Chapter 1

Introduction

1.1 Introduction: Financial and Non-Financial Analysis

1.2 Literature Review
1.1 Introduction to Financial and Non-Financial Analysis

(A) Financial Analysis

It is well known in the economics literature that product and labor markets are no perfect. Empirical studies also do not universally and unequivocally support the efficient capital market hypothesis. The financial economists do recognize market imperfections such as transaction cost, bankruptcy cost, taxes, information gap, agency cost, signaling effect etc.

Business whether new or existing may vary from one another in terms of the industry they operate in, the environment they function in, the product/services they render or the operations that they undertake, however, the finance issues that business grapple with, notwithstanding their industry characteristics, geographical location, product profile etc. are largely universal.

Finance is central to all business activities for survival and growth alike. All business performance, targets and goals though set in absolute terms have a common measurement in financial terms similarly all comparisons either with the past or with competitors are measured or analyzed with financial data.

A firm should be managed effectively and efficiently. This implies that the firm should be able to achieve its objectives by minimizing the use of resources. One systematic approach for attaining effective management performance is financial planning and budgeting.

Strategic and financial planning considers all markets, including product, labor and capital as imperfect and changing. Strategies are developed to manage the business in uncertain and imperfect market conditions and environment and exploit opportunities. It is an important management task to analyze changing market conditions and environment to make forecasts and plan generation and allocation of resources.

1. Pandey I M, Financial Management, Tata McGraw Hill, Pg. 32.3
Study of Financial Performance Evaluation of Indian Companies

The role of a financial analyst is immense and his responsibilities are onerous in facilitating informed decision making by the investors. As an analyst, you are expected to be well versed with the Anatomy of financial statements so that you are able to read in between the lines and decipher the red flags in the financial reporting.

Financial analysis (also referred to as financial statement analysis or accounting analysis) refers to an assessment of the viability, stability and profitability of a business, sub-business or project. It is performed by professionals who prepare reports using ratios that make use of information taken from financial statements and other reports. These reports are usually presented to top management as one of their bases in making business decisions.

- Continue or discontinue its main operation or part of its business;
- Make or purchase certain materials in the manufacture of its product;
- Acquire or rent/lease certain machineries and equipment in the production of its goods;
- Issue stocks or negotiate for a bank loan to increase its working capital;
- Make decisions regarding investing or lending capital;
- Other decisions that allow management to make an informed selection on various alternatives in the conduct of its business.

Financial analysis is the process of evaluating businesses, projects, budgets and other finance-related entities to determine their suitability for investment. Typically, financial analysis is used to analyze whether an entity is stable, solvent, liquid, or profitable enough to be invested in. When looking at a specific company, the financial analyst will often focus on the income statement, balance sheet, and cash flow statement. In addition, one key area of financial analysis involves extrapolating the company's past performance into an estimate of the company's future performance.
Financial analysis serves the following purposes:\textsuperscript{2}:

\textbf{A.1 Measuring the profitability}

The main objective of a business is to earn a satisfactory return on the funds invested in it. Financial analysis helps in ascertaining whether adequate profits are being earned on the capital invested in the business or not. It also helps in knowing the capacity to pay the interest and dividend.

\textbf{Indicating the trend of Achievements}

Financial statements of the previous years can be compared and the trend regarding various expenses, purchases, sales, gross profits and net profit etc. can be ascertained. Value of assets and liabilities can be compared and the future prospects of the business can be envisaged.

\textbf{Assessing the growth potential of the business}

The trend and other analysis of the business provide sufficient information indicating the growth potential of the business.

\textbf{Comparative position in relation to other firms}

The purpose of financial statements analysis is to help the management to make a comparative study of the profitability of various firms engaged in similar businesses. Such comparison also helps the management to study the position of their firm in respect of sales, expenses, profitability and utilizing capital, etc.

\textbf{Assess overall financial strength}

The purpose of financial analysis is to assess the financial strength of the business. Analysis also helps in taking decisions, whether funds required for the purchase of new machines and equipments are provided from internal sources of the business or not if yes, how much? And also to assess how much funds have been received from external sources?

\textbf{Assess solvency of the firm}

The different tools of an analysis tell us whether the firm has sufficient funds to meet its short term and long term liabilities or not.

\textsuperscript{2} Pandey, I M, TMH, pg. 6.1
3. Financial statement analysis consists of 1) reformulating reported financial statements, 2) analysis and adjustments of measurement errors, and 3) financial ratio analysis on the basis of reformulated and adjusted financial statements. The two first steps are often dropped in practice, meaning that financial ratios are just calculated on the basis of the reported numbers, perhaps with some adjustments. Financial statement analysis is the foundation for evaluating and pricing credit risk and for doing fundamental company valuation.

1) Financial statement analysis typically starts with reformulating the reported financial information. In relation to the income statement, one common reformulation is to divide reported items into recurring or normal items and non-recurring or special items. In this way, earnings could be separated into normal or core earnings and transitory earnings. The idea is that normal earnings are more permanent and hence more relevant for prediction and valuation. Normal earnings are also separated into net operational profit after taxes (NOPAT) and net financial costs. The balance sheet is grouped, for example, in net operating assets (NOA), net financial debt and equity.

2) Analysis and adjustment of measurement errors question the quality of the reported accounting numbers. The reported numbers can for example be a bad or noisy representation of invested capital, for example in terms of NOA, which means that the return on net operating assets (RNOA) will be a noisy measure of the underlying profitability (the internal rate of return, IRR). Expensing of R&D is an example when such investment expenditures are expected to yield future economic benefits, suggesting that R&D creates assets which should have been capitalized in the balance sheet. An example of an adjustment for measurement errors is when the analyst removes the R&D expenses from the income statement and put them in the balance sheet. The R&D expenditures are then replaced by amortization of the R&D capital in the balance sheet. Another example is to adjust the reported numbers when the analyst suspects earnings management.
3) Financial ratio analysis should be based on regrouped and adjusted financial statements. Two types of ratio analyses are performed: 3.1) Analysis of risk and 3.2) analysis of profitability:

3.1) Analysis of risk typically aims at detecting the underlying credit risk of the firm. Risk analysis consists of liquidity and solvency analysis. Liquidity analysis aims at analyzing whether the firm has enough liquidity to meet its obligations when they should be paid. A usual technique to analyze illiquidity risk is to focus on ratios such as the current ratio and interest coverage. Cash flow analysis is also useful. Solvency analysis aims at analyzing whether the firm is financed so that it is able to recover from losses or a period of losses. A usual technique to analyze insolvency risk is to focus on ratios such as the equity in percentage of total capital and other ratios of capital structure. Based on the risk analysis the analyzed firm could be rated, i.e. given a grade on the riskiness, a process called synthetic rating.

Ratios of risk such as the current ratio, the interest coverage and the equity percentage have no theoretical benchmarks. It is therefore common to compare them with the industry average over time. If a firm has a higher equity ratio than the industry, this is considered less risky than if it is above the average. Similarly, if the equity ratio increases over time, it is a good sign in relation to insolvency risk.

3.2) Analysis of profitability refers to the analysis of return on capital, for example return on equity, ROE, defined as earnings divided by average equity. Return on equity, ROE, could be decomposed: ROE = RNOA + (RNOA - NFIR) * NFD/E, where RNOA is return on net operating assets, NFIR is the net financial interest rate, NFD is net financial debt and E is equity. In this way, the sources of ROE could be clarified.

Unlike other ratios, return on capital has a theoretical benchmark, the cost of capital - also called the required return on capital. For example, the return on equity, ROE, could be compared with the required return on equity, kE, as estimated,
for example, by the capital asset pricing model. If \( \text{ROE} < kE \) (or \( \text{RNOA} > \text{WACC} \), where WACC is the weighted average cost of capital), then the firm is economically profitable at any given time over the period of ratio analysis. The firm creates values for its owners.

Insights from financial statement analysis could be used to make forecasts and to evaluate credit risk and value the firm's equity. For example, if financial statement analysis detects increasing superior performance \( \text{ROE} - kE > 0 \) over the period of financial statement analysis, then this trend could be extrapolated into the future. But as economic theory suggests, sooner or later the competitive forces will work - and ROE will be driven toward \( kE \). Only if the firm has a sustainable competitive advantage, \( \text{ROE} - kE > 0 \) in "steady state".

**A. 2 Importance of Financial Analysis**

The analysis and interpretation of financial statements is useful in achieving several objectives:

1. The evaluation of past performance
2. The assessment of current status
3. The prediction of future potential
4. Take the right decisions to maximize profits and resources
5. Measuring the profitability
6. Indicating the trend of achievements
7. Assessing the growth potential of the business
8. Comparative position in relation to other firms
9. Assess overall financial strengths
10. Assess solvency of the firm

Being basically historical in nature, the financial statements are more convenient for the first two purposes. However, most readers of the financial statements are interested in the future, i.e. by the Company's ability to grow and prosper and the availability of the company to adapt to varying conditions. Properly used, the analysis of financial statements can provide a basis for projecting future and clues about how the company will respond to these future situations.
From an internal perspective of the company, analysis of financial statements provides many advantages to the administration:

1) In planning the short and long term, when choosing between alternatives, objectives, policies, procedures and programs.

2) In an organization, to coordinate the actions of people who work in an organization with the goal of better preservation of the tangible assets, technical and human resources, allowing them to detect possible deficiencies in the operations of the different areas of a business.

3) In the integration, in seeking to articulate the elements and human elements and materials that show planning and organization as necessary for the proper functioning of the entity.

4) In the address, to ensure obtaining the results or objectives through the administrator’s authority exercised directly or by delegating to other factors, to organize, guide and supervise their subordinates, providing a firm basis for directing the efforts towards the aims of the entity.

5) In the control, to measure and compare the results with those expected, i.e. if there is a balance between planning and execution.

From an external perspective, allows presenting the situation and possible evolution of the entity to all external users: credit institutions, shareholders, suppliers, employees, customers, auditors, analysts, government agencies, competitors, investors, etc.

A. 3 Tools of financial analysis

1. Actual vs. Planned Performance

This financial statement analysis should be performed line item by line item. If you had fewer sales than planned one should know or find out why. If any costs were greater than planned again, you should know or
find out why. Ever dollar received, and every dollar spent shows up on your financial statements, and every dollar that is different than you planned should be analyzed. This could be a good thing as you may need to change your planning. This is where it becomes important to have an advisory group where you can bounce information, and ideas, around.

2. Trend Analysis

By comparing current financial statements to previous financial statements you can see which areas of your business have changed, and by how much. Then you need to determine why the change occurred, whether positive or negative. Are sales trending up? Are costs trending down (which ones aren’t)? Are profits trending up? Is your cash flow improving? These are the types of things you will want to look at in your financial statement analysis.

Like the performance analysis, you need to analyze you financial statements line item by line item to determine trends...and don't be afraid to change your planning if you see a new trend emerging.

3. Industry Comparisons

This analysis is not only a comparison or your business’s performance to others in your industry, but also to standards set by your banker, your investor(s), your advisory group, or even yourself. These comparisons are usually made in the form of financial “ratios.” Here are a few of the more common financial ratio analyses:

**Balance Sheet Ratios** - Balance Sheet ratios typically measure the strength of your business, using the following formulas:

**Current Ratio** — this is one of the most widely used tests of financial strength, and is calculated by dividing Current Assets by Current Liabilities. This ratio is used to determine if your business is likely to be able to pay its bills. Obviously, a minimum acceptable ratio would be 1:1; otherwise your company would not be expected to pay its bills on time. A ratio of 2:1 is much more acceptable, and the higher, the better.

3. Khan and Jain, Financial Management, TMH, pg. 6.2
Quick Ratio — this is sometimes called the “acid test” ratio because it concentrates on only the more liquid assets of your business. It is calculated by dividing the sum of Cash and Receivables by Current Liabilities. It excludes inventories or any other current asset that might have questionable liquidity. Depending on your history for collecting receivables, a satisfactory ratio is 1:1.

Working Capital — bankers especially, watch this calculation very closely as it deals more with cash flow than just a simple ratio. Working Capital equals Current Assets minus Current Liabilities. Quite often your banker will tie your loan approval amount to a minimum Working Capital requirement.

Inventory Turnover Ratio — not every business has an inventory that needs to be of concern, and if that is your situation you can ignore this ratio. If you are concerned about your inventory, then you definitely should watch this ratio carefully when comparing it to industry guidelines. This ratio tells you if your inventory is turning over fast enough, and is calculated by dividing Net Sales by your average Inventory (at cost).

Leverage Ratio — this is another of the analyses used by bankers to determine if your business is credit worthy. It basically shows the extent your business relies on debt to keep operating and is calculated by dividing Total Liabilities by Net Worth (total assets minus total liabilities). Obviously, the higher the ratio is, the more risky it becomes to extend credit to your business. This is often the calculation a supplier to your business will make before extending credit to you.

P&L Ratios — Profit and Loss (P&L) financial statements also have some important ratio calculations for your financial statement analysis:

Gross Profit Ratio — this is the most common calculation on your P&L—it is simply your Gross Profit divided by Net Sales. Often, different industries will have standard guidelines that you can compare your business’s numbers to. It is also desirable to watch your trends and not let this number move too far from your target.

Net Profit Ratio — this calculation is simply Net Pre-tax Profit divided by Net Sales. Other than wanting this number to be as large as possible, I usually don’t pay too much attention to it because it includes
too many non-operating costs (depreciation, amortization, etc.) to be of any real analysis value. (Your banker may be interested however.)

Management Ratio - There are a couple of other ratios that interested outside parties will want to analyze:

**Return on Assets** — this is calculated by dividing Net Pre-tax Profit by Total Assets. The ratio is supposed to indicate how efficiently you are utilizing your assets. To me this is a useless analysis for helping you run your business, however, bankers and investors will always calculate this ratio if you don’t.

**Return on Investment (ROI)** — to a bank or investor this is the most important ratio of all. It is supposed to tell you—the business owner—if you are investing your time, and money, properly, or should you just liquidate your business and put the money into a savings account. This, of course, is pure bull... concocted by non-entrepreneurs and academics who have no idea what it means to be an entrepreneur.

Having said that, I do realize it can be of some value to a banker or investor—they likely want to know if they could make a better return on their money by investing or loaning it to someone other than you. So, for that purpose, it can be valuable...to them. To calculate your Return on Investment, divide your Net Pre-tax Profit by your Net Worth (total assets minus total liabilities).
4. Du Pont Analysis:

It is believed that measuring assets at gross book value removes the incentive to avoid investing in new assets. New asset avoidance can occur as financial accounting depreciation methods artificially produce lower ROEs in the initial years that an asset is placed into service. If ROE is unsatisfactory, the DuPont analysis helps locate the part of the business that is underperforming.

This method of performance measurement was started by the DuPont Corporation in the 1920s. With this method, assets are measured at their gross book value rather than at net book value in order to produce a higher return on equity (ROE). It is also known as "DuPont identity".

DuPont analysis tells us that ROE is affected by three things:

- Operating efficiency, which is measured by profit margin

- Asset use efficiency, which is measured by total asset turnover

- Financial leverage, which is measured by the equity multiplier

The Du Pont analysis can be depicted via the following chart:
At the apex of the Du Pont chart is the Return On Total Assets (ROTA), defined as the product of the Net Profit Margin (NPM) and the Total Assets Turnover Ratio (TATR). As a formula this can be shown as follows:

\[
\frac{\text{Net profit}}{\text{Total assets}} = \frac{\text{Net profit}}{\text{Net sales}} \times \frac{\text{Net sales}}{\text{Total assets}}
\]

\[
\text{ROTA} = \frac{\text{NPM}}{\text{TATR}}
\]

Such decomposition helps in understanding how the return on total assets is influenced by the net profit margin and the total assets turnover ratio.

4. Chandra, Prasna, pg. 178
The right side of the chart highlights the determinants of total assets turnover ratio. If this study is supplemented by the study of other ratios such as inventory, debtors, fixed asset turnover ratios, a deeper insight into efficiencies and inefficiencies of asset utilisation can be sought.

The basic Du Pont analysis can be extended to explore the determinants of the Return On Equity (ROE).

\[
\text{Return on equity} = \text{Asset turnover} \times \text{Net profit margin} \times \text{leverage}
\]

\[
\frac{\text{Net profit/Equity}}{\text{Net profit/Sales} \times \text{Sales/Total assets} \times \text{Total assets/Equity}} = \frac{\text{ROE}}{(NPM) \times (TATR)} \times \frac{1}{1-DR}
\]

Where DR is the debt ratio = debt (D)/assets (A)

Breaking ROE into these three parts allows evaluation of how well one can manage the company’s assets, expenses, and debt. A manager has basically three ways of improving operating performance in terms of ROA and ROE. These are:

- Increase capital asset turnover
- Increase operating profit margins
- Change financial leverage

Each of these primary drivers is impacted by the specific decisions on cost control, efficiency productivity, marketing choices etc.

**Importance of Du Pont Analysis**

Any decision affecting the product prices, per unit costs, volume or efficiency has an impact on the profit margin or turnover ratios. Similarly any decision affecting the amount and ratio of debt or equity used will affect the financial structure and the overall cost of capital of a company. Therefore, these financial concepts are very important to evaluate as every
business is competing for limited capital resources. Understanding the interrelationships among the various ratios such as turnover ratios, leverage, and profitability ratios helps companies to put their money areas where the risk adjusted return is the maximum.

5. **Cash flow and Fund flow analysis**

Cash flow is essentially the movement of money into and out of your business; it's the cycle of cash inflows and cash outflows that determine your business' solvency.

Cash flow analysis is the study of the cycle of the business' cash inflows and outflows, with the purpose of maintaining an adequate cash flow for the business, and to provide the basis for cash flow management.

Cash flow analysis involves examining the components of the business that affect cash flow, such as accounts receivable, inventory, accounts payable, and credit terms. By performing a cash flow analysis on these separate components, one is able to more easily identify cash flow problems and find ways to improve your cash flow.

A quick and easy way to perform a cash flow analysis is to compare the total unpaid purchases to the total sales due at the end of each month. If the total unpaid purchases are greater than the total sales due, there is need to spend more cash than what is received in the next month, indicating a potential cash flow problem.

A fund flow statement, also called a statement of changes in capital and statement of changes in financial position, is a financial statement that represents how an organization has been financed, the sources of funds and how they have been used within a specific period of time. Author Roy A. Foulke, writing in the book, "The Commercial Market Paper," defines a fund flow statement as a "statement of sources and application of funds is a technical device designed to analyze the changes in the financial condition of a business enterprise between two
dates." Simply put, a fund flow statement highlights the flow of funds (sources and uses) between two dates.

A fund flow statement is a financial analysis tool that helps managers makes decisions. It highlights the changes in the financial position of a company. Unlike other financial statements, such as an income statement and balance sheet that provide only a static view of an organization's financial operations, a fund flow statement is dynamic and depicts the flow of funds and how they have been allocated between various business activities. It provides complete information to financial managers on the effectiveness of fund allocation and reveals an organization's fund-generating strengths and weaknesses. A fund flow statement also throws light on the financial position of a firm at a given point in time and highlights the financial consequences of major business operations, allowing managers to take corrective actions if required. Funds flow statements allow financial managers to plan on how to improve the rate of return on assets, manage the effects of insufficient funds and cash balance and plan how to pay interest to creditors and dividends to shareholders.

6. Common size statement analysis

Vertical analysis of financial statements is a technique in which the relationship between items in the same financial statement is identified by expressing all amounts as a percentage a total amount. This method compares different items to a single item in the same accounting period\(^5\).

The financial statements prepared by using this technique are known as common size financial statements.

This analysis is performed on the income statement as well as the balance sheet.

- **Balance Sheet:**

When applying this method on the balance sheet, all of the three major categories accounts (i.e. assets, liabilities, and equity) are

\(^5\) Khan and Jain, Financial Management, pg. 6.42
compared to the total assets. All of the balance sheet items are presented as a proportion of the total assets. These percentages are shown along with the absolute currency amounts.

- **Income Statement:**

And when applying this technique to the income statement, each of the expense is compared to the total sales revenue. The expenses are presented as a proportion of total sales revenue along with the absolute amounts.

The main advantage of using vertical analysis of financial statements is that income statements and balance sheets of companies of different sizes can be compared. Comparison of absolute amounts of companies of different sizes does not provide useful conclusions about their financial performance and financial position.

Usually the vertical analysis is performed for a single accounting period to see the relative proportions of different account balances. But it is also useful to perform vertical analysis over a number of periods to identify changes in accounts over time. It can help to identify unusual changes in the behavior of accounts.
(B) Non Financial Analysis

The great emphasis placed on financial aspects when considering investment decisions has been questioned by recent literature: see for example Skitmore et. al. (1989), Proctor and Canada (1992), Chen (1995), Lopes & Flavell (1998), Adler (2000), Meredith and Mantel (2000), Mohamed and McCowan (2001), Love et al. (2002). All these authors have been emphasizing the need to take both financial and non financial aspects into account when considering investment decisions.

The decision-making process for investments is complex and goes beyond the financial aspects. Skitmore et al. (1989) point out that “any knowledge that can help the decision makers to recognize and minimize the uncertainty and risk is expected to have some potential value”. Many of the firm’s goals tend to be qualitative and not easily measurable, apart from being long term goals and not immediately verifiable. The financial techniques must be used only as a guide, or a baseline, and other factors that may influence the uncertainty analysis must be considered.

The financial evaluation is only a part of the decision making process and additional information is needed. Therefore, even if the financial conditions are extremely favorable, neglecting some of the qualitative aspects may cause serious problems. The business analysis process must enclose a wide spectrum of analysis dimensions, whether financial or not, as a way to fully study all the aspects that may influence its viability. With the financial analysis, strategic, commercial, political, environmental, human resources and managerial analysis got equal importance.

5. Skitmore et. al. (1989)
B.1 Importance of Non-Financial Analysis:

Non-financial information may be a window through which light can be shed on key elements of corporate performance to help investors and companies to better determine how to allocate money and take decisions. Though advocates argue that non-financial information forms or should form an increasingly important part of investor decision-making, relatively little research has been done to analyze the non-financial information currently available or to determine how investors value specific types of non-financial information.

For all the emphasis on enhanced non-financial reporting, there remain serious obstacles to effecting new forms of corporate disclosure. Three obstacles in particular stand out;

• **Lack of data comparability**: Without adherence to consistent disclosure guidelines still absent despite the work of multi stakeholder groups such as the Global Reporting Initiative, non-financial information can lack the comparability of traditional financial data.

• **Lack of data clarity and reliability**: Without clear regulations or effective auditing systems governing non-financial reporting, the credibility of voluntary corporate disclosures may be called into question.

• **Limited time and resources**: Investors have limited time and resources to analyze corporate data. Information overload – especially if that information has no clear link to investment decision-making – is a serious concern. Information ought to be accessible, easy to use and reliable for it to effectively support an efficient market.

B.2 Tools of non-financial analysis

1. SWOT Analysis: In its simplest form, a SWOT analysis can be understood as the examination of an organization's internal strengths and weaknesses, and its environments opportunities, and threats. It is a general tool designed to be used in the preliminary stages of decision-making and as a precursor to strategic planning in various kinds of applications (Johnson et al., 1989; Bartol et al., 1991). An understanding of all external factors, (threats and opportunities) together with an internal examination of strengths and weaknesses assists in forming a vision of the future.

SWOT Analysis is the most frequently used device for audit and evaluation of strategic position of the company. It gives an overall view of the company's operating environment including its capabilities and resources to align the specific business model. It actually forms a firm ground to plot and evaluate the potentials and limitations in the external and internal setting of the company. The big optimism seen in such reports is that, the factual data about the company regarding its negativities is exposed including weaknesses and threats. The overall picture of the company aligns the policies and strategies in a right direction and helps a great deal towards stable future of the company.

SWOT can help management in a business discover:

- What the business does better than the competition
- What competitors do better than the business
- Whether the business is making the most of the opportunities available
- How a business should respond to changes in its external environment

2. **PEST Analysis**: PEST analysis is concerned with the key external environmental influences on a business. The acronym stands for the Political, Economic, Social and Technological issues that could affect the strategic development of a business. Identifying PEST influences is a useful way of summarizing the external environment in which a business operates. However, it must be followed up by consideration of how a business should respond to these influences. The PEST analysis is a useful tool for understanding market growth or decline, and as such the position, potential and direction for a business. A PEST analysis is a business measurement tool.

PEST analysis is very important that an organization considers its environment before beginning the marketing process. In fact, environmental analysis should be continuous and feed all aspects of planning. The PEST model is sometimes extended (some would say unnecessarily) to seven factors, by adding Ecological (or Environmental), Legislative (or Legal), and Industry Analysis (the model is then known as PESTELI).

PEST analysis can be used for marketing and business development assessment and decision-making, and the PEST template encourages proactive thinking, rather than relying on habitual or instinctive reactions.

3. **Five Forces analysis**: The model of pure competition implies that risk-adjusted rates of return should be constant across firms and industries. However, numerous economic studies have affirmed that different industries can sustain different levels of profitability; part of this difference is explained by industry structure.

Michael Porter provided a framework that models an industry as being influenced by five forces. The strategic business manager seeking to develop an edge over rival firms can use this model to better understand the industry context in which the firm operates.
Porter explains that there are five forces that determine industry attractiveness and long-run industry profitability. These five "competitive forces" are

- The threat of entry of new competitors (new entrants)
- The threat of substitutes
- The bargaining power of buyers
- The bargaining power of suppliers
- The degree of rivalry between existing competitors
1.2 Literature Review

A literature review is a critical and in depth evaluation of previous research. It is a summary and synopsis of a particular area of research, allowing anybody reading the paper to establish why you are pursuing this particular research program. A good literature review expands upon the reasons behind selecting a particular research question.

It is not a chronological catalog of all of the sources, but an evaluation, integrating the previous research together, and also explaining how it integrates into the proposed research program. All sides of an argument must be clearly explained, to avoid bias, and areas of agreement and disagreement should be highlighted.

It is not a collection of quotes and paraphrasing from other sources. A good literature review should also have some evaluation of the quality and findings of the research.

A good literature review should avoid the temptation of impressing the importance of a particular research program. The fact that a researcher is undertaking the research program speaks for its importance, and an educated reader may well be insulted that they are not allowed to judge the importance for themselves. They want to be re-assured that it is a serious paper, not a pseudo-scientific sales advertisement.

Every one of us is involved in financial decision making on a daily basis. Every activity in today’s world begins with finance and ultimately ends in terms of finance. Financial transactions occupy a significant part of man’s social relations with his fellow being. One may be involved in manufacturing, providing services, in HR, marketing, social service or growth; to quantify and project at the end one looks at financial figures. The performance of a company depends upon financial strengths of a company and is measured in terms of finance. Even the economic welfare of the people of a country depends upon the country’s financial position.
Finance, being daughter of economics, has emerged as one of the most vital component for growth and development. Its emergence as a discipline in the last quarter of the 20th century brings forth its vitality. Finance, one of the most-scare resources, has been the constraining factor in the growth and development of an economy, firm, corporate and even an individual.

Finance is the centrifugal force of any activity whether it is corporate, household or any other type. Even the smooth functioning of society, a particular organization or an entire economy is not possible without the efficient financial management. Any organization can submerge into deep state of bankruptcy and financial anarchy if financial decisions are inculcated with flaws. Till now there are plethora of theory and model have been developed to understand the significant impact of financial development and their inter linkage. Though one cannot say for sure that it is the financial development that leads to economic development be it an organization or an economy and so we need to have an understanding of basic tenets of finance which helps an individual to link it to various happening around him.

Most of the literature in finance in the past six decades since World War II has focused on corporate finance, investments, banking and financial systems, securities markets and public finance. As a result finance as a field of study has been directly identified with these areas and most often treated as an extension of economics or accounting. The financial management of various sectors of the economy which play a pivotal role in the development processes of a country and required massive investments, equally attracted the attention of international agencies, policy makers, academicians and practitioners as these sector required massive investments as well as creative solutions to finance these sectors.

8. Thaker, Keyur, Business Performance Measures: A study with Reference to companies in India, Finance India, pg. 535
Researchers in the discipline of business performance evaluation have mainly remained varied and broad based rather than in depth or build upon the work of others. The unique characteristics of the research in this area is that significantly the major, influential and widely published researches are carried out on sponsored basis and on an organized way by premier business schools across the world and by top management consultancy firms and organizations.

News reports and articles on the topic have been appearing at the rate of one every five hours every working day since 1994. A search of the World Wide Web reveals over 12 million sites dedicated to this topic.

The consultancy firms dominate the studies in the area. There are certain models and software available for the performance evaluation for the firms. Individual researchers from variant fields of accounting, finance and control, economics, human resource management, strategy, marketing, operations are exploring the performance and linkages between them. They are examining how the performance evaluation leads to profitability, share prices, market valuation of the firm, and its reputation.

In 1998, the first multidisciplinary conference on performance measurement was held at the Churchill College in Cambridge. Between then 94 papers were presented at the conference cited some 1246 different books and articles. Of these, less than 10 percent were cited more than once and only 3 percent were cited more than five times.

There are large numbers of text books as well as research studies, available on Finance but to the best of my knowledge there is no compendium presenting at one place the literature available on Finance, recognizing the fact that there exist wide time gap in the research being done, published in journal and included in books.

The benefits which the society may derive from serious research remain untapped and the findings based on hard labor and serious efforts of researchers decorate the columns of professional and academic research journals which in turn either pile dust in some obscure of the libraries or decorate the offices of senior professors.