

Financial Statement Analysis and

Financial Statement Analysis and Interpretation

Interpretation

1. Purpose

- Financial statement analysis evaluates a company's performance, financial position, and cash flows to support investment, credit, and management decisions.

2. Horizontal Analysis

- Compares financial data across multiple periods to identify trends and growth rates.

3. Vertical Analysis

- Expresses each line item as a percentage of a base figure (e.g., revenue on the income statement, total assets on the balance sheet).

4. Ratio Analysis

- Liquidity ratios** (current ratio, quick ratio): ability to meet short-term obligations.
- Profitability ratios** (gross margin, ROE, ROA): efficiency in generating profit.
- Solvency ratios** (debt-to-equity): long-term financial stability.
- Efficiency ratios** (inventory turnover, receivables turnover): how well assets are used.

5. Limitations

- Ratios can be distorted by accounting policy choices, seasonality, or one-off items, so analysis should always be read alongside the notes to the accounts.

6. Practical Use

- Analysts, lenders, and managers use these techniques together to form a complete picture of financial health rather than relying on any single ratio.