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Short note on financial statement analysis

Deepak Tandon*

Department of Economics, Jagan Institute of Management Studies, Delhi, India .

DESCRIPTION

Financial Statement Analysis (FSA) is a diagnostic and research study of financial statements for making logical business decisions. Financial reporting analysis takes raw financial information from financial statements and transforms it into actionable information that can be used for decision making. There are three types of analysis horizontal analysis, vertical analysis, and ratio analysis. Each of these tools gives decision makers a little more insight into the performance of their organization. It is important for companies to compare the generated data with other data in the industry and understand that their competitors need to be closed. Companies also need to consider comparing past experience with current and future performance expectations. Three common analytical tools are used to make decisions.

Horizontal analysis (also known as trend analysis) examines trends over time in various balance sheet items. The company looks at one period (usually one year) and compares it to another. For example, a company can compare this year's sales to last year's sales. Trend items in these financial statements can provide a company with valuable information about overall performance and specific areas to be improved. It is most valuable to perform a horizontal analysis of the information over multiple time periods to see how each line item is changing. Without using multiple time periods, it can be difficult to see trends. The year used for comparison is called the base year (usually the previous period).

The base year for horizontal analysis is analyzed for changes in dollars and percentages from the base year. Vertical analysis shows the comparison of one line item in a statement with another line item in the same statement. For example, a company can compare cash to total assets for the current year. In this way, the entity can see the percentage of cash (comparison items) in total assets (other items) during the period. This is different from horizontal analysis, which compares over the years. Vertical analysis compares the items in the statement for the current year. This helps companies know how much an item contributes to overall operation. For example, a company may want to know how much inventory contributes to its total assets. You can use this information to make budget preparation, cost reduction, increased sales or capital investment. Financial metrics help both internal and external users of information make informed decisions about a company. Based on the results of the relationship analysis, stakeholders can, among other things, invest, become suppliers, take out loans, or modify internal processes.

The income statement provides revenue by comparing the company's revenue to the costs associated with its business. H. Net profit or net loss. The income statement is divided into three parts that help you analyses the efficiency of your company in three different locations. To determine your gross profit, start with revenue and the direct costs associated with revenue. After that, it shifts to operating profit and deducts indirect costs such as marketing costs, general costs, and depreciation costs. The end result after deducting interest and taxes is net income. A basic income statement analysis usually calculates gross margin, operating margin, and net margin. Each of these is profit divided by sales.

The rate of return helps indicate whether business costs are low or high at various points in operation. Reported financial statement revisions and restatements are financial statement revisions and restatements in such a way that the financial statements serve better for analytical purposes and allow the company's performance to be interpreted more efficiently and accurately. In the case of a restatement of the income statement, the restatement takes the form of splitting the reported items into recurring and non-recurring items and splitting revenue into core revenue and provisional revenue. In the restatement of the balance sheet, the balance sheet items are divided into operating assets / liabilities and financial assets / liabilities.

To improve the quality of the reported accounting numbers, measurement error adjustments are made to remove noise present in the input data. For example, remove R & D expenses from your income statement and report them to your balance sheet.

Financial analysis determines the health and stability of a company and provides insights into how a company is doing business. However, it is important to understand that balance sheet analysis has its limitations. The different accounting methods used by different companies change the level of apparent health and profits, for better or for worse. Different analysts can get different results from the same information. Therefore, we must conclude that financial statement analysis is only one tool in the decision-making process (although it is an important tool).