

UNIT 1

Nature and Scope of Financial Management

FINANCIAL MANAGEMENT

FINANCIAL MANAGEMENT = FINANCIAL + MANAGEMENT

FINANCIAL ; it mean money required for the Business, and **MANAGEMENT** mean to manage the money for the business (when the money is required, how much money in required, for how many terms money is required)

On the other hand Financial Management means the whole efforts of management towards the managing of finance- both its sources and uses of the firm. Thus FM is concerned with proper management of funds. The financial manager must strike a proper balance between the cost and risk, while raising funds and utilisation of funds.

Soloman, said FM is concerned with efficient use of an important resource, namely capital funds. FM is concerned with managerial decision that deals in acquisition and financing of long term and short term credits for the firm.

OBJECTIVES OF FINANCIAL MANAGEMENT:

1. Financial Management help to maintain liquid assets and maximisation of profits. All business firms seek profit and it was considered to be sole criteria to test the efficiency of a business.
2. Financial Management ignores time value of money.
3. It overlooks quality aspects of future activities: emphasize on growth of sales to gain stability provided by higher sales volume.
4. following are the other objectives of FM:
 - a) Ensuring a fair return to share holders.
 - b) Building reserves and surplus for growth and expansion.
 - c) Ensuring maximum operational efficiency by efficient and effective utilisation of finances.
 - d) Ensuring financial discipline in the organisation.
 - e) wealth maximisation is considered to be the main objective of FM.



RELATIONSHIP OF FINANCE WITH THE OTHER

1. FINANCE AND ECONOMICS

Finance is correlated with the Economic as because both are the branch of Mathematic. Microeconomics deals with the economic decisions of individuals and organizations. Financial Management deals with effective operations of a firm. The concepts and theories of microeconomics relevant to Financial Management are

- a). supply and demand relationships,
- b). profit maximisation strategies,
- c). product mix, optimal sales level and
- d). product pricing strategies, risk and value and rationale for depreciating assets.

FINANCE AND ACCOUNTING

Finance is incomplete without Accounting as these are closely related to each other and accounting information is an important input for financial management to take the financial decisions. There are key differences between Accounting and Finance that Accounting is a sub function of finance. Accounting end results i.e. financial statements provide the help for assessing the past performance and indication for future directions to the firm and comply with the legal obligations such as taxes. The two key differences between finance and accounting relates to the treatment of funds and the second relate to the decision making.

The Treatment of Funds in accounting is based on accrual method, whereas in finance view it is base on cash flows.

Decision making: Accounting process is meant for collection and presentation of financial data. The financial manager uses such data for financial decision making. It does not mean that financial manager never collects data and accountant never make decisions. But the primary focus of accountant is to collect and presentation while Financial manager's responsibility to financial planning, controlling and decision making. Thus, in a sense finance begins where accounting ends.

FUNDS FLOW ANALYSIS

Fund flow is the net of all cash inflows and outflows in and out of various financial assets. It is usually measured on a monthly or quarterly basis; the performance of an asset or fund is not taken into account, only share redemptions, or outflows, and share purchases, or inflows. Net inflows create excess cash for managers to invest, which theoretically creates demand for securities such as stocks and bonds.

Generally speaking, the Fund Flow analysis requires the preparation of two statements:-

Statement of Changes in Working Capital

Fund Flow Statement.

Statement of Changes in Working Capital :

The working capital does change due to various transactions. The working capital position at the beginning of a period is changed to a different position at the end of that period. A Statement of working capital is prepared to depict the changes in working capital. Working capital represents the excess of Current Assets over Current Liabilities.

The Statement shows the changes in individual items of current assets and current liabilities and their effect of working capital. The total increase and the total decrease in the end is compared and the difference of total increase and total decrease shows the net increase or net decrease in the working capital.

Steps:

Current Asset of the current year is compared with its amount of previous year.



If the amount of current asset of the current year is less than its amount of the previous year, the deficiency is recorded in credit column.



Make sure that all the accounts relating to current assets appearing in the two Balance Sheets are gone through and differences are properly recorded.



Current liability of current year is more than its amount of previous year, the excess is recorded in the credit column



Current liability of current year is less than its amount of previous year, the deficiency is recorded in debit column.



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Find out totals of all debit amounts and all credit amounts.



Difference shows decrease or increase in the Working Capital.

Fund Flow Statement:

The study and control of this funds flow process is the main objective of Financial Management to assess the soundness and solvency of a business., financing and investing activities over the related period. Like the Balance Sheet, even the Profit and Loss Account does not depict the changes that have taken place in financial condition of a business concern between two dates. Hence there is a need to prepare an additional statement to know the changes in assets, liabilities and owners' equity between dates of two Balance Sheets. Such a statement is called Funds Flow Statement or Statement of Sources and Uses of funds or where come and where gone statement.

According to **Anthony:** Funds Flow Statement describes the sources from which additional funds were derived and the use to which these sources were put.

This is second but most important part of Fund Flow Statement. After preparing the Statement of Working Capital, the Statement of Sources and Application of Fund is prepared. This Statement is prepared with the help of remaining items in the Balance Sheet of the two periods all non-current assets and non-current liabilities and other information given in the problem.

Sources of Funds:

- (i) Issue of share capital.
- (ii) Funds from business operations
- (iii) Issue of debentures of long term loans.
- (iv) Sale of fixed assets or long term investments.
- (v) Non-trading income.
- (vi) Decrease in working capital.
- (vii) Any other increase in liability and decrease in asset.

Illustration 01:

From the following Balance Sheet of PKJ Ltd., Prepare Funds Flow Statement for 2016.

₹ '000

Liabilities	31-3-15	31-3-16	Assets	31-3-15	31-3-16
Equity Share Capital	150	200	Goodwill	50	40
9% Redeemable Preference Share capital	75	50	Land & Buildings	100	85
Capital Reserve	—	10	Plant & Machinery	40	100
General Reserve	20	25	Investments	10	15
Profit & Loss Account	15	24	Sundry Debtors	70	85
Proposed Dividend	21	25	Stock	39	55
Sundry Creditors	13	24	Bills Receivable	10	15
Bills Payable	10	8	Cash in hand	7	5
Liability for Expenses	15	18	Cash at bank	5	4
Provision for tax	20	25	Preliminary Exp.	8	5
	339	409		339	409

Additional information:

1. A part of land was sold out in 2016, and the profit was credited to Capital Reserve.
2. A machine has been sold for ₹5,000 (written down value of the machinery was ₹6,000). Depreciation of ₹5,000 was charged on plant in 2016.
3. An interim dividend of ₹10,000 has been paid in 2016.
4. An Amount of ₹1,000 has been received as dividend on investment in 2016.

Illustration 02:

The Balance Sheets of A, B, & C Co. Ltd. as at the end of 2015 and 2016 are given below:

LIABILITIES	2015 (₹)	2016 (₹)	ASSETS	2015 (₹)	2016 (₹)
Share Capital	1,00,000	1,50,000	Freehold land	1,00,000	1,00,000
Share premium	---	5,000	Plant at cost	1,04,000	1,00,000
General Reserve	50,000	60,000	Furniture at cost	7,000	9,000
Profit & Loss Account	10,000	17,000	Investments	60,000	80,000
6% Debentures	70,000	50,000	Debtors	30,000	70,000
Provision for Depreciation on Plant	50,000	56,000	Stock	60,000	65,000
Provision for Dep. on Furniture	5,000	6,000	Cash	30,000	45,000
Provision for taxation	20,000	30,000			
Sundry Creditors	86,000	95,000			
	3,91,000	4,69,000		3,91,000	4,69,000

A plant purchased for ₹ 4,000 (Depreciation ₹ 2,000) was sold for Cash for ₹ 800 on September 30, 2015. On June 30, 2015 an item of furniture was purchased for ₹ 2,000. These were the only transactions concerning fixed assets during 2015. A dividend of 22½ % on original shares was paid. You are required to prepare funds Flow Statement and verify the results by preparing a schedule of changes in Working Capital.



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Illustration : 03

From the Balance Sheet of A Ltd., Please prepare:

- A. A Statement of changes in the Working Capital.
- B. Funds Flow Statement.

BALANCE SHEET

LIABILITIES	31st March		ASSETS	31st March	
	2015 (₹)	2016 (₹)		2015 (₹)	2016 (₹)
Equity Share Capital:	3,00,000	4,00,000	Goodwill	1,15,000	90,000
8% Preference share capital	1,50,000	1,00,000	Land & Buildings	2,00,000	1,70,000
P & L A/c	30,000	48,000	Plant	80,000	2,00,000
General Reserve	40,000	70,000	Debtors	1,60,000	2,00,000
Proposed Dividend	42,000	50,000	Stock	77,000	1,09,000
Creditors	55,000	83,000	Bills Receivable	20,000	30,000
Bills Payable	20,000	16,000	Cash in hand	15,000	10,000
Provision for Taxation	40,000	50,000	Cash at Bank	10,000	8,000
	6,77,000	8,17,000		6,77,000	8,17,000

Following is the additional information available:

- (i) Depreciation of ₹ 10,000 and ₹ 20,000 have been charged on Plant and Land and Buildings respectively in 2016.
- (ii) Interim dividend of ₹ 20,000 has been paid in 2016.
- (iii) Income tax of ₹ 35,000 has been paid in 2016.

CASH FLOW STATEMENT

A *cash flow statement* presents information about the cash flows associated with the company's main operations and those associated with its investing and financing activities of the period.

Benifits-

- To assess the ability of a firm to manage cash flows
- To assess the ability of a firm to generate cash through its operations
- To assess the company's ability to meet its obligations and its dividend policy
- To provide information about the effectiveness of the firm to convert its revenues to cash
- To provide information to estimate or anticipate the company's need for additional financing.

Basic cash flow activities-

(1)Operating cash flows – cash flows related to selling goods and services; that is, the principle business of the firm.

Examples-

- Receipts from sale of goods and rendering of services (cashing in of receivables included)
- Receipts from taxes on sales and VAT
- Receipts from royalties, fees, commissions,...
- Payments to suppliers (payment of creditors included)
- Payments to employees
- Payments of taxes, VAT, fines,

(2)Cash flow from investing activities- Investing activities relate to the acquisition and disposal of fixed assets and other investments.

Cash flows from investing activities are an indication of the expansion or downsizing of operating capacity.

Examples:

- Payments for newly acquired equipment
- Receipts from the disposal of a building
- Payments for new investments

(3)Cash flow from financing activities- Financing activities relate to changes in the size and composition of contributed capital and financial debt of the company

Examples:

- Receipts from issuing new shares or bonds
- Receipts from new bank loan



- Payments for buy-back of shares
- Repayments of loans
- Payments of interest and dividend.

Differences between Funds Flow Statement and Cash Flow Statement

The following are the main differences between a Funds Flow Statement and a Cash Flow Statement:-

Funds Flow Statement	Cash Flow Statement
1. Funds Flow Statement reveals the change in working capital between two Balance Sheet dates	Cash Flow Statement reveals the changes in cash position between two balance sheet dates.
2. Funds Flow Statement is based on accounting	Cash Flow Statement is based on cash basis of accounting
3. In the case of Funds Flow Statement a schedule of changes in working capital is prepared.	No such schedule of changes in working capital is prepared for a Cash Flow Statement.
4. Funds Flow Statement is useful in planning, Intermediate and long term financing.	Cash Flow Statement as a tool of financial analysis is more useful for short-term analysis and cash planning.
5. Funds Flow Statement deals with all components of working capital.	Cash Flow Statement deals only with cash and cash equivalents.
6. Funds Flow Statement reveals the sources and application of funds. The difference represents net increase or decrease in working capital.	Cash Flow Statement is prepared by taking into consideration the inflows and outflows in terms of operating, investing and financing activities. The net difference represents the net increase or decrease in cash and cash equivalents.

Financial statement Analysis, Ratio Analysis, Common Size Statement, Du Point Analysis

FINANCIAL STATEMENT ANALYSIS

Financial statement analysis (or financial analysis) is the process of reviewing and analysing a company's financial statements to make better economic decisions. These statements include the income statement, balance sheet, statement of cash flows, and a statement of changes in equity. Financial statement analysis is a method or process involving specific techniques for evaluating risks, performance, financial health, and future prospects of an organization.

It is used by a variety of stakeholders, such as credit and equity investors, the government, the public, and decision-makers within the organization. These stakeholders have different interests and apply a variety of different techniques to meet their needs. For example, equity investors are interested in the long-term earnings power of the organization and perhaps the sustainability and growth of dividend payments. Creditors want to ensure the interest and principal is paid on the organizations debt securities (e.g., bonds) when due.

RATIO ANALYSIS

Ratio Analysis is a form of Financial Statement Analysis that is used to obtain a quick indication of a firm's financial performance in several key areas. The ratios are categorized as Short-term Solvency Ratios, Debt Management Ratios, Asset Management Ratios, Profitability Ratios, and Market Value Ratios.

Ratio Analysis as a tool possesses several important features. The data, which are provided by financial statements, are readily available. The computation of ratios facilitates the comparison of firms which differ in size. Ratios can be used to compare a firm's financial performance with industry averages. In addition, ratios can be used in a form of trend analysis to identify areas where performance has improved or deteriorated over time.

Advantages of Ratio Analysis

1. To measure the liquidity position.
2. To know the solvency position.
3. Operating efficiency or turnover of the firm.
4. To assess the profitability position of the firm.
5. Inter - firm and intra - firm comparison .
6. Trend Analysis



Profitability Ratios

These ratios give an indication of the efficiency with which the operations of business are carried on. The following

are the important profitability ratios:

(i) Overall Profitability Ratio:

This is also called as Return on Investment (ROI) or Return on Capital Employed (ROCE) ratio. It indicates the percentage of return on the total capital employed in the business. It is calculated as follows:

$$\text{ROI} = \frac{\text{Operating Profit}}{\text{Capital Employed}}$$

The term 'Operating Profit' means "profit before interest and tax while the term 'capital employed' refer to the sum-total of long-term funds employed in the business.

(ii) Price Earning Ratio (P/E Ratio):

This ratio indicates the number of times the earning per share is covered by its market price. It is calculated as follows:

follows:

$$\text{P/E Ratio} = \frac{\text{Market Price Per Equity Share}}{\text{Earning Per Share}}$$

For example, if the market price of an equity share is ₹ 20 and earnings per share is ₹ 5, the price earnings ratio will be 4 (i.e., $20 \div 5$). This means for every one rupee of earning people are prepared to pay ₹ 4. In other words, the rate of return expected by the investors is 25%

(iii) Gross Profit Ratio (GPR):

This ratio expresses the relationship between Gross Profit and Net Sales. It can be computed as follows:

$$\text{GPR} = \frac{\text{Gross Profit}}{\text{Net Sales}} \times 100$$

(iv) Net Profit Ratio (NPR):

The ratio indicates net margin earned on a sale of ₹ 100. It is calculated as follows:

$$\text{NPR} = \frac{\text{Net Profit}}{\text{Net Sales}} \times 100$$

(v) Operating Ratio:

This ratio is a complementary of net profit ratio. In case the net profit ratio is 20%, the operating ratio will be 80%. It

is calculated as follows:

$$\text{Operating Ratio} = \frac{\text{Operating Cost}}{\text{Net Sales}} \times 100$$

(vi) Fixed Charges Cover Ratio (FCCR):

The ratio indicates the number of times the fixed financial charges are covered by income before interest and tax.

This ratio is calculated as follows:

$$\text{FCCR} = \frac{\text{Income before Interest and Tax}}{\text{Interest}}$$

(vii) Pay-out Ratio:

The ratio indicates what proportion of earning per share has been used for paying dividend. It can be calculated as follows:

$$\text{Pay-Out Ratio} = \frac{\text{Dividend per equity share}}{\text{Earning per equity share}}$$

(viii) Dividend Yield Ratio (DYR):

The ratio is calculated by comparing the rate of dividend per share with its market value. It is calculated as follows:

$$\text{DYR} = \frac{\text{Dividend Per Share}}{\text{Market Price Per Share}} \times 100$$

(ix) Return on Shareholders funds or Return on Net Worth:

This ratio expresses the net profit in terms of the equity shareholders funds. This ratio calculated as follows:

$$\text{Net Worth} = \frac{\text{Net Profit after Interest \& Tax}}{\text{Net Worth}} \times 100 \quad [\text{Net Worth} = \text{Equity Capital} + \text{Reserves \& Surplus}]$$

Turnover Ratios / Activity Ratio

These ratios indicate the efficiency with which capital employed is rotated in the business. The various turnover ratios are as follows:

(i) Over-all Turnover Ratio:

The ratio indicates the number of times the capital employed has been rotated in the process of doing a business.

The ratio is computed as follows:

$$\text{Overall Turnover Ratio} = \frac{\text{Net Sales}}{\text{Capital Employed}}$$

ii) Fixed Assets Turnover Ratio:

The ratio indicates the extent to which the investment in fixed assets has contributed towards sales. The ratio can

be calculated as follows:

$$\text{Fixed Assets Turnover Ratio} = \frac{\text{Net Sales}}{\text{Net Fixed Assets}}$$

(iii) Debtors' Turnover Ratio:

The ratio indicates the speed with which money is collected from the debtor. It is computed as follows:

$$\text{Debtors Turnover Ratio} = \frac{\text{Credit Sales}}{\text{Average Accounts Receivable}}$$

The term average account receivable includes trade debtors and bills receivable. Average accounts receivable are computed by taking the average receivables in the beginning and at the end of the accounting year. The higher the ratio, better it is. Debtors turnover ratio is used for computing the debt collection period.

(iv) Creditors Turnover Ratio:

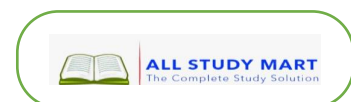
This is similar to Debtors Turnover Ratio. It indicates the speed with which payments for credit purchases are made

to creditor it can be computed as follows:

$$\text{Creditors Turnover Period} = \frac{\text{Credit Purchases}}{\text{Average Accounts Payable}}$$

The term 'accounts payable' include trade creditors and bills payable.

From the creditors turnover, ratio, creditors payment period can be computed as follows:



Credit Period Enjoyed = $\frac{\text{Months or days in a year}}{\text{Creditors Turnover}}$

(v) Stock Turnover Ratio

The ratio indicates whether the investment in inventory is efficiently used and whether it is within proper limits. It is calculated as follows:

Stock Turnover Ratio = $\frac{\text{Cost of Goods Sold during the year}}{\text{Average Inventory}}$

Average inventory is calculated by taking the average of inventory at the beginning and at the end of the accounting year.

Financial Ratios:

They are also termed as ‘Solvency Ratios’. These ratios indicate about the financial position of the company. A company is considered to be financially sound if it is in a position to carry on its business smoothly and meet all its obligations both short-term and long-term without strain. The Financial or Solvency Ratios can therefore be classified into following categories:

- (i) Long-term Solvency Ratios, which include fixed assets ratio, debt equity ratio and proprietary ratio;
- ii) Short-term Solvency Ratios, which include current ratio, liquidity ratio, super-quick ratio and defensive interval ratio & debt service coverage ratio.

Each of these ratios are now being discussed in detail in the following pages:

Long-term Solvency Ratios

(i) Fixed Assets Ratio:

The ratio indicates the extent to which fixed assets have been acquired by use of long-term funds. The ratio is expressed as follows:

Fixed Assets Ratio = $\frac{\text{Net Fixed Assets}}{\text{Long-term Funds}}$

The term ‘Net Fixed Assets’ means original cost of fixed assets less depreciation to date. The ratio should not be more than ‘1’. The ideal ratio is 0.67.

(ii) Debt-Equity Ratio:

The ratio is determined to ascertain the proportion between the ‘outsiders’ ‘funds and share-holders funds’ in the capital structure of an enterprise. The term outsiders’, funds is generally used to represent total long-term debt. The ratio can be computed as follows:

Debit - Equity Ratio = $\frac{\text{Total Long-term Debt}}{\text{Shareholder's Funds}}$

(iii) Proprietary Ratio

It is a variant of Debt-Equity Ratio. It establishes relationship between the proprietors’ or shareholders’ funds and the total tangible assets. It may be expressed as follows:

Proprietary Ratio = $\frac{\text{Shareholder's Funds}}{\text{Total Tangible Assets}}$

Short-term Solvency Ratios

(i) Current Ratio

The ratio is an indicator of the firm’s commitment to meet its short-term liabilities. It is expressed as follows:

Current Ratio = $\frac{\text{Current Assets}}{\text{Current Liabilities}}$

An ideal current ratio is '2'. However, a ratio of 1.5 is also acceptable if the firm has adequate arrangements with its bankers to meet its short-term requirements of funds.

(ii) Liquidity Ratio / Quick Ratio / Acid Test Ratio:

The ratio is also termed as Acid Test Ratio or Quick Ratio. The ratio is ascertained by comparing the liquid assets i.e., current assets (excluding stock and prepaid expenses) to current liabilities. The ratio may be expressed as follows:

$$\text{Liquidity Ratio} = \frac{\text{Liquid Assets}}{\text{Current Liabilities}}$$

$$\text{Liquid Assets} = \text{Current Assets} - \text{Inventory} - \text{Prepaid Expenses}$$

Some accountants prefer the term liquid liabilities for current liabilities. The term 'liquid liabilities' means liabilities payable within a short period. Bank overdraft and cash credit facilities (if they become permanent modes of financing) are excluded from current liabilities for this purpose. The ratio may be expressed as follows:

$$\text{Liquidity Ratio} = \frac{\text{Liquid Assets}}{\text{Liquid Liabilities}}$$

$$\text{Liquid Liability} = \text{Current Liability} - \text{Bank Overdraft} - \text{Cash Credit}$$

The ideal ratio is '1'.

(iii) Super-quick Ratio:

It is a slight variation of quick ratio. It is calculated by comparing the super quick assets with the current liabilities (or liquid liabilities) of a firm. The ratio may be expressed as follows:

$$\text{Super-quick Ratio} = \frac{\text{Super Quick Assets}}{\text{Current Liabilities}}$$

The term 'Super-Quick Assets' means current assets excluding stock, prepaid expenses and debtors. Thus, super quick assets comprise mainly cash, bank balance and marketable securities.

(iv) Defensive-Interval Ratio (DIR)

This ratio denotes the liquidity of a firm in relation to its ability to meet projected daily expenditure from operations. It can be expressed as follows:

$$\text{Defensive Interval Ratio} = \frac{\text{Liquid Assets (quick assets)}}{\text{Daily Cash requirements (Projected)}}$$

$$\text{Daily cash requirements (projected)} = \frac{\text{Projected cash operating expenditure}}{\text{Number of days in a year}}$$

(v) Debt Service Coverage Ratio (DSCR)

This ratio indicates whether the business is earning sufficient profits to pay not only the interest charged, but also whether due of the principal amount. The ratio is calculated as follows:

$$\text{Debt Service Coverage Ratio} = \frac{\text{Profit after Taxes} + \text{Depreciation} + \text{Interest on Loan}}{\text{Interest on Loan} + \text{Loan repayment in a year}}$$

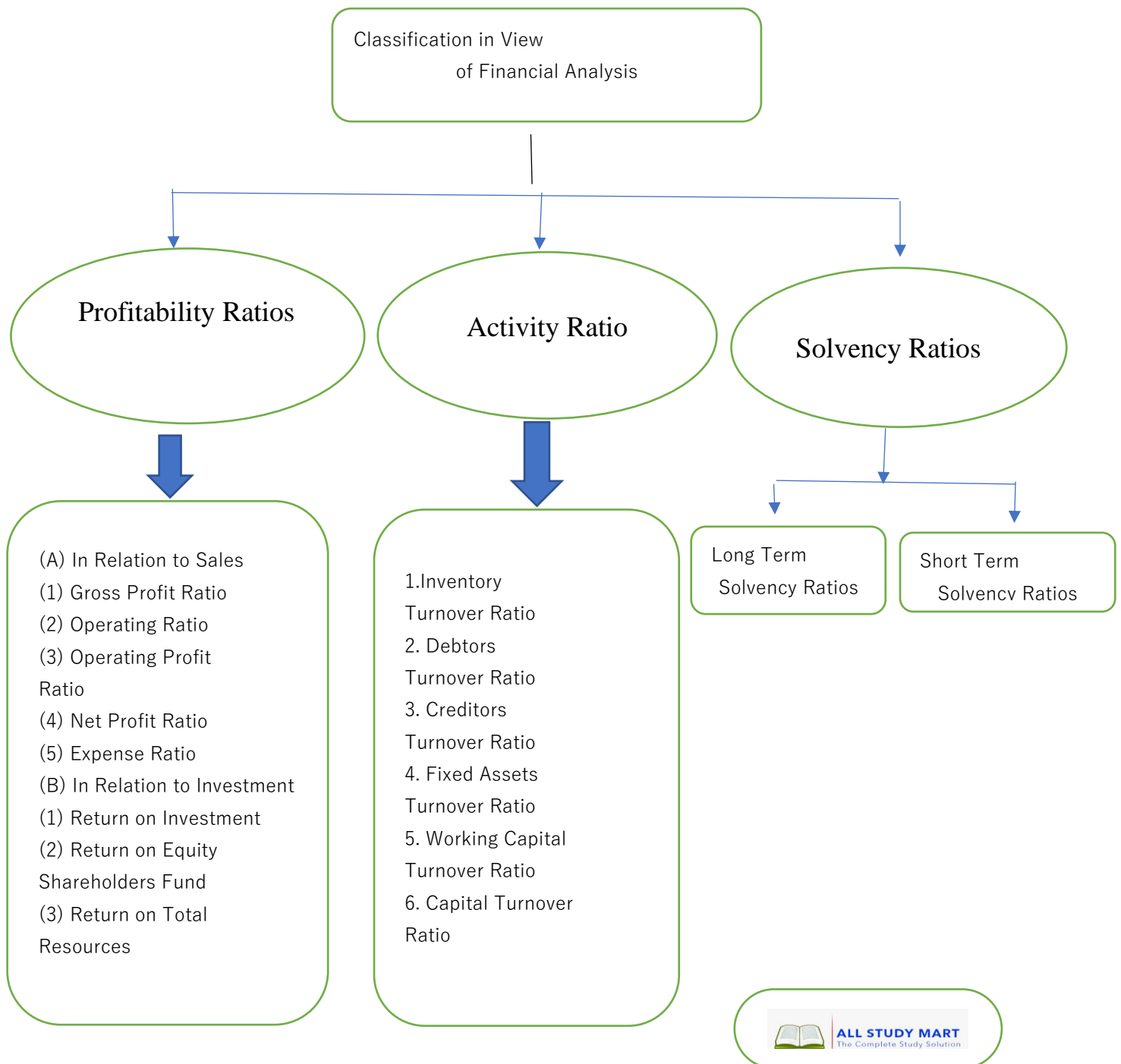
Classification of Ratios:

Illustration : 01

Following is the Profit and Loss Account and Balance Sheet of PKJ Ltd. Redraft them for the purpose of analysis

and calculate the following ratios:

- 1) Gross Profit Ratio
- 2) Overall Profitability Ratio
- 3) Current Ratio
- 4) Debt-Equity Ratio
- 5) Stock-Turnover Ratio
- 6) Finished goods Turnover Ratio
- 7) Liquidity ratio

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Profit and Loss A/c

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Particulars	Amount (₹)	Particulars	Amount (₹)
Opening stock of finished goods	1,00,000	Sales	10,00,000
Opening stock of raw material	50,000	Closing stock of raw material	1,50,000
Purchase of raw material	3,00,000	Closing stock of finished goods	1,00,000
Direct wages	2,00,000	Profit on sale of shares	50,000
Manufacturing Exp	1,00,000		
Administration Exp	50,000		
Selling & distribution Exp	50,000		
Loss on sale of Plant	55,000		
Interest on debentures	10,000		
Net Profit	3,85,000		
	13,00,000		13,00,000

Balance Sheet

Liabilities	Amount (₹)	Assets	Amount (₹)
Equity share capital	1,00,000	Fixed assets	2,50,000
Preference share capital	1,00,000	Stock of raw material	1,50,000
Reserves	1,00,000	Stock of finished goods	1,00,000
Debentures	2,00,000	Bank balance	50,000
Sundry Creditors	1,00,000	Debtors	1,00,000
Bills Payable	50,000		

650000

650000



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Position Statement

	(₹)
Bank	50,000
Debtors	1,00,000
Liquid Assets	1,50,000
(+) Stock (R.M.+F.G.)	2,50,000
Current Assets	4,00,000
(-) Current liabilities (S.C.B.P.)	(1,50,000)
Working capital	2,50,000
(+) Fixed assets	2,50,000
Capital employed in business	5,00,000
(-) External liabilities	(2,00,000)
Shareholders funds	3,00,000
(-) Preference share capital	(1,00,000)
Equity share capital	2,00,000

Represented by

Equity share capital	1,00,000
(+) Reserves	1,00,000
	2,00,000

COMMON SIZE FINANCIAL STATEMENT

A common size financial statement displays all items as percentages of a common base figure. This type of financial statement allows for easy analysis between companies or between time periods of a company. The values on the common size statement are expressed as percentages of a statement component, such as revenue.

COMMON SIZE INCOME STATEMENT

Common size income statement is an income statement in which each account is expressed as a percentage of the value of sales. This type of financial statement can be used to allow for easy analysis between companies or between time periods of a company. Common size income statement analysis allows an analyst to determine how the various components of the income statement affect a company's profit.

DU PONT ANALYSIS

The Dupont analysis also called the Dupont model is a financial ratio based on the return on equity ratio that is used to analyze a company's ability to increase its return on equity. In other words, this model breaks down the return on equity ratio to explain how companies can increase their return for investors.

The Dupont analysis looks at three main components of the ROE ratio.

- Profit Margin
- Total Asset Turnover
- Financial Leverage

Based on these three performances measures the model concludes that a company can raise its ROE by maintaining a high profit margin, increasing asset turnover, or leveraging assets more effectively.

