ECONOMIC AND FINANCIAL ANALYSIS OF A COMPANY

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ABSTRACT

In this era, it is almost impossible for a business manager to be able to operate an enterprise without understand how financial aspects influences the company life.
The reason I chose the title " Economic and financial analysis of a company " is that for any business manager is essential to have the ability to understand financial data, because the finance could be considered the language of business.
The purpose of this paper is to present a way of a financial analysis of a company, and in this sense has been realized an analysis for a Romanian company.
I think that this case study will be useful for those who want to know how we can make and interpret an economic and financial analysis of a company, being a suitable source of information in this area.

Keywords – financial analysis, company, net profit, turnover, profitability

JEL Classification – G30, G32

Paper type – Case study

Introduction

The performance analysis of a company has a decisive role in determining the strategy to be followed. This case study has as the main theme *the economic and financial analysis of a company.* I chose this topic because I think that any business manager must have the ability to understand financial data, because the finance could be considered the language of business.

This project contains two chapters, the first one is about theoretical aspects about a financial analysis and the second one presents the applicative part of this paper.

Regarding the research methodology, I chose a company and I used its financial data for the 2012 - 2014 period, from the Ministry of Finance, then I analyzed and explained them in Microsoft Office Excel 2007.

The project is based on the following *research question: How can a young manager make a simple, but consistent financial analysis?* So, I made an analysis, based on data from an e-commerce company balance sheet, using a system of relevant indicators and interpreting certain conclusions. I tried to use a number of indicators considered as a system to define, finally, a model for analyzing the performance of a company.

1. Theoretical aspects regarding the financial analysis of a company

In this chapter I will briefly present the main theoretical aspects relating to the financial analysis of a company.

I agree with the phrase according to which Way J. says that „a company's financial statements provide various financial information that investors and creditors use to evaluate a company's financial performance. Financial statements are also important to a company's managers because by publishing financial statements, management can communicate with interested outside parties about its accomplishment running the company."

I think that having the ability to analyze the financial position of a company is a useful skill for any manager.

Many enterprises can appear successful, even if they have structural problems regarding the way they are financed and managed. The consequences of starting a partnership with another company who goes bust, or who, despite appearing credible, never seems capable to comply on their promises because of secret financial problems, are very dangerous.

The main sources of data for any financial analysis are a company's balance sheet and the profit and loss statement (P&L).

A balance sheet is „a summary of the financial balances of an individual or organisation, a business partnership, a corporation, private limited company or other organization such as Government or not - for - profit entity.

Assets, liabilities and ownership equity are listed as of a specific date, such as the end of its financial year. A balance sheet is often described as *a snapshot of a company's financial condition.* (Williams and Haka, 2008, p.40)

The profit and loss statement (P&L) „is one of the financial statements of a company and shows the company's revenues and expenses during a particular period and it indicates how the revenues are transformed into the net profit. It displays the revenues recognized for a specific period, and the cost and expenses charged against these revenues, including write-offs and taxes.

The purpose of the P&L is to show managers and investors whether the company made or lost money during the period being reported." (Helfert, 2001, p.40)

Financial analysis and common-size help the financial performance and condition of a company through an examination of relationships among these many financial items.

A comprehensive financial review of a company should consider its effectiveness in putting assets to work, liquidity, solvency and its profitability. Any trained manager can use the tools of a financial analysis, to help understand where the company has been.

In conclusion, I can say that the financial analysis is an important tool for all business owners and managers, in order to reflect their progress toward reaching company goals, as well as toward competing with larger companies within an industry.

2. Economic and financial analysis of an e-commerce company

To realize an analysis of the financial stability of the company, I made a summary of the balance sheet for the period 2012 - 2014, presented in Table no. 1 in order to calculate the balance indicators (working capital, working capital requirements and net cash) necessary for this analysis.

Table no. 1 - Company balance S.C ABC S.R.L.*

S.C. ABC S.R.L. Company balance
2012 - 2014 -RON-

Balance sheet elements	Financial Year			Balance sheet elements	Financial year		
	2012	2013	2014		2012	2013	2014
Permanent assets	**79772**	**254797**	**319829**	**Permanent liabilities**	**268495**	**464434**	**649221**
Intangible assets	79772	254797	319829	Capital	227631	433040	627822
-	-	-	-	Long-term Liabilities	40864	31394	21399
Current Assets	**222455**	**525131**	**583462**	**Current Liabilities**	**288254**	**454341**	**538305**
Current assets	218796	523388	574144	Short-term liabilities	288254	454341	538305
-Stocks	164374	287746	563302	-	-	-	-
-Debts	54422	235642	10842				
Prepaid expenses	3659	1743	9318				
Treasury Assets	**254522**	**138847**	**284235**	**Treasury Liabilities**	**-**	**-**	**-**

Cash and bank accounts	254522	138847	284235	-	-	-	-
TOTAL ASSETS	**556749**	**918775**	**1187526**	**TOTAL PASIVE**	**556749**	**918775**	**1187526**

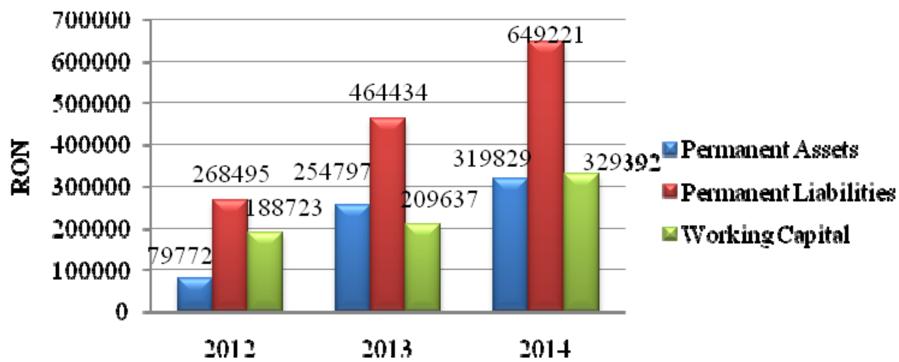
Source: Own processing – mfinante.ro
** It is conventionally attributed for confidentiality reasons, data being obtained from a real company.*

Table no. 2 – Working capital analysis in 2012 – 2014 period

Indicators	u.m.	Financial Year		
		2012	2013	2014
Permanent Liabilities	RON	268495	464434	649221
Growth rate of PL (n/n-1)	%	100	173	140
Permanent Assets	RON	79772	254797	319829
Growth rate of PA (n/n-1)	%	100	319	126
Working Capital	**RON**	**188723**	**209637**	**329392**
Δ of Working Capital (n/n-1)	RON	0	20914	119755
Growth rate of WC (n/n-1)	%	100	111	157
Capital	RON	227631	433040	627822
Growth rate of Capital (n/n-1)	%	100	190	145
Own Working Capital	RON	147859	178243	307993
Foreign Working Capital	RON	40864	31394	21399

Source: Own processing based on data obtained from company balance sheet

Figure 1 – The working capital evolution in 2012-2014 period

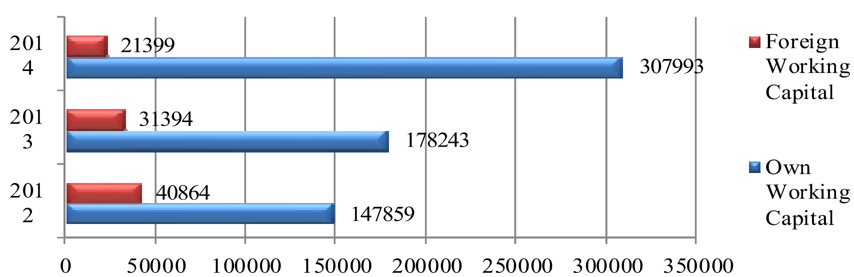


As can be seen in Table no. 2 and Figure 1, during the analyzed period, the working capital has been positive, which increased from year to year, with 20914 RON (11%) in 2013 compared to 2012 and 119755 RON (57%) in 2014 compared to 2013.

This situation is favorable for the company because the long-term resources can fully supports the permanent needs that the company has, which is primarily due to the increasing permanent liabilities by 73% in 2013/2012 and 40% in 2014/2013 .

I also believe that the positive development of working capital gives the company a higher safety because it is protected from unexpected events that may occur.

Figure 2 – Working capital structure by its origin in 2012-2014 period



About sharing working capital in own and foreign working capital, we can see that permanent needs of the company are fully satisfied through owned capital, which represents a favorable aspect.

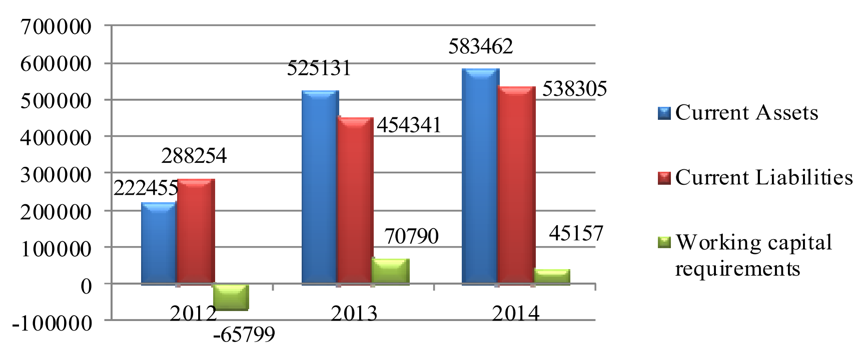
While the own working capital increases from year to year, going from 188723 RON in 2012 to 329392 RON in 2014, which is due to increasing capital, it seems that foreign working capital decreases in 2014 compared to 2012 from 40864 RON to 21399 RON, a favorable issue result of the decrease occurred in long-term debt of the company.

Table no. 3 – Working capital requirements analysis in 2012 - 2014 period

Indicators	u.m.	Financial Year		
		2012	2013	2014
Current Assets	RON	222455	525131	583462
Growth rate of CA (n/n-1)	%	100	236	111
Current Liabilities	RON	288254	454341	538305
Growth rate of CL (n/n-1)	%	100	158	118
Working capital requirements (WCR)	**RON**	**-65799**	**70790**	**45157**
Δ WCR (n/n-1)	RON	0	136589	-25633

Source: Own processing based on data obtained from company balance sheet

Figure 3 – Working capital requirements evolution in 2012-2014 period



According to Table no.3 and Figure 3, working capital requirements in 2012 recorded a negative value (-65799 RON) favorable situation for the company, because it represented a surplus of short-term resources.

In 2013, working capital requirements increased by 136589 RON over the previous year so that it registered a positive value, unfavorable to the company which means a surplus of temporary needs in relation to short-term resource deficit.

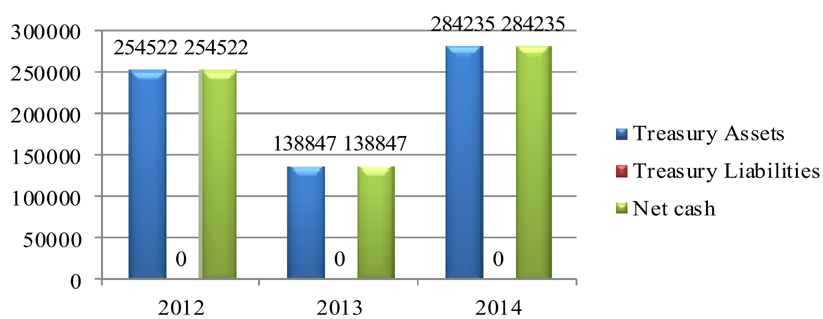
However, this positive value is normal, considering the fact that turnover has grown from 2012 in 2013 to about 1.4 million RON. Also in 2014, the working capital requirements are all positive, but dropped by 25633 RON compared to 2013.

Table no. 4 - Net cash analysis in 2012 - 2014 period

Indicators	u.m.	Financial Year		
		2012	2013	2014
Treasury Assets	RON	254522	138847	284235
Treasury Liabilities	RON	0	0	0
Net cash	**RON**	**254522**	**138847**	**284235**
Δ NC (n/n-1)	RON	0	-115675	145388

Source: Own processing based on data obtained from company balance sheet

Figure 4 – Net cash evolution in 2012-2014 period



Regarding net cash position in the 2012 - 2014 period, according to Table no. 4 and Figure 4, it seems that throughout the period analyzed, the values recorded are positive, which means a favorable situation for the company, since there is a surplus of cash. Also, it can be seen that Net Cash = Treasury Assets, Treasury liabilities being equal to 0.

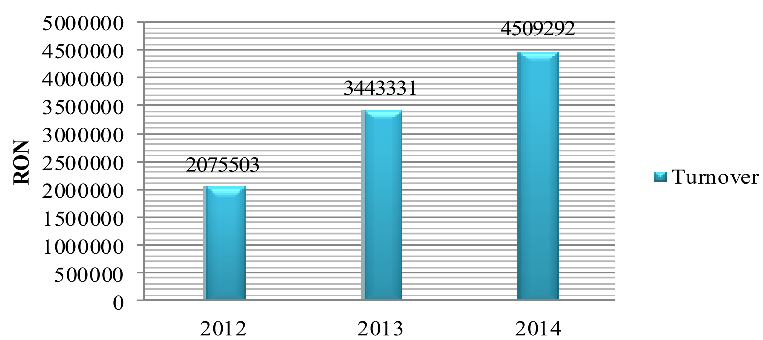
Regarding the evolution of Net Cash, it seems that in 2013, compared to 2012, the Net Cash decreased by 115675 RON, due to increasing working capital requirements in 2013, unlike 2014, when it was increased by 145388 RON compared to 2013.

Table no. 5 – Turnover evolution in 2012-2014 period

Indicators	u.m.	Financial Year		
		2012	2013	2014
Turnover	RON	2075503	3443331	4509292
Δ Turnover	%	100	166	131

Source: Own processing based on data obtained from company balance sheet

Figure 5 – Turnover evolution in 2012-2014 period



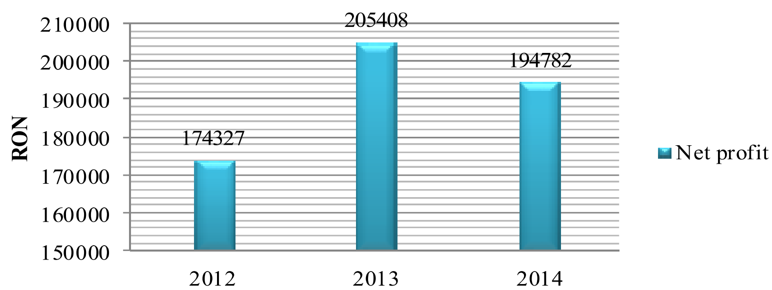
In Table no. 5 and Figure 5, I represented the turnover evolution, which recorded an upward trend from year to year. It seems that the biggest increase has been recorded in 2013, while it increased by 66% over the previous year.

Table no. 6 – Net profit evolution in 2012-2014 period

Indicators	u.m.	Financial Year		
		2012	2013	2014
Net profit	RON	174327	205408	194782
Δ Net profit	%	100	118	95
Profitability rate (Profit/Turnover*100)	%	8.40	5.97	4.32

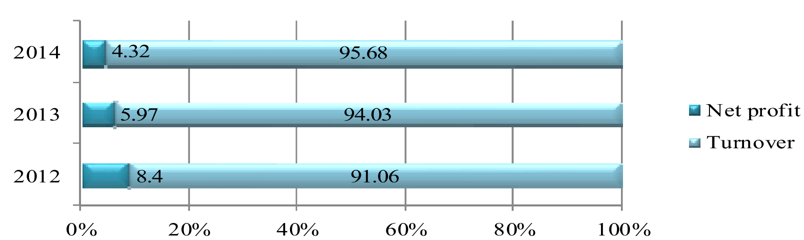
Source: Own processing based on data obtained from company balance sheet

Figure 6 – Net profit evolution in 2012-2014 period



According to Table no. 6 and Figure 6, the analysis focuses on the net profit evolution recorded by the company in 2012-2014, so in 2013 compared to 2012 there was an increase of net profit by 18%, unlike in 2014 compared to 2013, when it dropped by 5 %.

Figure 7 – Profitability rate



Referring to profitability, Figure 7 highlights what is the percentage of net profit in turnover in these three years. The situation is not very good, because the values should be between 10 and 20%. While in 2012 the rate was closer to 10%, it seems that until 2014 it decreased to 4.3%.

Table no. 7 – Current assets and liabilities rotation length

Rotation rates - days -	Financial Year		
	2012	2013	2014
Stock rotation length	29	30	50
Δ stock rotation length	0	1	15
Debts rotation length	9	25	1
Δ Debts rotation length	0	16	-24
Short-term liabilities rotation length	50	48	43
Δ Short-term liabilities rotation length	0	-2	-5

Source: Own processing based on data obtained from company balance sheet

As can be seen in Table no. 7, stock rotation length increased from 29 days in 2012 to 50 days in 2014. This means that it takes 50 days for stocks to be turned into cash. Increase of 15 days stock rotation lenght in 2014 compared to 2013 is a negative aspect, because the company needs products that are sold quickly and must be avoided the situation where there are products that are more in stock and give rise to too big storage costs.

The debts rotation length was 9 days in 2012, so it took nine days to recover money from customers, reaching as 2014, the debts rotation length to fall to just one day, favorable issue, because money is collected from customers very quickl

Regarding the short-term liabilities rotation length, it seems that it was 50 days in 2012, 48 days in 2013 and 43 days in 2014. It is noted that the number of days has decreased by 5, but I think 43 days are enough to the company to pay its short-term liabilities, whereas debts are collected every day.

Table no. 8 – Capital structure rate in 2012-2014 period

Capital structure rate	Financial Year		
	2012	2013	2014
Patrimonial solvency (Capital/Liability)	0,41	0,47	0,53
Financial leverage (Long-term liability /Capital)	0,18	0,07	0,03

Source: Own processing based on data obtained from company balance sheet

As can be seen in Table no. 8, the patrimonial solvency shows the extent to which capital covers the liabilities and indicates its share in total capital, so that in 2012 and 2013, solvency is 0.41, respectively 0.47, representing a normal situation, because it falls in the range [0.3 to 0.5], while in 2014 exceeds 0.03.

Regarding the financial lever, it is below unit in all three years, this showing that the long term liabilities are less than the resources brought by shareholders.

Conclusions

Any business manager needs to be able to operate an enterprise and understand how financial aspects influences the company life, because the finance could be considered the language of business.

This analysis shows a good situation for this company and this result shows that the company's strategy functioned correctly, so the duty of manager is to maintain and continuously improve the activity for better results.

In conclusion, I can say that the financial analysis is an important tool for all business owners and managers, in order to reflect their progress toward reaching company goals, as well as toward competing with larger companies within an industry.

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