



## The five-minute read # 7: Introduction to Financial Statement-1



The saying goes, "If one can't manage finances, they can't manage a business." Grasping financial concepts is pivotal for the successful operation of a business. Numerous startups falter due to depleted cash reserves, a result of founders failing to anticipate the situation. Anticipation is only feasible with a solid understanding of financial statements and a keen eye on future cash flow. Should the cash flow appear negative on the near-term horizon, founders must proactively secure funds to avert such a crisis. The moment cash flow turns negative, it marks a critical juncture in the business's trajectory.

### UNDERSTANDING CASH FLOW IS KEY TO BUSINESS SUCCESS

Data compiled by cbinsights.com reveals that a notable proportion of company failures stem from cash depletion. This data underscores the aforementioned logic. All individuals, whether entrepreneurs or not, who bear any connection to a company's historical, current, or future financials, should possess a firm understanding of financial

statements. Running out of cash was behind 44% of startups failures in 2023. Many of these failures could have been averted by preparing projected cash flow statements and engaging in pre-emptive fund raising.

### ACCESS TO FINANCIAL INFORMATION

The fundamental objective of financial statements is to communicate the precise financial condition of a company to all stakeholders. Since the majority of stakeholders lack insight into the company's daily operations, they rely on the released financial statements (alongside occasional statutory disclosures) to evaluate the company's financial well-being. These stakeholders encompass:

- \* Founders/ Promoters / Owners
- \* Shareholders
- \* Lenders (bankers)
- \* Government (Income tax and GST department)
- \* Economists
- \* Analysts
- \* Investors



Employees

Policymakers or Statisticians

## SIGNIFICANCE OF FINANCIAL STATEMENTS

A single data point underscores the importance of financial statements: the combined transaction value of all shares traded in global stock markets surpasses the total aggregate GDP of all nations worldwide. Investment choices within these stock markets hinge on the financial standing disclosed in the statements of the represented companies. Irregularities within financial statements could distort assessments and misguide investment decisions. This underscores the necessity for a robust system to ensure the dissemination of high-quality information in the form of precise financial statements.

*Financial statements warrant examination from two distinct viewpoints:* that of entrepreneurs or promoters, and that of other stakeholders. Depending on one's position, the assessment can differ significantly.

Owners of a company often manipulate the data within financial statements for varying motives. Notably, over-reporting may occur to present a rosier performance to stakeholders, with the ultimate aims of either providing false reassurance or artificially boosting share prices. Conversely, under-reporting might be employed to depress share prices, enabling discreet purchase at a low cost, followed by selling at a higher price after inflating the reported results. Regrettably, there is no shortage of individuals with fraudulent intentions engaging in such practices.

Accounting regulators globally have grappled for centuries to devise new methodologies or regulations to thwart the manipulation of financial statements. Yet, the prevalence of such manipulation persists to this day. However, an in-depth understanding of financial statements coupled with thorough analysis can aid in detecting inaccuracies or falsifications. This can lead to a genuine portrayal of the situation through a comprehensive reevaluation of the statements.

### Major Disaster for Accounting Frauds

#### Accounting Fraud: Enron

At its peak, Enron was one of America's largest corporations with 22,000 employees. Enron reported \$111 billion in revenues in 2000, overstated profit, and hid the size of the debt. Investors were gung-ho about the shares and the share price went up to \$90 plus. The size of the manipulation became so large that it was no longer sustainable. It came to light due to some inspection. The share price went down from \$90.75 in August 2000 to just \$0.67 in 2002 to 0.0 soon after that.

#### Accounting Frauds: WorldCom

Three key financial statements are prepared by most enterprises:

1. **Balance Sheet**
2. **Profit & Loss or Income statement**
3. **Cash Flow statement**

Balance sheet shows the financial position, i.e., the comprehensive list of assets and liabilities of an enterprise as on a particular day.

The Profit & Loss account/statement shows all the earnings and expenses of an enterprise during a certain period, such as year, half year, or quarter and the surplus left after meeting all the expenses.

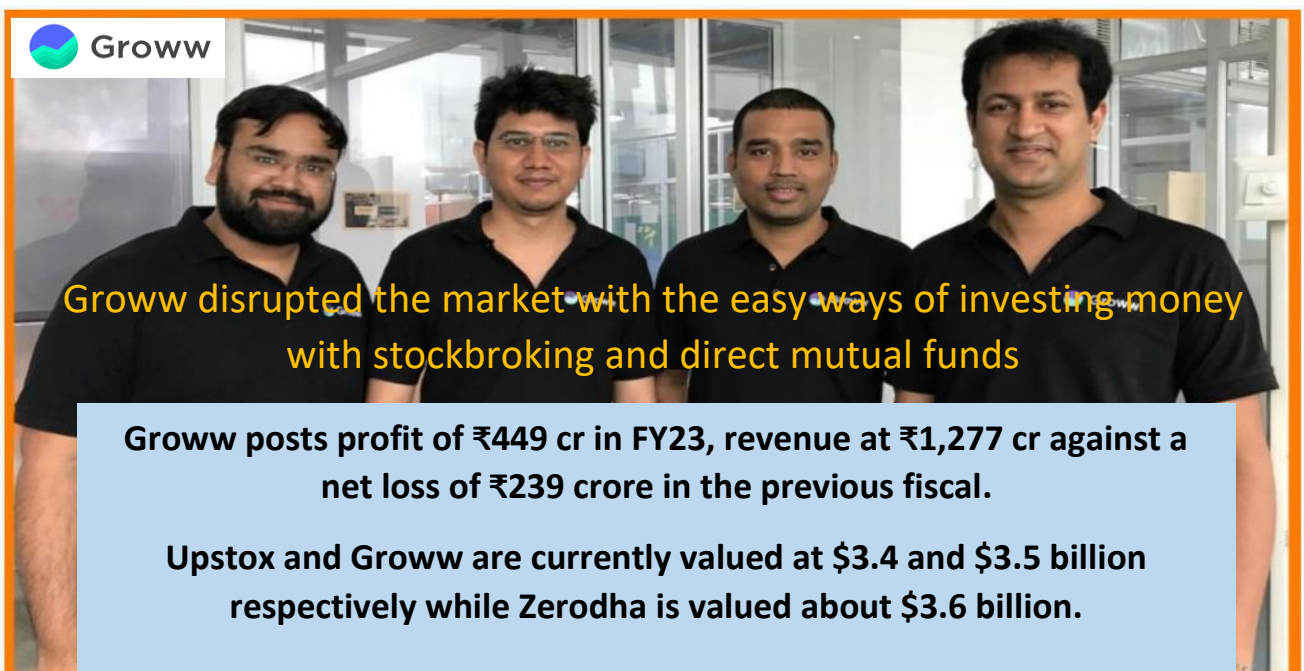
The Cash Flow statement exhibits the inflow of cash and outflow of cash. It ends with the final cash balance as on the last day of a particular period for any business.

WorldCom, USA, was the second-biggest phone company. The company was going through tough times and were incurring huge losses consecutively for years. But they fraudulently underreported the cost of a staggering \$3.8 billion. As it happens in all fraudulent acts, they could not sustain the over-reporting and, in 2002, filed for bankruptcy.

### Accounting Frauds: Satyam Computers of Hyderabad

The chairman of Satyam Computers, Ramalinga Raju, confessed that the company's accounts had been falsified to the extent of Rs 12,318 crore. The company went through indescribable turmoil rendering thousands of employees jobless and millions of investors poorer. Imagine that you bought 1000 shares of Satyam Computers @₹1000 each for ₹10,00,000. Your value went down to ₹10,000 after the scam was busted.

You can now appreciate the importance of having a clear understanding of financial statements for a meaningful assessment of company performance.



**Groww**

**Groww disrupted the market with the easy ways of investing money with stockbroking and direct mutual funds**

**Groww posts profit of ₹449 cr in FY23, revenue at ₹1,277 cr against a net loss of ₹239 crore in the previous fiscal.**

**Upstox and Groww are currently valued at \$3.4 and \$3.5 billion respectively while Zerodha is valued about \$3.6 billion.**

### MEET MAN WHO FAILED TO CRACK IIT, CO-FOUNDED ₹25,000 CRORE COMPANY

Ishan Bansal (BITS Pilani and XLRI Jamshedpur), Lalit Keshre (IIT Bombay), Neeraj Singh (ITM, Gwalior and CDAC) and Harsh Jain (IIT Delhi and UCLA School of Management),

*Lalit is the CEO of Groww. Lalit looks after all the aspects of the business, predominantly the product and customer experience at Groww. Before starting Groww, Lalit was in a senior product management role at Flipkart, where he launched and led Flipkart Quick and helped launch Flipkart Marketplace. Earlier, Lalit founded*



*an online learning company called Eduflix, and he has also been an early team member at Ittiam Systems.*



*Harsh Jain heads Growth and Business at Groww. Before Groww, Harsh was part of the product management team at Flipkart. Previously, Harsh had co-founded a story-telling start-up. Harsh holds a B-Tech in Electrical Engineering and a Masters in Information and Communication Engineering from IIT Delhi. He studied for his MBA in product management and marketing from UCLA School of Management.*

*Groww is looking to launch its neo-banking platform. It is planning to emerge as a one-stop solution for the users to help with their banking and investments and thus, be more holistic for the users.*

*They are alumnae of e-commerce companies. They could rightly predict that the disposable incomes of Indians are on the rise and people would explore ease of investment. They made extensive studies of customers' pain and did numerous experiments to identify the best way to provide the best possible customer experience. They observed that the existing process of opening various accounts for investment was inefficient, cumbersome, and discouraging.*

*Initially, the founding team took a lot of time to understand the market and identify the users' fundamental pain points. They also had to do a lot of experiments to figure out the right user experience. Also, because the user's hard-earned money was at stake, they had to ship a safe and secure product, and that took them some time to build.*

*In 2017, Groww started as a direct mutual fund distribution platform and within a year became one of the most popular mutual fund investment platforms in the country. Following user demand, Groww added stocks in the early half of 2020 and the same year launched digital gold, ETFs, Intraday trading, IPOs in quick succession.*



## **MICROSOFT CEO SATYA NADELLA JOINS GROWW AS INVESTOR ADVISER**

*Groww enables users to invest in stocks, mutual funds, ETFs, IPOs, Gold etc. Starting in 2017, it claims to have more than 15 million registered users.*

*Groww had raised USD 251 million (around Rs 1,885 crore) in October 2022 in a funding round led by Iconiq Growth, which valued the mutual fund and stock investment platform at USD 3.6 billion.*

Link to a lecture by Sam Altman:-

<https://www.youtube.com/watch?v=0IJKucu6HJc>