

Introduction to Balance Sheet

Introduction to the Balance Sheet

Fundamental concepts, components, and how to read a balance sheet

1. What Is a Balance Sheet?

Aspect	Description
Definition	A financial statement that presents a company's financial position at a specific point in time.
Purpose	Shows what the company owns (assets), owes (liabilities), and the residual interest of owners (equity).
Key Principle	Accounting Equation: Assets = Liabilities + Equity
Timing	Prepared at the end of an accounting period (e.g., month, quarter, year).

2. The Accounting Equation in Detail

[\text{Assets} = \text{Liabilities} + \text{Shareholders' Equity}]

- Assets:** Resources controlled by the company that are expected to generate future economic benefits.
- Liabilities:** Obligations the company must settle, typically by transferring assets or providing services.
- Equity:** Owners' claim on the assets after liabilities are satisfied (includes contributed capital and retained earnings).

3. Main Sections of the Balance Sheet

3.1 Assets

Category	Typical Items	Presentation Order
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Current Assets	Cash & cash equivalents, marketable securities, accounts receivable, inventory, prepaid expenses	Listed first because they are expected to be converted to cash within 12 months.
Non?Current Assets	Property, plant & equipment (PP&E), intangible assets (goodwill, patents), long?term investments, deferred tax assets	Listed after current assets.

3.2 Liabilities

Category	Typical Items	Presentation Order
Current Liabilities	Accounts payable, short?term debt, accrued expenses, current portion of long?term debt, taxes payable	Listed first because they are due within 12 months.
Non?Current Liabilities	Long?term debt, lease obligations, pension liabilities, deferred tax liabilities	Listed after current liabilities.

3.3 Equity (Shareholders' Equity)

Component	Description
Common Stock / Share Capital	Par value of issued shares.
Additional Paid?In Capital	Amount paid by shareholders above par value.
Retained Earnings	Cumulative net income retained in the business (minus dividends).
Other Comprehensive Income	Items that bypass the income statement (e.g., foreign?currency translation adjustments).
Treasury Stock (if any)	Cost of shares repurchased and held by the company (shown as a negative equity item).

4. Formatting Conventions

Feature	Typical Practice
Vertical Layout	Assets on the top, liabilities and equity below, all aligned to the right for monetary amounts.

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Feature

Typical Practice

Horizontal Layout	Assets on the left, liabilities & equity on the right (both sides must balance).
Currency	Use the functional currency of the entity; indicate the reporting date.
Comparative Figures	Show at least two columns: current period and prior period for trend analysis.
Notes to the Financial Statements	Provide detailed explanations, accounting policies, and breakdowns of line items.

5. How to Read a Balance Sheet

1. Verify the Equation

- Ensure **Total Assets = Total Liabilities + Equity**. Any discrepancy signals a reporting error.

2. Assess Liquidity