

# Importance of financial statements

[Finance](#)



It is extremely important that companies to maintain financial statements. These companies can be large, medium or large sized operating in either public or private sector. Once the transactions of a company are identified and recorded, the following four financial statements are prepared:

#### Income statement

This is also known as profit and loss statement or earnings statement. It presents the revenues and expenses and shows the resulting profit or loss of the company. Revenue may be form the selling of a product or service and expenses may include advertising, utilities, interest, salaries etc. Tax and interest are also deducted to obtain the profit/loss.

#### Balance sheet

This shows the assets, liabilities and owner's equity at a particular point I time. It gives the stakeholders a picture of the company's investments, splits assets into fixed and current assets and shows the borrowing and lending.

#### Owner's equity statement

This reflects the changes in the owner's equity. It increases with additional investments and revenue and decreases with loss and drawings.

#### Cash flow statement

This summarizes details on where the cash has from, where it is being spent and the ending cash balance. It states the effect of operation on cash, the net increase/decrease and the financing and investing transactions.

#### Purpose

Each financial statement plays an extremely important role as it gives the stakeholders of the company including customers, suppliers, creditors, banks, government authorities, shareholders and employees a true of where the company stands. These financial statements are also used to determine the various accounting ratios required to analyze the company's position from various angles. Shareholders view them for investment purpose and expected dividends on their share, government officials for taxation purpose, banks and creditors for approval of loans, employees and stakeholders for liquidity position. It is therefore strongly advised to maintain these records.

#### References

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Wood's F. (1998) *Business Accounting* . Land & Unwi, Bugbrooke