
Interpretation of financial statements

2017-18

FINANCIAL STATEMENTS

International Accounting Standards Board requires the following statements:

- ▶ statement of *financial position* (or *balance sheet*)
→ shows assets, liabilities, capital
- ▶ statement of *comprehensive income* (or *profit and loss account*)
→ shows profits and losses of the year

KEY INFORMATION

STATEMENT OF COMPREHENSIVE INCOME

	2014 (£m)	2013 (£m)
Revenue	25.4	21.2
Cost of sales	12.3	11.7
Gross profit	13.1	9.5
Selling expenses	3.2	2.3
Admin expenses	6.4	5.2
Operating profit	3.5	2.0
Finance costs	0.4	0.4
Profit for the year (net profit)	3.1	1.6
Taxation	0.6	0.3
Profit for the year (net profit) after taxation	2.5	1.3

KEY INFORMATION

STATEMENT OF COMPREHENSIVE INCOME

- ▶ *Revenue (or turnover)*: must not include VAT
- ▶ *Cost of sales*: production cost
- ▶ *Gross profit*: revenue - cost
- ▶ *Selling expenses*: commission, advertising, distribution
- ▶ *Administrative expenses*: overheads/indirect costs (e.g., salaries, stationary, ...)
- ▶ *Operating profit*: gross profit - selling & administrative costs
- ▶ *Finance costs*: e.g., interest
- ▶ *Profit for the year (net profit)*: operating profit - cost of finance
- ▶ *Profit for the year (net profit) after tax*: revenue - all expenses - taxes

STAKEHOLDER INTEREST

STATEMENT OF COMPREHENSIVE INCOME

- ▶ *Shareholders*: assess performance and growth of business
- ▶ *Managers and directors*: monitor progress of business
- ▶ *Employees*: employees and representatives seeking wage increases
- ▶ *Suppliers*: suppliers offering trade credit
- ▶ *Government*: estimate taxes (HMRC) and calculate public consumption (ONS)

STATEMENT OF FINANCIAL POSITION

Balance sheet: summary of a firm's assets, liabilities and capital

- ▶ *Assets*: resources that a business owns and uses
 - ▶ current asset: are used up in production (e.g., stocks, raw materials)
 - ▶ non-current asset: are used again and again (e.g., machines)
- ▶ *Liabilities*: debts of a business
 - ▶ short-term: e.g., overdraft
 - ▶ long-term: e.g., mortgage
- ▶ *Capital*: money brought by owners

see worked example at page 369.

$$\text{asset} = \text{capital} + \text{liabilities}$$

KEY INFORMATION

FINANCIAL POSITION (BALANCE SHEET)

	2014 (£m)	2013 (£m)
Non-current assets		
Goodwill	30.5	27.8
Other intangible assets	15.2	11.6
Property, plant & equipment	97.7	94.1
	143.4	133.5
Current assets		
Inventories	8.6	6.7
Trade and other receivables	3.4	3.1
Cash and cash equivalents	3.1	2.7
	15.1	12.5
Total assets	158.5	146.0
Current liabilities		
Trade and other payables	5.5	5.1
Dividends payable	1.2	0.8
Current tax liabilities	6.7	5.7
	13.4	11.6
Non-current liabilities		
Borrowings	24.5	26.1
Provisions	4.1	3.4
Pensions	7.8	6.7
	36.4	36.2
Total liabilities	49.8	47.8
Net assets	108.7	98.2
Shareholders' equity		
Share capital	30.0	30.0
Other reserves	17.7	9.7
Retained earnings	61.0	58.5
Total equity	108.7	98.2

KEY INFORMATION

NON-CURRENT ASSETS

Intangible and tangible assets that are the long-term (> 12 months) resources of the business.

- ▶ *Goodwill*: based on good reputation (returning customer)
- ▶ *Other intangible assets*: brand names, copyrights, trademarks, patents
- ▶ *Property, plant and equipment*:
- ▶ *Investments*: financial assets owned by business (e.g., shares held in other companies)

KEY INFORMATION

CURRENT ASSETS

Liquid assets that belong to the business.

- ▶ *Inventories*: stocks of raw materials, stocks of finished goods
- ▶ *Trade and other receivables*: amount owed to business and likely to be paid < 12 months
- ▶ *Cash at bank and in hand*:

KEY INFORMATION

CURRENT LIABILITIES

Money owed by business and expected to be repaid < 12 months

- ▶ *Borrowings*: short-term loans, bank overdrafts
- ▶ *Trade and other payables*: trade credit owed to suppliers
- ▶ *Dividends payable*: dividends that will be paid
- ▶ *Current tax liabilities*: corporation tax, income tax

KEY INFORMATION

NON-CURRENT LIABILITIES

Long-term liabilities of business (> 12 months)

- ▶ *Other loans and borrowings:*
- ▶ *Retirement pension obligations:* money owed to past employees
- ▶ *Provisions:* future expenditures that arise in contracts or warranties

KEY INFORMATION

NET ASSETS

- ▶ (value of all assets) - (value of all liabilities)
- ▶ same value as *total equity*

KEY INFORMATION

EQUITY

Equity: amount of money owed to the shareholders

- ▶ *Share capital*: amount of money paid by shareholders for their shares when originally issued
- ▶ *Share premium account*: (value of new shares issued) - (nominal value)
- ▶ *Other reserves*:
- ▶ *Retained earnings*:

STAKEHOLDER INTEREST

- ▶ *Shareholders:*
- ▶ *Managers and directors:*
- ▶ *Suppliers and creditors:*
- ▶ *Others:*

KEY TERMS

- ▶ *Finance cost*: interest paid by a business on any borrowed money
- ▶ *Finance income*: interest received by a business on any money held in deposit accounts