also has limitations, as it does not consider the entire life cycle of the investment, the time value of money, and the return after the payback period. Therefore, it is usually used with other indicators, such as net present value, for a more comprehensive assessment of the investment.

Discount Coefficient

The discount factor is critical in financial analysis, estimating the value of future cash flows and money's time value. It represents the rate of return or discount used to identify the present value of future cash flows.

The discount factor reflects the alternative returns that the company could have achieved by investing in another project with the same level of risk. In general, the discount factor is determined by reference to two key components:

1. *Required rate of return.* This is the rate of return required by an undertaking to bear the risk of a financial investment. The required rate of return usually depends on the investment risk, industry standards, cost of capital, and other factors. A higher required rate of return usually means that higher-risk investments are less attractive.
2. *Inflation rate.* The inflation rate represents the increase in general market prices. If inflation rises, the value of money will be lower in the future than it is today. Therefore, the inflation rate is also used to calculate discounting to adjust future cash flows to their present value.

The discount factor calculates the present value of future cash flows. This process, called discounting, involves dividing the future cash flow by the value of the discount factor raised to the appropriate time power.

Choosing the correct discount factor is crucial to assessing an investment's value. If the discount factor is too high, the investment may appear unattractive despite having a high future return. Conversely, if the discount factor is too low, the investment may appear too attractive, even if it has a low future return.

The correct determination of the discount factor depends on the specific circumstances of the investment, including risk, industry trends, cost of capital and socio-economic factors. Using an appropriate discount factor is essential to correctly assess the value of investments and make informed financial decisions.

Rate of Return on Capital

Return on investment (ROI) is a financial indicator used to measure the return on investment relative to the capital invested. ROI is expressed as a percentage and shows the return on each capital invested.

The return on investment is usually calculated using the following formula:

$$\mathrm{ROI} = \frac{\textit{return on investment}}{\textit{invested capital}} \times 100. \tag{8.1}$$

The return on investment can be calculated as the difference be-

tween the income and the investment cost, considering the time frame and the corresponding cash flows. Capital employed represents the total amount of funds invested in an investment.

Return on investment is an essential indicator for assessing return on investment, making it easy to compare different investment options. A higher return indicates a higher return, while a lower rate indicates a lower return.

When using ROI, we need to keep in mind some limitations. ROI does not consider the time value of money, the duration of the investment or the risk associated with the investment. It also does not consider the scale of the investment or its long-term sustainability.

In addition, it should be noted that ROI is not the only indicator for assessing the return on investment. Other indicators such as net present value (NPV), internal rate of return (IRR), payback period (payment period) and others should also be considered in a comprehensive assessment. ROI is a valuable indicator for assessing return on investment. However, its limitations must be considered and combined with other financial indicators to get a comprehensive picture of ROI.

Sensitivity and Scenario Analysis

Sensitivity analysis and scenario analysis are two methods used in financial analysis to assess the impact of changes in critical variables on investment returns. Both methods help to understand risks and opportunities and to make more informed decisions.

1. *Sensitivity analysis* focuses on the impact of changes in one variable on the return on investment. It changes the values of single variables such as future cash flows, costs, selling prices, or interest rates and assesses the effects of these changes on investment returns. This tests an investment's sensitivity to changes in single variables and allows for assessing risk in adverse scenarios.
2. *Scenario analysis* focuses on examining the effect of a combination of variables on the return on investment. It creates different scenarios that consider different possible developments and combinations of variables. Each scenario represents a particular combination of variables and conditions and assesses their impact on the return on investment. This allows for a more comprehensive risk and opportunity assessment and helps to understand the impact of different variable combinations on investment returns.

Sensitivity analysis and scenario analysis can be instrumental in assessing the return on investment and making decisions. These methods identify the critical variables that have the most significant impact on investment performance and consider different scenarios that could affect it. This allows better preparation for potential changes and risks and timely investment strategy adjustment.

In addition, sensitivity analysis and scenario analysis can help communicate with key stakeholders by clearly presenting the different options and their impact on the investment. However, it should be noted that sensitivity analysis and scenario analysis are based on assumptions and estimates and cannot.

Risk Management in Investment Decisions

Risk management in investment decisions is crucial to reducing uncertainty and increasing the chances of investment success. With proper risk management, companies can better identify, assess, and manage the potential adverse effects of investments on their financial position and performance.

Some essential steps in managing risk in investment decisions include (Aharoni, 2015):

1. *Identifying the risks.* First, the potential risks of the investment must be identified and defined. This includes an analysis of the internal and external factors that may affect the investment. Internal factors include operational risks, financial risks, and human resources risks. External factors include market, regulatory, political, and other risks.
2. *Risk assessment.* Once risks are identified, their likelihood and potential impact on the investment should be assessed. This can be done using both quantitative and qualitative risk assessment methods. Quantitative methods include statistical analysis, modelling, and the use of data, while qualitative methods include expert judgment, expert opinion, and the use of experience.
3. *Developing risk management strategies.* Risk management strategies and measures should be developed based on a risk assessment. This may include adopting preventive measures to reduce the likelihood of risks, establishing systems for early detection and control, and using collateral or financial instruments to mitigate financial risks.

4. *Monitoring and control.* It is also essential to monitor and control risks throughout an investment's lifetime. This includes regularly monitoring key indicators, identifying risk changes, adapting risk management strategies, and taking measures to manage unforeseen risks.

In addition, it should be remembered that risk management is not a one-off process but an ongoing process. Risk management in investment decisions requires continuous monitoring and adaptation to changing circumstances and new information.

It is also essential to remember that it is not always possible to eliminate risks. Investments are usually associated with risks, as there is no guarantee of future results. However, risk management aims to minimise the adverse effects of risks on investments and maximise the chances of achieving the desired returns.

It is also crucial to risk management to involve all relevant stakeholders who impact the investment. This includes corporate governance, financial experts, risk experts, and other stakeholders. Collaboration and communication between stakeholders allow for a better understanding of the risks and joint risk management decisions.

Managing risk in investment decisions is crucial to a business's long-term success. Correctly identifying, assessing, and managing risks enables better asset management, reduced exposure to unwanted events, and a remarkable ability to adapt and take advantage of market opportunities.

It should be noted that risk management is not entirely foolproof and that unforeseen risks still exist. Therefore, it is important that investment decisions also consider other factors, such as the company's strategic objectives, the competitive environment, regulatory frameworks, and other factors that may affect the return on investment.

Taking Specific Factors into Account in the Financial Analysis of Investments

When analysing the financial performance of investments, it is essential to consider the specific factors that affect the return and risk of an investment. Each investment is unique and has its characteristics, and financial analysis should be tailored to these factors. Some vital specific factors to consider are (Brandstetter & Lehner, 2016):

1. *Industrial factors.* Different industries have different growth rates,

competitiveness, cyclicality, and risks. The financial analysis must consider each industry's specificities and trends and their impact on investments. For example, some companies in a fast-growing industry may have more potential for high returns but be exposed to higher risks.

2. *Market factors.* Market factor analysis examines market size, competition, demand and supply trends, and growth potential. Understanding market conditions is critical to assessing the potential return on investment. For example, investments in a growing market segment could be more profitable than those in a saturated market.
3. *Macroeconomic factors.* The financial analysis should consider the global and regional economic climate, interest rates, inflation, political stability, and other macroeconomic factors. These factors can affect cash flow, financing costs, demand for products or services, and the overall risk of investments.
4. *Company-specific factors.* Each company has specific characteristics, such as its business model, competitive advantage, management team, and financial position. These specific factors should be considered to assess whether a company has the potential to make a profitable investment. For example, a company with a well-established brand and a robust business model is likelier to achieve high returns.
5. *Legal and regulatory factors.* Legal and regulatory frameworks can significantly impact the profitability and risk of investments. This includes legislation on tax, environmental protection, workers' rights, industry standards, and other regulations. Understanding these factors is critical to adequately assessing costs and liabilities.
6. *Financial factors.* Financial factors such as cost of capital, interest rates, debt and capital levels, debt-equity ratios, and liquidity play an essential role in the financial analysis of investments. These factors affect the cost of funding, return on capital, capital structure, and the company's ability to adapt to market changes.
7. *Technological factors.* Technological change and innovation can significantly impact the return on investment. Technological advances can increase production efficiency, reduce costs, improve product quality, or open new market opportunities. Financial

analysis should assess how technological factors may affect future cash flows and return on investment.

When analysing the financial performance of an investment, it is essential to consider the specific factors relevant to a particular investment. This analysis allows a more accurate assessment of an investment's risk, return and sustainability. It is therefore advisable to involve experts from different fields in the analysis, who can contribute their knowledge and experience and provide a comprehensive understanding of the specific factors affecting the investment.

Examples of the Use of Financial Analysis for Investment Decisions

Examples show how financial analysis is used in different investment decisions. It helps to assess the return, risk and other important factors affecting an investment. It helps to make more informed investment decisions and contributes to the efficient management of financial resources. It is important to note that financial analysis is only one of many elements in investment decision-making. In addition to financial indicators, other aspects, such as the company's strategy, market conditions, competitiveness and social and environmental impacts, should also be considered. A holistic approach to investment analysis allows for a better understanding and assessment of potential opportunities and reduces risks in investment decision-making (DePamphilis, 2019):

1. *Estimating the profitability of a new project.* Financial analysis is used to estimate the profitability of a new project or business venture. For example, a company may use methods such as net present value (NPV) or internal rate of return (IRR) to estimate expected cash flows and return on investment. These results may be used to decide the feasibility of the project.
2. *Comparing alternative investment options.* Financial analysis is also used to compare options. A company can assess each option's expected returns, risks, and other key indicators to determine which financial investment is the most attractive. Comparisons can be made using methods such as net present value, internal rate of return, payback period, or viability indicators.
3. *Investment portfolio management.* Financial analysis is also used

to manage investment portfolios. Investors and asset managers can use financial analysis to assess the return and risk of different portfolio investments. Based on these results, they can decide whether to increase or decrease their exposure to individual investments or create a balanced portfolio.

4. *Valuation of the purchase or sale of a business.* When buying or selling a business, financial analysis is used to assess its value and the potential profitability of the transaction. For example, the valuation of a business may be based on the discounted cash flow (DCF) method, which considers expected cash flows and applies an appropriate discount rate. Such an analysis may lead to decisions to buy or sell a business.
5. *Assessing opportunities for expansion or diversification.* Financial analysis is also used to assess business expansion or diversification opportunities. The company can assess expected returns, risks, and other indicators for potential new markets, products, or business models. These assessments can lead to decisions on investments in new opportunities.

Chapter Nine

Rent Or Buy: How to Decide between Renting and Buying a Property for Your Business

Companies often face a significant dilemma when deciding between leasing and buying movable assets. Movable assets such as real estate, equipment, or rolling stock are vital parts of a business and can represent a significant financial contribution. The decision between leasing and purchasing movable assets can significantly affect a company's financial position, liquidity, and long-term strategy. Renting movable assets allows companies to obtain the necessary funds to operate without significant initial investments. Contractual arrangements allow a company to lease movable assets for a fixed period, providing greater flexibility and the possibility to update equipment. On the other hand, purchasing movable assets means long-term ownership and the possibility of long-term savings by avoiding recurrent rental costs.

When deciding between leasing and buying movable assets, various factors need to be taken into account, such as the business's financial viability, expected growth, the expected lifetime of the movable assets, tax considerations, flexibility, risk sensitivity, and the business's objectives. Each option has its advantages and pitfalls, so it is crucial to thoroughly consider and evaluate all aspects before making a final decision.

This section will explore the advantages and pitfalls of leasing and buying movable assets for a business. We will examine specific cases such as real estate, equipment, and rolling stock and analyse the key issues to consider when making decisions. In addition, we will look at the impact on the company's liquidity, risk management, and tax aspects of both options. The aim is to provide companies with a comprehensive insight into the decision-making process between leasing and purchasing movable assets so that they can make the most appropriate decision for their specific needs, objectives and circumstances.

Benefits of Renting a Movable Property

The benefits of leasing movable assets (Merrill, 2020):

1. *No sizeable initial outlay.* Renting movable assets allows companies to acquire the necessary equipment or space without a large initial outlay. Instead of paying the total purchase price, the company pays periodic rentals, which relieves financial pressure and allows better liquidity management.
2. *Flexibility.* Renting movable assets allows businesses greater flexibility. A company can adjust the rental volume to its current needs and adapt more quickly to changes in the business environment. The company also has the option to upgrade equipment or move to another location at the end of the rental period.
3. *Maintenance and repairs.* When renting movable property, it is often the landlord's responsibility to maintain and repair it. This can significantly reduce the company's costs by avoiding the cost of regular maintenance, upgrades, and repairs of the equipment.
4. *Faster access to new equipment.* Renting movable assets allows companies to acquire new equipment or space faster without lengthy purchasing processes. This is particularly useful in situations where it is necessary to upgrade or adapt quickly to business needs.
5. *Reduced risk of obsolescence.* Technology and business trends fluctuate rapidly. Renting movable assets allows companies to avoid the risk of equipment obsolescence, as they can upgrade or replace equipment at the end of the rental period.
6. *Tax benefits.* In some cases, renting out movable property can bring tax benefits. Rental payments can be treated as operating costs and deducted from the tax base, reducing the company's tax burden.

The benefits of leasing movable assets can give companies greater financial flexibility, adaptability, and risk reduction. However, the pitfalls and specific needs of the business must also be considered when deciding whether to lease movable assets. Each case is unique, so it is essential to consider all aspects and assess whether recruitment is the best option for the company's growth and success.

Traps for Renting Movable Property

Traps for renting movable property:

1. *Long-term costs.* While renting a movable asset requires a smaller initial investment, it may be a more expensive option in the long

run compared to buying. Over time, the total cost of renting may increase and exceed the cost of buying. In addition, landlords may charge additional costs such as maintenance, insurance or management costs.

2. *Limited adaptations.* The company's adaptations are limited to its requirements for renting movable property. The rental contract may restrict changes, upgrades, or adaptations to the equipment or space. This may limit the business's flexibility and affect its ability to adapt to changing needs.
3. *Limited control over the property.* The company does not have complete control over the property when it is rented. The owner of the movable property often has the right to inspect, impose certain restrictions on the use or even remove the equipment or space. This can affect the operational efficiency and flexibility of the business.
4. *Limited ownership and transfer of value.* When leasing movable property, the entity does not acquire an equity interest in the assets. This means that the enterprise cannot realise the potential value of the investment as it would be able to with a purchase. If the business grows and adds value, this value remains the lessor's property.
5. *Limited flexibility and constraints.* Renting movable assets can limit a company's flexibility regarding location, type of equipment, or other factors. The company is often tied to the contract period, and it is more difficult to terminate the lease or change the terms if needed.
6. *Failure to manage risks.* When leasing movable property, the company does not have complete control over the risks associated with owning the equipment or premises. For example, if equipment breaks down or is damaged, the lessor must repair or replace it. However, the company may be unable to influence the speed of repair or the choice of replacement equipment.

When deciding to lease movable assets, the pitfalls must also be carefully considered and assessed. The business's needs, financial capacity, long-term objectives, and operational requirements must be considered. Each company has unique characteristics, and the pitfalls of leasing movable assets may vary depending on the industry, the size of the company, and other factors.

A thorough cost-benefit analysis is essential when deciding whether

to lease movable property. This includes a comparative study of the costs of renting and buying, including consideration of maintenance, insurance, depreciation, and any associated tax benefits. The long-term value of the investment and the potential for future upgrades or relocations should also be considered.

It is also essential to consider the lease's legal and contractual aspects, including the lease period's length, renewal terms, the possibility of terminating the contract, and the rights and obligations of both parties. It is also advisable to check the landlord's reputation and reliability and, if necessary, consult a legal expert.

All these checks and analyses will enable the company to make a more informed decision about leasing movable property. This decision should consider long-term business objectives, financial stability, operational needs, and possible changes in the market. Companies may also opt for a hybrid approach, combining leasing and purchasing according to their needs.

A comprehensive analysis of the advantages and pitfalls of leasing movable assets is critical to making the right decision that will allow your business to make the most of its business needs and objectives.

Advantages of Buying Movable Property

The advantages of buying movable assets (Kirillova et al., 2015):

1. *Ownership and value.* The purchase of movable assets allows a company to become the owner of the equipment or space. This means that the business acquires long-term equity value and can benefit from any future appreciation in the value of the movable assets. In addition, the enterprise usually acquires the right to use, control and adapt the movable assets to its needs.
2. *More flexibility.* The company can use and adapt its assets without relying on external lessors by owning movable assets. It can adapt to business changes, company growth, or industry changes without restrictions on lease contracts.
3. *Long-term savings.* Although purchasing a movable asset requires a more significant initial investment, it can yield savings in the long term. Instead of periodic rentals, the company pays only the costs of maintenance, insurance, and possible renovation of the movable assets. This can lead to lower costs in the long term and improve the return on investment.

4. *Tax benefits.* Buying a movable property can also bring tax benefits. The cost of purchasing and maintaining movable property can be depreciated over time, reducing the company's tax base and thus reducing the tax burden. In addition, certain costs, such as interest on loans to purchase movable property, can be deducted from the tax base.
5. *Long-term use.* Purchasing movable assets allows the company to use and exploit them long-term and adapt them to its specific needs and requirements.
6. *Balance sheet impact.* Purchases of movable property can positively impact a company's balance sheet. Ownership of movable property is recognised as an asset on the balance sheet. It can increase the value of the business and improve its creditworthiness and reputation with business partners and investors.

Buying movable property has advantages, such as ownership, long-term savings, greater flexibility and the possibility of long-term use. It allows the company to gain greater control over the movable assets and to benefit from any future increase in value. It can also bring tax benefits and positively impact the company's balance sheet.

Certain factors must also be considered when deciding whether to buy movable assets, such as the company's financial capacity, long-term needs, the lifetime of the movable assets, maintenance, risks, and flexibility. The purchase cost should also be assessed, including financing, maintenance, insurance, and any additional costs associated with the ownership of the movable assets.

In addition, it is also important to consider alternatives to purchase, such as right-to-buy leases, which can offer certain advantages of a combination of ownership and lease.

It is essential to weigh the benefits of purchasing and leasing movable assets against the business's specific needs and objectives and assess the long-term benefits and costs. It is also essential to consider how the purchase affects the business's financial position, cash flow, operational efficiency, and overall strategy.

The right decision to lease or buy movable assets will depend on individual circumstances, company priorities, and long-term vision. A comprehensive financial, operational, and strategic analysis is essential to making an informed decision that best suits the company's needs and objectives.

Traps for Buying Movable Property

Traps for buying movable property:

1. *High initial investment.* Buying a movable asset requires a higher initial investment than renting. This can place a financial burden on a business, especially on smaller or start-up companies with insufficient funds to make the purchase.
2. *Depreciation of value.* Property, especially equipment, wears out and loses value over time. Purchasing a movable property means the enterprise bears the risk of depreciation and loss of value over its useful life. This may affect the company's balance sheet and require additional costs for maintenance and renewal of equipment.
3. *Technological obsolescence.* Technology is evolving rapidly in today's fast-changing business environment. Purchasing movable assets and incredibly technologically advanced equipment can carry the risk of obsolescence. A company may find itself with old and outdated equipment, which can affect its competitiveness and efficiency.
4. *Limited flexibility.* The purchase of movable assets can limit a company's ability to respond to changes in business needs. If the business is tied to a specific equipment or space, it may need to adapt or upgrade quickly. This may limit the company's ability to adapt to changes in the market or business opportunities.
5. *Financial risk.* The purchase of movable property represents a financial risk, as the company assumes responsibility for the maintenance, repair, and eventual replacement of the movable property in the event of failure or damage. This may entail unexpected costs that affect the company's liquidity and financial situation.
6. *Restricted access to newer equipment.* The company can restrict the purchase of movable property in terms of access to newer and more advanced equipment. As the purchase is a long-term investment, the company may need more resources to upgrade equipment frequently or to acquire the latest technological solutions, which may affect the company's competitiveness.

The specific needs of the company, its long-term objectives, and its financial capacity should also be considered when deciding whether to buy movable property. The following pitfalls should also be carefully

considered when deciding whether to purchase movable assets (Hammond et al., 2015):

1. *Write-off.* A write-off procedure must also be followed when purchasing a movable property. Movable property has a limited useful life, and its value decreases over time. The Company follows the rules and guidelines for the write-off of movable property by accounting standards. This may impact the balance sheet and the presentation of the Company's financial results.
2. *Limited lifetime.* The asset's life expectancy must be considered when buying movable assets. In some cases, the valuable life of movable assets may be shorter than expected, or unforeseen circumstances may arise that affect their useful life. This may mean that the entity will need help to realise the total value of the investment.
3. *Liquidity risks.* Purchasing movable property means tying up capital in equipment or space, which can affect a company's liquidity. If a company needs quick liquidity or funds for other investments, selling the movable assets or converting them into cash may be difficult.
4. *Responsibility for maintenance.* The purchase of movable assets means that the company takes responsibility for the maintenance and repair of the equipment. This requires extra effort, cost and skills to ensure that the movable assets function and are adequately maintained during their useful life.
5. *Limited flexibility to meet changing needs.* Purchasing movable assets can limit a company's flexibility to change its needs. If a business needs to change or grow, it may become apparent that the movable assets no longer meet its requirements. This may require additional costs for upgrading or replacing movable assets.
6. *Risk of obsolescence.* Any technology can quickly make purchased movable property obsolete. Technological advances can bring new, better, and more efficient solutions. If a company decides to buy equipment, there is a risk that the equipment will quickly become obsolete, which can affect the company's efficiency, competitiveness, and profitability.

Companies should be aware of these pitfalls and carefully consider them when purchasing movable assets. A thorough cost-benefit analy-

sis is essential, including purchase costs, maintenance, repairs, insurance and possible upgrades. The business's specific needs, long-term objectives, financial stability and risks should also be considered.

Businesses must know that purchasing movable assets entails a long-term commitment and responsibility. Therefore, it is important to consider alternatives, such as right-to-buy leases, which can offer some benefits of a combination of ownership and leasing.

When deciding whether to purchase movable assets, a comprehensive analysis should be carried out, considering financial, operational, strategic, and environmental aspects. A company should weigh the benefits and pitfalls, assess the long-term benefits and costs, and assess the impact on the balance sheet, cash flow, operational efficiency, and overall corporate strategy. The right decision to buy movable assets will depend on individual circumstances, company priorities, and long-term vision. A company must conduct a thorough analysis and consider its specific needs and long-term objectives to make an informed decision that best serves its interests.

Comparative Cost Analysis

A comparative cost analysis between purchase and lease is critical when deciding these two options. It allows a company to compare the costs and benefits of both approaches and choose the most economical and profitable option.

When benchmarking costs between buying and renting, the following steps should be taken (Horton & Zeckhauser, 2016):

1. *Defining the options.* Select purchase and rental as the options you want to compare. For example, if you are considering equipment, consider buying and owning it or leasing it, where the company pays periodic rental fees for using the equipment.
2. *Specify the period.* Specify the period over which you will estimate the costs. This may be less than one year or longer, such as five years or more. Considering the lease contract length and the equipment's expected lifetime is essential.
3. *Identification and estimation of costs.* Prepare an identification and analysis of all associated costs for each option. For the purchase of equipment, include the cost of purchase, maintenance, insurance, repair, refurbishment and any additional costs associated with ownership of the equipment. However, equipment, rentals,

maintenance costs, insurance, and all other costs related to the lease should be considered when leasing.

4. *Evaluating the benefits.* In addition to the costs, it is essential to consider the benefits of the different options. When buying equipment, the benefits are ownership, flexibility in use, upgradability, and the possibility of selling in the future. When leasing equipment, the benefits are lower initial investment, lower maintenance costs, and greater flexibility to adapt to changes in business needs.
5. *Discounting cash flows.* The time value of money should also be considered when benchmarking costs between purchase and lease. Discount cash flows that occur in the future at an appropriate discount rate to compare the costs and benefits of the two options.
6. *Analysis of the results.* After estimating the costs, benefits, and discounted cash flows, you can analyse the results of a cost benchmarking analysis between buying and renting. Find the option with the lowest cost or the best cost-benefit ratio that best suits your company's needs and objectives. Consider other factors such as risk, flexibility, long-term needs, and company strategy.

It is also essential to consider the company's specific circumstances in the benchmarking exercise. Each company has unique needs, objectives, financial stability, and other factors influencing buying or leasing movable assets. Therefore, a comprehensive analysis should be carried out that considers all relevant factors and the company's specific needs.

Comparative cost analysis between the purchase and lease of movable assets can be helpful in corporate decision-making. It allows a better understanding of both options' costs and benefits and helps make informed and rational decisions. A proper comparative cost analysis allows a company to choose the most optimal option according to its needs, objectives and financial capacity.

Impact on the Liquidity of the Company

The decision between buying and leasing movable assets can significantly impact a company's liquidity. Liquidity refers to a company's ability to meet its short-term financial obligations and to have sufficient cash to operate smoothly.

Impact on liquidity when purchasing movable property:

1. *Larger start-up.* Purchasing movable assets requires a more significant initial investment, as the company has to pay the total value of the asset, either in a lump sum or through financing. This can lead to a higher cash outflow from the business, affecting the available liquidity.
2. *Long-term capital commitment.* The purchase of movable assets implies a long-term commitment to the company's capital. Funds that could be used for other investments or to improve liquidity are tied up in movable assets, which may limit the liquid assets available to the company.
3. *Maintenance and repair costs.* Owning movable property means the company is responsible for maintenance and repairs. The cost of maintenance and repairs may impact the entity's available liquid assets, as funds must be set aside for this purpose.

Impact on liquidity in the leasing of movable property:

1. *Low initial investment.* Leasing movable property requires a lower initial investment than buying. This can make it easier to maintain the business's liquidity.
2. *More flexibility.* Renting movable assets gives your business more flexibility. The company can adapt to changes in the business environment without long-term commitments and capital ties, allowing better liquidity management and adaptation to the changing needs of the business.
3. *Lower maintenance costs.* Renting movable assets often involves maintenance by the landlord. This reduces maintenance costs that would otherwise drain the company's liquidity. The company only has to pay rent, while maintenance costs are still the lessor's responsibility.
4. *Easier upgrades and replacements.* Renting movable assets makes upgrading or replacing equipment easier if your business needs more advanced or customised equipment. A company can acquire newer, more efficient equipment to improve its liquidity and competitiveness by entering a new lease agreement.

When deciding between buying and leasing movable assets, it is essential to consider their impact on the company's liquidity. Liquidity is crucial for the smooth operation of the business and the fulfilment of financial obligations. Therefore, careful consideration should be given

to the company's cost, flexibility, long-term needs and economic capacity to determine which option better meets the company's liquidity requirements and objectives.

Flexibility and Long-Term Strategy

Flexibility and a long-term strategy are vital considerations when deciding between financing options. Both aspects play an essential role in achieving the company's objectives and adapting to changes in the business environment.

1. *Flexibility* refers to a company's ability to adapt to changing circumstances and requirements. When choosing between buying and leasing movable assets, it is essential to consider how flexible each option is about changes in the business environment, customer needs, technological advances, etc.
    - Leasing movable assets often offers more flexibility, as the company is not tied to a specific piece of equipment or space in the long term. The company can adapt its needs to market changes, business opportunities, and growth.
    - The purchase of movable assets may limit flexibility, as the company becomes the owner of the equipment and is tied to it in the long term. If the business's needs change or technology advances, movable assets may no longer be the optimal solution.
2. *Long-term strategy.* A company's long-term strategy is crucial when deciding on the financing of movable property. Long-term strategy refers to the company's vision and objectives and planning for the future.
    - If your long-term business strategy is to own movable assets for the long term and you benefit from the equipment throughout its lifetime, buying movable assets can be a sensible decision. This allows the company to take complete control of the equipment, adapt to its needs and potentially gain the real estate value of the movable asset.
    - However, if your long-term strategy is focused on flexibility, adapting quickly to change and using the latest technology, renting movable assets may be a better option. Renting gives the company access to the newest equipment, reduces financial risk and allows it to adapt to changes in the business environment.

When deciding between flexibility and a long-term strategy, it is essential to consider the company's specific needs and objectives and analyse the benefits and challenges of both aspects. The following elements should be taken into account:

1. *Business flexibility.* Flexibility is vital to a rapidly changing business environment. Renting movable assets allows a company to adapt the size or type of equipment to the moment's needs. This is particularly important in rapidly changing sectors, such as technology companies or companies in fast-growing industries.
2. *Financial flexibility.* Leasing movable assets can provide greater financial flexibility as it does not require a significant initial investment. This means less impact on the company's liquidity and greater cash availability for other essential activities such as growth, development or business opportunities.
3. *Technological flexibility.* Technological flexibility is essential in today's fast-changing business environment. Leasing movable assets allows businesses to access the latest technology without purchasing and making equipment obsolete. This makes a company more competitive and up-to-date compared to its competitors.
4. *Long-term strategy and ownership.* Buying and leasing movable assets is also linked to the company's long-term strategy. If the company's objective is to own and use movable assets long-term, purchasing is a sensible choice. However, it should be noted that technology is changing rapidly, and leasing movable assets may allow better adaptation to the company's long-term strategies.

When deciding between flexibility and a long-term strategy, the company's specific needs, objectives, and circumstances must be considered. Analysing costs, benefits, operational needs, technological trends, and financial capacity will help the company decide on the best option between leasing and purchasing movable assets.

Rent Tax and Depreciation

Rental tax and depreciation are two essential aspects to consider when deciding between buying and renting movable property. Both factors have financial and tax implications for the company.

1. *Rental tax.* When leasing movable property, a company usually pays rental payments, which can be treated as business expenses

and deducted from the company's tax base. The rental charge depends on each country's tax laws and may vary depending on the type of equipment, the duration of the lease and other factors. A company needs to consider the tax aspects of the lease and consult a tax professional to determine the appropriateness of the tax deduction.

2. *Depreciation.* The purchase of movable property also raises the issue of depreciation, which relates to the gradual spreading of the cost of the purchase over its useful life. Depreciation can reduce a company's tax base and thus reduce its tax liability. However, it should be borne in mind that the rules and rates of depreciation depend on the tax legislation and the type and duration of the asset. An enterprise should consider these when calculating the cost and tax consequences of acquiring movable property.

When deciding between buying and leasing movable property, rent tax and depreciation must be considered. Assessing how these two components affect the business's costs and tax liabilities is essential. The company should consult accounting and tax experts to properly assess both options' financial and tax implications and choose the most optimal option according to its needs, objectives, and tax considerations.

Specific Examples: Real Estate, Equipment, Rolling Stock

Certain aspects must be considered when deciding between buying and leasing certain movable assets, such as real estate, equipment and rolling stock. Examples for each category are given below.

1. *Real estate*
   - *Purchase.* If the company plans to use the property long-term and the expected return on investment is high, it may decide to purchase. Purchasing allows the company to own the property, make long-term investments, adapt the building to its needs, and potentially gain value.
   - *Lease.* If the company needs the property for a short period or changes in space needs are expected, leasing is a reasonable option. Leasing offers greater flexibility, lower initial costs, less risk and relieves the responsibility for maintenance and repairs.

2. *Equipment*
   - *Purchase.* If the equipment is vital to the company's long-term business, highly specialised, or provides a competitive advantage, the company may consider purchasing it. Purchasing allows ownership of the equipment, customisation to the business's needs, quality control, and the possibility of upgrading and selling it in the future.
   - *Lease.* Leasing is a viable option for specialised equipment that is often upgraded or quickly obsolete. It allows greater flexibility to account for changes in the business environment, reduced risk of obsolescence, cost-effectiveness, and easy access to the latest equipment.
3. *Fleet*
   - *Purchase.* If a company needs to use vehicles permanently and has long-term transport needs, purchasing vehicles is a viable option. Purchasing allows for vehicle ownership, increased flexibility, adaptation of the fleet to the company's needs, and the possibility of future vehicle sales.
   - *Renting.* Renting vehicles is a reasonable option when fleet flexibility, vehicle needs fluctuations, or the desire to control costs are needed. Hiring provides the flexibility to meet changing needs, reduce costs, improve financial predictability, and relieve the burden of maintenance and repairs.

In each case, the company's specificities, equipment and vehicle needs, and long-term objectives must be considered. Financial analysis, operational requirements, cost-effectiveness, flexibility, and risks are vital when deciding between purchasing and leasing.

In addition, other factors such as tax implications, financing options, risk management, and the need to preserve, sell, and acquire the assets being valued should also be considered. A comprehensive analysis and comparative assessment between purchase and lease in specific cases of movable assets will help the company make an informed decision consistent with its strategy and long-term development objectives.

Key Questions for the Decision

When deciding between buying and leasing movable assets, it is essential to consider some key questions that will help the company make an informed decision. Some of the critical issues that should be explored

TABLE 9.1 Critical Issues That Should be Explored When Deciding between Buying and Leasing Movable Assets

What are the long-term needs of the company	Find out whether the need for movable property is long-term or temporary. If a short-term need is expected, leasing movable property can offer more flexibility. However, in the case of long-term needs, purchasing movable assets may prove to be a more viable option.
What is the financial capacity of the company	Consider the financial capacity of the company to buy or lease movable property. Consider available sources, financing options, costs and possible tax implications. A comparative cost analysis will help you to assess which option is more financially advantageous and feasible for the company.
What is operational efficiency and flexibility	Consider how buying and leasing affect the company's operational efficiency. Consider flexibility about changes in needs, cost-effectiveness, maintenance, upgrades and replacement of movable assets. Ensure that the chosen option supports the company's operational processes in the best possible way.
How the decision fits in with the company's long-term strategy	Consider how the choice between buying and leasing movable assets fits into your company's long-term strategy. Check that the chosen option aligns with the company's vision, growth and development objectives. Also, the potential long-term liabilities associated with the selected option and opportunities to acquire valuable assets should be considered.
How the decision translates into risks and opportunities	Consider the risks and opportunities associated with buying and leasing movable property. Assess the financial, operational, legal and other risks both options pose while looking for potential growth opportunities.
What are the tax consequences	Consider the tax implications of choosing between buying and leasing movable property. Consider the depreciation and deduction of purchase costs and the tax benefits of leasing movable property. Consult a tax professional to understand how the choice translates into tax liabilities and benefits for the business.
What are the legal obligations and responsibilities	Consider the legal aspects of choosing between buying and leasing movable property. Check the legal obligations, contractual conditions and possible restrictions. Also, consider the potential legal costs and administrative procedures of your chosen option.

Continued on the next page

are presented in table 9.1. Analysing these critical issues will help the company gain a comprehensive insight into the different aspects and implications of the decision to buy or lease movable assets. It is essential to consider the company's specific needs, objectives, and circumstances and choose the option that best suits those needs and long-term objectives.

TABLE 9.1 *Continued from the previous page*

How the decision reflects the liquidity of the company	Analyse how buying and leasing movable assets affects a company's liquidity. Check the impact on available funds, cash flow and liquidity risk. You should consider the long-term financial needs of the business and ensure that the chosen option does not compromise liquidity and the ability to meet financial obligations.
How the decision is reflected in long-term value	Assess how the choice between buying and leasing movable assets affects the long-term value of the business. Check how the chosen option translates into the company's assets, sales and future fundraising. Ensure that the selected option supports the long-term growth and value of the business.

NOTES Adapted from Horton and Zeckhauser (2016).

Managing the Risks of Renting or Buying

Risk management is critical when deciding whether to rent or buy movable property. Both options present risks that must be identified, analysed and managed accordingly. The following are some of the aspects to be considered when managing the risks involved in leasing or purchasing movable property:

1. *Financial risk* refers to the possibility that an investment in the lease or purchase of movable property will not yield the expected financial benefits. It is essential to assess the costs, revenues, profitability and cash flow associated with the lease or purchase of movable property. Performing an economic analysis, including calculating the net present value (NPV), internal rate of return (IRR), and payback period (payback period), will help assess the financial risk.
2. *Operational risk* refers to the possibility that movable assets may not meet the business's operational needs or their use will cause problems or disruption. When leasing or purchasing movable assets, consideration is given to operational requirements, performance, quality, maintenance, delivery, and potential problems in use. Proper management of operational risks can reduce the likelihood of disruption and ensure business continuity.
3. *Legal risk* refers to the possibility that the lease or purchase of movable property may involve legal obligations, restrictions, or disputes. When leasing, it is essential to consider the lease agreements, the protection of the lessee's rights and obligations, and possible restrictions on use. When buying, it is essential to con-

sider property rights, contracts, warranties, and potential legal complications. Legal, due diligence and support can manage legal risks and reduce the likelihood of legal disputes.

4. *Technical risk* refers to the possibility that a movable asset will not function properly and will be subject to defects or obsolescence. The movable assets' technical condition, maintenance, and any restrictions on their use should be considered when leasing them. When purchasing, it is essential to check the quality, reliability and technical support of the movable property manufacturers or sellers. Adequate technical risk management includes regular maintenance, servicing and possible upgrades of the movable assets.
5. *Flexibility risk*: When leasing movable property, it is essential to consider whether the lessee will have enough flexibility to adapt to company needs changes. In the case of a purchase, it is necessary to assess whether the company can adjust and upgrade the movable assets in line with changes in the business environment. Managing flexibility risk involves assessing long-term needs, negotiating contract flexibility and considering the company's long-term development plans.

In managing the risks arising from the leasing or purchase of movable property, it is essential that an entity carries out a comprehensive analysis, identifies potential risks and takes appropriate action to manage them. This includes due diligence in the selection of lessors or vendors, consideration of contractual terms, compliance with technical and operational requirements, management of financial risks and compliance with legal and regulatory requirements. Appropriate risk management will enable the company to minimise potential negative consequences and achieve the desired benefits from leasing or purchasing movable assets.

Chapter Ten

Working Capital Policy: How to Manage Short-Term Financial Resources and Manage Risks

Working capital policy is a crucial aspect of a company's financial management, focusing on the efficient management of short-term financial resources and the management of the associated risks. Working capital represents the difference between a company's short-term assets, such as inventories and receivables, and its short-term liabilities. Working capital management is critical to maintaining a company's liquidity, ensuring day-to-day operations and managing the risks posed by the scale and time dynamics of the business.

Managing financial and working capital risks in the short term requires a comprehensive approach that includes optimising inventory levels, managing receivables and payables, and adequately managing liquidity, credit, and supply chain risks. In addition, conducting a financial analysis of working capital is essential to monitoring and analysing the effectiveness of the company's working capital policy and identifying opportunities for optimisation.

This chapter will look at critical aspects of working capital policy, including inventory management, receivables and payables, and the management of the associated risks. We will also examine the importance of financial analysis of working capital and how it can optimise working capital policy. Understanding and effectively implementing a working capital policy will help a company achieve liquidity stability, reduce risks and ensure a sustainable and successful business in the short term.

The Importance of Working Capital Policy

A working capital policy is crucial for a company's successful financial management. Working capital is managing a company's capital, linked to short-term assets such as inventories, accounts receivable, and current liabilities. A working capital policy sets out the strategy and guidelines for effectively managing these assets and risk management (Is-

mail, 2017). A working capital policy's primary importance is to ensure liquidity for the company. Proper management of inventories, accounts receivable, and accounts payable allows a company to have sufficient funds to meet short-term financial obligations such as paying suppliers, employee salaries, and other operating expenses. A proper working capital policy ensures that an undertaking maintains the liquidity stability essential for its smooth operation and fulfilling its obligations.

In addition to providing liquidity, the working capital policy also impacts the company's profitability. Efficient management of inventories, accounts receivable, and accounts payable allows for cost reduction, cash flow optimisation, and increased return on capital. Adequate inventory management reduces the cost of tied-up capital and the risk of obsolescence, while effective debt management ensures timely payment to customers and reduces exposure to credit risk. However, managing payables allows for the optimisation of supplier payment terms and avoids unnecessary financial burdens.

Working capital policy affects a company's reputation, liquidity, and profitability. Stable liquidity, timely compliance, and effective risk management increase customers, suppliers, and other business partners' confidence. This can lead to better business conditions, greater negotiation flexibility, and a more significant competitive advantage in the market.

This high level of importance requires a company to develop and implement an appropriate working capital policy. This includes setting objectives, strategies and guidelines for managing balances, receivables and payables. A proper working capital policy should be tailored to the enterprise's specific needs and characteristics and consistent with its strategy and business objectives. The key aspects to be considered when designing a working capital policy are (Ismail, 2017):

1. *Optimising stock levels.* Inventory management is essential to balance sufficient stocks for smooth operations and avoid over-consolidating capital in inventories. The working capital policy should set appropriate parameters for inventory control, such as optimal stock levels, ordering methods and inventory control.
2. *Receivables management.* Effective debt management is critical to reducing the risk of customer default and improving cash flow. The working capital policy should set guidelines for monitoring payment terms, implementing credit policies, collecting receiv-

ables, and using an appropriate methodology to assess customers' creditworthiness.

3. *Accounts payable management.* Proper management includes optimising delivery times, negotiating payment terms, using appropriate cash flow smoothing strategies, and effectively managing short-term funding sources. The working capital policy should set guidelines for payables management and establish good relations with business partners.
4. *Risk management.* The working capital policy should include measures to manage risks related to liquidity, credit, supply chain and other operational risks. This includes understanding and assessing risks and implementing appropriate management controls and procedures.
5. *Financial analysis.* The working capital policy also requires regular monitoring and analysis of financial indicators such as working time, working capital to sales ratio, average payment terms and other relevant indicators. Financial analysis allows the effectiveness of the working capital policy to be assessed and opportunities for improvement and optimisation to be identified.

A properly designed and implemented working capital policy significantly impacts a company's business performance. The key advantages and benefits of a working capital policy are (Mathuva, 2015):

1. *Increased liquidity.* Managing inventories, receivables, and payables by the working capital policy allows the company to be more liquid. This means the company has enough cash to meet its short-term financial obligations, pay suppliers, and keep its business running smoothly.
2. *Better cash flow.* Efficient working capital management leads to optimised cash flow. Reducing the time needed to convert inventories and receivables into cash and managing supplier payment terms allows for a better distribution of cash flows and a reduction in liquidity risk.
3. *Reducing finance costs.* A sound working capital policy helps reduce the costs associated with tied capital and credit. Optimising inventories reduces the need to finance inventories, debt management reduces the risk of default and credit risk, and accounts

payable management allows taking advantage of favourable supplier terms.

4. *Increasing return on capital.* Effective working capital management affects a company's return on capital. Reducing capital tied up in inventories and accounts receivable allows for better capital utilisation and increased profitability. In addition, optimising payment terms for deliveries and using short-term sources of finance can reduce the cost of capital and improve profitability.
5. *Risk management.* The working capital policy also allows for effectively managing liquidity, credit, and supply chain risks. With appropriate controls, procedures and analysis, the company can reduce the likelihood of negative consequences associated with these risks and better manage its financial stability.

Remember that working capital policy is not static; it adapts to business needs, the industry, the competitive environment, and business cycles. Regular monitoring, evaluation, and adaptation of working capital policy are essential to maintaining its benefits and effectiveness in a changing business environment.

In addition to the benefits associated with a working capital policy, it is essential to identify some challenges and risks a company may face in implementing it. The most common risks include:

1. *Unpredictable changes in demand.* Unexpected changes in demand for a firm's products or services can cause fluctuations in inventory and receivables. A firm needs to be able to adjust its working capital policy to respond effectively to changing conditions and maintain liquidity.
2. *Credit risk.* Customer defaults or difficulties collecting debts can negatively impact the company's financial stability. An effective working capital policy should include assessing customers' creditworthiness, monitoring payment terms, and applying an appropriate credit risk management methodology.
3. *Return on Inventories.* Optimized inventory management is critical to efficiently using capital and reducing costs. However, inadequate inventory management can lead to higher storage costs, stock obsolescence, or loss of value. The company also considers risks related to inflation, changes in commodity prices, or legislation.

4. *Supply chain risks.* Dependence on suppliers can be risky. A supplier must meet agreed deadlines or quality standards to ensure the company's performance is maintained. The working capital policy should consider the possibility of alternative suppliers, negotiate favourable payment terms, and monitor supplier reliability.

To manage risk successfully, it is essential that the company regularly monitors and analyses financial data, applies appropriate control mechanisms, builds good relationships with customers and suppliers, and adapts to the changing business environment. It is also essential to adjust the working capital policy to fit the business cycles, the industry, and the competitive environment. A company must be able to adapt its working capital policy to market conditions, changes in demand, technological developments and other factors affecting the business.

Managing short-term financial resources and managing risks in a working capital policy also requires active communication and cooperation between different departments and functions of the company, such as finance, procurement, sales and production. Only a holistic approach involving all key stakeholders can ensure the successful implementation of a working capital policy and achieve optimal results.

A working capital policy is essential for effectively managing short-term financial resources and the associated risks. A properly designed and implemented working capital policy enables an enterprise to maintain liquidity, improve cash flow, increase profitability and manage risks. An enterprise needs to consider its business's specific needs, objectives and characteristics and adapt its working capital policy to changes in market and business cycles. A company can achieve effective and efficient working capital management through appropriate control mechanisms, financial data analysis, interdepartmental cooperation and flexibility.

Working Capital Components

Working capital is an integral part of a company's financial resources and is crucial to its business. It consists of current assets such as inventories, trade receivables and current liabilities to suppliers and other business partners. The working capital policy focuses on efficiently managing these components to ensure smooth operations, liquidity and risk management.

The components of working capital are the fundamental building blocks that make up total working capital and influence a company's financial stability. Each component has its characteristics and affects the business in its own way. Understanding these elements is essential for successful working capital management.

This section examines the critical components of working capital, their definition, importance, and impact on a company's performance. We will review balances, receivables, and current liabilities and examine their characteristics, challenges, and relevance to working capital management. Understanding these components will enable us to manage the company's financial position better, optimise liquidity, and reduce risks.

In the following, we will examine each component of working capital and explore its role, importance, and the challenges that companies face in managing it.

Stocks

Inventories are critical components of working capital. They represent physical or tangible goods a company holds in stock for sale or use in production. These may include raw materials, semi-finished goods, finished goods, or products for sale.

Proper inventory management is essential for the efficient operation of a business. It directly impacts business processes, costs, liquidity and customer satisfaction. Excessive inventories can increase storage costs, the risk of obsolescence or the loss of stock value. On the other hand, stock shortages can lead to a lack of demand, lost sales and customer dissatisfaction.

Several factors must be considered when managing inventories. These include determining optimal stock levels, monitoring demand and sales trends, effectively planning orders, applying stock valuation methods, and implementing appropriate control mechanisms to prevent theft or damage to stock.

In addition, seasonal changes in demand, market trends, supplier discount policies and possible changes in raw material prices or legislation should also be considered. Effective inventory management requires close cooperation between the purchasing, production, sales and finance departments to balance inventory availability and the cost of tied capital.

Inventory analysis involves monitoring key indicators such as stock

turnaround times, average stock age, turnaround period, and storage costs. A company can identify potential improvements, optimise stock levels, and reduce associated costs and risks with proper analysis and appropriate methods.

Inventory management is a complex process that requires constant monitoring, adjustment, and optimisation. Proper inventory management enables better use of capital, improved liquidity, reduced risks, and increased customer satisfaction. This gives the company a competitive advantage and increases its stability and performance.

Claims

Accounts receivable represent financial receivables due from customers for selling goods or services on credit. This means that the entity allows customers to pay for goods or services within a specified period after the purchase. Receivables are a current asset and an essential part of an enterprise's working capital.

Receivables management is critical to ensuring a company's liquidity and financial stability. Effective receivables management involves several aspects, including setting credit terms, assessing customers' creditworthiness, monitoring payment terms, collecting receivables, and applying an appropriate credit risk management methodology.

Several factors must be considered when setting credit terms, such as customers' financial stability, credit history, credit rating, and payment terms. The company needs to set optimal terms that allow customers to pay within the agreed timeframe while minimising the risk of default.

Monitoring payment deadlines is crucial to identify any late payments in time. The company shall implement an effective system to monitor and manage payment terms to reduce the risk of default and improve liquidity.

Debt recovery is an essential step in managing receivables. In the event of late payment, immediate action must be taken and procedures implemented to recover debts. This includes communication with customers, reminders, legal guidelines, and, as a last resort, cooperation with the enforcement authority.

Managing receivables requires using an appropriate credit risk management methodology. This may include credit insurance, guarantees or advances, and monitoring customer financial indicators.

Claim analysis includes monitoring key indicators such as aver-

age payment terms, default rates, claim age, and losses due to non-payment. Proper analysis allows a company to identify risks, improve its debt management processes, and optimise its recovery approaches.

Effective debt management brings many advantages and benefits to a company:

1. *Increased liquidity.* Proper receivables management allows better cash flow management and improves the company's liquidity. Timely payment of receivables allows the company to obtain funds to finance operations, meet obligations, and smooth business processes.
2. *Reducing default risk.* A proper process for checking customers' creditworthiness and using correct credit terms reduces the risk of default. This helps maintain the company's financial stability and reduces default losses.
3. *Improved return on capital.* Receivables management enables the company to improve its return on capital. Reducing the time of late payments, reducing the risk of default and enhancing the efficiency of collection procedures contribute to improved profitability and more efficient use of capital.
4. *Strengthening customer relations.* Timely and effective debt management increases customer confidence and improves customer relations. The company establishes itself as a reliable business partner by meeting obligations on time and proactively resolving potential payment problems.
5. *Reduction of financial costs.* Receivables management also impacts the company's financial costs. Reducing late payments and losses due to defaults reduces financing costs and improves the company's profitability and performance.

The company should use appropriate methods and approaches to manage its receivables effectively. This includes establishing clear policies and procedures for granting credit, regularly monitoring payment deadlines, using effective collection systems and continuously improving procedures based on the analysis of financial data.

Effective receivables management is essential for a company's liquidity, financial stability, and performance. Critical elements in managing receivables are correctly setting credit terms, monitoring payment rolls, collecting debts, and applying an appropriate credit risk manage-

ment methodology. A company should have clear debt management policies and procedures tailored to its industry, customers, and business objectives.

Managing receivables also requires close cooperation between the company's various departments and functions, such as sales, finance, purchasing, and collections. Interdepartmental collaboration is critical to promptly identifying potential risks, improving customer communication, and efficiently carrying out collection procedures.

In addition, continuous monitoring and analysis of critical receivables indicators such as average payment terms, delinquency rates, receivable ageing, and losses due to defaults are also necessary. This allows the company to identify trends, potential problems, and necessary adjustments to its debt management policy.

Debt management is a dynamic process that requires constant adaptation and improvement. The entity should proactively identify and manage risks, work with customers to resolve potential payment problems and apply appropriate credit risk management methods.

Receivables management is essential for a company's liquidity, financial stability and performance. Effective receivables management involves setting optimal credit terms, monitoring payment terms, collecting receivables and applying an appropriate credit risk management methodology. By managing receivables appropriately, the company ensures timely payments, improves liquidity, reduces default risk, and builds strong customer relationships. The company maintains its competitive advantage and achieves better financial results by continuously monitoring, analysing and adapting its debt management policy.

Obligations

Liabilities represent the amount of money an entity must pay its suppliers, business partners, or other creditors for goods, services, or other financial obligations received. They are integral to working capital and affect an enterprise's financial stability and liquidity.

Accounts payable management is crucial in ensuring timely payments and maintaining good relations with business partners. Proper accounts payable management includes setting and meeting payment terms, monitoring payment deadlines, coordinating with business partners and optimising cash flow.

The company and its business partners' interests must be consid-

ered when setting payment terms. A balance must be struck between ensuring favourable conditions for business partners and maintaining the company's financial stability. This may include agreed-upon payment terms, discounts for early payment, or other benefits to encourage prompt payment.

Monitoring payment deadlines is essential to ensuring that obligations are met on time. The company must have a system to monitor and track payment deadlines that allow for the timely identification of possible delays. In the event of delays, immediate steps must be taken to agree on new payment deadlines and, where necessary, establish effective recovery procedures.

Coordination with business partners is critical to building and maintaining a good relationship. Regular communication, cooperation, and coordination of payment terms help improve relations and ensure long-term cooperation.

Optimising cash flow is an essential objective in liability management. This includes paying liabilities on time, taking advantage of early payments, and optimising payment schedules to improve the company's liquidity and cash flow.

The analysis of commitments includes monitoring key indicators such as average payment terms, the proportion of late payments, and the cost of commitments. Proper analysis and application of appropriate methodologies can help a company identify opportunities to improve liability management, reduce costs, and optimise its financial position.

Accounts payable management brings many advantages and benefits to the company:

1. *Ensuring liquidity.* Proper liability management allows payment obligations to be met on time and the company to remain liquid. This ensures smooth operations, meeting obligations to suppliers and business partners, and maintaining the company's good reputation in the market.
2. *Strengthening relationships with business partners.* Meeting commitments correctly and on time strengthens relationships with business partners. This increases trust, reliability, and the company's reputation, leading to long-term cooperation, better negotiations, and more favourable business terms.
3. *Benefits and discounts.* Liability management can also bring bene-

fits through benefits and discounts. Timely payment allows the company to benefit from early payment, reducing purchasing costs, improving profitability and increasing competitive advantage.

4. *Reduce financing costs.* timely compliance reduces the need for external financing or loans, which can minimise financing and interest costs. In doing so, the company retains much of its profits and improves its financial stability.
5. *Risk management.* Liabilities are crucial to managing non-payment risks. Timely monitoring and action in the event of late payments or payment difficulties allow for reducing default and loss risks and better-managing business risks.

Liability management is essential to ensure liquidity, maintain good relations with business partners, reduce costs and manage risks. Timely fulfilment of payment obligations, optimisation of payment terms, coordination with business partners and continuous monitoring and analysis of liabilities are essential steps in effective liability management. A company can achieve better financial performance, increased liquidity, and improved business results with suitable approaches and methods. Key aspects of effective liability management include:

1. *Determining optimal payment terms.* The company must set payment terms consistent with its business strategy and financial stability. This includes setting appropriate payment terms, considering early payment discounts and flexibility to meet specific customer needs.
2. *Monitoring and controlling payment deadlines.* The company must set up a system to monitor payment deadlines and regularly check that customers meet the agreed deadlines. In the event of delays, immediate action should be taken, and communication with the customer should be established to resolve any problems.
3. *Optimising payment terms.* A company can optimise its payment terms by taking advantage of early payment or agreeing to tailored payment terms with its business partners. This can reduce the financial burden and improve the company's cash flow.
4. *Liaising with suppliers.* Close cooperation is essential in managing commitments. Agreeing on benefits, communicating transparently, and establishing long-term relationships with suppliers

can result in better payment terms, higher discounts, or preferential pricing.

5. *Effective communication and dispute resolution.* The company must have an effective dispute resolution process in case of any disputes or payment problems. Clear and open communication with customers and timely identification and resolution of issues can help maintain good business relations.

Liability management is essential to maintain liquidity, build good relationships with business partners and mitigate risks. Correctly setting payment terms, monitoring payment deadlines, optimising payment timelines and effectively communicating and resolving disputes are critical elements of effective liability management. By managing accounts payable properly, a company improves its financial stability, reduces the risk of default, optimises cash flow and strengthens relationships with business partners. Effective liability management requires a systematic approach and appropriate tools and procedures.

Inventory Management

Inventory management is crucial to working capital policy and financial management. Inventories are physical goods or raw materials held in a company's warehouse or sales premises for sale or use in production. Inventory management involves determining the optimum level of inventories, controlling inventories, monitoring stock movements and optimising orders and purchases.

Efficient inventory management is crucial to the success of a business for several reasons. Proper inventory planning and management can:

1. *Ensuring availability.* Adequate stock levels enable a company to meet customer demand and ensure the continuous availability of products or raw materials. This preserves the company's reputation and prevents loss of business.
2. *Cost reduction.* Excessive storage leads to storage costs, obsolescence and loss of value. Inventory management allows you to optimise inventory levels and reduce these costs, helping to improve your company's financial position.
3. *Improving cash flow.* Excess inventory means tying up capital, which can hurt a company's cash flow. Inventory management

allows better cash flow optimisation by ordering on time and adjusting inventory levels to sales trends and demand.

4. *Optimising orders and purchasing.* Monitoring stock movements allows better order and purchase planning. By properly analysing demand, forecasting sales, and using the right inventory management tools, a company can improve its ordering and purchasing and achieve lower purchasing costs.
5. *Risk management.* Inventory management is also crucial to managing the risks associated with inventories. This includes preventing stock-outs, managing obsolescence and loss of value risks, and effectively dealing with supply or storage problems.

This introduction will examine these aspects and highlight the importance of effective stock management. We will focus on crucial inventory management approaches and strategies to help companies achieve better business and financial performance.

The first step in effective inventory management is determining the optimal stock level. This means determining stock levels that meet customer needs while minimising storage costs, obsolescence, and loss of value. Analysing sales trends, seasonal patterns, and demand is critical to correctly determining optimal stock levels.

The next step is to control and monitor stocks. The company needs an efficient inventory recording and monitoring system for regular updates, quickly identifying shortages or surpluses, and optimising purchasing and sales processes. Modern information technology and inventory management software can greatly facilitate this process.

Optimising orders and purchasing is also crucial to inventory management. The company needs to analyse orders, monitor supply chains, negotiate with suppliers and execute orders on time. It is also essential to consider various factors such as purchasing costs, delivery times, product quality and supplier reliability.

Inventory management also includes loss prevention and risk mitigation. The company must carry out regular stock checks, check expiration dates, monitor stocks likely to become obsolete and take appropriate risk mitigation measures. In addition, a suitable product return policy and supplier relationship can contribute to risk mitigation.

Finally, we will highlight that effective inventory management can bring many benefits, such as cost reduction, cash flow improvement, improved product availability, order optimisation and risk reduction.

Proper planning, control, optimisation and risk management are critical steps in effective inventory management that can contribute to a company's viability and competitive advantage. Therefore, companies must develop strategies and procedures for effective inventory management tailored to their specific needs and industry.

It is also important to note that inventory management is not a static process but requires constant monitoring, analysis, and adjustment. Changing market conditions, customer demand, new products and technologies, and other factors can influence optimal inventory management. Therefore, it is necessary to regularly assess the effectiveness and efficiency of existing strategies and adapt and improve processes in light of changes.

Optimising Stock Levels

Optimising stock levels is a critical element of effective inventory management. The aim is to ensure sufficient stocks for smooth operations while minimising the costs and risks associated with overstocking.

When optimising stock levels, several factors need to be taken into account (Ziukov, 2015):

1. *Demand analysis.* Analyzing the demand for products or raw materials is essential. We can forecast future demand based on historical data, market trends, seasonal fluctuations, and other relevant information. This way, we can better plan optimal stock levels to meet customer needs and avoid unnecessary surpluses or stock-outs.
2. *Inventory management methods.* Choosing the proper inventory management method is essential to optimise inventory levels. Different techniques, such as the ABC method (dividing inventories into categories A, B, and C according to their contribution to the total value), the Just-in-Time (JIT) method or other methodologies allow better planning and management of inventories.
3. *Cooperation with suppliers.* Cooperation with suppliers is critical to optimising stock levels. Establishing long-term partnerships with key suppliers, conducting regular reviews of purchasing contracts, and negotiating more favourable supply terms can help reduce purchasing costs and improve inventory management.
4. *Technology and automation.* Modern technology and automation can improve the inventory management process, enabling more

accurate traceability and faster response to changes in demand. Automated inventory tracking, ordering, and management systems can help improve efficiency and reduce errors.

5. *Adapting supply chains.* Adapting supply chains and working with key stakeholders in the supply chain can help optimise stock levels. Frequent communication with suppliers, sharing demand information, joint planning, and implementing measures to improve the flow of materials can help reduce inventories and increase efficiency. Adaptation of supply chains allows better coordination between manufacturers, suppliers and market needs, leading to faster material flow and reduced stock holding times.
6. *Cost and risk analysis.* Optimising stock levels should also consider the costs and risks associated with stock. Excessive storage can lead to high storage costs, obsolescence, loss of value and potential losses due to unsold or unused stock. On the other hand, stock shortages can lead to loss of business and customer dissatisfaction. Therefore, It is necessary to assess the costs and risks and find a balance between optimal inventories and cost-effectiveness.

Optimising stock levels is an ongoing process that requires constant monitoring, analysis, and adjustment. Companies should regularly assess the effectiveness of their stock management strategies and keep abreast of market trends and changes. Adapting to changes in demand, improving purchasing and sales processes, and optimising the use of technology are critical elements in achieving effective stock management.

Demand-Driven Stock Management

Demand-driven inventory management is crucial to optimising stock levels and managing inventories efficiently. Customer demand is one of the main factors influencing stock levels and company performance. Therefore, it is essential to understand the market and adapt inventory management to its characteristics.

The following aspects should be taken into account when managing demand-based inventories:

1. *Demand analysis and forecasting.* Analysing and forecasting the demand for products or raw materials is essential for successful

inventory management. This includes collecting historical data, analysing trends, seasonal patterns, changes in consumer preferences and other factors that influence demand. With this information, we can better predict future demand and adjust stock levels.

2. *Adjusting stocks to demand.* Stock levels must be adjusted according to forecast demand. During increased demand, stocks should be increased to ensure uninterrupted customer supply. Conversely, stocks should be reduced in reduced-demand periods to minimise storage costs and obsolescence losses. Adapting stocks to demand allows better responsiveness to market changes and increases the efficiency of stock management.
3. *Use of advanced tools and technologies.* It is advisable to use them to manage stocks according to demand effectively. Modern IT platforms and inventory management software allow more accurate demand monitoring, faster data processing, and better demand forecasting. In addition, automated inventory tracking and automated ordering technology can help better align inventories with actual demand.
4. *Cooperation with customers and suppliers.* Cooperation with customers and suppliers is critical to managing stocks according to demand. The company must actively communicate with customers and get feedback on demand, trends and changes. Cooperation with customers may include joint demand plans and forecasts to adapt inventories better and improve product availability. Collaboration with suppliers is also essential. Liaison with suppliers allows for faster adjustment of stocks to demand. Regular cooperation, exchange of demand information, negotiation of flexible supply terms, and resolution of potential problems can help coordinate inventories better and improve the overall supply chain.
5. *Flexibility and agility.* Demand can change quickly, so flexibility is critical. A company must be able to adjust stock levels and processes in response to changes in demand. Agility in inventory management allows a company to react quickly to changes and better adapt inventories to actual market needs.

Demand-driven inventory management is the key to a company's efficient and effective inventory management. Companies can achieve

optimal inventory management and improve their business results by analysing demand correctly, adjusting inventories using advanced tools, and working with customers and suppliers. In the next part of this chapter, we will look at specific demand-driven inventory management methods and strategies and analyse practical examples to understand this critical aspect of inventory management better.

Warehousing and Logistics Management

Warehousing and logistics management are critical elements of working capital policy and the effective management of short-term financial resources. They include the physical management and tracking of inventories, the organisation of transport and distribution, and the provision of adequate logistics processes for the smooth operation of the business.

Warehousing and logistics management should take into account the following vital aspects (Richards, 2017):

1. *Systematic storage.* Stocks must be appropriately organised and distributed in the warehouse. This includes setting up transparent labelling systems and storing and tracking stocks. Modern technologies such as automated inventory tracking systems, barcode scanners, RFID technology, and other advanced methods can facilitate storage and accurate inventory tracking.
2. *Efficient logistics network.* The company must develop an efficient logistics network that allows products to be distributed quickly and efficiently. This includes planning optimal routes, selecting appropriate means of transport, managing warehouses and distribution centres, and working closely with carriers and logistics partners. The aim is to ensure that products are delivered to customers on time and at minimum cost.
3. *Stock monitoring and control.* Effective storage management involves regular stock monitoring and control. This includes regular inventories, real-time tracking of inventory, monitoring use-by dates, identifying stocks likely to be obsolete, and implementing appropriate risk mitigation measures. Proper inventory monitoring and control allow for cost reduction, loss prevention, and unnecessary stock reduction.
4. *Transport management.* Efficient transport management is critical to ensuring the timely delivery of products to customers. This

includes selecting suitable operators, optimising routes and transport planning, and closely monitoring and controlling the supply chain. Proper transport control allows for the reduction of costs, the optimisation of delivery times, and the improvement of customer satisfaction.

5. *Safety and security.* Warehouses and logistics procedures require appropriate precautions to protect stock against theft, damage, or unauthorised access. This includes using security systems such as video surveillance, alarms, restricted access, and appropriately trained personnel. Ensuring safety and security helps prevent losses and maintain the integrity of stocks.
6. *Efficiency analysis.* Regularly analysing the efficiency of warehousing and logistics is crucial to identifying possible improvements. This includes measuring key performance indicators such as warehousing costs, working hours, delivery times, stocks in operation, stock accuracy, and customer satisfaction. Performance analysis helps to identify opportunities for optimisation, cost reduction, and improvement of overall logistics processes.

Warehousing and logistics management significantly impact a company's performance, affecting costs, product availability, customer satisfaction and competitive advantage. A company achieves increased liquidity, reduced costs, increased customer satisfaction, and improved business performance through an appropriate working capital policy and effective warehousing and logistics management. In the remainder of this chapter, we will look more at specific methods, strategies and approaches for effective warehousing and logistics management and analyse practical examples to better understand this critical aspect of working capital policy.

Claims Management

Receivables management is integral to a company's working capital policy and financial management. Receivables represent outstanding debts owed by customers from selling products or services. Effective receivables management is critical to ensuring the company's liquidity, reducing the risk of default, and improving cash flow.

The following key aspects should be taken into account when managing claims:

1. *Credit policy.* The company must have a clear credit policy that sets out the terms and conditions of credit sales, payment terms, credit limits, and procedures for verifying customers' creditworthiness. This ensures an appropriate credit policy and minimises the risk of default on receivables.
2. *Customer credit check.* We must conduct a thorough credit assessment of our customers before granting a loan. This includes analysing customers' financial data, checking business history, obtaining references and using external credit rating agencies. This reduces the risk of default and improves receivables management.
3. *Monitoring and management of claims.* Regular monitoring and management of claims is essential for effective claims management. This includes systematic follow-up of overdue claims, notification of payments to customers, implementation of recovery procedures and monitoring of customer payments. This reduces the risk of default and improves cash flow.
4. *Financial instruments for risk management.* An entity may use various financial instruments to manage the risks associated with its receivables. These include collateralisation, pledges, assigning receivables to a factor, or other economic instruments to reduce default risks and improve liquidity.
5. *Effective recovery procedures.* In the event of default, effective recovery procedures must be in place. This includes regular communication with customers, warnings, dispute resolution negotiation, use of legal means to collect claims, cooperation with legal experts, and use of legal remedies where necessary. Effective collection procedures allow for a reduction in outstanding receivables, improve liquidity, and reduce risks for the company.
6. *Analysis and reporting.* Regular analysis and reporting on receivables' situation are essential for effective management. This includes monitoring key indicators such as average payment terms, the proportion of overdue receivables, the proportion of disputed receivables, and the recoverability of receivables. This allows problems to be identified quickly and appropriate measures to be taken to improve receivables management.

Managing claims requires a systematic approach and continuous

monitoring. Companies need to develop a clear debt management policy, carry out appropriate credit checks on customers, establish effective collection procedures, use financial instruments to manage risks and regularly analyse and report on the situation of their receivables. This ensures the company's liquidity and improves financial management. In the remainder of this chapter, we will explore concrete methods and strategies for managing receivables, analyse practical examples and discuss critical challenges and solutions.

Credit Policy Management

Credit policy management is critical to effective claims management and default risk management. A company's credit policy sets out the terms of credit, payment terms, credit limits and procedures for verifying customers' creditworthiness. A properly designed and implemented credit policy helps mitigate the risk of unpaid debts and ensures the company's liquidity.

The following essential aspects should be taken into account when managing credit policy (Wheelen et al., 2018):

1. *Establishing credit terms.* The company establishes clear credit terms, including payment terms, contractual terms, interest rates for late payment, minimum credit limits and other relevant parameters. The credit terms should be tailored to the enterprise's specific needs and characteristics and should also consider industry standards and competitiveness.
2. *Customer creditworthiness check.* Before granting credit, it is essential to conduct a thorough credit assessment of customers. This includes analysing customers' financial data, verifying their business history, obtaining references, and using external credit rating agencies. A credit assessment of customers enables evaluation of their ability to meet their financial obligations and minimises the risk of default.
3. *Setting credit limits.* The company must set clear credit limits for customers, limiting the maximum amount of credit a customer can obtain. Credit limits are set based on a review of the customer's creditworthiness, payment history, business relationship, and other relevant factors. Setting credit limits minimises the risk of default and maintains a balance between business opportunities and risks.

4. *Monitoring payment terms.* Systematic monitoring of customer payment terms is crucial. This includes regular monitoring of invoices, informing customers of overdue payments, sending reminders and implementing procedures to recover claims in the event of late payment. Monitoring payment terms allows for the timely identification of potential payment problems and enables the company to act quickly and take appropriate measures to resolve overdue claims. Regularly monitoring payment deadlines is essential to maintain cash flow stability and reduce the risk of default.
5. *Establishing a discount and interest rate policy.* The company should establish a clear policy on discounts and interest rates for up-front or fixed-term payments. Setting appropriate discounts and interest rates encourages customers to pay faster and reduces the risk of default. It is also essential to consider the market's competitiveness and ensure that discount and interest rate policies are consistent with the company's business objectives and strategy.
6. *Systematic reporting and analysis.* The company shall establish a systematic reporting and analysis of credit policy and receivables performance. This includes monitoring key indicators such as the proportion of overdue receivables, average time to pay, average age of receivables, etc. This allows the performance of the credit policy to be assessed, potential problems to be identified, and policy adjustments to improve receivables management.

Credit policy management is critical to effective claims management and default risk management. Through a clearly defined credit policy, customer credit checks, credit limits, monitoring of payment terms, discount and interest rate policies, and systematic reporting and analysis, companies can reduce the risk of default on receivables, improve cash flow and maintain a stable financial position. In the remainder of this chapter, we will look at specific methods and strategies for credit management, analyse practical examples and discuss critical challenges and solutions for managing receivables.

Monitoring Payment Deadlines

Monitoring payment deadlines is critical to managing receivables and providing liquidity for the company. It allows for the timely identification of potential late payments by customers and rapid action to man-

age the risk of default. A company can avoid financial difficulties and maintain a healthy cash flow by monitoring payment terms.

The following essential aspects should be taken into account when monitoring payment deadlines (Georgiadis, 2017):

1. *Systematic approach.* The company should establish a systematic approach to monitoring customer payment terms. This includes establishing clear procedures and responsibilities for monitoring and recording payment terms and setting up appropriate payment tracking tools. Monitoring is essential to ensure that late payments are not overlooked.
2. *Automation and digitisation.* Computer systems and tools that automate and digitise the process of monitoring payment deadlines allow for more efficient and accurate monitoring. Companies can use claims management software solutions to automatically track payments, generate alerts in case of delays, and produce reports to analyse payment deadlines.
3. *Regular customer information.* the company must establish clear communication channels with its customers and keep them informed of payments due. This includes sending reminders about overdue invoices, communicating by phone or using email notifications. Regular communication with customers encourages timely payments and reduces the risk of late and non-payment.
4. *Systematic debt recovery.* In the event of late payment, it is essential to have systematic procedures for recovering debts. This includes sending formal reminders, setting up dispute resolution discussions with customers, using external debt collectors, or, in extreme cases, resorting to legal remedies. Systematic debt recovery allows for swift action and reduces the risk of non-payment.
5. *Analysis of payment terms.* Regular analysis of payment terms is crucial to gain insight into customers' payment habits and identify possible patterns of delays or problems. Systematic analysis identifies customers at high risk of default and enables timely action to mitigate risks. Payment terms analysis includes a review of average payment times, the proportion of late payments, an assessment of the improvement or deterioration of payment habits, and a comparison with the industry or competitors.
6. *Continuous process improvement.* Since managing payment deadlines is dynamic, it is essential to improve the monitoring process

continuously. This includes identifying and correcting potential weaknesses in monitoring procedures, improving customer communication, and introducing new technologies or tools to monitor payment deadlines more efficiently.

Managing payment deadlines requires consistency, accuracy and systematicity. Companies can effectively manage default risks and ensure stable cash flow and liquidity by establishing clear procedures, using automation, keeping customers regularly informed, systematically collecting debts, analysing payment terms, and continuously improving the monitoring process. In the remainder of this chapter, we will look at the concrete management of payment terms, analyse practical examples and discuss critical challenges and solutions in managing receivables.

Recovery of Claims

Debt recovery is essential in managing receivables and the risk of default. In the event of late payment, measures must be taken, and effective collection procedures must be implemented to recover debts and preserve the company's liquidity. The following key aspects should be taken into account in the recovery of claims:

1. *Communication with customers.* The recovery process begins with appropriate communication with the customer who has missed a payment. It is essential to liaise, check the reasons for the delay, and try to reach a payment agreement. Communication should be professional but decisive, emphasising establishing and maintaining a good business relationship.
2. *Warnings and reminders.* Written reminders and warnings must be sent if the customer fails to respond to a request for payment or fails to comply with the payment agreement. Warnings should be clear, precise and professional, including information about the debt, interest for late payment and possible legal action if not paid within the agreed time.
3. *Negotiating to resolve disputes.* In some cases, there may be a dispute over payment or other problems. In these cases, it is helpful to negotiate with the customer to resolve the dispute. Negotiations may involve finding compromise solutions, making instalments, or other agreed-upon payments. The aim is to reach a sustainable agreement allowing the debt to be repaid.

4. *External recovery.* If traditional recovery procedures fail, the company may seek help from external recovery agencies or legal experts. These agencies have specialised knowledge and experience in debt recovery and can take more aggressive legal action if necessary. Working with legal experts can lead to legal proceedings to recover debts.
5. *Monitoring the recovery process.* It is essential to monitor and record it, including communication with the customer, reminders sent, negotiations, payments, and any legal proceedings. Monitoring allows you to track the recovery's progress and gain insight into its effectiveness. It also allows you to identify patterns or problems and adjust the recovery strategy to improve results.
6. *Use of legal remedies.* If traditional collection procedures and negotiations do not produce the desired results, legal means may be necessary to recover the debt. This may include filing a lawsuit or using other legal procedures to enforce the debt recovery. However, legal remedies should be carefully considered as they may lead to additional costs and lengthy proceedings.
7. *Continuous improvement of procedures.* Debt recovery is a dynamic process, so it is essential that a company continuously improves its recovery procedures. This includes analysing the effectiveness of the procedures, identifying weaknesses and making changes to improve results. This ensures continuous improvement of the recovery process and better management of non-payment risks.

Managing debt recovery requires consistency, professionalism and systematicity. By communicating correctly with customers, sending reminders and warnings, negotiating dispute resolution, using external recovery agencies, monitoring the recovery process, applying legal remedies, and further improving procedures, companies can effectively recover their debts, reduce default risk, and preserve liquidity. In the remainder of this chapter, we will look at concrete methods and strategies for debt recovery, analyse practical examples and discuss critical challenges and solutions in debt management.

Liability Management

Accountability management is a vital part of corporate financial management. Liabilities are a company's financial obligations to other parties or institutions. This includes obligations to suppliers, lenders,

employees, the government, and other stakeholders. Effective liability management is essential to maintaining liquidity, preserving good business relations, and avoiding financial difficulties.

This section will focus on different aspects of liability management, including managing supply obligations, long-term credit management, payments to employees, and obligations to the state. We will examine the key elements, strategies and tools that enable companies to manage liabilities effectively, reduce risks and improve their financial position. Emphasis will be placed on tailoring the commitment policy to the specific needs and objectives of the company, meeting payment deadlines, and managing costs and risks. We will illustrate the different aspects of liability management through practical examples and stress the importance of establishing an effective control and reporting system for monitoring commitments.

Managing Supplier Deadlines

Managing supplier deadlines is critical to a company's accounts payable management. Supplier terms refer to the timeframe a company pays its suppliers for products or services received. Effectively managing supplier deadlines is essential to maintaining good business relations with suppliers, ensuring a stable supply chain, and maintaining the company's liquidity.

The following key aspects should be considered when managing supplier deadlines (Lawson et al., 2015):

1. *Review and analysis of supplier terms and conditions.* The company carefully reviews and analyses the supplier's terms and conditions, including payment terms, discount terms, default interest rates, and other relevant details. Understanding these terms and conditions is crucial for making payment and cash flow management decisions.
2. *Monitoring payment terms.* The company must regularly monitor the supplier's payment terms. This ensures timely payment and prevents late payment or penalties for non-payment. Systematic monitoring of payment terms also enables potential problems to be identified and acted upon promptly.
3. *Negotiating payment terms.* When a company wants to adjust payment terms with suppliers, it is essential to establish open communication and negotiation. Negotiations may include extensions

of payment terms, agreements on discounts for early payment, or other adjustments according to the company's specific needs. The aim is to reach sustainable and mutually satisfactory payment terms for both parties.

4. *Process automation and optimisation.* Computer systems and tools can help increase efficiency by automating payment processes and managing delivery times. This includes electronic systems for sending and receiving invoices, setting up automated payment reminders, and centralising a system for managing supplier deadlines.
5. *Maintaining good business relations.* A company must maintain good business relations with its suppliers, as they are critical stakeholders in the supply chain. This includes timely payment of invoices, strict compliance with contractual obligations, and compliance with agreed-upon payment terms. By fostering good business relations, a company can negotiate more favourable terms, receive preferential treatment, and obtain suppliers' support in case of potential problems.
6. *Managing your supply chain strategy.* Effective supply chain management also requires an integrated strategy. This involves analysing and optimising the entire process, including procurement, production, distribution, and warehousing. Proper alignment of these factors allows for better coordination with suppliers and reduced risks in the supply chain.
7. *Supplier diversity.* Supplier diversification is essential to reduce risks and ensure continuity of supply. To meet its needs, a company must develop a portfolio of reliable, competitive suppliers. Supplier diversity also allows it to adapt to market problems or changes.

Managing supplier deadlines requires a systematic approach, continuous monitoring and adjustment. By properly reconsidering supply terms, regularly monitoring payment terms, negotiating payment terms, automating processes, maintaining good business relationships, managing supply chain strategy and diversifying suppliers, companies can achieve better liquidity, reduce risks and build a stable and efficient supply chain. In the remainder of this chapter, we will explore concrete methods and strategies for managing supplier dead-

lines, analyse practical examples and discuss critical challenges and solutions for managing supplier commitments.

Negotiating Payment Terms

Negotiating payment terms with suppliers is integral to liability management and critical in establishing a mutually satisfactory relationship between the company and its suppliers. Negotiations allow payment terms to be tailored to the company's specific needs and capacities and improve liquidity and risk management. The following key aspects should be taken into account when negotiating payment terms:

1. *Analysis of payment terms.* Before entering into negotiations, it is essential to analyse the payment terms with existing suppliers thoroughly. This includes reviewing payment terms, possible discounts for early payment, interest rates for late payment and other vital elements. The analysis will allow a better understanding of the current situation and identify areas where payment terms can be improved.
2. *Setting objectives and strategies.* Clear goals and a negotiating strategy should be set before negotiations. Objectives may include extending payment terms, obtaining more favourable prices, obtaining early payment discounts, or other adjustments to payment terms. The strategy will set out the means of communication, the arguments for negotiation, and possible compromises.
3. *Preparing the arguments.* Relevant arguments and data to support the company's demands during the negotiations are essential. This includes financial analysis, market price comparison, payment terms with other suppliers, and relevant information. Strong arguments will help the company achieve the desired payment terms changes.
4. *Negotiating mutually beneficial agreements.* The aim of the negotiations should be to establish mutually beneficial contracts that meet the needs of both parties. It is essential to keep an open line of communication, listen to the suppliers' views and find solutions that benefit both the company and the suppliers. Sometimes, compromises can be reached that improve payment terms without negatively affecting supplier relationships.
5. *Monitoring and implementing agreed changes.* Once an agreement has been reached, it is essential to follow up on the agreed changes

and implement them effectively. This includes updating internal systems and procedures for new payment terms, adjusting financial reports and records, and regularly monitoring suppliers' compliance with the agreed terms.

6. *Maintaining good relations in the long term.* Negotiating payment terms is part of the broader process of establishing and maintaining good relations with suppliers. Regular communication, transparency, and respect for agreed-upon terms are essential. This builds long-term trust between the company and its suppliers and creates the foundations for successful future cooperation.
7. *Monitoring and evaluating the results of negotiations.* Once negotiations have been concluded, it is essential to systematically monitor the results and effects of the changes in payment terms achieved. This includes analysing financial indicators such as liquidity, cash flow, and risk management. Monitoring the results will help assess the negotiations' success and identify possible further adjustments that could improve the payment terms and the company's financial performance.

Effective negotiation of payment terms with suppliers requires preparation, analysis, communication skills and consistent implementation of agreed changes. With the right strategy, arguments and mutually beneficial agreements, a company can achieve improved payment terms, increased liquidity and effective management of its payables to suppliers. In the remainder of this chapter, we will look at concrete methods and strategies for negotiating payment terms, analyse practical examples and discuss critical challenges and solutions for managing payables.

Use of Short-Term Financing

Short-term financing is an essential element of the Company's working capital policy. It provides the means to cover short-term liabilities such as payments to suppliers, salaries to employees, and other operating expenses. Properly using these resources is essential to maintaining the company's liquidity and ensuring its smooth operation.

In this section, we will look at the different sources of short-term finance available to companies:

1. *Bank loans.* Banks offer short-term loans, such as bridging loans,

revolving credit, and overdrafts on current account balances. These loans allow companies to obtain the necessary funds to cover short-term liabilities.

2. *Credit cards.* Business credit cards are one option for short-term financing. Businesses can use credit cards to pay suppliers or cover other short-term expenses. It is important to consider interest rates and fees and to pay off debts on time to avoid high costs.
3. *Payment terms from suppliers.* Companies can use longer payment terms to extend the payment term and better use funds. However, it is essential to maintain good relations with suppliers and respect agreed payment terms.
4. *Factoring.* Factoring involves selling a company's receivables to a third party, called a factor, to raise funds quickly. The company sells its receivables to suppliers or customers at a discounted price, which allows it to finance its receivables immediately and improve its liquidity.
5. *Short-term commercial paper.* Companies can issue short-term commercial paper, which are non-recourse securities with a fixed maturity. These securities are sold on the market, allowing investors to return interest on a short-term investment.

The correct use of short-term funding depends on the company's specific needs and situation. It is important to consider costs, interest rates, and repayment terms and carefully plan the use of these funds. Managing short-term funding sources involves monitoring and controlling cash flow, meeting obligations to creditors within set deadlines, and managing risks effectively. When using short-term funding, it is essential to consider the following aspects:

1. *Liquidity planning.* A company must carefully plan its liquidity needs to use short-term funding sources efficiently. This includes monitoring cash flow, identifying periods of increased liquidity needs, and adjusting the use of short-term resources accordingly.
2. *Liability management.* Properly managing liabilities to creditors ensures that payment deadlines are met and good business relations are maintained. This includes monitoring payment deadlines, providing timely compliance, and establishing regular communication with creditors.

3. *Analysis of financing costs.* When using short-term sources of financing, it is essential to assess the costs associated with these sources. This includes interest rates, commission costs, possible penalties for late payment and other related expenses. With this information, the company can select the most appropriate and advantageous sources of financing.
4. *Diversifying sources of finance.* A company should consider diversifying its sources of finance so that it is not dependent on a single source. Diversification reduces risk and increases flexibility in the event of market changes or difficulties in accessing specific sources of finance.
5. *Timely repayment of loans.* When using short-term loans, these loans must be repaid on time according to the agreed repayment terms. Timely loan repayment helps maintain a company's good creditworthiness and build creditor confidence.

Effective short-term funding management requires attention to liquidity, liabilities, costs, diversification of sources, and timely loan repayment. The company maintains its financial stability, manages risks, and ensures smooth short-term operations.

Risks and Governance

Managing a company's short-term financial resources and liabilities entails specific risks affecting its stability and liquidity. Identifying and managing these risks is essential to minimise the adverse effects on the company's business and financial performance.

This section examines companies' key risks when managing short-term financial resources and liabilities. We will also discuss the methods and strategies used to manage these risks and their impact on business performance. Risks related to short-term financial resources may include insufficient liquidity, difficulties accessing funding, changes in interest rates, credit risk, and other external factors. Risks related to liabilities include delays in supplier payments, increased risk of collection of receivables, and exposure to interest rates. Managing these risks requires a systematic approach that includes (Kerzner, 2017):

1. *Risk analysis and identification.* An entity identifies and assesses the risks associated with its short-term financial resources and liabilities. This includes reviewing the business environment, mon-

itoring market developments, analysing financial indicators and identifying key risks.

2. *Developing risk management strategies.* Using detected risks, methods should be developed to manage them. This may include adopting liquidity management policies and procedures, developing new funding sources, establishing an adequate system for monitoring payment terms, and setting up a debt recovery system.
3. *Risk diversification.* By diversifying risks, a company can reduce its exposure and increase its resilience to potential adverse events. This includes diversifying funding sources, suppliers, markets, and products and taking other measures to reduce risk concentration.
4. *Monitoring and control.* It is essential to monitor the implementation of the risk management strategies adopted regularly and to monitor and control the company's financial assets and liabilities regularly. This includes regular liquidity monitoring, financial report analysis, audits, and assessing the effectiveness of risk management measures.
5. *Communication and cooperation.* It is essential to establish good communication and cooperation between the different departments and stakeholders in the company. Risk management should involve all relevant interests, such as the finance department, procurement, sales, and governance. Regular communication and cooperation allow for coordinated action and rapid identification and response to potential financial problems or risks.
6. *Monitoring changes in the market.* A company needs to be alert to changes in the economic environment, legislation, interest rates, and other factors that may affect its financial position and risks. Regularly monitoring market conditions allows timely adjustment of strategies and risk management measures.

Risk management involves managing short-term financial resources and liabilities requiring constant attention and adjustment. Appropriate analysis, strategies, and controls can minimise risks' adverse effects and ensure operations' stability and liquidity.

Financial Analysis of Working Capital

Financial analysis of working capital is essential for assessing and monitoring the effectiveness of an enterprise's management of its short-

term financial resources and liabilities. This analysis provides insight into the liquidity, efficiency, and risks associated with working capital and helps make informed decisions to improve the company's financial position.

This section will examine the key indicators and financial analysis methods used to assess working capital. We will analyse their application in practice and highlight their importance in understanding and optimising the management of short-term financial resources and liabilities.

The financial analysis of working capital includes an assessment of the following aspects:

1. *Liquidity.* Working capital liquidity analysis focuses on assessing an enterprise's ability to meet its short-term commitments. This includes analysing the asset-liability ratio, the inverse interest rate, and other liquidity indicators.
2. *Inventory management performance.* Inventory management performance analysis focuses on assessing how well a company manages its inventories. This includes analysing the average inventory holding period, inventory costs to turnover ratio, and other performance indicators.
3. *Receivables management.* Debt management analysis assesses how well a company manages its customer receivables. This includes analysing the average payment period, the ratio of claims to turnover, and other effectiveness indicators in receivables management.
4. *Liability management analysis* assesses how well an entity manages its short-term liabilities to suppliers and creditors. This includes analysing the average payment period, the ratio of payables to turnover, and other performance indicators for managing liabilities.

A proper financial analysis of working capital can help a company identify opportunities to improve its financial position, optimise managing short-term financial resources and liabilities, and reduce risks. Based on the analysis results, the enterprise can take appropriate measures to improve its liquidity, inventory, receivables, and liability management.

In addition, financial analysis of working capital allows a company

to be benchmarked against its competitors or industry standards, allowing it to understand its position in the industry better and identify strengths and weaknesses in working capital management.

When carrying out a financial analysis of working capital, it is essential to follow a comprehensive approach, including a review of key indicators, comparison with historical data and benchmarking against industry averages. It is also essential to monitor trends and changes in working capital and to take timely action in case of deviations from expected values.

Working Capital Indicators

Working capital ratios are an essential tool in financial analysis and in assessing the effectiveness of a company's management of its short-term financial resources and liabilities. These ratios provide insight into the relationships between the various components of working capital and allow an assessment of the enterprise's financial stability, liquidity, and efficiency.

Below, we will look at some of the critical working capital indicators:

1. *Inventories to sales ratio.* This indicator measures the ratio of the value of inventories to the enterprise's total sales. Higher values of this ratio may indicate too much inventory, which can negatively impact the company's liquidity.
2. *Claims to sales ratio.* This indicator reflects the ratio between the value of claims on customers and the company's total sales. Lower values of this indicator indicate better management of receivables and better liquidity.
3. *Trade payables to sales ratio.* This indicator measures the ratio of the value of trade payables to the enterprise's total sales. Higher values of this indicator may indicate longer payment terms to suppliers, negatively impacting business relations.
4. *Working capital to sales ratio.* This indicator reflects the ratio of the value of working capital to the enterprise's total sales. Higher values of this ratio indicate an increased need for working capital to support sales activities.
5. *Working capital conversion ratio.* This indicator measures how quickly a company's working capital turns over. Higher values indicate greater efficiency in managing short-term financial resources.

6. *Average period of payments to suppliers.* This indicator measures the average period over which an enterprise pays its obligations to suppliers. A more extended average payment period may indicate greater liquidity but may also lead to deteriorating business relations with suppliers.

These indicators are just a few examples and can be tailored to the company's needs and requirements. These indicators must be regularly monitored and compared with historical results and industry averages to assess the effectiveness of working capital management and identify potential problems or opportunities for improvement.

In addition, other factors and indicators specific to each industry or company should also be taken into account; for example, in some industries, indicators such as the average collection period, the ratio of inventories to the speed of sales of receivables, customer payment terms, etc., may be relevant.

The correct use and interpretation of working capital indicators can bring several benefits to a company, including:

1. *Better liquidity management.* By monitoring liquidity indicators, a company can identify potential problems early and take appropriate measures to increase liquidity. This includes changing customer payment terms, optimising inventory management and obtaining more favourable payment terms from suppliers.
2. *More efficient asset management.* Analysing inventory, receivables, and liability indicators allows a company to optimise its operational processes and achieve greater efficiency. Reducing inventories, reducing the average payment term for customers, and improving payment terms with suppliers can contribute to better resource use and increase profitability.
3. *Risk mitigation.* By properly managing working capital and monitoring relevant indicators, a company can better prepare itself for potential risks such as difficulties in paying obligations, an increase in customer credit risk or changes in the market. This allows the company to act quickly and minimise the negative impact of these risks on its business.

As we delve deeper into this chapter, we will unravel the use and interpretation of working capital ratios. This understanding will empower companies to manage their short-term financial assets and lia-

bilities better, contributing to their long-term success and competitive advantage in the marketplace.

Cash Flow Analysis

Cash flow analysis is a vital tool in working capital management. It allows a company to assess and monitor cash flows within the company. This analysis provides insight into cash flow from operations, investments, and financing and helps the company better understand liquidity patterns and trends.

Different approaches and methods are used in cash flow analysis, the most common of which are (Fernández, 2019):

1. *Direct method.* This cash flow analysis method focuses on directly tracking and recording an enterprise's cash inflows and outflows. The enterprise tracks all cash received from customers, payments to suppliers, payment of accounts payable, tax payments, payroll costs, capital expenditure, financing and other cash flows. This method gives the company a detailed overview of its cash flow and identifies any problems or opportunities. For instance, it can help identify if the company is spending too much on certain expenses or if there are opportunities to negotiate better payment terms with suppliers.
2. *Indirect method.* In this method, cash flow analysis uses the balance sheet and income statement. The company calculates net profit less non-cash expenses (for example, depreciation) and considers changes in working capital (balances, receivables, payables). This is how operating cash flow is calculated. In addition, cash flows from investments and financing are also taken into account.
3. *Free cash flow analysis.* Free cash flow is the cash flow that remains after a company has met all its obligations, including interest, taxes, and investment recovery. Free cash flow analysis helps a company assess how much cash is available to finance growth, pay dividends, reduce debts, or other purposes. It is an essential indicator of a company's financial stability and liquidity.

Cash flow analysis provides a sense of security, enabling a company to properly plan its financial resources and manage its working capital. It allows the company to identify the need for additional financial

resources or to optimise using existing resources to improve liquidity. It also allows cash flow to be compared with industry averages or historical results, which helps to assess performance and identify any deviations or trends in cash flow.

In addition, cash flow analysis allows the company to understand the causes of changes in liquidity better. Monitoring cash flows from operating, investing and financing activities can reveal patterns and trends that affect a company's liquidity. For example, suppose it is observed that operating cash flow is decreasing while investing cash flow is increasing. In that case, this may indicate that the company is investing in financial investments at the expense of liquidity. Such findings enable the entity to take appropriate measures to improve liquidity and ensure sustainable cash flow management.

It is crucial to note that cash flow analysis is not a one-time task but a continuous process that monitors changes over time. This ensures that the company's liquidity is kept up to date and that timely action is taken in case of any problems. It is also advisable to compare the company's cash flow with competitors and industry standards to assess its efficiency and competitiveness in cash flow management.

Optimising Working Capital Policy

Optimising working capital policy is key to effectively managing a company's short-term financial resources and liabilities. This process involves reviewing and adjusting the various components of working capital, such as inventories, accounts receivable, accounts payable, and payment terms, to achieve optimal liquidity, profitability, and risk levels. Understanding that each company has specific working capital needs and objectives is essential. Optimising the working capital policy is tailored to the individual company and its specific circumstances. However, some general approaches and guidelines can help companies optimise their working capital policies.

Identifying and eliminating surplus stocks is critical in optimising working capital policy. Overstocking can lead to higher storage costs, reduced liquidity, and supply chain congestion. A company can optimise its inventories and achieve better liquidity by studying demand, analysing sales trends, and using modern inventory management tools.

It is also essential to manage customer claims effectively. Long and non-payment terms can hurt a company's liquidity and financial posi-

tion. By establishing a clear credit policy, tracking payment terms, and implementing collection procedures, an entity can reduce the risk of default and improve its liquidity. Optimising the working capital policy also includes managing payables to suppliers. A company can optimise its payment terms and improve liquidity by negotiating preferential payment terms, applying early payment discounts, and establishing good relationships with key suppliers.

Considering the company's long-term strategy when optimising working capital policy is also essential. Changes in the industry, company growth, expansion into new markets, or new business opportunities may affect working capital needs. Therefore, it is essential that the company regularly reviews its strategy and objectives and adjusts its working capital policy in line with these changes.

There are several advantages for a company in managing and optimising its working capital policy effectively:

1. *Improved liquidity.* Optimising your working capital policy can help improve your liquidity. By striking the right balance between inventories, receivables and payables, a company can ensure that it has enough cash to meet its short-term obligations and to finance its operations.
2. *Cost reduction.* Managing working capital to the company's needs allows for reducing excess inventories, default risks, and optimising payment terms with customers and suppliers. This can lead to reduced storage costs, reduced collection costs, and improved terms of cooperation with key business partners.
3. *Increased profitability.* Efficient working capital management allows better use of a company's financial resources. Reducing the capital in inventories and receivables and improving the management of payment terms enables the company to increase its return on capital and improve its financial performance.
4. *Risk mitigation.* Optimising working capital policy allows a company to manage liquidity risks better. Monitoring key working capital indicators and taking timely action in case of deviations reduces the risk of liquidity problems or default.

In the remainder of this chapter, we will look in more detail at the methods and approaches for optimising working capital policy and highlight the importance of continuously monitoring and adapting

policy in line with changes in the business environment. This will enable companies to manage their short-term financial resources and liabilities better and achieve long-term financial stability and performance.

Management Objectives and Strategies

When optimising a working capital policy, it is essential to set clear objectives and management strategies that will guide the company in achieving the desired results. Objectives and strategies may vary depending on the specific needs and objectives of the company, but some general objectives are often present in working capital management (Punt et al., 2016):

1. *Increasing liquidity.* One main objective is ensuring the company has sufficient liquidity to meet its short-term financial obligations. This includes monitoring and managing working capital components such as inventories, accounts receivable and accounts payable to ensure sufficient cash is available to meet obligations.
2. *Optimising the use of resources.* The objective is to efficiently use the company's resources by reducing the capital tied up in inventories and receivables. This allows better utilisation of the company's assets and an increase in the return on capital.
3. *Risk mitigation.* Working capital management is closely linked to risk management. The aim is to reduce the risks of liquidity problems, late payments, and defaults. By monitoring and acting promptly, a company can reduce the adverse effects of risks on its business.
4. *Improving customer and supplier relations.* Establishing and maintaining good relations with customers and suppliers is an important objective. This includes negotiating payment terms, applying early payment discounts, and promptly communicating and resolving any problems.

Working capital management strategies should also consider the business's specific needs and characteristics. This includes an analysis of the industry, competition, market trends, the company's financial position, and long-term strategy. The company can design strategies tailored to its specific circumstances based on these analyses.

Working capital management strategies can include:

1. *Optimising inventory management.* Deciding optimal order quantities, tracking and managing inventory correctly, and implementing methods such as just-in-time, which can help reduce capital tied up in inventory and improve a company's liquidity.
2. *Receivables management.* An appropriate credit policy, checking customers' creditworthiness, timely invoicing, monitoring payment deadlines and implementing recovery procedures are critical factors for managing the risk of default and improving liquidity.
3. *Liability management.* Negotiating favourable payment terms with suppliers, using early payment discounts, and adjusting payment terms to meet the company's liquidity needs can help optimise liabilities and improve liquidity.
4. *Managing payment terms.* Good coordination of payment terms with customers and suppliers, the use of favourable payment means (e.g., discounts for cash payments, bank guarantees), and the establishment of good relationships with key business partners can all impact a company's liquidity.
5. *Risk management.* Identifying, assessing, and managing the risks associated with working capital is crucial. Monitoring fundamental indicators such as average payment terms, ratio of outstanding receivables, average days to pay suppliers, etc., allows timely action and risk management.

When designing working capital management strategies, it is also essential to consider the company's context. Understanding the competitive environment, industry trends, market changes, and legislation is critical to designing appropriate strategies.

Adapting Policy to Business Cycles

Business cycles and economic developments significantly impact a company's business and working capital policy. At different stages of the business cycle, the business's needs and challenges may change, requiring adjustments to the working capital policy.

1. *Growth phase.* In the growth phase, a company experiences increased demand, orders, and sales. During this period, it may be essential to increase inventories to meet the increased demand

and prevent stock-outs. Collecting customer requests on time and ensuring stable supply relationships is also essential.

2. *Peak phase.* Demand usually decreases or falls at the peak. Managing stocks carefully during this period to avoid surpluses and excessive capital tying-up. Adjusting production and purchasing to demand and optimising payment terms with customers and suppliers can help maintain liquidity.
3. *Declining phase.* In the declining phase, demand decreases, sales decrease, and revenues decline. During this period, effective management of receivables and payables is crucial to reduce the risk of default and ensure liquidity stability. Adjustments to credit policy, improvements in collection procedures, and the timely matching of liabilities to customers' solvency are essential measures.
4. *Recovery phase.* In the recovery phase, the economy gradually recovers, and demand increases. A company may increase inventories and receivables during this period to benefit from market growth. However, monitoring the risks and avoiding excessive tie-up sales of capital in inventories is essential.

Adapting working capital policy to business cycles requires analysing and monitoring market trends, economic indicators and internal company data. This allows the company to identify changes over time and adjust its working capital policy.

Policy Monitoring and Adaptation

Monitoring and adapting working capital policies are critical to effectively managing short-term financial resources and risk management. Businesses need to continuously adapt to changes in the business environment, customer needs, competitive pressures, and financial targets.

Some of the most important factors to monitor in a working capital policy include:

1. *Key indicators.* Monitoring key working capital indicators is essential to assessing the policy's effectiveness. These indicators include average customer payment terms, average supplier payment terms, percentage of outstanding receivables, percentage of excess inventories, etc. Regular monitoring of these indicators allows for identifying potential problems and timely action.

2. *Risk analysis.* Monitoring the risks associated with working capital is essential. This includes analysing customers' creditworthiness, monitoring the risk of default on receivables, assessing suppliers' risk, identifying potential problems in the supply chain, and identifying other risks that could affect the business's liquidity. Based on these analyses, appropriate risk management measures can be taken.
3. *Policy adaptation.* A company must be prepared to adapt its working capital policy to changing circumstances. This includes adjustments in light of changes in demand, competition, economic conditions, legislation, and other factors affecting the enterprise. Policy adjustment requires proactive decision-making, such as adjustments to credit terms, optimising inventories, negotiating payment terms, and other measures to improve liquidity and risk management.
4. *Continuous improvement.* The company must constantly keep up with new trends, innovations, and best practices in working capital management. Continuous improvement of policies and processes enables efficient management and better results. This includes continuously assessing the effectiveness of existing practices, finding new ways to optimise working capital policies, and adapting strategies and procedures to industry innovations.

Good communication between the different departments and stakeholders in the company is also crucial to monitoring and adjusting the working capital policy. Cooperation between the finance department, purchasing, sales, production and other relevant units allows for a better understanding of needs and challenges and coordinated action in working capital management.

Adjustments to working capital policy should be long-term oriented and not limited to short-term solutions. A company needs to develop a long-term working capital management strategy based on a comprehensive understanding of its business, objectives and competitive environment. This strategy should include establishing appropriate systems and procedures for data collection, performance monitoring, regular evaluation, and improving the working capital policy.

Managing working capital policies is essential to managing short-term financial resources and risks effectively. Monitoring, adjusting and optimising policies allows a company to improve liquidity, improve

efficiency and reduce risks. It is essential to understand that working capital policy is not static but requires constant adaptation to environmental changes. With appropriate policy and management strategies, a company can achieve an optimal balance between liquidity, efficiency and risk and create a sound financial basis for its operations.

Chapter Eleven

Corporate Finance in the European Union: Challenges and Opportunities in International Business

Corporate finance in the European Union plays a crucial role in supporting and promoting international business and creating a favourable business environment. With 27 members and a single economic area, the European Union is one of the world's largest and most developed economies. In this context, companies face several challenges and opportunities in managing their financial resources and activities in international business.

This chapter focuses on the analysis of corporate finance in the European Union and examines the challenges and opportunities that companies face when operating internationally. It focuses on the regulatory framework, the macroeconomic environment and the financial challenges faced by companies in the EU. We will also examine the future of corporate finance in the EU and look at the opportunities offered by operating internationally in this environment.

Understanding the challenges and opportunities in business finance in the European Union is crucial for companies wishing to do business successfully in the region. Understanding the regulatory framework, market trends, and financial instruments and adapting to dynamic changes in the business environment is essential to achieving competitive advantage and successful international business in the EU. In the next section, we will look more at the different aspects of business financing in the European Union and analyse the challenges and opportunities that companies face in this respect.

Business Finance in the European Union

Corporate finance in the European Union refers to managing financial resources, including providing funds, risk management, investment financing, liquidity management, capital management and optimisa-

tion. In this context, it is essential to understand the regulatory framework established by the EU and its impact on the business environment and financial activities.

This chapter will examine corporate finance in the European Union in more detail. We will first focus on the economic environment in the EU, including macroeconomic indicators, economic growth, and stability. We will then examine the market environment, including the regulatory framework for business, market competitiveness, and trends in the business environment.

We will also examine the financial environment in the European Union, including institutions that play a crucial role in ensuring financial stability and liquidity, such as the European Central Bank, European supervisors, and the banking sector. We will also pay particular attention to the euro as the single currency in most EU Member States and its impact on business finance in the European Union.

Understanding business finance in the European Union is essential for companies operating in this field, as it allows for a better understanding of the business environment, regulatory requirements and financing and investment opportunities. In the following, we will take a closer look at the different aspects of business finance in the European Union and analyse the challenges and opportunities that international business presents in this environment.

Economic Environment in the European Union

The European Union's economic environment is one of the world's largest and most dynamic markets. The EU is a single economic area, bringing together 27 Member States with a combined population of more than 450 million people. This creates a comprehensive internal market that facilitates the free movement of goods, services, capital, and labour.

One key feature of the EU's economic environment is the high degree of integration between Member States. This makes it easier for companies to access a broader market, increase competitiveness, and expand into new geographical regions. In addition, the single currency-the euro-which has been adopted by most EU Member States-has helped to facilitate business and reduce currency risks in the area.

The economic environment in the EU is constantly evolving and adapting to global trends. The EU faces many challenges, including demographic change, technological progress, climate change and geopo-

litical tensions. At the same time, there are many opportunities for businesses, particularly in innovation, digitisation, sustainable development, and international business.

In addition, the economic environment in the EU has its own specific characteristics and regulatory framework. The EU has a wide-ranging body of legislation covering areas as diverse as competition, consumer protection, taxation, labour law, environmental and social policy, and financial services. Companies operating in the EU must comply with these rules and adapt to changes in the regulatory environment.

Understanding the economic environment in the European Union is crucial for businesses to operate successfully in this market. Businesses must be aware of economic trends, the regulatory framework, market opportunities and competitive challenges in the EU. They must also adapt to change and exploit the EU's economic environment.

Market Environment in the European Union

The European Union's market environment is diverse and dynamic, offering many opportunities and challenges for businesses. The EU has one of the largest internal markets in the world, allowing the free movement of goods, services, capital, and labour between Member States. This creates a large and competitive market in which businesses face different aspects of the market environment.

One key feature of the EU market environment is the high level of competition (Rubashkina et al., 2015). In the internal market, companies face local competitors from other Member States, which requires and encourages innovation, quality, and efficiency. Competition law also promotes competition in the EU, protecting fair play and preventing the abuse of dominant market positions.

In addition, businesses in the EU face different cultures, languages, and consumer preferences. The EU brings together a diversity of countries and regions with different economic, cultural, and social characteristics. This requires adapting marketing strategies to take account of local preferences and needs and developing targeted approaches to market segmentation.

The EU market environment also reflects global trends such as digitalisation, e-commerce and changes in consumer behaviour. Businesses face the challenges of digital transformation, which requires adapting business models, innovative marketing approaches and leveraging digital channels to reach customers. In addition, consumer be-

haviour is changing, raising expectations for products, services, sustainability and corporate social responsibility.

The EU regulatory framework plays a vital role in the market environment. EU legislation governs many areas, including consumer protection, trade, intellectual property, data protection and environmental policy. Businesses need to comply with these rules, obtain the relevant certificates and licences and adapt to changes in the regulatory environment.

Understanding the European Union's market environment is crucial for companies wishing to thrive in this market. Companies must know the competitive environment, consumer needs, market trends, and regulatory requirements. They also need to develop flexible market strategies that respond to change and exploit opportunities.

Regional and local differences in the EU market environment must also be considered. Each Member State has its characteristics, regulations, and consumer preferences. Companies must adapt their products, services, and marketing strategies to local needs and expectations. Cultural and linguistic differences must also be considered, and effective communication channels with customers in different countries must be established.

There are also opportunities for international business in the EU market environment. The EU internal market and free trade agreements give companies access to potential customers and partners in different countries. As globalisation increases and European companies expand into international markets, new business growth opportunities are opening.

Financial Environment in the European Union

The financial environment in the European Union is essential for businesses operating in this economic area. The EU has a comprehensive and diversified financial sector, including banking, insurance, capital markets and other financial institutions. This creates a favourable financial environment for businesses by providing access to finance, managing risks and ensuring liquidity (Woolcock, 2016).

One of the critical institutions in the EU's financial environment is the European Central Bank (ECB), which is responsible for monetary policy in the euro area. The ECB ensures price stability, monitors the money supply and provides liquidity in financial markets. In addition, the ECB plays a vital role in supervising the banking sector and en-

suring the financial system's stability in the EU. The EU has also established a common regulatory framework for financial services called the European Financial Regulation. This framework includes guidelines, directives, and regulations covering banking, insurance, securities, investment funds, payment services, accounting, and auditing. It ensures consistency and transparency across the EU financial sector and protects the interests of investors, consumers, and businesses.

The euro is the common currency of most EU countries and is an essential factor in the financial environment. Its introduction has facilitated trade and commerce between Member States, reduced currency risks, and promoted economic integration within the EU. Businesses operating in the euro area benefit from the stability and ease of doing business in a common currency.

At the same time, new financial technologies such as digital currencies, blockchain technology, crowdfunding and financial platforms are emerging in the EU financial landscape. These technological innovations open new possibilities for financing, paying, investing and managing financial resources.

Understanding the financial environment in the European Union is crucial for companies operating in this economic area. Businesses must know the EU's financial instruments, services, and regulatory requirements. This includes knowledge of banking services such as credit, deposits and transaction accounts and using the capital market to raise equity or issue bonds. Businesses should also be familiar with the procedures and requirements for obtaining loans or other forms of finance. They should comply with regulatory standards relating to accounting, auditing, reporting and compliance.

It is also essential to consider the different financial and tax regimes in the EU Member States. Each country has laws and tax policies that can affect the business environment and corporate taxation. Businesses must be aware of national rules, adapt to local tax requirements, and manage their financial obligations effectively.

Currency and liquidity risks may also arise when operating internationally in the EU. Companies should consider these risks and take measures to manage them, such as using exchange rate hedging instruments or establishing adequate liquidity buffers.

Maintaining sound financial conditions and financial stability is crucial for the long-term viability of businesses in the European Union. Businesses must monitor their financial position, conduct regular fi-

nancial analyses, manage risks, and plan and budget their financial resources accordingly.

Challenges for Business Finance in the European Union

Corporate finance in the European Union faces various challenges affecting companies and their financial management in international business. These challenges stem from the complexity of the economic environment, the regulatory framework, financial markets, and socioeconomic and political conditions (McCann & Ortega-Argilés, 2018).

One crucial challenge is to ensure the stability and sustainability of the financial system in the EU. Financial crises and instability have recently affected the banking sector, capital markets, and business environment. Businesses face challenges in obtaining finance and liquidity, managing risks, and ensuring their stability.

The second challenge concerns the diversity of legislation and tax systems in EU Member States. Companies operating in several EU countries must adapt to regulatory requirements, reporting, and tax policies. This requires adequate knowledge of local regulations, adaptation of accounting and tax procedures and compliance with the legislation in each country.

International business in the EU also poses challenges in managing currency risks. Businesses face exchange rate fluctuations between currencies and must implement effective risk management strategies. They also face liquidity challenges, as different regulatory requirements and operating conditions can make it difficult to obtain short-term funding.

Digital transformation and technological advances in business finance are also significant challenges. Businesses must adapt to the rapid development of digital technologies such as e-commerce, online payments, artificial intelligence, and blockchain. They also need to consider security considerations, data privacy, and regulatory guidelines on using technological innovation in business.

Regulatory Challenges

Corporate finance in the European Union faces various regulatory challenges that affect companies in international business. The EU regulatory framework is complex and constantly changing, and companies must pay attention to new rules, guidelines, and requirements introduced by European institutions (Young & Pagliari, 2017).

One of the key regulatory challenges in the EU is compliance with competition rules. The European Commission has a vital role in monitoring and preventing illegal practices that could distort competition in the internal market. Companies must comply with restrictions on cartels, abuses of dominant positions, and concentrations of undertakings and avoid unfair competition.

Another regulatory challenge relates to tax legislation in the EU. Member States have different tax policies and systems, which can impact companies' business finances. Companies need to be aware of the tax rules in each country in which they operate and adapt to different tax rates, reporting rules and payment terms.

In recent years, the regulation of personal data protection has also increased. With the advent of the General Data Protection Regulation (GDPR), EU companies have been given stricter guidelines on collecting, processing and storing customers' and employees' personal data. Companies must ensure adequate security measures, inform customers about their data protection policy and respect individuals' privacy rights.

In addition, there are other challenges, such as environmental regulation and sustainable development, regulation of financial services in banking, insurance and securities, and regulation of digital technologies such as artificial intelligence.

Companies must adapt to regulatory requirements and keep abreast of changes in EU legislation. This may include implementing internal controls, training staff on regulatory requirements, working with legal experts, and setting up tracking and reporting systems to comply with legislation.

Macroeconomic Challenges

Corporate finance in the European Union also faces macroeconomic challenges stemming from the economic situation in the region. Macroeconomic factors such as GDP growth, inflation, unemployment, interest rates, and currency stability can significantly impact the business environment and companies' financial decisions.

One of the main macroeconomic challenges in the EU is economic growth. EU Member States face different levels of GDP growth, which can affect demand for products and services and business opportunities for companies. Businesses must adapt to changing economic conditions, plan their activities in line with expected economic growth,

and monitor indicators that measure economic activity in the EU.

Inflation is another crucial macroeconomic challenge. It affects production costs, commodity prices, and consumer demand. Businesses need to adapt to inflationary pressures and consider variable prices when planning product and service prices and managing operating costs.

Interest rates are a critical macroeconomic factor affecting corporate finance. Changes in interest rates can affect the cost of borrowing and the availability of capital. Businesses need to adapt to interest rate fluctuations and take appropriate measures to manage this risk, such as hedging interest rates or using different funding sources.

Currency stability is another critical macroeconomic challenge in the EU, especially for companies operating in several Member States. Exchange rate changes can affect companies' price competitiveness, exports and imports, and profitability. Businesses should be aware of currency risks and implement appropriate strategies to manage these risks, for example, using financial instruments to hedge exchange rate differences.

Another macroeconomic challenge is the impact of the political situation and events on the business environment. Political changes such as elections, political tensions, or introducing new regulatory measures can affect the business environment and the stability of companies.

Financial Challenges

Several financial challenges in business financing in the European Union affect companies in international business. These challenges relate to different aspects of financial management and arise in companies, financial markets, and the broader economic and political environment.

One of the challenges is access to finance. Businesses face challenges raising capital to finance their activities, especially during economic instability. Access to bank loans, bond issuance or attracting investors may be limited due to tight credit conditions or reduced investor confidence. Therefore, companies need to adapt and seek alternative financing such as start-up capital, venture capital funds or other forms of financing such as crowdfunding.

The second financial challenge is risk management. Companies face various financial risks, such as currency, interest rate, customer default, and operational risks. Effective risk management requires appro-

priate strategies, the use of financial instruments to hedge risks, and the monitoring and adjustment of financial policies.

The diversity of financial markets in the EU is also a challenge for businesses. Different Member States have different capital markets, banking sectors and regulatory frameworks. Companies operating internationally must adapt to different requirements and procedures when issuing securities, obtaining credit or managing financial investments. They also have to consider differences in tax systems that may affect their financial decisions (Busch et al., 2016).

In addition, EU companies are exposed to economic and political risks at the global level. International events such as trade wars, political tensions or financial crises in other regions can significantly impact the business environment in the EU. Companies must be aware of these risks and conduct appropriate analyses, such as planning and adapting their financial strategies and portfolios to the global economic situation.

Debt management is also a significant financial challenge in the EU. Companies can face high levels of indebtedness, limiting their financial flexibility and investment ability. Debt management includes monitoring and managing payment terms, optimising debt structure and adopting refinancing and debt reduction strategies.

In recent years, there has also been a challenge related to the regulatory framework for financial services. The EU has introduced several regulatory measures, such as MiFID II, which impact how firms provide financial services and manage financial instruments. Firms must adapt to the new rules, ensure compliance with regulatory requirements, and implement adequate internal controls and reporting procedures.

In international business, the European Union has specificities that present company challenges and opportunities. One of these characteristics is related to the different languages, cultures, and business practices among EU Member States. Companies need to adapt to diversity and be able to communicate and cooperate effectively in a cross-cultural environment.

The Future of Corporate Finance in the European Union

Corporate finance in the European Union continually evolves and adapts to the dynamic environment of international business. Rapid technological change, political and economic conditions, and regula-

tory changes significantly impact the future of corporate finance in the EU. Businesses need to be aware of these changes and prepare for the future to remain competitive and thrive in the marketplace (Daniels et al., 2019).

One of the critical changes facing corporate finance in the EU is digital transformation. Digital technologies and innovations radically change how businesses operate and manage financial resources. Financial technologies and digital platforms enable faster and more efficient operations, transaction management, and access to finance. Businesses must adapt to these changes, take advantage of digitalisation, and integrate digital strategies into their business processes.

Other essential facts for the future of corporate finance in the EU relate to environmental sustainability. The EU is committed to reducing its carbon footprint and promoting the transition to a low-carbon economy. This has implications for business finance, as companies need to consider environmental considerations in their financing decisions, including investment in sustainable technologies, environmental risk management, and sustainability reporting.

Regulatory changes in the EU will continue to impact corporate finance significantly. The EU is working towards a single market and harmonising the financial framework between Member States. This will require businesses to adapt to new regulatory requirements, including consumer protection, improving financial information transparency, and ensuring financial markets' stability and integrity.

In addition, business finance in the EU will also face global challenges and opportunities. International business is expanding, trade policies are changing, and innovation and technological advances offer new global growth and cooperation opportunities. Businesses must adapt to changes in the global economic environment, understand the diversity of markets and manage risks and opportunities in international markets.

The future of corporate finance in the European Union also implies the need for greater integration between Member States and more robust economic cooperation. The EU is focused on building strong links between businesses, financial institutions and governments to foster growth, job creation and innovation. This opens up new opportunities for financing and international business but also requires adjustments and appropriate risk management.

In the future, business finance in the EU is also likely to face chal-

lenges in terms of demographic changes, fluctuations in economic growth, political developments and new technological innovations. Businesses must adapt to these changes and develop flexible financial strategies to respond to changing circumstances and seize new opportunities.

Opportunities in International Business

International business in the European Union offers many opportunities for companies in different areas. The European Single Market, the free movement of goods, services, capital and labour, gives companies access to a broad consumer market and allows them to increase their competitiveness at the international level. Here are some of the key opportunities in international business in the EU (Bradford, 2020):

1. *Market expansion.* The EU Single Market, with over 500 million inhabitants, is a massive market for consumers and businesses. Businesses can expand their operations into new Member States and reach more customers. This allows them to increase revenues, increase market share and exploit synergies between different markets.
2. *International partnership.* The European Union promotes cooperation and company partnerships. Businesses can use opportunities to set up business partnerships, joint ventures, distribution networks, and exchange know-how. Working with local partners can help companies quickly enter new markets and adapt to local requirements.
3. *Access to finance.* International business also provides access to a broader range of finance. Businesses can use international financial institutions such as the European Investment Bank, the European Fund for Strategic Investments, and others to obtain soft loans, investment funds, and support for project development. Businesses can also benefit from various EU programmes and incentives to promote innovation, R&D, and internationalisation.
4. *Access to talent.* International business also provides a broader talent pool. Businesses can attract a highly skilled workforce from different EU Member States and benefit from diverse expertise, which increases their innovation, diversity, and competitiveness.
5. *Technological progress.* The EU encourages the development and deployment of technological innovation in areas such as digitali-

sation, energy efficiency, the green economy, artificial intelligence, and data analytics. Doing business internationally in the EU enables companies to access and use these advanced technologies to improve business processes, develop new products and services, and increase market competitiveness.

6. *Diversity and cultural richness.* The European Union is known for its diversity, which allows businesses to gain experience and knowledge of different cultures, business practices and market preferences. This can help create innovative solutions tailored to local needs and build strong partnerships with customers and stakeholders.
7. *EU support and incentives.* The European Union offers several programmes, subsidies, and incentives for companies doing business internationally. These include financial support for research and innovation, export incentives, support for internationalisation, and training and mentoring programmes. Companies can use these opportunities to strengthen their competitiveness and conduct international business activities successfully.

In the future, international business in the European Union will continue to grow and create new opportunities for businesses. Businesses must keep abreast of market changes, adapt to regulatory frameworks, take advantage of digital innovation and respond to consumer needs. With the right strategy and by seizing the opportunities offered by international business in the EU, companies can achieve growth, competitiveness and long-term success in the global marketplace.

Developing Financial Instruments and Markets in the EU

The European Union is actively committed to developing financial instruments and markets that promote economic growth, increase access to finance and strengthen stability and confidence in the financial system. Here are some of the critical development initiatives (Moloney, 2023):

1. *Capital market.* The EU is working towards a single capital market, allowing the free movement of capital between Member States. This includes simplifying rules and procedures for issuing shares and bonds, facilitating companies' access to equity finance, and encouraging investment in European companies.

2. *Alternative investment funds.* The EU encourages the development and regulation of alternative investment funds, such as private equity, real estate, and infrastructure funds. These funds offer alternative sources of finance for businesses, stimulate innovation, and contribute to economic growth and job creation.
3. *Green finance.* The European Union is leading the fight against climate change and promoting sustainable development. In this context, financial instruments and markets are being developed to stimulate investment in green infrastructure, renewable energy, energy efficiency, and other sustainable projects. This includes issuing green bonds, setting up green funds, and promoting sustainable investments.
4. *Financial technology (fintech).* Innovative financial technologies are being developed in the EU to facilitate access to finance, improve payment systems, enable digital banking, and offer other innovative services. This includes developing blockchain technology, mobile banking, online credit platforms, and automated financial advice.
5. *Financial Markets Regulation.* The EU is working to establish a consistent and stable regulatory framework for financial markets in all Member States. This includes the supervision and monitoring of financial institutions, the regulation of markets, consumer protection, and the promotion of transparency and integrity.

Developing financial instruments and markets in the EU opens up new opportunities for companies to raise finance, manage risks, and conduct international business activities. Businesses can use these opportunities to access capital, diversify their investments, optimise risk management, and build more robust and stable financial foundations.

In addition, the development of financial instruments and markets in the EU is also reflected in the increased liquidity and transparency of financial markets, which facilitates trading and increases business transparency. This makes raising capital more cost-effective, reducing transaction costs and promoting competition between financial institutions.

However, there are also some challenges. International business in the European Union requires a good understanding of the complex legal and regulatory environment, which can vary between Member States. Businesses must adapt to different tax, trade and legal rules and

ensure compliance with different requirements. Risks are also associated with currency fluctuations, political changes, economic crises and other global events. Companies need to be aware of these risks and implement effective strategies to manage them, including insurance, hedging and diversification of investments.

Further developments and innovations in corporate finance are expected in the European Union. Digitalisation, artificial intelligence, blockchain technology, and other advanced technologies will continue to shape the financial sector and create new business opportunities and challenges.

To successfully conduct international business in the EU, companies must keep abreast of trends and changes in financial markets, understand regulatory frameworks, and implement appropriate governance and financing strategies. By adequately exploiting opportunities and effectively managing risks, companies can achieve success and competitive advantage in the international market in the European Union.

The Impact of Digitisation on Business Finance in the EU

Digitalisation profoundly impacts corporate finance in the European Union, changing how companies manage, execute and optimise their financial operations. The following are some of the fundamental changes and opportunities that digitalisation brings (Boikova et al., 2021):

1. *Digital transformation of processes.* Companies are increasingly focusing on the digital transformation of their financial processes. This includes automating accounting operations, using the cloud to store and share financial data, using digital platforms to manage invoices and payments, and introducing electronic invoicing. Digitalisation enables greater efficiency, accuracy and speed in processing financial transactions and reduces potential errors.
2. *Financial analytics and data analysis.* Digitisation enables better use of data for financial analytics and decision-making. Businesses can use advanced analytical methods such as machine learning and artificial intelligence to predict trends, detect patterns and optimise financial decisions. This increases forecast accuracy, reduces risk and improves companies' financial performance and competitiveness.
3. *Digital banking and payment solutions.* Digitalisation has also brought significant changes in banking and payments. Businesses

can use digital banking services such as online banking, mobile banking and e-wallets to carry out financial transactions, manage accounts and track payments. In addition, innovative payment solutions such as blockchain technology, cryptocurrencies and instant payments are being developed to make financial transactions better, safer and faster.

4. *Crowdfunding and alternative finance.* Digitisation has enabled the rise of crowdfunding and alternative finance models. Companies can raise funds through online platforms where investors can contribute money to finance projects and business ideas. This opens up new funding opportunities for start-ups, innovative projects and smaller companies that may find it harder to access traditional sources of finance. Crowdfunding directly links businesses and potential investors and encourages innovation and entrepreneurial spirit.
5. *Regulatory framework.* The digitalisation of the financial sector in the EU requires an adapted regulatory framework. The EU is working towards harmonised rules and standards in data security, consumer protection, anti-money laundering, and cyber security. The regulatory framework promotes and protects digital services while ensuring trust and protection for all parties involved.

The digitisation of business finance in the EU brings many benefits and opportunities for businesses. It enables greater efficiency, accuracy and speed in financial operations, better use of data for analytics and decision-making, improved customer experience in banking services and new opportunities for alternative financing. At the same time, it requires adaptation to innovative technologies, digital security and compliance with regulatory requirements.

Businesses that successfully adapt to the digital transformation of business finance can benefit from competitive advantages, increased efficiency and better financial management. It is essential that companies keep pace with technological developments, adapt to market changes and seize opportunities for digital innovation in their financial processes. This will enable them to meet customer expectations better, increase their competitiveness, and achieve success in international business in the European Union.

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Reviews

The monograph *Business Finance and Financial Governance in the European Union: Challenges and Opportunities* is a comprehensive and systematic handbook addressing key aspects of business finance and financial management in a European context. The monograph's table of contents is well structured, allowing the reader to search for and access the desired topics easily.

The authors started with an introduction to inform the reader about the book's content and highlight the importance of business finance and financial management in the European Union. Chapter 1 critically addresses the core concepts of business finance, risk and return, and EU financial management regulations and policies, providing a solid basis for understanding the topics.

The chapter on the time value of money discusses key concepts such as the time value of money, the impact of inflation, and other factors that affect the value of money over time. Financial methods for considering the time value of money are described, and an emphasis is placed on the importance of taking this concept into account in economic decisions.

The division of the chapters on equity and debt financing of a company provides a comprehensive overview of the strengths, pitfalls and strategies of raising capital. It also addresses the legal, regulatory and analytical aspects of funding and alternative funding options.

The chapter on investment risks and returns provides insight into the relationship between expected profits and investment losses. It considers the impact of the risk-return relationship, portfolio diversification, and risk-return analysis before investments. The management of investment risks is also discussed in detail, together with a comparison of different types of investments and the impact of global and macroeconomic factors.

The chapter on the cost of capital provides insight into calculating financing costs and managing financial resources. It presents the cost of capital's components and calculation methods and explains its impact on company decisions.

The chapter on capital structure addresses key aspects of capital structure, including its appropriate allocation and debt and equity

management. The importance of the capital structure is described in detail, along with the different sources of financing and how debt and equity are managed. Financial analysis of the capital structure provides the reader with insight into the analytical aspects and adapts the capital structure to the company's needs.

The chapter on financial analysis of investment decisions provides insight into calculating profitability, risk, and other key investment indicators. The methods for calculating profitability and assessing risk are described in detail, together with sensitivity, scenario analysis, and risk management in investment decisions. Practical examples of financial analysis of investment decisions further contribute to understanding concepts.

The section on the choice between renting and buying assets for the company addresses essential issues regarding strengths, traps, costs, flexibility and long-term strategy for both options. It also focuses on rental and depreciation taxes and presents exceptional cases such as real estate, equipment and rolling stock. Key decision-making and risk management issues when renting or purchasing further contribute to a comprehensive understanding of the topic.

The working capital policy chapter provides insight into the short-term management of financial resources and risk management. It describes the importance of the working capital policy in detail, along with its components, inventory management, receivables and payables, and financial analysis of working capital. Optimising working capital policy and management strategies is also a key topic.

The last chapter on corporate finance in the European Union deals with challenges and opportunities in international business. It presents business finance in the European Union, regulatory and macroeconomic challenges and the future of business finance in the EU. The development of financial instruments and markets and the impact of digitalisation on business finance are key aspects that have been explored in more detail.

The monograph offers a comprehensive and in-depth discussion of the European Union's key business finance and financial management topics. The authors have covered many essential aspects of understanding and managing European business finance.

Prof. Dr. Vito Bobek

The monograph, which focuses on business finance and financial management in the European Union, presents a comprehensive overview of the key challenges and opportunities companies and institutions face in this complex environment. The authors conducted extensive research and analysis and provided insights into several aspects that affect financial operation and management in the EU context.

The monograph's structure is thought out and well-distributed, allowing the reader to gain systematic insight into various topics. Fundamental concepts such as the time value of money, risk, and return and their application in the European financial context are discussed at the outset. This is followed by chapters focusing on specific aspects of business finance, such as equity and debt financing strategies, investment risk management, and capital structure and working capital optimisation.

An essential focus of the monograph is its scientific contribution. The authors conducted an in-depth analysis of the underlying concepts and their relation to the European regulatory environment. In addition, they presented new theoretical models that allow a better understanding of the dynamics of financial markets and institutions within the EU. This scientific study sheds light on the current state of business finance in the EU and lays the foundations for further theoretical and empirical studies in this area.

However, the monograph is not only theoretical. The authors have also carefully incorporated the practical aspects of managing financial resources in the EU business environment. Through concrete examples, advice, and strategies, they guide readers towards a better understanding and application of the acquired knowledge in real-life situations. The practical part of the monograph thus represents a valuable source of information and guidance for business professionals facing the challenges of financial management in the EU.

Furthermore, the monograph encourages discussion and further research in business finance in the European Union. The authors identify key trends, challenges, and opportunities that international business presents in Europe and propose guidelines for future research work. By discussing regulatory environments, financial policy coordination and the impact of global factors on business finance in the EU, the monograph lays the foundations for further academic and practical progress in this field.

The monograph can be regarded as a comprehensive source of in-

formation and analysis on the European Union's business finance and financial management. Its structure, combining theoretical and practical aspects, provides a thorough understanding of the economic processes and challenges EU stakeholders face. Together with numerous examples, guidelines and suggestions for further research, the monograph represents a valuable source of knowledge for academics, researchers, business professionals and decision-makers operating in the European business environment.

Prof. Dr. Jaka Vadnjal

The monograph *Corporate Finance and Financial Governance in the European Union: Challenges and Opportunities* provides a comprehensive overview of key aspects of corporate finance and financial governance in the European Union. It explores economic, regulatory, and financial challenges and opportunities businesses face in the EU financial landscape. It is structured into several chapters, covering fundamental concepts such as business financing, risk and return, financial planning, and EU financial regulations. It delves into the time value of money, analysing how inflation and other factors affect monetary value over time, emphasising financial decision-making based on future cash flows. Additionally, it discusses capital raising strategies, including equity crowdfunding, debt financing, and alternative funding methods. The book also examines investment risks and returns, focusing on portfolio diversification and risk management techniques to optimise financial decision-making. A significant part of the book is dedicated to the cost of capital and capital structure, helping businesses allocate financial resources efficiently while balancing debt and equity. Overall, the book serves as an essential guide for academics, policymakers, and financial professionals, offering insights into corporate economic strategies, governance policies, and the evolving financial landscape of the European Union.

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