Class 12 Business Studies Chapter 9: Financial Management - Notes, Important Questions and MCQs (2026-27)

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These Class 12 Business Studies Chapter 9 notes cover “Financial Management” from the NCERT textbook Business Finance and Marketing (2026-27): meaning, role and objectives of financial management, investment, financing and dividend decisions with factors affecting them, financial planning, capital structure and trading on equity, and fixed and working capital with their determinants – with tables, Q&A, 10 MCQs and a free PDF.

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Chapter Overview

Business finance refers to the money required for carrying out business activities. Financial management is concerned with the optimal procurement and usage of finance – raising funds at minimum cost and investing them where returns are highest.

The primary objective of financial management is wealth maximisation – maximising the market value of equity shares. Managers achieve this through three key decisions: investment, financing and dividend decisions, supported by financial planning and a sound capital structure.

Important Topics and Concepts

Role and Objectives

- Financial management affects size and composition of fixed and current assets, amount and mix of long-term finance, profit and risk.
- Primary objective: wealth maximisation – increasing market price of equity shares.
- A decision is good if it increases the value of shareholders' wealth.

Financial Decisions

- Investment decision (capital budgeting): where to invest; long-term affects growth and risk. Factors: cash flows, rate of return, investment criteria.
- Short-term investment decisions relate to working capital.
- Financing decision: how much to raise from which sources (debt or equity). Factors: cost, risk, floatation costs, cash flow position, fixed operating costs, control considerations, state of capital market.
- Dividend decision: how much profit to distribute and retain. Factors: earnings, stability of earnings and dividends, growth opportunities, cash flow, shareholder preference, taxation, stock market reaction, access to capital market, legal and contractual constraints.

Financial Planning

- Preparing a financial blueprint of future operations.
- Objectives: ensure availability of funds when needed; ensure the firm does not raise funds unnecessarily.
- Importance: anticipates future requirements, helps avoid surprises, coordinates functions, reduces waste, links present with future, eases control.

Capital Structure and Trading on Equity

- Capital structure: mix of owners' funds (equity) and borrowed funds (debt).
- Debt is cheaper (interest is tax-deductible) but riskier.
- Trading on equity: increase in profit per equity share due to use of fixed-cost debt – works when ROI > rate of interest.
- Factors: cash flow position, interest coverage ratio, debt service coverage ratio, return on investment, cost of debt and equity, tax rate, floatation cost, risk, flexibility, control, regulatory framework, stock market conditions.

Fixed and Working Capital

- Fixed capital: investment in long-term assets. Factors: nature of business, scale of operations, choice of technique, technology upgradation, growth prospects, diversification, financing alternatives, level of collaboration.
- Working capital: current assets – current liabilities. Factors: nature of business, scale, business cycle, seasonal factors, production cycle, credit allowed and availed, operating efficiency, availability of raw material, growth prospects, level of competition, inflation.

Trading on Equity – Example

Illustration.

Item	Company A (all equity)	Company B (₹20 lakh debt at 10%)
Total capital	₹30 lakh	₹30 lakh
EBIT (ROI 20%)	₹6 lakh	₹6 lakh
Interest	Nil	₹2 lakh
EBT	₹6 lakh	₹4 lakh
Tax at 30%	₹1.8 lakh	₹1.2 lakh
EAT	₹4.2 lakh	₹2.8 lakh
Equity shares (₹10)	3 lakh	1 lakh
EPS	₹1.40	₹2.80

Three Financial Decisions

Decision	Question answered	Key factors
Investment	Where to invest?	Cash flows, rate of return, investment criteria
Financing	From where to raise funds?	Cost, risk, floatation cost, control, cash flow
Dividend	How much to distribute?	Earnings, growth, cash flow, taxation, legal limits

Important Definitions and Terms

Term	Meaning
Business finance	Money required for business activities
Financial management	Optimal procurement and use of funds
Wealth maximisation	Maximising market value of equity shares
Capital budgeting	Long-term investment decisions
Floatation cost	Cost of raising funds
Capital structure	Mix of debt and equity
Trading on equity	Using debt to raise EPS
Financial leverage	Proportion of debt in total capital
Fixed capital	Investment in long-term assets
Working capital	Current assets minus current liabilities

Short Answer Questions

Q1. What is the primary objective of financial management?

Wealth maximisation – maximising the market value of equity shares.

Q2. What is an investment decision?

Deciding how the firm’s funds are invested in different assets.

Q3. Name two factors affecting financing decision.

Cost and risk of sources.

Deciding how much profit to distribute to shareholders and how much to retain.

Q5. State two objectives of financial planning.

Ensure availability of funds and avoid raising unnecessary funds.

Q6. What is capital structure?

The proportion of debt and equity in a firm’s long-term finance.

Q7. When does trading on equity work?

When the rate of return on investment is higher than the rate of interest on debt.

Q8. Define working capital.

Excess of current assets over current liabilities.

Long Answer Questions

Q1. Explain the factors affecting dividend decision.

Amount of earnings and their stability.

Growth opportunities.

Cash flow position.

Shareholder preference and taxation.

Legal and contractual constraints.

Q2. Explain factors affecting capital structure.

Cash flow position and interest coverage.

Return on investment.

Cost of debt and equity; tax rate.

Risk, flexibility and control.

Floatation cost and market conditions.

Q3. Explain the factors affecting working capital requirements.

Nature and scale of business.

Business cycle and seasonal factors.

Production cycle.

Credit allowed and availed.

Operating efficiency, raw material availability, inflation.

MCQs with Answers

1. Primary objective of financial management(a) profit maximisation (b) wealth maximisation (c) sales maximisation (d) cost minimisationAnswer: (b) wealth maximisation

2. Capital budgeting relates to(a) dividend decision (b) long-term investment decision (c) financing decision (d) working capitalAnswer: (b) long-term investment decision

4. Trading on equity works when ROI is(a) less than interest (b) more than interest (c) equal to interest (d) zeroAnswer: (b) more than interest

5. Working capital =(a) CA + CL (b) CA – CL (c) FA – CL (d) FA + CAAnswer: (b) CA – CL

6. Cheapest source of finance usually(a) equity (b) debt (c) retained earnings (d) preference sharesAnswer: (b) debt

7. Seasonal business needs more(a) fixed capital (b) working capital in season (c) no capital (d) equity onlyAnswer: (b) working capital in season

8. Financial blueprint of a firm is(a) capital structure (b) financial planning (c) dividend policy (d) budgetingAnswer: (b) financial planning

9. Floatation cost affects(a) dividend decision (b) financing decision (c) marketing (d) staffingAnswer: (b) financing decision

10. Trading business needs more(a) fixed capital (b) working capital (c) both equal (d) no capitalAnswer: (b) working capital

Quick Revision Points

- Meaning; wealth maximisation.
- Investment, financing, dividend decisions with factors.
- Financial planning objectives.
- Capital structure; trading on equity.
- Factors of capital structure.
- Fixed and working capital factors.

Chapter Summary

Financial management is concerned with optimal procurement and use of funds to maximise shareholders’ wealth. It involves investment, financing and dividend decisions, supported by financial planning that ensures funds are available when needed without excess.

Capital structure is the mix of debt and equity, where trading on equity raises EPS when ROI exceeds interest cost. Fixed capital funds long-term assets and working capital funds day-to-day operations, each shaped by several business factors.

Exam Tips and PYQ Pattern

- Practise trading on equity calculations.
- Identify the financial decision in case studies.
- Learn factors with keywords.
- Distinguish fixed and working capital factors.
- Remember wealth maximisation as objective.

Frequently Asked Questions

Is this chapter in the 2026-27 CBSE syllabus?

Yes. It is part of the NCERT Class 12 Business Studies Part II textbook “Business Finance and Marketing”, prescribed in the CBSE 2026-27 syllabus.

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What are the three financial decisions?

Investment decision, financing decision and dividend decision.

What is trading on equity?

Using fixed-cost debt to increase earnings per share when the return on investment is higher than the interest rate.

Conclusion

Financial Management is the key chapter of Part II. Learn the decision factors and trading on equity example and save the free PDF.

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Author Bio: Written and reviewed by the Nextoper Editorial Team, a group of CBSE business studies educators who build chapter notes directly from the NCERT textbook and past board paper patterns.

Freshness Note: These notes follow the NCERT Class 12 Business Studies textbook, Business Finance and Marketing (NCERT reprint 2026-27, rationalised syllabus), and the CBSE syllabus for the 2026-27 session. Last checked on 26 November 2026.