The Financial Performance

Study Unit 3

Study Unit 3: The Financial Performance

What do users want to know about your financial performance

Lecture 1

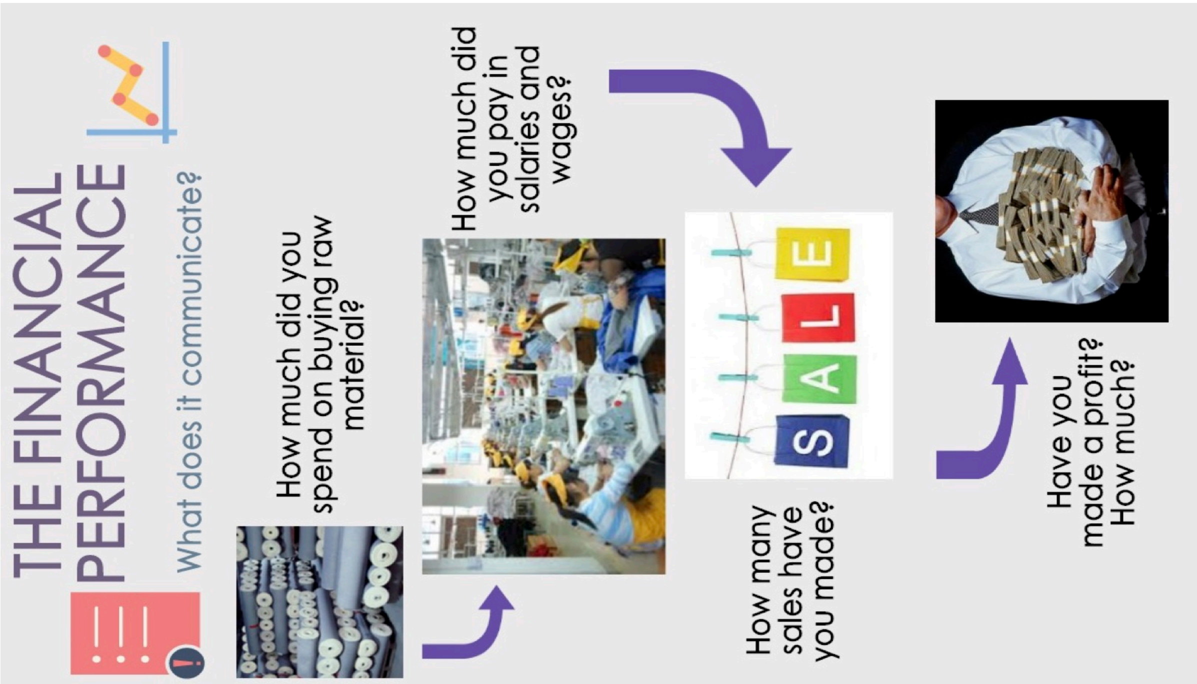
Basic business example

- We'll use the interactive infographic from Study Unit 2, and this time, consider what users may want to know about your financial performance

Use this infographic as a tool to visualise WHY we include and prepare information the way we do

Lecture 1

A basic business example



Lecture 1

A basic business example

- Would users of your financial information want to know the following:
  - How much you've spent on raw materials for your product?
  - How much you've spent making your product?
  - How much you've paid in salaries and wages?
  - How many sales you've made?
  - Your profit for the year? For the prior year?

Lecture 1

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The types of financial information that must be included

Lecture 2

Financial Performance information

- What are the results of your financial performance for the year?
  - Income
  - Expenses
  - Profit / Loss

Lecture 2

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The elements of the Statement of Profit or Loss and Other Comprehensive Income

Lecture 3

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Profit = Income - Expenses

Lecture 3

Income

- Increases in economic benefits during the accounting period
  - In the form of inflows or enhancements of assets
  - Or decreases of liabilities
- Results in an increase in Equity
  - Does NOT include Equity increases from capital contributions

Lecture 3

Expenses

- Decreases in economic benefits during the accounting period
  - In the form of outflows or depletions of assets
  - Or increases of liabilities
- Results in a decrease in Equity
  - Does NOT include Equity distributions

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Profit and Equity

Profit / Loss

- Income – Expenses = Profit
- If Expenses are more than Income, then you will make a Loss

Lecture 3

Income & Expense: Examples

- A short read, listing some examples of income and expenses that we will probably come across in this module
- Note that not all income is considered revenue

Lecture 4

Income & Expense: Examples

- Revenue earned from ordinary activities:
  - Fees Earned
  - Sales
  - Interest Income
    - If you're in the business of making loans, then this is your ordinary activity
    - If you're not in the business of making loans, then this will be Other Income, not Revenue
  - Dividend Income
    - If your business is owning shares, then this is your ordinary activity
    - If not, then this will be Other Income, not Revenue

Income & Expense: Examples

- Rent Income
  - If you're in the business of owning property and renting them out, then this is your ordinary activity
  - If not, then this will be Other Income, not Revenue
- Commission Income
  - If your business is earning commission on sales, then this is your ordinary activity
  - If not, then this will be Other Income, not Revenue

Income & Expense: Examples

- Normal Expenses:
  - Purchases of inventory
  - Transport costs on purchases and sales
  - Rent expense
  - Salaries and wages
  - Depreciation
  - Administrative expenses
  - Water & electricity
  - Advertising
  - Interest expense
  - Insurance

Lecture 4

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Relationship between Performance and Position?

Lecture 5

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Profit and Equity - Example

Effect of Profit on Equity

- Equity is the owners' share of the business
- If you made a profit, then you have a net increase in assets
- This increase will belong to the owners, thus it becomes Equity
- Equity = Capital + Profit

Equity & Profit: Example

- Bob's Electrical Financial Position information at the beginning of the year:
  - Assets: R100 000
  - Equity: R 60 000
  - Liabilities: R 40 000
- The income and expenses for the year:
  - Revenue: R 20 000
  - Wages paid: R 8 000
  - General Expenses: R 2 000

Equity & Profit: Example

- *BAE at the beginning of the year:* *A = E + L*

  100 000 = 60 000 + 40 000
- *Profit = Income – Expenses*

  Profit = 20 000 – (8 000 + 2000)

  Profit = 20 000 – 10 000

  Profit = 10 000
- *Equity at the end of the year:*

  Equity at the beginning of the year + Profit for the year

  60 000 + 10 000 = 70 000

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Income and Expenses: Differentiating between ordinary activities and other gains and losses

Lecture 6

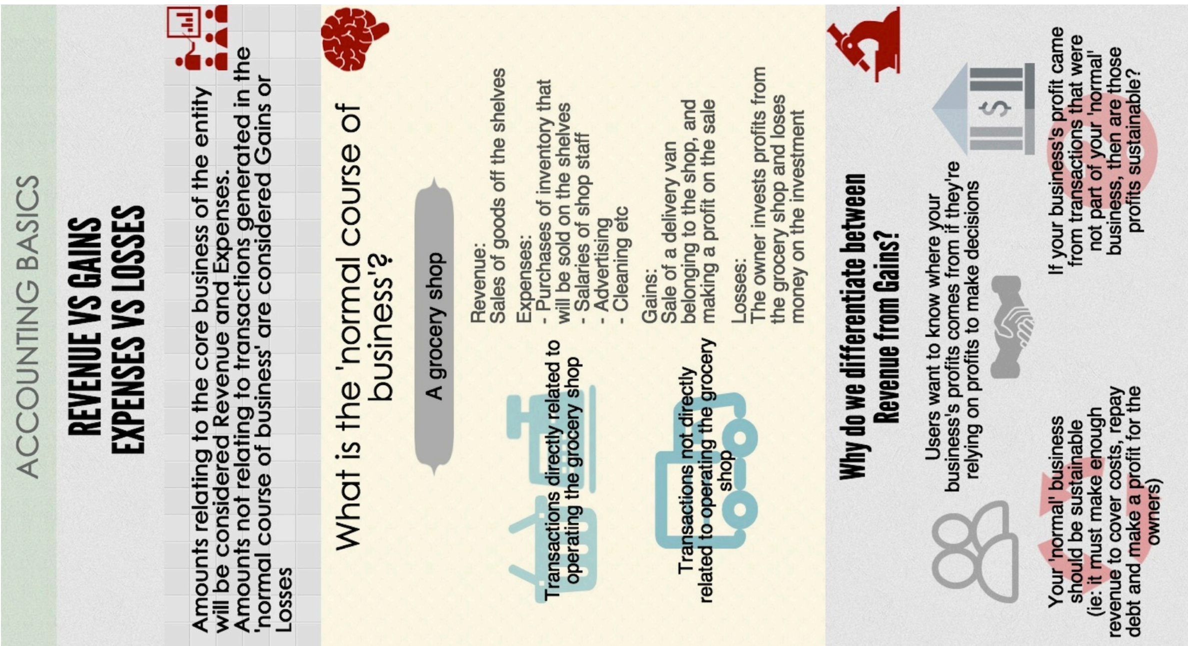
Revenue vs Gains; Expenses vs losses

- The infographic explains the difference between amounts generated within the 'normal' course of business and other amounts

Use this infographic as a tool to understand why we make this differentiation

Lecture 6

Revenue vs Gains; Expenses vs losses



Lecture 6

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The Statement of Changes in Equity

Lecture 7

Statement of Changes in Equity

- A short read on the contents of this part of the financial statements

We'll look at examples of this in Study Unit 4

Statement of Changes in Equity

- This part of the Annual Financial Statements includes information on the changes in ownership and equity from year to year
- It will indicate the Equity at the beginning of the year, any additional capital contributions, any drawings taken out by the owners, and add or deduct the profit or loss for the year. This will leave you with the end of year balance on Equity

Statement of Changes in Equity

- Basic format:
  - Equity (beginning of year)
  - Additional Contributions during the year
  - Drawings during the year (deducted from equity)
  - Add: Profit for the year (or Deduct: Loss for the year)
  - Closing balance on Equity

Lecture 7

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Notes to the Financial Statements

Lecture 8

Notes to the Financial Statements

- A short read on the need for additional information to be disclosed in the Financial Statements

We'll look at examples of this in Study Unit 4

Notes to the Financial Statements

- Not everything can be communicated by numbers. Some information, or additional information about the basis for the calculations and measurements is given in the Notes to the Financial Statements.

We will not be going into detail on the Notes until later in the module