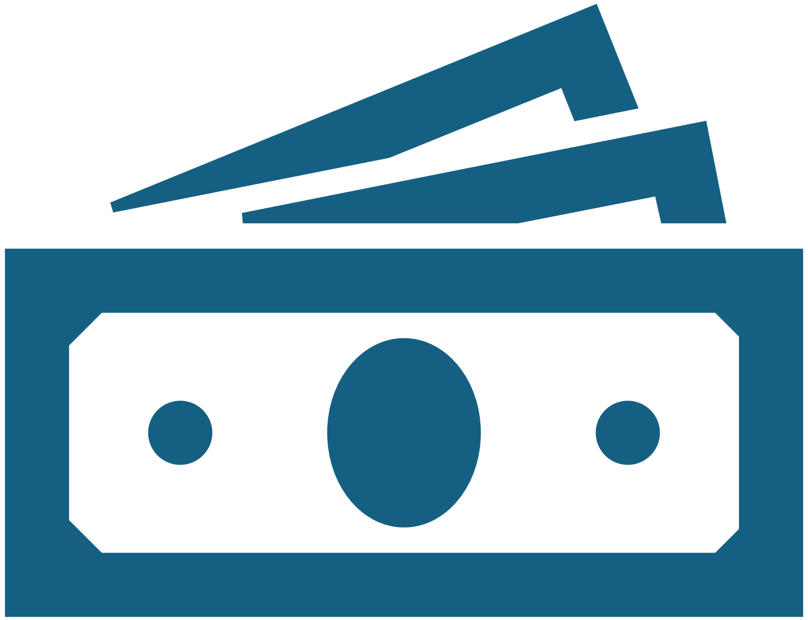


Introduction to Finance

L3

Financial statements

- Balance sheet
- Profit and Loss statement (or account)
- Cash Flow statement

Financial Statements

- Financial statements are reports compiled by the business/firm that explains/ provide overview of the financial performance of the company.
- Financial statements provide governments, investors, executives, and lenders with a picture of a company's financial activities and profitability.
- Statements required by Generally Accepted Accounting Principles (GAAP) are the balance sheet, the income statement, and the statement of cash flows.
- The balance sheet provides an overview of assets, liabilities, and shareholders' equity as a snapshot in time.
- The income statement reports a company's revenues and expenses, including a company's profit figure called net income.
- The cash flow statement (CFS) tracks how a company uses its cash to pay its debt obligations and fund its operating expenses and investments.

Balance Sheet

A balance sheet is a two-sided financial statement. **The left side** records an organizations **assets**, while the **right side** depicts **shareholder's equity and** business **liabilities**

BS provides a **summary of** company's **financial standing in** a specific **accounting period.**

It shows the capital in a business, what all assets business owns, and what are the liabilities(owes to others) of the business

Lenders and investors use the balance sheet to make an informed decision before financing a business

Balance sheet

Assets

- An asset is any resource an organization owns and can use to produce value. Business can use an asset to provide services or make products that generate income. Alternatively, a business can sell assets to get revenue.
  - ✓ Accounts receivable
  - ✓ Real estate, buildings, plants
  - ✓ Inventory/stock
  - ✓ Other investments
  - ✓ Machineries and Equipments
  - ✓ Vehicles
  - ✓ Trademarks and patents
  - ✓ Cash, Bank account deposits

Liabilities and SHs Equity Capital

- Liabilities: The amount business owes to others. These are the debts of the firm/company
  - ✓ Outstanding rent
  - ✓ Accounts payable (unpaid loans, debt to suppliers etc.)
  - ✓ Unpaid salaries
  - ✓ Payable tax
- Shareholder's Equity (or Capital) :
  - It is the difference between asset and liabilities of the company. It is the balance of assets left over after a business pays off all its liabilities.
  - It is the money that would go to the owners of SHs should the business **liquidate.**
  - SHs equity is also called **share capital**

- **Balance Sheet**

GLOBAL CONGLOMERATE CORPORATION

Consolidated Balance Sheet
Year Ended December 31 (in $ million)

Assets	2022	2021	Liabilities and Stockholders' Equity	2022	2021
Current Assets			**Current Liabilities**		
Cash	21.2	19.5	Accounts payable	29.2	24.5
Accounts receivable	18.5	13.2	Notes payable/short-term debt	3.5	3.2
Inventories	15.3	14.3	Current maturities of long-term debt	13.3	12.3
Other current assets	2.0	1.0	Other current liabilities	2.0	4.0
Total current assets	57.0	48.0	Total current liabilities	48.0	44.0
Long-Term Assets			**Long-Term Liabilities**		
Land	22.2	20.7	Long-term debt	99.9	76.3
Buildings	36.5	30.5	Lease obligations	—	—
Equipment	39.7	33.2	Total debt	99.9	76.3
Less accumulated depreciation	(18.7)	(17.5)	Deferred taxes	7.6	7.4
Net property, plant, and equipment	79.7	66.9	Other long-term liabilities	—	—
Goodwill and intangible assets	20.0	20.0	Total long-term liabilities	107.5	83.7
Other long-term assets	21.0	14.0	**Total Liabilities**	**155.5**	**127.7**
Total long-term assets	120.7	100.9	**Stockholders' Equity**	**22.2**	**21.2**
Total Assets	**177.7**	**148.9**	**Total Liabilities and Stockholders' Equity**	**177.7**	**148.9**

Balance sheet

The Equity (Shareholders'/stockholders' Equity) is the difference between the firm's assets and liabilities, is an accounting measure of the firm's net worth.

The assets on the left side show how the firm uses its capital (its investments), and the right side summarizes the sources of capital, or how a firm raises the money it needs.

Because of the way stockholders' equity is calculated, the left and right sides must balance

The Balance Sheet Identity : $Assets = Liability + capital$

i.e. $Assets = Liabilities + Stockholders'\ Equity$

Assets

- Assets are generally divided into current assets and long-term (or non-current) assets.
- **Current Assets** are either cash or assets that are most liquid

(liquid asset are those assets that could be converted into cash within a short period. Liquidity of an asset is measured by how fast it can be converted into cash).

- Some of the categories in Current Account (CA) are as follows:
  - ✓ Cash, bank a/c deposits
  - ✓ Marketable securities (short-term , low-risk investments such as govt. bonds, or other money-market instruments)
  - ✓ Accounts receivables: Amount owed to the firm by customers who have purchased goods and services on credit
  - ✓ Inventories: Raw-materials, work-in-progress and finished goods stock
  - ✓ Pre-paid expenses

Assets

- **Long-term assets or non-current assets:**
  - ✓ This includes tangible assets that generate value/ produce benefits for the business for more than one year
  - ✓ Eg: Property, Plants & Machineries, Equipment, Building
  - ✓ **Depreciation**: Equipment and Machines tend to wear out or become less valuable or obsolete over time. Hence firms will reduce the value recorded for these items each year by deducting **depreciation expense.**

    Thus, the **firm reduces the value of fixed assets** (other than land) **over time** according to a depreciation schedule that depends on the asset's life span.

    Depreciation is not an actual cash expense that the firm incurs, rather it is a way of recognizing that some long –term (or fixed) assets wear out and thus becomes less valuable over time

Assets

- Long-term assets or non-current assets:
  - ✓ **Goodwill and Intangible assets**: Brand names, trademarks, patents, customer relations and relationship with employees etc.
  - ✓ Like depreciation if a firm accounts (considers/assess) that value of these intangible assets declined over time, it will reduce the amount listed on the balance sheet by an **amortization or impairment charge**. This charge captures the change in value of the acquired intangible assets. Like depreciation amortization in not an actual cash expense. The amortization is relevant when acquisition or mergers occur.

Liabilities

- Liabilities: Divided into current and non-current (or long-term) liabilities
- **Current Liabilities** :
  - Liabilities that should be obliged/satisfied within one year are known as current liabilities (CL).
  - Some items of CL are as follows:
    1. Accounts (a/c) payable : the amounts owed to suppliers for credit purchase of goods/services
    2. Short-term debt: Exchange notes payable, current maturities of ling-term debt which are all repayments of debt that will occur within the next 1 year
    3. Unpaid – salaries and –taxes
    4. Deferred revenue: revenue received for products (Goods or services) not yet delivered
    5. Dividends payable : Dividends that have been declared to be awarded to shareholders but have not been yet paid
    6. Accrued expenses: These are expenses yet to be paid, but have a high probability of being paid

Long-Term Liabilities

- Long-term Liabilities or non-current liabilities are liabilities that extend beyond one year. Following are such items:
  - **Long-term debt**: Any loan, mortgages, bond funds or debt obligation with maturity of more than 1 year.
  - **Leases** are long-term contracts that obligate the firm to make regular lease payments in exchange for use of an asset

Shareholder’s Equity

- Total Liability = Current Liability + Non-current Liability
- Total Asset= Current Assets + Non-current assets
- **Shareholder’s (SHs) Equity/Stockholders Equity/ Book value of Equity/ SHs Equity capital**

  = Total Assets-Total Liabilities

SHs Equity is a company’s total assets minus its total liabilities. It represents the amount of money that would be returned to SHs (or left over for SHs) if all the assets are liquidated, and all debts are paid off. It is an accounting measure of the net worth of the firm

- **Retained Earnings (REs):** REs are part of SHs Equity capital. This the amount of net earnings that were not paid to SHs as dividends

Balance Sheet (BS)

- A BS thus consist of all the assets and liabilities of the company. It shows the **value and nature of these items** which helps in assessing the **financial position** of the firm .
- However, **BS does not show any revenues or expenses**.
- Balance Sheet follows Asset= Liability + capital ;and both of its sides are always equal
- **Net working capital (NWC)**= Current asset – current liabilities
- NWC indicates the capital available in the short term to run the business
- Firms with low (or negative) NWC may face shortage of funds unless they generate sufficient cash from ongoing activities

Market Value v/s Book value

Ideally, the balance sheet would provide us with an accurate assessment of the true value of the firm's equity. Unfortunately, this is unlikely to be the case.

First, many of the assets listed on the balance sheet are valued based on their historical cost rather than their true value today. The true value today of an asset may be very different from, and even exceed, its book value.

Second, and probably more important, problem is that *many of the firm's valuable assets are not captured on the balance sheet*.

Market Value v/s Book value

- or example, the expertise of the firm's employees, the firm's reputation in the marketplace, the relationships with customers and suppliers, the value of future research and development innovations, and the quality of the management team. These are all assets that add to the value of the firm that do not appear on the balance sheet.
- Hence, the book value of equity, while accurate from an accounting perspective, is an inaccurate assessment of the true value of the firm's equity.
- Successful firms are often able to borrow in excess of the book value of their assets because creditors recognize that the market value of the assets is far higher than the book value. Thus, it is not surprising that the book value of equity will often differ substantially from the amount investors are willing to pay for the equity.

Market Value v/s Book value

The total *market* value of a firm's equity equals the number of shares outstanding times the firm's market price per share:

$$\textit{Market Value of Equity} = \textit{Shares outstanding} * \textit{Market price per share}$$

Market value of equity is also known as market capitalization or market cap

The market value of a stock does not depend on the historical cost of the firm's assets; instead, it depends on what investors expect those assets to produce in the future.

$$\textit{Book value} = \textit{Assets} - \textit{Liability} = \textit{Book value of equity}$$

$$\textit{Book value per share} = \frac{\textit{Book value}}{\textit{no. of outstanding shares}}$$

Price to book ratio (P/B ratio)

P/B ratio is also known as the Market to Book ratio

$$P/B = \frac{Market\ value\ of\ equity}{Book\ value\ of\ equity}$$

- Market value of equity: Perception of market regarding the companies net worth
- PB ratio implies how many times of BV is the MV
- It signals whether the stock is overpriced or underpriced
- The market-to-book ratio for most successful firms substantially exceeds 1, indicating that the value of the firm's assets when put to use exceeds their historical cost.
- Variations in this ratio reflect differences in fundamental firm characteristics as well as the value added by management.
- Analysts often classify firms with low market-to-book ratios as **value stocks**, and those with high market-to-book ratios as **growth stocks**.

BALANCE SHEET
As at 31st March, 2023

(₹ in crore)

	Notes	As at 31st March 2023	As at 31st March 2022
Assets			
Non-Current Assets			
Property, Plant and Equipment	1	2,32,238	2,23,824
Intangible Assets	1	12,926	15,802
Capital Work-in-Progress	1	30,958	19,267
Intangible Assets Under Development	1	17,957	15,395
Financial Assets			
Investments	2	3,03,558	3,30,493
Loans	3	22,448	41,951
Other Financial Assets	4	2,215	2,247
Other Non-Current Assets	5	2,333	7,297
Total Non-Current Assets		**6,24,633**	**6,56,276**
Current Assets			
Inventories	6	48,926	45,923
Financial Assets			
Investments	7	86,074	78,304
Trade Receivables	8	16,898	14,394
Cash and Cash Equivalents	9	56,811	21,714
Loans	10	595	161
Other Financial Assets	11	49,408	54,901
Other Current Assets	13	7,220	7,001
Total Current Assets		**2,65,932**	**2,22,398**
Total Assets		**8,90,565**	**8,78,674**

(₹ in crore)

	Notes	As at 31st March 2023	As at 31st March 2022
Equity and Liabilities			
Equity			
Equity Share capital	14	6,766	6,765
Other Equity	15	4,72,328	4,64,762
Total Equity		**4,79,094**	**4,71,527**
Liabilities			
Non-Current Liabilities			
Financial Liabilities			
Borrowings	16	1,35,561	1,67,231
Lease Liabilities		2,786	2,790
Other Financial Liabilities	17	584	3,210
Provisions	18	1,296	1,598
Deferred Tax Liabilities (Net)	19	33,968	30,832
Other Non-Current Liabilities	20	-	504
Total Non-Current Liabilities		**1,74,195**	**2,06,165**
Current Liabilities			
Financial Liabilities			
Borrowings	21	80,262	27,332
Lease Liabilities		97	86
Trade Payables Due to:	22		
Micro and Small Enterprises		210	138
Other than Micro and Small Enterprises		1,10,512	1,33,867
Other Financial Liabilities	23	25,611	33,225
Other Current Liabilities	24	19,659	5,438
Provisions	25	925	896
Total Current Liabilities		**2,37,276**	**2,00,982**
Total Liabilities		**4,11,471**	**4,07,147**
Total Equity and Liabilities		**8,90,565**	**8,78,674**
Significant Accounting Policies	A-D		

P/B ratio

- Book Value= 479094 cr
- Book value per share=1058
- Price per share: 1283
- P/B ratio= ?
- No.of Outstanding shares=?
- Market Cap=?

P/B ratio

Book Value= 479094 cr

Book value per share=1058

Price per share: 1283

P/B ratio= 1.21

Number of O/S shares=452 cr

Market cap: 579916 cr

EXAMPLE : Reliance Industries Limited (RIL)

The first Indian company to cross

₹20,00,000 Crore

In market capitalisation; becomes world's 48th most valuable company

rt 2023-24

Reliance
Industries Limited
Growth is Life

Valuation Metric

BOOK VALUE PER SHARE

(₹) ↑ 10.9%

₹1,173

FY 2023-24	1,173
FY 2022-23	1,058
FY 2021-22	1,152

Book value per share increased year on year due to increase in reserves and surplus.

MARKET CAPITALISATION

(₹ crore) ↑ 27.7%

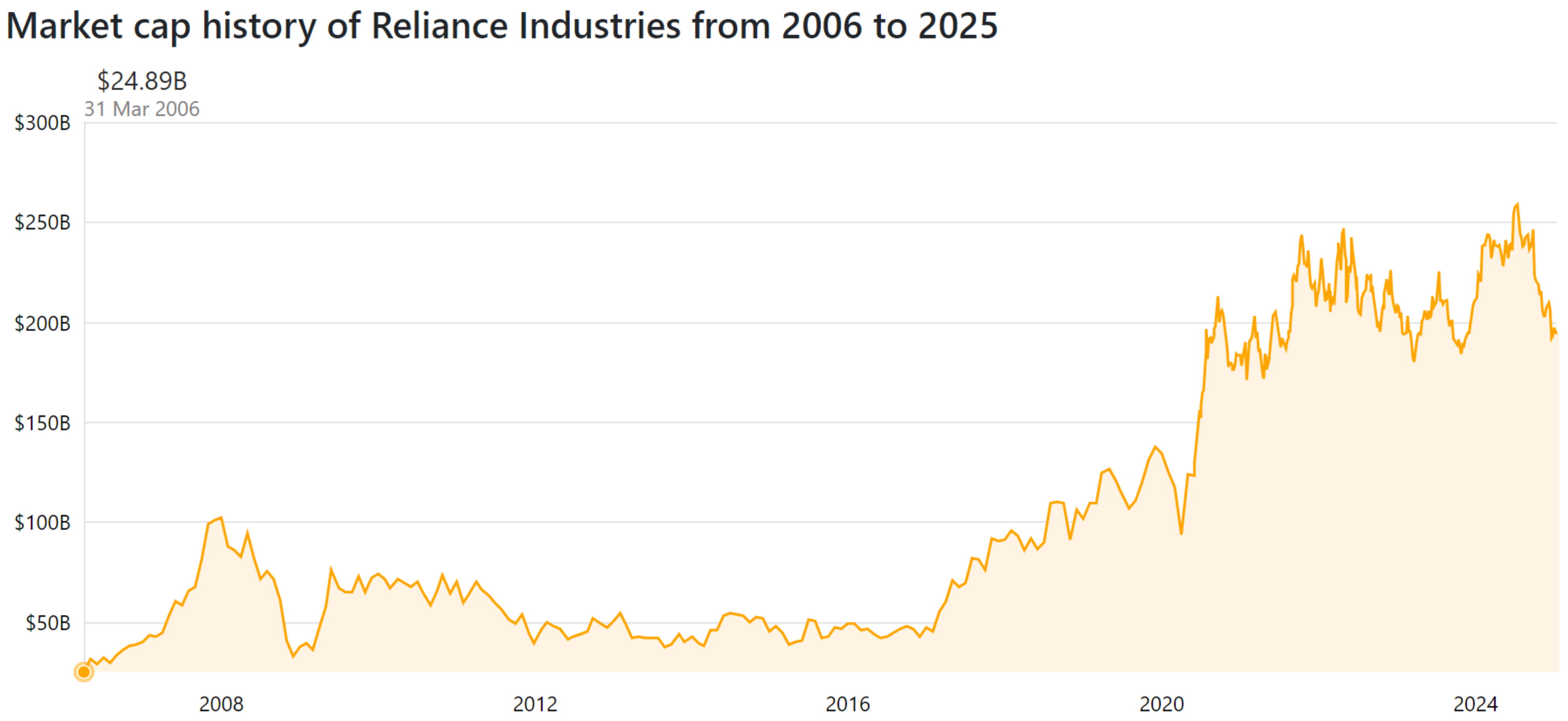
₹20,14,011 Crore

US$ 241.5 Billion

FY 2023-24	20,14,011
FY 2022-23	15,77,093
FY 2021-22	17,81,841

RIL becomes the first Indian listed company to cross the ₹ 20,00,000 crore milestone.

Market-cap trends Reliance Industries



P/B ratio RIL

Reliance Industries (RELIANCE.NS) - P/B ratio

P/B ratio as of January 2025 : 1.70

According to **Reliance Industries**'s latest financial reports the company has a price-to-book ratio of **1.74757**.
The price-to-book ratio is a way to measure how much the stock market thinks a company is worth compared to how much the company says its assets are worth on paper.

P/B ratio by year

Year	P/B ratio
2024-12-31	1.70
2023-12-31	1.99
2022-12-31	1.88