Balance Sheets

- The balance sheet shows the value of a business's assets and liabilities at a particular time. Sometimes referred to as the statement of financial position.
- The balance sheet is different from the income statement
- The income statement records the income and expenses of a business, and the profit and loss it makes over a set time period
- The balance sheet records the value or worth of the business at one moment in time, the ned of the financial year

Assets

- Assets are those items of value which are owned by the business. They may be current or non-current assets
- Non-current assets are items owned by the business for more than one year
- Examples of non-current/fixed assets: land, buildings, equipment and vehicles
- They are likely to be kept in the business for more than one year
- Most fixed assets, apart from land, depreciate over time so the value of these will fall on the balance sheet from one year to the next
- Intangible assets are those that do not exits physically but still have a value- such as brand names, patents and copyrights [intellectual property][Example of a fixed asset]
- Current assets are owned by the business and used within one year
- Examples of current assets: cash, inventories (stocks) and accounts receivable (debtor customers who owe money to the business)

Liabilities

- Liabilities are debts owed by the business
- Non-current liabilities are long term debts owed by the business
- Non-current liabilities are long term borrowings which do not have to be repaid within one year
- Current liabilities are short-term debts owed by the business
- Current liabilities are amounts owed by the business which must be paid within one year (bank overdrafts, accounts payable, suppliers/creditors owed money by the business)

Why assets and liabilities are of importance

- When the value of assets is greater than the value of liabilities, then wealth is owned
- In the case of business, this wealth belongs to the owners
- In the case of companies, it belongs to the shareholders
- This is why the balance sheet is important to the users of the accounts
- It shows how much wealth or equity the owners have invested in the business
- They would obviously like to see this increase year by year

$$\text{Total assets} - \text{total liabilities} = \text{owner's equity (shareholder's funds in a limited company)}$$

Explanation of balance sheet terms

- Total assets less total liabilities is always equal to total shareholders' funds or equity-otherwise the balance sheet would not balance
- Shareholder's equity/funds is the total sum of money invested into the business by the owners of the company- the shareholders. This money is invested in two ways:
    i. Share capital is the money put into the business when the shareholders bought newly issued shares
    ii. Reverse arise for a number of reasons. Profit and loss reverses are retained profits from current and previous years. This profit is owned by the shareholders but has not been paid out to them in the form of dividends. It is kept in the business as a part of the shareholders' funds.

Interpreting balance sheet data

- Shareholders can see if their stake in the business has increased or fallen in value over the last 12 months by looking at the total equity figures for 2 years
- Shareholders can also analyse how expansion by the business has been paid for-by increasing non-current liabilities; from retained profits or increasing share capital. If inventories or stocks have been sold off to provide capital for business expansion then this will be clear by this figure declining on the balance sheet
- Working capital can be calculated from balance sheet data

$$\text{Working capital} = \text{current assets} - \text{curreny liabilities}$$

- No business can survive without working capital. It is used to pay short-term debts. If these debts cannot be paid because the business does not have enough working capital, the creditors could force the business to stop trading.
- Capital employed can also be calculated using data from the balance sheet.

$$\text{Capital employed} = \text{shareholders; funds} + \text{non} - \text{current liabilities}$$

- This is the long term and permanent capital of the business which has been used to pay for the assets of the business
- Balance sheet data can also be used to calculate ratios which are used to assess business performance