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Procedia Economics and Finance 16 (2014) 258 – 269

Procedia Economics and Finance

www.elsevier.com/locate/procedia

21st International Economic Conference 2014, IECS 2014, 16-17 May 2014, Sibiu, Romania

Case Study Regarding Solvency Analysis, during 2006-2012, of the Companies having the Business Line in Industry and Construction, Listed and Traded on the Bucharest Stock Exchange

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Abstract

Beyond the financial performance assessed on the basis of profit and loss account, evaluating a company is made from the perspective of its ability to cope with due debts. A situation that was often encountered by companies listed on the BSE was insolvency, currently affecting six companies, while other have emerged from this process, being traded since November 2013.Considering the companies listed on BSE among the best performing, in this paper, which is part of a larger study, has been analyzed the ability of companies to meet medium and long term maturities, particularly from their own resources, and the way the financial crisis affected it.

Selection and/or peer-review under responsibility of Scientific Committe of IECS 2014

Keywords: Patrimonial solvency ratio (Psr), Global solvency ratio (Gsr), Financial autonomy

1. Introduction

Although the elements of liquidity and solvency are included in most of the specialty literature in the category of indicators of financial position, they are taken into account in most analyzes based on score functions for predicting the risk of bankruptcy (namely total lack of performance), which represents a mitigating factor in calculating various classical performance ratios and are analyzed in a privileged manner when performance is appreciated by creditors.

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Selection and/or peer-review under responsibility of Scientific Committe of IECS 2014
doi:10.1016/S2212-5671(14)00799-0

In addition, profitability is to be achieved in the presence of cash flow, coupled with the ability to honour outstanding debts, the proper management of assets and liabilities, all these elements acting holistically and are mutually conditioned in obtaining, maintaining and improving financial performance.

Given the above, along with consecrated performance indicators, liquidity and solvency analysis could provide a model for assessing the performance of an entity, especially in difficult financial times, marked by lack of liquidity and accumulation of accumulation of receivables and payables.

2. Literature review

Solvency reflects the company's capacity to meet medium and long term maturities, particularly from their own resources.

Solvency is the main objective of the entrepreneur who wants to preserve financial autonomy and management flexibility, resulting from the balance between cash receipts and cash payments and from a positive net working capital, which implies a better adjustment between the needs for long term funding in tangible and financial assets and permanent financing resources, namely equity and term indebtedness (Petrescu, 2008).

Solvency assessment is complex and can be approached from several perspectives. National, international and the economic practice uses the following ratios (Ișfănescu, 1999), (Stancu, 2007), (Balteş, 2010), (Bistriceanu, 2001), (Eros-Stark, 2001), (Halpern 1994), (Petcu, 2009), (Petrescu, 2008):

a) Patrimonial solvency ratio (Psr) is calculated as the ratio between equity and permanent equity (equity plus long term debts) or as the ratio between equity and total capitals. Patrimonial solvency is considered good when the result is between 0.3 and 0.5, indicating the share of own resources in total permanent resources of the enterprise. Values above 0.5 reflects normal circumstances (Petrescu, 2008)

$$Psr = \frac{Equity}{Equity+long\ term\ debts} \quad (1)$$

$$Rsp = \frac{Equity}{Total\ capitals} \quad (2)$$

b) Global solvency ratio (Gsr) quantifies the risk of the company's payment inability. The indicator shows the extent to which debts can be covered on account of the company's assets. The indicator must register sizes over-unity.

$$Rsg = \frac{Total\ assets}{Total\ debts} = \frac{Equity+Total\ debts}{Total\ debts} = \frac{1}{Financial\ leverage} + 1 \quad (3)$$

Creditors are interested in a high value as of the overall solvency ratio, the enterprise's assets constituting liability (Petrescu, 2008).

Another method of calculation of solvency is the ratio of equity - long term debts, that is required to be greater than one.

$$Rsg1 = \frac{Equity}{Long\ term\ debts} \quad (4)$$