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EQUILIBRIUM ANALYSIS OF FINANCIAL COMPANY BASED ON INFORMATION PROVIDED BY THE BALANCE SHEET

Lecturer PhD **Ştefăniţă ŞUŞU**
"Ştefan cel Mare" University of Suceava, Romania
stefanitas@seap.usv.ro

Abstract:
This article highlights the importance of indicators (as net working capital, working capital requirements and net cash) by means of which it is considered in the context of financial balances capitalization information released by the balance sheet of an entity tourist profile. Theoretical concepts presented in a logical sequence are combined with the practical example transposed Turism Covasna company. The results of the analysis are interpreted while trying to formulate solutions to the economic and financial viability of the entity.

Key words: balance sheet, financial balance, financial resources, uses financial flexibility.

JEL classification: M21, M41.

INTRODUCTION

The concept of financial balance is one of the most difficult to define financial, because the assumptions on which it is based and forms of expression that we have. Assumptions by which we can define and analyze financial balance refers to the functioning of financial markets and the behavior of those interested in knowing the financial situation of the company (shareholders and creditors). In this context, the economist G. Charreaux shows that *financial stability is satisfied if the retrofit investments can satisfy requirements in terms of rehabilitation of shareholders and creditors, given the risks they bear*. Risks may arise while the financial market does not work perfectly. In this case change the economic behavior of third parties: shareholders, if it is quotable operate with their actions and lenders reduce its loans. From the economic point of view, the assessment of financial balance is related to its objectives, which are survival, providing a satisfactory return for those who have brought the resources necessary for economic activity, economic growth, diversification and development depending on opportunities. All these represent the major objective of the enterprise: the enterprise value maximization. The financial equilibrium depends on the financial flexibility that is sometimes confused. Financial flexibility is the ability of an enterprise to take the necessary measures to amend the schedule of values and cash movements, in order to cope with unforeseen needs and situations. It means an adequate financial structure, an arbitrage between size and equity, debt and cost, in order to ensure the financing of investment opportunities, strategic or commercial. In other words, it seeks the use of owned and borrowed resources of the entity. It can be said that for a trader, a financial balance appears as a state or as a system of partial states that cover all elements of heritage and its financial results. As part of the financial equilibrium, the the economic balance is given by the equality between the economic capital and the resources, the formation between the receipts and the payments between funds and resources. One way that we can express the financial equilibrium is the equality of financial resources and their uses.

The analysis of the financial balance of the assets of the business aims at reflecting the ratio of the equality between funding sources and the uses of financial resources of income and expenditure, company activity terms (long term, medium term, short term) and its main functional components (operating, financial extraordinary).

The financial analysis highlights the ways to achieve the financial balance with the objectives:

- *Long-term equilibrium* when covering permanent capital assets (working capital);

- *Current balance* when comparing current assets to short term liabilities (working capital needs);

- *Balance short-term* working capital when compared with the need for working capital (treasury).

The rates and the working capital are tools to measure the financial situation at a given time, their interpretation allowing to assess the present state of balance and to anticipate its evolution. The rates do not provide the information on the operations that lead to obtaining a state of equilibrium.

The analysis must consider the following:

- The increase of the active station is a use of funds during the period (the purchases from cash on hand or borrowings);

- The reduction of asset item is a resource (the physical or financial asset transformation into currency);

- The growth of a passive post is a resource (the increase of equity or loan capital).

The movement in balance sheet values summarizes the equilibrium relations, the material and technological imbalance between the consumption of material and energy resources (actual input) and the production of useful goods and services (real outputs), which reflects the relationship of balance-imbalance value of collections current payments, receivables and short term liabilities, assets and permanent capital.

Regarding the financial equilibrium analysis, this was based on the information provided by the financial statements (balance sheet) of the Turism Covasna company, taken from the Stock Exchange website, Bucharest (www.bvb.ro).

In order to perform the analysis of the financial equilibrium, the information in the balance sheet were adjusted for the liquidity-chargeability of assets and liabilities, respectively, as shown in the balance sheet below:

Financial Balance at 31.12.2012

Asset	Balance at		Liabilities	Balance at	
	01.01.2012	31.12.2012		01.01.2012	31.12.2012
Intangible assets	7.189	26.725	Equity	25.651.398	32.233.923
Tangible assets	31.676.307	47.771.202	Debs of more than 1 year	9.687.523	19.297.493
Financial assets	3.390	3.390	Debts of less than 1 year	7.776.596	2.604.034
Fixed assets	*31.686.886*	*47.801.317*	Provisions	57.706	53.349
Stocks	187.967	355.676	Revenue in advance	107.190	335.136
Claims	772.484	1.546.351			
Short-term investments	12.296	16.240			
Cash and bank accounts	10.593.315	4.781.437			
Current assets	*11.566.062*	*6.699.704*			
Prepayments	27.465	22.914			
TOTAL ASSETS	***43.280.413***	***54.523.935***	***TOTAL LIABILITIES***	***43.280.413***	***54.523.935***

Source: Information processed by balance sheet of TURISM COVASNA Company

The main indicators that are calculated based on the balance sheet in order to reflect the financial balances are *the net situation (NS), the working capital (WC), the need for working capital (NWC)* and *the net cash (NC).*

They are static indicators; they express a certain state of a business at some point comparing the balance sheets items liability with the asset. This is an interesting evolution of these indicators from one period to another, based on the data that can be obtained from several consecutive balance sheets.

THE NET SITUATION ANALYSIS

The simplest expression of the value of the date of closure of businesses represents the net asset value (the net situation) and the equity, calculated as the difference between the total assets and the total debt contracted, or by adding to the capital reserves due to the results or shareholders. Unlike equity, the notion of net situation is more restrictive in their category excluding investment subsidies and allowances covered. Therefore, the net situation is a more relevant indicator expressing the value of activities at a certain time. This indicator is interesting not only for the shareholders and the company owners who want to know the value they possess, but equally for the lenders for which the collateral asset is feasible for their claims. The situation highlights the net amounts that will return to members or shareholders in case of liquidation.

The positive and the increasing net situation reflects a healthy economic situation since the company's assets are growing faster than the debt accumulated by it, and the net profits are generally positive, while the negative value pointer highlights an unhealthy situation of the company, to be facing soon. An enterprise fund is unable to work in the long term accumulation of debt; in this case it is not economically viable. Of course, during the expansion of the business, the investment needs are also greater than the internal resources generated by the operating profits and the cash flows, the company will attract debt sources in order to fund this expansion. But it is essential that any asset growth will also result in an increase of the profits or enterprise competitiveness [9].

So, in order to exemplify the methodology of calculation of net positions there are used financial data which are presented in the table below:

Table no. 1. Methodology of calculation of the net statement

Current Issue	Computing elements	Financial year		Absolute change	Development indices (%)
		2011	2012		
1	Total assets	43.280.413	54523935	+11.243.522	125.98
2	Total debt	17.464.119	21901527	+4.437.408	125.41
3	Revenue in advance	107.190	335.136	+227.946	312.66
4	Provisions	57.706	53349	-4.357	92.45
5	**Statement of Net (1-2-3-4)**	***25.651.398***	***32.233.923***	***+6.582.525***	***125.66***
6	Total assets - Current liabilities	35.396.627	51.584.765	+16.188.138	145.73
7	Debts of more than one year	9.687.523	19.297.493	+9.609.970	199.20
8	**Statement of Net (6-7-4)**	***25.651.398***	***32.233.923***	***+6.582.525***	***125.66***

Source: the balance sheet of TURISM COVASNA Company

The positive value of the net in the entity under review reflects a sound economic management. Based on the data from the above table it is found that the increase of the net with 6582525 RON (25.66%) was the consequence of the increase in net assets of 11,243,522 RON (25.98%) due to higher total debt of 4,437,408 RON (25.41%), revenues in advance 227 946 RON (212.66%) and lower provisions to 4357 RON (-7.55%). Also the increase in equity (net situation) is the result of the reinvestment of part of the net profit, proving favorable development and increase of the company's net assets.

THE ANALYSIS OF THE WORKING CAPITAL

The working capital represent the surplus resulted when the resources are beyond what is required to finance the company's permanent needs[4], which serves to pay the suppliers, the raw materials waiting to be turned into products which are sold and collected.

It is important that the time lag between the payment of expenses and the revenue collection, to be borne by the permanent capital. In addition, given that the need for the working capital does not produce cash, it is preferable that its funding not to be from loans (which require cash outflows with some regularity), but from equities (capitalized benefits increases of capital or transfer of assets).

This indicator has the character of a *safety margin* that allows the company financial independence from lenders when there are issues of current activity [10], which increases the confidence of funding partners (shareholders and creditors), which in turn will answer, in terms of funding, depending on the strategy that has established a compliance with certain financial structure designed to maximize the enterprise value [1].

The working capital as an indicator is used in Western practice and has a particular importance for the analysis of the financial equilibrium of the company in the long term. The financing and investment policy of the company is supported by the working capital because it shows the existence of difficulties.

Regarding the method of calculation, the working capital can be determined based on the financial balance sheet in two ways:

a) Based on the elements with a permanent character (from top financial accounts)

In this case, the working capital surplus expresses the permanent resource over-current assets, and it is calculated using:

FR = Permanent capital - Fixed assets

b) Based on the short-term elements (from financial accounts)

According to this operation, the accepted working capital highlights that part of current assets that cannot be funded on the basis of short-term liabilities, determining the relationship:

FR = Current assets – Short-term debt

In order to illustrate the methodology of calculation of the working capital here are used the financial data presented in the table below:

Table no. 2. Methodology of calculation of working capital

Computing elements	Financial year		Absolute change	Development indices (%)
	2011	2012		
I. Working capital = Permanent capital – Fixed assets (net)				
1. Equity	25.651.398	32.233.923	+6.582.525	125.66
2. Debs of more than 1 year	9.687.523	19.297.493	+9.609.970	199.20
3. Investment subsidies	97.319	327.114	+229.795	336.13
4. Provisions (long term)	57.706	53.349	-4.357	92.45
5. Permanent capital	*35.493.946*	*51.911.879*	*+16.417.933*	*146.26*
6. Fixed assets net	*31.686.886*	*47.801.317*	*+16.114.431*	*150.86*
Working capital I	***3.807.060***	***4.110.562***	***+303.502***	***107.97***
II. *Working capital* = Current assets net – Debts of less than 1 year				
1. Current assets	11.566.062	6.699.704	-4.866.358	57.93
2. Prepayments	27.465	22.914	-4.551	83.43
3. Asset net working (total)	*11.593.527*	*6.722.618*	*-4.870.909*	*57.99*
4. Debts of less than 1 year	7.776.596	2.604.034	-5.172.562	33.49
5. Revenue received in advance	9.871	8.022	-1.849	81.27
6. Debts of less than 1 year (total)	*7.786.467*	*2.612.056*	*-5.174.411*	*33.55*
Working capital II	***3.807.060***	***4.110.562***	***+303.502***	***107.97***

Source: own after the balance sheet of TURISM COVASNA Company

Analyzing the data in the table above is an increase in working capital of 303 502 RON (7.97%), which reflects the financial balance between resources and needs permanent funding. The company has a surplus of permanent resources that finance temporary needs financial resources. The favorable evolution of the working capital (7.97%) is explained by increasing both permanent resources (46.26%) and the permanent needs (50.86%). The permanent increase in resources is essentially the effect of increasing the minimum capital of the company, the long-term debt and the investment subsidies. The increasing demand is the result of permanent financed investments in intangible assets (purchase of software), tangible assets (equipment furnished, equipment, new facilities).

The working capital calculated based on items in the bottom of the financial balance sheet highlights the trend of growth, showing that the liquidity of current assets is higher chargeability achievable and available short-term liabilities; the enterprise is potentially liquid, despite the fact that both the temporary needs likely to be turned into cash decreased by 42.21% and also the temporary resources that would become payable were reduced by 66.45%.

THE ANALYSIS OF THE NECESSARY WORKING CAPITAL

Some analysts believe that the demand for the working capital is the most relevant indicator for the study of the financial equilibrium, because it keeps the structure of assets and liabilities and the current liquidity ratio/chargeability of them [4].

The working capital requirements designate the financial needs generated by the execution of the repetitive operations that make up the current operating cycle (purchases, sales, paying salaries), all of which must be covered at least partially stable resources [5].

The working capital requirements of current assets covered by expressing in terms of short-term financial resources (suppliers and other current liabilities) and other resources that are needed. It is determined as the difference between current assets (except cash) and short-term liabilities (excluding short-term bank loans). The size of the working capital requirement is determined by the size of current assets used in the short term, which is different depending on the specificities of each sector or branch of activity [9].

Unlike the working capital, reflecting the financial balance in the long term, the working capital requirements reflect the company's current balance which is more fluctuating, more unstable and depends on the following factors: turnover, production cycle, duration of rotation stocks, the gap between the return on receivables and the payment of suppliers.

In this regard, the need for the working capital can be expressed in days sales via *speed of rotation*, reflecting the unfavorable gap between receipts and payments (normal should be between 30-60 days) [5].

In order to illustrate the methodology of calculation of the working capital needs there are used the financial data presented in the table below:

Table no. 3. Methodology of calculation of the necessary working capital

Computing elements	Financial year		Absolute change	Development indices (%)
	2011	2012		
(+) Current assets	11.566.062	6.699.704	-4.866.358	57.93
(+) Active regularization	27.465	22.914	-4.551	83.43
(-) Cash	10.593.315	4.781.437	-5.811.878	45.14
(-) Short-term investments	12.296	16.240	+3.944	132.08
Temporary needs	*987.916*	*1.924.941*	*+937.025*	*194.85*
(+) Debts of less than 1 year	7.776.596	2.604.034	-5.172.562	33.49
(+) Liabilities regularization	9.871	8.022	-1.849	81.27
(-) Short-term bank loans	1.172.394	1.711.811	+539.417	146.01
Temporary resources	*6.614.073*	*900.245*	*-5.713.828*	*13.61*
NWC = Temporary needs – Temporary resources	***-5.626.157***	***1.024.696***	***+6.650.853***	**-**

Source: the balance sheet of TURISM COVASNA Company

The negative working capital requirement in 2011 highlights the temporary resource surplus (6,614,073 RON) in relation to the need to finance the current assets (987916 RON). This can be regarded as positive if the rotation speed is due to the acceleration of current assets or liabilities in the result of obtaining a more distant chargeability, which is equivalent to reducing the deadlines of the receipts and the relaxation in case of payment obligations to third parties.

The positive working capital requirements in 2012 reflects an additional temporary needs (1,924,941 RON) in relation to the temporary resources that can be mobilized (900245 RON). This can be considered normal as a result of the investments which increased the borrowing of the operating cycle.

THE ANALYSIS OF THE NET CASH

The net cash is the most conclusive expression of an activity, it is balanced and effective. It shows the quality of the company's overall balance both in the long-term and in the short-term.

The positive value of this indicator shows an economic growth, but also the effect of a slowdown in the inventory turnover and receivables, while the negative value will highlight a surplus of temporary sources as a result of accelerating the rotation of the current assets [8].

In order to illustrate the methodology for calculating the net cash there are used the financial data presented in the table below:

Table no. 4. Methodology of calculation of the net cash

Computing elements	Financial year		Absolute change	Development indices (%)
	2011	2012		
Working capital	3.807.060	4.110.562	+303.502	107.97
Necesary working capital	-5.626.157	1.024.696	+6.650.853	-
I. Net cash	***9.433.217***	***3.085.866***	***-6.347.351***	***32.71***
(+) Available in bank accounts	10.593.315	4.781.437	-5.811.878	45.14
(+) Short-term investments	12.296	16.240	+3.944	132.08
Active Treasury (AT)	***10.605.611***	***4.797.677***	***-5.807.934***	***45.24***
Short-term bank loans	1.172.394	1.711.811	+539.417	146.01
Treasury Liabilities (TL)	***1.172.394***	***1.711.811***	***+539.417***	***146.01***
II. TN = AT – TL	***9.433.217***	***3.085.866***	***-6.347.351***	***32.71***

Source: own after the balance sheet of TURISM COVASNA Company

The positive net cash in both periods is the expression of the financial equilibrium established at the enterprise level. In 2011, a favorable situation occurs both as a result of a surplus of financial standing and as a temporary surplus of resources as a result of performance management operating cycle. In 2012, as a consequence of a positive working capital and higher working capital requirements, it was provided a funding operating cycle but there was a worsening of the treasury (negative cash flow), especially due to the increasing short term bank loans (46.01%) given the lower cash and cash equivalents (-54.86%).

CONCLUSIONS

A very important principle in financing the economic activity of the enterprise is the need to cover the assets and the undertaking of the procured capital remaining at its disposal for a certain period, at least equal to the life of those assets. This is an elementary but not a sufficient condition to ensure the financial stability of the company. Only in this way one can provide the necessary liquidity and a healthy treasury. It is an important condition to be met in order to avoid the risk of default and therefore a greater risk of bankruptcy. At the same time, the respect of the rules and the insurance of the necessary liquidity enhance the contribution of the enterprise to ensure a healthy monetary movement in the economy and to avoid bottlenecks in chain.

In order to cover the gap flows (cash flow deficiency) of the Turism Covasna company, we recommend the decreasing due to predictable revenue by reducing the trade credit to customers or by request in advance of the sales receipt; deferral of payments. However, we also recommend trying the postponement of expenditures (investments, etc.) the achievement of extraordinary income (through sale of available assets that are not necessary and have not ended their life). If, however, the treasury balance is kept scanty, it may be covered by new loans, but that will increase the indebtedness of the company and the additional costs.

For a better analysis of the company's financial situation it is also necessary to monitor the financial rates, an issue that will be discussed in a future article. This analysis will show to what degree the company can meet its payment obligations, how much it can be funded through loans, how efficiently the assets at its disposal are used, not at least its management efficiency.

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