

What Finance Is For, and Where It Is Done

Before any technique is worth learning, it is worth knowing what the technique is for and who uses it. This short chapter answers both questions. It sets out the one test that every investment decision in this course is measured against, and it describes the settings in which finance work actually happens — because the same set of accounts is read very differently by a lender, an owner, and an analyst inside the business.

Nothing here requires arithmetic. Read it once before Chapter 1, and return to the table in section 0.2 when you are deciding what kind of finance work you want to do.

HOW TO USE THIS CHAPTER

This chapter gives you the purpose of the discipline and a map of the jobs within it. It is the shortest chapter in the course and the only one with no calculations in it.

The videos describe what each of those roles looks like day to day, including what a first year in each actually involves.

There is no case. The argument starts in Chapter 1, with two bakeries and a question about which one you would rather own.

0.1 What Finance Is For

A firm exists to convert money into more money. It raises funds from people who have them, buys assets, uses those assets to produce something customers will pay for, and returns cash to the people who supplied the funds. Every decision a finance function makes falls into one of three categories, and it is worth learning them as a triple, because most confusion in practice comes from mixing them up.

- **Investment decisions.** Which assets to buy. Chapters 6 through 9 are almost entirely about this question.
- **Financing decisions.** Where the money to buy them comes from — owners, lenders, or cash the business generates itself. Chapters 3, 4, and 10 deal with this.
- **Operating decisions with financial consequences.** How much credit to give customers, how much stock to hold, how quickly to pay suppliers. Chapters 2 and 4 show that these decisions consume capital just as surely as buying a building does.

The test applied to an investment decision is the same everywhere, and it is worth stating before any machinery exists to compute it. **An investment creates value when the cash it produces, valued today, exceeds what it costs today.** Every technique in Chapters 6 through 11 is a way of making the phrase "valued today" precise. Nothing else about the rule changes.

Two consequences of that rule are worth absorbing early. First, profit is not the test — cash is, because profit can be reported in a year when no money arrived. Second, the comparison is not against zero but against what the same money could have earned elsewhere at similar risk. A

project returning eight percent is a bad project if the capital could safely have earned twelve, and that remains true even though eight percent is a positive number.

0.2 Where Finance Work Happens

The word "finance" covers several distinct jobs that share a body of technique and differ in what they are trying to achieve. The distinction that matters most is between working inside a company and working on companies from outside.

WHERE FINANCE WORK HAPPENS

SETTING	WHAT THE JOB IS	WHAT IT OPTIMISES
Corporate finance	Deciding which projects a firm funds, how it is financed, how much working capital it carries	The value of one firm
Commercial and development banking	Deciding whether to lend, on what terms, against what security	Repayment, not upside
Private equity and venture capital	Buying whole businesses or stakes in them, improving them, selling	Return to the fund's investors
Investment banking and advisory	Advising on transactions and raising capital for clients	Completed transactions
Asset management and research	Deciding which securities to hold	Return against a benchmark
Financial planning and analysis	Forecasting, budgeting, explaining variance inside a firm	Decision quality, not a return

These roles read the same statements and weight them differently, and the difference is instructive. A lender reads a set of accounts looking for the ways the company might fail to pay, and is largely indifferent to how well it might do — a loan repaid in full pays the same whether the borrower doubled or merely survived. An equity investor reads the same accounts looking for the ways the company might do far better than expected, and treats survival as a precondition rather than an objective. **The same page supports both readings, and switching between them deliberately is one of the more valuable habits you can build in an internship.**

In practice, junior work in every one of these settings begins in the same place: assembling reliable numbers, checking that they tie to a source, and being able to say where each one came from. Analytical judgement is built on top of that and is never a substitute for it.

IN THE VIDEOS *Videos 0.1 and 0.2 describe what these roles look like day to day, including what a first year in each actually involves.*

0.3 Reference

CHAPTER 0 • THE THREE DECISIONS

DECISION	THE QUESTION IT ASKS	WHERE THE COURSE TREATS IT
Investment	Which assets should we buy	Chapters 6–9
Financing	Where does the money come from	Chapters 3, 4, 10
Operating	How much capital do our daily choices tie up	Chapters 2, 4

CARRY FORWARD

An investment creates value when the cash it produces, valued today, exceeds what it costs today. Everything from Chapter 6 onward is a way of making "valued today" precise. The rule itself never changes.

The comparison is never against zero. It is against what the same money could have earned elsewhere at similar risk, which is why a positive return can still be a bad decision.

A lender and an owner read the same page for different things. The lender reads for the ways it fails; the owner reads for the ways it does better than expected. Knowing which you are doing is a habit worth building early.