

THE OPEN UNIVERSITY OF TANZANIA
FACULTY OF BUSINESS MANAGEMENT

DEPARTMENT OF ACCOUNTING AND FINANCE

OFN 454 FINANCIAL STATEMENT ANALYSIS
COURSE OUTLINE

INTRODUCTION

This course prepares students to become better consumers of, and decision makers with, financial information. It will cover the fundamental concepts and procedures of financial statement analysis and enable students to recognize the importance of the economic, cultural, legal and competitive environment in understanding financial results.

Financial statement analysis relies on the application and interpretation of accounting numbers and economic concepts. In this course, you will learn how to analyze a company's published financial information and comment on its financial position and performance. You will primarily focus on financial statements to facilitate such decisions as: credit, investment, employment, merger, performance evaluation, financial budgeting, etc. To do so, this course will focus on alternative accounting treatments and the "range of ordinary" interpretations. Each student is encouraged to obtain a set of published financial statement from a company of his or her choice and use it to conduct a full analysis, individually or in groups, as he or she learns the materials. These published accounts should be used when learning topics 4 and 5.

Learning objectives

After completing this course you should be able to:

- Understand the importance of accounting information to the firm and its providers of capital
- Acquire a framework for using financial statement information in a variety of business analyses
- Identify, compare and contrast information sources for corporate financial statements and information
- Explain the importance of economic, cultural, legal and competitive environment in financial statement analysis
- Investigate accounting principles and financial concepts and understand the basic techniques of financial statement analysis - horizontal, vertical, and ratio analysis
- Use accounting numbers shown in financial statements to make a reasonable assessment of the firm's future financial position, present a comprehensive analysis of the same while recognizing the limitations of the underlying assumptions..
- Discuss and illustrate the impact of selected accounting rules regarding assets, liabilities and equity on reported financial results.

TOPIC ONE: THE DEMAND FOR FINANCIAL STATEMENT INFORMATION

Financial statements are a product of a diverse set of demand and supply forces. This topic therefore, requires students to look at the demand side forces and how they affect the content of financial statements or the timing of their release.

Sub-topics

1.1 Parties demanding financial statements

A student is expected to cover in depth, the types of financial statement users and kind of information each group is interested with. Among others, a student has to look at the following groups of financial statement users:

- Shareholders, Investors and Security analysts
- Mangers
- Employees
- Lenders and other suppliers
- Customers
- Government/Regulatory agencies

1.2 Conflicts Among diverse users.

Each part covered in 1.1 above does have its own kind information needs. The kind of information required by one group is likely to contradict with the information needed by another group. A student is therefore expected to have an in-depth coverage of these.

1.3 Factors affecting Demand for financial statement information

The student is expected to read and understand the main factors affecting the demand for financial statement information with particular emphasis on the potential of information to reduce uncertainty and on the availability of competing information sources

- Economic environment factors
- Cultural environment factors
- Legal environment factors
- Competitive environment factors

TOPIC TWO: THE SUPPLY OF FINANCIAL STATEMENT INFORMATION

Basically in this topic, we envisage to look at factors affecting the supply of financial statement information provided to external parties. In particular, the students are expected to place an emphasis on regulatory and market forces that affect the content of financial reports.

2.1 Regulatory forces and the Supply of Financial Statement Information

- The Institutional framework in Tanzania
- The influence of regulatory forces

2.2 Market forces and the supply of Financial Statement Information

- Capital market forces
- Labour market forces
- Corporate market forces

2.3 Information Sources for Financial Statement Analysis

- Annual reports
- Industry reports and analyses

TOPIC THREE: TYPES OF FINANCIAL STATEMENTS.

A financial statement is an organized collection of data according to logical and consistent accounting procedures. Its purpose is to convey an understanding of some financial aspects of a business firm. The student ought therefore to have an understanding of the major three types of financial statements - Income statement, Balance sheet and Cash flow statement.. In particular, he/she is expected to have knowledge of how these financial statements are prepared together with their composition. Above that a student is expected also to cover the limitations of financial statements.

TOPIC FOUR: FINANCIAL STATEMENT ANALYSIS

Financial statement analysis includes the study of relationships between accounting variables within a set of financial statements at a point in time and with trends in these relationships over time. Under this topic a student is expected to have a thorough understanding of the following techniques used in the analysis of financial statements:

4.1 Cross Sectional techniques

Common size statements
Financial Ratio analysis

4.2 Time series techniques

Trend statements
Financial Ratio Analysis
Variability measure

TOPIC FIVE: FINANCIAL RATIOS ANALYSIS

Financial ratios are relationships expressed in mathematical terms between figures which are connected with each other in some manner. A student is supposed to practice computing the financial ratio together with making their respective interpretations. The following classes of ratios have to be covered inline with their respective components.

- Liquidity ratios
- Profitability ratios
- Turnover ratios
- Gearing ratios
- Performance ratios

TOPIC SIX: ACCOUNTING PROCEDURES AND PRONOUNCEMENTS THAT IMPACT ON FINANCIAL STATEMENTS

- Revenue recognition

- Financing with Accounts Receivables
- Inventory Valuation Methods
- Deferred Income Taxes
- Asset impairment

COURSE ASSESSMENT

The course shall be evaluated as follows

Course work		
• Two assignments	@ 7.5%	15%
• Two timed tests	@12.5%	<u>25%</u>
Total course work		40%
Final Examination	@60%	<u>60%</u>
Total		<u>100%</u>

Pass mark shall be 40% and no candidate shall be allowed to pass with coursework or final examination alone.

REFERENCES:

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Foster G, (1986) *Financial Statement Analysis* (2nd Edit), Prentice-Hall, New Jersey

Fridson, M. and Alvarez, F (2002) *Financial Statement Analysis: A Practitioner's Guide* 3rd Edition, John Wiley and Sons, Cincinnati.

Helfert, E. A. (2001) *Financial Analysis: Tools and Techniques, A guide for Managers*, McGraw Hill, New York.

IASC website for international financial accounting standards: www.iasc.org.uk.

Maheshwari S.N & Maheshwari S.K, (2005) *Corporate Accounting* (4th Edit), VIKAS Publishing House Pvt Ltd, New Delhi.

Penman, Stephen H. (2007) *Financial Statement Analysis & Security Valuation*.3rd edition, McGraw-Hill, Boston,

White G.I., Sondhi, A.C. and Fried, D. (2002) *The Analysis and Use of Financial Statements* 3rd edition, John Wiley and Sons, Cincinnati

Wild, Bernstein and Subramanyam, *Financial Statement Analysis* 7th ed. Irwin McGraw Hill