Accounting and Finance in AS Diena

Introduction

“Accounting is the language of business”…Indeed, like no man without ability to express his thoughts clearly and understandably can achieve very much in life, no firm can succeed without a good accounting system. Accounting is a necessary tool which not only provides information to the owners about how its money is working, and to the state about how big the taxes are to be fetched, but, the most important, enables the company to control, to plan and to trace all the actions, processes and projects. The purpose of this report is to find out how the accounting is done in a successful company, and how the principles and methods used there differ from the traditional accounting theory. In addition, the analysis of the company’s performance will be worked out using the standard ratios.

The decision to choose AS Diena for the report has been based on several criteria: it is one of the 100 largest companies in Latvia, it has a leading position in its branch of industry, and it is a good example of young and fast-developing Latvian business.
Methodology

The analyses and findings presented in the paper are based on the information received from the interview with the chief accountant of AS Diena Inese Janikovska and from the Annual Report 1997 of the company. The Report mirrors the financial data of AS Diena and its subsidiaries: publishing house Diena Bonnier SIA, advertising agency METRO, Bauskas Dzive SIA, agency Agro Apgads SIA, Kursas laiks SIA, Dzirkstele SIA, Zemgales Zinas SIA. The information about subsidiaries is included in Annual Report in limits of financial year starting from the date of acquisition.

Furthermore, the theoretical side was strengthened with the knowledge gained from the lectures by Elvi Sederlin and Gunnar Lindholm, and from the course textbooks “Business Accounting” and “The Profitability, Financing, and the Growth of the Firm”.

To make the key ratio analysis sensible, a similar size enterprise operating in the same branch of industry was chosen for comparison. For this purpose, the figures from the final accounts of AS Preses Nams were taken from the Lursoft database and used in the analysis.
Company background

The Latvian-Swedish joint-stock company AS Diena was founded in 1992. In 1996 it was transformed into stock corporation. In fact, it is a group of companies with parent company and subsidiaries. The share capital of the company consists of 6000 fully paid ordinary shares, moreover, each share has a nominal value of LVL 10 and its owner possesses one voting right. The shares of AS Diena do not participate in stock exchange, and no deals among the shareholders are allowed. The most important shareholder is a Swedish company “Expressen AB”, which owns 2940 shares, i.e., 49% of share capital and votes. In addition, it can be pointed out that the sales turnover at 1997 constituted almost LVL 9.5 mil, and the average number of employees was 847. The officially registered kinds of activities of AS Diena are as follows:

publishing

printing work and related services

reproducing of computerized materials

agents dealing with sales of the wide range of goods

wholesale

The present strategy of the firm is development as a media and media infrastructure company. To conclude, AS Diena now enjoys the benefits of the large market share and solid reputation, and it will undoubtedly try to maintain and to improve the current position.
Accounting system

Accounting system in AS Diena is fully kept on software and all the transactions are done automatically. The main software accounting program used is Mac Hansa. When the record is made, the account is closed automatically, and the balance is sent to the next stage, i.e., Profit of Loss Account, Balance Sheet, Cash Flow Statement etc. Printed information of accounting actions is kept in the company’s archive. As AS Diena is a very large company, the chief accountant could not tell exactly how many transactions were recorded per year, but the approximate number is about 50,000. The most common transactions are those in connection to cash and bank accounts.
Annual reports

The Annual report is prepared according to legislation of Latvia Republic and the laws “About Accounting” and “About Annual Reports of the Company”. The main principles used in accounting are the consistency concept (methods of valuation of assets and calculation of revenues and expenses are kept constant from one year to another) and the prudence concept (e.g., stock is valued taking the lowest from prime cost and market value). Cash flow statement is prepared by using indirect method.

As per legislation of Latvia Republic, all the company’s books are closed at the end of the financial year (in this case at December 31 each year), when the Annual Report has to be made. This report is handed over to auditors and to financial inspection. Usually, the inspected Annual Report is available for users in about three months after the end of the financial year. In addition, a smaller report for internal use of the company is prepared at the end of each month. This report is handed over to the management of the company.

As all the reports are made automatically by means of software accounting program, the problems occur only when transactions are recorded. The main difficulties outlined by the chief accountant of AS Diena were settling accounts with debtors and creditors and recording expenditures and revenues of the company. Difficulties also appear when making records for financial and tax accounting.

As per Balance Sheet at December 31, 1997, the highest value of the company’s assets is taken by debtors which in total amount to 1,780,777, i.e., 35.42 % of the total assets. The biggest amount of debts is observed with regard to bought goods and subscriptions. Each debtor is examined individually by the management of the company, and those admitted as bad are included in provision for bad debts for 100% of the debited amount. Quite impressive are also figures observed as creditors. Short-term creditors amount to 2,619,142 that is 52% of the total passives of the company.

As it was pointed out by the chief accountant of AS Diena, cash is regarded as the most important asset of the company because of its liquidity. If the company runs out of cash, it can easily go bankrupt.

The highest level of revenues is observed from sales of newspapers. The highest expenses are salaries, purchase of paper and depreciation of fixed assets.
Analyses used in Annual Report

The annual report of AS Diena includes analysis of the current situation and changes during the year 1997.

There was LVL 5.27 million of total assets in the balance sheet at the end of 1997; of those fixed assets were 30.1%. Current assets were LVL 3.51 mil; of those debtors comprised of 50.7 %. The most important fact is that trade debtors have increased by 40.5 % in 1997. The reason behind it is the increase in net turnover. Unfortunately, previous trade partners systematically ignore terms of repayment.

27.6 % of all capital plus liabilities was equity. According to Arvils Ašeradens, the equity has grown to LVL 1.4 millions, which is 2.3 times more than year before (Annual Report, 1997, p. 5). This was only due to profit for 1997; share capital and reserves were not altered.

Changes in the profit and loss account were analyzed mostly in the president’s report. The first item mentioned is the increase in net turnover. According to Arvils Ašeradens, the net turnover of the whole concern has increased by 29 per cent reaching LVL 9.5 million, and such a situation is conventional for the company during last years. The main reason for that is staff’s excellent accomplishment of their job (Annual Report, 1997, p. 5).

Consequently, also the profit after taxes has been increased to LVL 813 thousand. It is 16 times more than in 1996 (Annual Report, 1997, p. 5), and there are three crucial factors which determine such a tremendous change. The first factor is the more efficient use of resources in 1997. As mentioned above, net income has increased by 29 per cent, but manufacturing cost of goods sold has increased only by 15% in the same time. These calculations were made based on the Profit or Loss statement. (Annual Report, 1997, p. 7) Next, there was a considerable growth in other operating income. Finally, there was a rapid decrease in effective tax ratio and reduction in interest payable.
Key ratios

Calculating the key ratios, average values were used because profit was made during the year. There is also an assumption that profit is the same each day during the year. All the ratios and necessary data are given in Table 1.

ROA

This ratio does not depend on the capital structure of the firm (The Profitability, Financing, and Growth of the Firm, p. 26). Profit before interest and taxation should be used in order to separate ROA from the company’s financial policy. The ratio is 28.83 per cent (Table 1) which is more than the same ratio for AS Preses Nams, thus telling about better business performance.

The difference from the previous ratio is that ROE shows the return from the owners’ point of view; however, here the minority interest is also regarded as equity. Thus the profit after taxes (with minority interest added back) has to be applied. In AS Diena’s case ROE is 69.83 % (table 1). The reason why there is so large difference comparing to AS Preses Nams (17.91%) is explained under D / E ratio section.

Average cost of debt in 1997 for AS Diena was 2.15 per cent and being 3 times less than

for AS Preses Nams (Table 1) shows how debt structure affects COD. AS Diena has higher proportion of non-interest bearing debt, thus, its COD is lower.

D / E describes the financial policy of firm. It is 2.53 in AS Diena’s case (Table 1) which shows that concern finances its operations two and half times more using debt than its own equity. Here an important notice should be made: LVL 655.7 th (Annual Report, 1997, p. 23) are subscription fees for the next year which calculating D/E and COD are regarded as debt. The fact that for AS Preses Nams D / E = 0.52 explains why there is much sharper difference for ROE than ROA. Equity is less important source of financing for AS Diena, so the difference in ROE occurs.

It should be noted that effective tax rate can deviate from the statutory tax rate during years. (The Profitability, Financing, and Growth of the Firm, p. 60) This difference can be seen in AS Diena’s case. The denominator in the ratio is profit before tax. In 1997 t was 27.47 per cent. (Table 1) However applying the same formula in 1996 this ratio was 60.32 per cent.
Current ratio; Quick ratio

The quick ratio shows the liquidity in very short terms when it is impossible to sell stock. Both ratios for AS Diena are similar and larger than 1 (Table 1). Thus, it should not be very hard for AS Diena to get over short-term problems. Little difference between these ratios indicates the low proportion of stock in current assets. In contrast, current ratio for AS Preses Nams is 2 times more than quick ratio because it has large amount of stock.
Equity ratio

Equity ratio for AS Diena is 33.15 %, and it is 2 times less than for AS Preses Nams. The reason for this difference is of similar nature as for D / E discussed above.
Profit margin; Capital turnover

ROA depends on two factors. The first one is profit margin, and it is 13.15 %. (Table 1) The second factor is capital turnover that can indicate the speed of operations. The decomposition of ROA shows that the difference between AS Diena and AS Preses Nams in ROA is due to faster capital turnover in AS Diena’s case.

ΔE / E0 = ROE0 – Div / E0 + NI / E0

This formula decomposes equity changes. Because there was no new issue of shares in 1997, only profit and dividends affects equity for AS Diena.

ROE = (1 – t)(ROCE + (ROCE – COD) \* D / E)

In this formula only interest-bearing debt should be taken into consideration. Thus COD was 7.99% (Table 1), and it is similar to COD for AS Preses Nams, because there COD does not depend on company’s debt structure.
Conclusion

It is fair enough to say that it takes more than just analysing the Annual Reports to draw serious conclusions about the accounting system and finance in the firm. However, some important findings can be listed to summarise the investigation conducted in the report.

First, there is no doubt that the computerised accounting system is the only one applicable for the company of the similar size because of the immense number of transactions and complicated structure of the business.

Next, the analysis has revealed some features that characterise the publishing and printing business:

operating activities are mainly financed by short-term liabilities, most of them being non interest -bearing

debtors are the main component of the current assets of the company, due to the need in the high level of stock turnover

To conclude, the AS Diena financial indices show an outstanding, if compared to competitors, business performance.