# Foundations of Entrepreneurship

## INTRODUCTION TO FINANCIAL STATEMENTS

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Lecture Note # 6

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## Topics to be covered

- Understanding financial statements
- Balance sheet
- Profit & Loss Account
- Cash Flow Statement

# How Important is Financial Statements

01 There is a saying:

If one can't manage finances, won't be able to manage a business.

03 The fact that a major cause of startup failure is 'running out of cash', reinforces the above statement.

04 All entrepreneurs and non-entrepreneurs who are directly or remotely connected to the past, present, and future financials of a company must have a grip on financial statements.

# The primary purpose of financial statements is to report the actual financial state of any company to all stakeholders.

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

- **Financial statements should be viewed from two perspectives: one from the entrepreneurs, and the other, from the other stakeholders' perspectives.**
- **Depending on which side you are in, you would like to look at it through different prisms.**
- **Owners of a company frequently under-report or over-report performance to derive values.**
- **The consumers of the data in financial statements are the victims of such wrong reporting.**

# From Owners' Perspective

- **Decisions**
  - Cost cutting
  - Pricing
  - Hiring
  - Hiving off
  - Capacity augmentation
  - Making-vs.- outsourcing
  - Borrowing
  - Capital raising

# Major Disaster for Accounting Frauds: Enron

- At its peak, Enron was one of America's largest corporations with 22,000 employees.
- Reported $111 billion revenues in 2000
- Overstated profit and hide debt.
- When it came to light,
  - Share price went from $90.75 in August 2000 to just $0.67 in 2002 to 0.0 soon.

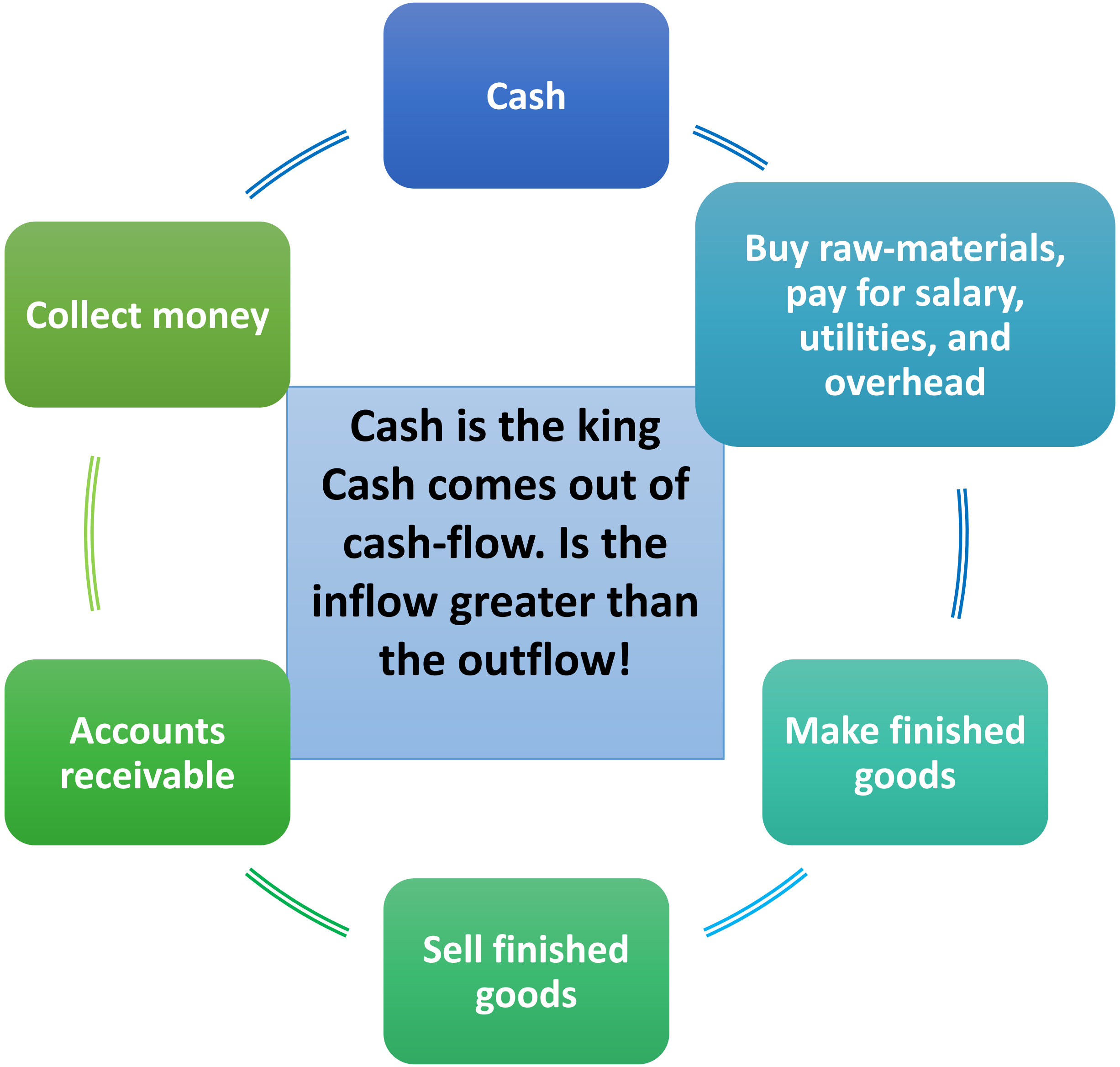
# Major Disaster for Accounting Frauds: WorldCom

## WorldCom, USA

- Was the second biggest phone company
- WorldCom fraudulently underreported cost of a staggering \$3.8 billion (£3bn).
- In 2020, it filed for bankruptcy.

## Satyam Computers of Hyderabad

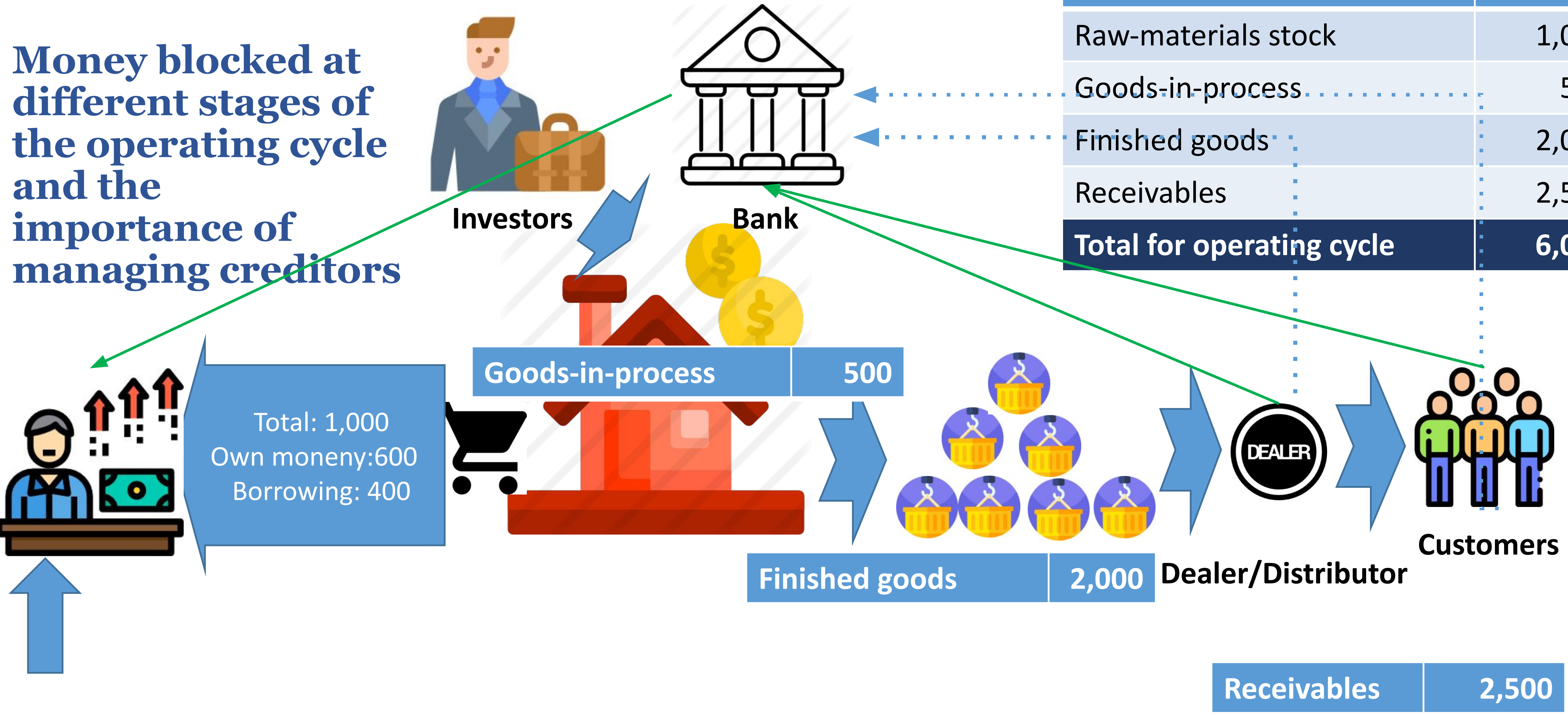
- The chairman of Satyam Computers, Ramalinga Raju confessed that the company's accounts had been falsified to the extent of Rs 12,318 crore.
- The company went through turmoil rendering thousand of employees jobless and millions of investor poorer.




Operating cycle starts from cash and moves through purchase of raw materials, converting them into finished goods, selling them and receiving the cash.
In numeric term, the operating cycle is the average period of time required for a business to complete this process.

# Money blocked at different stages of the operating cycle and the importance of managing creditors

| | |
|---|---|
| Investment in fixed assets | 10,000 |
| Raw-materials stock | 1,000 |
| Goods-in-process | 500 |
| Finished goods | 2,000 |
| Receivables | 2,500 |
| Total for operating cycle | 6,000 |

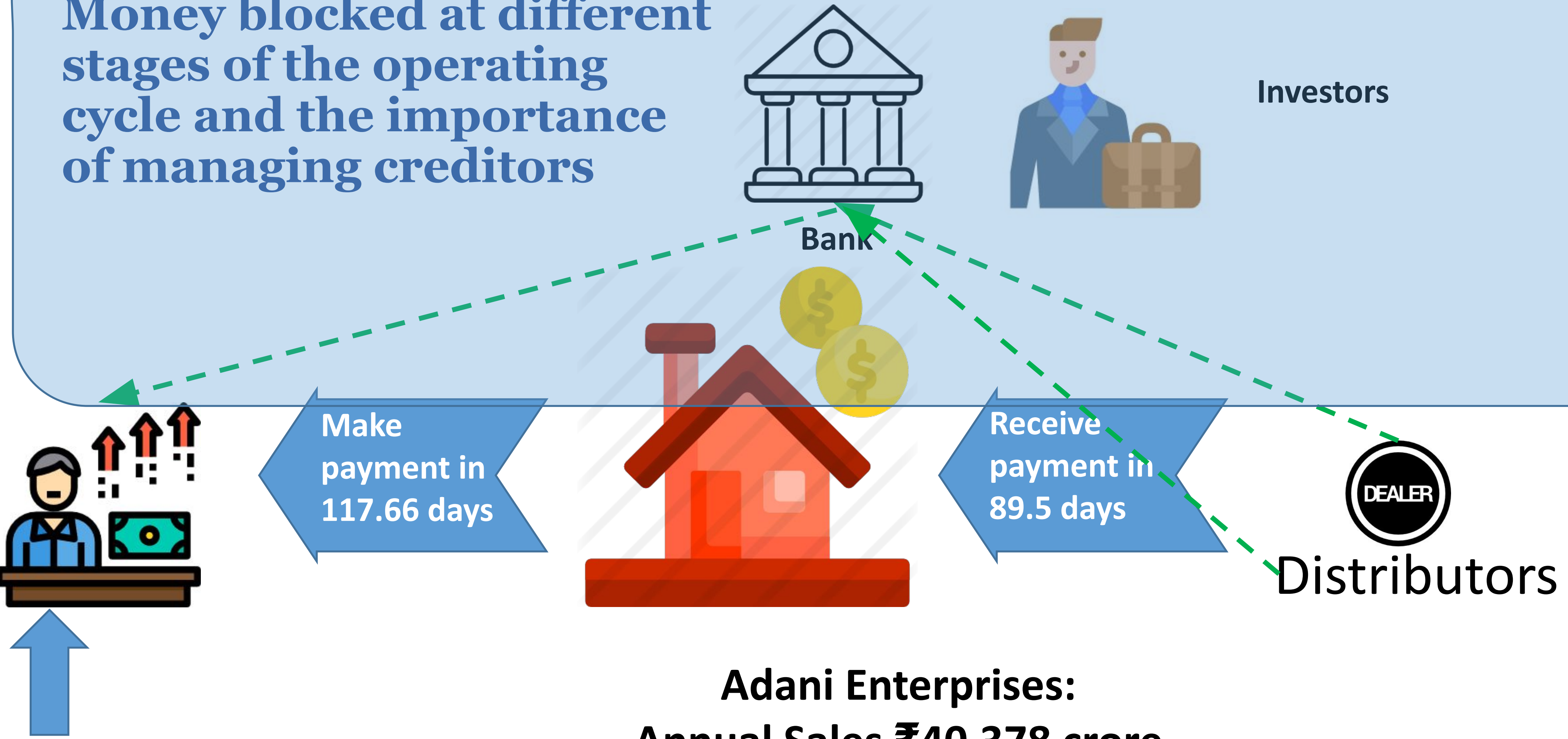



Adani Enterprises:

**Adani enterprise : has**
**Receivable cycle of 89.55 days and**
**Payable cycle of 117.66 days.**

**Define receivable cycle:**
**Average outstanding in Receivable: 2,500**
**Annual sales: 10,000**
**Receivable turnover ratio: 10,000/2,500 = 4**
**Receivable cycle: 365/4 = 91.25 days**

# Money blocked at different stages of the operating cycle and the importance of managing creditors




**Adani Enterprises:**
**Annual Sales ₹40,378 crore**

# Double entry system

- **Double entry system** of accounting means that every business transaction involves two or more accounts.
- Example: Your company 'A' purchases raw-materials (₹500) from company 'B' in cash. Your cash account reduces and raw-material purchase account increases. The books where you enter these data are called ledgers. For example 'Cash Ledger', 'Sales Ledger', 'Purchase Ledger', etc.

# Double Entry System

- If your payment is partly on cash (₹300) and partly on credit,(₹200) three accounts will be affected:
  - Purchase: ₹500
  - Cash: ₹300
  - Accounts payable: ₹200

Purchase of goods worth ₹500

# The debit – credit rule

**The debit – credit rule is that asset account is debited when value increases; opposite is for liabilities.**

**Income account is credited when value increases; opposite is for expenses.**

**Purchase: ₹500 (Expense type account) Purchase ledger debited**
**Cash: ₹300 (Asset type account) Cash ledger credited**
**Accounts payable: ₹200 (Liability type account) Accounts payable ledger credited**

- **The English words credit and debit come from the Latin words credre and debere, respectively. Credre means "to entrust," and debere means "to owe".**
- **In financial accounting or bookkeeping, "Dr" (Debit) indicates the left side of a ledger account and "Cr" (Credit) indicates the right.**
- **The rule that total debits equal total credits applies when all accounts are totaled.**
- **An increase (+) to an asset account is a debit. An increase (+) to a liability account is a credit.**
- **Conversely, a decrease (-) to an asset account is a credit. A decrease (-) to a liability account is a debit.**
- **It is important for us to consider perspective when attempting to understand the concepts of debits and credits.**

# Three Major Financial Statements

- Balance Sheet
- Profit & Loss or Income statement
- Cash Flow statement

**A fourth statement is also used**

**Statement of changes in owners' equity or stockholders' equity.**

# Balance sheet

- Balance sheet is a snapshot of financial position at a particular point in time.
- It aims to convey the position of the assets, liabilities and owner's equity at any particular point in time.

# Profit & Loss or Income Statement

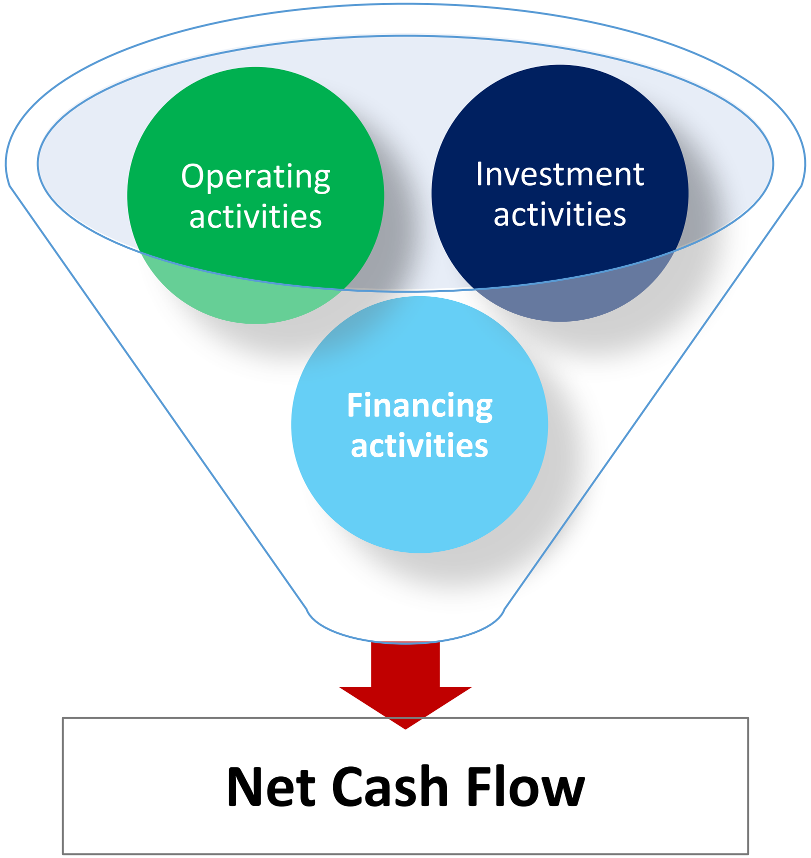
Profit & Loss Statement, also known as 'Income Statement' shows the operational performance of an enterprise for a certain period of time (contrary to balance sheet which refers to the status at a point in time).

Balance sheet as on 31.03.2021
Profit & Loss account for the year starting from 01.04.2020 to 31.03.2021

# Cash Flow Statement

- A cash flow statement is the financial statement that provides information on cash sources and uses from i. Operational activities, ii. Investment activities & iii. Financing activities, is the net cash flow of an enterprise for a specific period.
- Cash flow statement contains all the receipts and payments of cash and cash equivalent of an enterprise and the net cash receipt during an accounting period. It reveals whether net cash flow is increasing or decreasing.
- The net cash flow data is very useful in understanding liquidity position of a company and help eliminate any possible misperception stemming from profit data.

# Cash flows from i. Operational activities, ii. Investment activities & iii. Financing activities



# Use of Cash Flow Statement for Startups

- Money gets used up in assets, dividend, investment, and accounts receivables, some of which becomes sticky and illiquid.
- Cash flow shows how liquid the business is and projected cash flow reveals if the company is likely to fall short of cash to make essential payments in the future.
- If cash shortage is imminent, the founders can take preemptive action to arrange fund.

- The fundamental and critical question to answer is how much money it will take to get the venture started.
- Let us take a very simplistic example. Let's start from setting up a new firm: a retail store.
- Financial statements for any company engaged in retail business are simpler compared to those of a manufacturing company. So, let us start with a retail store.
- Let us start something with which you all may connect very easily. Suppose you are starting a stationery shop at your hostel.

- Let us see what all you need to start the business and estimate the requirement of fund:
- Counter : ₹ 500
- Rack : ₹ 600
- Chair : ₹ 400
- Subtotal ₹ 1,500
- Purchase materials i.e. stationery items (pens, notebooks, files/folders, pencils, and the like): ₹ 5,000
- Suppose that you want to keep some small change (cash): ₹500
- Subtotal: ₹ 5,500
- Total : ₹ 7,000

# Your Business Has Two Kinds of Assets

## Long-term or Fixed assets

Counter : ₹ 500
Rack : ₹ 600
Chair : ₹ 400
Subtotal ₹ 1,500

## Short-term or Current assets

pens, notebooks, files/folders, pencils, and the like): ₹ 5,000
And some cash: ₹ 500

# Fixed Assets or Long-Term Assets

- All the above are assets of your business.
- Give a sharp look at the items in the first part and try to understand that these items are not for sale. You need them to facilitate your business. At some point of time you may like to replace them and sell them as used machine. But that is not part of the business.
- These assets are called "Long-Term Assets" or "Fixed Assets". They contribute to your business but they remain with you for a long time.

# Short-Term Assets or Current Assets

**Contrary to 'Fixed Assets' the raw-materials or the stationery items are meant for selling and they are meant to be with your business for shortest possible time so that you can convert them into revenue (sales) and make profit. These are "Short-Term Assets" or "Current Assets".**

# Arranging the Money

- How do you propose to fund purchase of these fixed and current assets?
- Suppose you have ₹ 3,000 with you. So, there is a shortfall of ₹ 4,000. Suppose you could borrow the remaining amount of ₹ 4,000 from your friend Rohit. So, your budgeted project outlay is fully tied up (your project reached financial closure).
- Let us now prepare the balance sheet.

| Balance sheet as on 31.03.2020 | |
|---|---|
| **Assets** | ? |
| **Current assets/ Short-term assets** | |
| Cash | 500 |
| Accounts receivable | 0 |
| Inventory | 5,000 |
| **Fixed assets/ Long-term assets** | |
| Furniture/Fixture | 1,500 |
| Total of Assets: | **7,000** |
| **Liabilities** | |
| **Current liabilities/ Short-term liabilities** | |
| Accounts payable | 0 |
| Short-term Bank loan | 0 |
| **Long-term liabilities** | 0 |
| Long-term Bank loan | 0 |
| Other loan | 4,000 |
| **Owners' equity:** | 3,000 |
| **Total of Liabilities and owners' equity** | **7,000** |

# You have now started the business on 1st of April 2020.

- Soon you realise that there is good demand and that you have your own engagements. So, you decide to hire an employee, say, with monthly salary of ₹ 5,000
- Now you need a billing machine to keep track of inventory and sales.

| Balance sheet as on 31.03.2020 | |
|---|---|
| **Assets** | ? |
| **Current assets/ Short-term assets** | |
| Cash | 500 |
| Accounts receivable | 0 |
| Inventory | 5,000 |
| **Fixed assets/ Long-term assets** | |
| Furniture/Fixture | 1,500 |
| Total of Assets: | **7,000** |
| **Liabilities** | |
| **Current liabilities/ Short-term liabilities** | |
| Accounts payable | 0 |
| Short-term Bank loan | 0 |
| **Long-term liabilities** | 0 |
| Long-term Bank loan | 0 |
| Other loan | 4,000 |
| **Owners' equity:** | 3,000 |
| **Total of Liabilities and owners' equity** | **7,000** |

## Following are the transactions during the year 2020-21 (from 01.04.2020 to 31.03.2021)

| | | | |
|---|---|---|---|
| Sales | 5,00,000 | | |
| Purchase of materials | 2,50,000 | Depreciation | |
| Salary | 60,000 | Furnit | 1500 |
| Rent | 12,000 | Depreciation@10% | 150 |
| Closing stock | 10,000 | Book Value | 1350 |
| Transportation | 5,000 | | |
| Telephone | 3,000 | Billing m/c | 10000 |
| Electricity | 6,000 | Depreciation @10% | 1000 |
| Trade license | 5,000 | Book Value | 9000 |
| Depreciation | 1,150 | | |
| Closing cash in hand | ? | Total deprn. | 1150 |
| Accounts payable | 12,000 | | |
| Accounts receivable | 15,000 | | |
| | | | |
| Gross profit | | | |
| Opening inventory | 5,000 | | |

- **Gross profit = Sales – Cost of goods sold**
- **Operating profit = Gross profit – Operating expenses**
- **Profit Before Tax (PBT) = Operating profit – Interest expenses**
- **Net profit = Profit before tax – Income tax**
- **Retained profit = Net profit – dividend**
- **EBITDA = Earnings (profit) before Interest, tax, depreciation & amortization.**

# Profit Margin is percentage profit with respect to sales

$$Gross\ Profit\ Margin = \frac{Gross\ profit}{Sales} \text{x}100$$

$$Operating\ Profit\ Margin = \frac{Operating\ profit}{Sales} \text{X}100$$

$$Net\ Profit\ Margin = \frac{Net\ profit}{Sales} \text{X}100$$

$$EBITDA\ Margin = \frac{EBITDA}{Sales} \text{X}100$$

Notice that the denominator is always ‘sales’.

# Why different types of profits??

# Why to Estimate Different Profits

- Each type of profit helps to make an apple-to-apple comparison.
- Some company may be efficient in managing the process better than others. Some may be efficient in managing the operating expenses.
- EBITDA helps to compare companies by eliminating the differences of depreciation, interest and tax.
- Some company's capital structure may have a high debt. So, even if they are more efficient in managing process and operation, may perform poorly on the PBT.
- You want to know the cause of certain performance.

All figures are in Rupees billion

| | Mahindra & Mahindra | | Tata Motors | | Maruti Suzuki | |
|---|---|---|---|---|---|---|
| | 19-20 | 18-19 | 19-20 | 18-19 | 19-20 | 18-19 |
| Net Sales | 951 | 1047 | 2610 | 3019 | 756 | 860 |
| Operating Profit | 136 | 162 | 209 | 276 | 106 | 135 |
| Operating profit margin % | **14.30** | **15.47** | **8.01** | **9.14** | **14.02** | **15.70** |
| Interest | 60.65 | 50.21 | 72 | 57 | 1 | 0.1 |
| Interest % to OP | **44.60** | **30.99** | **34.45** | **20.65** | **0.94** | **0.07** |
| PBDT | 75 | 112 | 137 | 218 | 105 | 134 |
| Profit Before Tax | 6 | 75 | -105 | -313 | 69 | 104 |
| Provision for Tax | 19 | 28 | 3 | -24 | 14 | 29 |
| Profit After Tax | -13 | 46 | -109 | -289 | 55 | 74 |
| Net profit margin | -0.01 | 0.04 | -0.04 | -0.10 | 0.07 | 0.09 |
| Share price ₹ | **615** | | **148** | | **7128** | |

# Why to Estimate Different Profits

- **Gross profit reflects efficiency of converting inputs into sales. If one company's gross profit margin (percentage) is more than others in the same industry, it is because one or more of the followings:**
  - **More efficiently converts raw-materials into finished goods.**
  - **More energy-efficient process.**
  - ***Sells at higher price than competitors.***
  - ***Bargaining power in buying inputs.***
  - ***Use more efficient manufacturing process than others.***
- **In short, they are more efficient and likely to be more profitable than competitors**

# Operating Profit Margin is Combination of Processing and Operational efficiency.
# However, it does not take into account the differentiation caused due to cost of financing across companies.
# PBT margin takes into account the finance costs.
# Net profit margin takes into account the income tax management.

You prepare balance sheet at this point of time, i.e. as on a particular date: here, as on 31.03.2020

You prepare Profit & Loss Account for this entire period, i.e. from 01st April 2020 to 31st March 2021

You prepare balance sheet at this point of time, i.e. as on a particular date: here, as on 31.03.2021

Year 2019-20

Year 2020-21

Year 2021-22

PURCHASE DURING THE YEAR

Closing stock

Opening stock

You purchase a lot of stocks and sell a lot of them during the year. But some stocks remain unsold, they are the closing stock

Closing stock

Opening stock

**Closing stock: ₹5,000**
**Year 2019-20**

**Opening stock: ₹5,000**
**Year 2020-21**

**Closing stock: ₹10,000**
**Year 2020-21**

**Opening stock: ₹10,000**
**Year 2021-22**

Closing stock is the stock or inventory that remains unsold as at the close of business of any particular year. You begin the business in the next year with the closing stock of the previous year. Therefore, the closing stock of the previous year becomes the opening stock of the next year.

| | |
|---|---|
| **Cost of goods sold** | |
| Opening stock of materials | 5,000 |
| Purchase | 2,50,000 |
| Closing stock of materials | 10,000 |
| **Cost of goods sold** | **2,45,000** |

**Opening stock data is obtained from previous year balance sheet. It is the closing stock of previous year.**

**Cost of goods sold = Opening inventory + Purchase during the year – Closing Inventory**

| | |
|---|---|
| **Cost of Goods Sold** | |
| Opening stock of materials | 5,000 |
| Purchase | 2,50,000 |
| Closing stock of materials | 10,000 |
| **Cost of Goods Sold** | **2,45,000** |

Opening stock data is obtained from previous year balance sheet. It is the closing stock of previous year.

**For the purpose of estimating 'Materials consumed' to derive 'Gross Profit' previous year's 'Closing stock' is current year's 'Opening stock'.**

| Year 2019-20 | Year 2020-21 | | | Year 2021-22 |
|---|---|---|---|---|
| As on 31.03.2020 | As on 01.04.2020 | Purchase during the year ₹2,50,000 | As on 31.03.2021 | As on 01.04.2021 |
| Closing stock: ₹5,000 | Opening stock: ₹5,000 | | Closing stock: ₹10,000 | Opening stock: ₹10,000 |

| | | |
|---|---|---|
| **Sales** | | **5,00,000** |
| **Gross profit** | | |
| Opening stock of materials | | 5,000 |
| Purchase | (+) | 2,50,000 |
| Closing stock of materials | (–) | 10,000 |
| **Cost of goods sold (CoGS)** | | **2,45,000** |
| | | |
| **Gross profit = (sales - CoGS)** | | 2,55,000 |

**Opening stock data is obtained from previous year balance sheet. It is the closing stock of previous year.**

# Depreciation

- **Depreciation is an accounting method of gradual apportioning of the cost incurred to acquire a tangible asset as expense over its useful life.**
- **Businesses depreciate long-term assets differently for two different accounting purposes: i. for tax and ii. for reporting to stakeholders.**

# Depreciation is the process of charging the loss of value of capital assets in Profit & Loss A/C

- Through depreciation, the procurement costs of capital assets are gradually charged in the profit & loss account.
- The other alternative is to charge the entire cost of acquisition as expense in the year the expenditure is incurred.
- But that would cause great volatility in the bottom-line (profit), which is not desirable.

| Depreciation | |
|---|---|
| Furniture | 1500 |
| Depreciation @10% | 150 |
| Book value net of depreciation | 1350 |
| | |
| Billing m/c | 10000 |
| Depreciation @10% | 1000 |
| Book value net of depreciation | 9000 |
| Total depreciation | 1150 |

Detailed discussion on methods of depreciation and their significance would be made later

Depreciation is gradual apportioning of the cost of a tangible asset over its useful life span. Businesses depreciate long-term assets mostly differently for accounting and tax purposes.

## Following are the transactions during the year 2020-21 (from 01.04.2020 to 31.03.2021)

| | |
|---|---|
| Sales | 5,00,000 |
| Purchase of materials | 2,50,000 |
| Salary | 60,000 |
| Rent | 12,000 |
| Closing stock | 10,000 |
| Transportation | 5,000 |
| Telephone | 3,000 |
| Electricity | 6,000 |
| Trade license | 5,000 |
| Depreciation | 1,150 |
| Closing cash in hand | ? |
| Accounts payable | 12,000 |
| Accounts receivable | 15,000 |

| Depreciation | |
|---|---|
| Furnit | 1500 |
| Depreciation@10% | 150 |
| Book Value | 1350 |
| | |
| Billing m/c | 10000 |
| Depreciation @10% | 1000 |
| Book Value | 9000 |
| | |
| Total deprn. | 1150 |

## Let us estimate the operating expenses for the year 2020-21 (i.e. the year starting on 01.04.2020 and ending on 31.03.2021)

| | | | |
|---|---|---|---|
| Salary | 60,000 | Furnit | 1500 |
| Rent | 12,000 | Depreciation@10% | 150 |
| Transportation | 5,000 | | |
| Telephone expenses | 3,000 | Billing m/c | 10000 |
| Electricity | 6,000 | Depreciation @10% | 1000 |
| Trade license | 5,000 | Book Value | 9000 |
| Depreciation | 1,150 | | |
| Operating expenses | 92,150 | Total deprn. | 1150 |

| | |
|---|---|
| Gross profit margin % | 51 |
| Operating expenses | 92,150 |
| **Operating profit** | 1,62,850 |
| Interest | 40 |
| **Profit before tax** | 1,62,810 |
| Income tax @20% | 32,562 |
| **Net profit** | 1,30,248 |

Note that the profit of proprietorship firm is clubbed with personal income of the proprietor. All income tax benefits of personal income is available. We have considered 30% only for demonstration. The Current rate is about 22%

Continued from the previous slide

| | | | | |
|---|---|---|---|---|
| Net profit | 1,30,248 | | | |
| Suppose you pay yourselves some dividend | 50,000 | | | |
| Retained profit / earnings | 80,248 | | | |
| This amount belongs to the owners. | | | | |
| Therefore, it is added to owners' equity in the form of | | | | |
| Retained Profit or Reserves & Surplus | | | | |

| Balance sheet as on 31.03.2019 | |
|---|---|
| **Assets** | ? |
| **Current assets/ Short-term assets** | |
| Cash | 61,898 |
| Accounts receivable | 15,000 |
| Inventory | 10,000 |
| **Fixed assets/ Long-term assets** | |
| Furniture/Fixture | 1,350 |
| Machinery | 9,000 |
| **Total of Assets:** | **97,248** |

Assets portion of the balance sheet

| Liabilities | ₹ |
|---|---|
| Current liabilities/ Short-term liabilities | |
| Accounts payable | 12,000 |
| Short-term Bank loan | 0 |
| Long-term liabilities | |
| Long-term Bank loan | 0 |
| Other loan Loan from your friend, Rohit | 2,000 |
| Owners' equity: | |
| Equity capital | 3,000 |
| Retained profit/earnings | 80,248 |
| Total of Liabilities and owners' equity | 97,248 |

Liabilities portion of the balance sheet

| Balance sheet as on 31.03.2019 | |
|---|---|
| **Assets** | ? |
| **Current assets/ Short-term assets** | |
| Cash | 61,898 |
| Accounts receivable | 15,000 |
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| **Fixed assets/ Long-term assets** | |
| Furniture/Fixture | 1,350 |
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| **Total of Assets:** | 97,248 |
| **Liabilities** | |
| **Current liabilities/ Short-term liabilities** | |
| Accounts payable | 12,000 |
| Short-term Bank loan | 0 |
| **Long-term liabilities** | |
| Long-term Bank loan | 0 |
| Other loan | 2,000 |
| Owners' equity: | |
| Equity capital | 3,000 |
| Retained profit/earnings | 80,248 |
| **Total of Liabilities and owners' equity** | 97,248 |

Complete balance sheet
As on 31.03.2018

The total assets and the total liabilities must be the same

# Statement of Profit and Loss



For the year ended 31st March, 2020

# Reliance Industries Ltd

(₹ in crore)

| | Notes | 2019-20 | 2018-19 |
|---|---|---|---|
| **INCOME** | | | |
| Value of Sales | | 5,91,778 | 5,85,540 |
| Income from Services | | 67,427 | 39,672 |
| Value of Sales & Services (Revenue) | | **6,59,205** | **6,25,212** |
| Less: GST Recovered | | 47,560 | 42,118 |
| **REVENUE FROM OPERATIONS** | 23 | **6,11,645** | **5,83,094** |
| Other Income | 24 | 13,956 | 8,386 |
| **Total Income** | | **6,25,601** | **5,91,480** |
| **EXPENSES** | | | |
| Cost of Materials Consumed | | 2,60,621 | 2,75,237 |
| Purchase of Stock-in-Trade | | 1,49,667 | 1,23,930 |
| Changes in Inventories of Finished Goods, Work-in-Progress and Stock-in-Trade | 25 | (5,048) | (4,680) |
| Excise Duty | | 14,902 | 13,885 |
| Employee Benefits Expense | 26 | 14,075 | 12,488 |
| Finance Costs | 27 | 22,027 | 16,495 |
| Depreciation / Amortisation and Depletion Expense | 1 | 22,203 | 20,934 |
| Other Expenses | 28 | 89,211 | 78,067 |
| **Total Expenses** | | **5,67,658** | **5,36,356** |
| **PROFIT BEFORE SHARE OF PROFIT / (LOSS) OF ASSOCIATES AND JOINT VENTURES, EXCEPTIONAL ITEM AND TAX** | | **57,943** | **55,124** |
| Share of Profit / (Loss) of Associates and Joint Ventures | | **107** | **103** |
| **PROFIT BEFORE EXCEPTIONAL ITEM AND TAX** | | **58,050** | **55,227** |
| Exceptional Item (Net of Tax) | 28.2 | (4,444) | - |
| **PROFIT BEFORE TAX *** | | **53,606** | **55,227** |
| **TAX EXPENSES *** | | | |
| Current Tax | 12 | 8,630 | 11,683 |
| Deferred Tax | 12 | 5,096 | 3,707 |
| **PROFIT FOR THE YEAR** | | **39,880** | **39,837** |
| **OTHER COMPREHENSIVE INCOME:** | | | |
| i. Items that will not be reclassified to Profit or Loss | 24.1 | 22,286 | 77,470 |
| ii Income Tax relating to items that will not be reclassified to Profit or Loss | | (1,088) | (16,705) |
| iii. Items that will be reclassified to Profit or Loss | 24.2 | (7,085) | (2,177) |
| iv. Income Tax relating to items that will be reclassified to Profit or Loss | | 1,180 | 177 |
| **Total Other Comprehensive Income for the Year [Net of Tax]** | | **15,293** | **58,765** |
| **Total Comprehensive Income for the Year** | | **55,173** | **98,602** |
| **NET PROFIT ATTRIBUTABLE TO:** | | | |
| a) Owners of the Company | | 39,354 | 39,588 |
| b) Non-Controlling Interest | | 526 | 249 |
| **OTHER COMPREHENSIVE INCOME ATTRIBUTABLE TO:** | | | |
| a) Owners of the Company | | 15,311 | 58,773 |
| b) Non-Controlling Interest | | (18) | (8) |
| **TOTAL COMPREHENSIVE INCOME ATTRIBUTABLE TO:** | | | |
| a) Owners of the Company | | 54,665 | 98,361 |
| b) Non-Controlling Interest | | 508 | 241 |
| **EARNINGS PER EQUITY SHARE OF FACE VALUE OF ₹ 10 EACH** | | | |
| Basic (in ₹) – Before Exceptional Item | 29 | 70.66 | 66.82 |
| Basic (in ₹) – After Exceptional Item | 29 | 63.49 | 66.82 |
| Diluted (in ₹) – Before Exceptional Item | 29 | 70.66 | 66.80 |
| Diluted (in ₹) – After Exceptional Item | 29 | 63.49 | 66.80 |
| Significant Accounting Policies | | | |
| See accompanying Notes to the Financial Statements | 1 to 42 | | |

* Profit before tax is after Exceptional Item and tax thereon and Tax Expenses are excluding the Current Tax on Exceptional Item.

# Balance Sheet

As at 31st March, 2020



# Reliance Industries Ltd

(₹ in crore)

| | Notes | As at 31st March, 2020 | As at 31st March, 2019 |
|---|---|---|---|
| **ASSETS** | | | |
| **NON-CURRENT ASSETS** | | | |
| Property, Plant and Equipment | 1 | 4,35,920 | 3,02,115 |
| Capital Work-in-Progress | 1 | 59,096 | 1,50,178 |
| Goodwill | | 10,259 | 11,997 |
| Other Intangible Assets | 1 | 86,479 | 84,262 |
| Intangible Assets Under Development | 1 | 50,010 | 29,285 |
| Financial Assets | | | |
| Investments | 2 | 2,03,852 | 1,64,612 |
| Loans | 3 | 21,732 | 5,452 |
| Deferred Tax Assets (Net) | 4 | 2,900 | 4,776 |
| Other Non-Current Assets | 5 | 37,407 | 17,676 |
| **Total Non-Current Assets** | | **9,07,655** | **7,70,353** |
| **CURRENT ASSETS** | | | |
| Inventories | 6 | 73,903 | 67,561 |
| Financial Assets | | | |
| Investments | 7 | 72,915 | 71,023 |
| Trade Receivables | 8 | 19,656 | 30,089 |
| Cash and Cash Equivalents | 9 | 30,920 | 11,081 |
| Loans | | 669 | 545 |
| Other Financial Assets | 10 | 27,434 | 10,283 |
| Other Current Assets | 11 | 32,763 | 36,804 |
| **Total Current Assets** | | **2,58,260** | **2,27,386** |
| Assets Held for Sale | 39 | - | **4,667** |
| **Total Assets** | | **11,65,915** | **10,02,406** |
| **EQUITY AND LIABILITIES** | | | |
| **EQUITY** | | | |
| Equity Share Capital | 13 | 6,339 | 5,926 |
| Other Equity | 14 | 4,46,992 | 3,81,186 |
| Non-Controlling Interest | | 8,016 | 8,280 |
| **LIABILITIES** | | | |
| **Non-Current Liabilities** | | | |
| Financial Liabilities | | | |
| Borrowings | 15 | 1,97,631 | 2,07,506 |
| Other Financial Liabilities | 16 | 18,804 | 10,020 |
| Deferred Payment Liabilities | 17 | 18,839 | 18,839 |
| Provisions | 18 | 1,790 | 2,856 |
| Deferred Tax Liabilities (Net) | 4 | 54,123 | 49,923 |
| Other Non-Current Liabilities | | 465 | 548 |
| **Total Non-Current Liabilities** | | **2,91,652** | **2,89,692** |
| **Current Liabilities** | | | |
| Financial Liabilities | | | |
| Borrowings | 19 | 93,786 | 64,436 |
| Trade Payables | | 96,799 | 1,08,309 |
| Other Financial Liabilities | 20 | 1,44,778 | 87,051 |
| Other Current Liabilities | 21 | 75,663 | 52,901 |
| Provisions | 22 | 1,890 | 1,326 |
| **Total Current Liabilities** | | **4,12,916** | **3,14,023** |
| Liabilities directly associated with Assets Held for Sale | 39 | - | 3,299 |
| **Total Liabilities** | | **7,04,568** | **6,07,014** |
| **Total Equity and Liabilities** | | **11,65,915** | **10,02,406** |
| Significant Accounting Policies | | | |
| See accompanying Notes to the Financial Statements | 1 to 42 | | |

# Cash Flow Statement

- Cash flow statement is a summary of a company's cash inflows and outflows during a certain period of time.
- All cash flow items are grouped into three categories based on their origins: i. Operating activities, ii. Investment activities, and iii. Financing activities.
- Bankers and analysts are interested in all categories in order to understand if all three heads are in good shape.
- Founders are particularly interested in meeting cash requirements for all the three activities and the overall ending cash balance.

# Reliance Industries Ltd



## Cash Flow Statement

For the year ended 31st March, 2020

(₹ in crore)

| | 2019-20 | 2018-19 |
|---|---|---|
| **A. CASH FLOW FROM OPERATING ACTIVITIES** | | |
| **NET PROFIT BEFORE TAX AS PER STATEMENT OF PROFIT AND LOSS (AFTER EXCEPTIONAL ITEM AND TAX THEREON)** | 53,606 | 55,227 |
| **Adjusted for:** | | |
| Share of (Profit) / Loss of Associates and Joint Ventures | | |
| Loss on Buy back of Debentures | | |
| (Profit) / Loss on Sale / Discard of Property, Plant and Equipment and Other Intangible Ass | | |
| Depreciation / Amortisation and Depletion Expense | | |
| Effect of Exchange Rate Change | | |
| (Profit) / Loss on Divestment of Stake | | |
| Net Gain on Financial Assets# | | |
| Tax on Exceptional Item | | |
| Dividend Income# | | |
| Interest Income# | | |
| Finance Costs# | | |
| **Operating Profit before Working Capital Changes** | | |
| **Adjusted for:** | | |
| Trade and Other Receivables | | |
| Inventories | | |
| Trade and Other Payables | | |
| **Cash Generated from Operations** | | |
| Taxes Paid (Net) | | |
| **Net Cash Flow from Operating Activities*** | | |
| **B. CASH FLOW FROM INVESTING ACTIVITIES** | | |
| Purchase of Property, Plant and Equipment and Other Intangible Assets | | |
| Proceeds from disposal of Property, Plant and Equipment and Other Intangible Assets | | |
| Purchase of Other Investments | | |
| Proceeds from Sale of Financial Assets (including Advance Received) | 11,73,330 | 11,03,615 |
| Upfront Fibre Payment | (16,439) | - |
| Net Cash Flow for Other Financial Assets | 650 | (1,960) |
| Interest Income | 1,477 | 972 |
| Dividend Income from Associates | 18 | 3 |
| Dividend Income from Others | 70 | 498 |
| **Net Cash Flow used in Investing Activities** | **(75,717)** | **(95,128)** |

(₹ in crore)

| | 2019-20 | 2018-19 |
|---|---|---|
| **C. CASH FLOW FROM FINANCING ACTIVITIES** | | |
| Proceeds from Issue of Equity Share Capital | 18 | 117 |
| Proceeds from Issue of Share Capital to Non-Controlling Interest / Compulsory Convertible Debentures | 111 | 113 |
| Share Application Money | 1 | 2 |
| Payment of Lease Liabilities | (1,062) | - |
| Proceeds from Borrowings – Non-Current | 28,665 | 80,299 |
| Repayment of Borrowings – Non-Current | (18,179) | (20,245) |
| Borrowings – Current (Net) | 25,095 | 26,402 |
| Deferred Payment Liabilities | (1,370) | (870) |
| Movement in Deposits | (2,720) | (2,292) |
| Dividend Paid (including Dividend Distribution Tax) | (4,592) | (4,282) |
| Interest Paid | (28,508) | (23,338) |
| **Net Cash Flow (used in) / from Financing Activities** | **(2,541)** | **55,906** |
| **Net Increase in Cash and Cash Equivalents** | **19,816** | **3,124** |
| **Opening Balance of Cash and Cash Equivalents** | 11,081 | 7,336 |
| Add: Upon addition of Subsidiaries | 23 | 621 |
| **Closing Balance of Cash and Cash Equivalents (Refer Note 9)** | **30,920** | **11,081** |

## For additional reading please visit the site of Ministry of Corporate Affair at http://www.mca.gov.in/Ministry/notification/pdf/AS_3.pdf

- **Cash equivalents are short term, highly liquid investments that are readily convertible into known amounts of cash and which are subject to an insignificant risk of changes in value.**
- **For an investment to qualify as a cash equivalent, it must be readily convertible to a known amount of cash and be subject to an insignificant risk of changes in value. Therefore, an investment normally qualifies as a cash equivalent only when it has a short maturity of, say, three months or less from the date of acquisition.**

# Indirect Method: Cash Flow from Operational Activities

Total cash flow from operating activities =

+ Net profit (known as Net Income in USA)

+ Depreciation (This was deducted as expense. But no cash went out)

+ Losses from sale of fixed assets, if any.

— Gains from sale of fixed assets, if any.

(Note that sales value of fixed assets will be included in in cash flow from investment activity)

— Increase in current assets.

+ Decrease in current assets.

+ Increase in current liabilities

— Decrease in current liabilities

# Cash Flow from Investment Activities

+ Capital expenditure
+ Investment

# Cash Flow from Financing Activities

+ Net borrowing.

— Net investment in equity or debt.

— Dividend paid

+ Fresh equity induction.

| | |
|---|---|
| **Cash Flow from Operating Activities** | |
| A. Net profit | 1,13,995 |
| B. Plus Depreciation | 1,150 |
| C. Minus increase in current assets | 20,000 |
| D. Plus increase in current liabilities | 12,000 |
| **E. Cash Flow from Operating Activities** | **1,07,145** |
| | |
| **F. Cash flow from investment activities** | |
| G. Purchase of new fixed assets | 10,000 |
| | |
| **H. Cash flow from Financing activities** | |
| I. Decrease in loan | 2,000 |
| J. Divident payment | 50,000 |
| **K. Net Cash flow** | **45,145** |
| L. Add previous cash balance | 500 |
| **M. Net cash balance as at the end of the** | **45,645** |

= A + B – C + D

You have repaid ₹2,000 to Jack out of his loan of ₹ 4,000 during the year

= E – F – H

= K + L

Estimate Net Profit

Adjust for non-cash gains (add) and losses (subtract)

Estimate net cash inflow and outflow out of changes in current assets and liabilities

Add/subtract the above three to get cash flow from operating activities

Cash flow from Investment activities:

Changes in fixed assets/ investment

Cash flow from financing activities: Changes in long-term liabilities and equity

Add up cash inflows/subtract outflows from three activities

Add the closing cash balance of the previous year (with signs)

**Cash balance as at the end of the year**

## References:


- https://www.caclubindia.comText 1
- http://www.mca.gov.in/MinistryV2/accountingstandards1.html
- Horngren, C. T., Sundem, G. L., Elliott, J. A., & Philbrick, D. R. (2002). *Introduction to financial accounting* (Vol. 8). Prentice Hall.

**Understanding financial statements is easy.**
**Having an understanding of the financial statements is essential for everybody, no matter which profession one is in.**

- **Determination Is The Biggest Predictor Of Long-term Success**

# *Thank you*