FINANCE 101

Business Through the Numbers

Session Goal:

To DISCUSS AND EXPLAIN KEY FINANCE CONCEPTS, which will enable a better understanding of a company's performance and investment decisions.

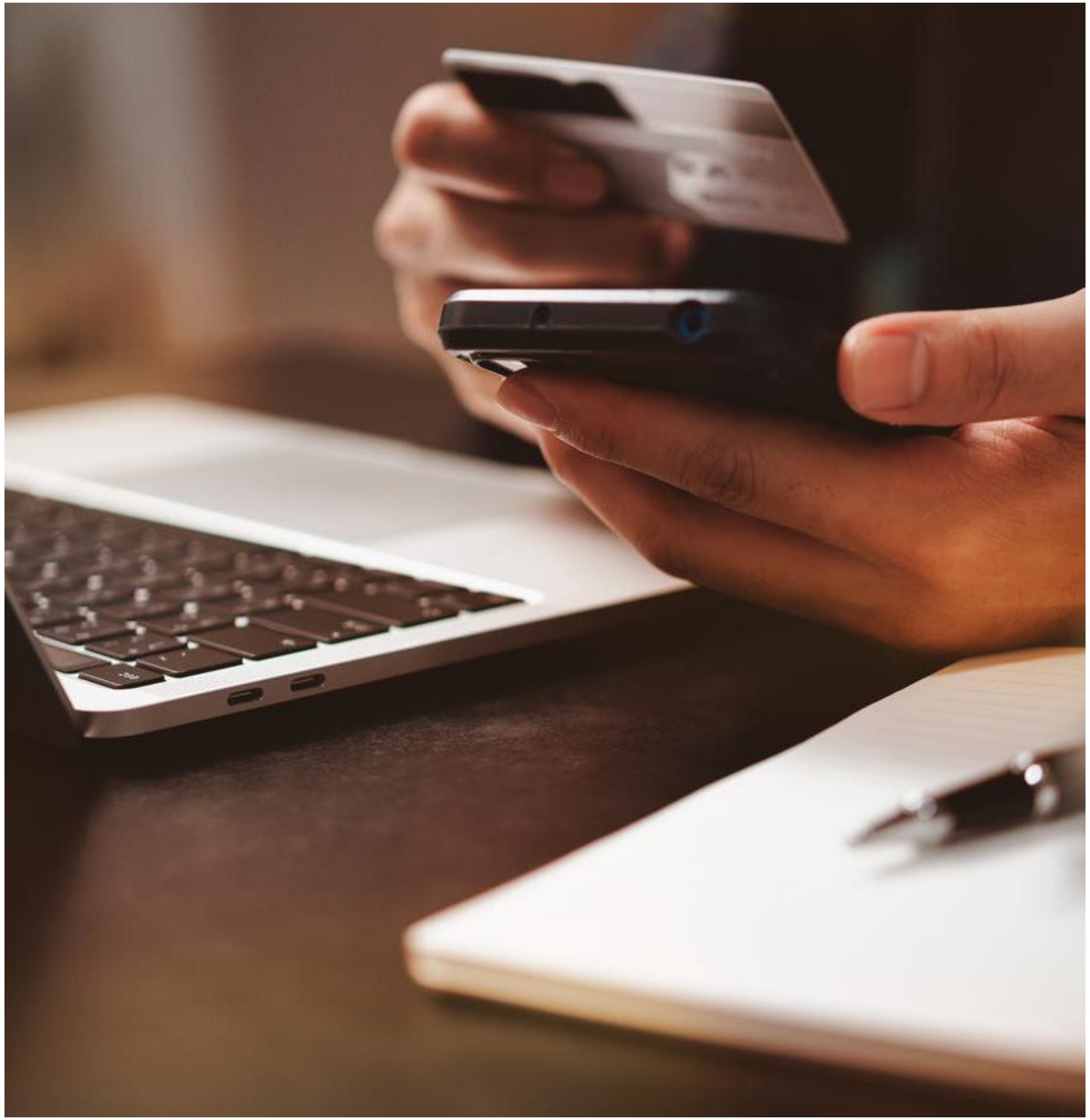
Agenda:

- Key Financial Concepts
- What Do Finance Teams Do?
- Valuation of companies

RUCHIE GUPTA

What comes to mind when you hear the word “finance”?

Key Financial Concepts



Financial Statements

Financial Statements

Income Statement
A financial report that shows a company's profit and loss over a specific period

Balance Sheet
A snapshot of a company's financial standing at a particular moment

Cash Flow Statement
A financial statement that reports a company's sources and usage of cash over a specific period

Common Use Cases

- How are we performing vs. our competitors?
- Do we have the capital to invest in new lines of business?
- How much cash runway do we have?
- Is purchasing this stock a good idea?

Users

Financial Reports

- Investors
- Financial Institutions
- Public Shareholders
- Management
- Compliance Authorities

Key Finance Metrics:

All values in USD millions	2023
(+)Revenues	100
(-) Operating Expenses	-61
EBITDA	39
EBITDA Margin	39.42%
(-)Interest, Taxes, Depreciation, Amortization & other expenses	-15
Net Income/Earnings	24
(+/) Non-Cash Expenses/Income	12
(-) Capital Expenditures	-8
Free Cash Flow	28

How would you rate
your **level of confidence**
in understanding these metrics?

Not confident at all

Very confident

Key Finance Metrics: Revenue & Revenue Growth

What is it?

Revenue is total income generated by the company by selling good or services from it's routine operations

Revenue Growth is **year over year growth in revenue** – typically normalized for M&A, divestitures

Why it's important?

Key metric used internally and by investors to gauge our performance. Stronger growth over time yields higher profits to fund reinvestment and shareholder returns.

How can you impact this metric?

Contribute to key revenue drivers – new sales, retention, and pricing by making better products, sell more, better service

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(+)Revenues	100
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Key Finance Metrics: Expenses

OpEx

Expenses a business incurs through its normal operations. *Impacts EBITDA margin, Earnings Per Share (EPS) and free cash flow.*

Examples: payroll, marketing, sales, support functions, T&E, customer support, etc.

CapEx

Funds used to acquire and maintain physical property or equipment. Includes capitalized software development spend. *Impacts free cash flow and EPS.*

Examples: new product development, property and equipment purchases, real estate upgrades, etc.

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Key Finance Metrics: EBITDA & EBIDTA Margin

What is it?

EBITDA is defined as Earnings before Interest, Taxes, Depreciation and Amortization.

EBITDA divided by Revenue is EBIDTA Margin

Why it's important?

It represents the operational profitability of the company. Used internally and by investors to gauge our performance.

How you can impact this metric?

Contribute to revenue growth, control expenses and/or find efficiency opportunities.

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Key Finance Metrics: Assets

What is it?

Anything of value owned by the company. It is something that the company controls and can be used for running the business. Many assets depreciate

Why it's important?

Represents available funds for generating revenue, increasing business value, facilitating operations, financing, attracting investors, etc. They are important to pay off liabilities

How can you impact this metric?

Protect and develop assets
Use them in the right way
Reduce value deterioration, if possible

All values in USD millions	2023
(+) Current Assets	43
(+) Property, plant and equipment, SW	25
(+) Intangibles Assets & Goodwill	145
(+) Other assets	62
Total Assets	275
Current Liabilities	48
Long term debt	43
Other liabilities including tax	0
Equity – capital, Retained earnings	185
Total Liabilities	275

Key Finance Metrics: Liabilities

What is it?

Debts or obligations that a company owes to others – they can be current or long term

Why it's important?

Understand financial flexibility of a business
Determines ability to stay solvent & pay debts
Interest expense & hence profitability

How can you impact this metric?

Compliance with policies, regulations
Avoid negligence, breach of contract
If owner, manage lifestyle

All values in USD millions	2023
(+) Current Assets	43
(+) Property, plant and equipment, SW	25
(+) Intangibles Assets & Goodwill	145
(+) Other assets	62
Total Assets	275
Current Liabilities	48
Long term debt	43
Other liabilities including tax	0
Equity – capital, Retained earnings	185
Total Liabilities	275

Key Finance Metrics: Equity

What is it?

It is the owner's stake in business including investment and residual stake in profits
Remember business is not the same as owner

Why it's important?

It provides resources for setting up, growth and expansion

How can you impact this metric?

Improve profitability and long-term viability of business

All values in USD millions	2023
(+) Current Assets	43
(+) Property, plant and equipment, SW	25
(+) Intangibles Assets & Goodwill	145
(+) Other assets	62
Total Assets	275
Current Liabilities	48
Long term debt	43
Other liabilities including tax	0
Equity – capital, Retained earnings	185
Total Liabilities	275

Key Finance Metrics: Free Cash Flow

What is it?

Net cash generated by a business after funding its operations and capital investments (CapEx).

Why it's important?

Represents the net cash generated by our business. It is used to fund reinvestment, M&A and capital returns.

How can you impact this metric?

Contribute to revenue growth, control costs, and pursue efficiencies (both OpEx and CapEx).

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Past, Present & Future

Each of the financial statements are for actuals performance OR for PLANNING & FORECASTING

Budgeting

Budgeting is a critical element of financial management that involves creating a detailed plan for allocating resources over a specific period of time. It helps organizations to better manage their finances and ensure that resources are properly allocated.

Forecasting

Forecasting is a critical element of financial management that involves predicting future performance based on past performance and industry trends. It helps organizations to make informed decisions and plan for the future.

Some practical examples

What can a ratio tell us

Financial ratio is a relative magnitude of two selected numerical values taken from Financial Statements

Standard ratios are used to evaluate overall financial condition of any financial entity

They are used by to compare strengths and weaknesses of various companies

managers within a firm,

current and potential shareholders of a firm,

Creditors

Financial Analysts

Compare same company across time

Compare different companies at the same time but not for buying stock!

Using Diagnostics & Prognostic methods & Common size statements – divide all #'s by Sales

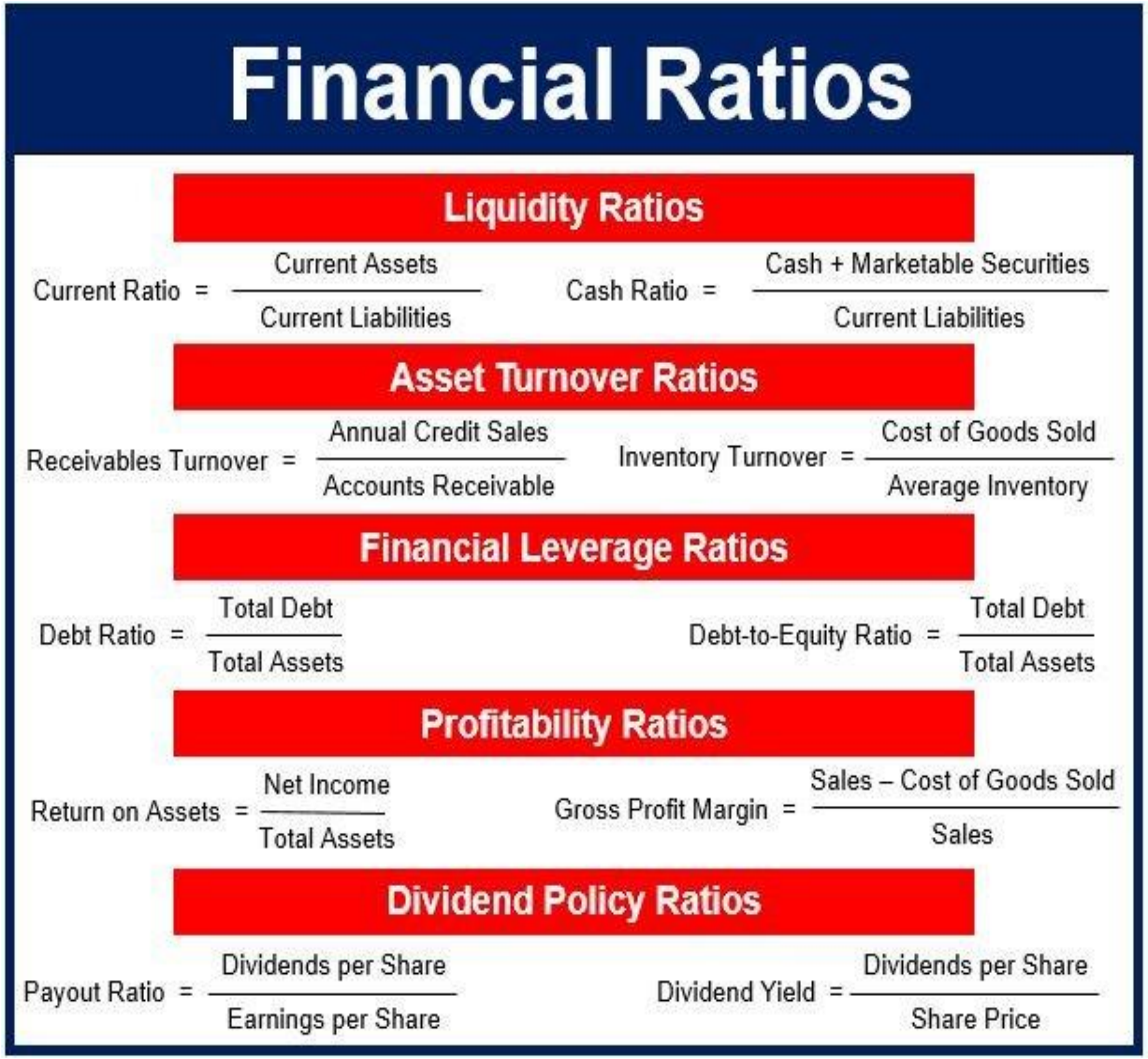
DuPont Framework – Profitability, efficiency, leverage

RoE = Financial Leverage * Asset Turnover * Profit Margin

Assets/Equity * Sales / Assets * Net Income / Sales

Ratios

Profitability Ratios
• Gross Profit Margin
• NOPAT %
• Profitability %
Liquidity Ratios
• Current Ratio
• Quick Ratio
• Operating Cash Ratio
The Financial Ratios
Profitability Ratios
Liquidity Ratios
Working Capital Ratios
Asset Usage Ratios
Efficiency Ratios
Efficiency Ratios
• Return On Equity
• Return On Total Assets
Working Capital Ratios
• Account Recievable Days
• Account Payable Days
• Inventory Days
Asset Usage Ratios
• Asset Turnover Rate
• Activity Ratio
• Woking Capital Absorption



Financial Ratios
Liquidity Ratios
Current Ratio = Current Assets / Current Liabilities
Cash Ratio = Cash + Marketable Securities / Current Liabilities
Asset Turnover Ratios
Receivables Turnover = Annual Credit Sales / Accounts Receivable
Inventory Turnover = Cost of Goods Sold / Average Inventory
Financial Leverage Ratios
Debt Ratio = Total Debt / Total Assets
Debt-to-Equity Ratio = Total Debt / Total Assets
Profitability Ratios
Return on Assets = Net Income / Total Assets
Gross Profit Margin = Sales – Cost of Goods Sold / Sales
Dividend Policy Ratios
Payout Ratio = Dividends per Share / Earnings per Share
Dividend Yield = Dividends per Share / Share Price

Valuation of a company

Method	Suited for	Benefits	Disadvantages
Asset-Based Valuation	Companies with significant tangible assets (e.g., real estate, equipment)	Simple to understand and calculate, relies on objective data	May undervalue companies with intangible assets (e.g., brand, intellectual property), may not reflect market value
Market-Based Valuation	Publicly traded companies or those with similar publicly traded counterparts	Reflects market perception of the company's value, relatively easy to apply	Requires comparable companies to be available, may not be accurate for unique or early-stage companies
Income-Based Valuation	Companies with predictable cash flows and growth prospects	Considers future earnings potential, can capture the value of intangible assets	Requires forecasting future cash flows, sensitive to assumptions about growth and discount rates
Comparable Transactions Method	Companies in industries with frequent mergers and acquisitions	Based on recent market transactions, reflects current market trends	Requires data on comparable transactions, may not be accurate for unique or early-stage companies
Venture Capital Method	Startups and early-stage companies	Considers the potential future value of the company, often used in venture capital financing	Requires making assumptions about future growth and performance, can be subjective
Option Pricing Theory	Companies with high growth potential and uncertain future cash flows	Can capture the value of optionality and flexibility, suitable for high-risk, high-reward scenarios	Complex and requires specialized knowledge of financial options, may not be widely applicable

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Agenda:

- Key Financial Concepts - RECAP
- Corporates Social Responsibility & Integrated Reporting
- Business cases and CBA

RUCHIE GUPTA
CA, CPA, CISA

What comes to mind when you hear the words “Corporate Performance – financial and social”. Let’s start with Financial and then go to social

Why do corporates take Social Responsibilities

Finance aims to maximize stakeholder value through sound financial planning, analysis and decision making; also plays a critical role in driving accountability through the organization and ensuring TR achieves its goals

Reputation and Brand Image	Customer Trust Attract and retain employees Investor Confidence
Better Relationships	Community Government Suppliers .
Risk Management	Reputation Legal compliance . Supply chain management through ethical sourcing / practices
Innovation & Sustainability	Design more sustainable products Environment friendly practices .
Employee Engagement and Motivation	Purpose and connection to purpose Culture .

Reporting via Integrated Report

An integrated report is a comprehensive document that provides a holistic view of a company's performance, combining financial, social, and environmental information.

Traditional annual reports focus on financial data, integrated reports shows how the company created value for all stakeholders, including shareholders, employees, customers, suppliers, communities and environment.

- **Holistic approach:** Combines financial, social, and environmental information.
- **Value creation focus:** Explains how the company creates value for all stakeholders.
- **Voluntary reporting:** Not mandated by regulatory bodies.
- **Long-term perspective:** Highlights the company's strategy, governance, and future outlook.

Downloads - DSM Integrated Annual Report 2022
sst-sustainability-statements-dsm-ar22.pdf

Business Case

What is a business case & how is it used

A document that lays out reasons for undertaking a particular project or initiative. It should be a roadmap that provides a clear justification for intended action and its potential benefits.

Business case is a powerful tool to drive innovation, efficiency, and achieve success.

Decision Making	To evaluate merits of a project and determine whether alignment with the organization's goals
Resource Allocation	To secure funding and other resources needed to implement the project
Communication of benefits	To communicate the project's objectives and benefits to stakeholders
Risk Management	To identify and address potential risks before they become significant problems
Performance Management	To track progress and ensure that the project is delivering the expected outcomes

Who creates business case; what should it convey

Anyone can create a business case – project manager, business head, M&A requestor, fund requestor. It needs to be compelling for it to be approved

Component	Description
Executive Summary	A concise overview of the project, its goals, and the expected outcomes.
Problem Statement	A clear and concise description of the problem or opportunity the project addresses.
Proposed Solution	A detailed explanation of how the project will solve the problem or capitalize on the opportunity.
Benefits Analysis	A quantitative and qualitative assessment of the potential benefits, including financial returns, improved efficiency, and enhanced customer satisfaction.
Cost-Benefit Analysis	A comparison of the project's expected costs and benefits to determine its financial viability.
Risk Assessment	An identification and evaluation of potential risks and mitigation strategies.
Implementation Plan	A detailed outline of the project's timeline, resources, and key milestones.

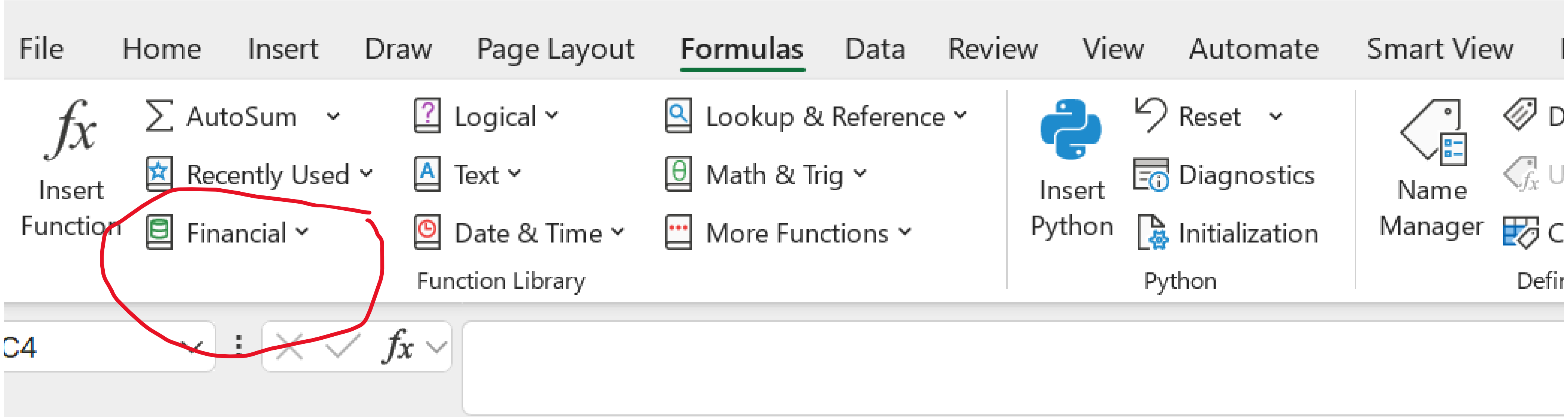
Cost Benefit Analysis

Component	Description	Example
Identification of Costs and Benefits	Clearly define the direct and indirect costs and benefits associated with project.	**Direct costs:** Equipment, labor, materials; Indirect costs: Increased utility bills, decreased productivity; **Benefits:** Increased revenue, improved customer satisfaction, cost savings
Quantification of Costs and Benefits	Assign monetary values to costs and benefits whenever possible. Use qualitative measures for intangible factors.	Direct costs: Estimated licensing fees, hardware costs; Benefits: Projected increase in sales, estimated reduction in customer churn
Discounting	Account for the time value of money by applying a discount rate to future costs and benefits.	Represents rate of return if org was to invest in an alternative, equally risky asset. Companies use Weighted Average Cost of Capital
Calculation of Net Present Value (NPV)/Internal Rate of Return (IRR)	Subtract the present value of costs from the present value of benefits to determine the financial viability of the project.	Positive NPV indicates a profitable project; Negative NPV project may not be financially viable. IRR is rate at which NPV = 0
Sensitivity Analysis	Evaluate how changes in key assumptions affect NPV.	Example: If assumptions were to change by 20% in sales what is the impact on the NPV.
Scenario Analysis	Examine outcomes under different scenarios. Use probabilities	Example: Sales if market is Optimistic, realistic/ baseline, pessimistic Example: Government supportive vs. non supportive

3 simple examples

Make versus Buy	Launching a new product	Installing a new machine
In-house production: Capital expenditures for new machinery: $200,000 Labor costs: $50,000 per year Material costs: $30,000 per year Overhead costs: $20,000 per year OR **Outsourcing:** Purchase price from external supplier: $130,000 per year	**Product Development Costs:** App development: $500,000 Marketing: $200,000 App store fees: $50,000 ? Cloud costs: $0.50 /user/month Revenue Projections: **Subscription model:** Monthly subscription fee of $0.99 per user. **Estimated user base:** 5,000 paid subscribers within the first year and 50,000 after that	**Cost of new machine:** $350,000 **Installation costs:** $75,000 **Salvage old machine:** $10,000 **Cost Savings:** **Increased efficiency:** new machine will reduce production time by 10%. **Energy consumption:** new machine has 10% reduction in energy costs. **Improved product quality:** new machine produces better products. **Revenue Increase:** **Increased production capacity:** by 5%. **Improved product quality:** may lead to increased sales and higher prices. **Annual cost savings:** $40,000 (from increased efficiency, reduced energy consumption, and improved product quality)

Use Excel for Financial Functions – few functions



Budgeting and Forecasting

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Financial Analysis

Financial analysis is the process of interpreting financial data to make informed decisions. It can help businesses make better investments, improve their financial performance, and manage risk effectively.

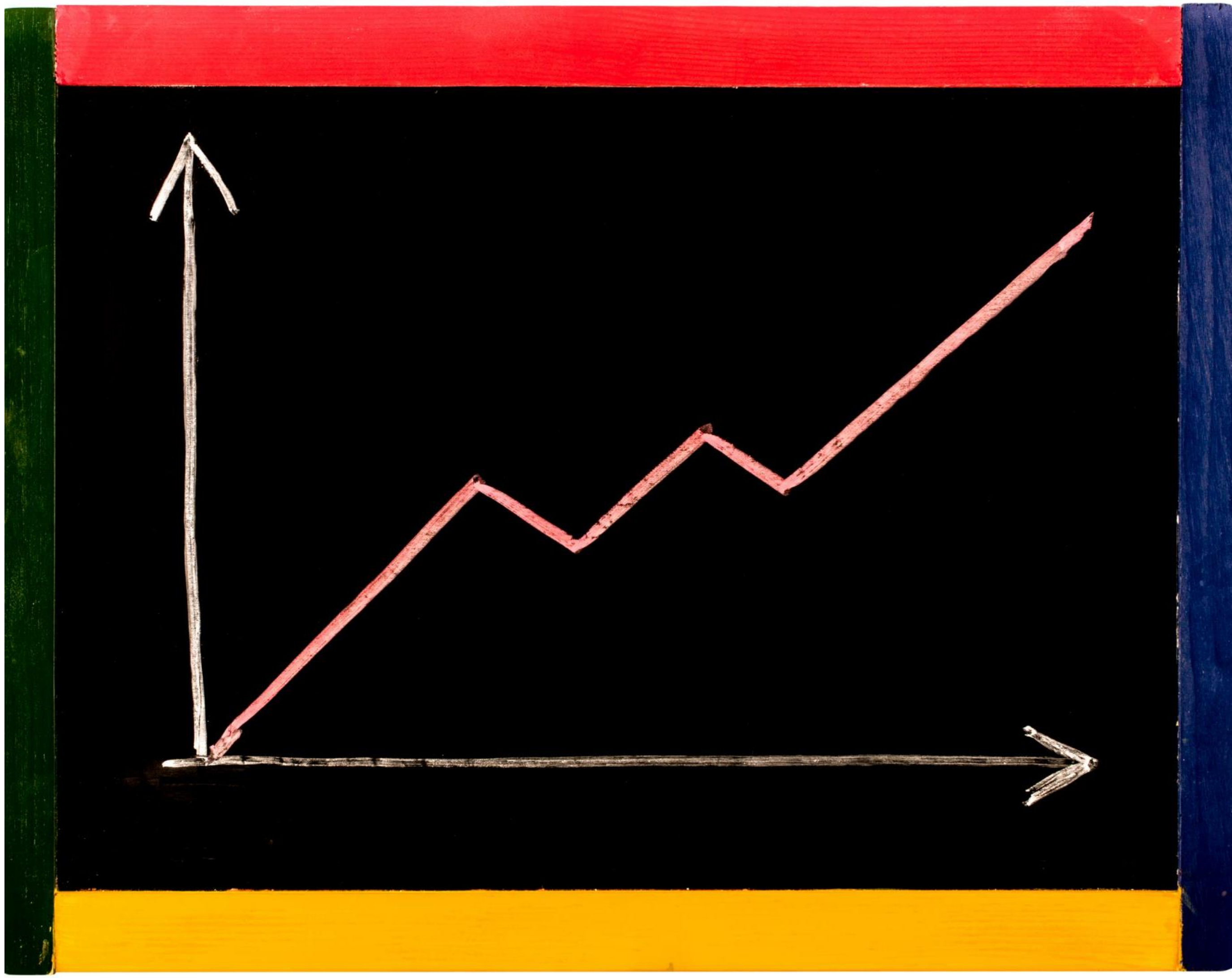
Corporate Performance - Financial and Social Aspects

Financial Performance

Measuring financial performance is crucial for evaluating a company's success. Financial performance indicators include revenue growth, profit margin, return on investment, and cash flow.

Corporate Social Responsibility

Corporate social responsibility initiatives are important for a company as they demonstrate a commitment to social and environmental issues. These initiatives can include sustainability, community involvement, employee engagement, and ethical business practices.



Burn Rate

- Burn rate is the rate at which a company is using up its cash reserves
- It is typically measured on a monthly basis and can be used to estimate how long a company can survive without additional funding
- If a company's burn rate exceeds its revenue, it may need to raise additional capital or cut costs to remain viable