

HORIZONTAL ANALYSIS OF FUNCTIONAL BALANCE OF FIRMS

Vintilescu Marian

ec. eng. drd. University „Constantin Brâncuși,, of Tg-Jiu, Romania

marian.vintilescu@gmail.com

Abstract: This paper presents a functional design aspects of the economic agent is an economic entity, which aims at producing goods and services, for which exercise economic functions of consumption, distribution, investment and divestiture and financing. Main indicators of functional balance are functional working capital or net working capital globally, need working capital for exploration and exploitation and outside the Treasury functional. Also, to achieve financial equilibrium phases are rendered functional.

Cuvinte cheie: company analysis, balance, indicators, structures, treasury, working capital

1. Functional concept of a company

Equilibrium analysis is to reveal functional and structural financial issues and links to management forecast to meet the needs of managers. Functional analysis considers the trader is an entity, whose objective is the production of goods and services to perform the following functions are economic:

- consumption
- the distribution
- investment and disinvestment
- financing

Combinations of these features reflect the specific behavior entity, its description and conclusions on the financial consequences. At the heart of functional analysis, is situated or operating cycle of production to achieve the following stages which are:

- supply - the stage where buy raw materials and materials necessary for carrying out
- production - includes the transformation of stocks into finished products, process trains or cash flows
- marketing - requires the enterprise to provide financing as long as the finished products are in stock and dispose of the necessary financial resources to hire marketing costs until the sale of such finished products
- collection of receivables - customers - the equivalent of debt settlement

Functional analysis involves a new conception of the enterprise and new content for the financial analysis. The objective of functional analysis is the impact of various business operations of the treasury.

2. Functional role of a company's balance sheet

Enable a quantitative balance sheet assets and liabilities of the entity. Financial analysis reaches a higher degree of detail, by way of regrouping of balance sheet components, according to the objectives pursued. Functional balance of drawing with applicable accounting principles, including the principle of double representation = all operations of the entity, the different categories:

- mining operations
- investment
- financing

= appearance of concrete, material, of receipts and payments resulting from these operations (as distribution operations or cash).

The construction of functional balance, job classification of assets and liabilities do not require the temporal criteria (long, medium and short), their grouping is performed after business destination combined capital (resources - passive) and the commitments it (use - in active).

The role of functional balance consists in assessing the financial structure of the enterprise, reflected by the evolution of net cash and in expressing the link between financial structure and nature of its business. *Balance functional needs analysis investigating company and how their funding by making a snapshot of the performance of different cycles* (fig.1).

ACTIVE	PASSIVE
- gross asset	- equity
- working actively operating	- depreciation and provisions
- actively working out the exploitation	- financial liabilities
- active in treasury	- debt service
	- debts out of operation
	- passive cash

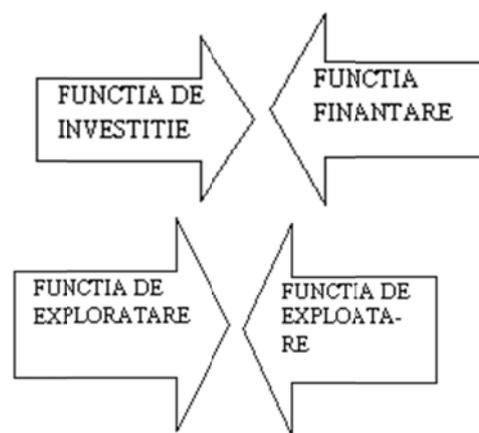


Fig. 1. Functional balance scheme

3. Analysis of functional horizontal balance of a firm

Horizontal analysis aims at year-end financial balance and financial balance between the resources released from this permanent. Horizontal objective analysis is valid functional balance analysis based on general obictivul balance, tracking of general equilibrium, the risk of bankruptcy and financial structure of the economic vulnerability. Functional balance between balance sheet items is highlighted by the four levels of functional balance:

a. Functional working capital or net working capital globally (FRNG)

- achieving financial balance of the company, not just the existence of a positive working capital as a safety margin, but a revolving fund that covers the financing needs of the operating cycle
- **functional working capital or net working capital surplus = global = FRNG** sustainable and stable resources (own or foreign) to the needs stable (fixed values)

$$\text{FRNG} = \text{sustainable resources} - \text{needs stable} = \text{permanent capital} - \text{net asset}$$

- FRNG value is given by the size and cyclical cash needs:

$$\text{FRNG} = (\text{needs to meet cash cycle}) - (\text{resources} + \text{resources cash cycle})$$

$$\text{FRNF} = (\text{ACE} + \text{ACAE} + \text{D}) - (\text{DE} + \text{DAE} + \text{CT})$$

where: ACE = operating assets

ACAE = assets outside exploitation

D = availability

DE = debt service

APR = debt outside exploitation

CT = cash loans

- functional working capital partly reflects the entity's financial balance, that balance of stable funding investment function or use of short-term loans; If available working capital will be higher or lower operating needs of employees (FRNG useful), the company will have cash or the contrary will be forced to hire new short-term loans to finance operating needs
- positive working capital allows assets to cover their own sources and allows acoperieii a part of the operating cycle, negative working capital is an indication of the risk of insolvency of the entity, because it is dependent on banks that may or may not i renew short-term loans that must seek to fully fund their uses - stable.

b. Need working capital for mining (NFRE) and outside exploitation (NFRAE)

- is the most relevant indicator of financial balance work because those needs highlight the covered cycle time and financial resources in the same permanent renewal operating cycles, the remaining unfunded

should be less than or at least equal to working capital functional so defective operation cycle leads to an imbalance that will affect treasury business functional

- **the need for working capital or total** = **NFRT or NFR** = difference between operating needs and outside exploitation and various operating and debt

$$\text{NRFT} = \text{needs cyclical} - \text{cyclical resources}$$

- renewal of resource use and cyclical nature of NFR provides permanent financing needs, sustainable, even if each of its components appears at first glance that an element of balance in the short term
- total working capital need has two components:

b.1. the need for operating working capital = NFRE (must be linked to the business, the evolution of turnover and economic context in which their company operates); if economic agents of production activity, NFRE is positive, releasing an operational need, the specific activity due to immobilization advertising stocks, a necessary period of time of receipt of the products delivered, and if economic agents trade or service activity, where the duration of storage and loan customers is negligible, NFRE is releasing negative operating source; there are two situation:

- increasing very fast and unruly turnover = experience a rapid growth company needs working capital parallel to the turnover
- increased turnover = failure over several financial years the company has a satisfactory liquidity = now accepting new regulatory conditions to its clients, embodied in its receivables growth = sharp rise in working capital needs, which degrades the situation treasury

$$\begin{aligned} \text{NFRE} &= \text{operating assets} - \text{operating liabilities or} \\ \text{NFRE} &= \text{use operating} - \text{operating resources} \end{aligned}$$

- if assets exceed liabilities by mining exploitation, highlights NFRE capital invested enterprise in liabilities over the level of circulating atrs; need working capital for mining has a progressive character dual including size determined by the volume of activity, turnover turnover and stocks, and variation of credit customers and suppliers; stable structural component determining the need of working capital; the equivalent of an asset, to be funded NFRE sustainable resources, working capital that is functional is equivalent stable funding NFR

b.2. the need for working capital outside exploitation = NFRAE

$$\text{NFRAE} = \text{outside exploitation assets} - \text{liabilities outside exploitation}$$

- the need for working capital out of operation is affected by negotiating credit terms with suppliers of fixed assets, working capital needs outside exploitation and necessary part of working capital for operation, be covered in short-term loans

c. Functional trezoreria

- treasury is „defined in relation to working capital and working capital needs, bringing together everything that does not include the first functional components of the balance; if cycles of investment, financing and exploitation of double representation of abstract reflection of economic operations, Treasury is committed specific aspects of monetary flows of these operations,,
- **TN = the net cash** = assets and liabilities cash difference, that excess cash and current bank loans, which are not automatically renew each production cycle:

$$\text{TN} = \text{need cash} - \text{cash resources}$$

- the treasury liabilities grow, especially the financial situation of the company becomes vulnerable
- functional balance is based on fundamental relationships that determine the Treasury from the assets and liabilities equal the functional:

$$\text{AIAE} + \text{IE} + \text{ACE} + \text{ACAE} + \text{D} = \text{RPR} + \hat{\text{IMPR}} + \text{DE} + \text{DAE} + \text{CT}$$

$$\begin{aligned} (\text{ACE} - \text{DE}) + (\text{ACAE} - \text{DAE}) + (\text{D} - \text{CT}) &= (\text{RPR} + \hat{\text{IMPR}}) - (\text{AIAE} + \text{IE}) \\ (\text{NFRE} + \text{NFRAE}) + \text{TN} &= \text{FRNG} \end{aligned}$$

where: AIAE = current assets outside exploitation
IE = operating assets

ACE = operating assets
 ACAE = Outside exploitation assets
 D = cash availability
 RPR = own resources
 IMPR = medium and long term loans
 DE = debt service
 DAE = debt outside exploitation
 CT = cash loans.

- the basic equation of the treasury is:

$$\text{FRNG} - (\text{NFRE} + \text{NFRAE}) = \text{TN}$$

4. Functional structures of functional balance

- working capital needs are funded entirely from stable resources (FR positive) or partially stable resources and cyclical resources, allows the release of a total value of a positive treasury
- stable and cyclical resources partially finance working capital needs, the difference being covered from treasury loans
- current bank loans, and working capital resources, finance part of fixed assets, working capital needs and availability
- resources exploitation cycle induced by adding excess of permanent resources to fund and release cycle needs a major cash surplus
- working capital resources is partially fixed assets, working capital needs, generating a positive net
- permanent resource asset partially financing, their failure is offset by credits suppliers and advances from customers and current bank loans; the company's external financial dependence is high, funding structure should be revised (fig. 2):

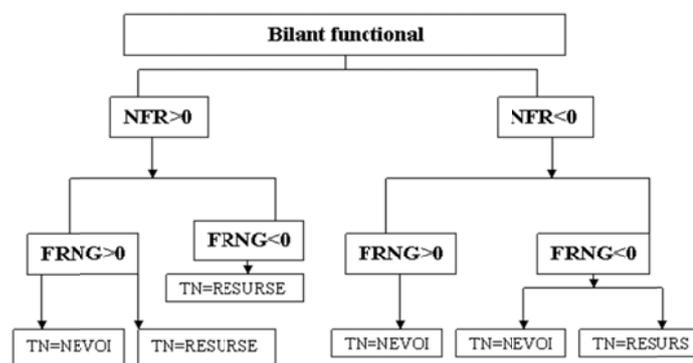


Fig. 2. Functional structures

Conclusions

- Equilibrium analysis is to reveal functional and structural financial issues and links to management forecast to meet the needs of managers.
- At the heart of functional analysis, is situated or operating production cycle, which takes up phases to achieve supply, production, marketing and collection of receivables – customers.
- Functional balance of drawing with applicable accounting principles, including the principle of dual representation, the overall operations of the entity, by category of service operations, investments and financing
- The role of functional balance consists in assessing the financial structure of the enterprise, reflected by the evolution of net cash and in expressing the link between financial structure and nature of its business.

Bibliography

- Bătrâncea M., Bătrâncea L.M., *Financial analysis of company*, Publisher Rissoprint, Cluj-Napoca, 2005
- Porojan D., Bișa C., *Business Plan - concepts, methods and procedures tehnics*, Publisher Irecson, Bucharest, 2002
- Robu V., Georgescu N., *Economic and financial analysis*, Publisher ASE, Bucharest 2001