

Introduction to Financial Statement Analysis

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What is the purpose of financial statement analysis?

Answer: To help people make better decisions.

Consider this scenario:

A firm's inventory is destroyed in a fire and the firm recognises a substantial loss on its income statement because it was under-insured.

->How should this loss influence a financial statement analysis?

->Would you deduct this loss when determining the income of this firm?

->Why or why not?

Your analysis depends on your perspective and the decision you need to make.

If you are an equity investor, deciding whether to buy or sell this firm's shares

The loss can be considered as non-recurring noise, and should be excluded when extrapolating from past income to forecast future income in order to determine the market value of equity.

If you are a creditor with collateral in the inventory

Your focus should be on the repayment from the insurance and other available sources.

If you are a board member, determining the bonus the management should receive

The loss should be considered, because the management has failed to insure the inventory adequately.

Therefore, financial statement analysis *matters* for

Equity-oriented
stakeholders



For example:
Equity investors
Financial analysts
Pension funds
Venture capital providers

Debt-oriented
stakeholders



For example:
Banks
*Mortgage-credit
institutes*
*Providers of
mezzanine capital*

Performance-oriented
stakeholders



For example:
The board
Management
Investors

Career opportunities for you

For further information, please refer to the textbook:

