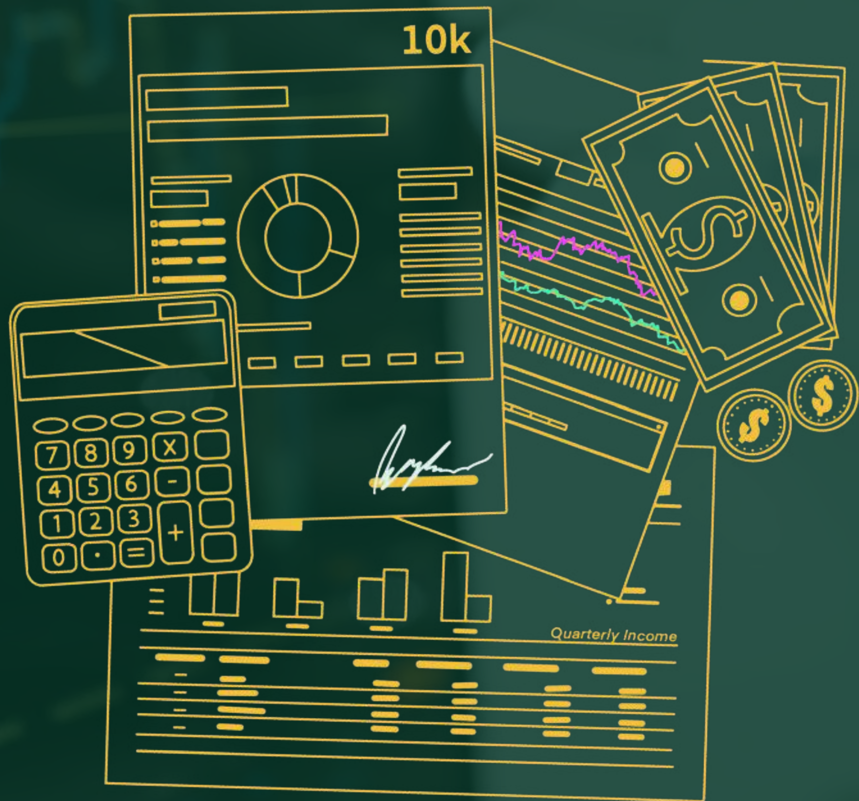
MODULE

Company Financials

This module helps students understand the basics of accounting, which provide crucial insight into how a company is performing. Without proper accounting practices, we would not be able to standardize companies' performances and compare them against each other.

Learn how financials are used to arrive at company valuations which help us better understand a stock's true value - and where the price is likely to move next.



POWERED BY

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Key Takeaways From This Module

Guiding Questions

- Where do companies report their financial progress?
- How can investors track company's growth and future plans?
- How do companies balance and track their revenues vs. spending?
- What is they key information for investors to look out for in company documents?

Enduring Understandings

- How to read and analyze company financial documents
- What accounting is and why companies need to do it.
- The type of information present in financial reports and its relevance.

Basics To Evaluate A Stock

Financial Statements provide the tell all vocals of a company's song (hopefully it's not the blues) or its overall financial performance. The three verses of this company song include the balance sheet, income statement, and statement of cash flows.

Annual Reports not only provide context on an organization's financial performance, but they tell a more comprehensive story about the business, management, and outlook for the future which give investors a more qualitative snapshot of the company.

Quantitatively

Balance Sheet

The *Balance Sheet* displays a company's **assets** (items that represent value), **liabilities** (debt or other financial obligations), and **equity** (value of all outstanding company shares) at a given point in time.

It is called a balance sheet because **Assets = Liabilities + Shareholders' Equity**, regardless of what point in time the equation must remain true.

Income Statement

The Income Statement includes the **expenses** and **incomes** of a company. It represents a **company's performance over a specific time frame**, versus the balance sheet being any given point in time. An extended period of time tells a better story than just any given day.

Statement of Cash Flows

The Statement of Cash Flows simply displays **all cash that flows in and out of the company** over a period in time and is broken into three distinct segments:

- **Investing Activities:** includes the purchase/ sale of long term assets

- **Financing Activities:** includes funds taken in/ paid by businesses to finance its activities

- **Operating Activities:** includes incomes/ expenses related to a businesses' day-to-day operations

Quantitatively Cont..

Here are some metrics that analyze earnings, which is the revenue a company keeps after paying expenses:

Earnings Per Share =
(Net Income - Preferred Dividends)/Equity
Value of company earnings per outstanding share of common stock.

Return on Equity =
Net Income/Equity
Measure of business profitability in relation to equity. The higher the ratio, the better

Price to Earning Ratio =
Share Price/Earning per share
The higher the ratio the more investors are willing to pay for its earnings

Qualitative

While consistent revenue growth is considered to be a factor, non-numerical aspects of the company are also important when analyzing a company as they are intangible, but nonetheless could impact the future values.

Senior Leadership

Leadership that has the right experience or reputation can be an indicator of future success

Pending Litigation

Lawsuits can hurt a company's bottom line and reputation, and may indicate an unworthy investment

Technology Innovation

Technology is a powerful advantage over competition and can signal a successful company

Customer Satisfaction

Ultimately the customer is king. The happier customers are, the more likely the company grows

It All Starts With
The Financials...

Understanding Accounting

What is it?

Accounting consists of **summarizing, analyzing, and reporting financial transactions** to different oversight agencies, tax collection agencies, and regulators. These transactions all get put into **financial statements**, which are a concise summary of all of the company's transactions for a certain timeframe.

Why is it important?

Accounting is necessary for **all types of businesses** because it keeps track of what is happening within the company. The reports that they create through either managerial or cost accounting, **help management make decisions** about the company and are invaluable.

Who does it?

Most basic accounting can be done by a bookkeeper while harder stuff will be handled by certified accountants, who are called **CPAs** or **CMAs** in the US. Some companies **outsource the role** but if the company is big enough there may be **several teams of people dealing with the accounting**.

The Accounting Balancing Act

The accounting equation is the key to EVERYTHING. This equation must always hold true for the financial statements to be valid. This is because every transaction always has two equal parts to it, a **Debit side** and a **Credit side**.

Assets

=

Liabilities

+

Stockholders Equity

Debits & Credits in Accounting

Every transaction a company makes has two sides two it: a **debit** and a **credit**. Whenever an accountant makes any entry into the records they will make at least one debit and one credit entry that will match each other. This ensures that the books are balanced at all times and the accounting equation is satisfied.

Debit

Transactions that **increase the value** of the company are debited

An increase in assets, a decrease liabilities, and expenses incurred are all debited

Credit

Transactions that **decrease the value** of the company are credited

A decrease in assets, an increase in liabilities, and incomes earned are all credited

Reasons Why We Report Financials

**Financial reports are super important to everyone who has an interest in the company.
This includes:**

Management
wants the reports to see their performance and where to improve

Investors
want the report to be able to further analyze the company and its worth

Government
wants to know to ensure you are in compliance of all laws and paying the proper taxes

Employees
want to know the success of their work or if they have pay attached to performance

Key Takeaways From This Module

CORE & FUNDAMENTALS

- Companies are required to report their financials quarterly and annually
- A company's financial statements are a summary of their transactions over a certain period of time.

APPLIED KNOWLEDGE

- The various sections in a 10k summarize a company's yearly financial information
- Companies use accounting to balance and keep track of their assets, liabilities and equity
- The three financial statements(balance sheet, cash flow, income statement) are connected and quantitatively display financial performance

RELEVANCE FOR YOU

- With practice, you will be able to navigate balance sheets with ease.
- Financial reporting provides transparency around company operations, so you as an investor can deeply research a corporation before buying shares.