

**Finance function**

is the finance department and is only found in larger businesses

**5:1 The Role of the Finance Function**

It is vital for any business to have accurate financial data. Without accurate data wrong decisions could be made which affect the business negatively.

**When will financial info be useful in business decision-making?**

**When a business decides to become more environmentally friendly**

There may be increased costs to monitor, it may need extra finance - finance function will provide this

**When the business is thinking about changing production methods**

A prediction in changes of costs will be needed from the finance function as well as what extra finance will be needed and how the changes might affect cash flow

**When the business wants to change the way it markets its products**

The finance department would provide information about the costs of these new advertising methods and may need to raise extra finance

**Financial information**

Includes details of profit, loss, cash flow, break-even, profit margin and average rate of return. These can be used to help make business decisions.

**5:3 Revenue, Costs and Profit**

	Calculation
Revenue	Quantity sold x selling price
Variable costs	Quantity sold x variable cost per unit
Total costs	Fixed costs + variable costs
Gross profit	Revenue - cost of sales
Net profit	Gross profit - expenses
Gross profit margin	$\text{Gross profit} \div \text{revenue} \times 100$
Net profit margin	$\text{Net profit} \div \text{revenue} \times 100$
Profit	Revenue - costs

Businesses will need to interpret these figures to help make business decisions

**Revenue**

Money from sales

**Average rate of return**

A method of measuring and comparing the profitability of an investment over its life

**Loss**

Occurs in a business when costs are greater than revenue

**Expenses**

The costs of operating the business

**Profitability ratios**

Calculations which help to interpret financial data

**5:2 Sources of Finance**

**Owners' capital**

Advantages	Disadvantages
<ul style="list-style-type: none"><li>▪ No need to repay the money</li><li>▪ No interest has to be paid</li><li>▪ No cost to raise the finance</li><li>▪ Readily available</li></ul>	<ul style="list-style-type: none"><li>▪ The owner might not have enough savings to cover the whole finance</li><li>▪ May leave the owner short in personal situations</li></ul>

**Retained profit**

Advantages	Disadvantages
<ul style="list-style-type: none"><li>▪ No interest has to be paid</li><li>▪ No need to repay the money</li><li>▪ No cost to raise the finance</li><li>▪ Readily available</li></ul>	<ul style="list-style-type: none"><li>▪ Business might not have enough profit to cover the whole finance</li><li>▪ May leave the business short in the future in emergency situations</li></ul>

**Loan**

Advantages	Disadvantages
<ul style="list-style-type: none"><li>▪ Repayment is spread over time</li><li>▪ Business knows exactly how much has to be repaid and when</li><li>▪ Money is available quickly</li></ul>	<ul style="list-style-type: none"><li>▪ Interest has to be paid</li><li>▪ Business may need to risk an asset as security</li><li>▪ Bank will want to see a business plan to ensure they can afford the loan</li></ul>

**Issuing shares**

Advantages	Disadvantages
<ul style="list-style-type: none"><li>▪ A lot of finance can be raised from many investors</li><li>▪ Money does not have to be paid back</li><li>▪ No interest is payable</li></ul>	<ul style="list-style-type: none"><li>▪ Dividends may have to be paid to shareholders</li><li>▪ Shareholders are entitled to have a say in the running of the business</li><li>▪ The business may be taken over by a competitor</li></ul>

**Interest**

The amount of money that has to be paid back on borrowed money

**Sale of assets**

Items sold by the business

**Crowd funding**

Money raised through an appeal to public

**Overdraft**

An arrangement with a bank to spend more money than it has in its account

**Retained profit**

Profit not distributed to owners

**Loan**

Sums borrowed for a certain period at an agreed rate of interest

**Owners' capital**

Money from savings put into the business by the owner

**Break-even forecast**

A prediction about the break-even quantity based on estimates of future sales revenues and costs

**Break-even quantity**

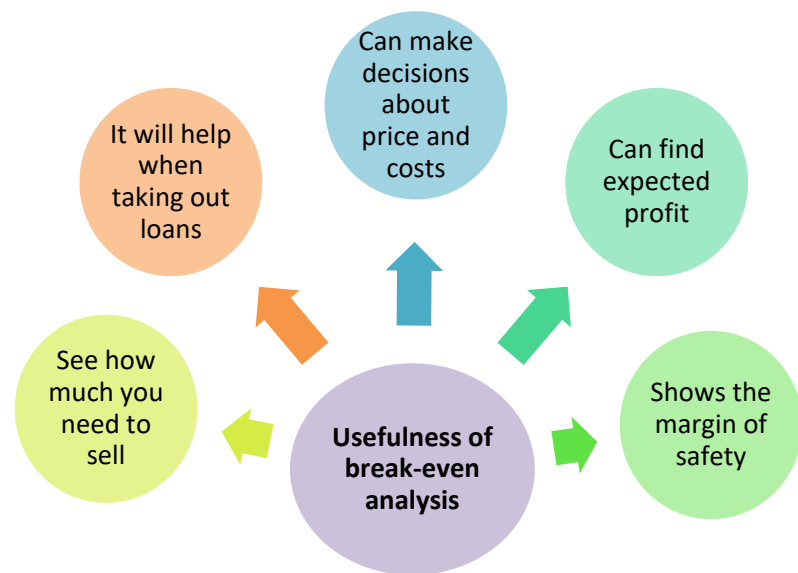
The amount a business must sell to earn enough revenue to cover its costs

**Margin of safety**

The amount by which a business' actual output is greater than its break-even output

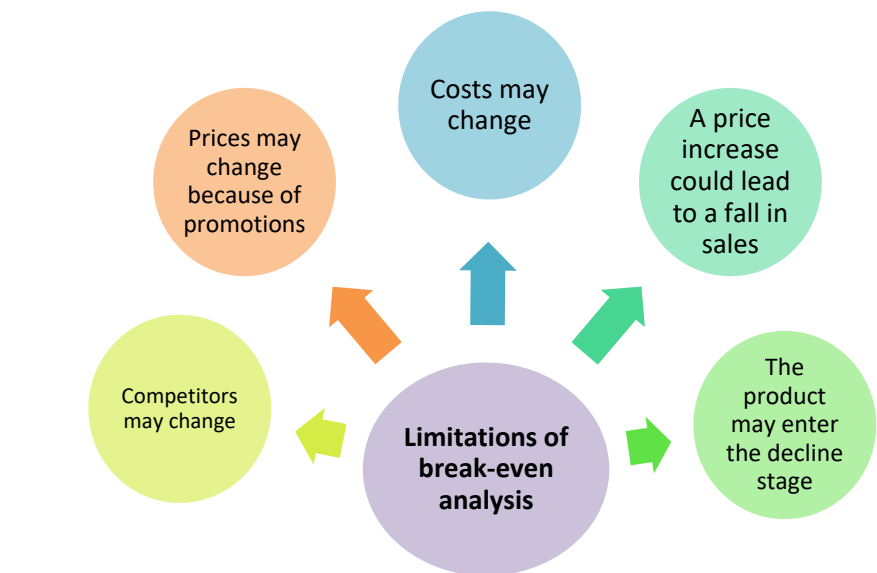
Businesses use information about revenues and costs to calculate the break-even level of output

**5:4 Breakeven**



**Calculating break even**

$$\text{Total fixed costs} \div (\text{price} - \text{variable costs per unit})$$



**Cash flow forecast:**

shows the expected flow of money into and out of a business

**Inflows**

Cash flowing into the business

**Outflows**

Cash flowing out of the business

**Expenditure**

Money that the business pays out

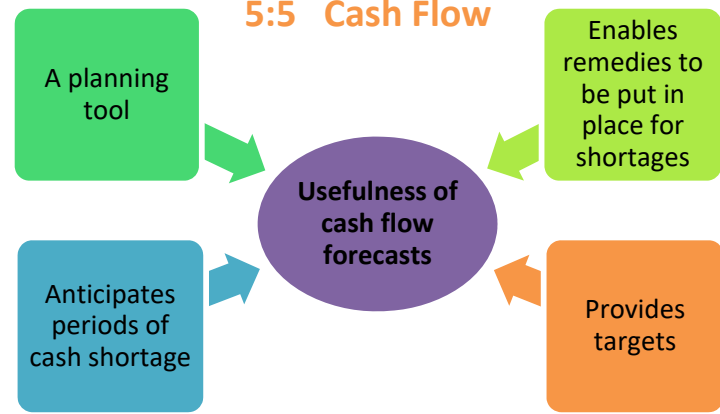
**Opening balance**

Cash available at the start of the month

**Closing balance**

Cash available at the end of the month

**5:5 Cash Flow**



A negative cash flow may:

- only be temporary and may not necessarily cause a problem for the business
- require the business to obtain additional finance in the form of an overdraft to help it overcome a shortage of cash
- mean that the business has to delay payment of money it owes to others such as suppliers

**Assessment Information**

Your assessment will take place during a normal timetabled lesson but you should be revising at home.

Number of marks available: 40  
Time allowed: 50 minutes

Answer ALL of the questions

The first 10 questions will be multiple choice - you must only select ONE answer, selecting two will score 0 marks.

The other questions will include a range of 2, 3, 4, 6, 7, & 9 mark questions

**Possible questions**

1. State one function of the finance department.
2. Calculate the profit a business would make in 4 weeks.
3. Analyse one benefit of owners' savings.
4. Recommend one source of finance for a business to use.
5. Evaluate whether a business should use a bank loan or retained profit.

**State**

**Explain**

**Analyse**

**Recommend**

**Evaluate**