

FINANCE AND ACCOUNTING
for
MANAGERIAL
COMPETITIVENESS



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KAPIL DHAMEJA

S. CHAND

FINANCE AND ACCOUNTING FOR MANAGERIAL COMPETITIVENESS

Revised and Enlarged Edition by

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FOREWORD TO THE REVISED EDITION

Human being without spine will akin to a corporate without able finance team. Rapid strides taken by finance are witnessed in vertiginous growth of finance professionals in last decade or so whether in corporate finance role or investment banking role.


Today finance manager is not only expected to take decisions based and financial parameters but also sound business rationale. Therefore, it would not be too stretched to say that a good finance professional is one who is a good business manager.

Two similar enterprises show different results and their managements' performance differs, primarily due to lack of clarity on the financial implication of the decision, in particular in the fast changing economic scenario and the rapidly developing area of finance and accounting.

Finance functions, as described in this book, comprise of (a) accounting and control, known as 'controller' and (b) financial policy matter known as 'treasurer', the former serves the purposes of a score board, attention-direction and problem-solving (chapters two to fourteen). The latter, the treasurer function of basic 'financial policy matters' covers investment decisions, capital structure planning and cost of capital and working capital management (chapters fifteen to seventeen); and emerging areas like infrastructure management, international finance are discussed in the last three chapters.

Last but not least, who better than Prof. Nand Dhameja with a passionate experience of over 40 years in this field to talk to this. If there was ever a list of most passionate and connected teacher (with students) above 60 years, I am sure Prof. Nand Dhameja will top the chart. Prof. Nand Dhameja has very simply put pen to his good oratory skills to bring out an interesting and elucidating book where he has tried to bring out energy of live classroom teaching in his books through examples and counterexamples.

I congratulate Prof. Nand Dhameja and his team for their great performance and wish them all the success.



Dr. BRIJMOHAN LALL MUNJAL

FOREWORD TO THE FIRST EDITION

In today's fast-changing economic environment, competitiveness, in terms of cost and productivity, is the key to success for any productive enterprise. Financial executives are, usually, assigned the responsibility for managing finance and cost to the best advantage of a company, but, in the changed context, such a responsibility has become very relevant at all the key decision-making points in an organisation. Decision-makers must recognise this reality, and would need to ensure that decisions, which have an impact on cost and productivity, are taken at every point in the organisation with professional competence.

We, in India, are yet to grasp the full implications of the changes currently sweeping our industrial environment. We continue to think in terms of compartmentalised functions and delude ourselves into believing that decisions, which have finance and cost implications, will be taken necessarily by a separate and exclusive group of people. This arises from the 'mystique' that one attaches to finance and cost disciplines. If we have to survive in a competitive world, this 'mystique' has to be broken; and towards that end, the present book is an extremely laudable effort.

Dr. Nand Dhameja and Dr. K.S. Sastry are acknowledged experts in the areas of finance and accounting, and they must be complimented for addressing themselves, assiduously, to this timely task of bringing out a book which will be of invaluable help for managers in taking crucial decisions impinging on productivity. Quite understandably, the book focuses on analysis and understanding of financial statements; the different building blocks for cost and cost sheet, for control and responsibility accounting; the complex elements that go into capital investment decisions; and working capital management. There are, of course, many books dealing with these topics, but the outstanding merit of this publication is its lucidity and clarity.

A good textbook is basically a labour of love, and brings out transparently the care and attention that has gone into it. This book passes this litmus test. It will certainly be a good textbook for students, but, more importantly, it should find a place on the bookshelves of every practising manager, particularly those who are not directly concerned with accounting and finance disciplines.

D. N. GHOSH

Disclaimer : While the authors of this book have made every effort to avoid any mistakes or omissions and have used their skill, expertise and knowledge to the best of their capacity to provide accurate and updated information, the authors and S. Chand do not give any representation or warranty with respect to the accuracy or completeness of the contents of this publication and are selling this publication on the condition and understanding that they shall not be made liable in any manner whatsoever. S.Chand and the authors expressly disclaim all and any liability/responsibility to any person, whether a purchaser or reader of this publication or not, in respect of anything and everything forming part of the contents of this publication. S. Chand shall not be responsible for any errors, omissions or damages arising out of the use of the information contained in this publication.

Further, the appearance of the personal name, location, place and incidence, if any; in the illustrations used herein is purely coincidental and work of imagination. Thus the same should in no manner be termed as defamatory to any individual.

PREFACE TO THE REVISED EDITION

Pager to ipads, State Banks to Investment Banks, domestic finance to international finance... that is how finance has changed in the last 10 years. In this fast-changing world, it is important to be abreast with the latest trends, updates and evaluation metrics for companies.

The revised edition of the book factors in such rapid changes in trends and is an enlarged and updated edition incorporating various developments over the years without going into intricacies of the subject.

As a result, some chapters have been merged, reorganised or updated and many new chapters have been added. The revised edition has twenty chapters and one annexure. The new chapters added include:

Chapter 7 : Financial Analysis : Creative Accounting – A Checklist

Chapter 19: Infrastructure Management and Financing: PPP Approaches and Experiences-India and Abroad

Chapter 20: International Financial Management

Annexure: Glossary of Finance and Accounting Terms

Chapters 2, 6, 8, 9, 12, 15, 16, 17 and 18 have been revised and enlarged. These chapters have been reorganised to discuss the various concepts and techniques, though the technicalities have been presented in appendices to respective chapters, a reader not interested in the technicalities can skip these appendices.

Details of cash and accrual bases, single entry system prevalent in government and the steps to convert from cash basis to accrual basis are illustrated in the Appendix to Chapter 2.

Aspects relating to material planning, procurement, storage and issue and to Activity-based costing approach of overhead allocation are presented in two appendices to Chapter 9.

Chapter 12 on Control and Responsibility Accounting has been reorganized to include details relating to responsibility centres, performance parameters like, ROI, EVA, Balanced Score Card and Mumbai Dabbawalla.

Certain advanced aspects of capital investment decisions are contained in the Appendix to the Chapter 16.

Chapter 17 has been recasted to contain aspects relating to capital structure planning, cost of capital, CAPM approach.

Chapter 18 titled, Emerging Trends in Accounting and Finance covers leasing, inflation accounting, human resource accounting, value-added statement, financial crisis and growing financial practices of shared services.

Every chapter starts with the Learning Objectives and concludes with 'Key Points to Remember' and 'Key Words'. In order to enable the interested reader to assess understanding of the subject and to have more practice, a set of evaluation section has been added at the end of every chapter. The evaluation section contains:

- Self-Assessment Questions
- Problems
- Exercises/Cases

Attempts have been made to keep the book a simple and a lucid reading, a reader not interested in technical aspects can skip the appendices to the various chapters.

Various people provided their different perspectives and utility of various topics in this book to practicing manager. First and foremost, thanks to Prof. Mukul Gupta, Director MDI, Gurgaon for his valuable guidance and facilities and also for his coaching on the nuts and bolts of accounting from his experience of entrepreneurship and academics.

Prof. N R. Bhusnurmath, MDI suggested practical and relevant changes from his experience of the corporate world assessed through the lenses of his students, and we express our thanks to him. We acknowledge with thanks Prof. Shailender Kumar Rai, MDI for his observations on the draft revised chapters. Prof. Pranab Banerji, IIPA guided at the various stages of the revision and we are thankful to him. We are indebted to Mr. Anthony Jose, Librarian MDI for helping us with various inputs in completing the book.

Dr. Samo Bobek, Dean Department of Economics and Business, University of Maribor, Slovenia has been instrumental in the process of the revision, in particular for his extensive comments on the chapters revised and added, and we would like to convey our thanks to him. Last but not least, best input always come from students. Therefore, most sincere thanks to participants of various programmes for their comments and suggestions; we do hope the revised edition would meet their expectations. We are indebted to our esteemed colleagues and friends for their valuable suggestions and comments at different stages of the book.

We would like to express our gratitude to Dr. Brijmohan Lall Munjal Chairman of Hero MotoCorp., Hero Cycles, and Munjal Showa Ltd. He is a man of world fame for his contribution to industry and society. He has been honoured with the award of Padma Bhushan, and also has a number of awards to his credit which include:

- National Award for outstanding contribution to the Development of Indian Small Scale Industry
- The Distinguished Entrepreneurship Award by the PHD Chamber of Commerce and Industry
- Sir Jehangir Ghandy Medal for Industrial Peace Award by XLRI
- Ernst & Young Entrepreneur of the Year Award
- Lifetime Achievement Award by TERI
- Lifetime Achievement Award by Ernst & Young
- Lifetime Contribution Award by All India Management Association
- Lifetime Achievement for the Asia Pacific Entrepreneurship
- Award by Enterprise Asia

He has always been a source of inspiration and expert guidance; he has agreed to write a Foreword to the book and we are indeed grateful to him

Our publishers deserve thanks for timely bringing out the book

We would welcome suggestions/comments from the readers as these would be helpful in the further revision.

Prof. NAND DHAMEJA
Prof. K.S. SASTRY
KAPIL DHAMEJA

PREFACE TO THE FIRST EDITION

This book covers various techniques and tools of finance and accounting and discusses their application in a variety of decision-making situations. Without going into the intricacies or mechanics of accounting, it seeks to explain the various concepts of financial and management accounting to help the reader understand accounting as a business language.

The book is based on the premise that a manager, in order to be competitive, should know the resources that have been deployed and also the costs related thereto, and be fully conscious of the impact of his decisions on the performance of the enterprise he works for. Hence, he should be equipped with proper understanding of accounting and finance.

The book has been developed on the basis of our teaching, training and consultancy experiences gained over the past two decades. Many techniques and tools discussed in the book have been tested for their managerial use and effectiveness at a number of training programmes organised by the National Productivity Council of India, Administrative Staff College of India and the Management Development Institute, Gurgaon, especially at its National Management Programme. However, we look forward to getting suggestions from our readers for further improving the book.

The book is intended primarily for managers in various functional and service areas involved in decision-making, and will also be useful for those pursuing a management programme for courses in the areas of management accounting and finance.

The book is divided into 18 chapters.

Chapter 1 provides an overview of the finance function. Chapters 2 to 6 deal with financial accounting, financial statements and their analysis, ratio analysis, and funds flow statements. Cost, cost accounting and its uses for planning, control, decision-making, budgeting, responsibility accounting and cost reduction are dealt with the Chapters 7 to 13. Financial aspects, such as working capital management, capital investment decisions, cost of capital and capital structure are explained and discussed in Chapters 14 to 16. Chapter 17 deals with effects of price level changes on financial statements and Chapter 18 discusses trends like leasing and financial reporting.

Each chapter, from its beginning to the end, has been so written that it proves extremely useful to the reader. The salient aspects of a chapter have been summed up at its end as 'Key Points to Remember' and 'Review Questions' for which a 'Key' has also been provided. Illustrations and short case studies have been incorporated, where necessary, to explain the topics discussed in the book.

We are greatly indebted to Mr. M. Wadhvani, Director, Indian Institute of Public Administration, New Delhi, and Mr. S.B. Budhiraja, Executive Director, Management Development Institute, Gurgaon, for their valuable advice and constant encouragement in writing this book.

We record our gratitude to Mr. D.N. Ghosh, Former Chairman of Larsen and Toubro, the State Bank of India and the Indian Institute of Management, Lucknow. He is currently the Chairman of Investment Information and Credit Rating Agency of India Ltd. (IICRA), Management Development Institute, Gurgaon, apart from being the Chairman of Phillips India Ltd. He not only agreed to write the Foreword to the book but also gave us an opportunity to seek his expert guidance on various topics which figure in it. We profusely thank our publishers for timely presenting the book to the readers.

NAND DHAMEJA

Professor, Indian Institute of Public Administration, New Delhi

K.S. SASTRY

Professor, University of Mauritius, Mauritius

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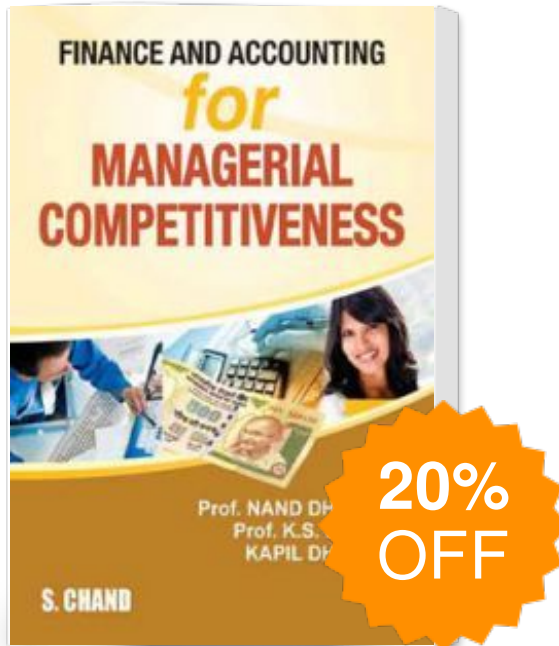
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