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**International financial statement analysis**

Financial statement analysis is a part of business analysis. Business analysis is the evaluation of a company’s business environment, strategies, financial position, and performance to be able to make decisions with respect to that company.

Financial statement analysis consists of the following steps:

1. **Accounting analysis**: Accounting analysis begins with an evaluation of the extent to which a company’s financial statements reflect economic reality. There are three common sources of distortion in financial statements:
* Accounting standards that are inconsistent with economic reality (a rule that requires all research and development costs to be expensed immediately with no possibility of recognizing an asset is an example).
* Estimation errors made by managers in applying accounting standards (the estimation of the cost of pension and other postretirement benefits is an example).
* The intentional manipulation of financial statements by managers; often referred to as earnings management (the intentional overstatement of an accrued restructuring charge is an example).
1. **Financial analysis:** it involves the use of adjusted financial statement information to conduct:
* Cash flow analysis: the analysis of how a company generates and uses cash.
* Profitability analysis: with a focus on return on invested capital
* Risk analysis: including an evaluation of liquidity and solvency to assess a company’s ability to meet its obligations.
1. **Prospective analysis:** it involves combining the results of accounting analysis and financial analysis, along with an analysis of the business environment and company strategy, to forecast future financial statement information, especially cash flows and income.

**Reasons to Analyse Foreign Financial Statements**

1. Foreign Portfolio Investment
2. International Mergers and Acquisitions
3. Making credit decisions about foreign customers.
4. Evaluating the financial health of foreign suppliers.
5. Benchmarking against global competitors.

**Potential Problems in Analysing Foreign Financial Statements**

Some of the potential problems that may arise in analysing foreign financial statements include:

1. Data Accessibility
2. Language
3. Terminology
4. Format
5. Extent of Disclosure
6. Timeliness
7. Differences in Accounting Principles