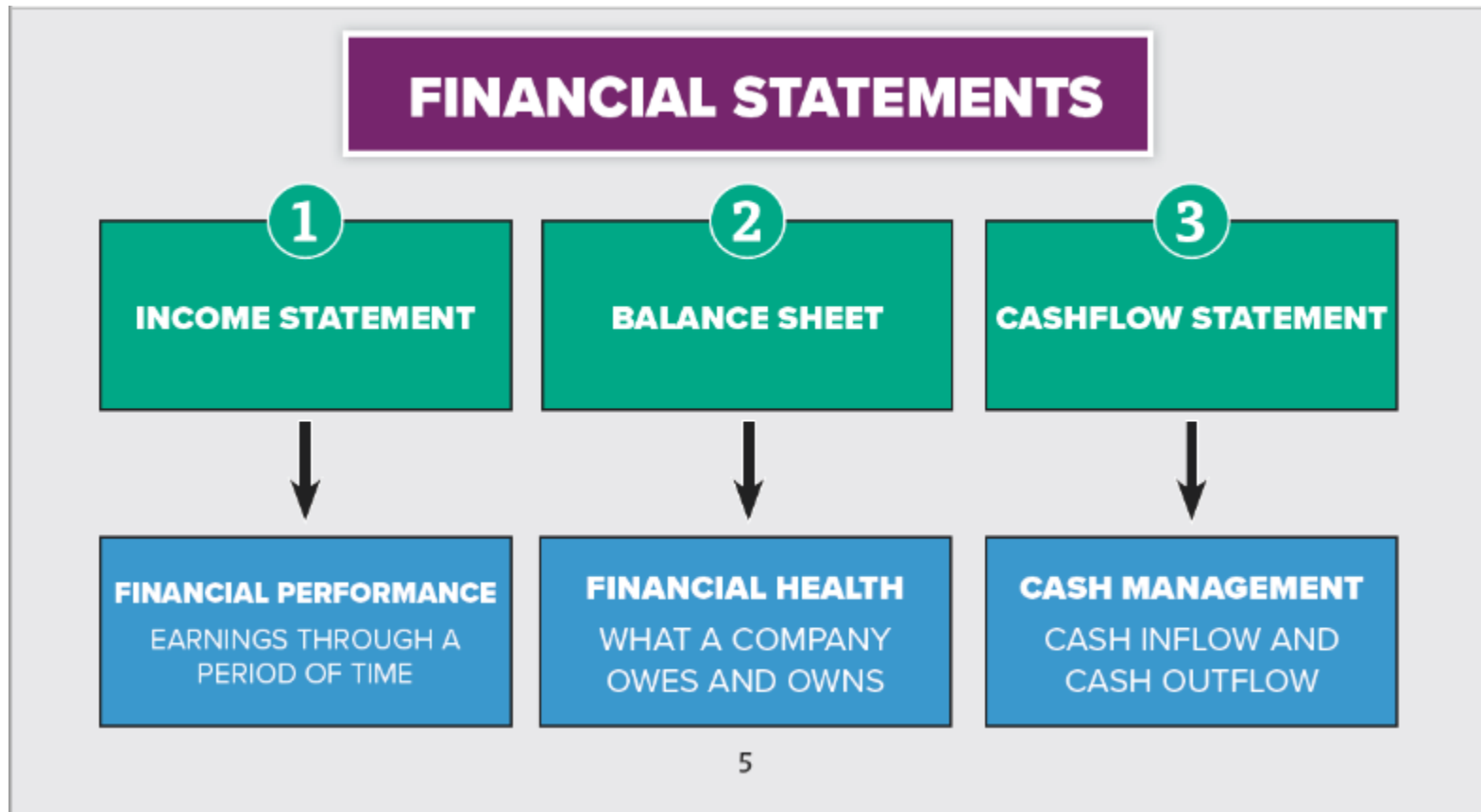


Finance Management & Planning

Balance Sheet

This Week

- The Elements of the Balance Sheet



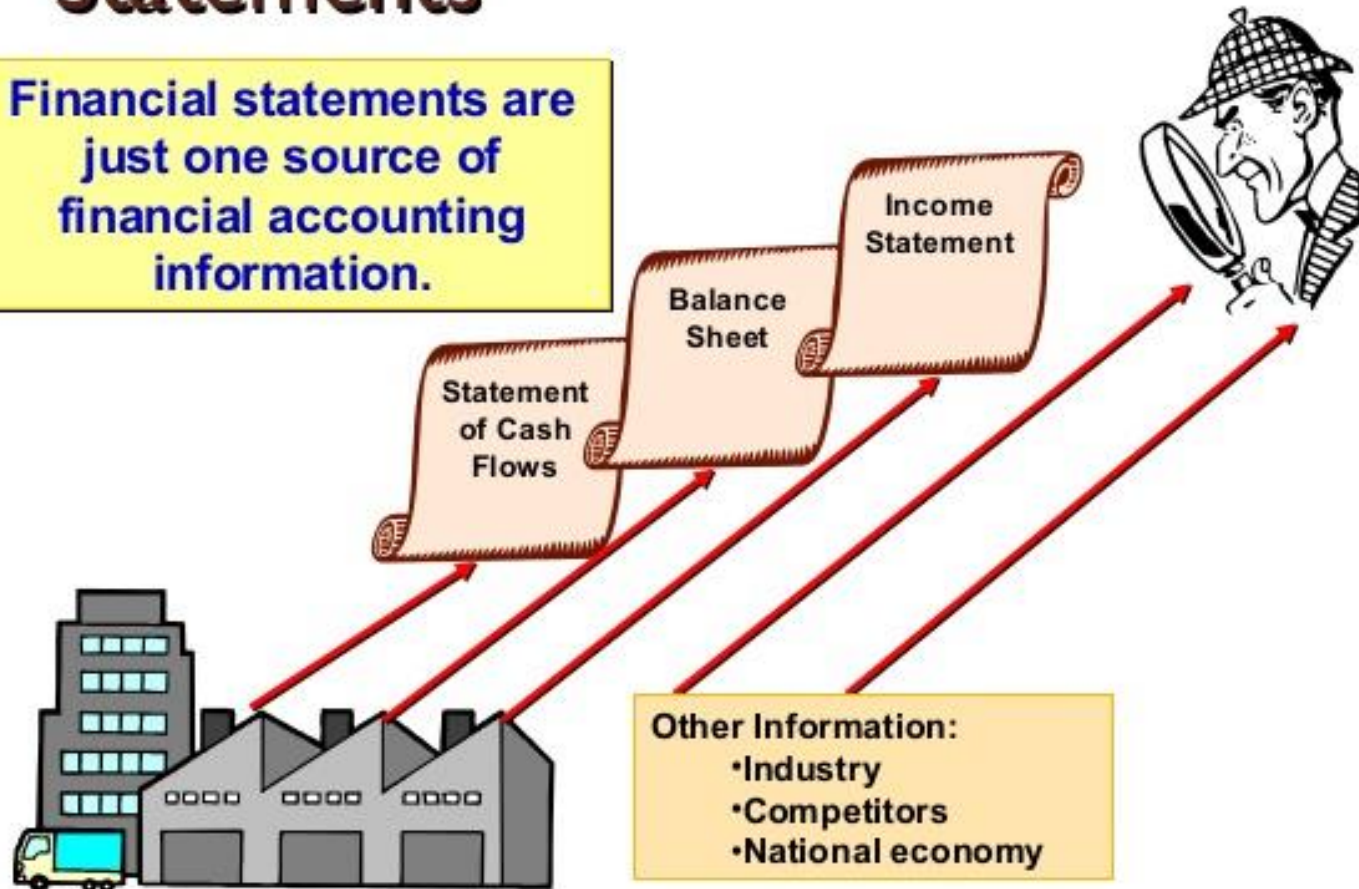
Financial Statements

- Overview of a business's performance through a specified period
- P&L
 - Business Performance
 - Revenue Levels
 - Cost of Good Sold
 - Gross margin
 - Overheads
 - Net Margin (EBITDA)
 - Usually compared to prior year
 - Internally compared to a forecast or budget
- Balance Sheet
 - Value of Assets and Liabilities within a business
- Cash-flow
 - How a businesses cash has flowed through the business.

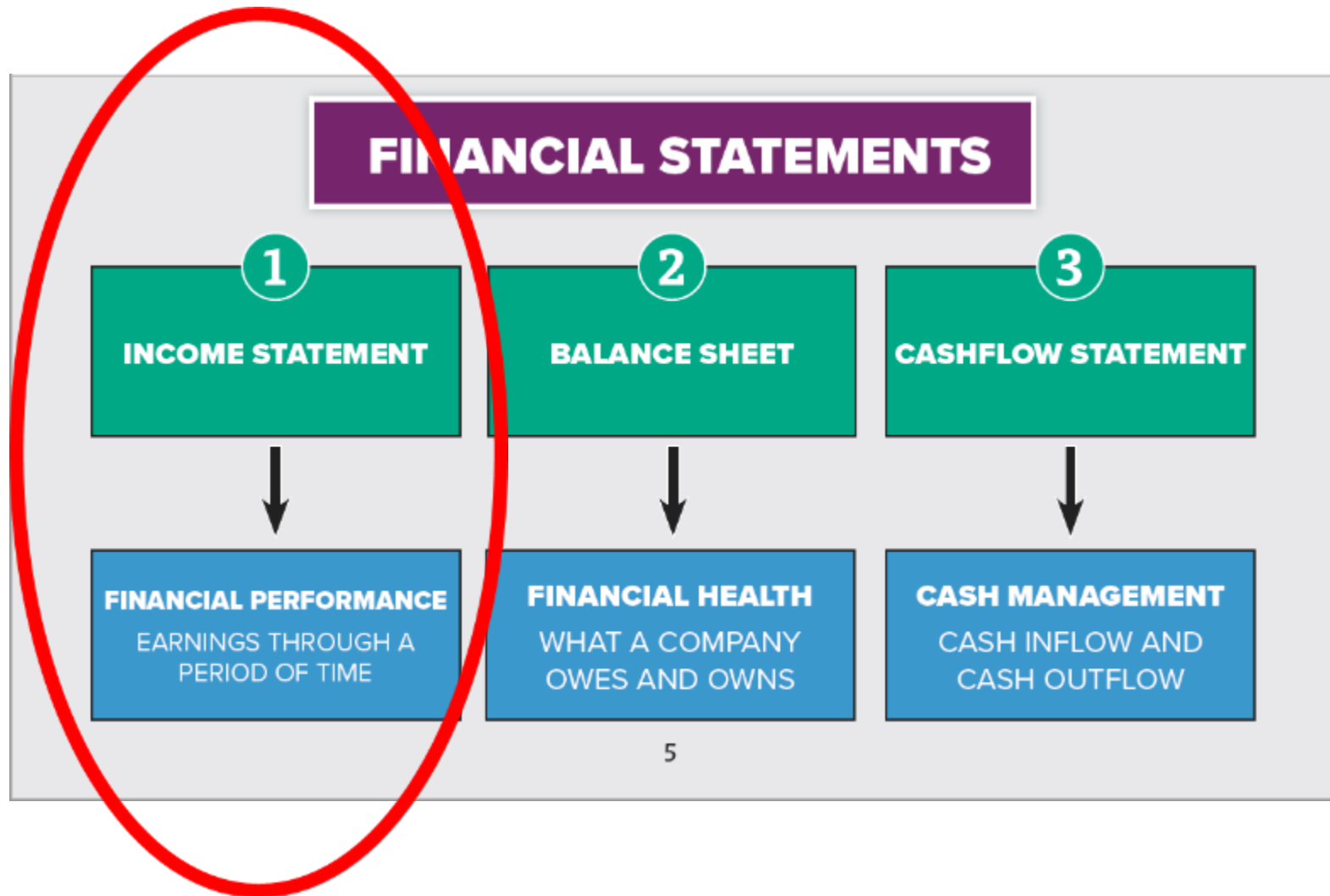
Financial Reporting and Financial Statements



Financial statements are just one source of financial accounting information.



2-19



Income Statement (or Profit and Loss Statement)

Definition :

An **income statement** is a **financial statement** that shows you how profitable your business was over a given reporting period. It shows your revenue, minus your expenses and losses

Purpose :

An **income statement** is a **financial statement** that shows you how profitable your business was over a given reporting period. It shows your revenue, minus your expenses and losses

Profit and loss statement example

Profit and loss of company XYZ

Total revenue	£100,000
Cost of goods sold	£20,000
Gross profit	£80,000

What your
business does

Operating expenses

Salaries	£10,000
Rent	£10,000
Utilities	£5,000
Depreciation	£5,000

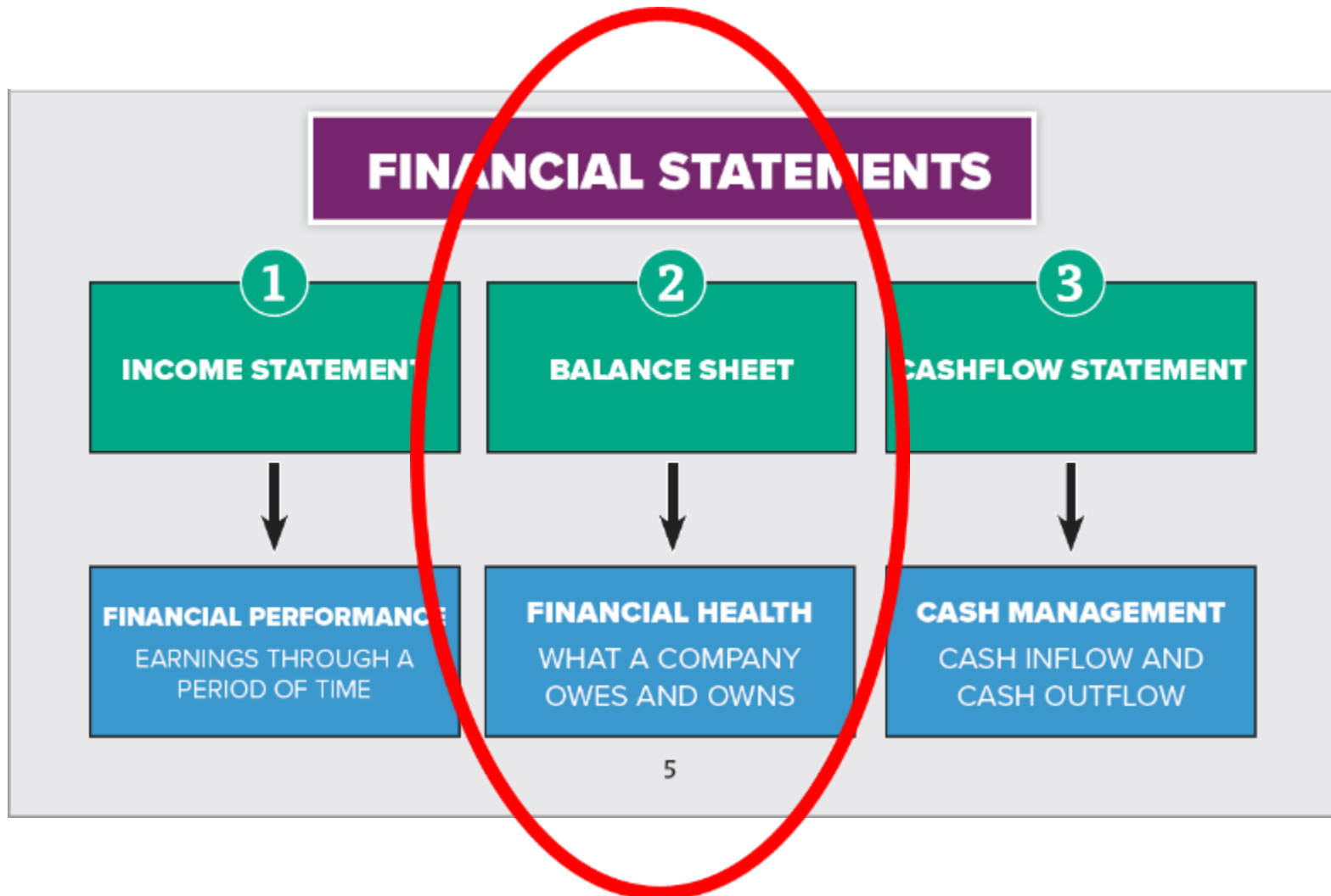
The additional
running costs of
your business

Total operating expenses	£30,000
Operating profit	£50,000
Interest expense	£10,000

Servicing
costs of your
business

Income before taxes	£40,000
Taxes	£10,000

Net income **£30,000**

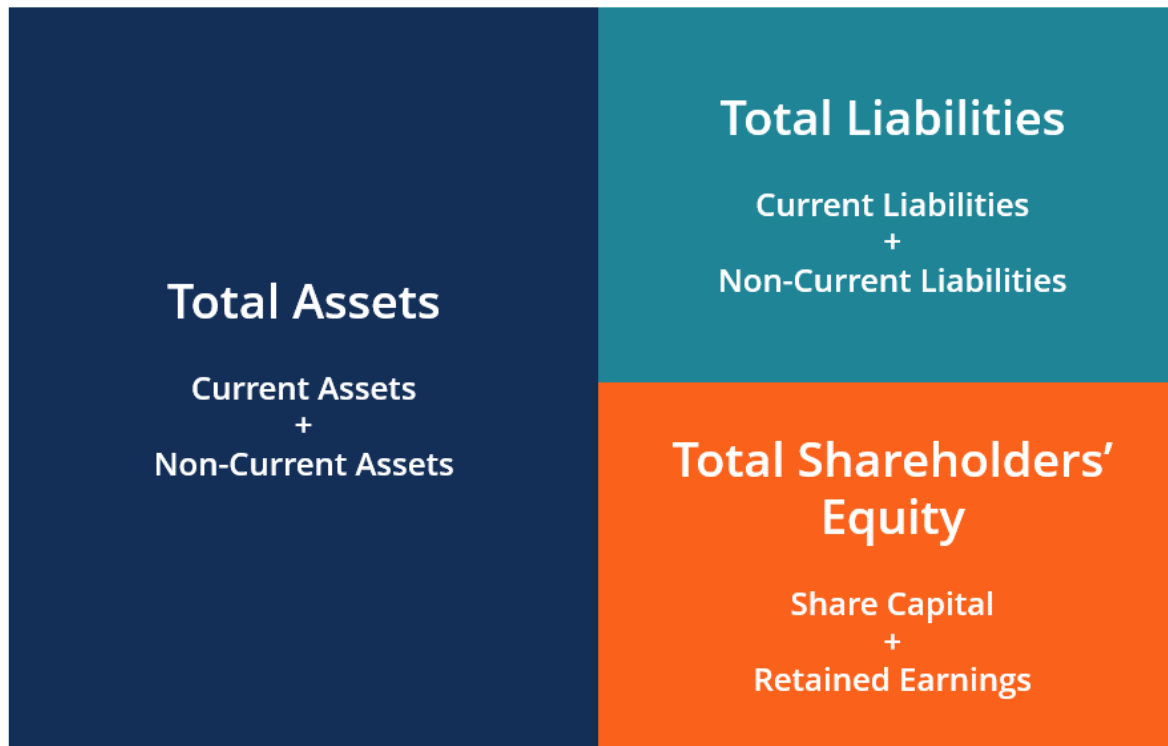


- The Balance Sheet is a statement of its financial position.
- The Balance sheet is a lists of the assets , liabilities and equity within its organisation.

It can highlight :

- The company's ability to meet its current obligations.
- Financial Health of an organisation.
- Why is it important ?
 - Short term Liquidity
 - Long Term Liquidity

A Simple Balance Sheet



<https://corporatefinanceinstitute.com/resources/accounting/balance-sheet/>

What is an asset within a business ?

‘A resource held by a business’

All 4 conditions must apply to be an ‘asset’

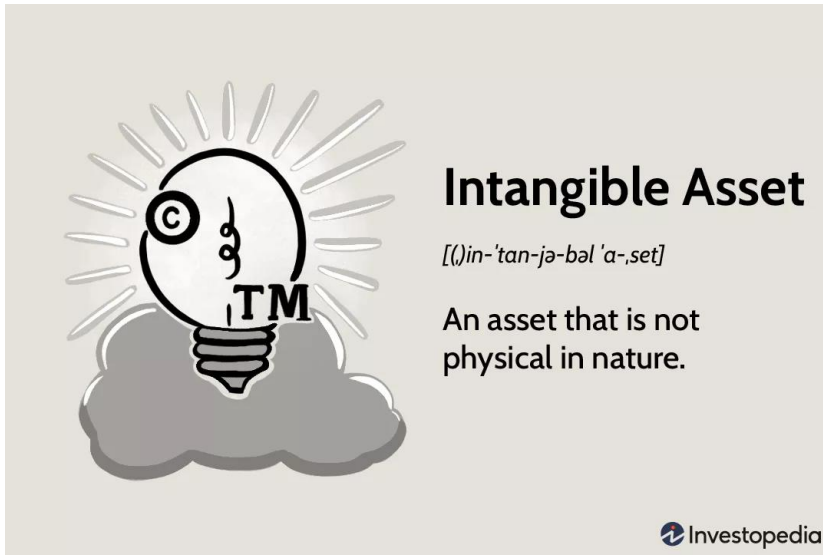
- A probable future economic benefit with some monetary value
- The benefit must arise from some past transaction or event
- The business must have the right to control the resource
- The asset must be capable of measurement in monetary terms

Does not have to be physical – can be non physical: - tangible or non-tangible

Types of Assets

- Non – Current – Long Term Value to the business – usually greater than one year.
 - Plant & equipment
 - Fixtures and fittings
 - Patents and trademarks
- Non Current Assets can be further split between Tangible and Intangible.

Assets of the Business (What the company owns)



Examples

- Goodwill
- Brand
- Trademark
- Copyright
- Patents
- Licencing Agreements
- Website Domain Names

Assets of the Business (What the company owns)

- Tangible Examples being:
 - Land
 - Plant and Machinery
 - Machinery and Equipment
 - Vehicles
 - Furniture and Fittings

Treatment of Non-Current Assets of the Business

Why do we treat certain assets as Non - Current Assets differently?

Depreciation

- To calculate Depreciation we need to understand four factors :-
 - The cost or fair value of the asset
 - The useful life of the asset
 - The residual value of the asset. (expected disposal value)
 - The Depreciation method
 - Straight Line method
 - Reducing Balance method

Depreciation – Straight Line methodology

- Company A
 - purchased a new Machine for £100,000 ,
 - expected lifespan of 5 years
 - Expected Residual value at end of 5 years is £10,000

Balance Sheet

- Company A – Straight Line Method

Total Cost	100,000
Residual Value	10,000
Total Depreciation	90,000
Depreciation per Year	18,000

	<u>Income Statement</u>	<u>Balance Sheet</u>
Year 0	0	100,000
Year 1	18,000	82,000
Year 2	18,000	64,000
Year 3	18,000	46,000
Year 4	18,000	28,000
Year 5	18,000	10,000

Depreciation

- Purchased a new Machine for £50,000 ,
- expected lifespan of 3 years
- Expected Residual value at end of 3 years is £0
- Straight Line Method

Total Cost	50,000
Residual Value	0
Total Depreciation	50,000

Useful Life	3
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Depreciation per Year	16,667
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Straight Line Method

	<u>Income Statement</u>	<u>Balance Sheet</u>
Year 0	0	50,000
Year 1	16,667	33,333
Year 2	16,667	16,667
Year 3	16,667	0
Year 4		
Year 5		

Depreciation

- To calculate Depreciation we need to understand four factors :-
- Reducing Balance method

$$DB = 1 - \sqrt[Years]{\frac{SalvageValue}{Cost}}$$

- Excel has a DB function to simplify the calculation
- Company A
 - purchased a new Machine for £100,000 ,
 - expected lifespan of 5 years
 - Expected Residual value at end of 5 years is £10,000
 - Calculated Reducing Balance 36.9% through the excel model

Balance Sheet

Depreciation

Total Cost	100,000
Residual Value	10,000
Total Depreciation	90,000
Useful Life	5
Reducing Balance %	36.9%

Reducing Balance Method

		Income Statement	Balance Sheet	Expected Residual Value
Year 0		0	100,000	10,000
Year 1	1	36,900	63,100	
Year 2	2	23,284	39,816	
Year 3	3	14,692	25,124	
Year 4	4	9,271	15,853	
Year 5	5	5,850	10,003	

Balance Sheet



Straight Line Method

	Income Statement	Balance Sheet	Expected Residual Value
Year 0	0	100,000	10,000
Year 1	18,000	82,000	
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Reducing Balance Method

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Year 4	9,271	15,853	
Year 5	5,850	10,003	

Straight Line

Vs

Reducing Balance

1. Equal depreciation each year
2. Total of depreciation and repairs may increase as the asset gets older
3. Value of asset could be reduced to Rs zero or scrap value
4. Depreciation rate = $\frac{\text{Depreciation} \times 100}{\text{Cost}}$
5. Suitable for assets which have low repairs and maintenance costs e.g leases, copyrights etc

1. Reducing depreciation each year
2. Total of depreciation and repairs may not vary much from year to year
3. Value of asset cannot be extinguished
4. Depreciation rate = $1 - \sqrt[n]{\frac{\text{Residual Value}}{\text{Cost of Assets}}} \times 100$
5. Suitable for plant and machinery which have high repairs and maintenance costs as the machine gets older

Types of Assets

- Current Assets – Usually less than one year
 - Cash at Bank
 - Debtors / Trade Receivables
 - Stock / inventories
 - Short Term Investments

Stock

Different levels of Valuation

- Raw Materials
- Work in Progress
- Finished Goods
- Machine store

Inventory Costing Method	Description	Benefit
First-in, First-out (FIFO)	Cost of goods sold has older, lower costs; Ending inventory has newer, higher costs	Most closely matches actual flow of goods; Maximizes net income which attracts investors and creditors
Last-in, First-out (LIFO)	Cost of goods sold has newer, higher costs; Ending inventory has older, lower costs	Minimizes net income and income taxes; reduces cash paid for taxes
Average cost	Average costs in Cost of goods sold and ending inventory	A “middle-ground” solution for reporting income and paying taxes

What other circumstances do we need to consider when valuing stock ?

- Obsolete Stock being held
- Major change in market value of goods (Fair valuation)
- Bad buying decision being made
- The goods are being used as a loss leader so full value may not be recovered.

Aged Report - Accounts Receivable

Account Name	Total As At 01-Aug-11	1 Day 30 Days	31 Days 60 Days	61 Days 90 Days	> 90 Days
A1 Realty	0.00	0.00	0.00	0.00	0.00
Bills Hardware	0.00	0.00	0.00	0.00	0.00
Great Outdoor Life	497.20	0.00	0.00	0.00	497.20
Pex Machines	55.00	55.00	0.00	0.00	0.00
Smithvile Realty	60.00	60.00	0.00	0.00	0.00
Southside Timber Supplies	125.00	0.00	30.00	65.00	30.00

Provision for Doubtful Debts ?

- Prepayments

* All costs held within the accounts are for a period of time *

End of Reporting period is Dec 21

Invoice received for Rent £3k for the months 1st Dec to 28th Feb.

How much of this should we recognise in the Income Statement to 31st Dec 2021?

Invoice processed of	£3k
Prepayment of	£2k
Shown in Income Statement	£1k

Balance Sheet – Assets



GROUP BALANCE SHEET

	Note	As at 27 March 2021 £m	As at 28 March 2020 £m
ASSETS			
Non-current assets			
Intangible assets	12	237.0	247.0
Property, plant and equipment	13	280.4	294.9
Right-of-use assets	14	818.1	834.0
Investment properties		2.4	2.5
Deferred tax assets	15	137.1	171.5
Trade and other receivables	16	45.0	53.7
		1,520.0	1,603.6
Current assets			
Inventories	17	402.1	450.5
Trade and other receivables	16	276.9	252.1
Derivative financial assets	18	2.2	6.7
Income tax receivables		39.7	50.4
Cash and cash equivalents	19	1,261.3	928.9
		1,982.2	1,688.6
Total assets		3,502.2	3,292.2

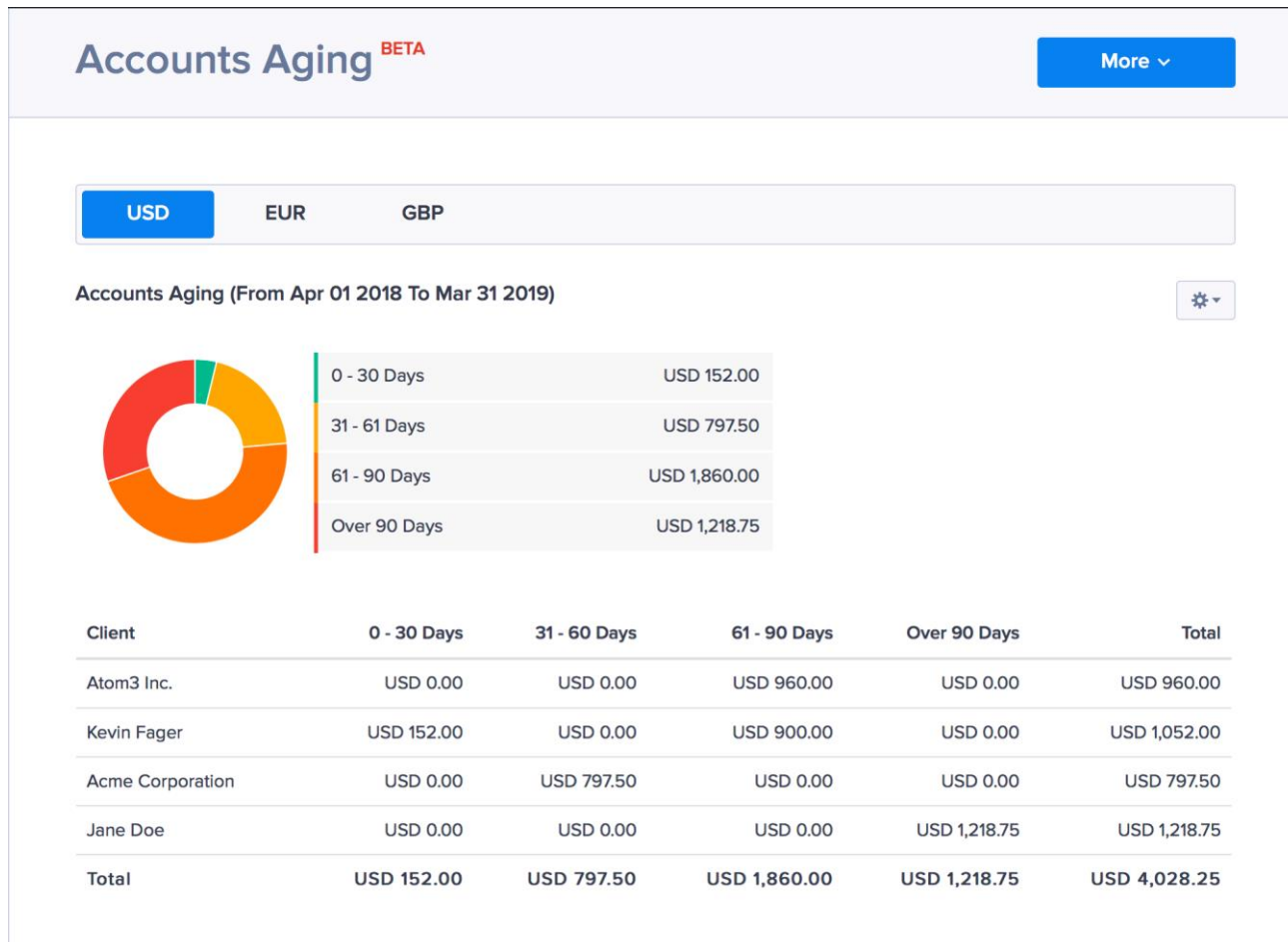
Source : Burberry Financial Statements 2021

- Liabilities - claims of individuals and organisations on the business e.g. supply of goods or lending money
- Split into Non Current and Current

- Liabilities (What the organisation owes)
- Current Liabilities (Obligation to be paid within one year)
 - Creditors
 - Cash and Cash Equivalents
 - Accrued Liabilities
 - Short term Bank loans

Balance Sheet

- Current Liabilities (Obligation to be paid within one year)
- Creditors / Accounts Payable <https://youtu.be/eljCaeNm-Vk>



- Accruals
- The year end is Dec 21
- The last rent bill received is Sept to Nov 21 for £3k , we pay £3k per quarter for rent .
- What value do we need to accrue to ensure we have all the costs in the accounts to Dec 21 ?
- Accrual £1k – shown as a current liability in the balance sheet and a charge to the Income statement.

- Liabilities (What the organisation owes)
- Non Current Liabilities (Obligation to be paid greater than one year)
 - Long Term lease Liabilities
 - Long Term Borrowings
 - Long Term Provisions

Balance Sheet



LIABILITIES			
Non-current liabilities			
Trade and other payables	20	(99.4)	(102.3)
Lease liabilities	21	(809.6)	(910.0)
Borrowings	24	(297.1)	(300.0)
Deferred tax liabilities	15	(0.8)	(0.1)
Retirement benefit obligations		(1.0)	(1.9)
Provisions for other liabilities and charges	22	(31.8)	(28.6)
		(1,239.7)	(1,342.9)
Current liabilities			
Trade and other payables	20	(392.9)	(447.5)
Bank overdrafts	23	(45.4)	(41.6)
Lease liabilities	21	(210.0)	(215.5)
Derivative financial liabilities	18	(2.6)	(4.8)
Income tax liabilities		(27.9)	(7.9)
Provisions for other liabilities and charges	22	(24.0)	(13.2)
		(702.8)	(730.5)
Total liabilities		(1,942.5)	(2,073.4)

Source : Burberry Financial Statements 2021

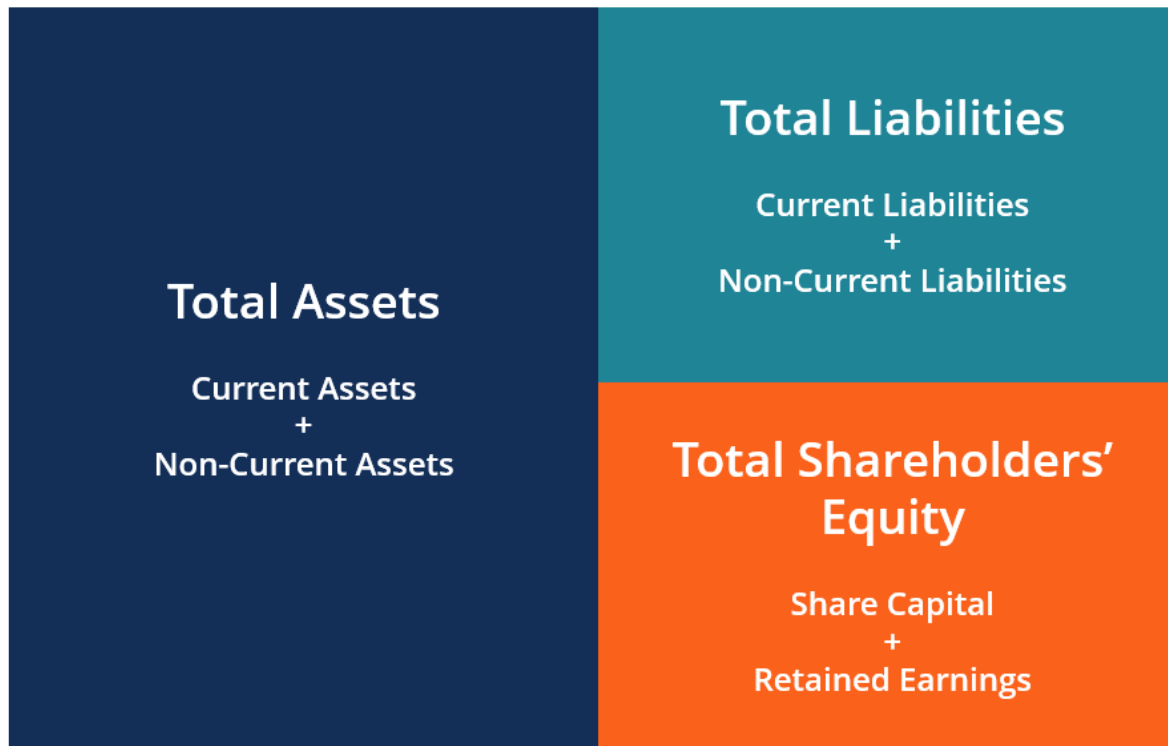
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Net assets		1,559.7	1,218.8

Source : Burberry Financial Statements 2021

A Simple Balance Sheet



<https://corporatefinanceinstitute.com/resources/accounting/balance-sheet/>

- Equity – sometimes referred to as owners capital
- $\text{Equity} = \text{Assets} - \text{Liabilities}$

Net assets		1,559.7	1,218.8
EQUITY			
Capital and reserves attributable to owners of the Company			
Ordinary share capital	25	0.2	0.2
Share premium account		223.0	220.8
Capital reserve	25	41.1	41.1
Hedging reserve	25	4.7	4.7
Foreign currency translation reserve	25	196.4	245.2
Retained earnings		1,091.2	702.2
Equity attributable to owners of the Company		1,556.6	1,214.2
Non-controlling interest in equity		3.1	4.6
Total equity		1,559.7	1,218.8

<https://youtu.be/rUBWG6n1fMk>

- Introduction to Ratios
- Profitability Ratios
- Liquidity Ratios