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NECESSITY OF ANALYZING FINANCIAL STATEMENTS FOR USERS

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Abstract

Any user of the financial statements, regardless of the level of qualification or professional training, it is necessary that, in addition to the financial statements, a detailed analysis of the economic and financial indicators be made available. This would make the content of the financial statements more understandable and would help decision-makers to make fairer decisions. Nowadays in Albania, the tendency of harmonizing the European Commission's Directive IV with the National Standards and International Financial Reporting Standards is becoming increasingly evident. Users of financial statements (internal or external) are interested in obtaining accurate information about the business-financial business activity. This paper will reflect the way of preparing and interpreting the key financial statements in accordance with International Accounting Standards and International Financial Reporting Standards, coupled with a financial analysis to help the key users of financial statements for decision making.

Keywords: Analysis of financial indicators, financial statements, financial reports, users of financial statements, financial decisions, national accounting standards, international accounting standards

INTRODUCTION

Prior to 1990, the Albanian economy was a demarcated economy and the financial statements were compiled according to the models of typical socialist economies, where the format and rules were strictly defined. Also, the financial statements were intended only for a small group of directors and the financial statement data constituted a state secret. Data processing was done in manual mode, in registers and diaries according to standard models. This made the information in many cases inaccurate and manipulated.

After 1990, as a result of the development of the market economy, the massive privatization of former state economies, the rapid growth of private business and the opening of the Albanian economy to foreign investments, the fundamental change in the accounting information processing and the compilation of the financial statements became imperative financial.

The objective of the financial statements is to provide information about the financial position, financial performance and changes in the financial position of an entity that are usable by a wide range of users in making their economic decisions.

As of January 1, 2008, all businesses registered in the Republic of Albania have the legal obligation to compile financial statements according to National Accounting Standards (NAS) and International Accounting Standards (IAS), namely according to the following breakdown:

1. The subjects of the implementation of international accounting standards are the entities defined in point 3 of Article 4 of Law no. 9228, dated 29.04.2004, "On Accounting and Financial Statements", as amended.

2. Other economic entities which are not subject to the aforementioned law shall be subject to the implementation of international standards when, in the last two years, they exceed these limits:

a) Annual revenues, in the amount of 1 250 000 000 (one billion two hundred and fifty million) ALL:

b) Average number of employees, over 100 employees a year.

The financial statements present the structured financial situation and transactions carried out by the Entity on a designated date (due date 31 December)

Based on the NAS and IAS, the financial statements provide information on:

• Accounting Balance
• Statement of expenses and expenses
• Statement of Capital Movement
• Cash Flow

• Explanatory Notes

Financial statements are needed because they help different users, make fair economic decisions, and understand financial reporting in order to improve decision making.

Users of financial statements

Blank financial users are classified into: In-user users and external users.

(a) Entity managers appointed by the owners of the undertaking to direct the business of the undertaking. Managers use the information of the company's financial statements

To see how the financial situation is now and how it is anticipated to perform in the future. This serves the leaders in achieving business objectives, measuring and controlling set goals and making useful decisions.

(b) The employees of the company are reserved for the right to obtain information about the financial situation of the company, for the fact that their future, careers, and wages depend on the financial situation of the enterprise.

c) Shareholders or business partners seeking information to control how the Objective and Objective Management is performing. They also receive information about earnings and make decisions about the use of profits and the future of the company.

(d) Debtors / Creditors / Suppliers require financial information to undertake, with the purpose of planning the sale of acquisitions from the enterprise in the future. Customers for Purchasing Planning and Future Work Guarantee and Suppliers, for future sales and warranty for bill payments.

(e) Banking and lending institutions (Banks) are interested in the financial results of the enterprise, as they provide short-term (overdrawn) bank financing or long-term financing. For these reasons, banking and credit institutions want to make sure that the enterprise has solvency to pay the loan and interest on the bank within the term.

(f) The state (tax institutions) are interested in obtaining information about the company's profits in order to calculate (measure) tax liabilities such as: Profit Tax, Value Added Tax, Contribution to Social and Health Insurance etc.

(g) Cultural Sports Institutions obtain information about the company's profits in order to seek sponsorships and donations from the enterprise for cultural sports activities.

As we discussed above all stakeholders, the information needed for decision-making is taken from the company's financial statements.

The financial statements are prepared by accounting economists, approved accountants or accounting experts, based on NAS, IAS and the Law on Accounting and Financial Statements.

Below we will present the 2018 balance sheet of an enterprise that has compiled the financial statements under the NAS and the law on accounting.

The Balance Sheet consists of Assets and Liabilities, showing active and passive accounts as at 31 December 2018. The balance sheet is presented in a framed manner, where the total of the asset is equal to the total of the liability and according to the accounting equation:

Own Equity (Net) = Total Assets Balance-Total Liabilities

BALANCE SHEET OF "DELTA LTD"

Year 2018 in 000 All

Balance Sheet Voices	2018	2017
ASSETS		
Current Assets:		
Cash and cash equivalents	2750	3360
Deposits	6865	4635
Accounts receivable	235784	357810
Inventory	137400	150000
Prepaid and deferred expenses	430	210
Production in process	658	385
Total Current Assets	***383787***	***516400***
Non-Current Assets:		
Property, buildings and equipment	957480	786420
Installations, machinery and equipment	89400	43600
Investments	10560	0
Office and computer equipment	1530	2320
Total Non-Current Assets	***1058970***	***832340***
TOTAL ASSETS	**1442757**	**1348740**
EQUITY AND LIABILITIES		
LIABILITIES		
Current Liabilities		
Accounts Payable	253460	135420
Liabilities for employee salaries	15350	13210
Short-Term Borrowings	125870	110400
Payable Dividends	4876	3525
Taxable income tax	650	325
Other payables	428	365
Total Current Liabilities	***400634***	***263245***
Non-Current Liabilities		
Long-Term Debt	286267	186530
Liabilities on borrowed capital	0	0
Total Non-Current Assets	**286267**	***186530***

CAPITAL AND RESERVES		
Share Capital	550434	420325
Reserves (Grants, donations, capital grants)	0	0
Current year profit	185427	132532
Retained earnings	19995	346108
Total Capital and Reserves	**755856**	***898965***
TOTAL EQUITY AND LIABILITIES	**1442757**	**1348740**

Statement of Income and Expenses

01.01.2018-31.12.2018

Voices	**2018**	**2017**
Incomes	**550620**	**490320**
Revenue / Sales	540810	485630
Financial Income	9810	4690
Cost of goods sold	(324271)	(328765)
Gross Profit	***226349***	***161555***
Financial Expenses	(8200)	(5635)
Earnings before tax	***218149***	***155920***
Taxes	(32722)	11748
Net Income	***185427***	***132532***
	0	0
Net Income (Current Year)	**185427**	132532

Analysis of some financial indicators of DELTA LTD

1. Liquidity Ratios
2. Efficiency Ratios
3. Debt Ratios
4. Profitability Ratios

In 000/ALL

FINANCIAL ANALYSIS RATIOS	**2017** Coeff,/%		**2018** Coeff,/%	
I. LIQUIDITY RATIOS				
Current Ratio = Current Assets / Current Liabilities	516400 / 263245	**1.96**	383787 / 400634	**0.95**
Acid Test Quick Ratio = Current Assets - Inventories / Current Liabilities	336400 / 263245	**1.39**	246387 / 400634	**0.61**
Cash Ratio = Cash & Cash Equivalents / Current Liabilities	7955 / 263245	**0.03**	9615 / 400634	**0.02**
II. EFFICIENCY RATIOS				
1.Total Assets Turnover				
Net Sales	490320		550620	

Asset Turnover Ratio =	--	-----------------------------	**0.36%**	------------------------------	**0.38**
	Average Total Assets	1348740		1442757	
	Net Sales	490320		550620	
Fixed Asset Turnover Ratio =	--	-----------------------------	**0.92**	------------------------------	**0.51**
	Average Fixed Assets	832340		1058970	
2.The Accounts Receivable Turnover Ratio					
	Average Accounts Receivable	357810		235784	
Average days of accounts receivables =	--	-----------------------------	**262**	------------------------------	**154**
	Net Sales/360 days	1362		1530	
=	(Beginning Accounts Receivable + Ending Accounts Receivable) / 2				
III.DEBT RATIOS					
	Total Liabilities	449775		686901	
Debt to Asset Ratio =	--	-----------------------------	**0.33**	------------------------------	**0.47**
	Total Assets	1348740		1442757	

Debt to Equity Ratio = Total Liabilities / Equity	449775 / 898965	**0.5**	656901 / 755856	**0.87**
IV.PROFITABILITY RATIOS				
Return on Assets Ratio (ROA) = Net Income / Total Assets	132532 / 1348740	**9%**	185427 / 1442757	**13%**
Return on Equity Ratio (ROE) = Net Income / Equity	132532 / 898965	**14%**	185427 / 755856	**24%**

Specifically

The quick ratio has deteriorated sharply in 2018 against 2017.

The current ratio has deteriorated sharply in 2018 against 2017.

The cash ratio has a slight deterioration in 2018 versus 2017.

Total debt to assets in 2018 has deteriorated compared to 2017.

Total debt to capital in 2018 has deteriorated compared to 2017.

The average days of accounts receivable in 2018 have improved considerably compared to 2017.

Return on Assets (ROA) in 2018 has improved significantly compared to 2017.

Return on Equity (ROE) in 2018 has improved considerably compared to 2017.

CONCLUSIONS

• The process of analyzing the financial statements is very important and comprehensible to make the most accurate and fair decisions.

• Conducting accurate financial analysis enables managers to make important business and financial decisions and serves them to increase financial performance in the future.

• Information obtained from the financial analysis and financial statements serves as a key basis in making accurate decisions both from internal users and external users. .

• Based on the analysis of the financial indicators of the enterprise, the managers conclude their financial situation over a certain period of time and take measures to improve the indicators that have not performed positively.

• All companies are required to prepare financial statements in accordance with the Accounting and Financial Statements Law, National Accounting Standards and International Accounting Standards.

• The legal responsibility for the preparation of financial statements of the enterprise is provided by the executives of the enterprise, who in cooperation with accountants or financiers compile the annual financial statements.

RECOMMENDATIONS

From Balance Sheet voices, the accounts receivable in 2018 decreased, this shows that the company has been able to collect its money.

The Inventory decreased too, this shows that we have sold the stock.

The voice Property, buildings and equipment increased in 2018, which means the company has made new investments.

On the other hand the voice of accounts payable increased in 2018, which shows that the company was not able to pay the suppliers.

The revenue from sales increased in 2018, the profit rate is also higher.

The current ratio in 2018 mean that the company has 0.95 times more current liabilities than current assets. The company was more liquid in 2017 than in 2018, it was easier for company to pay liabilities in 2017 than in 2018. The company should work to collect the account receivable faster.

Acid test shows if a firm has enough quick assets to cover its total current liabilities. In 2018 is lower this ratio, so the firm should sell the long-term assets or use financing (bank loans).

The cash ratio shows how well a company can pay off its current liabilities with only cash and cash equivalents. This ratio in 2018 is 0.02 which means that the company needs more than just its cash reserves to pay off its current debt.

The Asset turnover ratio, this ratio measures how efficiently a firm uses its assets to generate sales, so a higher ratio is always more favorable. In 2018 this ratio is higher than in 2017. However, to see how well a company's assets are being used, it must be compared to other companies in its industry.

The fixed asset turnover ratio is an efficiency ratio that measures a companies return on their investment in property, plant, and equipment by comparing net sales with fixed assets, so it calculates how efficiently a company is a producing sales with its machines and equipment. In 2018 this ratio is lower, so the company should invest in fixed assets to increase the production and consequently the sales.

The accounts receivable ratio measures how many times a business can turn its accounts receivable into cash during a period. So from the reports in 2018 the company is collecting its receivables not as frequently as in 2017.

The debt ratio shows a company's ability to pay off its liabilities with its assets, or how many assets the company must sell in order to pay off all of its liabilities. This ratio is preferable to be lower than higher.

The debt to equity ratio shows the percentage of company financing that comes from creditors and investors. A higher debt to equity ratio indicates that more creditor financing (bank loans) is used than investor financing (shareholders). So this ratio is higher in 2018 than in 2017.

The return on assets ratio measures the net income produced by total assets during a period by comparing net income to the average total assets. This ratio measures how profitable a company's assets are. In our case we have a higher ratio in 2018 so more favorable to investors because it shows that the company is more effectively managing its assets to produce greater amounts of net income.

The return on equity ratio how much profit each dollar of common stockholders' equity generates. In 2018 ROE is higher than in 2017, so this is a good thing for the company and investors see a high return on equity ratio because this indicates that the company is using its investors' funds effectively.

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