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Financial Analysis and Diagnostics of the Company

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Abstract

The financial and economic activities of the company are exposed to adverse external and internal factors. Signs of adverse influences are the: decrease of liquidity, loss of profitability, financial instability, increase of costs, to name a few. This paper demonstrates the financial analysis and diagnosis of the financial condition of the company by applying the improved normative model of diagnostics. Furthermore, the paper analyses each factor that impacts enterprise's activities and derives the possible perspectives of the company under study through econometric models.

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Key words: diagnostics; normative model; sustainability; inversion; matrix model; graph of preferences.

1. Introduction

The recent financial crisis proved that business entities of all types should monitor their financial and economic activities to avoid the distress. Evaluating the business and forecasting the bankruptcy applying the financial ratios is one of the most commonly used multivariate discriminant analysis approach. Due to the data availability and improvement of econometrical techniques the number of research devoted to the bankruptcy prediction models has grown enormously.

Beaver, 1966 established a uni-variable analysis, Altman, 1968 is the author of multi-discriminant analysis (MDA), Myer and Pifer, 1970 used linear probability model, Ohlson, 1980, Martin, 1977 applied logit model, and Zmijewski, 1984 probit model. Their research works were continued with introduction of artificial intelligence methods, which comprise of decision tree, case-based reasoning, genetic algorithms, neural networks, and fuzzy models. Consequently, bankruptcy prediction models have been extensively studied, and

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their accuracy and applicability have been questioned and argued as well. Nwogugu, 2007 evaluates and criticizes bankruptcy/recovery prediction models, exploring weaknesses of the listed above models.

The purpose of our work is to analyze financial-economic condition of Bayan Sulu Joint-Stock Company (further ‘the Company’) listed on the Kazakhstani Stock Exchange, and to introduce the methods of diagnosing sustainability of the enterprise.

2. Essence of economic diagnostics

The term of diagnostics was borrowed from the medical science. Diagnostics is the process of studying human’s oscillation from standard and diagnosing a problem. At the beginning of the twentieth century, the term “technical diagnostics” appeared, which was related to the study of machine fluctuation and its causes. Only at the beginning of the twenty first century, the term “economic diagnostics” emerged.

In the works of Russian scientists, the term of economic diagnostics is defined as the identification of the economic condition of an enterprise. The economic diagnostics defines and studies the signs of shortcomings in the management of economic activities in order to predict the consequences, both positive and negative, and the development of methods and means of identifying abnormalities and the impact on them. Periodic diagnostics of economic trends provides an opportunity for appropriate planning to mitigate the risks of the forthcoming crisis, and to remain competitive in current economic environment.

Economy, as any phenomenon, has its own rules. If these rules are followed, economy remains sustainable and competitive. However, miscellaneous events can bring adverse effects which could result in economic downturn. Upon determination of theoretical background and normative model of economic processes, deviation from that model can be easily identified and appropriate actions to be taken. Therefore, for diagnosing economic normative model must be developed, which will provide enterprise’s sustainable development.

Normative model of diagnostics is the model of effective work of an enterprise or its department. Comparative analysis of the enterprise’s actual condition with the normative model gives the opportunity to identify the reserves and deviation. The normative model, including economic factors, is scientific reflection of operational interrelations within the system of an enterprise.

A number of Russian authors do not consider “analysis” and “diagnostics” separately, since their subject and goals are similar. The others claim that analysis goes first, followed by diagnostics. Sheremet, 2008 asserts that the analysis is the research process, while diagnostics is its conclusion. “Analysis and diagnostics are tightly related to each other: without analysis diagnostics does not exist, and the main goal of diagnostics is making a final decision. Analysis and diagnostics are bases for decision making. In medicine the following chain has been established: analysis – diagnoses – treatment; while in economics it is: analysis – diagnostics – decision making”.

Economic processes are continuously dynamical. Factors of the economic process either increase or decrease during the time series. Match of the increase and decrease processes with the standards of economic theory guarantees economic success. Therefore, diagnostics of trends in dynamics of economic processes is of crucial importance. During the shift from one period to the other economic indicators might change positively or negatively in comparison with the standards. In practice, the tendency is not always positive, it goes up and down from time to time.

Unfortunately, methods of diagnosing economic processes have not been established yet. As mentioned earlier, analysis and diagnostics have been considered jointly, instead of being separated. Consequently, the methods have not been classified.

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