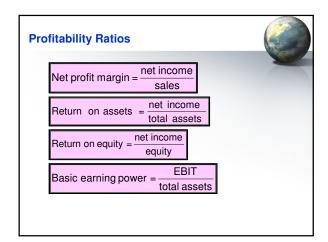
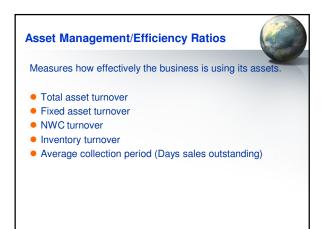
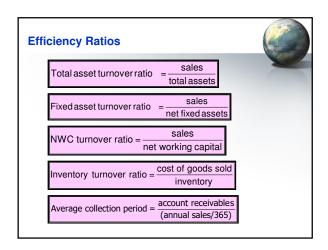
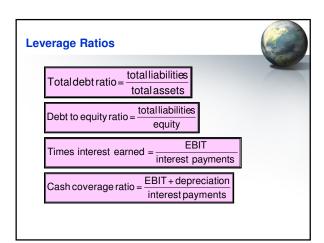
Ch. 4 Analysis of Financial Statements **Topics** Financial Ratios DuPont System Using Financial ratios **Financial Ratios** Financial Ratio Analysis: Technique used to examine a company's financial statements. Five areas Profitability Asset Management/Efficiency Debt Management/Leverage Liquidity Market Value • Common size analysis: Express a firm's I/S (and B/S) items in percentage of sales (and assets). Percentage change analysis: Focus on the growth rate of I/S and B/S items. **Profitability Ratios** Measures profit relative to revenue or an amount invested. Net profit margin Return on assets Return on equity Basic earning power

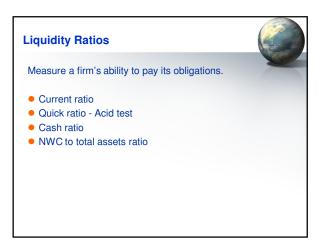


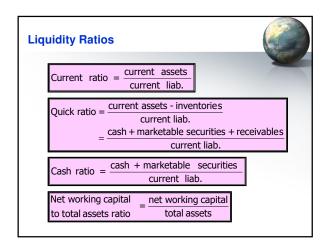


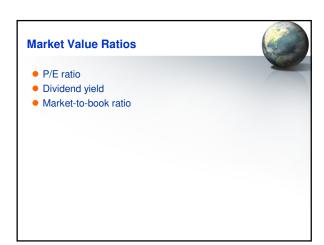


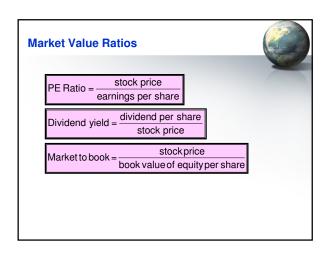












Commonsize Analysis

- Commonsize analysis, also referred as vertical analysis, coverts each item on balance sheet as a percent of total assets. For income statement, each item is shown as a percent of sales.
 - Commonsize analysis helps managers and investors to see how each item, relative to assets or sales, has changed over time.
 - It is also helpful when comparing firms with different sizes.

Percentage Change Analysis

- Percentage change analysis, also referred as horizontal analysis, computes the growth rate for each item over a period of time.
 - Percentage change analysis helps managers and investors to compare different growth rates for different items.
 - It also makes spotting long-term trends easier.

Two Period Example:

Percentage change for sales_t = $\frac{\text{sales}_t - \text{sales}_{t-1}}{\text{sales}_{t-1}}$

The DuPont System

A breakdown of ROE and ROA into component ratios

$$ROA = \frac{\text{net income}}{\text{assets}}$$

$$ROE = \frac{\text{net income}}{\text{equity}}$$

