SHORT-TERM FINANCIAL MANAGEMENT OF THE COMPANY

"BEREQETI" LLC

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ABSTRACT

Businesses in order to develop their activities, except fixed assets (property, land, equipment, etc), need raw materials, finished goods and labor, as to conclude the process of production and making ready products for sale.

Management of raw materials, finished goods, buyers demand, cash, etc., on the one hand, and short-term financial liabilities relates to short-term financial management company. Often this process is also known as working capital management. As part of our topic treatment will be considered the short - term funding sources, the financial operational management, cash budgeting and short - term financing plan. To illustrate theoretical concepts will be given an example at the end of the paper.

Short-term planning and financial decisions are of a particular importance for the company and its vitality, as well as for the new ones (start-up) and for those large and well consolidated. Even large companies with positive income statements have bankrupted, simply because they have been unable to carry out short-term obligations.

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Jel Classification: *G17, P40, G32*

1. Introduction

Financial management as a process has to do with the planning and decision making about important areas of the company and dealing with the decision for the usage of money as well as finding the funding sources.

Funding sources, forms and financial manners are some of the issues that the financial manager has to deal with them during his activity.

The short-term financial decisions include current asset decisions and current liabilities, or which have a lower maturity than a year.

The financial manager which is responsible for the short-term financial decisions, in the future should not go far. It must deal with the financial and operational activities related to the maximum for the next 12 months.

Unlike short-term financial decisions, long-term financial decisions deal with the financial and investment activities over 1 year or more and have to do with long-term assets and liabilities,

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as well as by nature they are not easily changed and put the company in a particular direction for several years.[3]

In following of the working paper are presented the issues mentioned above in a more detailed way.

2. Short-Term Financial Planning

In a manner to clarify the importance of financial management, initially we are presenting briefly the short-term financial planning and its role in the financial management process.

Financial planning denotes to prepare a financial plan. The financial plan is the evaluation of the total requirements of the company. It chooses the most economical sources of the company. The plan also shows us how to use profitability with the received funding. The financial plan gives a complete picture of the future financial activities of the company. Financial planning is as follows[4]:

Financial sources (Financial resources)	+	Use of funds (Financial techniques)	= Financial planning

Figure 1: Financial planning

Otherwise it can be said that the financial planning represents the strategy for:
a) Investment of surplus cash or
b) Financing of cash lack

One financial plan contains answers to the following questions:
1. How much funding (short, medium and long-term) is required by the company?
2. From which this funding will be ensured? In other words, which are the funding sources?
3. How will the company use this funding? Or how will be used these funds?

The financial plan in general is prepared during the promotion phase. It is prepared by entrepreneurs with the help of experienced professionals. Entrepreneurs need to be very careful during the preparation of the financial plan.

Financial planning as if the financial decisions are divided into different time periods, to be able to serve each other with accuracy. The literature encountered various divisions, but we have taken three divisions, as following:

[3] Luboteni, Dr.Gazmend,Financat e Korporatave,Prishtinë,2007
[4] Article from prof. Mudit Katyani in his webpage

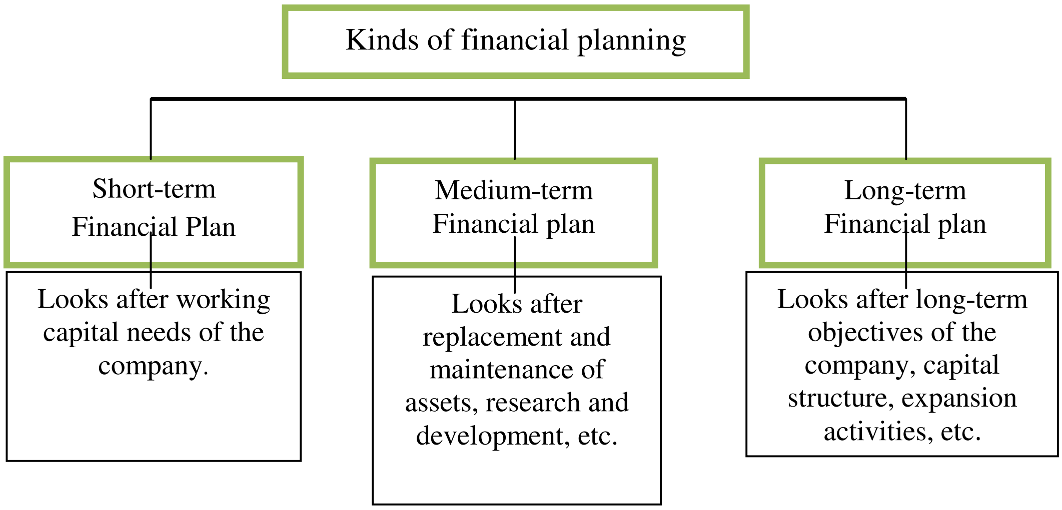

Figure 2: Types of financial planning

We mentioned that the short-term financial management has to do with the assets and current debts, respectively with the management of the working net capital. Through the figure are presented as following:

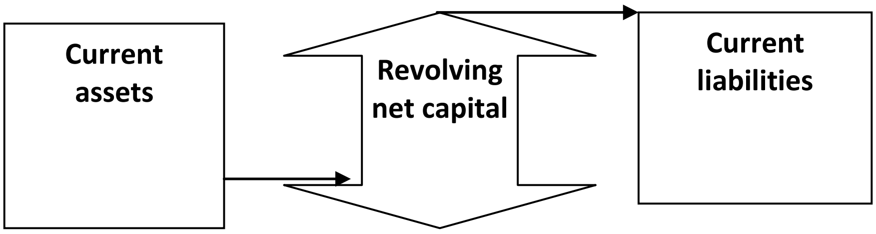

Figure 3: Short-term financial management – Working capital

2.1. Resources and Forms of Short-Term Financing

Financial sources of companies in general are internal and external sources. Internal sources include funding from proprietary capital or retained earnings, whereas the externals are dealing with loans outside the company, as those short-term as well as long-term ones. Our topic theme is the sources and forms of short-term financing.

2.1.1. Short-term financing sources

In general, a source of financing of a certain economic activity has to be in conjunction with the purpose for which will be used the funds.[5]

2.1.2. Short-term financing forms

In general we can say that the main sources of short-term financing are the trade credits (purchases with payment term), short-term bank loans, paper trading as well as outstanding liabilities (deferred payment)[6]. Below will be mentioned briefly each of them.

[5] Dr. Isa Mustafa, Menaxhmenti Financiar,Prishtinë, 2008

Trade credit- is a very important source of short-term financing. Most of companies in contemporary business are not obligated to pay the goods at the time of purchase or receipts of goods, but they have a fixed term that can do the payment, usually several days (30, 60 or max. 90 days). Thus, the trade credit appears in the moment when the supplier sells the goods and does not require an immediate payment, thus it allows a payment term.

Short-term bank loans – are a very important source of short-term financing and in this case financial are the commercial banks. In general as a source of the financing are used the small and medium-sized businesses, while the large businesses have a much greater opportunities of the financial diverse with different products and larger loan amounts. Among the most common form of short-term trade credit financing are:

- *Overdraft or the exceed of the current account*- is a very flexible way of financing, in which case the banks allow the company to use up to a certain account overdraft, causing their account be less until minus for the used amount of the working capital needs or seasonal.
- *Revolving line of credit or revolving approved lines*- these two products as short-term loans enable the company to utilize the loan up to a certain amount to the determined destination.
- *Paper trading*- represent a source less used than the first two, but still important. Usually trading papers are issued by large companies and are sold to other companies or the insurance companies, banks or pension funds.
- *Outstanding liabilities (deferred payment)* – represent a spontaneous source of the short-term financing. As more expressed forms are salaries and taxes. In both cases we are dealing with the postponing payment of two liabilities that have occurred, so to the actual business expenses that is not paid yet.

3. Short-Term Financial Management

As we have mentioned earlier, the short-term financial decisions include the current assets and liabilities. In a company it is very important to be analyzed the situation where it is situated and where is planned to be achieved. Therefore we continue to use the company's financial statements to evaluate the overall performance and its condition. After the mentioned analyses are complete, the financial planning gets a great importance. Namely the financial reports serve as the basis and as a starting point of the development of the future financial plan.

3.1. Cash Budgeting

Cash budgeting is the primary component of short-term financial planning. It relates to the cash inflows and outflows over a period of time. So, it has to do with the cash resources and the use of them. Generally different corporations use different models of preparing cash budget, including sophisticated computer programs ("corporate models"- "spreadsheets")

Looking at historical cash flow many conclusions can be drawn, but the future planning is also represented as a challenge for the financial management. There are four steps to find out how much extra cash the corporate need.

1 Step: Planning of the cash source
2 Step: Planning of the cash usage
3 Step: Calculation of the surplus or shortage of cash
4 Step: Pro-form preparation of the balance sheet

[6] Dr.Halit Xhafa, Drejtimi Financiar, Tiranë,2005

3.2. Short-term financial planning

Cash budgeting as mentioned earlier allows defining the financial need, and now it belongs to the financial manager to ensure the short-term financing to cover the needs for money. There are various options of the short-term financing, but in this part because of the more practical way treatment we have mentioned some of them, such as:

- Overdraft, Line of Credit
- Account Payable Financing
- Settlement Payment

Nevertheless, there are three common steps for the cash budget preparation.

- 1 Step: Planning of the cash source
  - Inflows from the sales receipts to customers
- 2 Step: Planning of the cash usage
  - Payments to accounts payable
  - Salaries, taxes and costs
  - Interest and dividends
- 3 Step: Calculation of the surplus or shortage of cash

In case the theoretical aspects that are shown during the working paper to be more explicit and more practical, we have done a research as it follows.

4. The Study Case

Data sheet sample for the company BEREQETI LLC (000MKD).

Unit	**2015**	**2014**	**Average**
Finished good	**5.117**	**6.444**	**5.780**
Buyers requirements – A/R	**6.446**	**6.464**	**6.455**
Suppliers liabilities –A/P	**893**	**1.169**	**1.031**
Net sales	**29.442**		
COGS	**27.282**		

The other elements of the sample are:

- Expected sales will be: 29.442
- Quarterly sales: Q1=6.436; Q2=6.598;Q3=7.317;Q4=9.093
- Initial accounts receivable = 6.464
- Receipts are 28.282. That is 96, 06 % of sales.
- Accounts payable are 79, 84 % of the short-term obtained loans and 20,16% of sales.
- Salaries, taxes and other costs are as 12, 68% of sales.
- Interest is 405 MKD for four months session, the 1, 38% of sales.
- Loans are 18.405 MKD, the 62, 51% of sales.
- Initial cash balance is 375 MKD. And at the end of the year is 855 MKD.

Is required to be calculated and prepared:

a) The operating cycle and cash cycle;
b) Cash Budgeting;
c) The short-term financing plan

The solution is as follows.

At first we right down the aforementioned formulas for calculating the operating cycle and that of currency:

1) **Operating cycle and Cash cycle**

a) **Operating cycle** = Goods days + A/Rdays
b) **Cash cycle** = Operating cycle – A/Pdays

Days of goods

Goods average = (6.444+5.117)/2= 5.780
Goods circulation = COGS/ Goods average = 27.282/5.780 = 4.72 times

Goods days = 365/4.72 = 77 days

Days of accounts receivable (A/R)

A/R Average = (6.464 = 6.446)/2 = 6.455
A/P circulation = Sales/ A/R Average = 29.442/6.455 = 4.56 times

Days of A/R = 365/4.56 = 80 days

a) **Operating cycle = 77+ 80 = 157 days**

Accounts payable days (A/P)

A/P days = (365/ A/P circulation)
A/P Average = 1.169+893/2=1.031
A/P circulation = COGS/ A/P Average = 27.282/1.031 = 26 times

A/P days = 365/26=14 days

b) **Cash cycle=157-14=171 days**

Goods and accounts receivable should be funded for 171 days.

2) **Cash budgeting**

Below we are presenting the sources and the use of cash.

Cash sources	Q1	Q2	Q3	Q4
Initial balance A/R	6.464	7.394	6.582	6.237
Sales	6.178	6.328	7.343	9.093
Cash collection	5.248	7.140	7.688	8.990
Final balance A/R	7.394	6.582	6.237	6.446

Cash fees	Q1	Q2	Q3	Q4

A/P fees	3.174	7.256	16.627	4.312
Salaries, taxes and other costs	896	1.100	1.142	594
Capital costs	0	7	0	99
Interest costs	58	48	157	142
Total cash usage	**4.128**	**8.411**	**17.925**	**5.147**

Net cash flow	Q1	Q2	Q3	Q4
Total cash accumulation	5.248	7.140	7.688	8.990
Total cash usage	4.128	8.411	17.925	5.147
Net cash flow	**1.120**	**(1.278)**	**(10.237)**	**3.843**

Cash balance sheet	Q1	Q2	Q3	TM4
Initial cash balance	375	1.495	217	(10.020)
Net cash flow	1.120	(1.278)	(10.237)	3.843
Final cash balance	1.495	217	(10.020)	(6.177)
Minimum cash balance	(68)	(68)	(68)	(68)
Accumulated surplus (absences)	1.427	149	(10.088)	(6.245)

Budgeting cash comments of the company “BEREQETI” LLC.

- At the Q3 and Q4, the company “BEREQETI” LLC has a deficit which needs to be covered.
- Sales during the 2015 are real and through the overdraft it has repaid A/P.
- However the company “BEREQETI” LLC has a positive outcome for 2015 and it covers the interest for the short-term loans.

3) Short-term financing plan

Short - term financial plan	Q1	Q2	Q3	Q4
Initial cash balance	375	(63)	(961)	(843)
Net cash flow	1.120	(1.278)	(10.237)	3.843
Net short - term debt	0	7.995	12.512	3.000
Short - term debt interest	(58)	(48)	(157)	(142)
Short - term debt repayment	(1.500)	(7.567)	(2.000)	(7.343)
Closing cash balance	(63)	(961)	(843)	(1.485)
Minimumi cash balance	(68)	(68)	(68)	(68)
Accumulated surplus (absences)	**(131)**	(1.029)	(911)	(1.533)
Initial short - term dept balance	4.500	**3.000**	**3.428**	13.940
Short-term dept change	(1.500)	428	10.512	(4.343)
Final short-term dept balance	3.000	3.428	13.940	9.597

As seen the company “BEREQETI” LLC has received a short-term debt in the second quarter, third and fourth.

5. Conclusions and Recomandations

Through the literature examination as well as the treatment of our working paper we can come to conclusion that the short-term planning and financing as a task of the financial manager requires a special concentration and commitment. Much of the business activity depends on this moment. Short-term financing decisions also require daily commitments and continuous monitoring of business.

Below we list some of the main conclusion of the working paper:

- Financial planning has to do with the surplus investment and/or the absence of financing
- Short-term financial decisions are more easier than those long-term ones but not less important
- There are software models of the cash budgeting preparation across various corporations.
- From the cash and cycle operating analysis can be observed the short-term financing need of the company "BEREQETI"LLC.
- Cash budgeting in short-term planning is done in maximum for 12 months.
- Short-term financing mainly has to do with the accounts payable usage or bank loans at mostly 12 moths.
- But, regarding the recommendations we can say that:
- Financial manager should pursue a balanced policy between the conservative and aggressive policy, and in this case should be considered issues relating to the cash reserves (1), the compliance maturities (2) and interest rates (3);
- Because of the costs and other limitations, intern resources need to be considered primary for funding the business activity of the company;
- To not be used the credit lines or overdraft (OVD) for investment purposes;
- To be used the short-term loans for current needs of the companies;
- To be held the cash reserves for emergencies that may occur in the company.

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