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FINANCE FOR ENTREPRENEURS - ONLINE WORKSHOP

(Training Manual for Students)

Written by: Mr. Bashir Hazim

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Introduction

Accounting & Finance involves the concepts of money, business and management, with an emphasis on professional careers in these areas. Accounting relates to information analysis for different aspects of a business, while finance solely concerns a business' monetary funds.

Finance is the management of money and investments for individuals, corporations, and governments. Finance professionals work in careers such as investment banking, wealth management, and financial planning and analysis (FP&A). Whether these professionals work on behalf of individuals or businesses, they are responsible for ensuring that there is adequate funding (capital) for the needs of the situation and that the funds are allocated as optimally as possible. Their job is to create value by managing capital in a way that earns higher than expected risk-adjusted returns.

Accounting is the recording, maintaining, and reporting of a company's financial records. Accounting professionals work for individuals, in-house at corporations, or on behalf of other businesses at a public accounting firm (such as the Big Four). These professionals are responsible for ensuring that all financial transactions are correctly entered into the general ledger, that account balances are correct, and that financial statements are accurate.

Why Financial Management?

Financial Management undoubtedly, is one of the most important aspects of a business. With huge funds, daily cash flow and continuous transaction, managing and monitoring all of the above turn necessary. Actually, managing finance is influential when it comes to making decisions. For instance, if the organization has greater funds, a part can be used for investment purposes and similarly, if the organization has funds lesser than the threshold value, it is important to put unnecessary spending to a stop.

To be specific, financial management helps the organization determine what to spend, where to spend and when to spend. It gives a better view of the financial status of the organization, which further outlines the financial processing of the same.

Taking this discussion forward, we highlight six reasons why financial management is important for your business.

1. **Generate Money:** To start a business, you would need money. It is obvious that to make the first step and launch your business, capital investment is required. Further, as you move up the timeline, getting materials, hiring professionals, marketing and testing, every single step would need financial management.

2. **Organize Operations:** Businesses generate enormous amounts of money every day. This money has to be used further to pay bills, delegate funds, invest in multiple engagements and monitor all. Managing the inflow and outflow of money within your organizations is important. Failing the above, it becomes tough to allocate funds efficiently and effectively. Not to forget that irregular flow of money can turn a business insolvent.

3. **Manage Cash Flow:** Having excessive funds is at fatal as having lesser ones. For an organization to be carried on with their day to day processing, it becomes imperative to manage the cash flow. In case you have higher funds and you aren't using it as needed, it signifies wastage of resources. For an enterprise that has surplus cash, putting them to use and investing in significant engagements would yield better returns and help them expand their business.

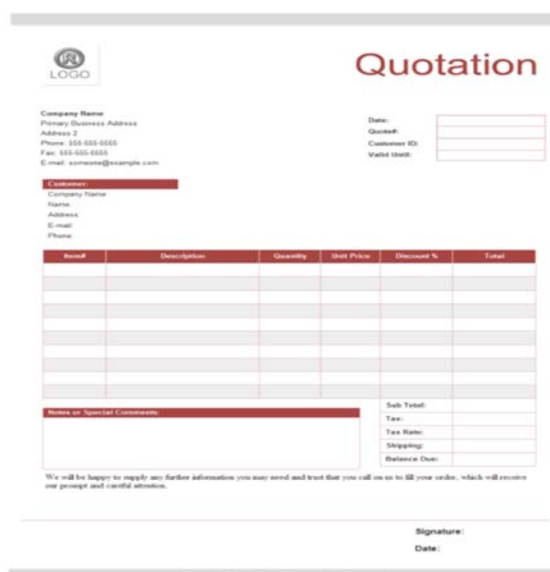
4. **Strategize Funding:** Of course, you would want to allocate funds and use it to map the expenses that take place on a regular basis. However, spending any or every cash without proper planning is not wise. You need to keep track of the expenses, monitor the frequency and then decide how to spend and how much to spend. At times, it is important to cut down extra costs and reduce expenses. This can only be done when you manage your financial undertakings effectively. It is advocated that companies must have sufficient funds to deal with crises.

5. **Outline Long Term Goals:** Organizations work to grow and scale their business high. To do so, it is important to have significant future goals that the organization aims to accomplish in a span of five or ten years. Financial Management helps an organization achieve its goals without fail. Consider that you have planned to expand your organization to three new cities. While actually implementing the plan, you run out of money. This wouldn't have happened had you managed your organization's finance and then executed. Pre-planning and working on the available cash of the organization helps you eliminate the future possibilities of crisis while moving ahead to attain your goal.

6. **Sustain Economic Downturn:** If you look at the growth graph of an organization, you will never find one that rises straight or is without any bends. The growth of the cycle of business organization is a mix and merge of highs and lows, which of course could be due to various reasons. Recession, depression, boom or failure, all add up to the fall of a business. With sufficient finance and significant financial management, it becomes easier for the organization to walk down the business cycle. No matter how bad the situation is, they are always ready to face the problem and bear the consequences without being under the threat of shutting down. Failure-proof financial management plans help the organization thrive even know adverse economic conditions.

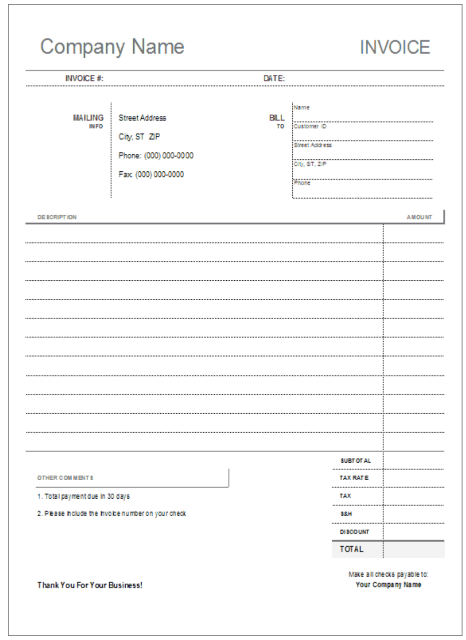
Understanding Basic Terms

- ✓ **Bookkeeping** is the exercise of identifying, categorizing, and recording all the transactions that take place in a business.
- ✓ **Accounting,** on the other hand, is the methodology used to record the transactions and prepare financial statements and reports.
- ✓ **Financial Statement** is a more widely requested formal document that is prepared in a specific format.
- ✓ **Financial ID:** is the legal identification number related to Ministry of Finance.
- ✓ **Quotation:**



  - ➢ A formal statement of promise (submitted usually in response to a request for quotation) by potential supplier to supply the goods or services required by a buyer:
  - ➢ At specified prices.
  - ➢ Within a specified period.
  - ➢ A quotation may also contain terms of sale and payment, and warranties.
  - ➢ Acceptance of quotation by the buyer constitutes an agreement binding on both parties.
  - ➢ Well Organized Companies send a request for Quotation.

- ✓ **Invoice:** is a proof of a sale between the company and the client. It must include the following:
  - ➢ Date
  - ➢ Sequence number
  - ➢ Client's name
  - ➢ Ministry of Finance number for both company and client (if a corporation)
  - ➢ Client's address and telephone number
  - ➢ Product/service sold
  - ➢ Quantity of each item sold
  - ➢ Price of each item sold
  - ➢ Terms of payment
  - ➢ Signature with stamp on the original copy for the client
  - ➢ A copy of the invoice signed by the client, to be filed in the accounting folder


Company Name INVOICE

INVOICE #: DATE:

MAILING INFO: Street Address, City, ST ZIP, Phone: (000) 000-0000, Fax: (000) 000-0000

BILL TO: Name, Customer ID, Street Address, City, ST, ZIP, Phone

DESCRIPTION	AMOUNT

OTHER COMMENTS
1. Total payment due in 30 days
2. Please include the invoice number on your check

SUBTOTAL	
TAX RATE	
TAX	
S&H	
DISCOUNT	
TOTAL	

Thank You For Your Business!

Make all checks payable to: Your Company Name

- ✓ **Credit Notes** has the same features as an invoice. It serves to offset the invoice or to reduce the outstanding balance and is generally used in case of:
  - ➢ Returned products
  - ➢ Undelivered products/services
  - ➢ Damaged goods
  - ➢ Errors and allowances

- ✓ **Receipts**: Once the client makes a payment, a receipt needs to be issued. It should include:
  - Date
  - Sequence number
  - Client's name
  - Ministry of Finance number for both company and client (if a corporation)
  - Amount received
  - Payment method and details (cash, check, wire transfer, credit card)
  - Signature with stamp on the original copy for the client
  - A copy of the receipt to be filed in the accounting folder

- ✓ **Statement of account** is a summary listing all invoices issued to a particular client and all payments received from that client.
  - It should always include start and end dates.
  - It should show the remaining account balance.
  - It is generally used to confirm balances between the two companies.

- ✓ **Fixed Costs (FC):** The costs which don't vary with changing output. Fixed costs might include the cost of building a factory, insurance and legal bills. Even if your output changes or you don't produce anything, your fixed costs stay the same.
- ✓ **Variable Costs (VC):** Costs which depend on the output produced. For example, if you produce more cars, you have to use additional raw materials such as metal. This is a variable cost.
- ✓ **Semi-Variable Cost:** Labor might be a semi-variable cost. If you produce more cars, you need to employ more workers; this is a variable cost. However, even if you didn't produce any cars, you may still need some workers to look after empty factory.
- ✓ **Total Costs (TC):** Fixed + Variable Costs

Cost	Variable	Fixed
Depreciation of executive jet		x
Cost of shipping finished goods to customers	x	
Wood used in manufacturing furniture	x	
Sales manager's salary		x
Electricity used in manufacturing furniture	x	
Packing supplies for shipping products	x	
Sand used in manufacturing concrete	x	
Supervisor's salary		x
Advertising costs		x
Executive's life insurance		x

- ✓ **Cost of Goods Sold:** Cost of goods sold (COGS) refers to the direct costs of producing the goods sold by a company. This amount includes the cost of the materials and labor directly used to create the good. It excludes indirect expenses, such as distribution costs and sales force costs. COGS=Beginning Inventory+P−Ending Inventory

  The COGS is an important metric on the financial statements as it is subtracted from a company's revenues to determine its gross profit. The gross profit is a profitability measure that evaluates how efficient a company is in managing its labor and supplies in the production process. Because COGS is a cost of doing business, it is recorded as a business expense on the income statements. Knowing the cost of goods sold helps analysts, investors, and managers estimate the company's bottom line. If COGS increases, net income will decrease. While this movement is beneficial for income tax purposes, the business will have less profit for its shareholders. Businesses thus try to keep their COGS low so that net profits will be higher.

  Cost of goods sold (COGS) is the cost of acquiring or manufacturing the products that a company sells during a period, so the only costs included in the measure are those that are directly tied to the production of the products, including the cost of labor, materials, and manufacturing overhead. For example, the COGS for an automaker would include the material costs for the parts that go into making the car plus the labor costs used to put the car together. The cost of sending the cars to dealerships and the cost of the labor used to sell the car would be excluded. Furthermore, costs incurred on the cars that were not sold during the year will not be included when calculating COGS, whether the costs are direct or indirect. In other words, COGS includes the direct cost of producing goods or services that were purchased by customers during the year.

The value of the cost of goods sold depends on the inventory costing method adopted by a company. There are three methods that a company can use when recording the level of inventory sold during a period: First In, First Out (FIFO), Last In, First Out (LIFO), and the Average Cost Method.

Many service companies do not have any cost of goods sold at all. COGS is not addressed in any detail in generally accepted accounting principles (GAAP), but COGS is defined as only the cost of inventory items sold during a given period. Not only do service companies have no goods to sell, but purely service companies also do not have inventories. If COGS is not listed on the income statement, no deduction can be applied for those costs.

Examples of pure service companies include accounting firms, law offices, real estate appraisers, business consultants, professional dancers, etc. Even though all of these industries have business expenses and normally spend money to provide their services, they do not list COGS. Instead, they have what is called "cost of services," which does not count towards a COGS deduction.

Financial Statements

Financial statements are written records that convey the business activities and the financial performance of a company. Financial statements are often audited by government agencies, accountants, firms, etc. to ensure accuracy and for tax, financing, or investing purposes. Financial statements include:

- ✓ Balance sheet
- ✓ Income statement
- ✓ Cash flow statement.

Investors and financial analysts rely on financial data to analyze the performance of a company and make predictions about its future direction of the company's stock price. One of the most important resources of reliable and audited financial data is the annual report, which contains the firm's financial statements. The financial statements are used by investors, market analysts, and creditors to evaluate a company's financial health and earnings potential.

The Balance Sheet

A balance sheet is a financial statement that reports a company's assets, liabilities and shareholders' equity at a specific point in time, and provides a basis for computing rates of return and evaluating its capital structure. It is a financial statement that provides a snapshot of what a company owns and owes, as well as the amount invested by shareholders.

The balance sheet is used alongside other important financial statements such as the income statement and statement of cash flows in conducting fundamental analysis or calculating financial ratios.

The balance sheet adheres to the following accounting equation, where assets on one side, and liabilities plus shareholders' equity on the other, balance out:

Assets = Liabilities + Shareholders' Equity

This formula is intuitive: a company has to pay for all the things it owns (assets) by either borrowing money (taking on liabilities) or taking it from investors (issuing shareholders' equity).

For example, if a company takes out a five-year, $4,000 loan from a bank, its assets (specifically, the cash account) will increase by $4,000. Its liabilities (specifically, the long-term debt account) will also increase by $4,000, balancing the two sides of the equation. If the company takes $8,000 from investors, its assets will increase by that amount, as will its shareholders' equity. All revenues the company generates in excess of its expenses will go into the shareholders' equity account. These revenues will be balanced on the assets side, appearing as cash, investments, inventory, or some other asset.

Assets, liabilities and shareholders' equity each consist of several smaller accounts that break down the specifics of a company's finances. These accounts vary widely by industry, and the same terms can have different implications depending on the nature of the business.

Assets

Within the assets segment, accounts are listed from top to bottom in order of their liquidity – that is, the ease with which they can be converted into cash. They are divided into current assets, which can be converted to cash in one year or less; and non-current or long-term assets, which cannot.

Here is the general order of accounts within **current assets**:

- ✓ Cash and cash equivalents are the most liquid assets and can include Treasury bills and short-term certificates of deposit, as well as hard currency.
- ✓ Marketable securities are equity and debt securities for which there is a liquid market.
- ✓ Accounts receivable refers to money that customers owe the company, perhaps including an allowance for doubtful accounts since a certain proportion of customers can be expected not to pay.

- ✓ Inventory is goods available for sale, valued at the lower of the cost or market price.
- ✓ Prepaid expenses represent the value that has already been paid for, such as insurance, advertising contracts or rent.

Long-term assets include the following:

- ✓ Long-term investments are securities that will not or cannot be liquidated in the next year.
- ✓ Fixed assets include land, machinery, equipment, buildings and other durable, generally capital-intensive assets.

- ✓ Intangible assets include non-physical (but still valuable) assets such as intellectual property and goodwill. In general, intangible assets are only listed on the balance sheet if they are acquired, rather than developed in-house. Their value may thus be wildly understated – by not including a globally recognized logo, for example – or just as wildly overstated.

Liabilities

Liabilities are the money that a company owes to outside parties, from bills it has to pay to suppliers to interest on bonds it has issued to creditors to rent, utilities and salaries. Current liabilities are those that are due within one year and are listed in order of their due date. Long-term liabilities are due at any point after one year.

Current liabilities accounts might include:

- ✓ current portion of long-term debt
- ✓ bank indebtedness
- ✓ interest payable
- ✓ wages payable
- ✓ customer prepayments
- ✓ dividends payable and others
- ✓ earned and unearned premiums
- ✓ accounts payable

Long-term liabilities can include:

- ✓ Long-term debt: interest and principal on bonds issued
- ✓ Pension fund liability: the money a company is required to pay into its employees' retirement accounts
- ✓ Deferred tax liability: taxes that have been accrued but will not be paid for another year (Besides timing, this figure reconciles differences between requirements for financial reporting and the way tax is assessed, such as depreciation calculations.)

Shareholders' Equity

Shareholders' equity is the money attributable to a business' owners, meaning its shareholders. It is also known as "net assets," since it is equivalent to the total assets of a company minus its liabilities, that is, the debt it owes to non-shareholders.

Retained earnings are the net earnings a company either reinvests in the business or use to pay off debt; the rest is distributed to shareholders in the form of dividends.

Treasury stock is the stock a company has repurchased. It can be sold at a later date to raise cash or reserved to repel a hostile takeover.

Some companies issue preferred stock, which will be listed separately from common stock under shareholders' equity. Preferred stock is assigned an arbitrary par value – as is common stock, in some cases – that has no bearing on the market value of the shares (often, par value is just $0.01). The "common stock" and "preferred stock" accounts are calculated by multiplying the par value by the number of shares issued.

Additional paid-in capital or capital surplus represents the amount shareholders have invested in excess of the "common stock" or "preferred stock" accounts, which are based on par value rather than market price. Shareholders' equity is not directly related to a company's market capitalization: the latter is based on the current price of a stock, while paid-in capital is the sum of the equity that has been purchased at any price.

ASSETS		**LIABILITIES**	
Current assets		**Current liabilities**	
Cash	2000	Bank overdraft	500
Inventory	5000	Accounts payable	1000
Accounts Receivable	3000		
Total current assets	10000	**Total current liabilities**	1500
Fixed assets		**Long-term liabilities**	
Land and buildings	13000	Mortgage	9000
Equipment	7000	Long-term loans	2000
Less Depreciation	1000	**Total Long-term liabilities**	11000
Total fixed assets	19000	**Total liabilities**	12500
		Capital	
		Shares	10000
		Retained earnings	6500
		Total capital	16500
TOTAL ASSETS	**29000**	**TOTAL LIABILITIES AND CAPITAL**	**29000**

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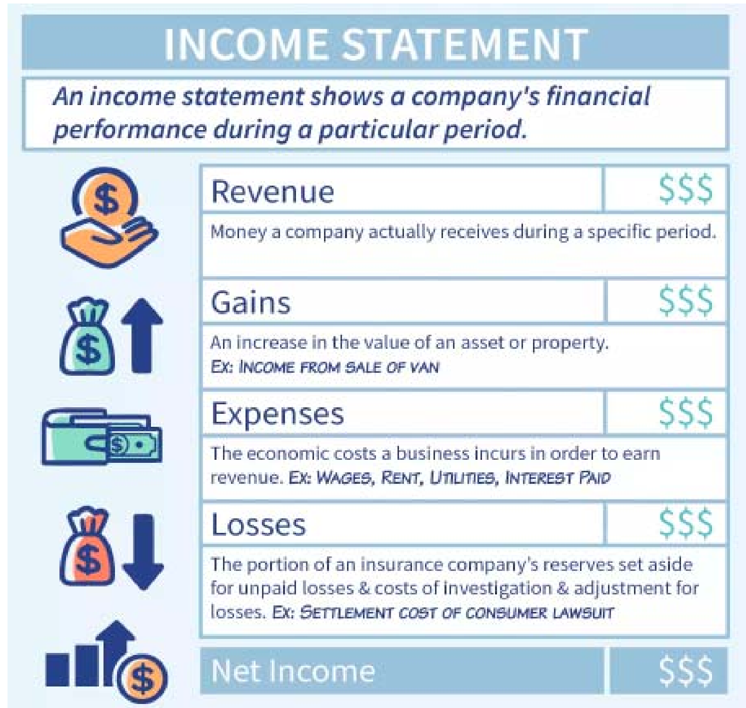
Income Statement

An income statement is one of the three important financial statements used for reporting a company's financial performance over a specific accounting period, with the other two key statements being the balance sheet and the statement of cash flows.

Also known as the profit and loss statement or the statement of revenue and expense, the income statement primarily focuses on the company's revenues and expenses during a particular period.



The income statement focuses on four key items—revenue, expenses, gains, and losses. It does not differentiate between cash and non-cash receipts (sales in cash versus sales on credit) or the cash versus non-cash payments/disbursements (purchases in cash versus purchases on credit). It starts with the details of sales, and then works down to compute the net income and eventually the earnings per share (EPS). Essentially, it gives an account of how the net revenue realized by the company gets transformed into net earnings (profit or loss).

Revenues and Gains

The following are covered in the income statement, though its format may vary depending upon the local regulatory requirements, the diversified scope of the business and the associated operating activities:

Operating Revenue

Revenue realized through primary activities is often referred to as operating revenue. For a company manufacturing a product, or for a wholesaler, distributor or retailer involved in the business of selling that product, the revenue from primary activities refers to revenue achieved from the sale of the product. Similarly, for a company (or its franchisees) in the business of offering services, revenue from primary activities refers to the revenue or fees earned in exchange of offering those services.

Non-Operating Revenue

Revenues realized through secondary, non-core business activities are often referred to as non-operating recurring revenues. These revenues are sourced from the earnings which are outside of the purchase and sale of goods and services and may include income from interest earned on business capital lying in the bank, rental income from business property, income from strategic partnerships like royalty payment receipts or income from an advertisement display placed on business property.

Gains

Also called other income, gains indicate the net money made from other activities, like the sale of long-term assets. These include the net income realized from one-time non-business activities, like a company selling its old transportation van, unused land, or a subsidiary company.

Revenue should not be confused with receipts. Revenue is usually accounted for in the period when sales are made or services are delivered. Receipts are the cash received and are accounted for when the money is actually received. For instance, a customer may take goods/services from a company on 28 September, which will lead to the revenue being accounted for in the month of September. Owing to his good reputation, the customer may be given a 30-day payment window. It will give him time till 28 October to make the payment, which is when the receipts are accounted for.

Expenses and Losses

The cost for a business to continue operation and turn a profit is known as an expense. Some of these expenses may be written off on a tax return if they meet the IRS guidelines.

Primary Activity Expenses

All expenses incurred for earning the normal operating revenue linked to the primary activity of the business. They include the cost of goods sold (COGS), selling, general and administrative expenses (SG&A), depreciation or amortization, and research and development (R&D) expenses. Typical items that make up the list are employee wages, sales commissions, and expenses for utilities like electricity and transportation.

Secondary Activity Expenses

All expenses linked to non-core business activities, like interest paid on loan money.

Losses as Expenses

All expenses that go towards a loss-making sale of long-term assets, one-time or any other unusual costs, or expenses towards lawsuits.

While primary revenue and expenses offer insights into how well the company's core business is performing, the secondary revenue and expenses account for the company's involvement and its expertise in managing the ad-hoc, non-core activities. Compared to the income from the sale of manufactured goods, a substantially high-interest income from money lying in the bank indicates that the business may not be utilizing the available cash to its full potential by expanding the production capacity, or it is facing challenges in increasing its market share amid competition. Recurring rental income gained by hosting billboards at the company factory situated along a highway indicates that the management is capitalizing upon the available resources and assets for additional profitability.

Income Statement Structure

Mathematically, the Net Income is calculated based on the following:

Net Income = (Revenue + Gains) – (Expenses + Losses)

Cash Flow Statement

A cash flow statement is a financial statement that provides aggregate data regarding all cash inflows a company receives from its ongoing operations and external investment sources. It also includes all cash outflows that pay for business activities and investments during a given period.

A company's financial statements offer investors and analysts a portrait of all the transactions that go through the business, where every transaction contributes to its success. The cash flow statement is believed to be the most intuitive of all the financial statements because it follows the cash made by the business in three main ways—through operations, investment, and financing. The sum of these three segments is called net cash flow.

Operating Activities	
Sales Receipts	$50,00,000
Payments for Products	($25,00,000)
Payments for Operations	($20,00,000)
Interest Payments	($1,00,000)
Taxes	($2,27,500)
Extraordinary Items	$2,00,000
Net Cash Flow from Operating Activities	***$3,72,500***
Investing Activities	
Purchase of New Fixed Assets (Property/Machinery)	($21,00,000)
Interest Received	$50,000
Net Cash Flow from Investing Activities	***($20,50,000)***
Financing Activities	
Short-term Debt	$7,00,000
Long-term Debt	$11,00,000
New Equity Issued	$5,00,000
Net Cash Flow from Financing Activities	***$23,00,000***
Net Increase (Decrease in Cash)	$6,22,500
Cash at the Beginning of the Year	$1,00,000
Cash at the End of the Year	**$7,22,500**

Cash Flows From Operations

This is the first section of the cash flow statement covers cash flows from operating activities (CFO) and includes transactions from all operational business activities. The cash flows from operations section begins with net income, then reconciles all noncash items to cash items involving operational activities. So, in other words, it is the company's net income, but in a cash version.

This section reports cash flows and outflows that stem directly from a company's main business activities. These activities may include buying and selling inventory and supplies, along with paying its employees their salaries. Any other forms of in and outflows such as investments, debts, and dividends are not included.

Companies are able to generate sufficient positive cash flow for operational growth. If there is not enough generated, they may need to secure financing for external growth in order to expand.

For example, accounts receivable is a noncash account. If accounts receivable go up during a period, it means sales are up, but no cash was received at the time of sale. The cash flow statement deducts receivables from net income because it is not cash. The cash flows from the operations section can also include accounts payable, depreciation, amortization, and numerous prepaid items booked as revenue or expenses, but with no associated cash flow.

Cash Flows From Investing

This is the second section of the cash flow statement looks at cash flows from investing (CFI) and is the result of investment gains and losses. This section also includes cash spent on property, plant, and equipment. This section is where analysts look to find changes in capital expenditures (capex).

When capex increases, it generally means there is a reduction in cash flow. But that's not always a bad thing, as it may indicate that a company is making investment into its future operations. Companies with high capex tend to be those that are growing.

While positive cash flows within this section can be considered good, investors would prefer companies that generate cash flow from business operations—not through investing and financing activities. Companies can generate cash flow within this section by selling equipment or property.

Cash Flows From Financing

Cash flows from financing (CFF) is the last section of the cash flow statement. The section provides an overview of cash used in business financing. It measures cash flow between a company and its owners and its creditors, and its source is normally from debt or equity.

Analysts use the cash flows from financing section to determine how much money the company has paid out via dividends or share buybacks. It is also useful to help determine how a company raises cash for operational growth.

Cash obtained or paid back from capital fundraising efforts, such as equity or debt, is listed here, as are loans taken out or paid back.

When the cash flow from financing is a positive number, it means there is more money coming into the company than flowing out. When the number is negative, it may mean the company is paying off debt, or is making dividend payments and/or stock buybacks.

Financial Ratios

Ratio—the term is enough to curl one's hair, conjuring up those complex problems we encountered in high school math that left many of us babbling and frustrated. But when it comes to investing, that need not be the case. In fact, there are ratios that, properly understood and applied, can help make you a more informed investor.

Applying formulae to the investment game may take some of the romance out of the process of getting rich slowly. The ratios could help you pick the best stocks for your portfolio, build your wealth and even have fun doing it. There are dozens of financial ratios that are used in fundamental analysis, here we only briefly highlighted six of the most common and basic ones. Remember that a company cannot be properly evaluated or analyzed using just one ratio in isolation - always combine ratios and metrics to get a complete picture of a company's prospects.

1. **Working Capital Ratio**

Working capital represents a company's ability to pay its current liabilities with its current assets. Working capital is an important measure of financial health since creditors can measure a company's ability to pay off its debts within a year.

Working capital represents the difference between a firm's current assets and current liabilities. The challenge can be determining the proper category for the vast array of assets and liabilities on a corporate balance sheet and deciphering the overall health of a firm in meeting its short-term commitments.

Assessing the health of a company in which you want to invest involves understanding its liquidity—how easily that company can turn assets into cash to pay short-term obligations. The working capital ratio is calculated by dividing current assets by current liabilities.

So, if XYZ Corp. has current assets of $8 million, and current liabilities of $4 million, that's a 2:1 ratio—pretty sound. But if two similar companies each had 2:1 ratios, but one had more cash among its current assets, that firm would be better able to pay off its debts quicker than the other.

2. **Quick Ratio**

Also called the acid test, this ratio subtracts inventories from current assets, before dividing that figure into liabilities. The idea is to show how well current liabilities are covered by cash and by items with a ready cash value. Inventory, on the other hand, takes time to sell and convert into liquid assets.

$$\text{Liquidity ratio} = \frac{\text{current assets} - \text{inventory}}{\text{current liabilities}}$$

If XYZ has $8 million in current assets minus $2 million in inventories over $4 million in current liabilities, that's a 1.5:1 ratio. Companies like to have at least a 1:1 ratio here, but firms with less than that may be okay because it means they turn their inventories over quickly.

3. **Earnings per Share (EPS)**

When buying a stock, you participate in the future earnings (or risk of loss) of the company. Earnings per share (EPS) measures net income earned on each share of a company's common stock. The company's analysts divide its net income by the weighted average number of common shares outstanding during the year.

If a company has zero or negative earnings (i.e. a loss) then earnings per share will also be zero or negative.

4. **Price-Earnings (P/E) Ratio**

Called P/E for short, this ratio reflects investors' assessments of those future earnings. You determine the share price of the company's stock and divide it by EPS to obtain the P/E ratio.

If, for example, a company closed trading at $46.51 a share and EPS for the past 12 months averaged $4.90, then the P/E ratio would be 9.49. Investors would have to spend $9.49 for every generated dollar of annual earnings.

Note that if a company has zero or negative earnings, the P/E ratio will no longer make sense, and will often appear as N/A for not applicable.

Even so, investors have been willing to pay more than 20 times the EPS for certain stocks if hunch that future growth in earnings will give them an adequate return on their investment.

5. **Debt-Equity Ratio**

What if your prospective investment target is borrowing too much? This can reduce the safety margins behind what it owes, jack up its fixed charges, reduce earnings available for dividends for folks like you and even cause a financial crisis.

The debt-to-equity (D/E) is calculated by adding outstanding long and short-term debt, and dividing it by the book value of shareholders' equity. Let's say XYZ has about $3.1 million worth of loans and had shareholders' equity of $13.3 million. That works out to a modest ratio of 0.23, which is acceptable under most circumstances. However, like all other ratios, the metric has to be analyzed in terms of industry norms and company-specific requirements.

6. **Return on Equity (ROE)**

Common shareholders want to know how profitable their capital is in the businesses they invest it in. Return on equity is calculated by taking the firm's net earnings (after taxes), subtracting preferred dividends, and dividing the result by common equity dollars in the company.

Let's say net earnings are $1.3 million and preferred dividends are $300,000. Take that and divide it by the $8 million in common equity. That gives a ROE of 12.5%. The higher the ROE, the better the company is at generating profits.

Budgeting – Why & How?

A budget is an estimation of revenue and expenses over a specified future period of time; it is compiled and re-evaluated on a periodic basis. Budgets can be made for a person, a family, a group of people, a business, a government, a country, a multinational organization or just about anything else that makes and spends money. At companies and organizations, a budget is an internal tool used by management and is often not required for reporting by external parties. It outlines an organization's financial and operational goals.

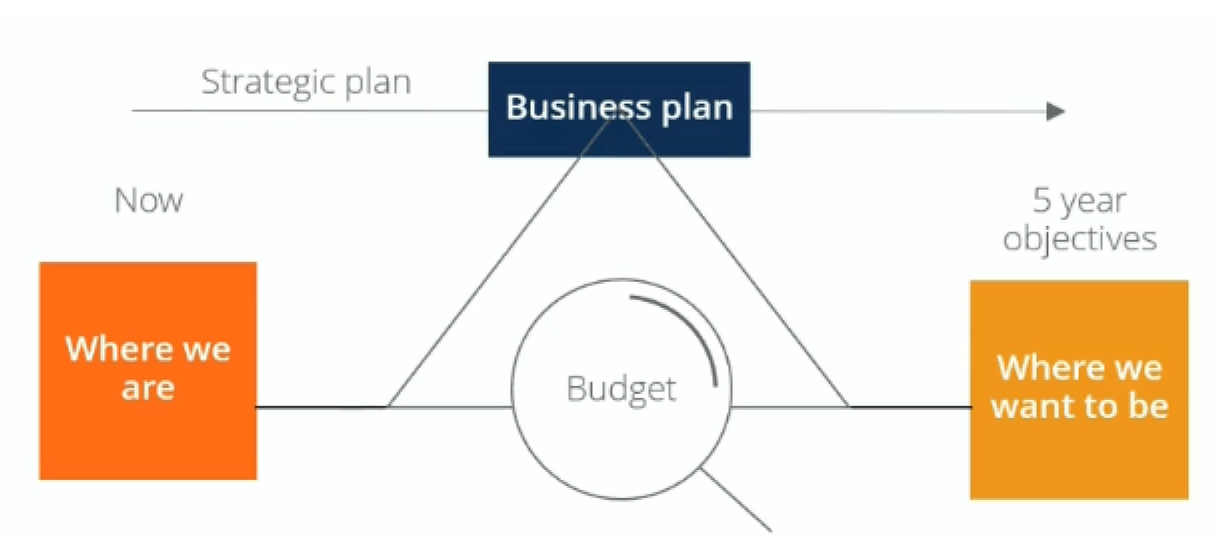
Budgeting is more than just a job we have to get done to satisfy the financial department. Planning and budgeting can help us lead our team to success. Sometimes, when we write a plan, we catch errors. It's a lot better to catch errors in a plan than to have problems later on in the office or on the shop floor because you didn't catch the errors. In fact, it's been shown that good planning will typically reduce the costs of a project by about a factor of 10.

A Corporate budgeting refers to the process by which a business estimates its finances for a future period and plans its operations accordingly. In developing a corporate budget, a business usually starts with a project plan, then determines the amount of time, goals and costs of the project.

Function

To achieve its goals, a business must express its strategy in a measurable way. The business must determine whether a project is financially feasible, then link the corporate goals with the available resources. Corporate budgeting allows higher management develop a strategy that makes sense to those in the lower levels of the organization.

It is a tactical implementation of a business plan. To achieve the goals in a business' strategic plan, we need some type of budget that finances the business plan, sets measures and indicators of performance, and then make changes along the way to ensure that we arrive at the company's goals.



Dimensions

There are four dimensions to consider when translating high-level strategy, such as mission, vision, and goals, into budgets.

1. **Objectives** are basically your goals, e.g., increasing the amount each customer spends at your retail store.
2. Then, you develop one or more **strategies** to achieve your goals. The company can increase customer spending through expanding product offerings, sourcing new suppliers, promotion, etc.
3. You need to track and evaluate the effectiveness of the strategies, using relevant **measures**. For example, you can measure the average weekly spending per customer and average price changes as inputs.
4. Finally, you should set **targets** that you would like to reach by the end of a certain period. The targets should be quantifiable and time-based, such as an increase in the volume of sales or increase in the number of products sold.

Objectives	Strategies	Measures	Targets
What are you trying to achieve?	**How are you going to achieve it?**	**What are the input and output measures?**	**Quantifiable and time-based**
• Increase spend per customer	• Expand product offering • Source new suppliers • Promotion and marketing • Pricing	• Average weekly spend/customer • Spend by product type • Average price changes	• $ increase • Volume increase • % staff trained in new products

Why we make a budget?

There are several good reasons to create a budget and to make it a good one. The reasons are tied to the people who will read and use the budget. Each reader will look at the budget in a different way and do something different with it. If you know your readers, you can make a budget that will impress everyone— and, more important, show how your group is contributing to the organization and therefore approve the funds you need to proceed. If you know how the budget will be used, you will know how to write it in an easy-to-use way. More important, it will help you succeed and show that you are a good manager and that your team is doing a good job.

Budgeting is a critical process for any businesses in several ways.

1. **Aids in the planning of actual operations.**

   The budgeting process gets managers to consider how conditions may change and what steps they need to take, while also allowing managers to understand how to address problems when they arise.

2. **Co-ordinates the activities of the organization**

   Budgeting encourages managers to build relationships with the other parts of the operation and understand how the various departments and teams interact with each other and how they all support the overall organization.

3. **Communicating plans to various managers**

   Communicating plans to managers is an important social aspect of the budgeting process, which ensures that everyone gets a clear understanding of how they support the organization. It encourages communication of individual goals, plans, and initiatives, which all roll up together to support the growth of the business. It also ensures appropriate individuals are made accountable for implementing the budget.

4. **Motivates managers to strive to achieve the budget goals**

   Budgeting gets managers to focus on participation in the budgeting process. It provides a challenge or target for individuals and managers by linking their compensation and performance versus budget.

5. **Control activities**

   Managers can compare actual spending with the budget to control financial activities.

6. **Evaluate the performance of managers**

   Budgeting provides a means of informing managers of how well they are performing in meeting targets they have set.