

# Unit 9: Financials

THE BIGGEST RISK OF ALL IS NOT TAKING ONE





This unit is not to make you an accountant,  
but to help you understand the  
consequences of your financial decisions

# Importance of financial knowledge

- ▶ A good investment opportunity requires a product or service that meets a definite customer need and creates a sustainable competitive advantage.
- ▶ To be attractive, an opportunity must generate significant profits relative to the required amount of investment.
- ▶ Therefore, projections of a venture's profits, its asset and financing requirements, and its cash flows are essential in determining whether a venture is economically feasible.
- ▶ In order to make such financial projections, an entrepreneur must have a good understanding of financial statements.

# Three main financial statements

Balance sheet



Income statement



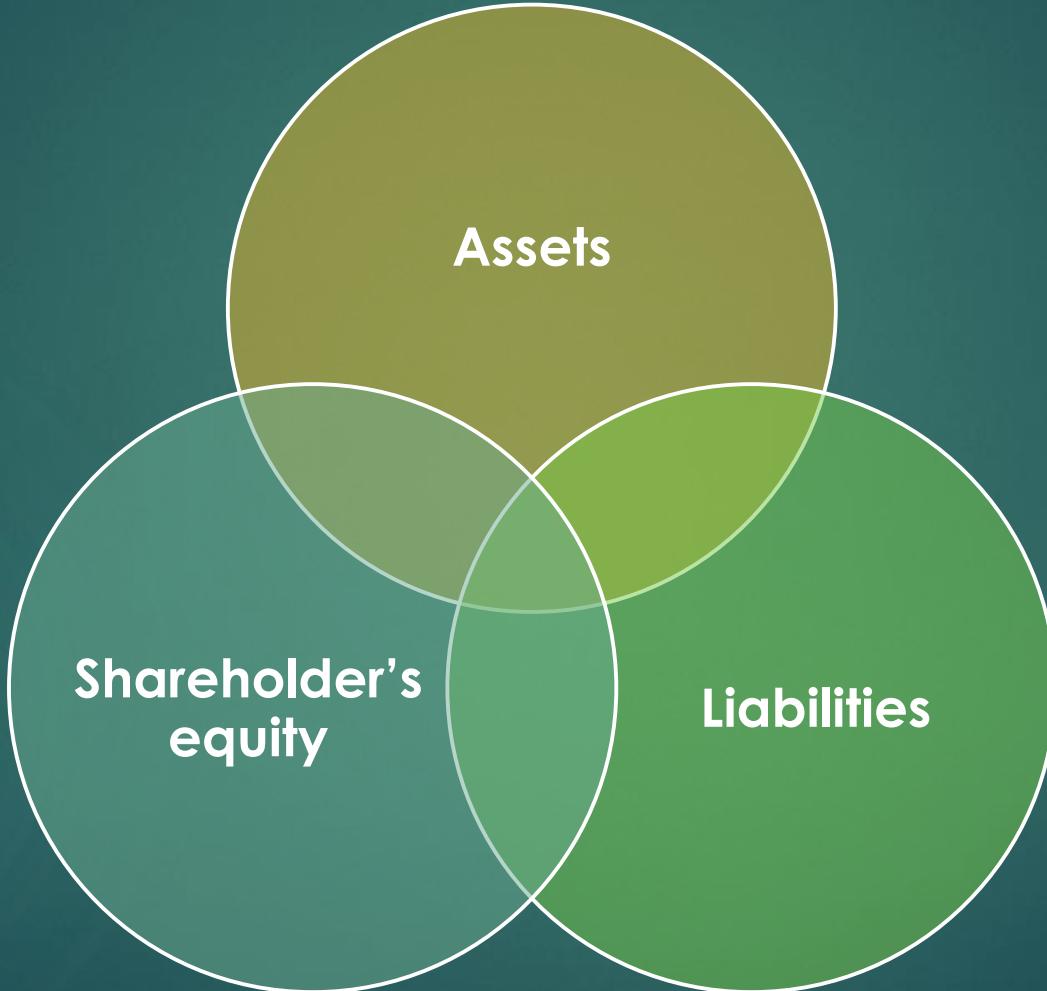
Cash flow statement



# Todays focus

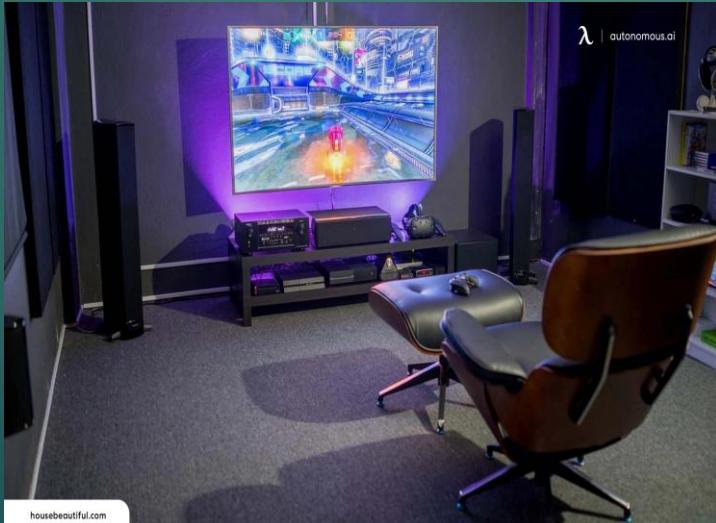


# Key terms used in balance sheet



# Assets

- ▶ Assets are things that a company owns that have value.
- ▶ They can be either be sold or used by the company to make products or provide services that can be sold.





# Classification of assets

## a. Based on convertibility



**Current assets**

**Non-current assets**

# Current assets

► Are things a company expects to convert to cash within a year.

E.g. Inventory, short term deposits and marketable securities, Account receivables

Marketable securities are financial instruments that can be easily converted into cash. Examples (stocks/shares)

# Non-current assets/Fixed assets

- ▶ Are things a company does not expect to convert to cash within one year or that would take longer than one year to sell.
- ▶ Fixed assets are those assets used to operate the business but that are not available for sale, such as trucks, office furniture, land, house etc.

# Classification of assets

b. Based on physical existence



**Tangible assets**

**Intangible assets**

# Tangible assets

- ▶ Assets that you can see and feel (physical presence)

Example: Machine, Equipment, Buildings.



# Intangible assets

- ▶ Assets that do not have physical existence
- Example: Patents, Brands, Copyrights



# Classification of assets

b. Based on Usage



Operating assets

Non-Operating assets

# operating assets

- ▶ Assets which are necessary to conduct business operations.

Examples: Machines, buildings and equipment



# Non-operating assets

- ▶ Short term investment or marketable securities that are not necessary for daily operations



# What are Assets?



Resources



Company/Individual

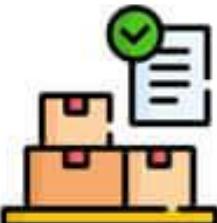


Money/Income

## Examples



Cash



Inventory



Machine



Building



Copyright



EDUCBA

# Liabilities

- ▶ Liabilities are the amounts of money that a company owes to others.
- ▶ E.g obligations; Money borrowed from the bank to launch a new product ,Rent for use of a building, money owed to suppliers for materials, payroll a company owes to the employees, environmental clean up costs, or taxes owed to government.
- ▶ Liabilities also include obligations to provide goods or services to customers in the future.

# Current and long term liabilities

- ▶ Liabilities are generally listed on their due dates.
- ▶ Liabilities are said to be either current or long-term.
- ▶ Current liabilities are obligations a company expects to pay off within a year. Examples: Accounts payable, interest payable, short term loans
- ▶ Long term liabilities are obligations due more than one year. Bonds payable, long term notes payable, deferred tax

- ▶ Accounts payable: Represents company's obligations to pay off a short term debt to its creditors or suppliers.
- ▶ Interest payable: Amount of interest currently owed to lenders that can be paid within one year.
- ▶ Bonds payable: It is a form of debt financing issued by corporations/governments to raise capital. The issuer of bonds is obligated to pay interest expenses periodically over the borrowing term and repay the principal at maturity.
- ▶ Long term notes payable: A loan that is expected to be paid in more than one year.
- ▶ Deferred tax: The amount of income tax payable in the future.

# Shareholders equity

- ▶ Shareholders' equity is sometimes called capital or net worth.
- ▶ It's the money that would be left if a company sold all of its assets and paid off all of its liabilities.
- ▶ This left over belongs to the shareholders, or the owners of the company.

They are outstanding shares, additional paid in capital, retained earnings and treasury stock.

Outstanding shares: The portion of a company's stock currently held by all its shareholders.

Additional paid in capital: Represents the excess amount paid in total by investors above the par value of a company's shares.

Retained earnings: The sum of company's earnings from prior period after deducting any dividends paid to the company's shareholders.

Dividend: distribution of profits by a corporation to its shareholders

Treasury stock: Formerly outstanding stock that has been repurchased and is being held by the company.

# Balance sheet

- ▶ Show what a company owns and what it owes at a fixed point of time.
- ▶ Provides detailed information about a company's **assets**, **liabilities** and **shareholders' equity**.
- ▶  $\text{ASSETS} = \text{LIABILITIES} + \text{SHAREHOLDERS' EQUITY}$
- ▶ A company's assets have to be equal to the sum of its liabilities and shareholders' equity.

**TEDDY FAB INC.**  
**BALANCE SHEET**  
**December 31, 2100**

**ASSETS**

**Current assets**

Cash and cash equivalents	\$ 100,000
Accounts receivable	20,000
Inventory	15,000
Prepaid expense	4,000
Investments	10,000
<b>Total current assets</b>	<b>149,000</b>

**Property and equipment**

Land	24,300
Buildings and improvements	250,000
Equipment	50,000
Less accumulated depreciation	(5,000)

**Other assets**

Intangible assets	4,000
Less accumulated amortization	(200)

**Total assets**

\$ **472,100**

**LIABILITIES AND SHAREHOLDERS' EQUITY**

**Current liabilities**

Accounts payable	\$ 30,000
Notes payable	10,000
Accrued expenses	5,000
Deferred revenue	2,000
<b>Total current liabilities</b>	<b>47,000</b>

Long-term debt 200,000

**Total liabilities** **247,000**

**Shareholders' Equity**

Common stock	10,000
Additional paid-in capital	20,000
Retained earnings	197,100
Treasury stock	(2,000)

**Total liabilities and shareholders' equity** \$ **472,100**