The Ministry of Education of Azerbaijan Republic

ANALYZING OF FINANCIAL STATEMENTS

Vuqar Yusifzade

UNEC SABAH
Azerbaijan State Economic University

2018

ACKNOWLEDGEMENTS

Initially, I would like to thank to my scientific supervisor, PhD candidate Polad Azizov for his advice, encouragement and patient guidance. I am extremely lucky to have a supervisor who cared so much about my work and responded my questions so promptly.

ABSTRACT

ANALYZING OF FINANCIAL STATEMENTS

Vuqar Yusifzade

SABAH 2 Economy 1

Supervisor: PhD candidate Polad Azizov

UNEC SABAH
Azerbaijan State Economic University

The overall objective of the financial statements is to provide information on the results of operations, financial position and cash flow of the organization. This information is used by financial statement readers to make decisions about resource allocation. At a more subtle level, there is another goal related to each of the financial statements. The profit and loss account informs the reader about the ability of the business to make a profit. In addition, it shows the volume of sales and the nature of the various types of costs, depending on how the information about costs is aggregated. When considering for several periods of time, the profit and loss account can also be used to analyze trends in the company's performance.

Analysis of financial statements is a process of analyzing and evaluating the financial statements of a company (for example, a balance sheet or profit and loss account), which allows you to understand the financial state of the company and ensure more effective decision-making. Financial statements record financial data; but this information should be evaluated through an analysis of financial statements in order to become more useful to investors, shareholders, managers and other interested parties.

Contents

INTRODUCTION

Introduction to Analyzing Financial Statements presents the tools needed to analyze financial statements with confidence. This course reviews the importance of analyzing financial statements in the small business lending process, and teaches the terms and steps associated with analyzing financial statements, including the income statement, the balance sheet and the cash flow statement. This course will also explain how tax returns report income and expenses from a different perspective. This course examines the computation and meaning of four categories of financial ratios and how ratios are used to spot significant trends.

Personnel who are responsible for reviewing financial statements for the purpose of assisting in making lending decisions, monitoring the ongoing health of the business, or conducting the initial financial analysis.

Learning Objectives: After completing this course, students will be able to:

Define financial statement analysis and explain its importance in the small business lending process

List the basic steps of financial statement analysis and the purpose of each step

Analyze an income statement and balance sheet

Explain how tax returns are used in the lending process

Calculate and interpret key ratios

Perform a simple cash flow analysis

Financial statement analysis (or financial analysis) is the process of reviewing and analyzing 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.

Common methods of financial statement analysis include fundamental analysis, DuPont analysis, horizontal and vertical analysis and the use of financial ratios. Historical information combined with a series of assumptions and adjustments to the financial information may be used to project future performance. The Chartered Financial Analyst designation is available for professional financial analysts.

CHAPTER 1. CHARACTERISTICS OF FINANCIAL STATEMENT ANALYSIS

1.1 Financial statements

Financial reporting - a set of accounting indicators, reflected in the form of certain tables and characterizing the movement of property, liabilities and financial position of the company for the reporting period.

Financial reporting is a system of data on the financial position of the company, the financial results of its activities and changes in its financial position and is compiled on the basis of accounting data.

Financial reporting - a system of indicators reflecting the property and financial position of the organization at the reporting date, as well as the financial results of its activities for the reporting period.

The user of financial statements is a legal entity or an individual interested in information about the organization.

The balance is the means of the organization, which must work and make a profit.

Passive balance - the sources of education and placement of funds of the organization.

Non-current assets - funds acquired for the purpose of long-term use in the course of the economic activity of the organization.

Current assets - funds that are to be used during the reporting period are realized with the purpose of applying them to cash.

Revenues - increase in economic benefits as a result of the receipt of assets (cash, other property) and (or) repayment of liabilities, leading to an increase in the capital of this organization, with the exception of the contributions of participants (owners of property).

Expenses - decrease in economic benefits as a result of the retirement of assets (cash, other property) and (or) the occurrence of liabilities, leading to a reduction in the capital of this organization, with the exception of reducing contributions by decision of participants (property owners).

In a market economy, financial reporting becomes the main source of information for making informed management decisions. An important requirement for the management decision is the presence of facts relating to the financial position of the organization and the results of its activities. Such facts are presented in the form of accounting data, which are collected, grouped, summarized and reflected in the reporting. In the most general form, financial reporting is the final product of accounting in the organization.

Financial reporting in the management system is of interest to various groups of users, both internal and external.

Internal directly engaged in business in this organization: the management of the enterprise and various officials (managers, economists, etc.), who are responsible for the conduct of business and for the results of the organization. The results of the organization's work depend on the correctness and timeliness of management decisions, and many of these decisions are largely based on accounting information and its analysis.

External users combine two groups:

- Directly (directly) stakeholders in the activities of the organization;
- subjects with indirect interest in the activities of the organization.

The first group consists of the owners (shareholders) of the organization, creditors, investors, state tax agencies, employees (employees), other organizations that are present or potential partners of this organization.

Shareholders study information about profitability, changes in the organization's own capital.

Lenders use reporting to assess the solvency of the organization, its reliability as a customer and in determining the conditions for issuing loans.

Investors consider reporting from the position of profitability and reliability of investing their funds in this organization.

Tax authorities monitor the data on accrued and paid taxes.

Potential business partners, as well as companies that already have business relations with this organization, assess its financial situation, study the reporting in order to predict price trends, and seek new opportunities for cooperation.

The second group includes persons who have an indirect financial interest, but who defend the interests of the first group. These are various audit and consulting firms, stock exchanges, government agencies, news agencies, representatives of the press, trade unions, etc.

The audit firms give an opinion on the reliability of the reporting provided by the organization.

State bodies study financial reports in order to control the dynamics of prices and movement of shares, the implementation of economic planning, the improvement of accounting methods and reporting.

Information agencies and representatives of the press extract information from the reporting data for the preparation of surveys, assessment of development trends of individual organizations, industries, comparative analysis of the performance of various companies and calculation of generalized indicators of financial and economic activity.

From the point of view of providing management activities, the financial statements must satisfy the following basic requirements that meet the interests of users and, first of all, investors and creditors:

- contain data for making managerial decisions in the field of investment policy;
- provide an assessment of the resources available to the organization, taking into account the changes occurring in them and the effectiveness of their use;
- provide an assessment of the dynamics of profitability;
- contain data for a forward-looking assessment of the organization's position on the market.

Requirements for Financial Statements

The Accounting Regulation "Accounting Statements of the Organization" (PBU 4/99) defines the following reporting requirements: reliability, neutrality, materiality, integrity, consistency, comparability, observance of the reporting period, correctness of registration.

The requirement of reliability means that the financial statements should provide a reliable and complete picture of the organization's financial and financial position and the financial results of its operations. Reliable and complete is considered to be reporting, formed and compiled in accordance with the rules established by national accounting standards.

The requirement of neutrality excludes the unilateral satisfaction of the interests of certain groups of users over others, as well as the influence through selection or presentation form on decisions and assessments of users in order to achieve predefined results or consequences.

The requirement of materiality determines the right of the organization to include in the reporting additional indicators and explanations not provided for by standard forms of financial statements, in order to form a complete picture of the organization's property and financial position.

The requirement of integrity means the need to include in the reporting data on all business transactions carried out by the organization as a whole, and its branches, offices and other units.

The requirement of sequence fixes in the practice of forming accounting reports the need to maintain consistency in the content and forms of the balance sheet, the profit and loss account and explanations to them from one reporting year to another.

In accordance with the requirement of comparability, the financial statements should contain data allowing them to be compared with similar data for the previous reporting period.

The requirement to comply with the reporting period means that as the reporting year in Azerbaijan the period from January 1 to December 31 inclusive is adopted, i.e., the fiscal year coincides with the calendar year.

The requirement for proper registration is due to the observance of the formal principles of reporting: its compilation in Azerbaijan, in the currency of the Azerbaijan (in rubles), the signing by the head of the organization and the specialist conducting accounting (chief accountant, etc.).

Composition of Financial Reporting

The financial statements of the organization are a system of indicators reflecting the property and financial position of the organization at the reporting date, as well as the financial results of its activities for the reporting period.

The composition and forms of financial statements of organizations are established by the Ministry of Finance of the Azerbaijan.

At present, the annual accounting reports include:

1. Balance sheet - form number 1.

2. Profit and Loss Statement - Form No. 2.

Explanations to the balance sheet and profit and loss statement:

2.1. Statement of changes in equity - form No. 3.

2.2. Statement of cash flows - form No. 4.

2.3. Appendix to the balance sheet - form No. 5.

2.4. Explanatory note.

3. An audit report confirming the reliability of the company's financial statements if it is subject to mandatory audit in accordance with federal laws.

All elements of the financial statements are interrelated and reflect different aspects of the same business transactions and phenomena. The balance sheet contains information about the financial position of the organization on a certain date. The profit and loss account reflects information on the formation and use of the profit organization. The report on changes in capital - data on the movement of the company's own capital, funds and reserves and gives an opportunity to assess the changes occurring in the organization's own capital. The cash flow statement contains information on the cash flow of the organization in cash and non-cash forms. The directions of cash flows are considered in the context of the main activities of the organization: current, investment and financial.

An explanatory note and transcripts to individual indicators of reporting are of great importance for a correct understanding and interpretation of the balance sheet, profit and loss account. The purpose of these elements of financial reporting is to disclose the content and approaches to the formation of certain indicators of financial statements, the accounting policy of the organization.

The explanatory note includes information and additional data not reflected in the forms of the annual financial statements. This information contains a brief description of the organization's activities, key performance indicators and factors that have influenced economic and financial results, as well as data useful for obtaining a more complete and objective assessment of the organization's financial and financial position. An integral part of the explanatory note should be analytical information (indicators of the financial position of the organization).

The organization may submit additional information accompanying the accounting statements useful to users of the reporting. Such information can be presented in the form of analytical tables, graphs and diagrams and include information about the dynamics, the most important economic and financial performance of the organization for a number of years, the development plans of the organization; data on prospective capital and long-term financial investments; characterize the organization's policy with respect to borrowed funds, risk management, the organization's activities in the field of research and development, environmental protection, etc.

Balance sheet

The balance sheet (Form No. 1) is a static document, as it is compiled on a specific date and characterizes the financial position of the organization as of that date. It contains information about the resources (assets), liabilities and own capital of the enterprise (liability). In domestic practice, the balance is usually presented in the form of a two-sided table, the left side of which is an asset, the right side is a liability of the balance sheet. Articles of the asset are located on a specific system, which is based on the degree of liquidity, the articles of liability - on the degree of maturity of obligations. Construction of the asset of the balance of Azerbaijan enterprises is carried out in order of increasing degree of liquidity, liabilities - according to the increasing maturity of repayment (repayment) of obligations.

According to the definitions adopted in the domestic practice, the asset is considered as a property mass (organization funds), which should work and bring profit to the organization, and liabilities - as obligations for the received values (services) that are sources of education and placement of the organization's resources.

Consider the main components of the balance sheet.

Non-current assets include intangible assets, fixed assets and financial investments.

Intangible assets are different rights to objects of intellectual (industrial) property, for the use of separate natural objects, etc. Intangible assets are long-term assets that do not have physical form, but have a value and profit-making organizations. In the reporting, intangible assets are recorded at their residual value.

Fixed assets are long-term assets that provide income to the organization. This type of assets is recorded in the statement of the residual value

Long-term financial investments are defined as long-term investments of the organization in subsidiaries and dependent companies, authorized (joint-stock) capitals of other organizations created on the territory of the Azerbaijan or abroad, government securities, bonds and other securities of other organizations, as well as loans granted to other organizations. Long-term financial investments are shown in the statements in the actual amount of costs for their acquisition.

Current assets include inventories, accounts receivable, financial investments, cash.

Stocks include raw materials, materials and other similar values, costs in work in process, finished goods and goods.

Accounts receivable in the reporting are subject to separation depending on the terms of its repayment for receivables, payments on which are expected more than 12 months after the reporting date (long-term), and accounts receivable, payments are expected within 12 months after the reporting date (short-term) .

Short-term financial investments are a liquid part of current assets and represent a temporary placement of the organization's free cash assets for the purpose of making a profit - the repurchase of own shares from shareholders, investments in securities of other organizations, government securities, etc., and provision of loans to other organizations. In the reporting this type of financial investments is shown at the actual costs of acquisition.

The section "Capital and Reserves" reflects the organization's own capital. As part of the organization's own capital, the charter capital, additional and reserve capital, undistributed profits are taken into account.

Long-term and short-term liabilities represent the borrowed capital of the organization.

Long-term liabilities are liabilities of the organization that are repayable over a period of more than 12 months and include long-term bank loans and other loans.

Short-term liabilities are payable within

12 months by using current assets or refinancing for this purpose by taking other short-term (current) obligations.

Profits and Losses Report

The profit and loss account (Form No. 2) shows the effectiveness of management decisions in the financial and economic sphere of the organization, reflecting and summarizing the income and expenses of the organization.

Consider the main elements of the income statement.

The section "Income and expenses for ordinary activities" includes the following articles:

1. Proceeds (net) from the sale of goods, products, works, services (net of value added tax, excises and similar compulsory payments) shall be determined on the basis of temporary certainty of the facts of economic activity.

2. The cost price of the sold goods, products, works, services is the recorded costs for the production of products, works, services in a share relating to the products, works and services sold in the reporting period.

3. Gross profit is defined as the difference between the proceeds from sales and the cost of goods sold, products, works and services.

4. Commercial expenses show the level of costs associated with the sale of products (works, services) from producers and goods from trading and marketing organizations.

Administrative costs represent a combination of administrative and management costs, expenses for maintenance of general economic personnel, not related to the production process, expenses for the payment of information and consulting services and other similar expenses.

The calculated result obtained from deduction from sales of the cost of sales and management costs, characterizes the profit or loss from sales.

The section "Operating Income and Expenses" includes the following articles:

1. Interest income - accrued (received) interest on bonds, promissory notes, deposit accounts, government securities, loans and borrowings, etc.

2. Interest payable includes accrued (paid) interest on bonds, shares granted to the organization of loans and borrowings, etc.

3. Income from participation in other organizations - income (dividends) from equity participation and financial investments in the authorized capitals of other organizations, dividends on shares of other organizations that are the property of the compiler.

4. Other operating income includes income less the value added tax on the sale and other disposal of fixed assets and other property, securities and foreign currency; income from leasing property; receipts of compensation of expenses for the maintenance of canned production facilities and facilities for canceled orders and discontinued production that did not produce products.

5. Other operating expenses include the residual value of retired fixed assets and other depreciable assets; costs associated with servicing securities; expenses on leasing operations; costs for maintenance of canned production facilities and facilities; costs for canceled production orders and for production that did not produce products; expenses on transactions related to the receipt of operating income; charged amounts of taxes and fees paid in accordance with the law due to financial results.

Non-operating income includes income from write-off of accounts payable and depositors for which the limitation period has expired; receipts for the settlement of previously written-off receivables; restoration of unused reserves for doubtful debts; awarded (recognized debtors) fines, penalties, penalties, other sanctions for violation of economic contracts; receipts, reimbursing losses caused by third parties; the profit of previous years, revealed in the reporting year; The value of the excess inventory taken on inventory, revealed during the inventory; foreign exchange differences arising from the revaluation in accordance with the established procedure of property and liabilities denominated in foreign currency; incomes connected with gratuitous receipt of assets.

Other non-operating expenses include losses from mark-up of inventories, goods and finished goods; uncompensated losses due to outages for external reasons; accrued reserves for bad debts; losses from write-off of accounts receivable and other unreal debts; recognized (awarded) fines, penalties, forfeits, compensation of losses on business contracts; losses on operations of previous years, revealed in the reporting year; losses from writing-off of property shortages revealed during inventory; losses from debt cancellation due to insolvency of the debtor; legal costs; foreign exchange differences arising from the revaluation in accordance with the established procedure of property and liabilities denominated in foreign currency; losses on operations with containers.

The profit tax and other similar compulsory payments is the amount of the profit tax of the organization and other mandatory payments accrued from the beginning of the year in favor of the budget.

Profit from sales in the amount of interest receivable, income from participation in other organizations, other operating income and non-operating income net of interest payable, other operating expenses, non-operating expenses and income tax gives the result of financial and economic activities of the organization - profit or loss from normal activities.

Extraordinary income and expenses are the results of the consequences of extraordinary circumstances of economic activity (natural disaster, fire, accident, nationalization, etc.).

The net profit of the organization for the reporting period or loss is formed on the basis of profit or loss from ordinary activities, taking into account the impact on the result of the consequences of emergency circumstances of economic activity in case of their occurrence.

Statement of cash flows

The cash flow statement (Form No. 3) summarizes the cash flows of the organization. The directions of cash flows are considered in the report in the context of the main activities of the organization - current, investment and financial.

Current (production and economic) activities are activities that bring the main revenue to the organization.

Investment activity is the acquisition and sale of long-term assets and financial investments that do not relate to cash equivalents.

Financial activities - a set of transactions that lead to changes in the size and structure of the organization's own and borrowed capital, with the exception of current accounts payable.

The information contained in the statement of cash flows is required for the assessment of:

- the perspective ability of the organization to create positive cash flows (exceeding cash receipts over expenditures);
- the ability of the organization to fulfill its obligations under settlements with creditors, payment of dividends and other payments;
- the need for additional attraction of funds;
- the effectiveness of operations on the financing of the organization and investment transactions in monetary and non-monetary forms.

The statement of cash flows contains information that complements the balance sheet and income statement. The report provides an opportunity to obtain information on whether the achievement of profitability is ensured by a sufficient inflow of funds necessary to expand operations, and whether the flow of funds satisfies the required liquidity level of the organization. The report reflects investments in subsidiaries and other business entities, capital investments in fixed assets, increase in current assets, contains data on the withdrawal of funds from the investment sphere and provides an idea of the organization's activities to attract financial resources to finance its development and other needs.

Statement of changes in equity

The report on changes in capital (Form No. 4) contains information on the increase in capital in total, including through additional issue of shares, revaluation of property, property growth, reorganization of a legal entity, at the expense of income, and information at the expense of which capital has been reduced. In particular, by reducing the par value of shares, reducing the number of shares, reorganizing a legal entity, at the cost of expenses.

Appendix to the balance sheet

The Appendix to the Balance Sheet (Form No. 5) gives an idea of the performance of the organization, information about which is not available in the above reports. For example, accounts payable and receivable, urgent and overdue, depreciable property, social indicators, etc.

Explanatory note

The explanatory note to the financial report should reflect the features of the organization's activities, the main activities, the average annual number of employees, and the composition of the members of the executive and control bodies of the organization.

Audit report

The audit report should be compiled by an independent auditor and assess the reliability of the information presented in the financial statements.

In simple terms, these are tables that are compiled according to the organization's accounting records. These tables are also accompanied by an explanatory note - a document that is an obligatory component of the financial statements.

The explanatory note should disclose information relevant to the accounting policies of the organization, as well as provide users of reporting with additional data - those data that are not sufficiently disclosed in the tabular form of reporting, but which are necessary for users to assess the performance of the organization.

Structure of financial statements.

One of the normative legal documents regulating the rules of accounting and financial reporting in the Republic of Azerbaijan is the Law on Accounting and Financial Reporting No. i-38 of April 18, 2006. Article 15 of this Law states that the financial statements include:

1) the balance sheet;

2) profit and loss account;

3) a statement of cash flows;

4) statement of changes in equity;

5) an explanatory note.

The new order that approved the forms of financial statements is intended primarily for organizations of public interest, as described in the text of the order. Organizations of public interest are financial organizations, joint-stock companies (except for non-profit organizations), subsoil users (other than organizations that produce common mineral resources) and organizations in whose authorized capitals there is a share of state participation, as well as state enterprises based on the right of economic management .

Does this mean that organizations that do not belong to public interest organizations should compile financial statements in some other forms? Moreover, if we consider some of the financial statements that are available in the new approved forms, they are not intended for ordinary partnerships. The answer is no. The list and forms of financial statements should be applied by all organizations.

So why did you need to cancel the reporting forms that worked before and to which we all had time to get used to?

The need for changes is due to the fact that changes are made to international financial reporting standards, where new terminology is already applied. And also those sections or articles are subject to more detailed disclosure.

And why do you need financial statements? To whom and for what purpose is it needed? Who will watch it?

Simultaneously with the corporate income tax declaration, the payer of corporate income tax submits annual financial statements prepared in accordance with international financial reporting standards to the local tax authority (Author's note: here it should be read or national financial reporting standards) and the requirements of legislation Republic of Azerbaijan on accounting and financial reporting.

In this case, in case of adjusting the previously submitted annual financial statements, the payer of corporate income tax shall, within thirty calendar days from the date of such adjustment, submit the adjusted annual financial statements to the tax authority at the location.

Thus, the obligation to compile and submit financial statements arises in the organization already according to the requirements of tax legislation.

Who else can be a user of financial statements?

1. Leaders.

Any manager needs information about the results of the activity for a certain period that will help him make the right decision that can affect future success.

2. Banks.

Banks may need such information to make a decision on the issue of a loan.

3. Investors.

Investors need information specified in the financial statements to analyze the reasonableness of future investments in a potential customer.

4. Other

Other customers may also need information on financial statements to decide whether to work with potential suppliers or buyers.

1.2 Comparative analysis

Comparative financial analysis is based on comparing the values of certain groups of similar indicators with each other. In the process of using this analysis system, the absolute and relative deviations of the compared indicators are calculated.

The following types of comparative financial analysis were most widely used in enterprise management:

1. Comparative analysis of financial indicators of the company under study with average industry indicators. In the process of this analysis, the degree of deviation of the main results of the financial activity of the enterprise from the industry average is revealed with the purpose of assessing its competitive position on the financial results of management and identifying reserves for

further improving the efficiency of financial activities.

2. Comparative analysis of financial indicators of this enterprise and competitors. In the process of this analysis, the weak points of the company's financial activity are identified with the purpose of developing measures to increase its competitive position in a specific regional market.

3. Comparative analysis of financial indicators of certain structural units and divisions of this enterprise (its responsibility centers). Such an analysis is conducted for the purpose of comparative evaluation and search for reserves to improve the efficiency of financial activities of the company's internal divisions.

4. Comparative analysis of reporting and planned (normative) financial indicators. Such analysis forms the basis of the current financial activity at the enterprise. In the process of this analysis, the degree of deviation of the reporting indicators from the planned (normative) is revealed, the reasons for these deviations are determined and recommendations are made for adjusting certain areas of the company's financial activities.

Comparative financial analysis is one of the important sections of the analysis of financial statements. It allows you to get an idea not only about how the firm looks in comparison with its past position, but also in comparison with other similar firms. for this, it is necessary to compare the results of its activity with the results of another company or the average industry indicators. It is important that the balance sheets of companies are comparable. When intercompany comparisons, it is necessary to take into account the correspondence of dates, the size of firms, the rules for their assignment to a particular industry, and so on.

Comparison of the performance of one firm can show an improvement in the situation, while an intra-industry comparison may indicate relatively poor performance of the company by industry measures.

Comparative analysis of the financial condition of enterprises is of special importance for potential investors, banks, business partners, tax authorities, regional and federal authorities and other stakeholders in the changing economic situation.

1.3 Users of financial statements

The users of the financial statements are physical or legal persons interested in information about the activities of the enterprise. They can be divided into two categories: internal and external users.

Internal users are management personnel, who take various economic and financial decisions in the activities of the enterprise.

For example, on the basis of financial statements, the company's financial plan for the next year is drawn up, production, assortment and pricing policies are being developed, questions are raised about the appropriateness of attracting loans, etc.

External users are persons who are directly interested in the activities of the enterprise (owners, investors, creditors, partners, tax authorities, employees), and persons indirectly interested in it (audit services, consultants, registrars and legislatures, lawyers, press, trade unions).

The main requirement for financial reporting is that it is useful to users. The principle of usefulness of information means:

- relevance, which is determined by the importance, that is, the ability to influence the decisions made, and timeliness (not timely information gets lost its significance, and therefore becomes irrelevant);

- reliability, which is characterized by the adequacy of the reflection in the financial statements of actual results;

- comparability, that is, the possibility of a comparative evaluation of individual indicators or results for several reporting periods.

- intelligibility, defined by the simplicity of construction, compliance with certain standards, accessibility to the understanding of users for whom information is intended;

- the completeness of information, which is characterized by the completeness of the range of indicators required for analysis and decision-making.

CHAPTER 2. TOOLS OF FINANCIAL STATEMENT ANALYSIS

2.1 Horizontal analysis

Horizontal analysis of reporting is a comparative analysis of financial data for a number of periods. This method is also known as "trend analysis".

In the horizontal analysis of the reporting (for example, balance), the indicator (line) is taken and its change is traced for two or more periods. Any identical time intervals can be taken as periods, but usually quarterly analysis or data analysis by year is used for accounting reporting. The number of analyzed periods can vary depending on the specific task, but qualitative analysis is usually possible when the analyzed series has more than 3 periods.

In terms of financial statements, the most common horizontal analysis of the balance sheet, income statement; less often - a statement of cash flows, changes in capital. When analyzing the balance, the change in the value of certain types of property and liabilities during the period under review is traced. When analyzing the profit and loss account, the changes in revenue, costs, financial results are considered.

In horizontal analysis, two approaches are used:

Comparison of the change in absolute values (for example, rubles)

Comparison of changes in relative (percentage) values

Typically, in the report, the analyst uses both approaches. At the same time, a more obvious approach is the analysis of the change in percentages to the previous (or the first) period (for example, "over the last three months, revenue increased by 20%").

The opposite in meaning horizontal analysis is the vertical analysis of reporting, where the comparison is not in chronology (by period), but within the same period as compared with other indicators.

2.2 Vertical analysis

Vertical analysis of financial statements - a technical analysis of financial statements, which examines the ratio of the selected indicator with other similar indicators within the same reporting period.

Vertical analysis (ie analysis of indices of swelling in the vertical direction) is aimed at studying the structure of the property, liabilities, incomes, expenses of the organization. For example, a credible balance sheet asset analysis provides an overview of the share of fixed assets, intangible assets, inventories, receivables and other assets in the company's total assets (vertical analysis of the asset of the balance sheet). Having determined in percentage the share of each indicator in the total result, the analyst has the opportunity to compare the enterprise according to these indicators with other enterprises, which is impossible if you operate with absolute values. In the part of the balance sheet, structural analysis of own and borrowed funds, as well as the composition of borrowed funds by maturity (long-term and short-term liabilities) are carried out. An example of a vertical analysis can be found in the reports of your financial analyst.

As part of the analysis of the income statement, the vertical analysis is used to identify the structure of costs and expenses, determine the share or net profit of expenses in sales revenue.

Vertical analysis, by definition, is carried out within one reporting period. However, after calculating the percentage ratios of indicators, often resort to horizontal analysis, tracing the change in these indicators for a number of periods. For example, a vertical analysis showed that the share of fixed assets as of 31.12.2009 amounted to 40% of the total assets of the organization; as of 31.12.2010 - 45%. In turn, a horizontal analysis shows that over the year the share of fixed assets increased by 5%, i.e. production has become more capital-intensive.

2.3 Ratio analysis

The importance of making an administrative decision is taken by the analysis of the ratio of costs, output and profit. The analysis of the ratio of costs, production and profit (Cost-Volume-Profit; CVP-analysis) (operational analysis) is an analysis on the basis of which positive or negative results of the enterprise's activity are revealed.

With the ratio of costs, output and profit, you can determine the relationship between costs and profit for different sales volumes.

Operational analysis provides information on the influence of constant and variable factors on the expected profit for different volumes of production.

Profit functions:

1) characterizes the economic effect obtained as a result of the activity of production;

2) profit has a stimulating function (can be used to expand production, implement social and technical development of the enterprise, encourage employees);

3) the most important source of budgets of different levels.

The analysis of the ratio of costs, output and profit is aimed at achieving the following objectives:

1. Identifying the impact on profit of a change in the price of products sold.

2. Calculation of the volume of production, which will ensure maximum efficiency in making profits.

3. Identification of the optimal volume of production or purchases, which will correspond to consumer demand.

4. Determine the amount of sales, which will correspond to the calculation of the planned profit.

5. Identify the feasibility of producing goods or their components on their own, whether it is necessary to make purchases on the side.

6. Determination of the minimum and maximum prices for products for a given volume of production and sales.

7. Determination of the minimum price level for a given volume of production, which will avoid losses.

8. Determine the impact of changes in production on the level of profit.

9. Identify the impact of costs or production volume when they change to the expected profit.

10. Risk assessment in the conduct of entrepreneurial activities.

2.3.1 Liquidity ratios

Liquidity is the ease of selling, selling, transforming material or other valuables into cash to cover current financial obligations.

Liquidity ratios are the financial indicators calculated on the basis of the enterprise's reporting (the company's balance sheet - form No. 1) to determine the ability of the company to repay current debt due to available current (current) assets. The meaning of these indicators is the comparison of the amount of the current debts of the enterprise and its working capital, which must ensure the repayment of these debts.

Let's consider the basic factors of liquidity and formulas of their calculation:

Coefficient of current liquidity

Coefficient of fast (urgent) liquidity

Absolute liquidity ratio

Net working capital

The calculation of liquidity ratios allows an analysis of the liquidity of the enterprise, i.e. Analysis of the possibility for the company to cover all of its financial obligations.

Note that the assets of the enterprise are reflected in the balance sheet and have different liquidity. We will rank them in descending order, depending on the degree of their liquidity:

cash in the accounts and in the cash desks of the enterprise;

bank bills, government securities;

current receivables, loans issued, corporate securities (shares of listed companies, bills of exchange);

stocks of goods and raw materials in warehouses;

cars and equipment;

buildings and constructions;

Construction in progress.

Coefficient of current liquidity

Current Ratio or Coefficient of Coefficient or Total Ratio is a financial ratio equal to the ratio of current (circulating) assets to short-term liabilities (current liabilities). The source of the data is the company's balance sheet (form No. 1). The coefficient is calculated by the formula:

Current liquidity ratio = Current assets, excluding long-term receivables / Short-term liabilities

The ratio reflects the ability of the company to repay current (short-term) liabilities at the expense of only current assets. The higher the indicator, the better the solvency of the enterprise. The current liquidity ratio characterizes the solvency of the enterprise not only at the moment, but also in case of emergency.

Normal is the value of the coefficient from 1.5 to 2.5 depending on the industry. Unfavorable as a low, and a high ratio. The value below 1 indicates a high financial risk associated with the fact that the company is unable to sustain pay current bills. A value of more than 3 may indicate a non-rational structure of capital. But at the same time it is necessary to take into account that depending on the field of activity, structure and quality of assets, etc., the value of the coefficient may vary greatly.

It should be noted that this coefficient does not always give a complete picture. Usually, enterprises that have small inventories and have money to pay bills for payment easily can act with a lower coefficient value than companies with large inventories and sales of goods on credit.

Another way to verify the adequacy of current assets is to calculate the liquidity. This indicator is interested in banks, suppliers, shareholders, as the company can face the circumstances in which it will immediately have to pay some unforeseen expenses. Hence, it will need all of its cash, securities, receivables and other means of payment, that is, part of the assets that can be discontinued in cash.

2.3.2 Solvency ratios

Solvency of the enterprise (organization) is the ability of the entity of economic activity to fully and pay its accounts payable. Solvency is one of the key signs of the company's normal (sustainable) financial position.

The solvency of the enterprise consists of two factors:

1. Presence of assets (property and money) sufficient to repay all liabilities of the organization.

2. The degree of liquidity of assets that are sufficient to realize them, if necessary, is to be financed in the amount sufficient to repay the obligations.

When analyzing the former, the organization's net assets (equity) are examined. If the organization has negative net assets, i.e. there is no own capital, it can not in principle pay all of its obligations due to the excess of the amount of the obligation by the amount for all the assets that are held. Such an organization can be solvent in the short term, it can be calculated on current debts, but in the long term the probability of bankruptcy is high.

A more rigid index of the organization's solvency than the availability of equity is the ratio of own funds, approved by the Federal Office for Insolvency (Bankruptcy) (Order N 31-r of 12.08.1994). The ratio of own funds is calculated by the formula

(Equity - Non-current assets) / Current assets

and should be at least 0.1 (which is often unattainable in Azerbaijan and not only in conditions).

If an organization has positive net assets, this does not yet indicate its good solvency. It is necessary to analyze the second of the above factors - liquidity of assets. There may be a situation where there is a discrepancy between the liquidity of assets and the expected maturity of the obligation. For example, an enterprise, on the one hand, has a large proportion of non-current assets that are more difficult to sell (low-liquid assets), on the other, a large proportion of short-term liabilities. In this situation, there may come a time when the organization does not have enough funds to pay off current liabilities.

The solvency of an enterprise from the position of liquidity of assets is analyzed through special financial ratios - liquidity ratios:

current ratio

quick ratio

absolute liquidity ratio

All three factors are calculated from the balance sheet of the enterprise according to one principle: the ratio of current assets of different degree of liquidity to current liabilities. At the same time, the current liquidity ratio is calculated on the basis of all current assets; quick liquidity - using liquid current assets; absolute liquidity - using only highly liquid assets (cash and short-term financial assets). See for details about all liquidity ratios, their formulas and normal values).

Also in practice, you can meet the coefficient of total solvency. Coefficient of General Solvency A.D. Sheremet offers to calculate the following formula: all the assets of the enterprise (except for the debt of the founders) are divided into the liabilities of the enterprise (long-term and short-term).

The enterprise, whose liquidity ratios fit into the adopted standards, can be considered solvent.

2.3.3 Profitability ratios

Profitability Ratios - financial indicators that characterize the profitability of the company.

The coefficients of profitability are calculated on the basis of the data of the profit and loss statement, as well as the firm's balance sheet. As a rule, all these indicators reflect the ratio of the company's net or operating profit to one or another parameter of its activity (turnover, value of assets, own capital).

The most common coefficients are:

Coefficient of profitability of sales

Coefficient of return on assets

Coefficient of return on equity

Coefficient of return on invested capital

When using profitability indicators, one should pay attention to the fact that the same term, often referred to as indicators based on the analysis of net profit, and the indicators used in calculating profit before tax. In most situations, the use of net profit is recommended. The only exception is when it is necessary to compare the efficiency of companies that are in substantially different tax conditions.

In addition, the term "Return on investment" is widely used, which is sometimes used as a substitute for the term "Return on invested capital," sometimes used to refer to the group of the last three of the above indicators, and in some cases indicates a general formula for calculating the profitability of investment.

CHAPTER 3. ANALYSIS OF FINANCIAL STATEMENTS

3.1 Analyzing the Balance Sheet

The balance sheet is the most important form of the accounting (financial) reporting of a commercial organization (enterprise), which allows you to obtain information about the most significant characteristics of its financial position: property, financial stability, solvency and liquidity.

The main instrument for analyzing the financial state are financial ratios - relative indicators, calculated on the basis of accounting (financial) statements and giving an opportunity to get an idea of its individual characteristics.

Coefficient analysis of the balance sheet includes the calculation and comparative evaluation of financial ratios that characterize the property position, financial stability, solvency and liquidity of a commercial organization.

Financial ratios that characterize the property status of a commercial organization are calculated from the balance sheet asset and reflect the structure and dynamics of its assets in the accounting estimate.

Since practically all the financial ratios characterizing the property position are sector specific, they do not have universal recommended values.

The development of recommended values for these indicators is possible only within specific industries.

As a consequence, they are analyzed in dynamics, in comparison with the data of similar enterprises (belonging to the same industry) and industry average indicators. Based on the results of the analysis, a conclusion is made about the rationality of the structure of the property of a commercial organization (the most rational, generally rational, least rational), the reasons for its changes.

Financial stability is determined by the ratio of debt and equity in the structure of the capital of a commercial organization and reflects the degree of its independence from borrowed sources of financing.

The main financial ratios used in the process of assessing the financial stability of a commercial organization are presented in Table. 2 and are based on accounting for the purposes of analysis of equity, short-term liabilities, borrowed capital and own working capital, which can be determined using formulas based on the lines of the balance sheet lines.

Analysis of financial ratios characterizing the financial stability of a commercial organization is conducted in dynamics, in comparison with the recommended values, with the data of other enterprises. Based on the results of the analysis, a conclusion is made about the degree of financial stability of the commercial organization (absolute, normal, satisfactory, unsatisfactory) and the reasons for its change.

Solvency refers to the ability of a commercial organization to settle for all its obligations (long-term and short-term).

As indicators of the assessment of the solvency of a commercial organization, financial ratios can also be used, the main ones of which are presented in Table. 3. At the same time, it should be noted that the coefficients of financial independence, financial dependence, concentration of borrowed capital and debt can be used both for assessing financial soundness and for assessing the solvency of a commercial organization.

Analysis of financial solvency ratios is conducted in dynamics, in comparison with the recommended values, with the data of other enterprises. Based on the analysis, a conclusion is made on the degree of solvency of a commercial organization (absolute, normal, satisfactory, unsatisfactory) and the reasons for its change.

Liquidity of a commercial organization is its ability to settle on its short-term obligations (taken into account for analysis purposes).

The growth in the share of current assets and, accordingly, the decrease in the share of non-current assets in the assets of the commercial organization by 0.007 can also be characterized positively, as they indicate some increase in the mobility of its assets. However, both at the beginning and at the end of the reporting year, a greater share in the property is made up of non-current assets, which is expedient and justified for an industrial enterprise.

The increase in the share of cash and financial investments by 0.036 and the decrease in the share of stocks at 0.047 in current assets are signs of an increase in their liquidity, so they can be given a positive assessment. However, an increase in the share of accounts receivable in current assets by 0.010 is advisable to give an opposite assessment, since this means that an increasing portion of current assets is temporarily diverted from circulation.

Decrease in the share of intangible assets by 0.016 and especially the increase in the share of fixed assets by 0.006 in non-current assets as a whole is quite difficult to give a unambiguously negative assessment, however, the growth in the share of long-term financial investments and deferred tax assets in non-current assets by 0.004 and 0.007, it is advisable to assess the negative, as, as a rule, long-term financial investments involve the diversion of money from circulation for a long time and involve a significant risk and deferred tax assets are characterized by a zero yield.

So, based on the results of the coefficient analysis, it is possible to characterize the structure of the property of this commercial organization at the beginning and the end of the reporting year as a whole as rational, and its changes over the year are mostly positive.

On the one hand, the values of the coefficients of financial independence, financial dependence, concentration of borrowed capital, debt, own funds and mobility of own capital, both at the beginning and at the end of the reporting year, are within the recommended limits, but by the end of the reporting year they vary somewhat the worst side, which are signs of a certain decrease in the financial stability of a commercial organization. However, on the other hand, the value of the share of coverage by own circulating assets of stocks, also being at the beginning and the end of the reporting year within the recommended limits, improves slightly by the end of the reporting year, increasing by 0.001, which indicates a certain increase in the financial stability of this commercial organization. The value of the share of coverage by own circulating assets and long-term loans and loans of reserves does not match the recommended level at the beginning and at the end of the reporting year, having decreased by 0.003 in the reporting year, which is a sign of financial instability of the commercial organization.

Thus, according to the coefficient analysis, it is possible to characterize the degree of financial stability of a given commercial organization as satisfactory, the level of financial risk (in terms of financial stability) associated with its financial and economic activity, both at the beginning and at the end of the reporting year, and their changes in the reporting year - as ambiguous.

The values of all solvency assessment ratios at the beginning and end of the reporting year are within the recommended limits, but by the end of the reporting year there is a small decrease in their solvency, indicating a slight decrease in the solvency of the commercial organization.

Nevertheless, based on the results of the coefficient analysis, the degree of solvency of this commercial organization at the beginning and at the end of the reporting year can be characterized as absolute, which indicates the complete absence of financial risk (in terms of solvency) associated with its financial and economic activities, However, changes in the values of all financial ratios of solvency assessment for the reporting year should be considered as negative.

The values of the liquidity assessment coefficients (with the exception of the quick liquidity ratio (simplified version)) of the commercial organization at the beginning and at the end of the reporting year are within the recommended limits, however, by the end of the reporting year, the values of the average, interim and current liquidity ratios, respectively 0,369,0,370 and 0,370, and the growth of instantaneous, absolute, fast (simplified) liquidity ratios by 0.026, 0.029 and 0.015, respectively. The growth in instantaneous, absolute and fast (simplified) liquidity ratios indicates an increase in the share of short-term liabilities that can be repaid immediately and in the near future. At the same time, the decline in the values of the coefficients of the average, intermediate and current liquidity indicates a slight decrease in the short-term liabilities of the commercial organization to its circulating assets of medium and low liquidity.

So, the results of calculation and estimation of the liquidity ratios of the commercial organization show that its liquidity both at the beginning and at the end of the reporting year can be characterized as normal with ambiguous changes in the values of its valuation indicators, and the level of financial risk (in terms of liquidity) with the financial and economic activities of a commercial organization, can be defined as insignificant. Thus, summing up the results of a coefficient analysis of the balance sheet of a commercial entity (industrial enterprise), one can draw a general conclusion about the sufficient degree of stability of the financial state of a given industrial enterprise and the relatively low level of financial risk associated with its activities.

3.2 Analyzing Income Statements

The income statement describes the financial performance of the organization for the reporting period. In the income statement, data on income, expenses and financial results are presented in an aggregate amount from the beginning of the year to the balance sheet date.

The purpose of the profit and loss account and explanations to it is to provide external users with information:

1) on the results of the organization's activities,

2) sources of profit (causes of loss).

The data on the profit and loss account are used to evaluate the performance of the organization for the period and to forecast the future profitability of its activities. The forecast of future performance is an important indicator. For investors, it means the possibility of receiving dividends in the future, and the amount of such a dividend can be decisive in making a decision to invest. For the creditor, the future yield means the enterprise's ability to pay directly the amount of debt and, in addition, interest for the loan. If the activity is expected to be unprofitable, this situation can be assessed as a threat of non-repayment of debt and impossibility of interest repayment.

To solve the problems of analysis, the income and expenses of the organization, depending on their nature, the conditions for obtaining and the directions of the organization's activities are divided into:

a) income and expenses for ordinary activities. Income from ordinary activities is the proceeds from the sale of products and goods, income associated with the performance of work, the provision of services;

b) operating income and expenses;

c) non-operating income and expenses;

d) extraordinary incomes and expenses.

The usual activity is the activity for which the organization was created.

Operating incomes include non-core activities, for example, sale of fixed assets, other property, which is not a typical activity of the organization.

The distinction between ordinary activities and operating revenues and expenses is relatively arbitrary and is based on established practice. For the purposes of accounting, an organization is permitted to independently recognize revenue as income from ordinary activities or other income, based on the nature of its activities, the type of income and the conditions for obtaining it. For example, an industrial enterprise can sell surplus raw materials, reflecting revenue as revenue or as operating.

The practical approach to dividing these two types of income is conditioned by the requirement of "cleanliness" of the result of the main activity, ensuring comparability of the profitability of the activities of enterprises of one industry. For example, if one enterprise reflects only the sale of finished products as a normal activity, and the other includes the sale of surplus raw materials in a normal activity, the comparison of the profitability of the main activities of enterprises will not give the correct conclusion.

To avoid such problems, as well as for multidisciplinary enterprises, a requirement to disclose ordinary income by type of activity was introduced if the share of income for an individual type of activity is five percent or more of the total amount of income for the reporting period. This allocation allows you to make reporting more transparent for the investor, to determine and compare the profitability of the organization's activities with both the industry average and with the data of other enterprises.

The structure of the profit and loss account allows you to analyze the results of the organization's activities in terms of the sources of their receipt, which is taken into account by the analyst when calculating the forecast of the enterprise's activities. For the purposes of evaluating the performance of the data, data is provided for at least two reference periods at comparable prices. Companies can bring data for three to five reporting periods in order to attract investments. Given the rapidly evolving situation, the presentation of data over a longer period of time is not always appropriate.

The structure of the report is based on the varying degree of probability of repetition of incomes and expenses of the organization in the future.

When calculating the forecast trend of the result of the main activity, the analyst takes into account the information on disclosure of information on the segments of activity, the prospects for the development of sales markets, trends in the activity of the main buyers, especially in cases where the buyer is an affiliated person, etc. In the absence of serious fluctuations in the factors studied, the probability of maintaining the trend is quite high.

The probability of a repetition of the result of financial and non-core activities depends on the source of receipt of such income, therefore they are disclosed in the report additionally. As a rule, the probability of recurrence is lower than for events in the main activity (for example, the sale of fixed assets is not a recurrent operation), but it is high enough.

The probability of repeating extraordinary events is small. To determine the probability of recurrence, a specific situation is assessed.

As you can see, the final profit of all companies is the same. However, from the point of view of investment attractiveness, the most promising company is B, because in the future the repetition of the result of its main activity, with a low probability of repeating extraordinary events, will yield a fairly high overall profit.

For correct conclusions, the comparability of the report data is necessary. If the data for the same period of the previous year are not comparable with the data for the reporting period, then the first of these data is subject to adjustment based on changes in accounting policies, legislative and other regulations. The requirement to take into account the impact of prices is also directed to meeting the comparability requirement.

To form a more accurate forecast of future profitability, the rules of accounting contain a number of requirements:

1) the requirement to disclose information on discontinued activities;

2) the requirement to compile segmental reporting;

3) the requirement to disclose information on transactions with affiliates;

4) the requirement to reflect conditional facts;

5) the requirement to reflect events after the reporting date.

sale of a property complex (enterprise) or a part thereof, representing a combination of assets and liabilities and relating directly to the discontinued operation in concluding a single purchase-sale transaction;

sale of individual assets and termination (performance) in the manner prescribed by the legislation of the Azerbaijan of certain obligations related to discontinued operations;

refusal to continue part of the activity;

reorganization of the enterprise in the form of separation from its membership of one or more legal entities.

Assets, liabilities, income and expenses can be classified as discontinued operations only if they are subject to sale, redemption or retirement in another way as a result of the termination of the activities of the organization.

Data on discontinued operations are not taken into account by the analyst when building a trend to determine the future profitability of the organization, such an exception allows you to make the forecast more accurate.

3.3 Analyzing the Cash Flow Statement

Analysis of the cash flow statement (ODS) allows to significantly deepen and correct conclusions regarding the liquidity and solvency of the organization, its future financial potential, previously obtained on the basis of static indicators in the course of traditional financial analysis.

The main objective of the ODDS is to provide information on changes in the amount of cash and cash equivalents to characterize the organization's ability to generate cash.

The organization's cash flows are classified in terms of current, investment and financial activities. The ODDS shows the movement of the amount of cash taking into account changes in the structure of cash inflows and outflows, taking into account the balance of balances at the beginning and end of the period, which allows to determine the ability of the organization to maintain and generate net cash flow, i.e. excess of the volume of cash inflows over the amount of cash outflows taking into account the balances of balances. The balance of balances allows to manage liquidity, solvency and financial stability of the organization. The direct method of calculation, based on the analysis of cash flow on the accounts of the enterprise:

- allows to show the main sources of inflow and direction of outflow of funds;
- gives an opportunity to make operative conclusions concerning sufficiency of means for payments under current obligations;
- establishes the relationship between sales and cash revenue for the reporting period.

The direct method is aimed at obtaining data characterizing both gross and net cash flow of the enterprise in the reporting period. It is designed to reflect the entire amount of income and expenditure of funds in the context of certain types of economic activities and the enterprise as a whole. Differences in the calculation of cash flows received by direct and indirect method are related only to the operating activities of the enterprise. When using a direct method for calculating cash flows, direct accounting data is used that characterizes all types of receipts and expenditures of cash.

Calculations of the net cash flow of the enterprise for investment and financial activities, as well as for the enterprise as a whole, are carried out using the same algorithms as for the indirect method.

In accordance with the principles of international accounting, the company chooses the method of calculating cash flows independently, but it is preferable to use a direct method to obtain a more complete picture of their volume and composition.

Net cash flows from investment and financial activities are calculated only by a direct method.

The indirect method of calculating net cash flow, based on an analysis of balance sheet items and a report on financial results, allows to show the relationship between different types of enterprise activities; establishes the relationship between net profit and changes in the assets of the enterprise for the reporting period.

The calculation of the company's net cash flow by an indirect method is carried out by types of economic activity and the enterprise as a whole.

In terms of operating activity, the basic element of calculating net cash flow of an enterprise by an indirect method is its net profit received in the reporting period. By making appropriate adjustments, the net profit is then converted to a net cash flow indicator.

CONCLUSION

Financial reporting for analysis is a set of analytical processes that are part of the business analysis. All these processes use financial reports to varying degrees and base their primacy on business analysis.

Having established the primacy of the analysis of accounting and accounting in the analysis of business with all its components, we must highlight their sphere of application from the very constitution, that is, from within.

The volume of financial reporting can be determined in the light of four main activities of the company: planning, financing, investment and work.

- Planned activity of the company is fixed in the business plan, which describes the purpose, strategy and tactics of the company. This plan gives an idea of the current and future prospects of the company in terms of business environment and strategic analysis. He presents information on the competitiveness, movements in the markets and tactics of the company. All these actions contain uncertainty and risk. Analysis of financial statements helps us to assess the extent of this risk. Information about these actions is also disclosed in press releases and various financial and industry publications. Another important source of information is the Letter to Shareholders and the Discussion and Analysis of Management (MD & A).

- The company must raise funds in others to fulfill its plan. There are two main external sources of funds: investors and lenders. The decision on the composition of financial activities, volumes, sources, maturities and the structure of the financing agreement will affect the company's growth, its exposure to risk and determine the strength of outsiders in business decisions. Stock investors demand a return in the form of profit distribution from reinvestment of profits. The distribution of profits is the payment of dividends to shareholders (cash, dividends on shares or redemption of shares). Companies also receive financing from creditors: debtors and operating creditors. The contract with the creditors requires repayment of the loan with interest at certain times. The risk for creditors is the possibility of a business default when repaying a loan and interest.

- Investment activity refers to the acquisition and maintenance of the company's investments for the purpose of selling products and providing services, as well as for investing excess cash. Investments in operating assets are investments for the purpose of running a company's business. Securities in which an excess of cash is invested are financial assets. Investments in short-term assets are called current assets. It is expected that these assets will be converted into cash in the short term. Investments in long-term assets are called non-current assets.

- The operational activity is the "implementation" of the business plan, taking into account its financial and investment activities. They include at least five possible components: research and development, procurement, production, marketing and administration.

Whenever you plan to invest in a company, it is important to understand what it does, its market and the industry in which it operates. You should never blindly invest in a company.

One of the most important areas for any investor, which should be looked at while researching the company, is financial reporting. It is important to understand the purpose of each part of these statements and how to interpret them.

Recall that we learned:

Financial reports are required by law and are published quarterly and annually.

Management Discussion and Analysis (MD & A) gives investors a better understanding of what the company is doing, and usually points to some key areas in which it works well.

Audited financial statements have much more confidence than unaudited financial statements.

The balance sheet lists assets, liabilities and equity.

For all balances: Assets = Liabilities + Share capital. Both sides should always be equal (or balance each other).

The profit and loss account includes such indicators as income, expenses, profit and earnings per share.

For the company, the top line is revenue, and the final profit is net income.

In the income statement, certain non-monetary items, such as depreciation, are recorded.

The statement of cash flows removes all non-monetary items and tells how much actual money was generated by the company.

The cash flow statement is divided into three parts: cash from operations, financing and investment.

Always read the notes to the financial statements. They provide more detailed information on a wide range of indicators presented in the three financial statements.

REFERENCES

Accounting Law of Azerbaijan Republic. Augusts 10, 1995. “Azerbaijan” newspaper. Baku.

Accounting Law of Azerbaijan Republic. September 2, 2004. “Azerbaijan” newspaper. Baku

ADB.2002. *Accounting and Auditing Practices in Selected Developing Member Countries:A diagnostic Study of Azerbaijan,Fiji Islands,Marshall Islands,Philippines and Sri Lanka.Manila.*

*Azerbaijan Republic Tax Code***.** 2016. Baku-Azerbaijan.

Baku Stock Exchange. www.bfb.az (accessed April, 2017).

Barry J. Epstein, Eva K. Jermakowicz. 2008. *Interpretation and application of international accounting and financial reporting standards***.** Wiley IFRS.

Walton, Peter et al. 2003. *International Accounting*. Thomson Learning.

Primary source:

BD Sensors s.r.o (Czech Branch) 2005-2008 Annual Reports.

Books:

Brigham, Eugene F., and Joel F. Houstan, eds. 2004. *Fundamentals of Fiannacial Management.* Ohio: South-Western.

Brigham, Eugene F., and Micheal C. Ehrhardt, eds. 2005. *Financial Management: Theory*

and Practice. Ohio: South-Western.

Brealy, Richard A., and Stewart C. Myers, eds. 2003. *Principles of Corporate Finance*.

Boston: McGraw-Hill/Irwin.

Cannon, Joseph P., Perrault, William D., and McCarthy, E. Jerome. 2008. *Basic Marketing: A Global Managerial Approach*. New York: McGraw-Hill.

Edmonds, Thomas P., Cindy D. Edmonds, Bor-Yi Tsay, Philip R. Olds, and Nancy W. Schneider, eds. 2006. *Fundamental Managerial Accounting Concepts.* Boston: McGraw-Hill/Irwin.

Hermanson, Roger H., James Don Edwards, and R.F.Salmonson, eds. 1989. *Accounting Principles.* Boston: BPI/IRWIN.

McLaney, Eddie, and Peter Atrill, eds. 2005. *Accounting: An introduction*. New-Jersey:

Prentice-Hall.

Ross, Stephen A., Randolph W. Westerfield, and Jeffrey Jaffe, eds. 2008. *Corporate Finance*. Boston: McGraw-Hill/Irwin press.

Spiller, Earl A. and Phillip T. May, eds. 1990. *Financial Accounting: Basic Concepts*.

Boston: Irwin.

Weygandt, Jerry J., Donald E. Keiso, and Paul D. Kimmel, eds. 2002. *Managerial Accounting: Tools for decision making.* New York: John Wiley and Sons press.

Wild, John J. 2008. *Financial Accounting: Information for decisions*. New York: McGraw-Hill/Irwin.

Web Sites:

"*Financial Statement Analysis Limitations*", 24 Apr 2010.

http://www.cliffsnotes.com/study_guide/Financial-Statement-Analysis-Limitations.

topicArticleId-21248,articleId-21214.html (accessed April 22, 2010).