

Techniques (tools or methods) of analysis of financial statements:

Following techniques can be used in connection with analysis and interpretation of financial statements:

1. Comparative financial statements
2. Common size statements
3. Trend percentages analysis
4. Funds flow statement
5. Net working capital analysis
6. Cash flow statement
7. Ratio analysis

1. COMPARITIVE FINANCIAL STATEMENTS: Comparative Financial Statement analysis involves presenting the financial statements like income statement and balance sheet for the current year along with the amounts of the previous year for each component of the statements.

These statements are prepared in a way so as to provide time perspective to the consideration of various elements of financial position embodied in such statements. This is done to make the financial data more meaningful. The statements of two or more years are prepared to show absolute data of two or more years, increases or decreases in absolute data in value and in terms of percentages. Comparative statements can be prepared for both income statement as well as position statement or balance sheet.

Comparative Income Statement: This statement discloses the net profit or net loss resulting from the operations of business. Such statement shows the operating results for a number of accounting periods so that, changes in absolute data from one period to another period may be stated in terms of absolute change or in terms of percentage. This statement helps in driving meaningful conclusions as it is very easy to ascertain the changes in sales volume, administrative expenses, selling and distribution expenses, cost of sales etc.

Comparative balance sheet: this statement, prepared on two or more different dates, can be used for comparing assets and liabilities and to find out any increase or decrease in these items. This facilitates the comparison of figures of two or more periods and provide necessary information which may be useful in forming an opinion regarding the financial position as well as progressive outlook of the concern.

Illustration 1: Tejas Network Ltd presents their profit & loss a/c for the year ending 31st March, 2018. Prepare the Comparative Income Statement for the purpose of analysis:

Tejas Network Ltd
Income statement for the year ending 31st March 2018
(Rs. In Lakhs)

| Particulars | 31/3/17 | 31/3/18 | Particulars | 31/3/17 | 31/3/18 |
|-------------------------|---------|---------|-------------|---------|---------|
| To Materials | 200 | 250 | By Sales | 900 | 1200 |
| To Wages | 300 | 400 | | | |
| To Production Exps. | 75 | 100 | | | |
| To Administration Exps. | 25 | 25 | | | |
| To Selling Exps. | 85 | 75 | | | |
| To Net Profit | 215 | 350 | | | |
| Total | 900 | 1200 | | 900 | 1200 |

Solution:

Tejas Network Ltd
Comparative Income statement for the period ending 31st March 2018
(Rs. In Lakhs)

| Particulars | 2017 (base year) Rs. | 2018 (current year) Rs. | Change in Rupees | Change in Percentage $\frac{\text{Change}}{\text{Base Year}} \times 100$ |
|-------------------------|-------------------------------|----------------------------------|---------------------|-----------------------------------------------------------------------------|
| Sales: | 900 | 1200 | +300 | $\frac{300}{900} \times 100 = 33.33\%$ |
| (-) Material Cost | (200) | (250) | +50 | $\frac{50}{200} \times 100 = 25\%$ |
| (-) Wages | (300) | (400) | +100 | $\frac{100}{300} \times 100 = 33.33\%$ |
| ∴ Contribution | 400 | 550 | +150 | $\frac{150}{400} \times 100 = 37.5\%$ |
| (-) Production o/h | (75) | (100) | +25 | $\frac{25}{75} \times 100 = 33.33\%$ |
| (-) Admin o/h | (25) | (25) | 0 | 0% |
| (-) Selling o/h | (85) | (75) | -10 | $\frac{-10}{85} \times 100 = -11.76\%$ |
| Operating Profit (EBIT) | 215 | 350 | +135 | $\frac{135}{215} \times 100 = 62.79\%$ |

Illustration 2: From the following Balance sheet of Axis Ltd. as on 31.3.2017, prepare Comparative Balance sheet.

| Liabilities | 31/3/16 Rs. | 31/3/17 Rs. | Assets | 31/3/16 Rs. | 31/3/17 Rs. |
|-------------------|----------------|----------------|----------------|----------------|----------------|
| Share Capital | 1,00,000 | 1,00,000 | Fixed Assets | 60,000 | 54,000 |
| Profit & Loss a/c | 24,500 | 32,600 | Investments | 50,000 | 40,000 |
| Debentures | 20,000 | 30,000 | Current Assets | 42,000 | 88,000 |
| Creditors | 7,500 | 19,400 | | | |
| | 1,52,000 | 1,82,000 | | 1,52,000 | 1,82,000 |

Solution:

Axis Ltd.

Comparative Balance sheet for the period ending 31.3.2017

| Equities & Liabilities | 2016 (base year) Rs. | 2017 (current year) Rs. | Change in Rupees | Change in Percentage $\frac{\text{Change}}{\text{Base Year}} \times 100$ |
|----------------------------|-------------------------------|----------------------------------|---------------------|--------------------------------------------------------------------------------|
| Shareholders Funds: | | | | |
| Capital | 1,00,000 | 1,00,000 | 0 | 0% |
| Reserves & Surplus | 24,500 | 32,600 | +8,100 | $\frac{8,100}{24,500} \times 100 = 33.06\%$ |
| Non Current Liabilities | | | | |
| Debentures | 20,000 | 30,000 | +10,000 | $\frac{10,000}{20,000} \times 100 = 50\%$ |
| Current Liabilities | | | | |
| Creditors | 7,500 | 19,400 | +1,900 | $\frac{1,900}{7,500} \times 100 = 25.33\%$ |
| Total | 1,52,000 | 1,82,000 | +30,000 | $\frac{30,000}{1,52,000} \times 100 = 19.73\%$ |
| Assets | | | | |
| Non-Current Assets: | | | | |
| Fixed assets | 60,000 | 54,000 | -6,000 | $\frac{-6,000}{60,000} = 10\%$ |
| Investments | 50,000 | 40,000 | -10,000 | $\frac{-10,000}{50,000} = 20\%$ |
| Current assets | 42,000 | 88,000 | 46,000 | $\frac{46,000}{42,000} = 109.5\%$ |
| Total | 1,52,000 | 1,82,000 | +30,000 | $\frac{30,000}{1,52,000} \times 100 = 19.73\%$ |