

What Are Financial Statements?

Financial statements are reports businesses compile to record financial performance and health. They offer a clear, standardized picture to parties such as investors, creditors, and management, allowing them to assess operations and whether the business is headed in the right direction.

KEY TAKEAWAYS

- Financial statements provide an overview of a company's financial health to stakeholders.
- The four primary types of financial statements are: balance sheet, income statement, cash flow statement, and statement of shareholders' equity.
- Understanding how to read financial statements allows you to make informed investment decisions about a company's performance, stability, and future potential.



The illustration shows two hands shaking in a firm grip, symbolizing agreement or partnership. Behind the hands are several documents, likely financial statements, with dollar signs (\$) and scribbles around them, indicating financial data and transactions.

Financial Statements

['fə-'nan(t)-shəl 'stāt-mənts]

Written records that convey the business activities and the financial performance of a company.

 Investopedia

Financial statements must present complex data in a clear and accessible way for everyone, from CEOs to average consumers.

Investopedia / Julie Bang

How Financial Statements Work

Financial statements organize important financial data so stakeholders, including board members, investors, shareholders, creditors, employees, customers, and analysts, can analyze the health of a company's finances. These statements must present complex data in a clear and accessible way for everyone, from CEOs to average consumers.

Accountants prepare financial statements following specific accounting rules, like the [Generally Accepted Accounting Principles \(GAAP\)](#) for U.S. companies or the [International Financial Reporting Standards \(IFRS\)](#) for many international companies. These accounting standards ensure that financial statements are clear, consistent, and comparable, so financial data presentation is as similar as possible.

There are four primary types of financial statements that provide valuable insights into a company's financial position and performance.

Balance Sheet (Statement of Financial Position)

A company's balance sheet provides stakeholders with a snapshot of its assets, liabilities, and shareholder equity at a specific point in time—typically the last day of the reporting period. Rather than predicting future success or trends, the balance sheet reflects the company's current financial position.

Take the Next Step to Invest

Advertiser Disclosure

The balance sheets follow the standard equation: **Assets = Liabilities + Equity**.

You must understand a few basic financial terms to read a balance sheet effectively.

Assets

Assets represent what a company owns and are categorized as either [current or non-current assets](#).

Current Assets

Current assets, often considered short-term assets, can be converted into cash within the firm's fiscal year.

- **Cash and Cash Equivalents:** Any highly liquid asset, like cash, checking accounts, or money market funds.
- **Accounts Receivable:** Money owed by customers.
- **Inventory:** Products or raw materials used for products.
- **Prepaid Expenses:** Payments made in advance for expenses like rent or insurance.

Non-Current Assets

These assets, also called long-term assets, are critical for a company's success but cannot be converted into cash within the firm's fiscal year.

- **Property, Plant, and Equipment (PP&E):** Buildings, machinery, vehicles, or other equipment.
- **Intangible Assets:** Non-physical assets like patents and trademarks.
- **Long-term Investments:** Stocks, bonds, or notes held more than one year.
- **Deferred Tax Assets:** Taxes due back for overpayment or advance payment.

Liabilities

Current Liabilities

The [liabilities](#) due within a year.

- **Accounts Payable:** Money owed to suppliers and vendors.
- **Short-term Debt:** Loans or credit lines due within the year.
- **Accrued Expenses:** Incurred, but unpaid costs like wages or taxes.
- **Unearned Revenue:** Money received for goods or services not yet delivered.

Non-Current Liabilities

Often called [long-term liabilities](#), these are the company's financial obligations not due within a year.

- **Long-term Debt:** Debt payable in more than one year, such as bonds or long-term loans.
- **Deferred Tax Liabilities:** Future tax payments.
- **Pension Liabilities:** Employee retirement benefits obligations.
- **Lease Liabilities:** Long-term lease commitments for buildings or equipment.

Equity

Equity, also called net assets, represents the company's assets minus its liabilities. Net assets are payable to shareholders.

- **Common Stock/Preferred Stock:** Value of issued shares.
- **Retained Earnings:** Profits not distributed as dividends.
- **Treasury Stock:** The company's repurchased stock.