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Financial Statement Overview: Ferreting out the Secrets

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Financial Statement Overview:

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FERRETING OUT THE SECRETS

Ann Gibson, PhD, CPA
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Basic Financial Statements

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- Income Statement
 - (or Statement of Changes in Net Assets)
- Statement of Owners' Equity
- Balance Sheet
 - (or Statement of Financial Position)
- Statement of Cash Flows

Steps to Analyze Financial Statements

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- Run your thumb down the current asset side of the balance sheet and find the largest number
- Whoever controls the largest asset controls the organization

Steps to Analyze Financial Statements

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- Review the numbers in the format presented
- Look for large changes between the years

Steps to Analyze Financial Statements

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- Read the Audit Opinion Letter
 - Unqualified Opinion
 - May contain additional paragraphs about uncertainties, consistency or emphasis of a matter
 - Qualified Opinion
 - Contains the words “Except for”
 - Disclaimer of Opinion
 - Adverse Opinion

Steps to Analyze Financial Statements

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- Read the Footnotes to the Financial Statements
 - Descriptive notes for the organization (Note 1 or Notes 1 and 2)
 - Notes that provide additional disclosure about the accounts
 - Notes that provide additional information about the organization and its activities

Steps to Analyze Financial Statements

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- Calculate the Financial Ratios
 - Liquidity Ratios
 - Leverage (or Solvency) Ratios
 - Activity Ratios
 - Profitability Ratios

Steps to Analyze Financial Statements

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- **Liquidity Ratios:**

- Measures the organization's capacity to meet its short-term liabilities
- Current Ratio
- Quick (or Acid-Test) Ratio

Steps to Analyze Financial Statements

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Current Ratio:

Current Assets

Current Liabilities

$$\frac{\$33,076,109}{\$3,156,406} = 10.48$$

Steps to Analyze Financial Statements

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Quick (or Acid-Test) Ratio:

Cash + Marketable Securities + Accounts
Receivable

Current Liabilities

$$\frac{\$25,166,688}{\$3,156,406} = 7.97$$

Steps to Analyze Financial Statements

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- Leverage (Solvency) Ratios:
 - Measures the extent to which the organization has been financed by debt
 - Debt to Assets Ratio

Steps to Analyze Financial Statements

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Debt to Assets Ratio:

Total Liabilities
Total Assets

$$\frac{\$3,157,432}{\$41,612,712} = 7.6\%$$

Steps to Analyze Financial Statements

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- Activity Ratios:

- Measures the organization's use of its resources
- Receivables Turnover
- Inventory Turnover

Steps to Analyze Financial Statements

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Accounts Receivable Turnover:

Net Sales

Average Trade Accounts Receivable (net)

$$\frac{\$19,602,524}{\$4,140,816} = 4.73$$

Steps to Analyze Financial Statements

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Days Sales in Receivables:

365

Receivables Turnover

$$\frac{365}{4.73} = 77 \text{ days}$$

Steps to Analyze Financial Statements

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Inventory Turnover:

Cost of Goods Sold
Average Inventory

$$\frac{\$10,309,484}{\$7,993,291} = 1.29$$

Steps to Analyze Financial Statements

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Days Sales in Inventory:

$$\frac{365}{\text{Inventory Turnover}}$$

$$\frac{365}{1.29} = 283 \text{ days}$$

Steps to Analyze Financial Statements

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- Profitability Ratios:

- Measure the organization's ability to generate profit and return on investment
- Return on Revenue (Sales)
- Return on Assets

Steps to Analyze Financial Statements

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Return on Revenue (Sales)

Net Income (or Change in Net Assets)
Net Revenue (Sales)

$$\frac{\$635,972}{\$14,701,893} = 4.3\%$$

Steps to Analyze Financial Statements

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Return on Assets:

Net Income (or Change in Net Assets)
Average Assets

$$\frac{\$635,972}{\$41,447,937} = 2.0\%$$

Thank you very much!

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Any comments or questions?