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Financial Management of Economic Entity from the Perspective of Alternative Approach

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Abstract

Throughout the study the financial management presented is divided into three directions, namely financial analysis, financial planning and financial strategy, focusing on increasing the quality of financial management conducted at the economic entity by identifying an easier possible use for a system of alternative decisions in order to increase the profitability. The study also aims to identify new meanings of financial accounting information system in performing the managerial act through alternative decisions, trying to highlight the need to create a management tool generator of variants possible to be adopted with an impact on their application in the economic entity as a whole. Based on qualitative research on the financial management act, it is revealed the importance of the financial management act manifested in the economic entity and also its quality improvement through simulations targeting the management through budget system.

Key words

Economic entity, financial management, alternative decisions, profitability, management through budgets

JEL Codes: E62, G32

1. Introduction

Increasing the performance of the economic entity is possible in the context of adopting the proper decision to fully reflect the expectations of management, employees, investors and even collaborators, paving the way towards identifying new availabilities and new areas in which they will be used in order to fully achieve the goals of the economic entity. Considering predetermined objectives and the achievement of performance indicators proposed and approved through the warrant of the economic manager of the entity, it focuses on adopting fundamental decisions that insure the functioning of the economic entity in a set of legal provisions in the fields of social protection, taxation and accounting.

Financial management as part of the overall management must identify with the adopting of the best financial decisions. For this initiative to be fully implemented is mandatory the use of new types of management tools which facilitate simulation of alternative decisions supported or based on scientific reasons whose main purpose is to respond effectively and rapidly to requirements of the financial policies established and approved by the economic entity. Through these alternative decisions we are pursuing:

- Increasing the value of net assets available of the economic entity;
- Satisfy the interest of investors or shareholders which is to maximize their income.

Knowing all instruments, all financial assets, financial control variables [1] and processes and their use in decision-making process or in the process of coordinating their actions is an action that places financial management among activities of great importance in the life of any economic entity. Also, alternative decisions researched by financial management documents, analyzed and selected by them to adopt, are essential elements to strengthen control of collaborations with “financial partners and the markets which have implications in the activity”.[2]

Amid the dynamic development of financial flows on the European economic market, and in the context of economic globalization, Romanian economic entities are forced to refocus in terms of complying with new regulations and trends observed internationally, and management must undergo a stage of development, a change in mentalities and approaches, adapting to the needs of stakeholders in the life of the economic entity and adapt to global economic expectations.

Therefore, the financial management developed in the economic entities of our country represents a decisive element in Romania's integration into world economy; the qualities of financial management lie in the fact that it insures a performance increase of the economic entity on the long run, risks associated with financial accounting are known, analyzed, treated and kept under control, and not least solvency is maintained in a comfort zone to increase the competitiveness of the economic entity [3].

2. Literature review

In the area of financial management and financial decision as a direct result of its level of knowledge currently revolves around collecting, knowledge, analysis and interpretation of financial accounting information, the quality of which is strictly linked to quality and efficiency of the decision. We should not overlook the fact that financial management is placed on top among the important activities of the economic entity, being necessary to give it more attention.

Currently, the literature shifts us towards three categories of financial information underlying the statement, analysis, selection, adoption and improvement of financial decision. We present an excerpt from an article that reflects the views of the author of

these scientific papers in the most eloquent manner the types of information used in decision-making:

- *general fiscal, economic and monetary information;*
- *information regarding the economic sector of the enterprise;*
- *economic and legislative information on the enterprise". [4]*

Any process of management, therefore financial management as well, has three fundamental structures: *planning, analyzing and strategy*. We will describe below, these lines of action specific to financial management:

– *Financial planning* is a process of establishing actions necessary to achieve the targets set for the performance indicators that measure the degree of achievement of specific objectives and measures taken to accomplish the requirements of financial policies. Planning can be done several times: on a short-term (1 year), medium term (1-3 years) and long term (3-5 years). Depending on the targeted areas, financial planning is thus described:

- *Financial Planning* on the short-term or on a daily basis, involves establishing a set of actions to be taken during a financial year, primarily aimed at balancing the budget and getting the maximum profit possible, thus increasing to a maximum the level of revenue making charges at the minimum possible level;
- *Financial planning* to upgrade or on the medium term, that considers the development of activities, a refurbishment by introducing modern equipment, an investment process supported by new ways to improve the products or services offered, which can contribute to a good position on the selling market or to strengthening the existing one; applying the concept of "asset management" that involves management activities and financial tangible assets is common in this type of financial planning;
- *Strategic financial planning*, on the long-run has as central objectives the growth of capital by attracting new investors interested in its business, conquering new market segments, untouched before by diversifying products and services and increasing their availability. Such planning targeting long periods of time, up to 5 years, are a challenge for financial management that needs to activate and use the full capacity of revision function and its capacity to analyze and estimate the evolution, possibilities of development as well as the capacity to estimate what could happen during this period of time in the economic environment in which the entity operates.

– *Financial Analysis* is another complex course of action of financial management, without which the economic entity will not be able to know, in an objective and real way the dangers, risks and vulnerabilities to which it is exposed, it will not be able to operate in a reasonable manner the opportunities that it may encounter. To have a normal support for financial management, financial analysis consolidates a number of

techniques, tools and methods that have as central point financial information and this information is gathered, processed, classified, it is improved so that it is a defining element for financial decision-making;

– *Financial Strategy* is the third direction of financial management that helps the economic entity to establish support points that if followed will help achieve forecasted objectives; in literature we identified a definition of financial strategy that we believe is suitable to the topic studied: *"all long-term decisions (investment, financing, distribution of net profit decisions) through which are outlined possible paths to ensure a lasting and dominant positions in the competitive economic enterprise environment"* [5]. Starting from what concepts and interpretations exist up to date, on this research, we suggest as a topic of analysis in this material, the establishment of a decision-making system whose parts are alternative decisions, elements that support financial management in increasing the performance of the economic entity.

3. Methodology of research

The thorough study of *financial management* has been focusing on gathering information and analyzing their theoretical information as well as using a set of technical research that showed consistency and relevance of decision-making in the financial management system of the economic entities.

The research for the study focused on financial management and alternative *set of decisions* that can be generated for the future development of the economic entity. During studying financial management we have used several techniques such as in-depth research and research with a focus on development. Complementarity, observing and correspondence have been the main principles of scientific research that were taken into account in drafting this study. The bibliographic research was performed using sources represented by works found in national literature as well as international one. The study involved the creation of bibliographic records for synthesizing information; translation of literature, data processing synthesized using specific software tools (Microsoft Excel). Indexed databases were consulted of research in the field. The theoretical approach was complemented by an empirical research carried out at an economic entity which reveals the objective regarding management through *budgetary system*.

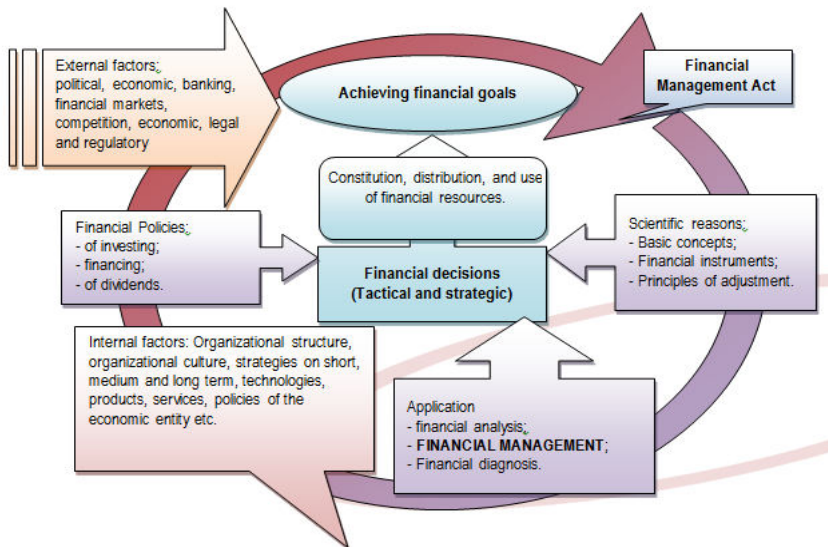
4. The way the environment manifests on financial management

"Management is a process involving a mixture of rational development of logical decision making and problem-solving activities with activities of intuitive judgment" [6].

By extension from this definition of general management, we say that financial management is the sum of manifestation possibilities in use, of financial management process, which has as main target increasing the value of the economic entity and

attracting those resources necessary to accomplish the object of activity. The following chart reflects the influence of external and internal factors on the activity of the economic entity following the impact of the financial management process, the financial and accounting policies and procedures and their application in practice.

Figure 1: Interaction and action of external and internal factors on financial decision



Source: own design

The above figure shows that to adopt financial management decisions management should focus on several areas, namely: theoretical directions and rational directions. Financial management founded on diagnostic analysis is based on tools and regulatory principles, on financial analysis and financial techniques. Alternative financial decisions are affected by internal and external factors of the economic entity. Detailing, internal factors are those targeting the organizational structure, functional and hierarchical relationships, organizational culture, policies and development strategies and the level of technology; external factors are determined by the competitive environment, the legislative framework, the political and economic environment. The fulfillment of the objectives and targets set by the economic entity can be achieved through a series of complex activities that interconnect, creating a system that works consistently and requires modeling in certain segments, influencing other components, so it is recommended to shape the whole system.

In conclusion: *"Things that need to be achieved by an effective manager, the items that will help form him, are defined through a careful analysis of the specific nature and circumstances of his business [...]"* [7].

Improving financial decision in economic entities

From literatures' perspective, decision is defined as a *"decision made after analyzing a problem, a situation etc., an adopted solution (from several); resolution"* [8]. Continuing literature review we noted several aspects related to the components of financial decision:

"a) The decision regarding the funding sources of the company's activity on different terms (short, medium and long term). This refers both to identifying sources and determining the amount of funds that can be provided from these sources.

b) Decision concerning the use of financial funds for investments, called investment decision, both in decision theory and in the practice of the entity.

c) Relative decision at the time of using the monetary funds of the company, namely their allocation for present or future consumption" [9].

In order to select the most adequate decision from a list of possibilities, Robert J. Marzano [10], considers that the following steps should be followed:

"- think of many other possible alternatives.

- think of the weak and strong points of each alternative.

- think of the probability of success of the best alternatives.

- chose the best alternative based on value and probability of success" [11].

As it can be seen, the financial decision must be founded, so that it can use concrete and tested action alternatives so that the decision maker to choose the right decision according to the scope and objectives of the economic entity.

Based on the analysis performed, we believe that to achieve an efficient financial management process it is useful that the decision factor, the leader of the economic entity should use substantiation and adoption tools of financial decision, that are timely, responsive and easy to apply. Among the instruments deemed appropriate for financial management "The Scoreboard" stands out. By extension, we consider that the financial decision can be substantiated and selected through a "Scoreboard" specialized on the financial field, conducted on the basis of economic and financial indicators whose calculation method use elements similar to those used in management performance evaluation activities designed and carried. Developing widespread use of a "Scoreboard" specialized in finance is likely to determine the choice of certain decisions and at the same time to show the decision-maker, the consequences of financial decisions on other sectors of the entire public entities.

Concluding, "The Scoreboard" specialized in finance can support financial management through elements from all sectors of the economic entity and allow

dimensioning the financial consequences of alternative decisions, thus creating an adequate system of financial decisions.

5. Management through budgetary systems

In the context of scientific research, adopting the Order of M.F.P. no. 1802 from December 29 2014 [12] will have a significant influence on the entity accounting and on the economic and financial management of it, from two perspectives:

- The one of financial reporting to ensure financial and accounting information useful, comparable, transparent and not least with a reduced cost to obtain them;
- The one of financial analysis through financial indicators derived from financial statements, but also through the income and expenses budget associated to performance criteria or indicators attached to the income and expenditure incurred by the management of the economic entity.

From the perspective of financial analysis and financial indicators, we delivered during this study, the insurance of the financial management of the economic entity as a whole, presenting below some practical cases targeting management through the budgetary system.

Case 1

Evaluating the achievement of revenue resulting from reviewing the key indicators included in the income and expenditure budgets for the years 2014, 2015 and the proposal for the year 2016 we found:

Table 1. Level of achievement for 2014-2015 and proposals for 2016

Indicators	Approved 2014	Achieved 2014	Level of achievement 2014 (%)	Approved 2015	Achieved 2015	Level of achievement 2015 (%)	Proposal BVC 2016
Total income, from which:	1.550.220	1.297.345	83,69	1.536.534	1.372.603	89,33	1.527.808
Operating income	1.446.425	1.202.447	83,13	1.447.646	1.276.419	88,17	1.438.095
Financial income	103.794	94.898	91,43	88.888	96.184	108,21	89.713

Although the level of achievement of „total income” for the year 2014 was 83.69% (1.550.220 thousands lei – approved/1.297.345 thousands lei – achieved) and for the year 2015 was 89.33% (1.536.534 thousands lei – approved/1.372.603 thousands lei – achieved), for 2016 „total income” indicator was not founded in a realistic manner (value of 1.527.808 thousands lei), thus infringing on paragraph (2), art. 9 from Government Order no. 26/2013, that says: *”In case the degree of achievement of total revenues approved in the budgets of income and expenditure in each of the last 2*

years was less than 90% of total revenue, justification for the current year is at most to the level of achievement of those from the previous year” [13]. For 2016 the total income justification should be limited to a maximum value of 1,372,603 lei and not to the value of 1,527,808 lei.

Furthermore, the unrealistic justification on the one hand and also the inefficient operating activity has determined each year the failure to achieve the revenues determined by the income and expenditure budget, which requires the management attention to make the activity performed by the economic entity more efficient.

Case 2

Assessing the fulfillment of objectives and performance criteria

Analyzing the Annex to the budget of revenues and expenditures approved as well as the budget implementation for the period 2013-2015, it follows that the objectives and performance criteria were not achieved and assumed by the management of the economic entity for the years 2013, 2014, 2015, the situation being presented in the table below:

Table 2. Revenues and expenditures for the period 2013-2015

(thousands lei)

Objectives and performance criterion	2013		Î/NÎ	2014		Î/NÎ	2015		Î/NÎ
	1	2	3	4	5	6	7	8	9
0	Approved	Achieved		Approved	Achieved		Approved	Achieved	
Outstanding payments (thousands lei)	295,06	117,84	NÎ	63,00	17,78	NÎ	14,00	0	NÎ
Overdue receivables (thousands lei)	3.800,00	2.795,81	NÎ	2.790,81	2.980,09	NÎ	3.300,00	3.215,12	NÎ
Expenses decrease (expenses to 1000 lei total income) (lei)	1.144,99	1.102,20	NÎ	1.075,35	1.084,91	NÎ	1.005,00	1.019,98	NÎ
Work productivity (thousand lei/ person)	1.129,12	1.097,60	NÎ	707,30	611,00	NÎ	725,27	678,95	NÎ
Sold production (thousands lei)	1.109.81 0,06	1.085.18 1,05	NÎ	1.394.07 8,21	1.138.69 6,98	NÎ	1.394.41 1,90	1.136.72 3,60	NÎ

Legend: Î – fulfilled / NÎ – not fulfilled

During 2013-2015 the objectives attached to performance criteria were not achieved and assumed by the management of the economic entity studied, as follows:

- The criterion of 'outstanding payments', the reduction target has not been achieved both in 2014 (achieved ~73.57%), and in 2015 (achieved ~97.42%);
- for the criterion "expense 1,000 lei to total income" the objective to reduce expenses to 1000 lei total income was not met, the value of the indicator was exceeded in both 2014 (with ~ 0,88%), as well as in 2015 (with ~1.49%);
- During the period verified, the objective of achieving work productivity was not met, work productivity recording a continuous decline from 1097.60 realized in 2013 to 378,95 in 2015;
- The criterion of sold production was achieved under the endorsed level and assumed as follows: 2013 ~ 97.78%; in 2014, ~81.68%; in 2015, ~81.51%.

Case 3

By analyzing Chapter X "Data substantiation" presented in the income and expenditure budgets approved for the years 2013, 2014, 2015 the outcome is that the following indicators were not achieved: "Average monthly earnings per employee (lei/person) determined based on the adjusted salary expenses "has been exceeded while" work productivity in total value units per total personnel average (thousand lei/person) "has not been achieved:

Table 3. Indicators for period 2013-2015

(thousands lei)

Year	Average monthly earnings per employee (lei/person) determination based on the adjusted salary costs			Work productivity in total value unit per total personnel average (thousand lei /person)			Number of personnel at the end of forecast		
	Approved	Achieved	Exceeding	Approved	Achieved	Unfulfilled	Approved	Achieved	Achieved
2013	5.307,75	5.426,54	102,24%	1.129,12	1.097,60	97,21%	2.110	2.112	100,09%
2014	5.427,97	5.488,86	101,12%	707,30	611,00	86,38%	2.110	1.986	94,12%
2015	5.532,40	5.854,00	105,81%	725,27	678,95	93,61%	2.083	1.980	95,06%

Average earnings per month per employee (lei/person) determined based on costs of salary has been exceeded every year, while work productivity in value units for total personal average (thousands lei/person) was performed considerably below the threshold approved and assumed by the management of the economic entity.

No correlation was observed between the monthly average gross salary increasing per employee and the work productivity index. According to article 9 paragraph (3), from Order no. 26/2016 during the financial exercises from 2013, 2014, 2015 "the monthly average gross salary increase per employee may not exceed 60% of work productivity index calculated in physical or value units". In 2013 the indicator "Number of personnel at the end of forecast" was exceeded with 0.09% (2.110 - approved vs. 2.112 - achieved) infringing on art. 10, paragraph (1), let. a) from Order 26/2013 that states:"

(1) *The budgets of income and expenditure shall conform to the following rules: a) salary related expenses, number of staff at the end of the year, approved by the income and expenditure budgets represent maximum limits that cannot be exceeded*" thus setting a contravention according to art. 13 let. (e) from the Order 26/2013, punishable by a fine between 5000 lei to 10000 lei.

Increasing the performance of the economic entity through alternative financial decisions requires from the management to fulfill the following conditions cumulatively:

- substantiation of the financial decision must be based on the financial information provided to decision-makers through a financial and accounting information system that is effortless and functional;
- selecting the most appropriate variant of financial decision in a relevant period is conditional on the inclusion of accounting management into the database managed by the financial and accounting informational system of the economic entity. Thus, accounting management may provide the decision maker with a set of necessary and timely information in a reasonable time, all of which are advantages; but, instead we find a series of disadvantages in using accounting management, including the most important one: the degree of accuracy of data that can sometimes be affected;
- coordination between management and financial decisions. Financial decision is a process that is done knowingly, positioning the business entity in a comfortable external environment to which it belongs;
- bringing to the attention of those concerned, an accurate financial decision content, so the one who adopted it made sure that it was understood clearly thus implementing will have maximum beneficial effect for the economic entity.

6. Conclusions

Financial management is focused on organizing and managing methodical activity and improving the activity of the economic entity through various ways:

- through budgetary system, especially financial forecast;
- Monitoring and continuous assessment of the achievement of financial targets planned;
- The effective management of assets and liabilities of the entity etc.

From the content of this scientific research it is noted that the theoretical, methodological and empirical approaches, any act or omission of the economic entity's management results in influences on the financial position and performance of the entity. These influences are reflected on the financial and accounting informational subsystems created in the activity sectors, on the financial and accounting informational system as a whole, on the informational management system and not least on the financial statements of the reporting entity. The complexity of the financial management process implemented within the economic entity determines the need for

a coherent financial and accounting informational system that will provide qualitative, relevant and opportune information. The beneficial effects of the financial management process on the activity of the economic entity are reflected in the results:

- financial stability of the economic entity;
- maintain control over expenditure and use in terms of efficiency and economy of the resources of the economic entity;
- the growth of the economic entity's performance reflected in profit maximization and for economic entities ensuring to maintain the financial balance while developing investment by improving the financial framework and by keeping in check the financial risks that the entity could assume;
- optimizing the economic entity cash flow;
- efficiency in the use of financial, human and logistic information etc.;
- strengthening the position of the economic entity in the economic and social environment in which it develops.

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