Lecture Summary (1)

LO. Describe the roles of financial reporting and financial statement analysis.

The role of financial reporting is to provide information about a company's performance (income statement and cash flow statement), financial position (balance sheet) and changes in financial position (statement of changes in equity).

The role of financial statement analysis is to use the financial reports prepared by firms and combine them with other sources of information to decide if you can invest in the equity of the firm or lend money to the firm.

LO. Describe the roles of the statement of financial position, statement of comprehensive income, statement of changes in equity, and statement of cash flows in evaluating a company's performance and financial position.

The balance sheet reports the firm's financial position at a specific point in time. It shows the firm's assets, liabilities, and owners' equity.

The income statement reports the financial performance of the firm over a period of time. It shows the firm's revenues, expenses, and net income.

Lecture Summary (2)

The cash flow statement reports the sources and uses of cash for the firm over a period of time. It shows the firm's operating, investing, and financing cash flows.

Statement of changes in owner's equity reports the changes in the owners' investment in the firm over time. It shows the firm's paid in capital and retained earnings.

LO. Describe the importance of financial statement notes and supplementary information - including disclosures of accounting policies, methods, and estimates - and management's commentary.

The notes (also called footnotes) are important as they disclose information about the accounting policies, methods, and estimates used to prepare the financial statements. They contain important information regarding acquisitions and disposals, commitments and contingencies, legal proceedings, employee stock options and other benefits, related party transactions and business, and geographic segments.

Management's commentary comprises of subjective information where management is presenting its view and interpretation of the data it has reported. Examples of content include trends and significant events affecting the company's operations, liquidity and capital resources, off-balance sheet obligations, and planned capital expenditures.

Lecture Summary (3)

LO. Describe the objective of audits of financial statements, the types of audit reports, and the importance of effective internal controls.

An audit is an independent review of a firm's financial statements. It enables the auditor to express an opinion on the fairness and reliability of the financial reports. An audit report can contain one of the following opinions:

- Unqualified Opinion - Reasonable assurance that financial statements are fairly presented.
- Qualified Opinion - Some misstatement or exception to accounting standards.
- Adverse Opinion - Financial statements are not presented fairly.

For listed companies, the audit report also includes a discussion of Key Audit Matters (international) and Critical Audit Matters (US). Effective internal controls are important to ensure the accuracy of financial statements. A firm's management is responsible for maintaining an effective internal control system.

IFT

Lecture Summary (4)

LO. Identify and describe information sources that analysts use in financial statement analysis besides annual financial statements and supplementary information.

Apart from the financial statements, other information sources available for an analyst are:

- Interim reports – Quarterly or semiannual reports prepared by the firm.
- Proxy statements - Statements distributed to shareholders about matters that are to be put to a vote.
- Press releases, conference calls, and websites – Firms often provide current information via these mediums.
- External sources – Information about the economy, industry, and the firm's competitors.

Lecture Summary (5)

LO. Describe the steps in the financial statement analysis framework.

The financial statement analysis framework consists of the following six steps:

1. Define the purpose and context of the analysis.
    - Define the purpose and context of the analysis based on your function, client inputs, and organizational guidelines.
    - Determine the time frame and the resources available for the task.
2. Collect data.
    - Collect data from financial statements and other information sources.
3. Process the data.
    - Make adjustments to financial statements.
    - Create graphs, ratios, common-sizes statements, etc.
4. Analyze and interpret the data.
5. Develop and communicate conclusions and recommendations.
6. Follow up.
    - Conduct periodic reviews to check if previous conclusions are still valid.