VIDYA BHAWAN BALIKA VIDYA PITH

शक्ति उत्थान आश्रम लखीसराय बिहार

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BUSINESS FINANCE (Important question answer)

Question 1:

What is business finance? Why do businesses need funds? Explain.

ANSWER:

Business finance refers to the funds required to carry out the establishment and running operations of a business. These operations include purchase of premises and payment of wages and salaries. The funds required to finance the expansion of a business are also considered a part of business finance.

The following are the reasons why a business needs funds.

(a) ***Fixed capital requirements:*** For setting up a business, fixed assets such as building, machinery, furniture and fixtures are required. The requirement of funds to purchase these assets is known as fixed capital requirement. The level of requirement of funds depends upon the size and nature of a business.

(b) ***Working capital requirements:*** Firms require funds for financing their day-to-day operations such as purchase of raw materials and payment of wages to workers. The requirement of funds for such operations is known as the working capital requirement.

Question 2:

List sources of raising long-term and short-term finance.

ANSWER:

The following are some of the sources of long-term funds.

(a) ***Equity shares:*** These represent the ownership capital of a company. The holders of such shares enjoy a say in the management and gain higher returns when the company earns higher profits.

(b) ***Retained earnings:*** These are the undistributed profits of a business that are retained in the business for future use.

(c) ***Debentures:*** Debentures are financial instruments used by companies to raise long-term debt capital. They carry a fixed rate of return and specify a time for repayment.

The following are some of the sources of short-term funds.

(a) ***Trade credit:*** It is the amount of credit that is extended by the supplier to the purchaser. It facilitates the purchase of goods on credit.

(b) ***Banks:*** Business enterprises can also obtain short-term funds from banks.

(c) ***Commercial paper:*** These are credit instrument used by creditworthy firms to obtain short-term finance for their business.

Question 3:

What is the difference between the internal and external sources of raising funds? Explain.

ANSWER:

Internal sources of funds are those that are generated within a business enterprise. When an enterprise obtains funds by selling surplus inventories, collecting bill receivables or by reinvesting profits, these funds are said to have been generated from internal sources. Internal sources of finance can satisfy limited needs of a business as the amounts that can be raised from such sources are generally small.

On the other hand, funds raised from sources outside the organisation, such as the suppliers, creditors, investors, banks and financial institutions, are known as funds from external sources. The amounts that can be raised from external sources are large, and therefore these funds can be used to finance large operations.

Question 4:

What preferential rights are enjoyed by preference shareholders? Explain.

ANSWER:

Preference shares are shares that provide the shareholders preferential rights regarding the repayment of capital and payment of dividends after a certain specified period of time. Preference shares are issued by a company to raise capital, and the repayment to preference share holders is made in accordance with the terms specified in Section 80 of the Companies Act, 1956. Preference share holders are entitled to the following preferential rights.

(a) Preference shares entitle their holders the right to receive dividends of a fixed amount or at a fixed rate.

(b) Preference shares entitle their holders the preferential right to receive repayment of capital invested by them before their equity counterparts at the time of winding up of the company.

Question 5:

Name any three special financial institutions and state their objectives.

ANSWER:

Financial institutions refer to central or state government establishments that exist to finance business operations. These institutions provide long-term finance to firms to help them in their expansion, modernisation and reorganisation programmes.

The following are the three main financial institutions.

(a) ***Unit Trust of India (UTI):*** The UTI was established in 1964 under the Unit Trust of India Act, 1963, with the objective of mobilising the community's savings and utilising the funds to finance profitable ventures.

(b) ***Industrial Credit and Investment Corporation of India (ICICI):*** The ICICI was established as a public limited company in 1955. The main objective of the ICICI was to facilitate the creation, modernisation and expansion of enterprises in the private sector.

(c) ***Industrial Finance Corporation of India (IFCI):*** The IFCI was established in 1948 under the Industrial Finance Corporation Act, 1948, with the objective of facilitating regional development and encouraging new entrepreneurs to enter the priority sectors of the economy.