

AN EVALUATION OF SELECTED ASSETS AND THEIR IMPACT ON THE DECLARATIVE CHARACTERISTIC OF RATIO INDICATORS IN FINANCIAL ANALYSES

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Introduction

The current state of the economy often places managers in the position where they have to determine how to best adjust criteria in order to measure success and define the required objectives. The current economic situation is marked by permanent changes, emerging new obstacles and opportunities. The main objective pursued by the majority of companies over the long-term horizon is increasing or maximizing their market value through their corporate strategy. The aim of this paper is to show concrete results of Czech firms to inventory valuation using their own expense or through direct costs may affect the explanatory power of certain indicators of financial analysis. At the same time article discusses the issue of the use of derivatives and their impact on the valuation of assets and the consequent influence the results of the financial analysis. The last part of the contribution includes the results of the survey related to the analysed issue. The research was conducted on business entities located in the Czech Republic that are interested in industrial production.

The question is what approach should actually be employed to measure the performance of a particular company and what methods should be used. This issue has been addressed by numerous economists worldwide. There is a wide range of approaches and methodologies that can be used to evaluate performance that measurement performance from both the financial and non-financial points of view. [19] A company's performance is a fairly common concept today, yet there is no single accurate definition of what it means. The term company performance is used in connection with determining the merits of a company's existence, its success and ability to survive. The purpose of measuring and evaluating a company's performance is to assess the company's actual condition, which is essential

for its owners and executive managers to be able to make future decisions; it is also a vital prerequisite for continued successful management of a company. Performance is mostly associated with efficiency, which refers to a company's ability to achieve certain objectives. This background can be used when determining a company's performance as its ability to best utilise and increase the funds that have been invested into the business's operations. When associated with a company, the meaning of the term performance appears to be even clearer, yet performance needs to be precisely defined so that it can be evaluated. Unfortunately, there is no harmonised definition for this term, which is why the term performance can be interpreted in several ways. Performance is the scope of results achieved by individuals, teams, organisation and processes. [3]

Performance is mostly defined as the ability of a company (business entity) to best increase the value of investments made into its business activities. [20] A company's performance is generally associated with the growth of market value, which is the effort to pursue efficient utilisation of the equity and loan capital leading towards maximisation of the company's market value over the long-term horizon, which relates to making profits or at least establishing conditions suitable for the future generation of profit. [16]

A basic requirement imposed on the scales (indicators) that show a company's performance is to have an accurate evaluation of the current situation in a particular company and these results should then be used to correctly interpret the company's actual performance. A company's performance is typically determined over a longer period, e.g. one-half of a year or a year.

There have been many criteria developed to determine a company's performance. These criteria are based on both theoretical knowledge as well as practical experience.

Tab. 1: An evaluation of methods and models for measuring performance

Approach of the measurement	Characteristics and application	Advantages	Disadvantages
Traditional approach (financial analysis)	used to identify positive and negative trends in a company	simplicity	keeps to an accounting system that is based on accrual principles
	provides feedback for strategic management purposes	comprehensibility	does not consider any changes in the market value of assets
	the indicators obtained help to assess progress with respect to cash-flow, income, etc.	elimination of subjectivity when selecting indicators	information about causal occurrence of problems is missing
	works mainly with data obtained from financial accounting		
The modern approach (EVA, MVA, CFROI)	the methods are based on value management	simple and comprehensible expression of a company's success	complicated calculation of indicators
	can be also used for certain complex managerial models	can be used to link operative and strategic management	demanding identification of input data
		market-recognized value	results gained through the work of managers not always clearly differentiated from the results caused by other circumstances
Complex managerial models (e.g. BSC, TQM, EFQM, Six Sigma, Benchmarking and other)	an evaluation of a company's overall performance	an evaluation of overall performance	time-consuming to perform
	focused on financial and non-financial indicators	used for strategic management	costly implementation
	not limited just to measuring performance, these can also be used to manage factors that affect performance	identification of causes, relationships and consequences	potential occurrence of problems with formulating a strategy and transferring it into operative management

Source: own based on [11], [13], [17], [20], [22]

The methods used for measuring a company's performance can be divided into three, which are briefly characterised in Table 1.

- a) Traditional criteria for measuring a company's performance,
- b) Modern criteria for measuring a company's performance,
- c) Complex managerial models.

The information that is given in Table 1 is obtained from the study of literature and the experience of the authors of this paper. Individual characteristics, advantages and disadvantages of the methods and models used for performance measurement are based on the acquired knowledge.

Further attention will be paid to the traditional approach of evaluating a company's

performance in this paper. The traditional criteria used for measuring a company's performance are mainly based on a financial analysis of the company concerned, as this is a vital analytical tool. The principle of financial analysis is based on a mutual comparison of the data obtained. The information obtained serve not only for evaluating the overall situation of the particular company, it also helps to identify the company's strengths and weaknesses. There are various methods and approaches to financial analysis described in technical literature and employed in practice. The disadvantage is that neither the approaches nor the terminologies are amended in legal terms. That is why comparing companies can be very difficult, as is assessing a specific company's progress over time. The input data for most indicators used in financial analysis come from accounting records, which is also a cause for criticism in this respect. These data are not corrected in terms of risk factor or inflation; they do not consider any impacts of time on the value of money or opportunity costs. Other disadvantages can be seen in the fact that information obtained in such a way only reflects the company's economic situation; the evaluation does not include the company's market position, there is no reflection on the effect brought on by competitors or on the image of its products and innovations, no attention paid to the quality of employees or the employees achieving their objectives. The main problem with the traditional indicators for measuring a company's performance is that these cannot function without additional information. The information refers to the progress of the company's liquidity, solvency, indebtedness, property and financial structure. This additional information is also obtained from a financial analysis of the company.

Financial analysis indicators cannot be expected to reveal all financial problems. The advantages of financial analysis include its comprehensibility and availability of data from the company's accounting records.

The traditional indicators of a company's financial performance include indicators showing the company's absolute profit value, which can be expressed in various forms. Other traditional indicators are indicators of return that express the efficiency of invested resources and cash-flow indicators.

Despite there being several critical comments against financial analysis, it still

remains a very important tool in financial management. Financial analysis provides an evaluation of the past and existing progress of operations from various points of view and provides input needed for future decision-making [2], [8], [16], [17], [22].

1. The Importance of Evaluation in Accounting in Accordance with the Czech Legislation

The principle of evaluation in accounting deals with assigning values to individual assets or liabilities. Expressing assets and liabilities in terms of value has a significant impact on the information about a company's financial situation. That is why the method of evaluation has extensive influence not only on accounting records and on the evaluation of the company's financial situation, but also on the determination of the company's value [1]. Fireš states the following: *"This is a substantial issue addressed in every financial accounting system, especially because the method of evaluation applied defines the content and informative utility of basically every basic financial value identified through accounting records."* [6] The impact considered therefore concerns total assets and liabilities, as well as the amount of equity capital and profit or loss. The main issue is in selecting the correct evaluation basis to proceed upon when evaluating the assets and liabilities in a company's accounting records in order to clearly show a particular accounting unit's economic status. Most of the new approaches strive towards implementing paradigms aimed at changing from historical costs to values for a better description of the economic avail of items subject to evaluation. [4], [12]

The issue of valuation of inventories is regulated by the Act on Accounting and Czech accounting standards that determine the value of specific assets and debts. It is important to distinguish to what time is the value determined. Following text is based on the various provisions of law mentioned above. Valuation of inventories takes place in two time levels:

- the moment of execution of the accounting transaction,
- evaluation to the end of balance sheet date.

For inventory valuation is used in both cases following price bases:

- purchase cost,
- replacement purchase cost,
- cost price.

In the event that the market value of inventories is lower than their initial price, it is necessary to make adjustment for these inventories.

Provisions of the said law continue the preceding stipulations and define the steps to be taken in case it is determined that the actual price differs from the accounting value. If the sales price of inventory after deducting the costs associated with the sale is less than the book value, the evaluation will be carried out using only the lower value. The same situation occurs when the value of liabilities obtained is greater than or lower than the book value - the evaluation will then be carried out using only the newly-established value [24].

The provisions also contain an enumerative description of the method for evaluating selected items using the real value:

- securities – except for securities held-to-maturity,
- derivatives,
- assets and liabilities in cases to be evaluated using the real value pursuant to special regulations,
- part of assets and liabilities secured by derivatives,
- receivables acquired by the accounting unit to be traded.

The real value applied can be the market value, an appraisal pursuant to a professional estimate or even by expertise. If the of market value professional estimate options cannot be applied, the evaluation process shall run in accordance with special legal regulations.

Kovanicová responds to conditions implied by legislation as follows: *“In compliance with international norms, Czech accounting standards also evaluate certain assets and liabilities using the real value applied at the end of balance sheet date. However, revaluating long-term assets to the real value is not acceptable. The nature of certain assets and liabilities implies the use of specific techniques for evaluating as of the balance sheet date.”* [12]

Another document that refers to the Accounting Act and the relevant regulations is the Czech Accounting Standards, which are issued by the Ministry of Finance in order to achieve compliance with the application of accounting methods in individual companies and to ensure better comparability of final accounts. Their main task is to approximate and harmonize accounting methods and procedures.

The contents of individual standards focus on the following: accounts and principles of bookkeeping on accounts, opening and closing of accounting books, capital accounts and long-term liabilities and costs and revenues. The evaluation agenda is not listed separately, rather it is included within specific standards relating to assets and liabilities. Examples include long-term tangible and intangible assets, long-term funds, derivatives and inventory with an exact determination of particular items and their entry with reference to the Accounting Act and the relevant regulations.

Special attention needs to be paid to the evaluation of inventory-produced internally, as these items have a significant effect on profits and losses. The mentioned legislation mainly differentiates the levels of cost price that is comprised of either the actual cost amounts or the costs defined by operative (planned) calculations, if identified under conditions for the technical preparation of production. Internally-produced inventory can be also evaluated differently depending on the duration of production cycle as follows:

- a) **In production with a short-term uninterrupted cycle** with wages charged against products or semi-products, only for direct material cost items (direct materials, semi-products),
- b) **In mass or large-scale production**, using direct costs only (direct materials, semi-products, direct wages and other direct costs),
- c) **In small-scale and unit (custom) production with a long-term cycle**, using items evaluated by two methods: direct costs or direct costs increased by production or administrative overheads (this item is absolutely evaluated only in exceptional cases where the production cycle duration exceeds one year). [7]

2. The Impacts of Evaluation on a Company's Performance Assessment

Impacts of valuation of assets are reflected in the company's performance, which is demonstrated on the example of the business entity operating in the Czech Republic. This entity is governed by the laws and regulations valid in this country. Furthermore, there are characteristics of the impact of valuation on the company from the perspective of Czech scientists.

The method of evaluation will be projected into the amount of assets and liabilities, which subsequently affects the amount of profit or loss, the values listed in accounting records and the indicators calculated in the financial analysis. Mařík states: *“As these values represent the starting point for various calculations and indicators that characterise the financial status of a company and its ability to generate income, including the rate of return on investment, the financial analysis of a company and conclusions derived from such analysis depend on the method of evaluation selected”* [13].

Financial analysis is one of the basic instruments used to assess a company's financial condition and performance. Most companies still use these indicators for making decisions and directing the focus of their future operations and activities. Results obtained from these indicators serve as background for making decisions about which measures to implement in order to achieve medium- and long-term objectives.

Professionals concerned with financial analysis and the relevant informative utility of accounting records on a long-term basis have agreed that books using historical costs represent a serious problem. Knápková, Pavelková, and Šteker commented that, *“An evaluation of assets using historical costs does not consider changes to the market prices of assets, ignores the changes of purchasing power of particular monetary units and therefore distorts the figures referring to profit and loss over a regular year”* [11]. This statement can be deemed true with regard to inflation, which is not reflected in the traditional concept of accounting. However, as far as selected assets and liabilities are concerned, one needs to respect the legislative measures that define the duty to write long-term assets off and to re-price other items in the records as of the balance sheet date in order to establish their real value. These steps help a company maintain the principle of safety and approximate the value of assets and liabilities to real values, because the process is still based on prices that can be documented, retrieved on objective basis and related to a specific item.

Referring back to the issue of accounting data from the financial analysis point of view, one may state that the informative utility of accounting records is actually a bottleneck of financial analysis.

This problem is further discussed by Kislingerová, who states, *“...the source for assessing a company's performance and other relevant analyses is represented by accounting records that need to be reflected”* [10]. The accounting standards, legislative amendments and measures are meant to ensure a precise and truthful presentation of accounting data. If this fact were not reflected in the accounting system, the system for arranging financial statements would most likely change. The main drawback of all the mandatory procedures lies in their failure to reflect inflation, especially with regard to long-term assets.

There are very frequent expressions of criticism aimed at the indicators of a company's performance, because these do not take various factors into account, i.e. the risk, the impact of inflation, the value of money over time and opportunity costs. That leads to critical comments addressing the level of profit and loss declared in books and their transformation into final income. It has to be emphasized here again that this issue not primarily due to indicators, but rather the input data being the actual accounting information.

3. The Fundamentals of Financial Analysis

Financial analysis is one of the instruments used by corporate management. It deals with assessing the financial and economic situation using specific procedures and methods. *“Financial analysis serves for making a complex assessment of the financial situation in the particular company.”* [11]

Outputs generated by financial analysis are utilised not only by managers in the relevant company, but also by future investors, business partners, financial institutions, government institutions, employees, auditors, competitors, professionals, etc. *“The actual target client group for financial analysis needs to be considered carefully, as each interest group prefers different information”* [10]. The processing of specific indicators is based on in-house records that can help outline future progress trends. *“An essential source of data is a company's financial statements - the balance sheet, the profit and loss report, cash-flow, the review on changes of equity and the appendix to final accounts”* [11].

Financial analyses have to be processed with respect to certain principles in order to

ensure the correct informative utility of specific results. The data identified and used for comparison over time must be obtained using the same methodology. Identifying the progress trend followed by a particular company requires processing financial analyses over time with a simultaneous comparison of entire accounting periods.

3.1 Specific Methods and Calculations of Financial Analysis Indicators

The processing of financial analysis can be based on elementary and advanced methods. Elementary methods of financial analysis include the analysis of absolute, differential and ratio indicators, together with the Du Pont analysis. Other indicators include the credit and bankruptcy models. [5]

The primary materials used to process financial analysis are financial statements. *“The balance sheet contains data referring to a company’s status as of a certain date (status indicators); the profit and loss report shows the revenues and costs over a specific time period (flow indicators). The difference between status indicators can be used to obtain the differential indicators. When setting up a ratio using the data processed, these values are called ratio indicators”* [11].

The main category of indicators for financial analysis is comprised of ratio indicators, most often used for comparing progress, comparisons

against competitors and a pre-defined plan. The basic and most important indicators in this category include profitability, activity, liquidity, indebtedness and capital market indicators, and last but not least, instruments represented by indicators based on net working capital and operating cash-flow. [7], [23]

Table 2 presents the main significance of the selected indicators of the financial analysis.

The return on equity should correspond at least to the return on risk-free assets. *“Measuring the return on equity helps to express the return on capital invested by the company’s owners. The positive difference between interest on savings and return is defined as the risk premium. This is the reward to owners, who bear the risk”* [11].

However, there is a certain level of indebtedness that is useful for the company, because loan capital is cheaper than equity capital. That is due to the fact that interest costs incurred by loan capital reduce the company’s tax burden, because cost interest is a cost category and reduces taxable profits (i.e. the tax effect or tax shield)” [11].

4. Survey Results

This chapter deals with the analysis and presentation of the results of the survey, which was carried out among selected business entities operating in the Czech Republic in February and March 2014. The aim of the

Tab. 2: The essence of selected indicators of financial analysis

Type of indicators	Significance
Return	evaluates the efficiency of the company
	ability to generate profit
	ability to increase the value of invested capital
	represents an important indicator for shareholders
Activity	express the period of capital fixed to selected assets or liabilities
	measure the company’s efficiency when handling its assets and liabilities
Liquidity	define a company’s solvency
	express ability to transform different assets into money
Indebtedness	presents the scope of risk borne by the company
	present the relationship between equity and debts
	the increase of indebtedness can lead to the growth of profitability (ie. leverage), but also increases the risk of financial stability

Source: own based on [9], [11]

survey was to find out what methods are used for measurement of the financial performance of the company in the case of companies that operate in the Czech Republic. Selected findings are presented in the following text.

4.1 Research Methodology

The methodology of the research is based on the survey. For the purpose of this article an electronic survey was implemented back in February and March 2014 in companies situated in the Czech Republic. The vast majority of analysed companies were located in the Central and North-East part of Bohemia. The research team received one hundred of completed questionnaires. The survey consisted of 3 main parts: first part contained basic information about a business entity, second part was focused on evidence of environmental costs in these companies and the last part analysed financial management. The main goal of the survey was to monitor present situation in practical use of performance measurement systems, mainly with focus on innovated approaches of strategic management. The survey was prepared in the electronic form and it contained 38 questions. To obtain relevant information about the analysed companies, both closed and open questions were used. The task of the respondents was to answer open questions with no options available. These answers were selected by companies at their sole discretion. Closed questions included some options to be used by respondents. Within the scope of the survey, 137 companies were contacted and

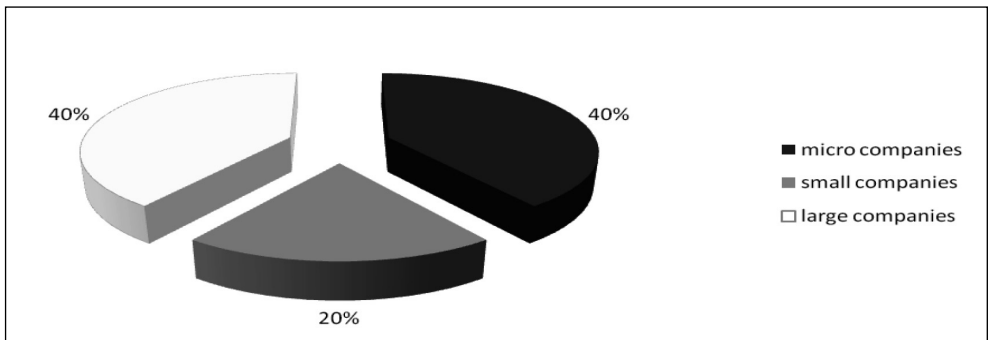
we obtained 117 completed questionnaires back. 110 of them were usable. There was a certain risk that respondents may understand the questions wrongly, which could affect the results of the survey. The data collected by questionnaires were subject to a thorough analysis. These data were processed with the help of an Excel spreadsheet application.

Figure 1 shows the structure of the companies addressed arranged by size in accordance with EU criteria. Micro companies are characterised by assets/property or turnover/income up to EUR 2 million. These limits are raised to EUR 10 million for small companies. Medium companies have assets/property worth up to EUR 43 million and turnover/income up to EUR 50 million. Large companies exceed these limits.

The questionnaire survey revealed the current approach to financial analysis to determine whether it was a common and frequently applied tool for assessing a company's financial status. Out of all the companies addressed, 69% of them used financial analysis in their regular reporting and 31% used this assessment tool on an irregular basis. Furthermore, 73% of the respondents process their financial analysis independently. Figure 2 shows the percentage of companies that evaluate their FA using in-house information systems.

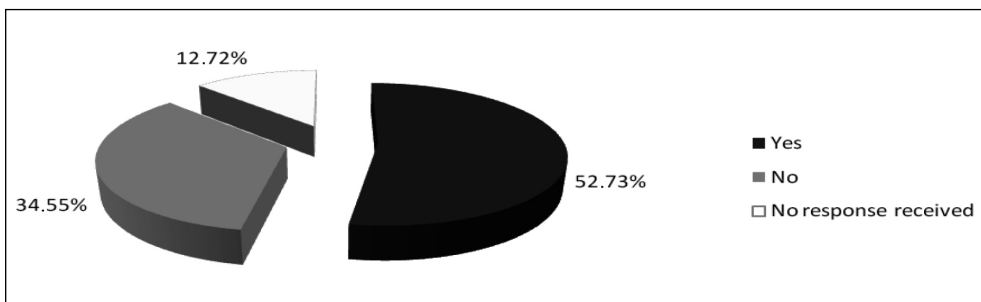
The last, yet still very important piece of information obtained, is that 78% of the companies addressed do not process any bankruptcy or credit models. 13% of the

Fig. 1: The structure of companies, arranged by size



Source: own

Fig. 2: The percentage of companies performing financial analysis using in-house information systems



Source: own

companies assess their overall financial status using the Altman model, 5% of respondents use the IN index and 4% of them use the Quick Test.

Figure 3 presents the utilisation of credit and bankruptcy models when performing a financial analysis.

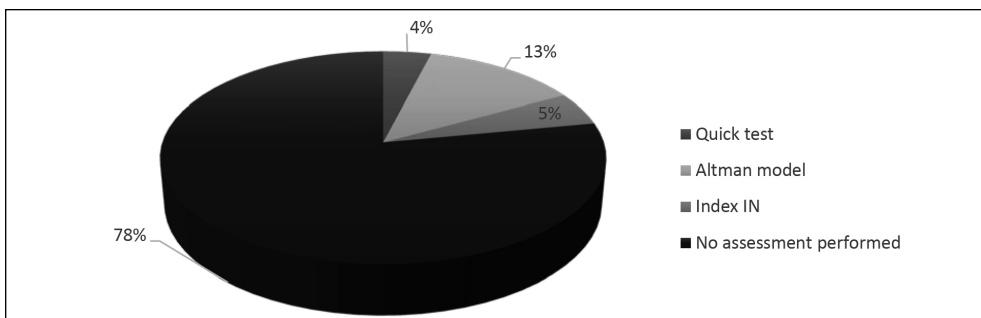
5. The Outputs of Financial Analysis with Different Methods for Evaluating Selected Asset Items

Current legislation allows the employment of different methods for evaluating assets and liabilities in certain cases. If the change of evaluation basis as such is left out of consideration and the evaluation based on purchase cost is considered, there are currently two main areas with potentially serious impact on the amount of profit and loss, the structure of assets and capital, etc. These are the

evaluation of internally-produced inventory using either direct costs or cost prices, including production overheads. The second problematic area deals with the revaluation of derivatives as of the balance sheet date to establish their real value; these are kept by accounting units to accommodate the exchange rate risk. This issue concerns local enterprises who export most of their production abroad who therefore face the deviations of exchange rate as well as the risk involved with the distortion of accounting records and the profit and loss declared regardless of whether transactions associated with the application of derivatives have been completed or not.

Further attention will be paid to the impacts of different evaluations of internally-produced inventory and the revaluation of derivatives to establish their real value up to the amount of

Fig. 3: The utilisation of credit and bankruptcy models when performing a financial analysis



Source: own

Tab. 3: Basic details of quantities, sales, change of inventory and profit/loss

line	Item	Product 1	Product 2	Total
1	Direct costs (CZK)	0.68	50.42	X
2	Production overheads (CZK)	0.97	71.92	X
3	Total costs (CZK)	1.65	122.34	X
4	Sales price (CZK)	1.91	141.62	X
5	Total production quantity (thousands of pcs)	29,466.00	3,118.00	32,584.00
6	Total quantity sold (thousands of pcs)	29,547.00	2,832.00	32,379.00
7	Change in inventory (thousands of pcs), (l. 5 - l. 6)	-81.00	286.00	205.00
An evaluation of inventory using direct costs				
8	Revenues (thousands of CZK), (l. 6 x l. 4)	56,435.00	401,068.00	457,503.00
9	Costs of quantity produced (thousands of CZK), (l. 5 x l. 3)	48,619.00	381,456.00	430,075.00
10	Costs of quantity sold (thousands of CZK), (l. 6 x l. 3)	48,753.00	346,467.00	395,219.00
11	Inventory level change (thousands of CZK), (l. 7 x l. 1)	-55.00	14,420.00	14,365.00
12	Profit or loss (thousands of CZK), (l. 8 - l. 9 + l. 11)	7,761.00	34,032.00	41,793.00
13	Tax rate (%)	19.00	19.00	19.00
14	Tax (thousands of CZK), (l. 12 x l. 13/100)	1,475.00	6,466.00	7,941.00
An evaluation of inventory using cost prices				
15	Revenues (thousands of CZK), (l. 6 x l. 4)	56,435.00	401,068.00	457,503.00
16	Costs of quantity produced (thousands of CZK)	48,619.00	381,456.00	430,075.00
17	Costs of quantity sold (thousands of CZK), (l. 6 x l. 3)	48,753.00	346,467.00	395,219.00
18	Inventory level change (thousands of CZK), (l. 7 x l. 3)	-134.00	34,989.00	34,855.00
19	Profit or loss (thousands of CZK), (l. 15 - l. 16 + l. 18)	7,682.00	54,601.00	62,283.00
20	Tax rate (%)	19.00	19.00	19.00
21	Tax (thousands of CZK), (l. 19 x (l. 20/100))	1,460.00	10,374.00	11,834.00

Source: own

assets, liabilities, income and into calculations to generate financial analysis indicators. All presented information in the following text is based on data of the real Czech company. This international company is focused on the production of glass and glassware and it is one of the major glass producers in the Czech Republic. From the view of the criteria of the European Union, it is a large company. The company was chosen because of its willingness to provide internal information to which it was possible to process the relevant analysis. On the basis of specific data, it is possible to present the impact of inventory valuation not only on the explanatory power of accounting but also financial analysis.

5.1 The Impact on Financial Results

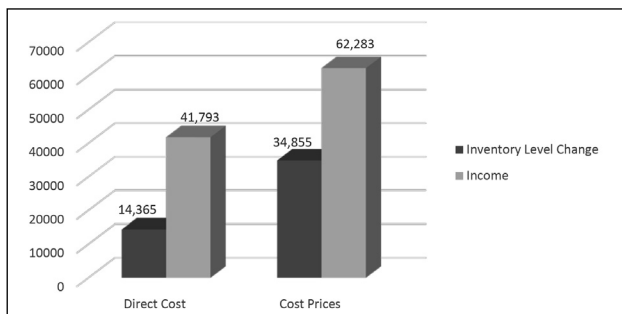
The first step outlines the impact of evaluating internally-produced inventory on the financial

results of a particular company. For details on quantities produced and sold, information on costs and sales price, refer to Table 3. If the company opts to evaluate its internally-produced inventory at the direct cost level, its financial result will reach CZK 41,793,000. However, if the company keeps the current method of evaluation using cost price, see Table 3, the financial result achieved will equal CZK 62,283,000. The impacts of different methods when evaluating internally-produced inventory on the total quantity of inventory and profit/loss are presented in Figure 4.

The selected method for evaluating internally-produced inventory has a substantial effect on profit and loss with consequences affecting the results obtained for return indicators. Impacts on changes to the inventory level will also affect the resultant stock turnover period, stock turnover and regular liquidity.

Fig. 4:

The impacts of different methods when evaluating internally-produced inventory on the total quantity of inventory and profit/loss (thousands of CZK)



Source: own

Evaluations using direct costs then distort the exact figure defining the amount of funds fixed in inventory.

Another important factor affecting the informative utility of financial statements and the profit and loss achieved is the use of derivatives for securing against the exchange rate risk. The issue of derivatives relates to companies exporting most of their production abroad. Similarly to the impact of inventory evaluations, the model example of the impact of derivatives was demonstrated using a joint-stock industrial company from the Czech Republic that exports most of its production to countries in South America and the EU. *“The Czech crown has*

been highly volatile since 1997. Business entities must deal with this volatility accordingly” [18]. The main instruments include derivatives. *“Certain risks can be counter-balanced by trading options, futures and some financial instruments”* [1], [15], [21].

The application of security is also affected by decision-making in compliance with financial policies and other policies [12], [21]. Modigliani and Miller stated, *“...with fixed investment policy and with no contracting costs or taxes, corporate financing policy is irrelevant”* [14].

The current legislation implies that accounting units are obliged to re-price their derivatives to their real value as of the balance

Tab. 4: Revaluing derivatives to the real value as of the balance sheet date (CZK) – Part 1

Line	Liability (derivative)	USD	EUR	Total
1	Derivative amount	2,500,000.00	1,000,000.00	X
2	Derivative price rate agreed upon with the bank	19.000.00	25.000.00	X
3	Initial derivative value (I.1 x I. 2)	47,500,000.00	25,000,000.00	72,500,000.00
4	Price rate as of the balance sheet date	20.072.00	25.735.00	X
5	Real derivative value (I.1 x I. 4)	50,180,000.00	25,735,000.00	75,915,000.00
6	Revaluation difference	2,680,000.00	735,000.00	3,415,000.00
Summary after revaluing internally-produced inventory using direct costs				
7	Total revaluation difference (thousands of CZK)			3,415.00
8	Total revenue gained when using the derivative (thousands of CZK)			471,868.00
9	Total costs incurred when using the derivative (thousands of CZK)			430,075.00
10	Revenues from revaluing securities and derivatives (thousands of CZK)			3,415.00
11	Other receivables (thousands of CZK)			3,415.00
12	Income gained using the derivative (thousands of CZK) (I. 8 – I. 9)			41,793.00
13	Income tax assessed when using the derivative (thousands of CZK) (I. 12 x I. 20/100)			7,941.00
14	Total revenue gained without using the derivative (thousands of CZK)			468,453.00
15	Total costs incurred without using the derivative (thousands of CZK)			430,075.00
16	Revenues from revaluing securities and derivatives (thousands of CZK)			0.00
17	Other receivables (thousands of CZK)			0.00
18	Income without using the derivative (thousands of CZK) (I. 14 – I. 16)			38,378.00
19	Income tax assessed without using the derivative (thousands of CZK) (I. 18 x I. 20/100)			7,292.00
20	Tax rate (%)			19.00
Summary after revaluing internally-produced inventory using cost prices				
21	Total revaluation difference (thousands of CZK)			3,415.00
22	Total revenue gained when using the derivative (thousands of CZK)			492,358.00
23	Total costs incurred when using the derivative (thousands of CZK)			430,075.00
24	Revenues from revaluing securities and derivatives (thousands of CZK)			3,415.00

Tab. 4: Revaluing derivatives to the real value as of the balance sheet date (CZK) – Part 2

Line	Liability (derivative)	USD	EUR	Total
25	Other receivables (thousands of CZK)			3,415.00
26	Income gained using the derivative (thousands of CZK) (I. 22 – I. 23)			62,283.00
27	Income tax assessed when using the derivative (thousands of CZK) (I. 26 x I. 34/100)			11,834.00
28	Total revenue gained without using the derivative (thousands of CZK)			488,943.00
29	Total costs incurred without using the derivative (thousands of CZK)			430,075.00
30	Revenues from revaluing securities and derivatives (thousands of CZK)			0.00
31	Other receivables (thousands of CZK)			0.00
32	Income without using the derivative (thousands of CZK) (I. 28 – I. 29)			58,868.00
33	Income tax assessed without using the derivative (thousands of CZK) (I. 32 x I. 34/100)			11,185.00
34	Tax rate (%)			19.00

Source: own

sheet date. Evaluation differences may be reflected in both balance sheet accounts, as well as revenues and costs, which influences profit and loss. Impacts brought by revaluing derivatives at the selected company are shown in Table 4 and the input data follow the basic values shown in Table 3.

When processing a financial and business plan for fiscal year 2013 with projections into 2014, the company's managers decided to secure their business transactions at USD 2.5 million and EUR 1 million, which had to be re-priced to the real value at the end of the fiscal year 2013 (the accounting period from 2012-04-01 to 2013-03-31). The profit gained through the accounting period was equal to CZK 62,283,000.

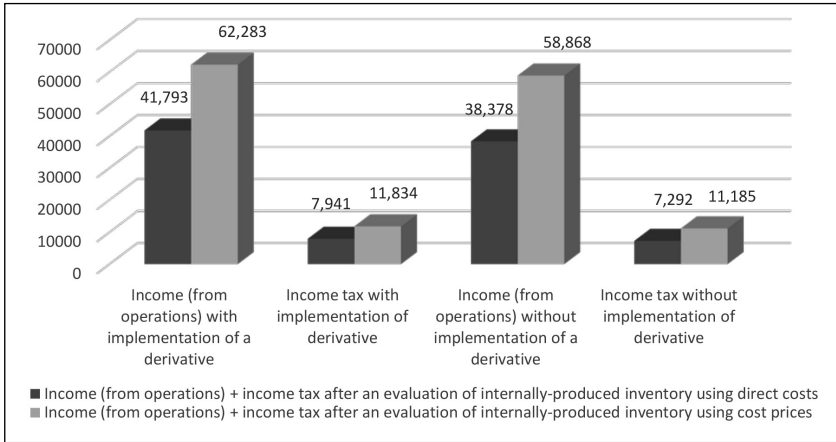
Changes in the exchange rate helped the company gain an additional CZK 3,415,000 of profit by the end of the accounting period, even though the volume of transactions secured by the agreed-upon derivative fell by one half over the same period. A clear illustration of the impact on the company's income and the amount of tax are shown in Figure 5.

If the company were to evaluate its internally-produced inventory using direct costs

without any derivative in place, its profit would be CZK 38,378,000. The difference obtained by using a different method of evaluation is equal to CZK 23,905,000, as shown in Figure 6.

If the company proceeds with evaluating its stock and opts for utilising a derivative for security against exchange rate risk, its income over the particular accounting period will reach of CZK 62,283,000. If the company keeps the derivative and evaluates its inventory using direct costs, its income will drop to CZK 41,793,000. On the contrary, if the company keeps evaluating its inventory using the cost price and avoids using a derivative and its compulsory revaluation, its income will reach CZK 58,868,000. Should the company decide to distort its financial statements by evaluating the inventory using direct costs in order to reduce its tax liability without using any derivatives, its income would reach CZK 38,378,000. As the company may not declare different amounts of income within a single accounting period depending on the bookkeeping methods selected, one needs to have a clear illustration of the impact such steps have on the financial analysis results.

Fig. 5: The impact of derivative revaluation on the income and tax due to the evaluation of internally-produced inventory using direct costs or cost prices (thousands of CZK)



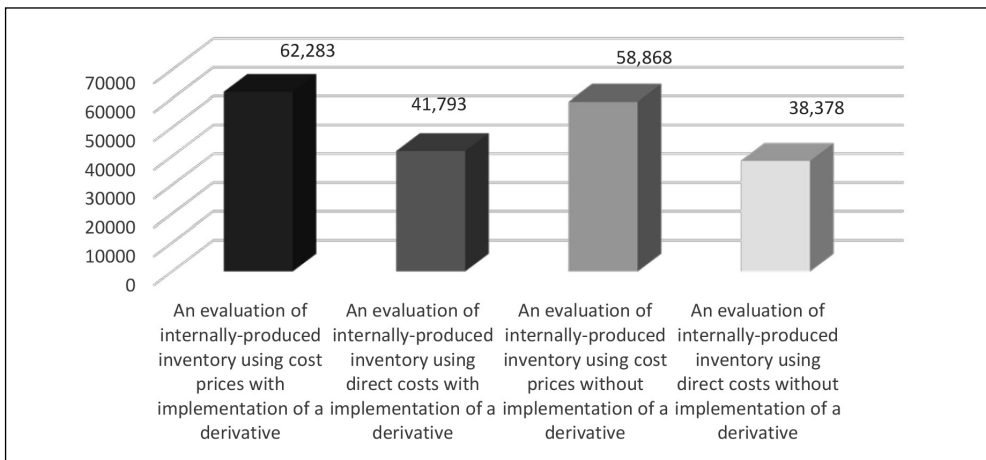
Source: own

5.2 The Impact on Results of Ratio Indicators

Financial analysis should serve not only for assessing the overall financial status of a particular company, but also help to focus on its future development. It is also an instrument used for making mutual comparisons of multiple companies. To ensure that the informative

utility of these data is as accurate as possible and provides correct information for making decisions regarding future steps and the company's focus, it is important to keep the accounting methods unified, both within and outside of the company. A basic prerequisite for comparing a company with other competitors in the area requires all the companies subject to

Fig. 6: A comparison of impacts generated by evaluating internally-produced inventory with/without any derivatives on the company's income (thousands of CZK)



Source: own

Tab. 5: Input data for financial analysis (CZK)

Item	Results of FA after evaluating internally-produced inventory using cost prices using a derivative	Results of FA after evaluating internally-produced inventory using direct costs with a derivative	Results of FA after evaluating internally-produced inventory using cost prices without a derivative	Results of FA after evaluating internally-produced inventory using direct costs without a derivative
Total assets	470,653,007.00	450,163,007.00	467,238,007.00	446,748,007.00
Long-term assets	192,921,330.00	192,921,330.00	192,921,330.00	192,921,330.00
Current assets	277,186,709.00	256,696,709.00	273,771,709.00	253,281,709.00
Inventory	34,855,000.00	14,365,000.00	34,855,000.00	14,365,000.00
Short-term receivables	80,891,144.00	80,891,144.00	77,476,144.00	77,476,144.00
Long-term receivables	0.00	0.00	0.00	0.00
Disposable funds	242,034,664.00	242,034,664.00	238,619,664.00	238,619,664.00
Cash	161,143,519.00	161,143,519.00	161,143,519.00	161,143,519.00
Equity	507,558,745.00	487,068,745.00	504,143,745.00	483,653,745.00
Short-term liabilities	61,706,753.00	61,706,753.00	61,706,753.00	61,706,753.00
Total loan capital	66,166,870.00	66,166,870.00	66,166,870.00	66,166,870.00
Interest expenses	2,034,562.00	2,034,562.00	2,034,562.00	2,034,562.00
Revenues	457,503,000.00	457,503,000.00	457,503,000.00	457,503,000.00
Revenues/365	1,253,433.00	1,253,433.00	1,253,433.00	1,253,433.00
Profit or loss / Income	62,283,000.00	41,793,000.00	58,868,000.00	38,378,000.00

Source: own

comparison to use identical procedures so that all the effects described above are eliminated. The impacts of different evaluations up to the income amount have been outlined; their projection into individual ratio indicators is shown in Table 6, whose input data was obtained from the financial statements contained in Table 5.

The results of ratio indicators are obtained when the company evaluates its inventory using cost prices or direct costs with or without simultaneously using a derivative. If the inventory were evaluated using direct costs without a derivative, the return on equity and total capital would be reduced. This indicator provides "... *an assessment of a company's economic efficiency and its ability to generate profit that expresses the scope of the company's ability to increase the value of invested capital*" [6].

The results of financial analysis imply that the method for evaluating inventory using cost prices or direct costs with or without using a derivative mainly affect the resultant values of return, activity, liquidity and interest earned.

To proceed with inter-company comparisons, the company needs to know more details about its competitors so that the managers can assess the results to get an idea that these results are either good or bad with respect to competitors.

6. Discussion

The results of our survey have confirmed that companies mainly use financial analyses to measure their performance and management efficiency. The output then corresponds to the size and legal form of each company, as most of the companies addressed were joint-stock companies or limited companies. These companies typically use financial analyses as financial management tool. The survey further showed that assessing performance based on financial indicators still prevails and the use of financial analysis in the future is still very likely.

The conflict between a company's need to remain competitive over the long run and having a rigid financial accounting model has opened up some space for implementing some

Tab. 6: Impact of different evaluation of internally produced inventory with/without implementation of derivative on results of financial analysis

Indicator	Results of FA after evaluation of internally produced inventory using cost prices with implementation of derivative	Results of FA after evaluation of internally produced inventory using direct costs with implementation of derivative	Results of FA after evaluation of internally produced inventory using cost prices without implementation of derivative	Results of FA after evaluation of internally produced inventory using direct costs without implementation of derivative
ROA (%)	10.72	7.52	10.21	6.96
ROE (%)	9.94	6.95	9.46	6.43
Stock turnover period (days)	27.81	11.46	27.81	11.46
Stock turnover (times)	13.13	31.85	13.13	31.85
Turnover of receivables (days)	64.54	64.54	61.81	61.81
Turnover of receivables (times)	5.66	5.66	5.91	5.91
Fixed asset turnover (times)	2.37	2.37	2.37	2.37
Immediate liquidity (%)	261.14	261.14	261.14	261.14
Quick liquidity (%)	392.23	392.23	386.70	386.70
Current liquidity (%)	449.20	415.99	443.67	410.46
Total indebtedness (%)	14.06	14.70	14.16	14.81
Debit ratio (%)	13.04	13.58	13.12	13.68
Interest earned (times)	30.61	20.54	28.93	18.86

Source: own

of the new modern methods and models for assessing a company's performance that have developed in recent decades. These models are characterised by a complex company management approach and respect the risk assumed by the company when generating value not only of for its owners, but also for its stakeholders. These reasons necessitate the need for assessing companies, even with respect to non-financial indicators. Using suitable scales to assess performance improves the competitive strength of companies. Improved competitive strength brings benefits not only to the owners, but also to employees, contractors and government authorities. One associated problem lies in the fact that many of these approaches define areas to be handled by managers. However, they do not determine specific indicators to be observed.

Conclusion

The current range of approaches used to assess financial performance in various companies is fairly broad. Methods based on assessing financial data, i.e. a financial analysis, are the oldest and still most-frequently applied. Evaluating a company's performance using financial indicators is the typical practice and it is well-founded beyond any doubt. These approaches are simple and clear; however, they have proven to be insufficient following changes in the business environment, as they often do not provide an explicit analysis of causal relations, nor do they cover any qualitative aspects of features and relationships within the corporate system. However, this does not reduce their significance in any way. Each company needs to be monitored and assessed on systematic basis.

In the case that the company uses for inventory valuation own direct costs or cost prices it will affect the costs, structure of assets and liabilities and, last but not least, also affects the profit including income tax expense. As these above mentioned items enter as a source data for processing financial analysis they also affect different results of the financial analysis. A similar situation affecting their own individual results of the financial analysis occurs even if the company decides to use derivative transactions to ensure stable input inventories. Again in derivative transactions must be taken into account the valuation of inventories, direct costs or cost prices.

If a company is to be compared to its competitors, the average within its industry or even the leader in a particular industrial segment, one needs to realise the lack of detail concerning such companies and the uncertainty surrounding the factors that affect the input values used to calculate financial indicators, as described in this paper. That is why managers need to treat such comparisons with great care.

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AN EVALUATION OF SELECTED ASSETS AND THEIR IMPACT ON THE DECLARATIVE CHARACTERISTIC OF RATIO INDICATORS IN FINANCIAL ANALYSES

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A company's financial performance is essential when investors compare its competitive position to determine how attractive it is. That is why performance needs to be evaluated from both the qualitative and quantitative points of view. The classical financial approach to measuring a company's performance based on past results is no longer sufficient; it needs to be complemented with a non-financial measurement method. This paper focuses on financial analysis, which is one of the tools used for assessing the performance and financial status of companies. The current individual financial analysis indicators must be processed taking into account the influences that potentially affect and distort the results, as well as with their comparability over time and within a single accounting unit or among individual companies. As far as financial analysis is concerned, attention has to be paid to the method used for evaluating assets and liabilities, as this issue greatly affects the informative utility of financial statements and the final data relevant to income from operations, which are the input data for processing individual financial indicators. After that the paper deals with the research that was focused on companies located in the Czech Republic. The aim of the research was to analyse the methods of measurement of financial performance use the Czech companies. Another important task is to plot the approach used by companies to conduct financial analysis in the Czech Republic. It should illustrate whether companies process such analysis independently and regularly using their in-house information systems and identify the most commonly- assessed indicators. It is important that companies process their financial statements so that they can subsequently be assessed and compared over time while maintaining adherence to the same accounting procedures.

Key Words: *Financial analysis, financial performance of company, inventories, survey, valuation.*

JEL Classification: M41, G32, G17, G12.

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