ABSTRACT
This paper tackles different issues related to the development of the system of the objectives of a company's financial management that also includes its sustainability. Prior to the recent financial crisis the formulation of the corporate finance management objective focused only on the company's finances that were reported and measured using the company's profit and its worth growth ratios. The financial crisis has highlighted an additional aspect in corporate management, i.e., a need for the company, as an object of the owners' investment, to generate the economic benefit for a prolonged period of time. For the purpose of formulation of the corporate finance management objective it is appropriate to refer not to a single objective or a set of same-level objectives; a much more expedient approach is a creation of the so-called objective tree integrating the requirements of the entity's going concern. The present article analyses certain factors affecting the financial performance of a company, discusses different ratios facilitating the quantitative effect of the factors upon the final results, and practically applies the management by interference model with a view to ensuring the operations of the company for a sufficiently long time.

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- G32
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- CORPORATE FINANCE
- MANAGEMENT OBJECTIVE
- GOING CONCERN

INTRODUCTION
Prior to the recent financial crisis the formulation of the corporate finance management objective both in research literature and in practice was excessively dominated by the financial aspect that was reported and measured by reference to the company's profit and its worth growth ratios. (Brigham & Ehrhardt, 2008). Some authors have been highlighting the significance (Verninmen, Quiry, Le Fur, Dallocchio, & Salvi, 2011) of the cash flow analysis arguing that for creditors the cash flow testifies a company's ability to fulfill its obligations, while the owners are able to monitor the net cash flow which the owners may dispose of at their own discretion (collect as dividends or increase the company's worth by reinvesting the funds). This treatment of the financial aspect in the corporate management was quite justifiable given the approach of the owners towards an entity as the object of their investment. Where the owners treat an entity as an investment of the cash flow they will give preference to solutions related to the payment of dividends. Where the owners treat an entity as capital investment, their decisions will be predominantly determined by reinvestment of the revenues earned and the enhancement of the company's worth (Černius, 2011).

The financial crisis, however, has revealed another very important aspect of corporate management – the need to ensure that the entity, as the object of the owners' investment, would generate economic benefit to the latter for a sufficiently long time. The observation has been well reflected in the most recent research papers of a number of authors (Conyon, Judge, & Useem, 2011). It is true that some authors consider a company's continuity, grown and profitability to be its main (Pearce & Robinson, 2009) objectives. Such authors note that the corporate growth should be the basis for profitable operations of a company. Other authors have specified a number of objectives sought by companies (Ross, Westerfield, Jaffe, & Jordan, 2009). Those include seeking profit, cost reduction, cash generation, creation of value added for shareholders, continuity, avoidance of crises or bankruptcy of the entity, advantages over its competitors, increasing of sales and the market share and a stable growth. In view of the on-going issue of the priority of objectives some authors have classified them into two major groups: profitability and risk control. In its own turn, increase of the owners' equity worth is designated as the main objective of corporate management.

Other authors have claimed that an increase of the share price should be considered the main objective of corporate management (Brooks, 2010). This approach highlights the importance of long-term projects, a well-considered choice of the funding strategy and a developed ability to manage the working capital.

In recent years researchers have also expressed a slightly different approach towards the objective of corporate management, claiming that the principal group of beneficiaries in any business is employees (De Bussy & Suprawan, 2012). These authors consider that the focus towards employees of the company effect the financial performance of an entity to a much larger extent than focusing upon other groups of stakeholders, such as customers, communities, suppliers and shareholders. Similar opinions have been expressed by other researchers claiming that most major corporations present themselves as not only money-making machines, but rather as tools for attaining social objectives (Kanter, 2011). Major corporations generate much more than a financial return; they rather bring into being long-standing and sustainable institutions and structures.

To sum up, it may be concluded that essentially all authors emphasize, in one way or another, the economic benefit that the owners or the society derive from an entity: the owners derive the economic benefit from an entity as from an object of their investment, while the society, in its own turn, benefits from the company as a socially responsible entity. Authors differ in terms of the objectives distinguished by them only in the sense that they highlight different aspects of the same process. Therefore, in our opinion, the formulation of the objective of corporate management should refer not to one single objective or a set of objectives of one level, but rather develop a system of objectives that includes a number of internally-coordinated objectives.
The system of corporate management objectives

The creation of a corporate financial management system should start with the acknowledgement that corporate objectives cannot be treated as a simple set of objectives as in certain cases the objectives might be contradictory to one another (Dutta, Lawson & Marcinko, 2012). For instance, an objective defined as "development of the company using internal resources only" may turn difficult to attain if at the same time the company seeks the objective "to pay increasingly larger dividends every year". Therefore it may be expedient to start the development of the corporate financial management system from the most generalized (global) management objective that may be formulated in terms of rather general economic categories. An overview of the current research literature and the recently offered definitions of corporate financial management objectives in view of the recent developments leads to a conclusion that, given the currently prevailing paradigm of finance management, in the most general sense the global corporate financial management objective should be formulated as the creation of a sustainable economic benefit for owners of the company. Three specifically important aspects of the corporate finance management objectives are highlighted in the current stage of its formulation. First and foremost, that the only and actual direct stakeholders of a company are its owners (shareholders), rather than its employees or customers. Both buyers and employees of entities gain some indirect economic benefit in case a company operates as a socially responsible partner of the economic system (Callan & Thomas, 2011); however, in the context of the direct management of a company's finance these beneficiaries are disregarded.

Second, the function of the company is to provide a maximum economic benefit to persons who are third parties in respect of the company. If in the formulation of the company's objectives the profit or value increase is defined as the principal objective of the company's finances without specifying the beneficiaries of such profit or value, it often remains unclear who needs this increase in the profit or the value. In certain cases making the maximization of the ratios an objective in itself is not beneficial for the owners of the company.

The third aspect increasingly prevailing in recent years is the sustainability of economic benefit. Companies must be managed in a way ensuring that the requirements of the global objective are realized for a sufficiently long time. In the ideal case the decision on the winding up of the company's operations or its transfer to other persons should be passed at the discretion of the company's owners without being affected by any negative external factors, such as the company's solvency or other problems.

Having regard to the above considerations, we think that the global corporate finance management objective (sustainable economic benefit for owners) should be further broken down into three lower level objectives such as:
1. increase of a company's value (selling price);
2. generation of a cash flow (dividends);
3. going concern.

Such a distinction of interim objectives and highlighting of the respective priorities would provide the basis for a different approach towards the decision taken by the company and would enable to avoid the situations where the future of the company as well as ecological considerations are sacrificed for the sake of a short-term benefit. These corporate management objectives taken together clearly highlight the requirement for the sustainable operation of the company that is manifested as its ability to operate as a going concern. With such a system of corporate management objectives in place and with all the objectives being organically combined, management decisions in the company should be passed considering many years, and probably decades ahead rather than a short-term period in the future.

In their own turn, lower-level interim objectives should be further broken-down to specific strategies that show how to attain the target of the owners to generate the economic benefit. Thus, for instance, the owners' target to generate economic benefit by developing the company and subsequently selling it is realized due to a consistent enhancement of the company's value. This interim objective and its realization level may be measured by assessing the company's market value (capitalization level) at a specific moment of time, or (using the internal corporate indicators) – the enhancement of the net worth of the company. The objective of the owners to obtain the economic benefit in the form of cash flow (dividends) is realized by the company yielding sufficient profit and due to the sound management of cash flows.

Ordinarily, economic benefit is considered realized when the owner of a company derives from the company more money than has been invested. The benefit can be realized through a continuous creation and generation of the cash flow for the owners (payment of dividends when it comes to internal resources of the company), and/or a one-off cash inflow by selling the company. For the economic benefit to be realized to its full extent the very formulation of the objectives of the company then involves a new aspect – the need to ensure that economic benefit is generated for as long as possible, or to ensure a guarantee (in case the company is disposed of) that the company’s value will be steadily growing, or at least will not decline to any significant extent.

An analysis of the operations sustainability issue encounters a problem of interpretation and measuring of the very concept. The basic concept of sustainability is defined as the ability of an object to persist in a constantly changing environment.

In the context of corporate finances the concept should be perceived as a company's ability to maintain its financial status in order to meet the financial expectations and goals of the company's owners.

In this case not only the retaining of the company as an object of management (going concern) should be highlighted, but also the need to maintain its financial capacity on an appropriate level to be able to regularly pay dividends to the company's owners, or generate a sufficient amount of cash in case the company is disposed of. Based on the above conclusion may be drawn that sustainability in the context of corporate finances may be measured using both time and value dimensions. In other words, in managing the company's finances under the current conditions the cash flow and company's value dimensions should be supplemented by another category – the time span during which the attainment of the objective measured in value dimensions must be ensured. This means that in the case when the owners consider the company to be a cash flow investment, from the point of view of sustainability the company must remain in operation for at least a period ensuring the pay-back of the initial investment. This statement could be formalized as follows:

\[ \text{Initial investment} \quad \text{annual dividends} \quad (1) \]

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where t – duration of the company's operations in years.

In the case where the owners consider the company as their capital investment from the point of view of sustainability the company is expected to reach its target value (and at the same time the projected sale price) at the future point in years when the owners anticipate to sell the company. This statement could be formalized as follows:

Initial investment ≤ Sale price after t years in operation, (2)

Formulas (1) and (2) may be used to summarize and measure the sustainability requirement. For a more detailed examination of the sustainability aspect in the operations of the company it is expedient to consider how external factors affect the company's performance and its condition, and in what respect the effect of the factors determine the attainment of the global objective.

Possibilities of the assessment of the effect of external factors upon the final results

Any examination of the sustainability factor in generating economic benefit needs to specifically consider that part of the market factors affect corporate finance not directly, but rather through several interim factors. Therefore, both for the purpose of formulating the objective of the company’s performance, as well as subsequently managing the company it is of utmost importance to identify the primary reasons that in fact determine the company's performance. It is also important to a most accurate extent measure or at least to estimate the scope of such influence. In the author's view the main issue encountered in the context of the corporate management is that conventionally management decisions are taken using the information generated on the basis of data of previous periods. Most often this is the data reported in the set of financial statements of the company. The data is used to compute different analytical ratios and determine the effect of the factors upon the ratio values; subsequently the ratios are used as a reference point to anticipate the prospects of the company's operations and take the respective management decisions. This approach could be referred to as "a glimpse from inside out", involving an attempt to predict the future prospects of an entity with reference to past events and using internal formalized ratios only. The most accurate illustration of the approach is the calculations of the "Z" model that are applied for the purpose of the anticipation of the future bankruptcy risk. These models are particularly suited for forecasting a probability of bankruptcy several years ahead; however they are not appropriate for projecting the prospects of a company in view of material changes of the economic situation as has happened in the case of the present financial crisis. From the point of view of the "Z" model some reliable companies went bankrupt as the situation changed although viewed from "inside" they seemed sufficiently stable and reliable.

A conclusion should be drawn in this respect that where the objectives of financial management pertain for a sustainability requirement, the approach towards factors affecting the condition of the company and the management of such factors should be modified. Since the financial sustainability of a company to a large extent depends on the influence of external factors, it is meaningful to expand the information field covered by analytical ratios referred to for the purpose of taking management decisions. This can be done by monitoring and forecasting the factors that under the current situation normally are left beyond the consideration of managers. The list of events and conditions that may cast significant doubt on the entity's ability to continue as a going concern in the short period is presented in the International Standard on Auditing 570 "Going concern". The Standard specifies financial, operational and other indicators the presence whereof create threat for the company as a going concern.

Currently more often than not part of the factors that play a determinant role in respect of the company's sustainability say are left outside the consideration of corporate management. This stems from the conventional approach towards the objectives of the financial management of a company. Therefore often a ratio that is affected by a number of factors, such as the quantity of the goods sold, in the context of a company's analysis, is considered to be the primary reason affecting changes in the sale volumes. Managers of companies, however, still fail to dedicate sufficient attention to the examination of reasons or trends affecting the changes in the sale volumes. Most often they limit themselves to expressing the percentage market share as a suitable measure to express the number of potential customers. Therefore most often companies limit the scope of their analysis to the outcomes (that in respect of companies are considered to be the primary reasons) rather than analysis the primary reasons themselves. As a result, the genuine reasons that determine the going concern of a company, remain deprived of any attention. The result of this approach is the loss of any link between the primary reason for the on-going changes and the final result.

It should be noted that some reasons in their own turn are not in all cases the primary factor affecting the value of the final result A further expansion of the spectrum of the reasons affecting the sustainability of the company would reveal the existence of global factors that in the long term play a determining role in the existence of the company.

The application of the earlier observations to the company makes it evident that the amount of the revenue earned depends on the number of buyers and the volume of the goods purchased. This link is normally expressed by a simple formula in which reasons and consequences are related by a linear link:

Sale = Total buyers x Quantity of goods x Price of goods, (3)

Usually, the management of a company and the analysis of its performance essentially use Formula 3 only. However, in the current situation it is not sufficient to record and analyze the past facts or events only; much more meaningful would be to shift to the so-called management by interferences (Kaliński & Černius, 1997). This model of management is different from the conventional management model by deviations in the sense that the monitoring object is not the outcomes (that are often identified with reasons); but rather the management decisions first and foremost respond to the primary reason with a view to minimizing the unwanted impact of the reason upon the future consequence prior to that reason even appearing. In order to shift to this management model first it is important to identify the primary factors that affect the final result.

This way it becomes clear that the number of buyers depends on the target group of buyers (children, youth, mature people) and the size of such group (population, birth rate, emigration), while the quantity and the price of the goods purchased depend on the needs of population and its purchasing power. In this case the estimation of the primary factor upon the final result might be a sufficiently complex task. Therefore the impact should be estimated approximately indicating that the final result (sales) is the function (f) of specific factors. This link, having expanded formula 3 by links as described earlier might be shows applying the formula:
Sales = Total buyers (f Size of the target buyer group, market share held by the company) x Quantity of goods (f Consumption, purchasing power) x Price of the goods (f Purchasing power),

\[ \text{(4)} \]

It should be noted that normally companies are not in a position to manage the primary reason that affects the ultimate performance of the company, i.e., companies cannot exercise any influence upon it. Also such reasons cannot be accurately measured. Their actual impact can only be estimated. However, having at its disposal the information of any forthcoming factors or their changes companies would be able to respond in advance to any future changes in the market with a view to minimizing their adverse impact, or, conversely, obtaining the maximum economic benefit.

Thus having the appropriate statistical data it is possible to assess the potential future sales of the company. The potential sales revenues could be estimated by applying formula 4 having regard to the estimated number of future buyers and the established expense structure (the latter would describe the amount of moneys potentially expensed for the purchase of the company’s supplies).

In the case of changing of the size of the buyer group the company could in advance react to future changes with a view to minimizing the unwanted influence produced by the reason for the reason.

The means used to identify the external reasons and trends may vary widely. This could include the introduction of the balanced scoreboard in the company (Chalmeta & Palomero, 2010), four corner analysis, the analysis of economic, social, legal and other factors, or other tools enabling an projection of changes of one or other factors (Capon, 2008), and their impact upon the future results of the company.

Where using the tools as earlier specified it is established that the future external conditions are favorable for the company, then it is possible to limit the management of the company to conventional corporate finance management measures. However, should the future situations relevant for the company is established to be adverse, the company should be additionally subjected to a stress test that is currently ordinarily applied to banks only. The essence of the test as tailored for a company is testing the company’s ability to function even in the case the pessimistic future prognoses prove true. In practice, such test may be performed by reducing the sales volumes to the extent they could decline in view of unfavorable demographic factors leading to smaller numbers of buyers, or in view of changes in the consumption level caused by adjustments in the consumer needs or purchasing power. Where a stress test does not show clearly manifested indications of bankruptcy, additionally the “Z” model can be applied that facilitates forecasting a short-term future prospect, and, in case the results of the model are favorable – it may reasonably concluded that the operations of the company are sufficiently sustainable, i.e., the company will remain a going concern even in view of unfavorable external conditions. And in the opposite case – should a significant possibility of the company’s bankruptcy is established – the management is obliged to notify the company’s owners thereof. Under such situation it is only the owners of the company that should be taking the decisions concerning the company’s further course ensuring that the company will not suffer significant financial damage thus eventually attaining the global financial objective.

To sum up, it could be concluded that if in the context of analyzing and managing a company the reason is identified with the consequence the objectives prescribed for the company may remain simply unrealizable. Thus, for instance, an objective to increase the sales and the number of customers without having regard to the changes in the buyer groups and their purchasing power may remain unrealistic. Therefore, with a view to ensuring the company’s sustainability for a longer period and attaining its financial objectives, it is necessary to expand the forecasting horizon of the data used for the formation of the information from several to ten or more years, and include the primary (in our case external) causes for the changes taking place inside the company. This way, the implementing of the management by interference model would practically realize the sustainability aspect of the financial management of the company.

**Conclusion**

Prior to the current financial crisis the corporate finance management was overly prevailed by the financial aspect that was formulated and measured using the company’s profit and value appreciation ratios. The financial crisis has highlighted an additional aspect in corporate management – the need for the company as an object of the owners’ investment to generate the economic benefit for a prolonged period of time. Therefore, currently the global financial objective of a company should be formulated as generation of sustainable economic benefit for the owners of the company. Therefore, for the purpose of the formulation of the objective it is necessary to design an objective tree specifying also the interim financial objectives of the company and assigning a prescribed level to each ratio.

Within the discussed system of objectives, apart from the interim objectives to increase the value of the company and generate cash flows for the owners, it is expedient to distinguish a requirement of the company's going concern as a guarantee for the sustainability of the global objective. The going concern (sustainability) requirement would ensure that the company operating as an object of investment would generate economic benefit to its owners for a sufficiently long time. In this case the company’s going concern ability should be measured in years and should be such that the generated economic benefit (amount of cash) would be larger than the amount of investment into the company.

An analysis of the effect of different factors upon the company's sustainability and its ability to attain the global objective requires a clear identification of the factors affecting the attainment of the objective. For that purpose the objective tree needs to be supplemented by lower rank ratios followed by a description of the internal links between the ratios. It should be noted that with the inclusion of the company’s going concern aspect into the objectives of the company’s management, non-financial ratios appear next to the financial ratios within the system of ratios describing the performance of the system. These are the ratios describing the company’s operating prospects in the long period and directly affecting the values of the financial ratios in the short period. These ratios that are external to the company are beyond the company’s control; however, they need to be assessed with a view to projecting the future conditions in which the company will have to operate.

The proposed set of measures that involves the assessment of any potentially adverse changes in the factors external to the company in the long-term, and the estimation of the possible impact of the changes upon the performance of the company will make it possible to project the long-term prospects of the company while implementing the global finance management objective – generation of maximum economic benefit for owners of the company.
The practical implementation of the approach will enable the companies to shift to a qualitatively different management model. Current practice is to respond to changes only when they are reflected in the internal corporate ratio system, i.e., only after the changes have taken place already. Provided the company monitors and assesses external factors that in the future will affect the internal condition of the company – it is possible to shift to the management by interference model, and thus avoid an unfavorable financial situation, or attain the maximum economic benefit at the time the external changes take place.

References


