Chapter – 1
Conceptual Framework of Financial Efficiency

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Chapter-1
Conceptual Framework of Financial Efficiency

1.1 Introduction:

Finance is always being overlooked in financial decision making since it involves investment and financing in short-term period. Further, also act as a restrain in financial performance, since it does not contribute to return on equity (Rafuse, 1996). A well designed and implemented financial management is expected to contribute positively to the creation of a firm’s value (Padachi, 2006). Dilemma in financial management is to achieve desired tradeoff between liquidity, solvency and profitability (Lazaridis et al., 2007). Management of working capital in terms of liquidity and profitability management are essential for sound financial recital as it has a direct impact on profitability of the company (Rajesh and Ramana Reddy, 2011). The crucial part in managing working capital is required maintaining its liquidity in day-to-day operation to ensure its smooth running and meets its obligation (Eljelly, 2004). Ultimate goal of profitability can be achieved by efficient use of resources. It is concerned with maximization of shareholders or owners wealth (Panwala, 2009). It can be attained through financial performance analysis. Financial performance means firm’s overall financial health over a given period of time.

Financial Performance is the snapshot of a position of concern and ability to withstand the ever-changing environment. It is the blue print of the financial affairs of the concern and reveals how a business has prospered under the leadership of its management personnel. In fact, it can be said that financial performance is the medium of evaluation of management performance.

The overall objective of a business is to earn satisfactory returns on the funds invested in it. Consistent with maintaining a sound financial position, an evaluation of such performance is done in order to measure the efficiency of operations or the profitability of the organization and to appraise the financial strength as compared with a similarly situated concern.
Thus, Financial Appraisal is generally directed towards evaluating the liquidity, stability and profitability of a concern which put together symbolizes the financial efficiency of a concern.

1.2 **Meaning of Finance:**

Whenever the word finance strikes your ears, the very first thing that strikes your mind is money. But is the scope of finance merely related to money? Well for a layman, the answer may be yes. But all you need to do is a little pondering and you will easily understand that finance is something much more than money terminologies. It is one of the most sought after courses in business schools and in job sectors. There must be something which makes it so popular and in demand. This article is written to find out few of the reasons behind popularity of finance.

Let us start with a well-structured and qualified finance definition. Academically speaking, “**Finance** is a branch of Economics, which deals with resource allocation and Investment”. Finance deals with matters related not only to money but also with matters related to market. Now this definition certainly expands the domain and scope of finance. And the most crucial part is the inter relativity of this two matters with each other. This interaction is highly dynamic and volatile and also requires high level of insight and expertise to handle the environment. That is the reason of high demand of financial experts.

Finance is the management of money and financial management shows the management of financial activities properly to achieve firm’s goal (wealth maximization). Actually financial management shows the techniques and strategies to determine the need of the fund, to identify the possible and plausible sources of fund, to collect the necessary fund from the identified sources and to invest the collected fund in different profitable sectors by maintaining the principles of finance to achieve the goal of the business firm.

So now we know the importance of finance. Now let us analyze how business schools imbibe these finance definitions in the minds of budding managers. Well we know that there are some predefined rule-sets and frameworks in economics. It is these frameworks
which are taught to the budding managers. Inside this framework, it is the individual's ability, creativity and insight that need application and implementation. With increase in exposure and practice the managers tend to find the best possible approach to different scenarios and hence become efficient managers. It is nothing but trial and error method which is taught to these managers.

1.3 Concept of Efficiency:

When we address ourselves to this question we soon realize that ‘efficiency’ is a very loose term indeed: a host of different concept of ‘efficiency’ come readily to mind. To an engineer ‘efficiency’ may mean the ratio output/input or output/theoretical capacity, percent (thus he speak of the ‘efficiency’ of a machine), while the cost accountant uses the ratio standard cost/ actual cost, percent or its inverse to measure the ‘productive efficiency’ of a firm, department, process or ‘cost Centre’. The economist, when he refers to the efficiency of a firm, generally means one of two rations. The first concerns the firm’s success in producing as large as possible an output from a given set of inputs (or, what amounts to the same thing, producing a given output with the least input); this is called productivity, or technical efficiency. For this purpose it is usual to include as inputs only resources which have physical properties; hence money capital is not generally included, only the things which are bought or hired by means of neither it; nor are such non-material inputs as ‘organization’. The second economic measure recognizes the fact that it is not sufficient for a firm to solve the technical problem of production; it must also suitably adjust its operations to prevailing market prices—in particular the relative prices of its inputs. Accordingly the second measure also a ratio of outputs, is in value terms. Sometimes it takes the form of the ratio value of output/value of inputs (i.e. product prices as well as input prices are introduced), but more commonly prices are only applied to inputs, to give a measure of efficiency in terms of unit costs (or inverse unit costs), which may be seen as the product of the firm’s ‘technical efficiency’ and price efficiency’.

‘Efficiency’ is closely related to security of the working system of a company as whole according to Sudha Nigam. Appraisal is a technique to evaluate past, current and
Projected Performance of a Concern.” It is a powerful applied tool to examine, to measure, to interpret to weigh critically and draw outputs. Different specialist who examines the specific problem with their company does appraisal. Appraisal can be divided into two Parts (I) internal (ii) external. According to Pitt Francis “Internal efficiency of the company not only means making some of having adequate human, Physical and Financial resources but seeing that they are optimally employed.” Thus, the concept of efficiency means the evaluation and performance of a concern included in the appraisal.

1.4 Concept of Financial Efficiency:

Financial efficiency is a measure of the organizations ability to translate to its financial resources into mission related activities. Financial efficacy is desirable in all organization of individual mission. It measures the intensity with which a business uses it assets to generate gross revenue and the effectiveness of producing, purchasing, pricing, financing, and marketing decisions. At the micro level financial efficiency refers to the efficiency with which resources are correctly allocated among competing uses at a point of time. Financial efficiency is a measure of how well an organization has managed certain trade of (risk and return, liquidity and profitability) in the use of its financial efficiency. Financial efficiency is regarded as a measure of total efficiency and a management guide to greater efficiency and the extent of the profitability, liquidity, productivity and capital strength can be taken as a final proof of a financial efficiency. Financial efficiency directed towards evaluating the liquidity, stability, and profitability of a concern which put together of a concern. The word efficiency as defined by the oxford dictionary states that; efficiency is the accomplishment of or the ability to accomplish a job with minimum expenditure of time and effort. As expressed by peter ducker “doing the things the right way is efficiency”. This denotes the fulfillment of the objective with minimum sacrifice of the available scarce resource. Fatless and speedy compliance of the process or system procedure is a measure of efficiency providing a specified volume and quality of services with the lowest level of resources capable meeting that specification, performance measures and or indicators are required. These are including measures, productivity, unit of volume of service etc.
Financial Efficiency is a measure of how efficiently firm’s assets are being used to generate revenue. The operational ratios are also used to measure efficiency.

1.5 Types of Efficiency Measurement:

There are such areas where the efficiency should be modified or improved by effective assessment of various types of activities performed by the business organization in different areas of operations. Those areas of operations may be termed as the areas of performance. The important areas described under the following heads:

1.5.1 Profitability:

Profitability means ability to make profit from all the business activities of an organization, company, firm, or an enterprise. It shows how efficiently the management can make profit by using all the resources available in the market. According to Harward & Upton9, “profitability is the ‘the ability of a given investment to earn a return from its use.’” However, the term ‘Profitability’ is not synonymous to the term ‘Efficiency’. Profitability is an index of efficiency; and is regarded as a measure of efficiency and management guide to greater efficiency. Though, profitability is an important yardstick for measuring the efficiency, the extent of profitability cannot be taken as a final proof of efficiency. Sometimes satisfactory profits can mark inefficiency and conversely, a proper degree of efficiency can be accompanied by an absence of profit. The net profit figure simply reveals a satisfactory balance between the values receive and value given. The change in operational efficiency is merely one of the factors on which profitability of an enterprise largely depends. Moreover, there are many other factors besides efficiency, which affect the profitability.

1.5.2 Productivity:

Productivity is usually defined as a ratio of output produced per unit of resource consumed by the process. "Productivity is a measure of performance in producing and distributing goods and services, value added or sales minus purchases divided by workers employed".10
1.6 Concept of Productivity:

"Productivity means different things to different things to different people. To workers, productivity means a speed up in their work pattern. To union leaders it means the productivity for opportunity to negotiate for higher wages. To management it means increased profitability to consumers and it means better goods at lower costs. To marketing directors productivity improvement increased the firm’s competitiveness abroad by reducing the cost of goods sold in foreign market and to economists; it means an increase in country's standard of living field to gain in output per man hour".

According to Dr. Chauhan P. L\textsuperscript{11}, "Productivity is at the heart of economic growth and development. It is focal point in business and economic matters all over the world. All working people, farmer, a carpenter, a black smith, a technician, businessmen, an engineer, a nurse or doctor, any one is interested in productivity. When any person strives to make a better living for himself and his family, he realizes more on productivity than on hard work". Productivity is the ratio of output to input. Productivity denotes the efficiency with which the various inputs are transformed into the goods and services. Productivity is said to be high when more output is derived from the same input. “Productivity denotes and trend of productiveness of the factors of production, labor, materials, and capital. It is usual today identify this trend as a measure, a ratio or a rate of return, a relationship between output and input over a period of time". Productivity is measured as the ratio between the output of a given commodity or service and the inputs used for that product, which are in the process. And therefore the concept of productivity term that" It should classify and bring order to an intricate array of variable relating to inputs and outputs. But to think of Productivity today is too often unproductive because the term lacks specific definition and general acceptance" Commonly, Productivity, as a source or cause of comparatively high levels of output and improvements in productivity as the major contributors to growth of particular business unit. Thus "Productivity is a rough measure of the effectiveness with which we use the most important productive resources". Productivity therefore, refers to the measurable relationship between well-defined outputs and inputs.
1.6.1 Production and Productivity:

Production and productivity are often not distinguished at all. Just as the Army is not the Navy and the Navy is not the Army. Production and productivity is not the same thing. Production is the amount of the absolute flow of product during a given period. Productivity is the measure of the efficiency in production of factors inputs and / or factor / input services the term 'productivity is used with reference to "The relationship between actual inputs and actual outputs". It is primarily measure overtime, comparing the performance this year with previous years and shows the improvements achieved by the organization. Productivity may also be used to compared production faculties or against bench marks”. According to international labor organization\textsuperscript{12} (ILO) productivity refers to "the effective and efficient utilization of all resources, capital, land, materials, energy, information, and time in addition to labor” There are few confusions about productivity.

Firstly productivity is not only labor efficiency or labor productivity. Secondly misconception is that it is possible to judge performance simply by input. Third with efficiency means producing high quality goods in the shortest possible time but there are requirement of consideration is those goods are needed. Fourthly cost cutting does not always improvement productivity. "It is the Pivot of all the productive economic activities affecting the cost of production and determining all the variables like the prices, wages, salaries and cost of capital and services” thus, increasing productivity means the increasing efficiency of different resources of production with shortest efforts. In other words, along with increase in quantities of factors and inputs, productivity improvements will also be contributing is additional source of output increase. For any given increase in output, improvement of a higher rate of productivity applied for connotes a saving or economy in the requirements of additional supplies of inputs and factors. Generally it can be said that production is an absolute term and refers to the total value of manufactured goods and provision of services produced during a period. Which aim is to satisfy people's wants whereas productivity on other hand denotes as relative terms in relation to the input or resources used in turning out a given amount of output. As well as productivity does not depend upon the increase in production.
1.6.2 Importance of Productivity:

Importance of productivity in contest of the present day competitive world economic environment is the adoption and use of the latest technology and therefore "Productivity is the change in results obtained for the resources expended or productivity change is any alteration in output - input relationships including those resulting from changes in the production process, changes in the methods of using existing processes, changes in the input proportions or input mix and changes in the rate or scale at which existing processes are utilized" It may be true that "in every country developed or developing with a market economy or a centrally planned economy, the main source of economic growth is an increase in productivity. Inversely slackening of growth stagnation and decline entail or are accompanied by a slowdown productivity improvement". Suppose industry is to be the engine of economic growth and modernization as well as competition the chosen paths for improving industrial efficiency, productivity improvements will be the indicators of success. "The National importance of extending economic incentives from standard factory production to services and less standard productive operations is, in the main three fold, there is first the fact that services and underside processes have advanced less in productivity".

Secondly if some operations are paid by piece, others by time, the piece workers are likely to take home much higher earnings than the time workers. Thirdly extending incentive schemes beyond standard factory production lies in the saving of man power. While at the micro level "Productivity finds a prominent place in the business mission of the organization. Discussions revealed that the top Management considers improvements in productivity as vital to the process of developing a competitive edge and generation of adequate internal resources to finance the company's growth."

According to Raman M.V.V "The importance of Productivity lies into understanding effectiveness and efficiency by providing a basis for doing right things, setting objectives, measurement and control, the significance of technology and management in productivity improvements and role of individual managers, get clarified, leading to managerial effectiveness."
1.6.3 **Relationships between Productivity and Efficiency:**

Productivity itself is a sign of efficiency in production. It may be improved when production is carried out with a view to economical manner. Lower productivity shows the waste and inefficiency in the use of resources. High-level productivity results in high level of profits. The sharing level of productivity looks to it that maximum output should take place from whatever minimum input one is engages in the best of a concern depends upon the maximum profit it can draws. According to Gordon K.C.\textsuperscript{16} et al., “with due allowances for temporary current value in fluctuations or changes in commodity of product prices there is strong positive correlation among time series data measuring productivity, profitability or efficiency”.

It means that all these measures indicates a rate of growth in capabilities of organization to fulfill their missions namely to produce and distribute more and better products or services by managing the development and application of technology as well as human resources. According to Alan Lawler\textsuperscript{17} “efficiency is comprehensive measure of how organization satisfy the effectively resources are used to generate useful output”. Generally efficiency can be measured by taking into account the inputs and outputs and therefore productivity is the efficiency and capacity of producing different articles by the raising the rate of productivity or efficiency of the company one can from an idea about its production performance. To sum up production performance measures the level of efficiency.

1.7 **Concept of Profitability:**

Simply, profitability is Profit making ability of a business organization, According to Gibson and Boyer\textsuperscript{18} “Profitability is the ability of the firm to generate earnings” the word Profitability is modulation of two words ‘Profit’ and ‘ability’ Profit is the bottom line of the financial statement of meaning of Profit derives according to the purposes and usages of figures, While term ‘ability’ indicates the power of the business organization to generate Profits. “Ability” is also referred to as” Earning power or “Operating performance of the concerned investment”.

According to Franks and Broyles\textsuperscript{19} “The expected return from the Capital Markets represents an opportunity cost. Since incrementally, companies can employ their funds in the capital market that market provides the appropriate reference point against which to measure profitability. Put another way a profitable investment project is one which provides a return sufficient to attract capital from the Capital Market” while how and up to believes that “The ability of a given investment to earn a return from its use” It may remarked that the ability of Profit making could denote improved or constant during a specific period In accountancy Profitability may be described as a yard stick of firm performance. It is a relative concept, which regulates and controls over management policy and decisions.

1.8 **Profit and Profitability**

Profits and then cream of the business without it may not serve the purpose it’s true the “Profits are useful intermediate become towards which a firms Capital should be directed,” ‘Weston and Brigham\textsuperscript{20} mentioned that “To the financial management Profit is the test of efficiency and a measure of control, to the owners a measure of the worth of their investment, to the creditors the margin of safety, to the government a measure of taxable capacity and a basis of legislative action and the country profit is an index of economic progress, national income generated and the rise in the standard of living” while profitability is an outcome of Profit. In the other words No Profit Derived towards no Profitability. “It may be remarked that the Profit making ability might denote a constant or improved or deteriorated state of affairs during a given period, thus, profit is an absolute connotation whereas profitability is a relative concepts” Profit and profitability are two different concepts, although they are closely related and mutually interdependent, playing distinct role in Business. R.S. Kulshrestha\textsuperscript{21} mentioned that “Profits in two separate business concerns might be the same and yet more often than note their profitability could differ when measured in terms of the size of investment.” As outcome of above statements it can be said that Profitability is broader concept comparing to the concept of Profit. The levels of Profitability help in establishing quantitative relationship between Profit and level of investment or sales.
1.9 Measurement Tools of Profitability:

For taking policy decision under different situations, measurement of Profitability is essential. According to Murthy V. S.22 “The most important measurement of Profitability of a company is ratio i.e. profitability of assets, variously referred to as earning power of the company, return on total investment or total resources committed to operations”. Profitability ratios are calculated to measure the operating efficiency of the firm. According to Block and Hirt23 “The income statement is the major device for measuring the Profitability of a firm over a period of time.” Measurement of profitability is as essential as the earning of profit itself for the business concern. Some managerial decisions like rising of additional finance, further expansion, and problems of bonus and dividend payments rest upon this measurement. It can be measured for a short term and as well as for a long term. The relation to sales is the good short-term indication of successful growth while profitability in relation to investment is the successful growth while profitability in relation to investment is the healthier for long turn growth of the business. Profitability provides overall performance of a company and useful tool for forecast measurement of a company’s performance. “The overall objective of a business is to earn a satisfactory return / Profit on the funds invested in it, while maintaining a sound financial position, profitability measures financial success and efficiency of Management”24. The importance of the analysis of profitability, performance can see from the reality that besides the management and owners of the company, financial institutions, creditors, and bankers also look at its Profitability. Appraisal of performance as regards to profitability can be drawn from interpreting various ratios.

1.10 Ratio Analysis:

To measure the financial efficiency of a company or Industry Ratio-Analysis is a very useful tool which gives the financial condition of company or industry. Ratio Analysis is a concept or technique which is as old as accounting concept. Financial Ratio analysis is a scientific tool to measure the financial condition / efficiency of the firm. It has assumed important role as a tool for appraising the real worth of an enterprise, its performance during a period of time and its pit falls25. Financial Ratio analysis is a vital apparatus for
the interpretation of financial statements. It also helps to find out any cross-sectional and time series linkages between various ratios.

Unlike in the past when security was considered to be sufficient consideration for banks and financial institutions to grant loans and advances, nowadays the entire lending is need-based and the emphasis is on the financial viability of a proposal and not only on security alone. Further all business decision contains an element of risk. The risk is more in the case of decisions relating to credits. Ratio analysis and other quantitative techniques facilitate assessment of this risk.

Ratio-analysis means the process of computing, determining and presenting the relationship of related items and groups of items of the financial statements. They provide in a summarized and concise form of fairly good idea about the financial position of a unit. They are important tools for financial analysis.

Ratio Analysis is used as a way of analyzing the performance of a company. It covers five major areas, namely, (i) Liquidity, (ii) Leverage, (iii) Profitability, (iv) Efficiency, (v) Market Value. Researcher has given detail interpretation in the chapter of Data Analysis and Interpretation.

1.10.1 Liquidity Ratios:

Liquidity Ratios are used to measure the short-term solvency of a company. They show the ability of the company to quickly convert its assets into cash to pay its short-term debts. The higher the ratios, the more liquid the company and the less likely the company experience financial distress in short-term basis.

**Current Ratio** = \( \frac{\text{Current Assets}}{\text{Current Liabilities}} \)

**Interest Coverage Ratio** = \( \frac{\text{Earnings before Interest and Tax (EBIT)}}{\text{Interests}} \)

**Quick Ratio** = \( \frac{(\text{Current Assets - Inventory})}{\text{Current Liabilities}} \)
1.10.2 Leverage Ratios:

Leverage Ratios are used to measure the extent of the company's financing with debt relative to equity and its ability to cover interest and other fixed charges. They address the company's long-term ability to meet its financial leverage. The higher the ratios, the more indebtedness the company owes, which signal the possibility the company will be unable to earn enough to satisfy its debt obligations.

**Long-term Debt/Equity Ratio** = Long-term Debt / Equity

**Total Debt/Equity Ratio** = (Short-term Debts + Long-term Debts) / Equity

1.10.3 Profitability Ratios:

Profitability Ratios measure the overall earnings performance of a company and its efficiency in utilizing assets, liabilities and equity.

**Net Profit Margin** = Net Profit after Taxation / Turnover

**Operating Profit Margin** = Operating Profit / Turnover

**Return on Equity** = Net Profit after Taxation / Equity

**Return on Total Assets** = Net Profit after Taxation / Total Assets

**Return on Capital Employed** = Net Profit after Taxation / (Total Assets - Current Liabilities)

1.10.4 Efficiency Ratios:

Efficiency Ratios demonstrate how efficiently the company uses its assets and how efficiently the company manages its operations.

**Inventory Turnover** = Turnover / Inventory

**Assets Turnover** = Turnover / Total Assets
1.10.5 Market Value Ratios:

Market Value Ratios are used for value comparison. These Ratios are not contained in financial statements and they can only be calculated from publicly traded companies.

Price Earnings Ratio = Current Stock Price / Earnings Per Share (EPS)

Market-to-Book Ratio = Market Value of Equity / Book Value of Equity

1.10.6 Other Fundamental Indicators:

Earnings Per Share (EPS) = Net Profit after Taxation / Issued Common Shares

Dividends Per Share (DPS) = Dividends / Issued Common Shares

Net Asset Value (NAV) = (Total Assets - Total Liabilities) / Issued Common Shares

1.11 Importance of Ratio in Analyses:

A ratio is known as symptom like blood pressure. The pulse rate of the temperature of an individual often ratio analysis is used as a devices to diagnose the financial position of an enterprise\(^3\). It shall point out if the financial condition is very strong, good, partly good, and poor. As such the ratio analysis is a powerful tool of financial analysis through it economic and financial position of a business unit can be fully x-rayed.

Ratio analysis becomes meaningful to judge the financial condition and profitability. Performance of a firm only when there is comparison of present in fact analysis involves two types of comparison. First a comparison of present ratio with past and expected future ratios for the same firm, the second method of comparison involves comparing the ratio of the firm with those of similar firms of with industry average at the same point of time.

Further, “The Ratio Analysis” is presents the figures in which the net result of the financial position and problems are concentrated\(^3\). They provide a co-ordinate frame of reference for the financial manage. They tell the entire story of the ‘Financial adventures
of the enterprise as heap of financial date are buried them. They simplify the comprehensive of financial statistics.

1.12 Limitations of Ratio Analysis:

Every flower of rose has its own beauty in spite of numberless thorns in the same way ratio analysis has a variety of advantages, though it is not free from limitations, some of which are as below:

1. The formula for calculating each ratio is not well standardized.
2. No standard ratios are available for evaluating the significance of each ratio.
3. Ratio ignores non-monetary factors like general economic climate, government and management policies, which vitally affect the financial health of the enterprises.
4. If too many ratios are calculated, they are likely to confuse, Instead of revealing meaningful conclusions.
5. The ratios are generally calculated from the past financial statement and thus, are no indicators of future.
6. Ratios are not exact measure of financial situation as the balance sheet and profit and loss account are based on accounting conventions, personal judgments and recorded facts.

As Ratios are simple to calculate, there is a tendency to over employ them, which lead to accumulation of mass data. However significant the ratio may they cannot replace business efficiency and decision - marking. They do not provide mechanical solution to business problems.

1.13 Trend Analysis

Trend analysis technique is useful to analyze the firm financial position and to put the absolute figures of financial statement in more understandable form over a period of years. This indicates the trend of such variable as sales cost of production, profit assets and liabilities.
The different approaches of trend analysis are as follows.

1. Common size vertical analysis
2. Common size horizontal analysis
3. Trend analysis helps the analyst and management to evaluate the performance, efficiency and financial condition of an enterprise.

1.13.1 **Common Size Vertical Analysis**

All the statement may be subject to common size vertical analysis a figure from the same year’s statement is compared with the basic figure selected from the statement should be converted into percentage to some common base. The common size vertical income statement and balance sheets of selected companies of fertilizer industry covered by this study are given in the study.

1.13.2 **Common Size Horizontal Analysis**

When asking horizontal analysis, a figure from the account is expressed in terms of same account figures from selected base years. It is calculation of percentage relation that each statement then bears to the same item in the base year. Horizontal analysis can help the analysis to determine how an enterprise has arrived at its current position.

The technique of common size statement is very useful when we wish to compare the performance of the industry for presentation of the data in percentage from since it eliminates problems relating to differences in organization size.

1.14 **Comparative statement analysis:**

Statement prepared in a form reflecting financial data for two or more periods are known as comparative statement. The data must first be properly set before comparison in the preparation of comparative financial statement uniformity is essential otherwise comparison will be vitiated. Comparative financial statement is very useful to the analyst because they contain not only the data appearing in a single statement but also information necessary for the study of financial and operating trends over a period of a year. They indicate the direction of the movement in respect of financial position and
operating results. Comparison of absolute figure has no significance if the scale of operation of one company is much different from that of others.

1.14.1 Comparative Balance Sheet

Increase and decrease in various assets and liabilities as well as in proprietor’s equity or capital brought about by the conduct of a business can be observed by a comparison of balance sheets at the beginning and end of the period. Such observation often yield considerable information, which is of value informing an opinion regarding the progress of the enterprise and in order to facilitate comparison a simple device known as the “Comparative Balance Sheet” may be used.

1.14.2 Comparative Income Statement

As income statement shows the net profit or net loss resulting from the operations of a business for designated period of time. A comparative income statement shows the operating result for a number of accounting periods so that changes in absolute data from one period to another may be started in terms of money and percentage. The comparative income statement contains the same columns as the comparative balance sheet and provides the same type of information. As the income statement presents the review of the operating activities of the business and the comparative balance sheet shows the effect of operation of its assets and liabilities. The latter contains a connecting link between the balance sheet and income statement. Income statement and balance sheet are contemporary documents and they highlight certain important facts.

1.15 Fund Flow Analysis

The balance sheet is in the nature of a showing the position of a firm at a particular moment of time. The business process is very dynamic with transactions occurring regularly, each of which affects in some way, the immediately preceding financial position. A balance sheet therefore, merely provides the picture of a fleeting condition at a point of time and if balance sheets drawn at different time are compared any different pound between the closing and beginning figures would be the result of various transaction taking place during the interim period. The business process involves a
continuous inflow and outflow of funds. This funds flow analysis helps the analysis to appraise the impact of the management’s decision on the business during a given period of time\textsuperscript{40}.

1.16 Other Techniques of Analysis

Several other techniques like cash flow analysis and break even analysis are also some time useful for analysis. The use of various statistical techniques is also used frequently for financial analysis, providing a more scientific analysis. The tools generally applied are moving average, index number, range, standard deviation, correlations, regression and analysis of time series\textsuperscript{41}.

Diagrammatic and graph orientations are often used in financial analysis. Graphs provides a simplified way of presenting the data and often give much more vivid understandable of trends and relationships\textsuperscript{42}. Pie graphs bar diagrams and other simple graphs are often used for financial analysis.

1.17 Tools of Financial Efficiency measurement Adopted in the Study:

The data used in the Study of Financial Efficiency of the Steel Industry in India during the period under study have been obtained from the annual reports of the selected Steel companies, CMIE Prowess database i.e. ‘Center for Motoring Indian Economy’ Pvt. Ltd., capital line database, Crisil Research, Minitab and SPSS software used for data collection and analysis. However, they have been supplemented with the secondary data wherever needed and found useful. For the purpose of the study financial efficiency the balance sheet and profit and loss account have been completely rearranged and presented in a 'condensed form'. The condensed profit and loss accounts and 'balance sheet' in a standard form have been given the appendices.

1.18 Significance of Financial Efficiency in Steel Industry of India:

It may be noted that the analysis and interpretation of financial statements represent the last of the four major steps in the realm of accounting. The first three steps, which
involve the work of the accountant in the accumulation and summarization of financial and operating data and in the construction of financial statements, are as follows:

1. Analysis of each transaction to determine the accounts to be debited and the measurement valuation of each transaction to determine the amounts involved.

2. Recording the information in the book of original entry, summarization in ledger, and preparation of trial balance.

3. Preparation of financial statements.

4. The fourth step of accounting the analysis and interpretation of financial statements results in the presentation of information in a manner that will enable business executives, investors and creditors to draw meaningful inferences. The analyst will have a more complete understanding of the significance and meaning of the financial data.

Opinions differ regarding the relative importance of income statement and the balance sheet. To some, it is the income statement, which is more significant, while for others the balance sheet is of greater importance. The fact is that both these financial statements are equally useful in studying and evaluating the results of business activity and their impact upon the financial position of a concern.

A study of any of these statements without referring to the others is futile. The worth of a business is what it earns. But the adequacy of earnings is always judged in relation to the total investments. Hence, a study of earnings without investments or conversely of investments without earnings is devoid of purpose.
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