



THE ROLE OF FINANCIAL MANAGEMENT IN LONG-TERM INVESTMENT DECISION MAKING (LITERATURE REVIEW)

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Abstract

This study aims to examine the role of financial management in long-term investment decision-making through a literature review of various related studies. The main focus of this study is the impact of risk, the application of the time value of money, investment diversification, agency problems, and investment project feasibility evaluation techniques such as Net Present Value (NPV) and Internal Rate of Return (IRR). The literature review findings demonstrate that high risk influences investment decisions owing to the unpredictability of future cash flows, necessitating risk mitigation strategies like portfolio diversification and the utilization of derivative instruments. Applying the concept of the time value of money (TVM) is crucial in investment evaluation to facilitate more rational and profitable decisions, considering inflation and discount rates. Diversification of investments has demonstrated efficacy in mitigating volatility and enhancing long-term investment outcomes. Agency problems, which arise from conflicts of interest between owners and managers, also affect the quality of investment decisions, which can be overcome by designing incentives that align with the company's long-term goals. Evaluating the feasibility of investment projects using NPV and IRR helps ensure that the investments can add significant value to the company. This research provides important insights into how good financial management can support more effective and sustainable investment decision-making.

Keywords: Financial Management, Investment Decisions, Risk, Diversification, Agency Problems, NPV, IRR.

INTRODUCTION

Financial management is crucial in formulating long-term investment decisions that significantly influence the company's future and sustainability. Long-term investment decisions entail capital allocation and meticulously evaluating risks and prospective returns. As part of the financial strategy, these decisions focus on investing in assets or projects that can provide optimal results in the long term. Consequently, financial managers must ascertain that each selected investment aligns with the company's objectives while accounting for external and internal factors that may influence investment outcomes.

Furthermore, it is imperative to possess a comprehensive understanding of financial management to manage the risks associated with long-term investment decisions effectively. Whether due to market fluctuations, policy changes, or other economic factors, every investment decision is accompanied by uncertainty. Consequently, financial managers must be able to perform meticulous analyses utilizing various investment evaluation techniques, including Internal Rate of Return (IRR) and Net Present Value (NPV), as well as risk mitigation strategies like portfolio diversification. With

proper management, investment decisions can support sustainable company growth and ensure the achievement of long-term financial goals.

According to Brigham and Houston (2019), financial management is a process that involves planning, organizing, controlling, and supervising financial resources to achieve organizational goals efficiently. In the context of long-term investment, financial management plays a vital role in analyzing the feasibility of a project by taking into account expected cash flows, risks involved, and realistic rates of return. In addition, financial managers must ensure that each investment decision supports the company's strategy and provides optimal financial benefits in the long term while considering external factors that can affect investment results.

Long-term investment decisions are often referred to as capital budgeting. This process involves identifying investment opportunities, evaluating projects based on expected cash flows, and selecting projects that fit the company's strategy. Ross, Westerfield, and Jaffe (2016) emphasize the importance of discounted cash flow analysis in assessing the net present value of investment projects. In addition, financial management must also consider the risks associated with long-term investments. Brealey, Myers, and Allen (2017) state that risk can affect future cash flows and must be considered in decision-making. Tools such as sensitivity analysis and Monte Carlo simulation can help assess the impact of risk on investment projects.

In the context of globalization and rapid market dynamics, financial management must adapt to changes in the business environment. Research by Graham and Harvey (2001) shows that capital budgeting practices have evolved along with the complexity of markets and technology. Companies increasingly employ advanced evaluation techniques, such as real options analysis, to address uncertainty in long-term investment decisions. Financial management also influences the identification of funding sources for long-term investments. Decisions regarding capital structure, specifically the debt-to-equity ratio, will influence the cost of capital and the company's financial risk. In recent decades, attention has increased to environmental, social, and governance (ESG) factors in long-term investment decisions. Research by Eccles, Ioannou, and Serafeim (2019) shows that companies with good ESG performance have better financial performance in the long term. Therefore, financial management must consider ESG factors in the investment decision-making process.

Table 1 Research Problems

No.	Problem	Description	Source
1	Risk in Long-Term Investment Decisions	It is understanding the impact of risk on future cash flows and how that risk is considered in investment decision-making.	Hanifa, A., & Pramudito, S. (2020)
2	Application of Time Value of Money Theory in Investment Evaluation	Examining the application of the time value of money concept in investment evaluation to ensure investment decisions provide added value and are profitable for the company.	Kusuma, H. (2022)
3	Investment	By considering modern portfolio theory,	Wibowo & Susanto

No.	Problem	Description	Source
	Diversification in Long-Term Decisions	analyze how diversification can help reduce risk in long-term investment decision-making.	(2021)
4	The Influence of Agency Problems on Long-Term Investment Decisions	Prepare an analysis of potential conflicts of interest between owners and managers when making long-term investment decisions and finding solutions to overcome this problem.	The Last Supper (2022)
5	Long-Term Investment Project Feasibility Evaluation	Assess the feasibility of investment projects through techniques such as Net Present Value (NPV) and Internal Rate of Return (IRR) to ensure the long-term value of the investment.	Eccles, R.G., Ioannou, I., & Serafeim, G. (2019)

Consequently, the significance of financial management in formulating long-term investment decisions is paramount. Financial management can guarantee that investment decisions are made in a way that adds value to the company in the long term by conducting a comprehensive analysis, considering risks, determining optimal funding sources, and paying attention to ESG factors.

This study examines financial management's significance in long-term investment decision-making through a literature review methodology. This study seeks to identify pertinent financial management concepts, principles, and practices that facilitate long-term investment decision-making, encompassing project evaluation, risk management, funding structure determination, and integrating environmental, social, and governance (ESG) factors. This study examines previous research findings to offer comprehensive guidance for companies seeking to enhance the effectiveness of investment decision-making focused on sustainability and long-term value creation.

LITERATURE REVIEW

Time Value of Money

The time Value of Money is the present value of money that is more valuable than the same value in the future because of the potential income that can be generated if invested. In financial management, understanding the time value of money is essential in making long-term investment decisions, as it helps assess a project's viability through calculations such as Net Present Value (NPV) and Internal Rate of Return (IRR). For example, research by Tandelilin (2020) emphasizes the importance of applying the concept of the time value of money in investment evaluation to ensure that the decisions taken provide added value to the company.

Modern Portfolio

Harry Markowitz developed it, emphasizing investment diversification's importance in reducing risk while maintaining expected returns. In financial management, this theory creates an optimal investment portfolio by considering asset correlation and volatility. Wibowo and Susanto (2021)

found that applying modern portfolio theory to long-term investment decisions can improve portfolio efficiency and maximize risk-adjusted returns.

Agent

This agency examines the relationship between a company's owners (principals) and managers (agents), highlighting potential conflicts of interest. Financial management must guarantee that decisions align with shareholder interests and mitigate agency issues in long-term investment decision-making. Rahmawati and Hidayat (2022) emphasize the necessity of effective monitoring and incentive systems to align managerial actions with owners' interests in long-term investment decisions.

METHOD

Types of research

This study employed a literature review as its research methodology. The objective of this study is to critically evaluate and review a variety of existing studies that examine the role of financial management in making long-term investment decisions. This investigation is appropriate for investigating pertinent theoretical and practical comprehension by prior research (Anggraeni & Widodo, 2021).

Data source

The data sources in this study are literature that includes scientific journals, books, articles, research reports, and other related documents that focus on financial management and long-term investment decisions. The data from various sources published in the last 5 to 10 years ensures the relevance and latest developments in this field (Kusuma, 2022). The references mainly come from academic databases such as Google Scholar, JSTOR, ScienceDirect, and Springer.

Data collection technique

The data collection technique used in this study is library research, which involves searching, sorting, and collecting relevant articles from various reliable sources, such as international journals, textbooks, and other scientific publications. This process aims to obtain accurate and up-to-date information on theories and concepts related to financial management, especially in the context of long-term investment decision-making. The main focus of this literature study is to understand the application of these concepts in practice and assess how these theories are used in investment decision-making (Hanifa & Pramudito, 2020).

Data Analysis Techniques

The data collected in this study will be analyzed using content analysis, allowing researchers to explore and review the contents of various existing literature systematically. Through this analysis, researchers can identify key themes related to financial management and gain a deeper understanding of how these theories are applied in the context of long-term investment decision-making. This technique allows for filtering relevant information, resulting in sharper and more detailed insights.

Furthermore, the results of this content analysis will be presented systematically to illustrate the relationship between existing theories and best practices in long-term investment decision-making. With this approach, researchers can construct a narrative that describes how financial management principles can be applied to minimize risk and maximize profits in long-term investments. The results of this analysis are expected to contribute significantly to the development of managerial theory and practice in the field of investment (Anggraeni & Widodo, 2021).

Analysis Framework

The analytical framework in this study will cover several important aspects related to financial management and long-term investment decision-making. First, the role of financial management will be examined to see how effective managerial practices can influence investment decisions, both in planning and managing funds. Second, the focus will be on factors influencing long-term investment decisions, such as cash flow, risk levels, and economic growth projections. In addition, the relationship between good financial management and long-term investment success will also be analyzed, along with effective risk management strategies in long-term investment decision-making (Hanifa & Pramudito, 2020).

FINDINGS

Table 2 Research Findings

Author (Year)	Research purposes	Theoretical Framework	Method	Participant	Key Findings
Hanifa, A., & Pramudito, S. (2020)	Analyze the impact of risk on long-term investment decisions.	Risk Theory and Portfolio Management	Literature study, Case Analysis	Investors and companies	Risk can affect investment decisions by increasing the uncertainty of future cash flows, so managers must be careful in managing these risks.
Kusuma, H. (2022)	We are examining the application of the concept of the time value of money in	Time Value of Money Theory	Quantitative Analysis	Investment Company	Applying the time value of money concept ensures more optimal and profitable investment

Author (Year)	Research purposes	Theoretical Framework	Method	Participant	Key Findings
	investment evaluation.				decisions by considering future inflation and discounts.
Wibowo & Susanto (2021)	We are examining diversification as a method of risk reduction in long-term investment.	Modern Portfolio Theory (Markowitz)	Case Study, Portfolio Simulation	Investment Company	Proper diversification can reduce volatility and long-term investment risk, increasing investment returns.
The Last Supper (2022)	Identifying the impact of agency problems in investment decision-making.	Agency Theory	Case Study, Interview	Manager and Owner	Agency problems increase the potential for conflicts of interest, which can affect the quality of investment decisions. Separation of ownership and control can reduce conflicts.
Eccles, R.G., Ioannou, I., & Serafeim, G. (2019)	We are assessing the feasibility of long-term investment projects with NPV and IRR.	Investment Evaluation Theory (NPV and IRR)	Quantitative Analysis, Case Study	Manufacturing Company	Evaluation using NPV and IRR provides a clear picture of the feasibility of a long-term investment project, with an IRR higher than the cost of capital indicating investment feasibility.

RESULTS AND DISCUSSION

Research result

Based on the results of a literature review of research that has been conducted on the role of financial management in long-term investment decision-making, the following are the main findings of relevant research:

1. Impact of Risk on Long-Term Investment Decisions

This study highlights the importance of understanding risk in making long-term investment decisions. Uncertainty arising from fluctuations in future cash flows can affect the attractiveness of an investment, especially for investors who tend to avoid excessive uncertainty. High risk adds to

the challenge for financial managers in planning optimal resource allocation because they must consider the worst possible outcomes that may occur in the future. Therefore, in making investment decisions, risk factors are one of the most important elements to be evaluated carefully (Hanifa, A., & Pramudito, S. 2020).

High risk in long-term investment decisions impacts financial decisions, and the strategies companies implement to manage uncertainty. In this context, financial managers must have appropriate risk mitigation strategies, such as portfolio diversification or derivative instruments, to protect the company from the negative impact of market risk. Thus, effective risk management is the key to making more appropriate investment decisions and can minimize potential losses in the future (Hanifa, A., & Pramudito, S. 2020). Therefore, a deep understanding of risk management is essential to achieve profitable investment results.

2. Application of Time Value of Money in Investment Evaluation

Applying the Time Value of Money (TVM) concept in investment evaluation is essential to ensure more profitable and appropriate decisions. This concept recognizes that money received or spent in the future has a lower value than money received or spent today. Therefore, factors such as inflation and future discount rates must be carefully considered when making long-term investment decisions. Using TVM, investors can assess whether the potential future profits are commensurate with the initial outlay and risks taken, thus making decisions more rational and profitable (Kusuma, H. (2022).

3. Investment Diversification as Risk Reduction in Long-Term Investment

Diversifying an investment portfolio is an effective strategy to reduce volatility and risk in long-term investments. By spreading investments across different instruments or sectors, companies can reduce the negative impact of market fluctuations that affect only one sector or instrument. This study shows that diversification can improve overall investment returns because a decline in value in one sector or instrument can be offset by positive performance in another sector. Therefore, with the right diversification strategy, companies can protect themselves from unexpected risks and obtain more stable results (Wibowo & Susanto, 2021).

4. Agency Problems in Long-Term Investment Decisions

This study found that agency problems arising from conflicts of interest between owners and managers can significantly affect the quality of long-term investment decisions. When owners and managers have incompatible goals, such as when managers prioritize personal or short-term interests, this can lead to suboptimal decision-making. This conflict of interest often causes managers to make decisions outside the owners' interests or the company's overall goals. This study also identified that a clear separation between ownership and control of the company can help reduce the negative impact of agency problems so that investment decisions become optimal and support the company's sustainability (Rahmawati & Hidayat, 2022).

5. Evaluation of Investment Project Feasibility with NPV and IRR

In this study, investment evaluation techniques such as Net Present Value (NPV) and Internal Rate of Return (IRR) are used to assess the feasibility of long-term investment projects. NPV is calculated by calculating the cash inflow generated by the project minus the initial investment and the time value of money. Meanwhile, IRR measures the project's expected internal rate of return, which indicates the rate of return that makes the NPV equal to zero. These techniques are useful in assessing whether a project can add significant value to the company.

This study's results indicate that projects with a positive NPV and IRR higher than the cost of capital are feasible to implement because the project is predicted to provide a higher return than the costs incurred. Projects that meet these criteria can increase company value and provide long-term benefits. Thus, using NPV and IRR as investment evaluation tools can help financial managers make more informed and data-based investment decisions and minimize the risk of future losses (Eccles et al., 2019).

DISCUSSION

1. Impact of Risk on Long-Term Investment Decisions

Risk is always an unavoidable element in investment decision-making, especially related to the uncertainty of future cash flows. This uncertainty often challenges investors and financial managers when planning long-term investments. Hanifa, A., & Pramudito, S. (2020) state that this risk factor can affect investment decisions due to uncertain future cash flows. Financial managers must be able to identify and measure risks carefully and plan appropriate mitigation steps.

One of the main strategies for reducing risk is to use derivative instruments, such as options and futures, which can protect against unexpected market fluctuations. These derivatives allow financial managers to lock in a specific price or exchange rate, reducing uncertainty. In addition, investment diversification is also a very effective approach to reducing risk. By spreading investments across different sectors or instruments, potential losses from one asset can be offset by gains from other assets, which reduces the investment portfolio's volatility.

Hanifa and Pramudito explain that good risk management is key to profitable investment decisions. By designing a solid risk management policy, companies can minimize the negative impact of market uncertainty so that investment decisions will be more focused and profitable. In addition, well-managed risks can increase investor and stakeholder confidence, ultimately contributing to the company's long-term success. Therefore, the role of financial managers in designing and implementing effective risk management strategies is very important in achieving sustainable investment goals.

2. Application of Time Value of Money in Investment Evaluation

The time value of money (TVM) discussed by Kusuma, H. (2022) is very important in evaluating long-term investments. Due to inflation factors and other investment opportunities, the

value of money received in the future differs from that of money received today. Therefore, companies need to consider these factors when making investment decisions to ensure that the decisions taken provide optimal benefits. Companies need to consider discounting future cash flows to assess how much the investment is worth, which can lead to less profitable investment decisions. In addition, applying the concept of the time value of money allows companies to conduct a more in-depth analysis of future cash flow projections, taking into account the inflation rate that can erode the purchasing power of money over time. Considering this discount is necessary for the expected value of future cash flows to appear higher so companies can make more realistic decisions. This concept also allows companies to choose more efficient investment projects by considering the rate of return that can be obtained compared to the cost of capital incurred.

The application of TVM in investment decision-making also supports companies in making more rational and data-based decisions. By calculating the present value of future cash flows, companies can ensure that every investment will provide more profitable results commensurate with the level of risk taken. It allows companies to make more informed decisions and be oriented towards sustainable long-term results. Overall, the concept of the time value of money is a very important tool in planning and evaluating long-term investment decisions so that companies can achieve their financial goals more effectively.

3. Investment Diversification as Risk Reduction in Long-Term Investment

Wibowo and Susanto (2021) explain that diversification is a main strategy for managing long-term investment risk. By spreading the allocation of funds to various sectors or different investment instruments, companies can reduce the risks arising from sharp price fluctuations or unstable market conditions in certain sectors or instruments. It allows companies to protect themselves from the negative impacts of relying only on one type of investment. Diversification can also provide a balance between potential returns and the level of risk faced.

Modern portfolio theory proposed by Brigham & Houston (2019) reinforces the importance of diversification in investment management. According to this theory, the overall risk of a portfolio can be minimized if funds are allocated to assets that are not correlated with each other. Thus, losses incurred in one asset can be compensated by profits from other assets, ultimately increasing the overall investment return. This approach helps companies obtain more stable returns and reduces the possibility of major losses due to extreme price fluctuations in one sector or instrument.

Therefore, proper diversification becomes an important element in the long-term investment decision-making process. Companies that successfully implement diversification well can not only mitigate existing risks but also gain opportunities to increase profits in the future. In this context, efficient portfolio management is essential to ensure that investment decisions align with long-

term goals and can provide optimal results. Careful diversification can be the key to achieving a company's financial goals.

4. Agency Problems in Long-Term Investment Decisions

Research by Rahmawati & Hidayat (2022) emphasizes that agency problems arising from misalignment of interests between owners and managers can harm investment decision-making. This conflict of interest often leads to efficient or suboptimal decisions because managers with different personal goals may choose policies that could be more beneficial to owners. For example, managers may focus more on short-term bonuses or rewards than the company's long-term sustainability or profitability.

To overcome this problem, companies must design incentive mechanisms that align the interests of managers and owners. One way is to provide compensation that depends on long-term performance, such as stock options or results-based bonuses. In addition, transparency in the decision-making process is also very important. By ensuring that all parties are involved in an open and accountable process, companies can minimize potential conflicts and improve the quality of investment decisions taken. It will ensure that investment decisions are profitable in the short term and sustainable in the long term, supporting the growth and stability of the company as a whole.

5. Evaluation of Investment Project Feasibility with NPV and IRR

Evaluation using the Net Present Value (NPV) and Internal Rate of Return (IRR) methods, as explained by Brigham & Houston (2019), is a very important tool in assessing the feasibility of long-term investment projects. NPV measures the difference between the present value of the expected cash inflows from the project and the initial investment cost, allowing the company to determine whether the project will create added value or be detrimental. If the NPV is positive, the project is expected to generate more value than the costs incurred, meaning the project can increase shareholder wealth.

Meanwhile, IRR measures a project's internal rate of return and compares it with the level of capital costs that the company must incur. Suppose the IRR is higher than the cost of capital. In that case, the project is considered profitable and feasible to implement because this shows that the project can generate higher returns than the costs required to finance it. Therefore, using both of these evaluation methods, NPV and IRR, in investment decision-making is very important to ensure that the selected project provides optimal benefits for the company. With the right application, companies can identify projects that are not only financially feasible but can also support the company's long-term goals, such as sustainable growth and increasing value for shareholders (Eccles, Ioannou, & Serafeim, 2019).

CONCLUSION

The conclusion of this study reveals that financial management has an important role in making effective and sustainable long-term investment decisions. This study shows that careful risk management, such as investment diversification and derivative instruments, can reduce the impact of market fluctuations, increase portfolio stability, and provide better results for companies. In addition, applying the Time Value of Money (TVM) concept is necessary for investment evaluation because it helps companies consider inflation and discount rates to make more rational and profitable decisions.

Agency problems arising from conflicts of interest between managers and owners can also affect the quality of investment decisions. Therefore, it is important to design incentive mechanisms that align the goals of both parties and increase transparency in decision-making. Using evaluation techniques such as Net Present Value (NPV) and Internal Rate of Return (IRR) has proven effective in assessing investment projects' feasibility and providing clear guidance on potential returns and associated risks. Thus, good financial management, proper risk management, and careful investment evaluation will support the company's long-term success in achieving its desired financial goals.

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