FINANCIAL STATEMENTS GLOSSARY: BALANCE SHEET, INCOME STATEMENT & KEY RATIOS

Meridian Capital Research | Reference Document

SYNTHETIC DOCUMENT — FOR DEMONSTRATION PURPOSES

INTRODUCTION

This glossary defines the key terms, line items, and ratios encountered in corporate financial statements, with particular emphasis on terms relevant to technology company analysis. It is intended for investors, analysts, and advisors who work with financial data but may not have a formal accounting background.

Terms are organized by financial statement, followed by derived ratios and advanced concepts.

PART 1: BALANCE SHEET TERMS

The balance sheet (also called the Statement of Financial Position) is a snapshot of what a company owns (assets), owes (liabilities), and the residual value belonging to shareholders (equity) at a specific point in time. The fundamental equation: Assets = Liabilities + Shareholders' Equity.

ASSETS

Cash and Cash Equivalents

Liquid assets including physical currency, bank deposits, and short-term instruments with maturities of 90 days or less (e.g., Treasury bills, money market funds). Apple held $29.9 billion in cash and equivalents at end of FY2023. High cash balances provide operational flexibility but may indicate management's inability to deploy capital productively if sustained over time.

Short-Term Investments

Marketable securities with maturities between 90 days and one year. Along with cash equivalents, these form a company's "liquidity reserve." Apple's combined cash, equivalents, and investments totaled approximately $162 billion at FY2023 year-end.

Accounts Receivable

Money owed to the company by customers for goods or services already delivered but not yet paid. Days Sales Outstanding (DSO) measures how long it takes to collect: DSO = (Accounts Receivable / Revenue) × 365. Rising DSO may indicate customer financial stress or aggressive revenue recognition.

Inventory

Goods held for sale or materials used in production. For technology hardware companies like Apple, inventory management is critical. Excess inventory (as seen in the PC industry in 2022) requires write-downs that reduce gross margins. Inventory Turnover = Cost of Goods Sold / Average Inventory; higher is generally better.

Property, Plant & Equipment (PP&E), Net

Physical long-term assets (buildings, machinery, servers, data centers) after accumulated depreciation. Capital-intensive businesses like cloud providers carry large PP&E balances. Microsoft's PP&E net was $87.9 billion at FY2023 year-end, reflecting its extensive data center infrastructure.

Goodwill

The premium paid above the fair value of net assets when acquiring another company. Goodwill is not amortized under US GAAP but must be tested annually for impairment. A goodwill impairment charge occurs when the acquired business performs below expectations and signals that the acquisition premium was not justified. Microsoft carried $67.9 billion in goodwill following the Activision Blizzard acquisition.

Intangible Assets

Non-physical assets with identifiable value: patents, trademarks, customer relationships, developed technology, and software. Acquired intangibles are amortized over their useful lives; internally developed intangibles are generally expensed as incurred under US GAAP (creating a structural understatement of asset value for R&D-intensive companies).

Deferred Tax Assets

Future tax benefits arising from temporary differences between book and tax accounting. A large deferred tax asset indicates that a company has paid more in taxes than its book income would require, creating a future benefit. Realizability depends on having sufficient future taxable income.

LIABILITIES

Accounts Payable

Money owed by the company to its suppliers for goods or services received but not yet paid. Days Payable Outstanding (DPO) = (Accounts Payable / Cost of Goods Sold) × 365. Apple's DPO is exceptionally high (~80–90 days), reflecting its bargaining power over suppliers — effectively using supplier credit as a source of free financing.

Deferred Revenue

Cash received from customers before the company has delivered the corresponding goods or services. Particularly important for subscription businesses. Microsoft's deferred revenue was $50.9 billion at FY2023 year-end, representing committed future revenue that will be recognized as services are delivered.

Long-Term Debt

Borrowings due beyond one year. Includes bonds, term loans, and other debt instruments. Despite holding over $160 billion in cash, Apple carries approximately $105 billion in long-term debt — a deliberate capital structure decision to take advantage of low-cost debt financing while preserving overseas cash (historically, repatriation of foreign cash triggered US tax obligations).

Operating Lease Liabilities

The present value of future lease obligations for office space, retail stores, data centers, and equipment under ASC 842 (effective 2019). Technology companies with large real estate footprints (Apple's retail stores, Microsoft's offices) carry significant lease liabilities.

SHAREHOLDERS' EQUITY

Retained Earnings

Cumulative net income since inception, less cumulative dividends paid. Negative retained earnings (an accumulated deficit) typically indicate a company that has historically lost money or returned more than it has earned. Many mature technology companies have reduced retained earnings through aggressive share buybacks.

Share Repurchase / Treasury Stock

Companies that buy back their own shares reduce the share count, increasing earnings per share for remaining shareholders. Apple spent $77.6 billion on share repurchases in FY2023 — one of the largest buyback programs of any company in history. Treasury stock is recorded as a contra-equity item, reducing total shareholders' equity.

PART 2: INCOME STATEMENT TERMS

Revenue (Net Sales)

The top line: total value of goods sold or services rendered during the period, net of returns, allowances, and discounts. Technology companies frequently disaggregate revenue by product/service line and geography.

Cost of Revenue (Cost of Goods Sold — COGS)

Direct costs attributable to producing goods or delivering services: manufacturing costs, component costs, data center operating costs, content acquisition costs. For software companies, COGS is primarily hosting and support costs.

Gross Profit / Gross Margin

Gross Profit = Revenue − Cost of Revenue. Gross Margin = Gross Profit / Revenue. Software and services businesses typically achieve gross margins of 60–80%; hardware businesses 30–50%. Apple's blended gross margin of 44.1% in FY2023 reflects its increasingly services-heavy mix.

Operating Expenses

Costs not directly tied to production: Research & Development (R&D), Sales & Marketing (S&M), General & Administrative (G&A). Technology companies characteristically invest heavily in R&D; Google parent Alphabet spent $39.5 billion on R&D in 2023, approximately 13% of revenue.

EBITDA

Earnings Before Interest, Taxes, Depreciation, and Amortization. A proxy for operating cash flow, used in valuation multiples (EV/EBITDA) and debt covenant testing. EBITDA adds back non-cash charges (depreciation, amortization) and financing costs to net income, allowing comparison across companies with different capital structures and tax situations.

EBIT (Operating Income)

Earnings Before Interest and Taxes. Revenue minus all operating expenses including depreciation and amortization. Represents the profit generated purely from operations, before financing and tax decisions.

Net Income

The bottom line after all expenses, interest, and taxes. Includes non-operating items (investment gains/losses, foreign exchange gains/losses) and is subject to tax planning decisions. Less useful than operating income for comparing core business performance.

Earnings Per Share (EPS)

Net Income / Weighted Average Diluted Shares Outstanding. Diluted EPS includes the hypothetical effect of all outstanding stock options and unvested RSUs being exercised, which increases the share count and reduces EPS. Always use diluted EPS for comparability.

PART 3: KEY RATIOS AND VALUATION METRICS

Price-to-Earnings (P/E) Ratio

Market Price per Share / Earnings per Share. The most widely cited valuation multiple. Forward P/E uses next twelve months (NTM) estimated earnings. A P/E of 30x means investors are paying $30 for every $1 of annual earnings — implying confidence in significant future growth or a low required rate of return.

Price-to-Sales (P/S) Ratio

Market Capitalization / Annual Revenue. Used when earnings are negative or highly variable. Particularly common for early-stage SaaS companies. A P/S of 10x was typical for high-growth SaaS in 2021; by 2023, median P/S for software companies had compressed to approximately 5–6x.

Enterprise Value (EV)

Market Capitalization + Total Debt − Cash and Equivalents. Represents the theoretical takeover price of a business. Used in EV/EBITDA and EV/Revenue multiples because it is capital-structure neutral — it doesn't matter whether a company is financed by debt or equity.

Return on Equity (ROE)

Net Income / Average Shareholders' Equity. Measures how effectively management generates profit from shareholders' capital. Apple's ROE appears extremely high (sometimes negative) because its aggressive buyback program has reduced book equity close to zero or below — illustrating that ROE must be interpreted carefully.

Free Cash Flow (FCF)

Operating Cash Flow − Capital Expenditures. The cash a business generates after maintaining and expanding its asset base. FCF is considered a purer measure of economic value creation than net income. Apple generated $99.6 billion in free cash flow in FY2023.

Net Debt / EBITDA

A leverage ratio used in credit analysis and debt covenant structures. Net Debt = Total Debt − Cash. A ratio below 2.0x is generally considered conservative; above 4.0x is considered aggressive for non-financial companies. Investment-grade technology companies typically maintain net debt/EBITDA below 2.0x.

PART 4: ADVANCED CONCEPTS

Debt Covenants

Contractual restrictions embedded in loan agreements and bond indentures that borrowers must comply with to avoid technical default. Common financial covenants include maximum leverage ratios (Net Debt/EBITDA), minimum interest coverage ratios (EBIT/Interest Expense), and minimum liquidity requirements. Breach of a covenant — even without missing a payment — can trigger lender rights including accelerating repayment. In leveraged buyout (LBO) transactions, covenant headroom is monitored closely because private equity-backed companies often operate with high leverage.

Goodwill Impairment

When a company's acquisition proves less valuable than expected, it must write down the goodwill on its balance sheet. The impairment test compares the "carrying value" of a reporting unit (book value including goodwill) to its "fair value" (estimated market value). If carrying value exceeds fair value, goodwill is impaired by the difference. Impairment charges flow through the income statement, reducing net income — but they are non-cash and typically added back in EBITDA calculations.

Working Capital

Current Assets – Current Liabilities. Represents the short-term operational liquidity of a business. Negative working capital (a situation where current liabilities exceed current assets) is common in retail and consumer technology — companies like Apple can operate with negative working capital because they collect cash from customers before paying suppliers.

END OF GLOSSARY