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3. Concept of performance appraisal
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Business concern needs finance to meet their requirements in the economic world. Any kind of business activity depends on the finance. Hence, it is called as lifeblood of business organization. Whether the business concerns are big or small, they need finance to fulfill their business activities.

In the modern world, all the activities are concerned with the economic activities and very particular to earning profit through any venture or activities. The entire business activities are directly related with making profit. (According to the economics concept of factors of production, rent given to landlord, wage given to labour, interest given to capital and profit given to shareholders or proprietors), a business concern needs finance to meet all the requirements. Hence finance may be called as capital, investment, fund etc., but each term is having different meanings and unique characters. Increasing the profit is the main aim of any kind of economic activity.

In this chapter, the researcher will discuss concept of finance management, financial statement, financial analysis and financial performance appraisal.
1. Concept of Financial Management

1.1 Meanings and Definition of Financial Management:

Financial management is an integral part of overall management. It is concerned with the duties of the financial managers in the business firm. The term financial management has been defined by Solomon, “It is concerned with the efficient use of an important economic resource namely, capital funds”. The most popular and acceptable definition of financial management as given by S.C. Kuchal is that “Financial Management deals with procurement of funds and their effective utilization in the business”.

Howard and Upton: Financial management “as an application of general managerial principles to the area of financial decision-making.”

Weston and Brigham: Financial management “is an area of financial decision-making, harmonizing individual motives and enterprise goals.”

Joshep and Massie: Financial management “is the operational activity of a business that is responsible for obtaining and effectively utilizing the funds necessary for efficient operations.”

Thus, Financial Management is mainly concerned with the effective funds management in the business. In simple words, Financial Management as practiced by business firms can be called as Corporation Finance or Business Finance. Financial management is that managerial activity which is concerned with the planning and controlling of the firm’s financial resources. Though it was a branch of economics till 1890 as a separate activity or discipline it is of recent origin. Still, it has no unique body of knowledge of its own, and draws heavily on economics for its theoretical concepts even today.

The subject of financial management is of immense interest to both academicians and practicing managers. It is of great interest to academicians because the subject is still developing, and there are still certain areas where
controversies exist for which no unanimous solutions have been reached as yet. Practicing managers are interested in this subject because among the most crucial decisions of the firm are those which relate to finance, and an understanding of the theory of financial management provides them with conceptual and analytical insights to make those decisions skillfully.

1.2 Finance Functions

Although it may be difficult to separate the finance functions from production, marketing and other functions, yet the functions themselves can be identified. The functions of raising funds, investing them in assets and distributing returns earned from assets to shareholders are respectively known as financing, investment and dividend decisions. While performing these functions, a firm attempts to balance cash inflows and outflows. This is called liquidity decision, and we may add it to the list of important finance decisions or functions. Finance functions or decisions include:

(A) Investment or long-term asset-mix decision
(B) Financing or capital-mix decision
(C) Dividend or profit allocation decision
(D) Liquidity or short-term asset-mix decision
(E) Evaluation of Financial Performance
(F) Co-ordination with Other Departments:

(A) Investment Decision: Investment decision or capital budgeting involves the decision of allocation of capital or commitment of funds to long-term assets that would yield benefits in the future.

(B) Financing Decision: Financing decision is the second important function to be performed by the financial manager. Broadly he or she must decide when, where and how to acquire funds to meet the firm’s investment needs. The central issue before him or her is to determine the proportion of equity is known as the firm’s capital structure. The financial manager must strive to of
debt and equity is known mix or the optimum capital structure for his or her firm. The firm’s capital structure is considered to be optimum when the market value of shares is maximized.

(C) **Dividend Decision:** Dividend decision is the third major financial decision. The financial manager must decide whether the firm should distribute all profits, or retain them, or distribute a portion and retain the balance. Like the debt policy, the dividend policy should be determined in terms of its impact on the shareholders’ value. The optimum dividend policy is one that maximizes the market value of the firm’s shares.

(D) **Liquidity Decision:** Current assets management that affects a firm’s liquidity is yet another important finance function, in addition to the management of long-term assets. Current assets should be managed efficiently for safeguarding the firm against the dangers of illiquidity and insolvency. Investment in current assets affects the firm’s profitability, liquidity and risk. A conflict exists between profitability and liquidity while managing current assets. If the firm does not invest sufficient funds in current assets, it may become illiquid. But it would lose profitability as idle current assets would not earn anything. Thus, a proper trade-off must be achieved between profitability and liquidity.

(E) **Evaluation of Financial Performance:** It is the responsibility of the financial manager to analyze the financial performance of the enterprise and to report the result to the Board of Directors. This facilitates changes to be made in future policies and plans by pointing out the errors committed. In financial evaluation, current year’s performance is compared with the progress of previous year and conclusions are drawn. This task is performed with the help of modern technique of financial analysis such as inter-firm comparison, ratio analysis, trend analysis, funds flow analysis, cost-volume profit analysis, etc. Evaluation of finance performance shows the progress of a business. This
function is the most important function of financial management, as it reflected financial manager’s ability to generate financials funds, to allocate funds and to make their optimum utilization.

(F) **Co-ordination with Other Departments:** The success of an enterprise depends on the co-ordination with the activities of different departments. Finance function affects each and every activity of a business; therefore, there should be proper co-ordination between the finance department and other departments of an enterprise. It is the duty of finance manager to maintain uniformity in decisions taken by the different departments of the enterprise. This will help in achieving the objectives of the firm.

**1.3 Importance of Finance Management**

Finance is the lifeblood of business organization. It needs to meet the requirement of the business concern. Each and every business concern must maintain adequate amount of finance for their smooth running of the business concern and also maintain the business carefully to achieve the goal of the business concern. The business goal can be achieved only with the help of effective management of finance. We can’t neglect the importance of finance at any time at and at any situation. Some of the importance of the financial management is as follows:

(A) **Financial Planning:** Financial management helps to determine the financial requirement of the business concern and leads to take financial planning of the concern. Financial planning is an important part of the business concern, which helps to promotion of an enterprise.

(B) **Acquisition of Funds:** Financial management involves the acquisition of required finance to the business concern. Acquiring needed funds play a major part of the financial management, which involve possible source of finance at minimum cost.
(C) **Proper Use of Funds:** Proper use and allocation of funds leads to improve the operational efficiency of the business concern. When the finance manager uses the funds properly, they can reduce the cost of capital and increase the value of the firm.

(D) **Financial Decision:** Financial management helps to take sound financial decision in the business concern. Financial decision will affect the entire business operation of the concern. Because there is a direct relationship with various department functions such as marketing, production personnel, etc.

(E) **Improve Profitability:** Profitability of the concern purely depends on the effectiveness and proper utilization of funds by the business concern. Financial management helps to improve the profitability position of the concern with the help of strong financial control devices such as budgetary control, ratio analysis and cost volume profit analysis.

(F) **Increase the Value of the Firm:** Financial management is very important in the field of increasing the wealth of the investors and the business concern. Ultimate aim of any business concern will achieve the maximum profit and higher profitability leads to maximize the wealth of the investors as well as the nation.

(G) **Promoting Savings:** Savings are possible only when the business concern earns higher profitability and maximizing wealth. Effective financial management helps to promoting and mobilizing individual and corporate savings.

Nowadays financial management is also popularly known as business finance or corporate finances. The business concern or corporate sectors cannot function without the importance of the financial management. to evaluate the profitability of the project in the given circumstances, so that a proper decision may be taken to minimize the risk involved in the project.
2. Concept of Financial Statement and Financial Analysis

A financial statement is an official document of the firm, which explores the entire financial information of the firm. The main aim of the financial statement is to provide information and understand the financial aspects of the firm. Hence, preparation of the financial statement is important as much as the financial decisions.

2.1 Meaning and Definition:

According to Hamptors John, the financial statement is an organized collection of data according to logical and consistent accounting procedures. Its purpose is to convey an understanding of financial aspects of a business firm. It may show a position at a moment of time as in the case of a balance-sheet or may reveal a service of activities over a given period of time, as in the case of an income statement.

Financial statements are the summary of the accounting process, which, provides useful information to both internal and external parties. John N. Nyeralso defines it “Financial statements provide a summary of the accounting of a business enterprise, the balance-sheet reflecting the assets, liabilities and capital as on a certain data and the income statement showing the results of operations during a certain period”.

Financial statements generally consist of two important statements:

(i) The income statement or profit and loss account.

(ii) Balance sheet or the position statement.

2.2 Techniques of Financial Statement Analysis:

Financial statement analysis is interpreted mainly to determine the financial and operational performance of the business concern. A number of methods or techniques are used to analyze the financial statement of the
business concern. The following are the common methods or techniques, which are widely used by the business concern.

1. Comparative Statement Analysis
   A. Comparative Income Statement Analysis
   B. Comparative Position Statement Analysis

2. Trend Analysis

3. Common Size Analysis

4. Fund Flow Statement

5. Cash Flow Statement

6. Ratio Analysis

7. Liquidity Ratio

**1. Comparative Statement Analysis**

Comparative statement analysis is an analysis of financial statement at different period of time. This statement helps to understand the comparative position of financial and operational performance at different period of time. Comparative financial statements again classified into two major parts such as comparative balance sheet analysis and comparative profit and loss account analysis.

**A. Comparative Balance Sheet Analysis**

Comparative balance sheet analysis concentrates only the balance sheet of the concern at different period of time. Under this analysis the balance sheets are compared with previous year’s figures or one-year balance sheet figures are compared with other years. Comparative balance sheet analysis may be horizontal or vertical basis. This type of analysis helps to understand the real financial position of the concern as well as how the assets, liabilities and capitals are placed during a particular period.
B. Comparative Profit and Loss Account Analysis

Another comparative financial statement analysis is comparative profit and loss account analysis. Under this analysis, only profit and loss account is taken to compare with previous year’s figure or compare within the statement. This analysis helps to understand the operational performance of the business concern in a given period. It may be analyzed on horizontal basis or vertical basis.

2. Trend Analysis

The financial statements may be analyzed by computing trends of series of information. It may be upward or downward directions which involve the percentage relationship of each and every item of the statement with the common value of 100%. Trend analysis helps to understand the trend relationship with various items, which appear in the financial statements. These percentages may also be taken as index number showing relative changes in the financial information resulting with the various period of time. In this analysis, only major items are considered for calculating the trend percentage.

3. Common Size Analysis

Another important financial statement analysis technique is common size analysis in which figures reported are converted into percentage to some common base. In the balance sheet the total assets figures is assumed to be 100 and all figures are expressed as a percentage of this total. It is one of the simplest methods of financial statement analysis, which reflects the relationship of each and every item with the base value of 100%.

4. Fund Flow Statement

Funds flow statement is one of the important tools, which is used in many ways. It helps to understand the changes in the financial position of a
business enterprise between the beginning and ending financial statement dates. It is also called as statement of sources and uses of funds. Institute of Cost and Works Accounts of India, funds flow statement is defined as “a statement prospective or retrospective, setting out the sources and application of the funds of an enterprise. The purpose of the statement is to indicate clearly the requirement of funds and how they are proposed to be raised and the efficient utilization and application of the same”.

5. Cash Flow Statement

Cash flow statement is a statement which shows the sources of cash inflow and uses of cash out-flow of the business concern during a particular period of time. It is the statement, which involves only short-term financial position of the business concern. Cash flow statement provides a summary of operating, investment and financing cash flows and reconciles them with changes in its cash and cash equivalents such as marketable securities. Institute of Chartered Accountants of India issued the Accounting Standard (AS-3) related to the preparation of cash flow statement in 1998.

6. Ratio Analysis

Ratio analysis is a commonly used tool of financial statement analysis. Ratio is a mathematical relationship between one number to another number. Ratio is used as an index for evaluating the financial performance of the business concern. An accounting ratio shows the mathematical relationship between two figures, which have meaningful relation with each other. Ratio can be classified into various types. Classification from the point of view of financial management is as follows:

● Liquidity Ratio
● Activity Ratio
● Solvency Ratio
● Profitability Ratio

7. Liquidity Ratio

It is also called as short-term ratio. This ratio helps to understand the liquidity in a business which is the potential ability to meet current obligations. This ratio expresses the relationship between current assets and current liabilities of the business concern during a particular period.

2.3 Limitation of financial statement:

The summary of accounts maintained by a business lump is presented in the form of financial statements. The amounts expressed in these statements are based on vouchers and accounting records. Hence decisions based on these information are more true and logical. However, the conclusions drawn on the basis of these information cannot be treated as final and accurate, because there are certain limitations to the financial statements. One must, therefore, keep in view these limitations while studying the profit and loss account and balance sheet of firm. Important and impact bearing limitations of financial statements are identified as below:

(A) Lack of Precision:

The information furnished by financial statements are not precise as they are prepared according to the concepts and conventions developed by the accounting profession and personal judgment of the accountant. On account of this reason, the financial position as disclosed by these statements is not realistic and cannot be measured precisely.

(B) Lack of Exactness:

These statements do not disclose fair value of the business. Different fixed assets are shown in the balance sheet at cost after deducting accumulated depreciation based on estimates. This value is quite different from the market value of the fixed assets. Thus, the value of the fixed assets as disclosed in the
balance sheet in not their realizable value but historical costs. Similarly, the profit disclosed by profit and loss account is also not a real profit from the economic point of view because a number of items shown there in such as depreciation, closing inventory, bad debts etc. are just estimates. These estimates depend on the competence, experience and logic of the accountant.

(C) Incomplete Information:

The information disclosed in the financial statements is not complete. Only that information, which can be expressed in monetary terms, is disclosed in these statements. We remain completely in the dark about such information which cannot be disclosed in monetary terms, though it has a great impact on the financial position of the business.

(D) Hiding the Real Position or Window Dressing:

Window dressing of the balance sheet and/ or creation of secret reserves also hide the real position or state of affairs from the management. Window dressing is, as it was, an ugly woman’s resorting to good dress and make-up to show herself faire that what she is. Secret reserve on the other hand, is a beautiful lady’s efforts to show herself not so far as she actually is, by shabby dress and make-up. By some accounting adjustments (manipulations) a firm’s position may be reflected through its balance sheet in a way better (window dressing) or worse (secret reserves) than what it actually is.

(E) Lack of Comparability:

The comparability study of the financial statements of two firms is not possible on account of the different accounting periods, methods and procedures followed and the nature of business. Similarly, price-level changes are also a factor contributing towards incomparability. The existing
accounting system results in over-statement of profit in times of inflation and under-statement in depression.

(F) Historical Costs:

Financial statements are prepared on the basis of past records which becomes historical by the passage of time. They fail to take into consideration the inflationary conditions. Therefore, the values shown in the financial statements are historical costs and not the current values. These statements are not prepared keeping in view the present economic conditions. That is why, it is said that they are post-mortem reports of the past events.

2.5 Relationship between Financial Statements and Financial Analysis:

Financial statements are only the mean providing general information regarding operational results and financial position of a business firm. These statements merely contain financial data about business events which do not reveal any significant conclusions such as efficiency of the management, strength and weakness of the firm, index of future progress etc. Therefore, their meaning and significance cannot be known till their users do not analyse and interpreter them for their specific purpose. Financial analysis is a multipurpose and multidimensional technique which involves a systematic and careful examination of information contained in the financial statements for a certain period. The use of this technique is an art which requires pertinent knowledge, experience and intuition for its development.

Financial analysis refers to the process of the critical examination of the financial information contained in the financial statements in order to understand and make decisions regarding the operations of the firm. The financial analysis is basically a study of the relationship among various financial facts and figures as given in a set of financial statements. The basic financial statements contain a whole of lot of historical data. The complex figures as given in these financial statements are dissected/broken up into
simple and valuables elements and significant relationships are established between the elements of the same statement or different financial statements. This process of dissection, establishing relationship and interpretation thereof to understand the working and financial position of a firm is called the financial analysis.

2.6 Meaning of Financial Analysis:

“Analysis of financial statements is the systematic numerical calculation of the relationship between one fact the other to measure the profitability, operational efficiency and growth potential of the business.” The analysis of such statements provides valuable information for managerial decision. Thus, the analysis of financial statements is basically a study of the relationship among various financial facts and figures as given in a set of these statements. The basic financial statements i.e. balance sheet and income statements, contain a whole lot of historical data. The complex figures, as given in these financial statements, are broken into simple and valuable elements and significant relationships are established between the elements of the same statements or different financial statements with the help of various techniques of financial analysis.

In the word of Metcaff and Titard, “Analysis of financial statements is a process of evaluating the relationships between component parts of financial statements to obtain a better understanding of a firm’s position and performance”.

2.7 Significance of Financial Analysis:

The analysis of financial data highlights upon the significant facts and relationships concerning various aspects of financial life of business entity. So, every person who has interest in business entity likes to take decisions
based on analyzed financial statements. The following factors enhance the significance of the analysis and interpretation of financial statements:

(A) **Disclosure of Facts:** With the help of financial analysis, all facts relating to liquidity, position, financing of fixed assets, credit policy, and quantum of working capital, solvency, and valuation of assets are made available. Thus, as a result of analysis, all undisclosed facts come to light for the benefit of all concerned parties.

(B) **Effective Planning and Control:** The analysis of financial statements provides adequate information for planning and controlling the affairs of the business. Future forecasts can easily be made by analyzing the past data with the help of information. The management can take corrective actions by drawing interfaces about routine activities.

(C) **Measures Operational Efficiency:** The management and the owners are interested in knowing about the operational efficiency of different activities of the concern. This can be judge by calculating different activity and profitability ratios.

(D) **Comparative Study:** With the help of financial analysis, business information and facts can be presented comparatively. Such presentation is made either in the form of last few years, showing position of the business or comparison of operating activities with other business engaged in the same industry. Thus, financial analysis is helpful in the comparative study of business efficiency.

2.8 **Limitations of Financial Analysis:**

Financial analysis has certain limitations which are as follows:

1) Financial statements suffer from variety of weakness. Such as assets are disclosed in the balance sheet as historical cost which is different from current cost. Financial statements suffer from these weakness, hence the
analysis based upon these statements can not be said to be always reliable.

2) Accounting is not an exact science, so it does not comprise universally accepted terminology. Different meanings are assigned to a particular term. Depreciation is provided by different methods and interest is charged at varied rates. In this way, there are a lot of chances of manipulation. As a result, financial analysis may be proved to be defective.

3) Financial analysis is the quantitative measurement of the performance of the firm. It does not disclose the skill, technical know-how and the efficiency of its employees and managers. It means that analysis of financial statements measures only the financial performance of the business. It completely ignores human aspect.

4) The results disclosed by financial statements may be misleading, if the price level changes are not taken into consideration. The gross profit ratio may improve with the increase in prices, whereas, actual efficiency may not improve. If prices of commodities differ, the ratios of two year will not be meaningful for comparison. Changes in price affect cost of production, sales and values of assets; thereby the comparability of ratios suffers.

5) Financial analysis shows the trends of the affairs of business. It may spot symptoms of financial weakness and operational inefficiency which cannot be accepted. A final decision in this regard will require further investigation and thorough diagnosis.

3. Concept of Performance Appraisal:
Important of performance appraisal is increasing day to day as all the active participants do become interested in varying degree in the performance of business enterprise.

3.1 Meaning of Performance Appraisal:

The phase ‘Performance appraisal’ is composed of two words i.e. ‘Performance’ and ‘Appraisal’. The word ‘performance’ is used to mean the efforts extended to achieve the targets efficiently and effectively. The dictionary meaning of performance refers to ‘achievement’. “The achievement of target involves the integrated use of human, financial and natural resources.”10 Performance directly reflected the disposition and utilization of resources.

Kohler Erich L. refers to performance as “a general term applied to a part or to all of the conduct of activities of an organization over a period of time, often with references to some standard such as past or projected costs, an efficiency base, management responsibility or accountability, or the like.”11

Appraisal refers to a critical review with a view to improving performance. It compares the actual performance with targets fixed, identifies cause of significant variations, and devises corrective actions. This is naturally turned to assessing whether the business operations would be safe, profitable, and appropriate in a given economic situation. Each business enterprise is assessed on its own merits.

The term ‘performance appraisal’ may be defined as a critical assessment or evaluation of various activities in different areas of operations of an organization. It includes planning as to what should be achieved by organization, comparing actual performance against what was expected and making a judgment on the quality of that performance, having regard to the actual circumstances under which it was achieved.
3.2 Performance Appraisal Through Financial Statement Analysis:

Financial Statements indicate the operating result and financial position of a concern; therefore, by analyzing and interpreting these statements, performance can be appraised. For this purpose analysis of financial statements is made. Financial statements analysis is a preliminary step towards the final evaluation of the results drawn by the analyst or management accountant. Appraisal or evaluation of such results is made thereafter by management. Financial statement analysis is the process of scientifically making a proper, critical and comparative evaluation of the profitability and financial position of the concern. According to Metoalf and Titard, “Analysis of financial performance is a process of evaluating relationship between component parts of financial statements to obtain a better understanding of a firm’s position and performance.”

Evidently, “Performance appraisal is the end of continuous accounting cycle which starts with the classification, recording, summarizing, presentation and analysis of data and ends with the interpretation of results obtained critical thereof.”

The financial statements contain all data relating to operating results and financial position of the business. Besides this, other documents such as reports, schedules and explanatory notes are also appended. Overall performance of the business is appraised by analyzing these statements; hence, the process of financial statement analysis is the key process of performance appraisal. The process of performance appraisal through financial statement analysis is summarized below:

- Some logical arrangement of financial data in an orderly sequence in condensed form is made. The balance sheet and profit and loss account figures are rearranged to facilitate performance appraisal.
Figures are approximated to the nearest thousand or lakh to simplify the process of appraisal.

The appraisal of performance is designed to make careful study of past financial records in the light of economics already experienced so as make an orderly attempt to make an informed guess to future probabilities.

The analyst should utilize his knowledge of financial statements to draw up performance appraisal programmed which must be tailored to fit in the specific needs.

3.3 Application of Appropriate Techniques:

3.3.1 The Techniques of appraisal of Efficiency

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3.3.2 Ratio Analysis As a Tool Of Efficiency Appraisal

A Ratio analysis means the process of computing, determining and presenting relationship of items and groups of items in the financial efficiency. Ratio express the numerical relationship between two figure. Accounting ratios are used to describe significant relationships, which exist between figures shown on a balance sheet, in a profit and loss account, in a budgetary control system or in any other accounting organization. The technique of ratio
analysis involves four step viz, determining the accounting ration to be used, comparison of ratio with the standard set and interpretation. An analyst has to determine which ratio is to be used, then he/she computes it and compares it with standards but no such standards have been setup by the Indian industries till today. The interpretation of ratio requires careful detailed study and sound judgment on the part of analysis.

3.3.3 Significance of Ratio Analysis

The significance of the ratio analysis depends on the purpose of which it is made by the analyst. The important points of significance are as under.

➢ A useful tool in the hands of management.
➢ Inter-firm comparison is possible.
➢ Trend Analysis may be easier.

3.3.4 Limitations of Ratio Analysis

Ratio Analysis suffers from a number of draw backs Difficulty in comparison due to

1. Different procedures and practice followed by different firms.
2. Different accounting periods.

3.3.5 Classification of Ratios

Ratio can be classified into two different categories depending upon the basis of classification

A. The Traditional classification
B. Classification Based on Nature of Ratios.

A. The Traditional Classification

The traditional classification has been made on the basis of the financial statements to which the determinates of a ratio belong on this basis the ratio could be classified as

(i) Profit and Loss Account Ratio  Ratios are calculated on the basis of the items of Profit and Loss Account only.
(ii) Balance Sheet Ratio are calculated on the basis of the figure of balance sheet only.

(iii) Compensative Ratio are calculated on the basis of Profit and loss account as well as balance sheet.

B. Classification Based on Nature of Ratio

To get a correct view of the profitability and financial soundness of a firm and to make a systematic study. Ratio are classified as under

(i) Liquidity Ratio This ratio indicate liquidity position of a company. These ratio shows the ability of a company to meet its short-term obligation. Current ratio, liquidity ratio and quick or acid-test ratio are included in liquidity ratio.

(ii) Leverage Ratio or Structural Ratio These ratio are used to judge the long term financial position of the firm. These ratio indicates the funds provided by the long-term creditors and owners. Leverage ratio are calculated from balance-sheet items. Leverage ratio are (i) Debt equity ratio (ii) Gearing Ratio (iii) Debt to total Capital Ratio.

(iii) Coverage Ratio The coverage ratios measure the relationship between what is normally available from operations of the firms and claims of the outsiders. Coverage Ratio include
a. Interest Coverage Ratio
b. Dividend Coverage Ratio
c. Total coverage Ratio

(iv) Profitability Ratio Profitability ratio are calculated to measure the management’s overall efficiency. Various other parties like creditors, share holders, prospective investors, bankers, financial institutions and the Government are also inserted in analysis of the profitability of a company. Therefore the following ratio can be computed to analyze the profitability.
(v) **From Management Point of View** The management is mainly interested in finding out the amount of profit in comparison with sales ratio are mostly computed

1. Gross Profit Ratio
2. Net Profit Ratio
3. Operating Ratio
4. Operating Profit Ratio
5. Return on net capital Employed
6. Return on shareholders Funds
7. Return on Total Assets
8. Return on Gross Capital Employed
9. Return on Paid-up Share-Capital

(vi) **From Share holder’s Point of View:** Share holders of the company are interested in the profitability a company as the earning are distributed amount them in the form of dividend. If the amount of earning is higher the rate of dividend will naturally be higher. For this purpose the following ratio are computed.

1. Earning Per Share
2. Dividend Per Share
3. Dividend Payout Ratio
4. Price Earning Ratio

(vii) **From Creditor’s Point of View:** Bankers, financial institutions and trade creditors look at the profitability ratio as an indicator whether or not the company earns substantially more for the payment of their interest and principal amount.

**3.3.6 Comparative And Common Size Income Statement Analysis**

Profitability analysis is very useful to comparative basis, so, it is paramount importance that a series of statements over a period of years should be used. Comparative and common size income statement is the simplest
technique, the figure of net sales is taken equal items are computed likewise. The statements so prepared provides a common basis for comparison as such the statement is termed as the common-size statement. The tent revealed by common-size is more authentic as it shows. “Qualitative Assessment” as opposed to “Quantitative Assessment” shown by absolute figures.\textsuperscript{14} This statement shows two important problems, which are as under

(1) It follows the concern of widely differing size to be directly compared.

(2) It allows an accurate comparison of financial activities of a company which have greatly changed in size over a few years.

\textbf{3.3.7 Trend Analysis}

Trend analysis is immensely helpful in making comparative study of the changes in an item of groups of items over a period of time and to make conclusions regarding the change in data. For this purpose, a base year is selected and the amount of the item relating to the base year is taken equal to a hundred. The technique of trend analysis over a period of time, Relating to this Anthony rightly noted that “If the values for other periods, this comparison is called a horizontal or trend analysis.” This technique shows the direction in which a concern is going on and on this basis a forecast for the future can be made in this technique.

\textbf{3.3.8 Comparative Financial Statement}

Comparative financial statements are statements of financial position of a business designed to provide time perspective to the consideration of various elements of financial position embodied in such statements comparative statements reveal following

(i) Absolute data (Money value rupee amounts)

(ii) Increase or reduction in absolute data (in terms of money values)

(iii) Increase or reduction in absolute data (in terms of percentage)

(iv) Comparison (in terms of ratios)

(v) Percentage of totals.
3.3.9 Comparative Profit And Loss Account

A comparative income statement / profit and loss account shows the absolute change from one period to another. Since the figures are shown side by side, the user can quickly understand the operational performance of the firm in different periods and draw conclusions.

3.3.10 Comparative Balance Sheet

Balance sheets as on two or more different dates are used for comparing the assets, liabilities and the net worth of the company. Comparative balance sheet is useful for studying the trends of an undertaking.

3.3.11 Standard Costing

“Standard costing” is a technique which uses standards for costs and revenues For the purpose of control through variance analysis. Standard is a predetermined measurable quantity set in defined conditions against which actual performance can be compared, usually for an element of work operation or activity. Standard costing involves the setting of predetermined cost estimates in order to provide a basis for comparison with actual costs. A standard cost is a planned cost for a unit of product or service rendered. Standard costing is universally accepted as an effective instrument for cost control in industries. Although the terms budgeted and standard cost are sometimes used interchangeably, budgeted costs described the total planned costs for a number of products. Usually budgetary control is operated with a system of standard costing because both systems are inter-related but they are inter-dependent.

3.3.12 Budgetary Costing

Budgetary costing is defined by the terminology as “The establishment of budgets relating the responsibilities of executives to the requirements of a policy and continuous comparison of actual budgeted results, either to secure by individual action the objectives of that policy or to provide a basis for revision.”
This definition clearly lays down that budgetary cost requires the establishment of budgets relating the responsibilities of executives to the requirements of a policy. Budgetary cost thus involves the preparation of budgets and their application for control purposes. Accordingly, there cannot be cost without budgets, and mere budgets do not achieve the objective of cost unless the actual results are compared with targets laid down.

Preparation of budgets of budgeting is planning function, and their application or implementation is a control function. The activity involved in both the functions accomplishes budgetary control.

References:
4. Ibid, p.3.
5. Ibid, p.3.
