CMF MSU

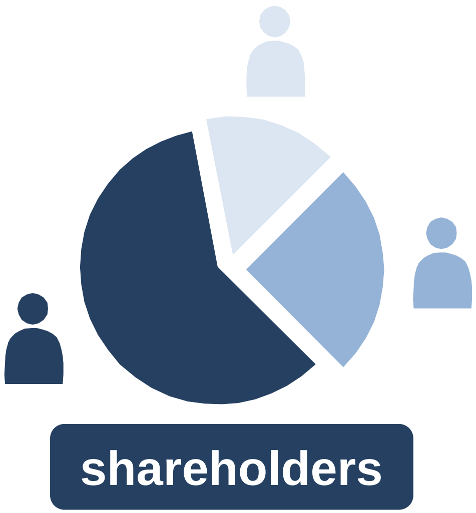
Financial Analysis: Intro

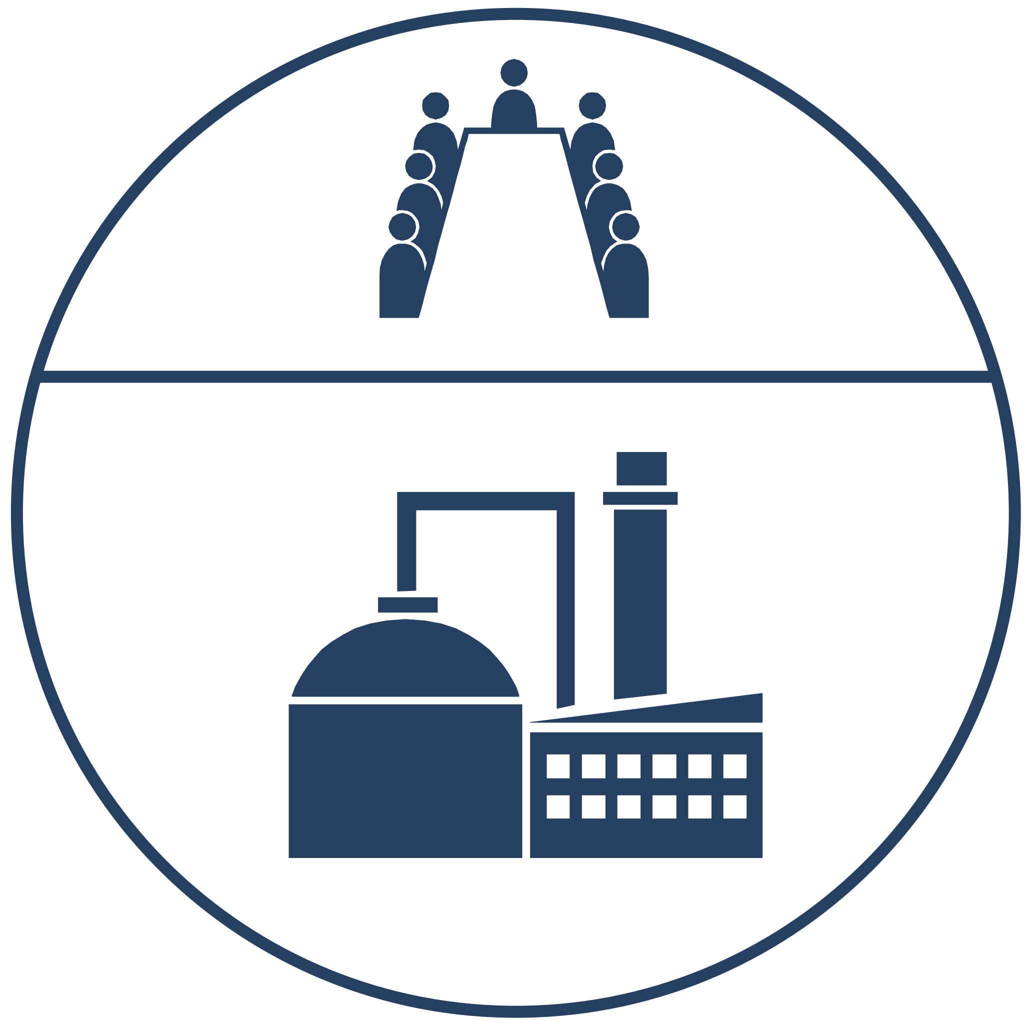
Financial statement & Accounting

17 October 2015

Corporate government

Division of company ownership and governance





Financial statement

Definition

Financial statement (financial report) is a *formal record* of financial activities and position of a business.

Object:

Provide information about the financial position, performance and changes of an enterprise that is useful in making economic decisions.

Should be

- understandable
- relevant
- reliable
- comparable

Users:

- owners and management
- prospective investors
- financial institution

Financial statement

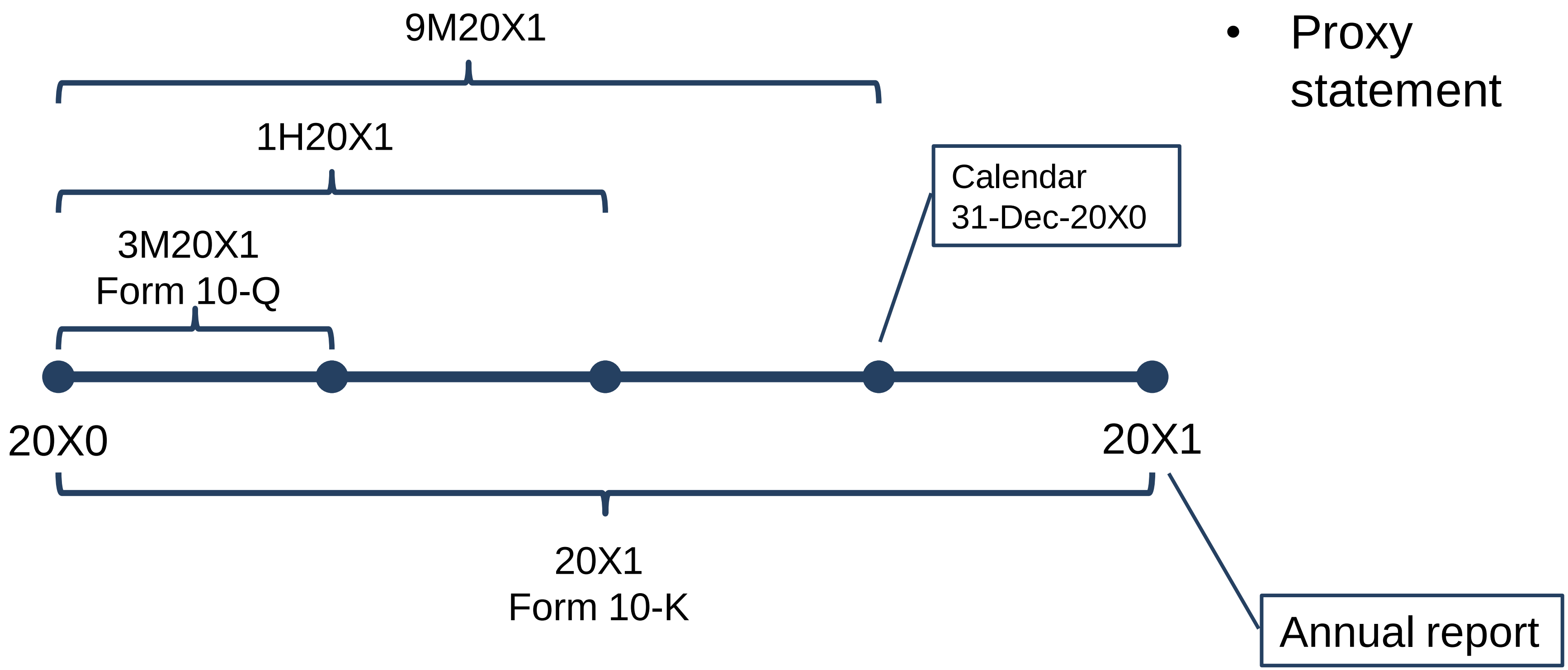
Financial statement content

- Financial statement
  - balance sheet
  - income statement
  - statement in changes in equity
  - statement of cash flow
- Footnotes to financial statement
- Management discussion and analysis (MD&A)
- Audit report

Financial statement

Update frequency

Periodical:



Non-Periodical:

- Form-8K
- Proxy statement

Financial statement

Footnotes and MD&A

Footnotes provide further *details* about information summarized in the financial statement.

- The basis of presentation and the list of consolidated subsidiaries
- Accounting methods, assumption and estimates
- Information about business acquisition and disposal, pension plans, legal actions, segments of the firm and ect.

Management discussion and analysis discuss trends and indentify significant event and uncertainness affecting the firm.

- Only included in annual report
- Impact of off-balance-sheet obligation
- Forward-looking expenditures and divestures

Financial statement

Audit report

The auditor's report is only an *opinion* on whether the information presented is correct and free from material misstatements.

The auditor's opinion

- **Unqualified opinion**

  "Everything is OK"

- **Qualified opinion**

  "There are some mistakes but financial statement is correct"

- **Adverse opinion**

  "Financial statement is wrong"

- **Disclaimer of opinion**

  "The auditor refuse to give any opinion"

Accounting

Principle

- Fair presentation
- Going concern basis
- Accrual basis
- Consistency
- Materiality
- Aggregation
- No offsetting

Accounting

Types of accounts

Asset account is economic resources owned or controlled by an entity.

Example:

- Cash on hand
- Cash in bank
- Land
- Equipment
- *Account receivables*
- *Inventory*
- Buildings
- Trademarks and patents
- etc.

Accounting

Types of accounts

Liability account is different types of economic obligation of an entity.

Example:

- Bank loan
- *Account payable*
- Bonds payable
- Note payable
- etc.

Equity account is the value of assets after deducting the value of liabilities.

Example:

- Common stock
- Paid-In capital
- Retained earning

Income and expense account is financial result of an entity.

Accounting

Double entry bookkeeping

The **debit and credit** system is used for recording changes in value resulting from business transaction.

Dr (debit) → **Cr (credit)**

Depending on types, *every* account could be **debited** or **credited**.

But!

- **Asset** and **expense account** could have only debit balance
- **Liability**, **equity** and **income account** could have only credit balance

Accounting

Double entry bookkeeping

Asset account

Dr	Cr
\$100	
\$400	
	\$300
\$200	

Debit balance

Liability account

Dr	Cr
\$100	
\$400	
	\$900
	\$400

Credit balance

The diagram shows how the value of different types of accounts change if it is debited or credited.

	Dr	Cr
Asset account	↑	↓
Liability account	↓	↑
Equity account	↓	↑
Income account	↓	↑
Expense account	↑	↓

Accounting

Bookkeeping examples – 1

Company X bought a computer for $500 from company Y and asked for payment delay for 10 days.

Dr Equipment **Cr** Account payable **=** $500

Dr Account payable **Cr** Cash in banks **=** $500

Equipment

Dr	**Cr**
$500	
$500	

A/P

Dr	**Cr**
$500	$500
	$0

Cash in bank
$650 – beginning

Dr	**Cr**
	$500
$150	

Accounting

Bookkeeping examples – 2

Company X bought a computer for $500 from company Y and asked for payment delay for 10 days and promised to pay for it $10 per day.

Dr Equipment	**Cr** Account payable	**=**	$500
Dr Account payable	**Cr** Cash in banks	**=**	$500
Dr Expenses	**Cr** Cash in banks	**=**	$100

Equipment

Dr	**Cr**
$500	
$500	

A/P

Dr	**Cr**
	$500
$500	
	$0

Expenses

Dr	**Cr**
$100	
$100	

Cash in bank $650

Dr	**Cr**
	$500
	$100
$50	

Accounting

Bookkeeping examples – 3

Company X, which produced cars, sold 100 new J-model for $1,000/car. The buyer paid after 5 days

Dr A/R	**Cr** Revenue	**=**	$100,000
Dr Cash in bank	**Cr** A/R	**=**	$100,000

Revenue

Dr	Cr
	$100,000
	$100,000

Account Receivables

Dr	Cr
$100,000	
	$100,000
$0	

Cash in bank
$0

Dr	Cr
$100,000	
$100,000	

Accounting

Bookkeeping examples – 4

Company X issued 100 shares with $100 face value and raised for it $120 per share.

Dr	Unpaid capital	**Cr**	Common shares	**=**	$10,000
Dr	Unpaid capital	**Cr**	Paid-In capital	**=**	$2,000
Dr	Cash in bank	**Cr**	Unpaid capital	**=**	$12,000

Unpaid capital

Dr	**Cr**
$10,000	
$2,000	
	$12,000
$0	

Common shares

Dr	**Cr**
	$10,000
	$10,000

Paid-In capital

Dr	**Cr**
	$2,000
	$2,000

Cash in bank $0

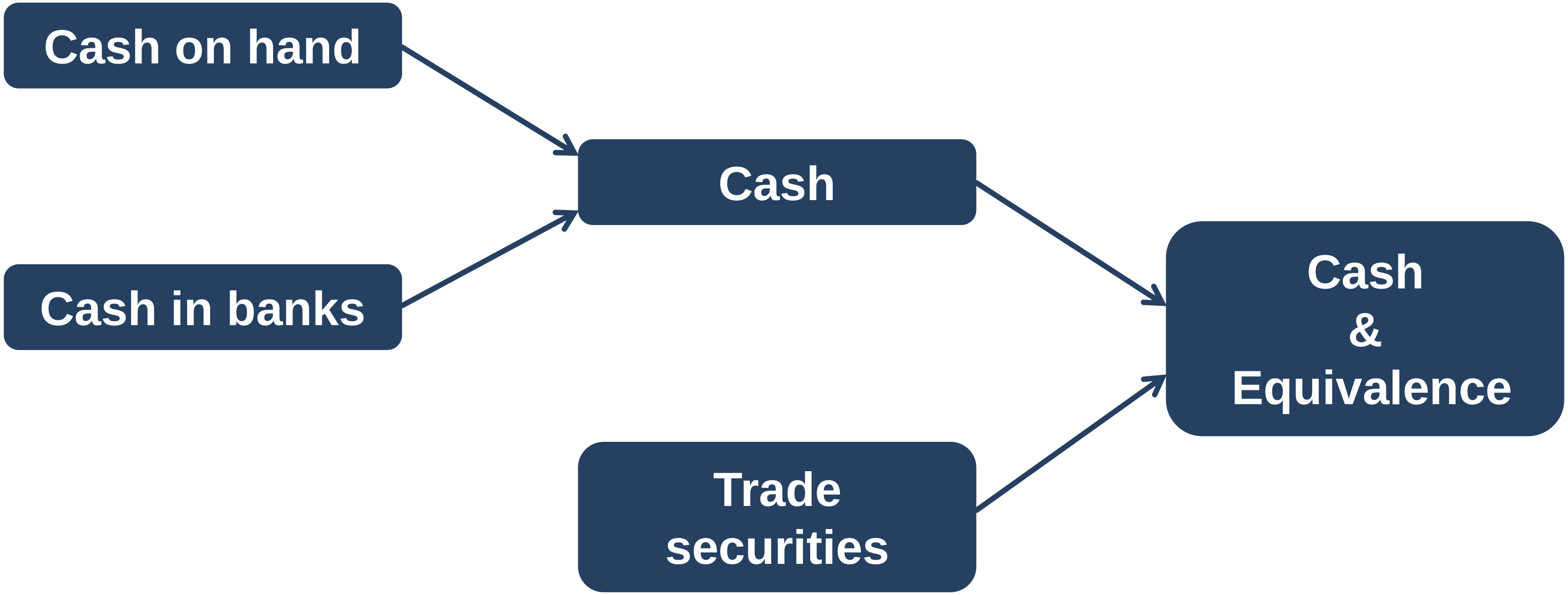
Dr	**Cr**
$12,000	
$12,000	

Balance sheet aggregation

Principle

A company could have enormous amount of accounts.

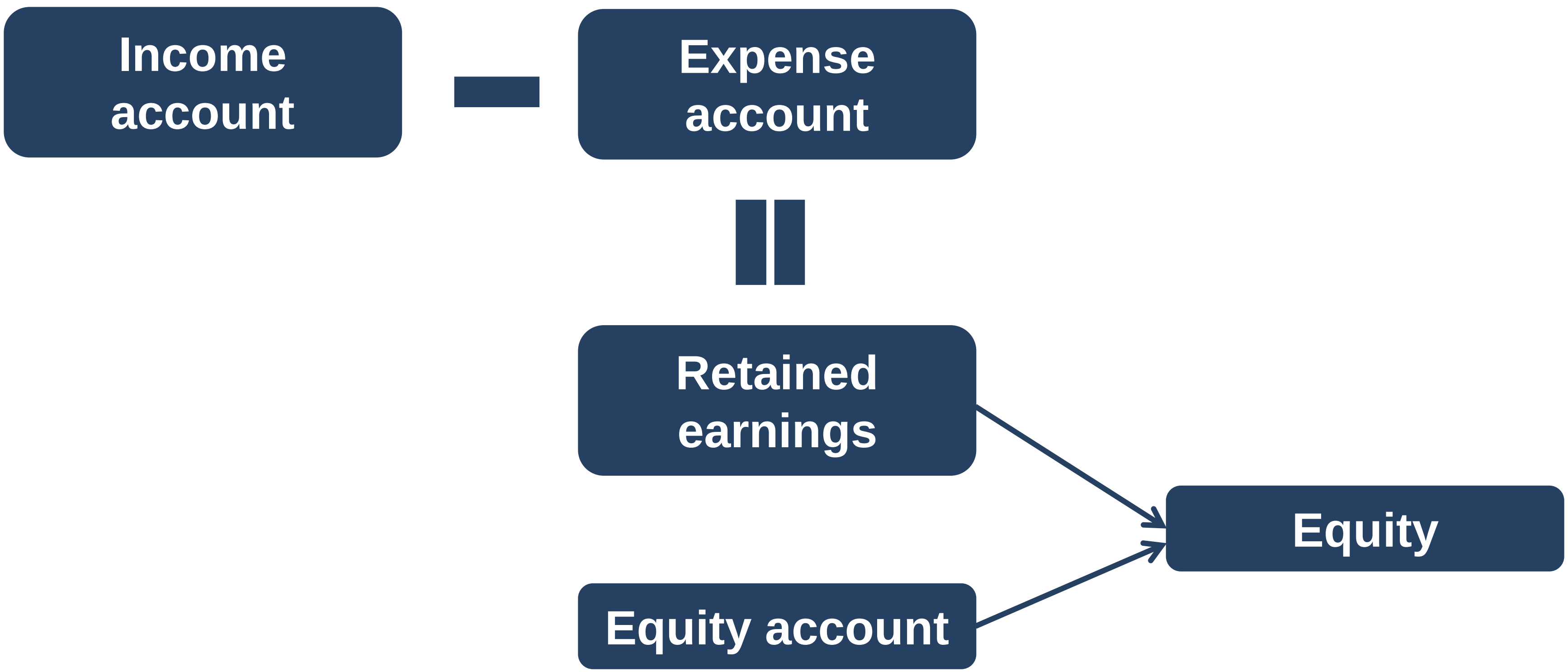
Producing a financial statement, accountants are grouping the similar accounts.



Balance sheet aggregation

Retained earnings

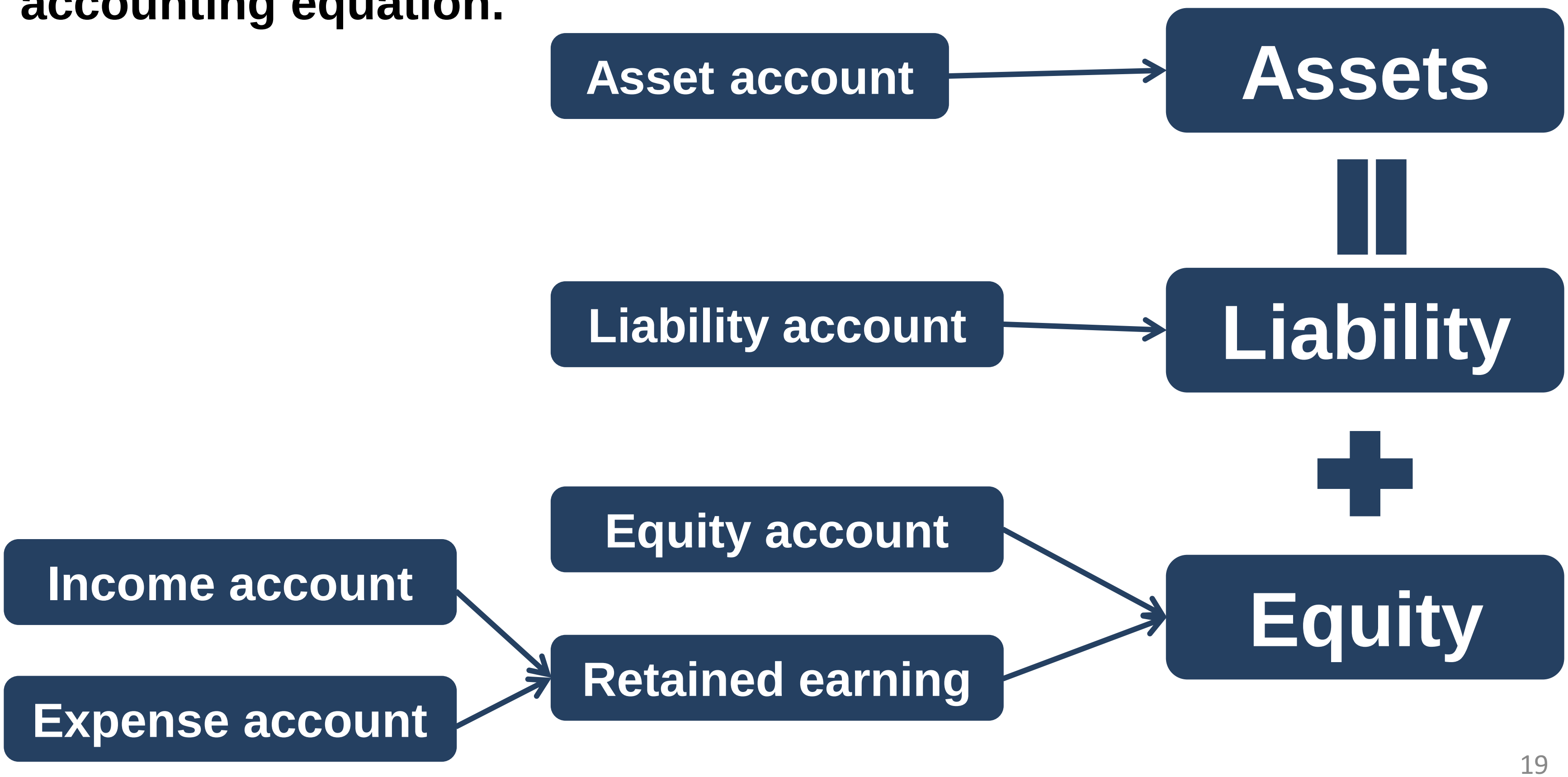
Preparing a financial statement, an accountants create special account **“Retained earnings”** which offsets all income and expense accounts.



Balance sheet aggregation

Fundamental accounting equitation

Assets accounts have only debit balance and others have only credit ones. Double bookkeeping rule ensures that business transaction is debited and credited at the same time. It give the **fundamental accounting equation.**



Q&A