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INTERNATIONAL FINANCIAL STATEMENT ANALYSIS

Business analysis is the assessment of a company’s business environment, financial positions, strategies and performance in order aid decision making in respect to the company. It requires relevant information about the company and financial statements are an important source of information for business analysis. A financial statement analysis is made up of the following steps;

1. Accounting analysis. This involves the extent to which a company’s financial statements reflect economic reality. It involves the identification of distortions in the financial statements and making adjustments where possible. Three common sources of distortions are; accounting standards that are inconsistent with economic reality; estimation errors made by managers in applying accounting standards and; the intentional manipulation of financial statement by managers.

2. Financial analysis. This involves using adjusted financial statements to conduct cash flow analysis, probability analysis and risk analysis. It mostly involves the use of financial ratios and these ratios are compared within and across the company to determine whether the company is improving or declining in its ability to generate cash flow, earn returns on invested capital etc.

3. Prospective analysis. This involves combining the results of the aforementioned steps, as well as, business environment and company strategy analysis in order to predict future financial statement information, mostly cash-flow and income. The reasons for analysing foreign financial statements include; benchmarking against global competitors, international mergers and acquisitions, foreign portfolio investment etc. While problems that could arise from analysing foreign financial statements include; language, format, timeliness etc.