INTRODUCTION

FINANCE

ACCOUNTS

NOTE

AKSHANSH

Introduction to Finance and Accounts Notes, First Edition

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Presented by: Akshansh Chaudhary
Graduate of BITS Pilani, Dubai Campus
Batch of 2011

Course content by: Dr. Aqila Raffiuddin
Then Faculty, BITS Pilani, Dubai Campus

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More content available at: www.Akshansh.weebly.com

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Introduction to Finance & Accounting

- Capital : Source of money which is being taken up.
- Investor : Someone who invests
  - ↳ can be me
  - ↳ can be others who I call to invest.
- Form of Business Organizⁿ
  - ↳ ① Sole Proprietership
    - ↳ Invest on own capital
  - ↳ ② Partnership
    - ↳ Capital comes from 2 or more.

Dept Financing	Equity
Irrespective of whatever I earn in my business, the investor gets a fixed amount / %age of my funds	Investor gets equal partnership in Profit & Loss.

Idea : If I'm sure my organizⁿ will be profitable, I'll prefer Dept Financing.
Reason : Why to share profit with others !

Corporations :
↳ Public limited company.

Finance and Accounts Notes by Akshansh

an obligation which is being created TO PAY BACK !

* LLC : Limited Liability Corpon
  ↳ deals with : Stock Capital
    ↳ Listing company on stock exchange ✓
  - Sole Proprietorship : Its UNLIMITED Liability Corpon (& Partnership)

- Growth Rate : Sole Proprietorship < Partnership < LLC (probable)
  ↳ Reason : more people to invest, more amount of care can be taken

- Registered capital
  ↳ I declare the amount of money that I'll invest in my LLC.
    ↳ ** In LLC, the liability ₹ comes ONLY to my registered capital.
    (in Sole Proprietorship & Partnership, everything is taken away)

Finance and Accounts Notes Akshansh

sth : something

ACCOUNTING

1 → Balance Sheet

2 → Income Statement (or Profit & loss Statement)

3 → Cash Flow Statement.

4 → Retained earning statement. (if prepared by others → owner's equity)

* Why do we need balance sheet?
  - Mainly for investers to tell them our performance so that they invest in us, we earn and grow. (share rate changes accordingly)
  - Gives a snapshot of financial status of company

* Income Statement
  - In short, it tells my company is at Profit or Loss
  - So, like Balance Sheet, shareholders keep a close look over it

* Cash Flow Statement :
  Just to give an account of inflows & outflows of cash.

Activities : ① Financing
② Investing : where we try to acquire assets
③ Operating : comes in Income Statement → where you buy sth & sell it.

Finance and Accounts Notes by Ashish

* Synonymous terms:
ON ACCOUNT ≡ CREDIT

classmate Date 9/9/14 Page

• Dividend:
Amount that is being earned by shareholders. After the end of a financial year, shareholders have to be given returns on their investment. The amount given to them is decided according to company's growth.

* Retained earnings:
Amount of money retained after paying dividends.

Note: Its not necessary to pay dividends after they are declared. If needed, the dividend amount can be invested back into the company, & that much share ~~are~~ will be ~~allocated to the investor~~ loan will be on the company.

☆ DETAILS ON BALANCE SHEET

• Assets = Liabilities + Owner's Equity
(if single proprietorship or partnership)

• Assets = Liabilities + Shareholder's Equity
(if corporation)

~~* ASSETS~~ → you OWN

Liabilities → you OWE

* Note: Generally, credit is given in the company for 90 days.

Finance and Accounts Notes Akshansh

* Cash : Most liquid asset
↳ ⇒ if I need money urgently, I can get anytime

✡ Assets

Tangible
- Current assets
  - (1) Cash
  - (2) Inventory (≡ raw material)
    - → mainly kept in manufacturing & merchandising
    - → should be limited (otherwise, wastage of space)
    - → We get finished good by using it. So, its current asset
  - (3) Supplies
    - eg: Stationery etc
  - (4) Accounts receivable
    - → The amount that we're supposed to take from others
    - → Mainly seen when we buy anything on credit. Then, we are supposed to pay the person.
    - → If I'm not able to pay back the loan, its called Bad dept for bank/organisation.
      - → comes in expense & is removed from assets
      - → comes in Income Statement

Intangible
- Copyrights
- Patents
- Good will
  - ↳ i.e, suppose I have a shop at a posche area, the facilities are nearby etc. So, I have a good will for that kind of company

Finance and Accounts Notes Rishansh

where to Put ☆

If Give anything on credit : Accounts Receivable
If Take anything on credit : Accounts Payable

↳(5) Prepaid expense
eg: we pay complete college fee at once. If we leave college in between, how much money will be returned to us — will be seen in it

- Fixed assets
  { Properties (buildings, land ...)
  { Machinery
  { Gold ...
  ↳ ≡ LONG Term assets

☆ Liabilities

- Accounts Payable
  ↳ when we BORROW from someone (anything), we have an obligation to pay)
  ↳ On asset side, its for ACCOUNTS RECEIVABLE
- Note Payable.
  ↳ comes when we borrow ONLY from the banks.
  ↳ a note is signed
- Interest Payable
  ↳ Interest which we are supposed to pay on the borrowed amount.
- Salaries/wages payable.

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where to Put ☆ If Borrow from Banks : Note Payable
If Borrow from everywhere else : Accounts Payable

Finance and Accounts Notes Akshansh

* Note: EPS is Earning per Share
* Shareholder ⊂ Investor (subset)

✡ Owner's / Shareholder's Equity = Retained Earnings

CAPITAL + REVENUE − EXPENSES

- CAPITAL: amount invested for start of business
  - other forms:
    - Stock capital (when shareholders invest)
- REVENUE: in different forms based on organisⁿ. eg: fee is revenue for college, sales is revenue for merchandising, charge/service is revenue for servicing sector
  - eg: If I have been paid in advance & I provide service later or I serve & I'm paid later → Accounts Receivable
- EXPENSES
  - Bills
  - Salaries
  - Maintenance
  - Supplies
  - Rent
  - Dividend

* Dividend is NOT an Expense.
  It is a reduction in Owner's Equity.

* A/C ≡ Account

Q(A) ① XYZ corpⁿ has incorporated its offᵉ in Jafza for a capital of AED 35,000 on July 1st, 2014.
② An equipment is being purchased worth AED 15,000 (on cash) on July 5th, 2014
③ Purchasing computers of AED 20K by paying 5K cash & remaining as on account (credit)
④ Purchase of inventory for 10K by paying 2K cash & rest credit
⑤ Take bank loan for 50K (assuming no interest charged)

. question continued later

Finance and Accounts Notes Akshansh

✱ Denote : 15000 ≡ 15K

: −15000 ≡ −15K ≡ (15K)

: its a corporation

Assets = Liabilities + Shareholder's Equity

	Cash +	Equipment +	Inventory +	Accounts Payable +	Note Payable +	Capital +	Revenue −	Expense
(1)	+35000			+A/c receivable		+35,000		
(2)	−15000	+15K			+Advt. Payable + Wage Payable			
(3)	(5K)			+20K		+15K		
(4)	−2K			+10K	+ 8K			
(5)	50K					+50K		

↳ reduction in cash by 15000 & addition of equipment (in asset side) by 15000.

(4) ≡ −5000 AED

continued Q(A) ⑥ Payment of 7000 AED to the computer supplies only

(6)	−7K				(7K)			

⑦ Inventory (purchased of 10K) is being sold to customer at 30K. 5K is taken initially & remaining will be taken later

(7)	+5K			+25K → A/c receivable.		+30K		

→ i.e, due

⑧ 750 AED is to be paid to Gulf news for the classified column in this month's newspaper, (i.e, we advertised)

Note : there may not be anything on Asset side

displaying Ad is an expense

(8)					+750			−750

Finance and Accounts Notes ARSharSH

(9) AED 2000 is to be paid to the workers as their wages

	+2000	−2000
Balancing		

61K + 70K +68750 +62250

→ 35K + 30K
− [expense]
= 65K − (750+2000)

Total 131K = 68750 + 62250.

131,000 AED = 131,000 AED

68750
+62250
131000

Balanced

Q. (B) (1) Owners invest $20K of capital in Acme Consulting
(2) Equipment costing $7K is purchased for $5K and account payable of $2K
(3) Supplies inventory costing $1K is bought for cash
(4) Salaries of $4500 are paid in cash
(5) Revenues of $10K are earned of which $5K has been recovered in cash. The remaining $5K is owed to the company by its customers.
(6) Accounts payable of $1.5K are paid in cash.
(7) Customers pay $1000 of the $5K they owe to the company.

Finance and Accounts Notes Akshansh

(8) Rent expense of $750 is paid in cash.
(9) Utilities of $500 are paid in cash.
(10) A $200 travel expense has been incurred but not yet paid.
(11) Supplies inventory costing $200 are consumed.

Solution

	Assets = Liabilities + Owner's Equity		
	Cash + Equipment + Inventory + A/c receivable	A/c payable	Capital + Revenue − Expenses
(1)	$20K		20K
(2)	(5K) +7K	2K	
(3)	(1K) +1K (Inventory)	+	
(4)	(4500)		−4500 (either write all expenses as −ve or write +ve & subtract later)
(5)	+5K (+5K → A/c receivable)		+10K
(6)	−1.5K	−1.5K	
(7)	+1K (−1K → cash paid by customers (out of 5K))		
(8)	(750)		−750
(9)	−500		−500 (utility cost are expenses)
(10)		200	−200
(11)	−200 → supplies inventory consumed		−200

Finance and Accounts Notes by Akshansh

26000
- 1450
24550

25000
- 1150
23850

Assets	=	Liabilities	+	Owner's Equity
Total $24550.		$700		+ $23850.

$\Rightarrow$ $24550 = $24550

Balanced

23850
+ 700
24550

Q.(B) Continued...

Prepared an Income Statement at the end of the month:

Idea: Don't do anything with capital

Calculate Revenue − Expenses.

So, we have:-

Revenue = $10K

Expense = 4500 + 750 + 500 + 200 + 200

So, Revenue − Expense = $3850

↳ Income.

Note: Tax & Declaration of dividend will come in later sections

* Dividend is not an expense. It is a reduction in owner's equity.

Finance and Accounts Notes Akshansh

Q(c) Thornton Computer Timeshare Company entered into the following transactions during May 2012.

(1) Purchased computer terminals for 20K $ from digital equipment on account
(2) Paid $4K cash for May rent on storage space
(3) Received $17K cash from customers for contracts billed in April
(4) Provided computer services to Fisher Construction Company for $3K cash.
(5) Paid Northern States Power Co. $11K cash for energy usage in may → the owner, not the company.
(6) Thornton invested an additional $29K in business.
(7) Paid digital Equipment for the terminals purchased in (1) above.
(8) Incurred advertising expense for May of $1.2K on account → ⇒ used

Q.(D) Ramona castro opened a veterinary business in Nashville, Tennesse on August 1. On August 31, the balance sheet showed cash $9K. A/c receivable $1.7K, Supplies $600. Equipment $6K, A/c payable $3.6K & Owner's Capital $13.7K. During september, following transactions occured:

(1) Paid $2.9K cash on A/c payable.
(2) Collected 1.3K on A/c receivable
(3) Purchased additional office equipment for $2.1K, paying $800 in cash & rest on account
(4) Earned revenue of $7.8K of which $2.5K is received in cash & balance is due in October
(5) Dividends have been declared.
(6) Paid salaries $1.7K, rent for September $900 & advertising expense $450.
(7) Incurred utilities expense for month on a/c $170.
(8) Received $10K from Capital Bank

Finance and Accounts Notes Akshansh

* Only business related transactions are supposed to be recorded.

Ans (c)

	Assets	Liabilities	Owner's Equity
	Cash + Equipment + Inventory + A/c receivables	A/c payable	Capital + Revenue − Expense
(1)	+20K	$20K	
(2)	−4K		−4K
(3)	+17K		+17K
(4)	+3K		+3K
(5)	−11K		−11K
(6)	+29K		+29K
(7)	−20K	−20K	
(8)		+1.2K	−1.2K

* any sales of previous month is put under revenue. Accomodated later on

* providing services is also seen as revenue.

(6) +29K → we are bringing in additional cash from his own

Balancing $34K = $34K

* Income Statement = Revenue − Expenses.
= 20K − (4K + 11K + 1.2K)
= 3.8K

Finance and Accounts Notes Akshansh

Owner/Shareholder Equity = Capital + Retained earnings

Imp

V. Imp → Revenue - Expense - Dividends

* Note: There is no entry for declaration of dividends

Ans (D)

	Assets	Liabilities	Shareholder's equity
	Cash + Equipment + A/c receivable + Supplies	A/c payable	Capital + Revenue - Expense
On Aug 31 (Initial)	$9K + $6K + $1.7K + $600	$3.6K	$13.7K
September			
(1)	-2.9K	-2.9K	
(2)	+1.3K -1.3K		
(3)	-800 + 2.1K	+1.3K	
(4)	+2.5K +5.3K		+$7.8K
(5)	———	— — —	— —
(6)	-1.7K - 900 - 450		-1.7K - 900 - 450
(7)		+$170	-$170
(8)	+$10K	+$10K	
			900 450 170 1520
Balancing	$30.95K	= $30.45K	14.800 -1.520 17.48

Note:

- Depreciation is an expense account.
- Dividends are not expense, but, they reduce owner's equity.

Finance and Accounts Notes Arshansh

* Fixed assets are based on cost value, not market value.

* We follow a STRAIGHT LINE Concept

~~Assets = Liabilities + O/s Equity~~

Debit

* Depreciation = Value of an asset / Useful life of asset (years or months)

↳ like, an equipment.

↳ decrease in the resale value of assets along with time.

eg: I purchased a 2014 model BMW in June at 60K, which has travelled for 2000 kms

→ Note: Resale value is less as the life of asset decreases over the years.

: Depreciation takes place in the used car.

So, for our asset, consider:

Useful life: 3 years & Worth: 60K

Hence, Depreciation = $\frac{60\,000}{3 \times 12}$ = $1667

ACCOUNTING CONCEPTS & CONVENTIONS

① Business Entity Concept

Idea: The business & its owner(s) are two separate existence entity

- Financial statement of a firm contain financial information about only that firm.
- Personal entries are not shown on balance sheet.

eg: If a company gives a car to an employee, then the car is company's asset, not employee's asset.

② Monetary Unit

Only those items which can be measured in terms of money are included in financial statements.

Finance and Accounts Notes

* Dual Aspect Concept & It states that
Assets = Liabilities + O/S equity
→ owner's / shareholder's

(3) Going Concern
i.e., financial statements have to be prepared assuming that business will exist in future (foreseeable future)
→ operational existence
eg: doing prepayments, making depreciation provisions

(4) Historical Cost / Cost Concept
Assets should be shown on balance sheet at the cost of purchase instead of current value

(5) Transparency / Disclosure
No over projection

(6) Conservatism: Revenues & profits are not anticipated. Only realized profits with reasonable certainty are recognised in P&L a/c.

(7) Period of Accounting: Fiscal Year
In India: April to March
In BITS: September to June
* Balance Sheet is made at a pt. in time but other things (Income stmt etc.) are made at ending period

(8) Recognition Principle
→ Revenue is recognized (put in balance sheet, say) when it is earned. Not, when cash is collected.
→ Accruals & Deferrals.
eg: If a company earns $50K worth revenue during July, then we will put the entry of $50K in the income statement for July, even if we get the cash for our revenue (say, sales) in August

(9) Matching Principle
Idea: Expenses are recognized as they are incurred, not when cash is paid
The net income for the period is determined by subtracting expenses incurred from revenues earned.
eg: In BITS, Chem. stream has less students. But, no. of teachers are same as other streams. So, its at loss. So, college will focus more on Chem. to get more students.

Finance and Accounts Notes Harshansh

Q.E) Mediterranean corpn commenced business on Dec 1, 2012. The ending balance as of Dec 31, 2012 are.

Accounts	$
Cash	14 K
Adv. supplies	2.7 K
Prepaid insurance	1.44 K
Prepaid rent	3.5 K
Office equipment	8.4 K
A/c payable	3.1 K
Note payable	4.2 K
Common stock	12 K
Dividends	1.16 K
Fees earned	15 K
Salaries expense	3.1 K

Additional Data:

1. Insurance expired for a month ($60 per month)
2. Supplies shown $500 on hand.
3. Rent for 10 months paid in advance.
4. Office equipment has 10 year useful life
5. 12% interest for note payable.

Prepare adjusted Trial balance, Income Stmt, Balance Sheet for Dec 31, 2012.

Idea: A list of all the accounts are given together. Sort it as per table & baland it (PTO)

Financial Accounts Notes Harshansh

★ Way to denote in tables:

	($\times 10^3$)	('000's)
15000 ≡	15K ≡	15 ≡ 15

Ans (E)

Assets	Liabilities	Shareholder's Equity
Cash + Supplies + Prepaid insurance + Prepaid rent + Office Equipment	A/c payable + Note Payable	Capital − Dividend + Revenue − Expense
14K + 2.7K + 1.44K + 3.5K + 8.4K	3.1K + 4.2K	12K − 1.16K + 15K − 3.1K

→ reduction in owner's equity

Balancing $30.04K = $30.04K

Now, putting statements

(1) (60) → we paid some amount as insurance. So, now, 1 month expired. Hence, reduce $60 from prepaid insurance (asset) & also add an expense of $60. −60

(2) −2200 → Supplies shown are left 500. We had 2700 previously. So, 2200 has been used (2200)

(3) −350 → Given 3500 is prepaid rent. So, for one month, we have 350 as prepaid rent (350)

→ 1 month ∴ we are only taking for Dec 2012.

(4) (−70) −70

8400 for 10 years
⇒ 8400 for 120 months
⇒ $\frac{8400}{120}$ for 1 month
⇒ 70 for 1 month

(5) +42 −42

$\frac{1}{12}\left(\frac{12}{100} \times 4200\right)$ ← paid as interest in one month

Finance and Accounts Notes

* Note: We cannot have Retained Earnings in the first year of operation!

Assets	Liabilities	S.H's E.
Cash + Inventory	A/c payable	Revenue - Expense

(6) 80K inventory has been bought on account

+80K +80K

(7) Inventory worth 60K is sold for 100K on cash

+100K +100K

70) 60K of inventory sold is COST OF GOODS SOLD

cost of goods sold is expense

-60K -60K

(8) A truck was purchased for 30K on account

Note: It is an investment activity of the organiz^{n}.

+30K +30K

Balancing $177.36K = $177.36K

Balanced.

* Purchase of an asset is never a part of expense.

Finance and Accounts Notes Akshansh

✱ AVOID CONFUSION :

Net Income = Revenue − Expense

& Net Income − Dividend = Retained Earnings (RE)

So, Revenue − Expense − Dividend = R.E (new)

So, in table, we write :

Owners / Shareholder's equity =

Capital + Retained Earnings (old) + RE (new)

= Capital + RE (old) + Revenue − Expense − Dividend

→ old ⇒ previous data to be included in RE.

→ new ⇒ in current statement

✱ Format of Retained Earning Statement

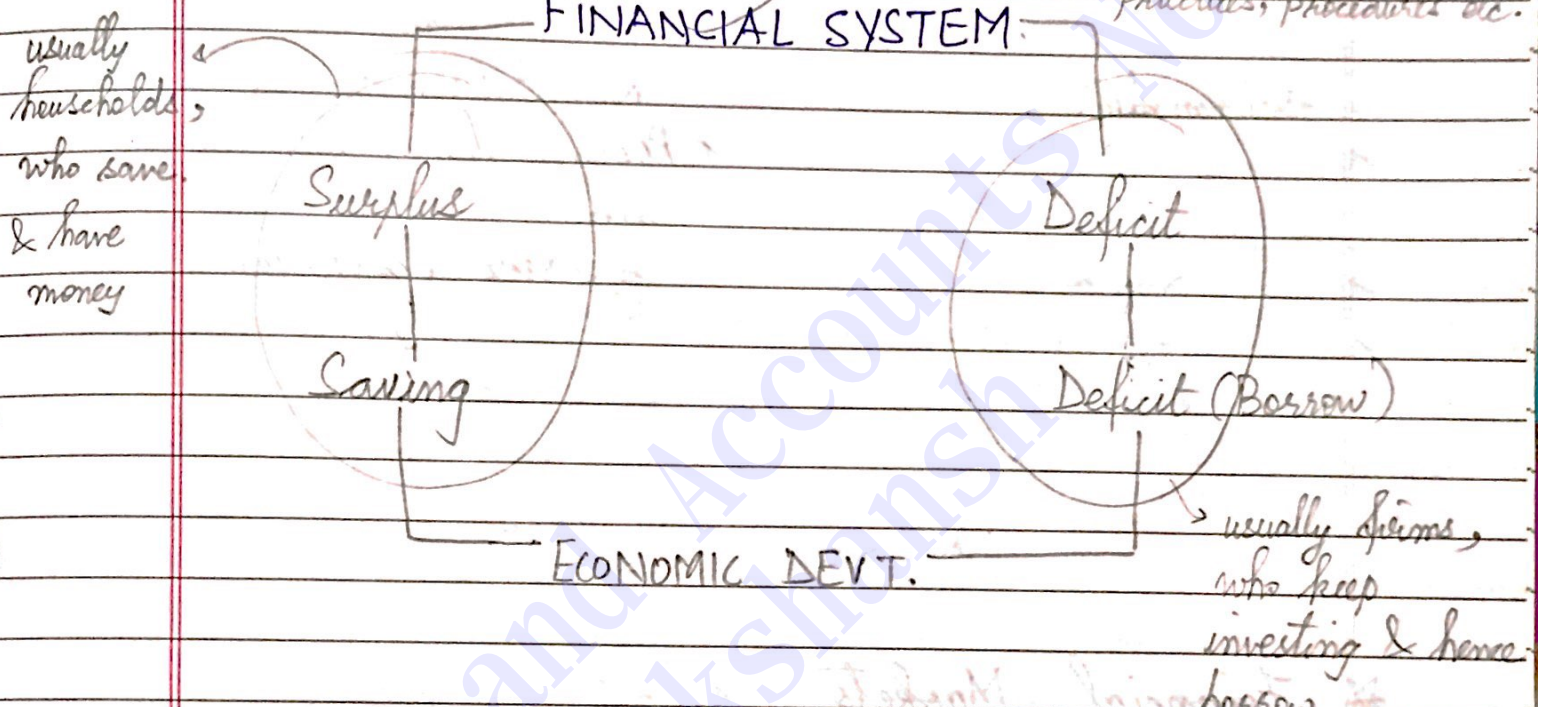
	Beginning RE balance	XXXX
or Net Income ←	+ Revenue	XXXX
	− Expenses	−XXXX
	− Depreciation	−XXXX
	Ending RE balance	XXXX
	Total RE	XXXX

Finance and Accounts Notes Akshansh

• financial institutions: eg – banks

Finance

→ A set of complex & closely intermixed financial institutions, markets, instruments, services, practices, procedures etc.



- Money : a medium of exchange.
- Credit : money which is being borrowed on interest
  ≡ DEBT
- Finance
  → Two forms
  - Debt
  - Equity

eg: If I need money to invest but dont have. So, how to do finance of this?
→ Take Debt
→ Sell a part of your equity.

Finance and Accounts Notes by Akshansh

$\exists$ ≡ There exists

DEBT ≡ Credit

Bond (By Govt.) | Debenture (By Company)

classmate Date Page

✱ Financial Institutions

Type 1

- Banking — eg: RBI, Banks, ...
- Non-Banking — eg: mutual funds

Mobilisers & Deposiers

Type 2

- Intermediaries
  - > When ∃ a bridge b/w me & money
  - > eg: RAK bank
  - > A link b/w savers & investors
- Non-Intermediaries
  - > Provide loan, but not for savers
  - > eg: SME (Govt. funds here)
  - > like for rural areas, agricultural sector etc.
  - > Does NOT have any saving or current account facility
    - ↳ Only gives loans

✱ Financial Markets

Type 1 (Issue)

- Primary — eg: Alibaba.com
- Secondary ≡ stock market

Type 2 (Maturity)

- Money
  - • Components →
  - (1) Treasure bills
  - (2) Commercial paper, STD
  - (3) Call money - bank borrows
  - (4) Certificate of deposits
  - (5) Commercial bill
  - → when we buy anything on credit like, a credit note. → give it to shopkeeper & bank pays for our shopping
- Capital Market
  - ↓
  - Equity, Bond, Preference shares
    - → Its like an equity — (bc) has command on dividends
    - → person investing in Equity, still getting dividends

Finance and Accounts Notes Mrshansh

Imp ★ Issue ≡ FLOATING shares in market

★DFHI : Discount Finance Housing of India

★PJSC : Public Joint Stock companies

→ ∃ risk

→ minimum risk

- **Diff. b/w Capital market & money market**

	Capital market	money market
- Participants	Companies listed on stock exchange	Banking & non banking Institutions
- Investment	very less price eg 20p	some min. amount like 2000 or sth
- Duration	> 1 yr	< 1 yr
- Liquidity	More liquid	Not liquid at all
- Safety	Not safe	safer
- Expected returns	Higher	Very less
Products ⇐ ⇒ Instruments		

- **Diff. b/w Primary & Secondary**

CRITERIA	Primary	Secondary
- Issues / sales	→ For 1st time shares are being sold (→ new)	• Existing ones
- Flow of funds	→ By Public	• Existing shares are sold.
- Buying (type of transaction)	→ Selling	• Buying & Selling
- Prices	→ • Prices are decided by Issuer	• Buyers decide on the basis of : Demand & Supply & Movement of funds
- Geographical location	→ not much significant criteria	

- **Methods of Floatation** → Both Primary & Secondary can make company anywhere

- Offer through (prospectus) → contains business plan of method of floatation
  - ↳ only for Primary Market
  - ↳ detailed plan of growth of organisation
- Offer for sale → Buying in some people, like Brokers & put it on sale
- Rights issue → For someone already having shares
  - ↳ They are allowed to invest
- e- IPO's → Float across internet.
- Private Placement
  - ↳ They are offered, but only to specific people. like, shared among only my family eg: Al-Futtaim in Dubai

★ IPO : Initial Public Offering → owner

Alibaba.com does IPO & ∃ keep all its shares. Now, when market is opened for my shares, I start selling them

- ~~Premium~~ :

Finance and Accounts Notes by Harshansh

eg iPhone 6Plus was launched on 19th September, 2014. The price of the Phone was put as $800, say. Now, some people bought it for $1000 (gray market) while some get it for $750.

So, Par Value / Face value : $800
Premium : $1000
Discount Price : $750.

ACCOUNTING PRACTICE

Q (A) Akshansh's consultancy services, LLC. took its setup on Aug 1, 2014.

(1) $7K is invested in business on Aug 1, 2014

Assets	Liabilities	Shareholder's E
Cash		Capital + Revenue - Expense
+7000		+7000

(2) Paid $900 towards the rent for the current month

-900		-900

Finance and Accounts Notes by Akshansh

Assets		Liabilities	S E
Cash + Supplies + Equip. + A/c receivable		A/c payable	Capital + Revenue - Expenses

(3) Purchased $600 worth of supplies on account

+600 +600

(4) Paid $125 to advertise in Gulf News

-125 -125

(5) Received $4K cash towards the services provided

+4K +4K

(6) Performed $5400 worth of services on account / to customers yet to be received

+5400 +5400

(7) Paid $2500 for employee salaries

-2500 -2500

(8) Paid for supplies purchased on a/c earlier this month

-600 -600

(9) Received cash payment of $4K for services paid on account.

+4000 -4000 → I have received 4000 out of 5400 I had to receive

(10) Borrowed $5000 from Emirates NBD

+5000 +5000

(11) Purchased office equipment worth $4200 on a/c

+4200 +4200

Finance and Accounts Notes Akshansh

classmate
Date
Page

Asset	Liabilities	SE
Cash		Revenue / Expense

(12) Paid $275 towards utilities.

-275 | -275

Balancing $21,800 = $21,800

(13) Estimated useful life of the bought office equipment is 5 years. (purchased of $4200)

here, the value 4200 → 5 years

⇒ 1 month → 4200 = $70
60 → 12 months x5

-70 → Depreciation cost (not to put unless asked) | -70

(14) 6000 is paid as insurance per annum

12 months → 6000

⇒ 1 month → 500

-500 → using 400 out of 600 (cost of goods sold) | -500

Close (15) I have used $400 of my supplies in the month's end | (-400) | (-400)

Balance as on Aug 30. $20,830 = $20830

Balanced

Now, Q: Prepare an income statement for the month of August

Income statement = Revenues − Expenses

= (5400 + 4000) − (900 + 125 + 2500 + 275 + 70 + 500)

Finance and Accounts Notes Akshansh

Note: In the previous questions:

Extra things

- If I have paid 600 worth of supplies (in transaction no. (3)) & I have $200 left with me. So $400 is what I used from supplies. This $400 is treated as an expense, under "cost of goods sold".
  → Transaction (15)

- If the balancing is done on September 15 (i.e., for 15 days only), we will have to modify the EXPENSES (for 15 days only)
  Note: Whatever revenue we generated in Aug will be written in income statement for September also.
  → In income statement, suppose the rent expense is 900 & we are calculating (TILL) Sep 15, (→ from Aug 1 – Sep 15)
  If is (900) + (900/2)
  (900) → for full Aug
  (900/2) → for half September
  So, under expense, for rent expense, it will be 900 + 450

☆ Note: This DEPENDS. i.e, if I've taken a flat for rent & the owner asks for full payment, even if I used till Sep 15, It will be (900+900) So, see what the question asks.

☆ Basically, check the dates carefully & then see the cost

☆ Gross Income: has the amount which is being utilized in the given time frame.

☆ IMPORTANT: Don't pre-assume anything. Do as per what is mentioned in the question.

Finance and Accounts Notes by Ashansh

SPERTEL : Socio Political Economic Regulatory Technological Ecological Legal

classmate Date Page

* TYPES OF ACCOUNTING

ACCRUAL Accounting ≡ Accumulating

CASH BASIS Accounting - mainly in small firms

• SPERTEL factors : vary on the type of business organizations

RISK

Factors having impact on RISK.

- ✓ Bank Interest Rate
- ✓ Currency fluctuation
- ✓ Industry Risk (ups & downs in any industry)
- ✓ SPERTEL factors
- ✓ Culture factors

* RISK

TYPE (1)

Business Risk or Unsystematic Risk or Diversifiable Risk

Factors in my control
- ↳ updation of tech.
- ↳ paying appropriate salaries & bonuses

✓ Factors affecting a very specific group of securities or individual security.

Market Risk or Systematic Risk or Undiversifiable risk

Factors not in my control
- ↳ provision of material, like electricity problem in a region

✓ Factors affecting the entire market

Diversification:

It relates to diversifying my ways of investing. I try to invest in a wide variety of options so that the negative effects of one may counter the positive of the other. So, in the end, I don't face loss even if the market of one type collapses. – I have reduced my risk.

Further diversification benefits can be gained by investing in foreign securities because they tend be less closely correlated with domestic investments. For example, an economic downturn in the U.S. economy may not affect Japan's economy in the same way; therefore, having Japanese investments would allow an investor to have a small cushion of protection against losses due to an American economic downturn.

Finance and Accounts Notes Rishabh

Types of Risk

Default Risk i.e., the risk for the borrower or debtor if the borrowed/lent money will be paid on time or not.

Credit Risk i.e., the risk for the bank, if I take money from the bank, whether I will pay back or not.

Settlement Risk i.e., the risk for both the parties just in case the settlement of trade or anything does not take place as expected.

Financial Risk i.e., the risk that is there for the shareholders as they might lose their money, because the company on debt financing may not be able to repay its debt.

Liquidity Risk i.e., a risk that arises from the difficulty of selling an asset, considering the times when an investment is required to be sold off quickly.

Maturity Risk i.e., the risk in making long term investments considering the market changes and I cannot predict that much.

Market risk (or Systematic Risk, or, Undiversifiable Risk) i.e., the risk that the value of my assets might change based on the factors that affect the entire market. Affects overall market, not a particular stock or industry.

For example, putting some assets in bonds and other assets in stocks can mitigate systematic risk because an interest rate shift that makes bonds less valuable will tend to make stocks more valuable, and vice versa, thus limiting the overall change in the portfolio's value from systematic changes. Interest rate changes, inflation, recessions and wars all represent sources of systematic risk because they affect the entire market. Systematic risk underlies all other investment risks.

Unsystematic risk (or specific risk, or diversifiable risk, or residual risk) i.e., the risk that is specific to a particular type of business, or does not affect everyone.

Examples of unsystematic risk include a new competitor, a regulatory change, a management change and a product recall.

Operational Risk i.e., anything that can be a risk in doing the operations of a company successfully. Also includes legal risk, like failure to comply with laws.

Interest Rate Risk or Funding risk i.e., the risk on change in the value of my asset in case the interest rate change.

Inflation Risk i.e., the possibility that the value of assets or income will decrease as inflation shrinks the purchasing power of a currency.

Exchange rate of currency risk i.e., the risk when the exchange rate changes in international transactions, leading to cash variability

Country Risk i.e., the risk associated with investing in a foreign country.

Business Risk i.e., the risk on what will happen with the company based on all the internal and external factors of the business.

Total risk is the total variability in the return on the asset or the portfolio, It is the combination of systematic and unsystematic risk.

LHS : left hand side
RHS : right hand side

COST

Fixed Cost — Variable Cost

DEBITS & CREDITS

GENERAL RULE OF DEBITS & CREDITS

- Dr is on the LHS of T account
- Cr is on the RHS of T account
- Debit – ALL assets
- Credit – ALL liabilities

Imp.

DEBIT	CREDIT
① Increase in asset or expense	① Decrease in asset or expense
② Decrease in liabilities, revenue & owner's equity.	② Increase in liabilities, revenue or owner's equity.

Notation :

DEBIT : Dr
CREDIT : Cr

Finance and Accounts Notes Assistant

classmate
Date
Page

✱ Note: On the company's income statement, a debit will reduce net income, while a credit will increase net income.

✡ TIME VALUE OF MONEY

- **Compounding**
  A process of investing & reinvesting money.
  formula:

$$FV_n = PV(1+r)^n$$

↳ FV: Future value
PV: Present value
r: rate (interest rate of return)
n: time period

- **Discounting**
  writing present value of a future thing

$$PV = FV\left(\frac{1}{1+r}\right)^n$$ (rearranging above equation)

- ∃ a PV table having all the values at different rates.

8 What is FV of money when deposit $1000 today @ 10% for 8 years.

$$FV = PV(1+r)^n.$$

Finance and Accounts Notes
Akshara

✡ Idea:

Importance: Today's $ > Tomorrow's $
Present ← → Future

classmate Date Page

$\Rightarrow FV = 1000\left(1+\frac{10}{100}\right)^8$

$\Rightarrow FV = \$2143.58$

$\Rightarrow FV \approx \$2144$

↳ SINGLE AMOUNT

Q What is PV of 1000 receivable for 6 years if rate is 10%
→ ⇒ we will receive 1000 ⇒ FV

$PV = (1000)\left(\frac{1}{1+10\%/100}\right)^6$

$= 1000\left(\frac{1}{1.1}\right)^6$

$\Rightarrow PV = \$564.47$

* ~~RULE OF 72~~.

eg Suppose I have invested in a corporation. After the time is over — I was supposed to get my investment back (with interest)
↳ If the corporation refuses to pay me back
What kind of Risk is this?
DEFAULT RISK

Finance and Accounts Notes Akshansh

✡ Doubling Period

estimating time when my money gets doubled

> RULE OF 72

$$\text{Time Period (yrs)} = \frac{72}{\text{Interest Percentage}}$$

(or)

> RULE OF 69

$$= 0.35 + \frac{69}{\text{Interest Rate}}$$

✡ ANNUITY:

A constant cash flow which comes at the end of each time period or the monthly/annual return which I get.

✡ PERPETUITY:

It also comes at the end of each time period.
- Life is unlimited. I have cash flow throughout my life

eg: Pension

Imp. for Quiz

CAPITAL BUDGETING PROCESS

1. Identification of Potential investment opportunities
2. Assembling of investment proposals (replacement expansion, new product)
3. Decision making
4. Preparation of Capital budget & appropriations.

Finance and Accounts Notes by Akshansh

CAPITAL BUDGETING PROCESS

If I want to invest anywhere
1. See the options where I can invest
2. Arrange & analyse them
3. Choose the best options
4. Decide how much & how to invest
5. Invest
6. See how is investment going.

5. Implementation
6. Performance review

✡ KEY STEPS IN PROJECT APPRAISAL.

- Forecast the costs & benefits
- Apply suitable investment criteria → Discounted / Non Discounted
- Assess the riskiness of the project (Actual values vs forecast values)
- Estimate the cost of capital
- Value the options.
- Consider the overall corporate perspective.

✡ BASIC PRINCIPLES.

- Focus on cash flow → components of cash flow stream
- Measure on incremental flows
- Ignore sunk costs
- Include opportunity costs.
- Allocation of overhead costs ≡ miscellaneous cost
- Net working capital. (current asset − current liabilities)
- Exclude the financing costs (interest on debt & dividend on preference & equity)
- Inflation

Finance and Accounts Notes Akshansh

Investment Criteria

- Discounting
  - Net Present Value (NPV)
  - IRR (Internal Rate of Return)
- Non Discounting
  - Pay Back Method
  - Avg. accounting rate of return. (ARR)

$$NPV = \sum_{t=1}^{n} \frac{CF_t}{(1+k)^t} - CF_0.$$

CF: Cash flow

Rule :

① If NPV is greater than zero, accept
less than zero, reject.

② IRR : greater than cost of capital : accept
less than cost of capital : reject

③ Payback period : less than time : accept
More than : reject.

eg: If outflow is 30K, i.e, I invest 30K & I am getting return as
10K in 1st year
12K in 2nd year
25K in 3rd year

→ I am getting my return in less than 3 yrs — accept.

Finance and Accounts Notes Akshansh

Average Rate of Return

> ARR = $\frac{\text{Profit after tax}}{\text{Book value of investment}}$ ≡ $\frac{\text{Net Income}}{\text{Net Investment}}$

☆ NPV: Takes into consideration time value of money.
So, advantageous

☆ Numericals will be asked on this topic
↳ Details done towards the end

Finance and Accounts Notes
Akshansh

classmate
Date 15/10/24
Page

DEBITS & CREDITS.

JOURNAL ENTRY

(first book entry that is done)

sample format:

(J12)	Explanation	Dr	Cr

any no. for a journal

T- ~~TABLE~~ ACCOUNT

Assets = Liabilities + Shareholder's Equity

~~Eq~~ Dr	Cr	=	Dr	Cr	+	Dr	Cr
(+)	(−)		(−)	(+)		(−)	(+)
Increase	Decrease						

Capital

Dr	Cr
(−)	(+)

Revenue

Dr	Cr
(−)	(+)

Expense

Dr	Cr
(+)	(−)

→ Based on the idea:
Debits: Increase in asset or decrease in liability or O/S Equity
Credits: Increase in liability or O/S equity or decrease in asset

Dr is +ve when expense takes place (∵ my equity decreases)

Finance and Accounts Notes Akshansh

MAKING JOURNAL ENTRY

classmate Date Page

* Note: For any journal entry:
  1. Write debits first
  2. Write credits second
  3. Always indent your credits.

Eg

(1) Equipment of 5000 was purchased on cash

Explanation	Dr	Cr
Equipment	5,000	
Cash		5,000

→ Indent credit

(2) An inventory of 10,000 was purchased. 2000 on cash & 8000 on credit

Explanation	Dr	Cr
Inventory	10,000	
Cash		2000
A/c Payable		8,000

→ Indent credit

(3) Invested 7,000 in business through stock

Explanation	Dr	Cr
Cash	7,000	
Capital		7,000

(4) Paid 900 as rent for current month

Rent	900	
cash		900

Finance and Accounts Notes Akshansh

(5) Purchased supplies of 600 on account
(6) Paid 125 to advertise in Gulf News
(7) Received 4K cash towards services provided
(8) Performed 5400 worth of services on account
(9) Paid 2500 for employee salaries
(10) Paid for supplies purchased on account earlier this month
(11) Received cash payment of 4K for services paid on account:

	Explanation	Dr	Cr
(5)	Supplies	600	
	A/c Payable		600
(6)	Advertisement	125	
	Cash		125
(7)	Cash	4000	
	Revenue		4000
(8)	A/c receivable	5400	
	Revenue		5400
(9)	Salaries	2500	
	Cash		2500
(10)	A/c payable	600	
	Cash		600
	(Decrease in A/c payable = Debit		
	Decrease in cash = Credit)		
(11)	Cash	4000	
	A/c receivable		4000
	(Inc in cash = Debit		
	Dec in A/c receivable = Credit)		

Finance and Accounts Notes Akshansh

✡ DEBIT BALANCES ON LEFT
✡ CREDIT BALANCES ON RIGHT

(12) Borrowed $5000 from Emirates NBD.
(13) Purchased office equipment worth 4200 on a/c
(14) Paid $275 towards utilities.

	Explanation	Dr	Cr
(12)	Cash	5000	
	Note Payable		5000
(13)	Equipment	4200	
	A/c payable		4200
(14)	Utility Expense	275	
	Cash		275

(15) Estimated useful life of equipment bought for 4200, is 5 years.
(16) 6000 is paid as insurance per annum
(17) I have used 400 of my supplies in the month's end.

	Explanation	Dr	Cr
(15)	Depreciation Expense	70	
	Accumulated Depreciation		70
	$\left(\frac{4200}{5\text{ yrs} \times 12\text{ months}} = 70\right)$		
	(All kinds of depreciation come under Accumulated Depreciation)		
	→ Prepaid asset		
(16)	Insurance	6000	
	Cash		6000
(17)	Cost of goods sold	400	
	Supply		400
	→ Decrease in supply		

Finance and Accounts Notes Arshdeep

classmate
Date
Page

(18) 12000 is being received as advance to provide services for whole year.

Explanation	Dr	Cr
Cash	12000	
Deferred Revenue		12000

→ Also called as Unearned Revenue

(i.e., I have received cash payment but my credit entry comes under liability (unearned revenue)

As time passes by, I start putting it in Revenue (earned revenue) } ∵ advance was paid for whole year

☆ In the above case, we made (JOURNALS). Now, we will make (T-Account) or (LEDGERS)

Difference:

Journals : we write explanations & then debit & credit for that (previous example)

Ledgers or T-Accounts : for every explanation/item (like cash, equipment, AR payable ... etc) we create a separate ledger (a table)

eg:- Dr Cash Cr

≡ T-Account.

Finance and Accounts Notes Akshansh

classmate
Date
Page

Eg. (Re-written the same eg. in ledger entry format)

(1) Invested 7000 in business through stock

Idea: we have 2 entries: one on cash & other on capital, so, make 2 ledgers:

* One on asset side, one on equity side.

Dr Cash Cr	
7000	

Dr Capital Cr	
	7000

(2) Paid 900 for rent of current month.

* One on asset, other on equity side.

Dr Cash Cr	
	900

Dr Rent Expense Cr	
900	

(3) Paid 900 as rent for next month

* Both on asset side.

Dr Cash Cr	
	900

Dr Prepaid rent Cr	
900	

(4) Purchased supplies of 600 on account.

* One on asset & other on liability side.

Dr Supplies Cr.	
600	

Dr A/c Payable Cr	
	600

Finance and Accounts Notes Akshansh

(5) Paid 125 as advertisement
* One on asset other equity

Dr Cash Cr
125

Dr Adv. Expense Cr
125

(6) Received 4000 towards services provided
* one on asset & other on equity

Dr Cash Cr
4000

Dr Revenue Cr
4000

(7) Performed 5400 worth of services on account
* One on asset & other on equity

Dr A/c Receivable Cr
5400.

Dr Revenue Cr
5400

(8) Paid 2500 towards salaries

Dr Cash Cr
2500

Dr Salaries Expense Cr
2500

(9) Paid for supplies that were earlier bought on account
* One on asset, other on liability

Dr Supplies Cr
600

Dr A/c Payable Cr
600

Finance and Accounts Notes Akshansh

(10) Received cash of 4000 for services paid on A/c.

Dr Cash Cr	Dr A/c Receivable Cr
4000	4000.

(11) Borrowed 5000 from NBD.

Dr Cash Cr	Dr Note Payable Cr
5000	5000

(12) Purchased equipment of 4200 on A/c.

Dr Equipment Cr	Dr A/c Payable Cr
4200	4200.

(13) Paid 275 towards utilities.

Dr Cash Cr	Dr Utilities Cr
275	275

(14) Estimated useful life of equipment bought of 4200, is 5 years. ($^{4200}/_{12 \times 5} = 70$)

& One on asset, other on equity

Dr Accumulated Depreciation Cr	Dr Depreciation Expense Cr
70	70

Finance and Accounts Notes Akshitesh

(15) Paid 6000 for prepaid insurance

Dr Cash Cr		Dr Prepaid insurance Cr	
	6000	6000	

Imp Now, after all the transactions are complete,

WHATEVER ON ASSET SIDE:

Do: $\sum$(Debits) − $\sum$(Credits)

Write Ans. on Debit side

WHATEVER ledger on liability or Equity side:

Do: $\sum$(Credits) − $\sum$(Debits)

Write Ans. on Credit side

→ eg: For the cash ledger, we have:

Dr Cash Cr

7000 (1)			
	900 (2)	→ Transaction no.	
	900 (3)		
	125 (5)	Do: Dr (7000+4000+4000+5000)	
4000 (6)		−	
	2500 (8)	Cr (900+900+125+2500+275	
4000 (10)		+6000)	
5000 (11)			
	275 (13)	= 20,000 − 10,400	
	6000 (15)	= (9600)	
		→ write it on Dr side	
9600		(∵ it's asset)	

Similarly, do for all ledgers. (Not shown in notes)

Finance and Accounts Notes Akshansh

(I)

Falaksamsa Corp. is a software programming & maintenance service provider to the educational institutions located in DIAC. On June 30, 2013 accountant reported ending balances for cash $30,000, Office supplies $3000 & Equipment of $36,000 A/c payable 25,200, Capital $52,800 but did not mention A/c receivable. Following transactions occured in July & August 2013

(1) On July 1st Received $72,00 from customers towards the services performed in the month of June
(2) 5th : Paid 16800 cash towards A/c payable
(3) 15th : Earned revenue of 45000 of which 18000 is collected in cash & balance is due in Aug.
(4) 16th : Purchased photocopy machine for 12000 by paying cash 2400 in cash & remaining on A/c it has a useful life of ~~5 yrs~~ 1 years
(5) 17th : Appoints 3 workers on a part time basis @ 300 per week for each worker
(6) 20th : Paid rent in advance for 3 months from July onwards @ 5400 per month
(7) 25th : Paid $15000 towards the salaries of workers.
(8) 28th : Paid Gulf news for advertising expense $2400
(9) 30th : Incurred utilities expenses $540
(10) Aug 6th : Dividends were paid of 4200 to the shareholders.
(11) 8th : Received 48000 towards programming services provided to Emirates University
(12) 15th : Received a loan of 12000 from ADCB
(13) 20th : Received $4800 from KHDA towards services provided in the month of July.

Finance and Accounts Notes by Alshams

classmate
Date
Page

What are adjustments?

They are corrections in the already prepared Ledger / T-account.

These are transactions that were not recorded previously. We try to convert Asset → Expenses
Liabilities → Revenues

> For the scope of the current problem, we will do it without adjustments & then, add ADJUSTMENTS later on in the continued problem. Basically, whenever the transaction says, "was not recorded" or similar term, then we are doing adjustments

☆ V. Imp

For most of the questions that come, the balancing might not be done. Some of the entries might be missing

So, ① balance it (Σ debit = Σ credit or Balance using Accounting eqn)

② Find missing entry

③ Continue solving question

Finance and Accounts Notes Akshansh

Soln.-

Dr Cash Cr	Dr A/c Payable Cr	Dr Capital Cr
30000	25,200.	52,800.

Dr Office supply Cr
3000

Dr Equipment Cr
36000.

Dr A/c Receivable Cr
x

$$69000 + x = 78000$$
$$x = 9000$$

---

① Dr Cash Cr

72000.

Dr A/c Receivable Cr

for services provided	72000.

② Dr Cash Cr

16800

Dr A/c Payable Cr

16800.

③ Dr Cash Cr

18000

Dr Revenue Cr

45000

Dr A/c Receivable Cr

27000

Finance and Accounts Notes Mrshansh

④ Dr Cash Cr

	2400

Dr A/c Payable Cr

	9,600

Dr Equipment Cr

12000.	

Now adding depreciation

Dr Accumulated Depreciation Cr

	1500.

Dr Depreciation Cr Expense

1500	

12 → 12000

3 months → $\frac{12000}{12} \times \frac{3}{2}$

$= 1500$

∵ purchased on 16th July.

So, 16th July — 31 Aug = $\frac{3}{2}$ months.

⑤ Workers were appointed on 17th July.

So, 17th July — 31st Aug = 6 weeks.

Hence, price paid = $(300 \times 6) \times 3$ workers

$= (1800) \times 3$

$= 5400$.

Dr Cash Cr

	5400

Dr Salaries Expense Cr

5400	

Note :

Don't make this entry :

I am told to do appointment.

When ? ⇒ NOT told.

If Income Statement is written, enter it there.

Finance and Accounts Notes Nishant

(5) Dr Cash A/c

5400×3 = 16200

Dr Prepaid Rent A/c

5400×3

(7) Dr Cash A/c

15000

Dr Wage A/c Expense

15,000

(8) Dr Cash A/c

2400

Dr Adv. A/c Expense

2400

(9)

Dr A/c Payable A/c

540

Dr Expense A/c Utilities

540

(10) If Dividends were declared, But WHEN it will be paid, NOT mentioned ∴ Don't change Here, we have paid

Dr Cash A/c

4200

Dr Dividend A/c

4200

Finance and Accounts Notes Akshansh

(11)

Dr Cash Cr	
48000	

Dr Revenue Cr	
	48000

(12)

Dr Cash Cr	
12000	

Dr Note Payable Cr	
	12,000

(13)

Dr Cash Cr	
4800	

Dr A/c Receivable Cr	
	4800

Now,

Note: The Above is ONLY for understanding. We DON't write multiple ledgers of the same thing (cash, A/c payable etc). We write all entries for cash in one ledger & BALANCE it.

Log (P.T.O). →

What has been done: Single ledger for each has been created. Now, for ledger of asset, do Dr − Cr & for ledger of liability/equity, do Cr − Dr. Finally write the total value below each ledger (below Dr for Asset & below Cr for liability/equity)

Finance and Accounts Notes Akshansh

WAY TO WRITE LEDGER:

classmate Date Page

Dr Cash Cr

30,000 (Starting Balance)	16800 (2)
7200 (1)	2400 (4)
18000 (3)	15000 (7)
8000 (11)	2400 (8)
12000 (12)	4200 (10)
4800 (13)	16200 (6)
63,000	

Dr Office Supplies Cr

3000 (Starting Balance)

Dr A/c Receivable Cr

9000 (Starting Balance)	7200 (1)
27000 (3)	4800 (13)
24,000	

Dr Equipment Cr

36000
12000 (4)
48000

Dr Accumulated Depreciation Cr

1500 (4)

Dr Prepaid Rent Cr

16200 (6)
16200

Dr A/c Payable Cr

16800 (2)	25200 (Starting)
	9600 (4)
	540 (9)
	18,540

Dr Note Payable Cr

12000 (12)
12000

Cr − Dr = 12000 (Now, put on Cr side)

As on Dr side. DON'T Do Cr − Dr on this (single entry)

*Note: ALL +ve balances ⇒ Adjustments not required.

Dr Dividend Cr

4200 (10)

Dr Revenue Cr

48000 (11)
45000 (3)
93000

Dr Capital Cr

52,800

Dr Depreciation Expense Cr

1500 (4)

Dr Wage Expense Cr

15000 (7)

Dr Adv. Expense Cr

2400 (8)

Dr Utility Expense Cr

540 (9)

Finance and Accounts by Akshansh Notes

Now, writing TRIAL BALANCE

Idea: Write the totals from each table of from the previous page & write the balances in Dr or Cr. Note: We cannot have Dr or Cr as -ve.

After writing all Dr & Cr, we should get

$$\sum Dr = \sum Cr$$

Format:

Falaksamsa Corporation
Trial Balance July, August 2013

Particulars	Dr ($)	Cr ($)
Cash	63,000	
A/c Receivable	24000	
Equipment	48000	
Accumulated Depreciation		1500
Prepaid rent	16200	
Account Payable		18540
Note Payable		12000
Depreciation Expense	1500	
Wage Expense	15000	
Adv. Expense	2400	
Utility Expense	540	
Dividend	1200	
Revenue		93,000
office Supplies	3500	
Capital		52,800
	177,840	177,840

Balanced

Finance and Accounts Notes Akshansh

$\forall$: for all

Q. (II)

Given: (₹) Ending balances in the month of December:

Cash	702,000
A/c Receivable	310,000
Merchandise Inventory	118,400
Prepaid rent	8000
Store Equipment	27,800
Note Payable	20,000
A/c Payable	? → missing
Paid in capital	800,000
Retained earnings	115,800

Stock ≡ being offered or shares being sold to get cash

Idea: Sort the above into Dr & Cr & then find A/c Payable

	Dr	Cr
Cash	702,000	
A/c receivable	310,000	
Inventory	118,400	
Prepaid rent	8000	
Store Equipment	27800	
Note Payable		20,000
Paid in Capital		800,000
R.E		115,800
A/c Payable		?
	1,166,200	= 1,116,200

$\Rightarrow$ A/c Payable = 230,400.

Now, writing/opening ledgers $\forall$ assets & liabilities

Tirana and Accounts Notes Akshansh

Merchanise business : Buy at its own value & sell it

LEDGERS :

Cash

	702,800	15,000 (2)
(1)	260,000	20,000 (3)
(4)	102,000	10,000 (9)
(8)	20,000	
	1,039,000	

Note Payable

	20,000
	20,000 (8)
	40,000

Paid in Capital

	800,000
	800,000

A/c Payable

150,000 (2)	
10,000 (9)	230,400
	160,000 (3)
	365400

Retained Earning

	115,800
	115,800

Merchandise Inventory

118,400	220,000 (5)
180,000 (3)	
78400	

Revenue (Sales)

	352,000 (4)
	352,000

Store Equipment

27,800	
27,800	

Cost of Goods Sold

(5) 220,000	

A/c receivable

310,000	260,000 (1)
(4) 250,000	
300,000	

Prepaid rent

8000	4000 (6)
4000	

Rent Expense

4000 (6)

Accumulated Depreciation

	200 (7)

Dep. Expense

200 (7)

Finance and Accounts Notes Akshansh

Transactions :

(1) Amt due from customers in 1st week of Jan : 260,000
(2) 15,000 is paid towards due of the suppliers.
(3) Acquired merchandise inventory of 180,000 (purchased) giving 20,000 cash. Remaining on credit
(4) Sales on a/c for 90 days for goods worth 352,000 for which cash worth 102,000 was received.
(5) Cost of inventory sold : 220,000.
⇒ Cost of goods sold as 220,000
(6) Recognized the expiration of rental services as 4000 per month
⇒ Start recognizing expense → Rent expense
We will credit Prepaid rent ∵ we are recognizing.
(7) Recognize expiration of equipment → 200 per month
(8) Took 20,000 loan from bank
(9) Paid 10,000 towards equipment paid previously

Now, make trial balance
① Balance all Ledgers
② Write :—

DIOR Corporation
Trial Balance – Jan 2014

Particulars	Dr ($)	Cr ($)
Cash	1,039,000	
A/c receivable	300,000	
Merchandise Inventory	78400	
Prepaid rent	4000	
Store Equipment	27,800	
Accumulated Depreciation		200
A/c Payable		36540
Note Payable		40,000
Paid in capital		800,000
R.E		115,800
Revenue		352,000
Cost of Goods sold	220,000	
Rent Expense	4000	
Depreciation Expense	200	
	1673400	1673400

→ Balanced

Financial Accounts Akhilesh Notes

(This type comes in exam)

Q. Westside repair services had the following balances on March 31 2014

A/c Particulars	Amount
Cash	10,000
A/c receivable	?
Inventory Parts	4000
Prepaid rent	4000
Building	72000
Equipment	16,000
A/c payable	3,800
Paid-in capital	54000
Retained Earning	44,200
Accrued Wages Payable	10,000

During April, following transactions occured:

(a) Collected A/c receivable 6000
(b) Rendered services to customers for cash 8400
(c) Cost of inventory parts used for services rendered, 600
* (d) Yearly depreciation 24000 on building & 19200 on equipment
(e) Paid towards utility bills $1000
(f) Partly settled accrued wages by paying $2000
(g) Paid cash for building repair & maintenance 1600
(h) Recognize rent expense for march 2000
(i) Paid advance to supplier for purchase & supply of inventory parts 1000.

* Unearned Revenue / Deferred revenue: Revenue which will be earned later —— Its a liability

Finance and Accounts Notes by Rishabh

Accrued ≡ Accumulated

(Imp ☆ comes for compre.)

classmate Date Page

Sol^n

Cash

10,000	
(a) 6000	
(b) 8400	
	1000 (e)
	2000 (f)
	1600 (g)
	1000 (i)
18800	

A/c payable

	3800

Paid-in capital

	54600

Accrued Wages Payable

(f) 2000	10000
	8000

Retained Earnings

	44,200

A/c Receivables

6000	6000 (a)
0	

Repair Expense

1600 (g)

Rent Expense

2000 (h)

Inventory Parts

4000	600 (c)
3400	

Revenue

8400 (b)

Prepaid Rent — recognising part of prepaid rent

4000	2000 (h)
2000	

Cost of goods sold

600 (c)

Building

72,000

Equipment

16000

Depreciation Expense

(d) 2000 + 1600
3600

Accumulated depreciation

	24000/12 + 19200/12 (d)
	3600

change yearly to monthly

Utility Bills

1000 (e)

Prepaid Expense

1000 (i)

Finance and Accounts Notes Akshansh

Solving :- A/c receivable initially not given. So, do Dr = Cr & find that value before starting with transactions

So, (106,000) + A/c receivable = 112,000

=) A/c receivable = 6000

Now,

Westside Repair Services
Trial Balance - April 2014

Particulars	Dr	Cr
Cash	18800	
A/c receivable	0	
Inventory Parts	3400	
Prepaid rent	2000	
Building	72000	
Equipment	16000	
Accumulated Depreciation		3600
A/c payable		3800
Accrued wages payable		8000
Paid in capital		54000
Retained earnings		44,200
Repair expense	1600	
Rent expense	2000	
Revenue		8400
Cost of goods sold	600	
Depreciation expense	3600	
Utility Bills	1000	
Prepaid expense	1000	
	122,000	122,000

Balanced

Finance and Accounts Notes Akshansh

Test - 2 Type

(IV) * Doing adjustments : Assets → Expenses
Liabilities → Revenue

Q. The balances as on Jan 1, 2012 for the corporation are given as follows (at the end of 1st 6 months) :

Particulars	Dr	Cr
Cash	8600	
A/c receivable	14000	
Equipment	45000	
Insurance expense	2700	
Salaries & wage expense	31000	
Supplies expense	3700	
Advertising expense	1900	
Rent Expense	1500	
Utility expense	1700	
Notes Payable		20,000
A/c Payable		9000
Owner's capital		22000
Sales revenue		52,100
Service Revenue		6000
	109,100	= 109,100

Analysis reveals the following data :

1) 3700 in supplies expense represents as on Jan. At June 30, 1500 of the supplies was found on hand

Idea : In 6 months, 2200 of supplies were used

So, decrease in supplies of 2200
& increase in supplies expense of 2200

Supplies	
3700	2200
1500	

when writing adjusted trial balance, both of them will come in Dr

Supplies Expense	
2200	

Note : Debits & Credits should be added. LEDGERS MAY NOT MATCH (during adjustments)

Finance and Accounts Notes Akshansh

(2) Note payable was issued on February with 9%, 6 month note ⇒ 20000 was issued from bank on Feb at 9% Rate.
So, take 9% into account for 5 months (Feb-June)
$20,000 \times 9\% \times \frac{5}{12} = 750$ → Interest expense

Interest Payable		Interest Expense	
	750.	750.	

(3) The balance in Insurance expense is a premium on one year policy, dated March 1, 2012
i.e, Insurance, paid in march is for whole year.
We are closing in June.
⇒ March - June = 4 months.
Insurance expense (in Dr) → prepaid is given as 2700. So, for 4 months
$\frac{2700}{12} \times 4 = 900$

So, I was given prepaid insurance. Now Cr the amount that was used in 4 months & Dr it in Insurance Expense

Prepaid Insurance		Insurance Expense	
2700.	900	900.	
1800			

both comes in Dr. side

(4) Service revenues are credited to revenue when received. At June 30, service revenue of 1300 is unearned
⇒ 1300 of service revenue is unearned.
So, out of 6000, I only earned (6000 - 1300) of my revenue. I still have to earn 1300.

Unearned Revenue		Service Revenue	
	1300	1300	6000
			4700

both in Cr side

Finance and Accounts Akshansh Notes

(5) Sales revenue earned but remains unrecorded at June 30 totals ₹2000

→ This account is deferred revenue account

eg: XYZ corp receives 5000 as deferred revenue.

Cash		Deferred revenue	
5000		3000	5000

> of this, 3000 is earned.

⇒ Dr: Deffered revenue

Cr: Revenue

Revenue	
	3000

Unrecorded ⇒ I did not enter this revenue that was incurred. So, this ADDITIONAL unrecorded revenue of 2000 has to be recorded

A/c Receivable		Sales Revenue	
2000			2000

(6) Depreciation is 2250 per year

→ $\frac{2250}{12} \times 6 = 1125$ (6 months)

Accumulated Depreciation		Depreciation Expense	
	1125	1125	

Q Now :—

(a) Journalize adjusting entries at June 30 (assuming adjustments are recorded every 6 months)

(b) Prepare adjusted trial balance

(c) Prepare income statement → OE statement for 6 months ending at June 30. Also make Balance Sheet at June 30

Finance and Accounts Notes Akshansh

(a) Making Journal entry for transactions ① to ⑥

	Explanation	Dr	Cr
(1)	Supplies Expense	2200	
	Supplies		2200
(2)	Interest expense	750	
	Interest Payable		750
(3)	Insurance Expense	900	
	Prepaid Insurance		900
(4)	Services Revenue	1300	
	Unearned Revenue		1300
(5)	A/c receivable	2000	
	Sales Revenue		2000
(6)	Depreciation Expense	1125	
	Accumulated Depreciation		1125

(b) ADJUSTED TRIAL BALANCE

Particulars	Dr	Cr
Cash	8600	
* A/c Receivable	16000	
Equipment	45000	
* Prepaid Insurance	1800	
Salaries & wage expense	30000	
* Supplies	1500	
Advertising expense	1900	
Rent expense	1500	
Utility Expense	1700	
* Insurance Expense	900	
* Interest expense	750	
* Depreciation Expense	1125	
Supplies Expense (3700-1500)	2200	

changed entries

Finance and Accounts Notes Akshansh

Particulars	Dr	Cr
Notes Payable		20,000
A/c Payable		9000
Owner's capital		22000
*Sales Revenue (52,100+2000)		54,100
Services Revenue (6000-1300)		4700
*Interest Payable		750
*Unearned Revenue		1300
*Accumulated Depreciation		1125
	112,975	112,975

This is the new trial balance.

(i)

(c) Income Statement

THE COMPANY
INCOME STATEMENT
For six months end June 30, 2012

Revenues		
Sales Revenue		54,100
Services Revenue		4700
Total Revenue		58,800
Expenses		
Salaries & wage expense	30,000	
Advertising expense	1900	
Rent expense	1500	
Utility expense	1700	
Insurance expense	900	
Interest expense	750	
Depreciation expense	1125	
Supplies expense	2200	
Total expense		40,075
Net Income (Revenue - Expence)		$18,725

Finance and Accounts Notes
Arsalan

(ii) OE statement

THE COMPANY
Owner's Equity Statement
For six months ended June 30, 2012

Owner's capital, Jan 1	0
Investment by owner	22,000
	22,000
Add: Net Income	18,725
Owner's capital, June 30.	40,725

(iii) Balance Sheet

THE COMPANY
Balance Sheet
June 30, 2012

Assets

Cash		8600
A/C receivable		16000
Supplies		1500
Prepaid Insurance		1800
Equipment	45000	
Accumulated Depreciation	-1125	
		43875
		$71,775

✓ Reduce depreciation from price of equipment to get its value.

Finance and Accounts Notes Akshansh

Liabilities and Owner's Equity

Liabilities		
Notes Payable		20,000
A/C Payable		9000
Interest Payable		750
Unearned Revenue	from OE statement (nothing else required)	1300
Total Liabilities		31,050
Owner's Equity → don't include expenses (its under Income statement)		40,725
Owner's capital		
Total Liabilities & OE.		71,775

Q. (V)

Given

McGEE COMPANY
Trial Balance
June 30, 2012

Account No.			
101	Cash	7150	
112	A/c Receivable	6000	
126	Supplies	2000	
130	Prepaid Insurance	3000	
157	Equipment	15000	
201	A/c Payable		4500
209	Unearned Service Revenue		4000
301	Owner's capital		21,750
400	Service revenue		7900
726	Salaries & wage expense	4000	
729	Rent expense	1000	
		38,150	38,150

(Note: In exam, it may not be given sorted into Dr & Cr)

Finance and Accounts Notes by Akshansh

Other data:

1. Supplies on hand (or ending balance of supplies) at June 30 are 750

So, we have supplies = 2000
left = 750
⇒ used = 1250.

Supplies	
2000	1250
750	

Supplies expense	
1250	

2. A utility bill for $150 has not been recorded & will not be paid until next month

A/c Payable	
	150

Utility Expense	
150	

3. Insurance policy is for an years.

Prepaid insurance	
3000	(1500) → $\frac{3000}{12} \times 6$
1500	

Insurance Expense	
1500	

4. $2800 of unearned service revenue has been earned at the end of the month

from what was given ←

Unearned Service Revenue	
2800	4000
	1200

⇒ liability comes

Service Revenue	
	(7900)
	2800
	10700

5. Salaries of 1900 are accrued at June 30

Salaries Payable	
	1980

Salaries & wage expense	
4000	
1900	
5900	

Financial Accounts Notes Arshansh

6. The equipment has a 5-yr life with no salvage value. It is being depreciated at $250 per month for 60 months

for 6 months, depreciation = 250 × 6

Accumulated Depreciation	
	1500

Depreciation Expense	
1500	

7. Invoice representing $1200 of services performed during the month have not been recorded as on June 30.

A/c receivable	
1200	

Service Revenue	
	1200

Now, close the ledgers & make adjusted trial balance

Service Revenue	
	10700
	1200
	11900

Adjusted :-

McGEE Company
Trial Balance
June 30, 2012

Cash	7150
* A/c receivable (6000 + 1200)	7200
* Supplies	750
* Prepaid Insurance	1500
Equipment	15000
* Supplies expense	1250
* Utility expense	150
* Insurance expense	1500
* Salaries & wage expense	5900
Rent expense	1000

Finance and Accounts Notes Akshansh

Income tax : Non-Operating Expense.

-- continued

* Depreciation expense	1000	
* A/c Payable (4500+150)		4650
* Unearned Service Revenue		1200
Owner's Capital		21,750
* Service revenue		11,900
* Accumulated Depreciation		1500
* Salaries payable		1900
	42900 =	42,900

(i)

McGEE Company
Income Statement
For six months till June 30, 2012

Revenues		
Service Revenue		11,900
Total revenue		11,900
Expenses		
Supplies expense	1250	
Utility expense	150	
Insurance expense	1500	
Salaries & wage expense	5900	
Rent expense	1000	
Depreciation expense	1500	
Total expense		11,300
Net Income		600

Finance and Accounts Notes Akshaish

Marketable securities ≡ TDR's, certificates kept in bank → short period
Instead of keeping bulk cash ← we get interest on cash

classmate
Date
Page

(ii)

McGEE
Owner's Equity Statement
For six months ended June 30, 2012

Owner's capital, Jan 1	0
Investment by owner	21,750
	21,750
Add: Net Income	600
Owner's capital, June 30	22,350

(iii)

MCGFE
Balance Sheet
June 30, 2012
Assets

Cash		7150
A/c receivable		7200
Prepaid Insurance		1500
Supplies		750
Equipment	15000	
Accumulated Depreciation	−1500	
		13500
Total Assets		30,100

Liabilities & OE

Liabilities	
A/c Payable	4650
Unearned service revenue	1200
Salaries payable	1900
Total liabilities	7,750
Owner's Equity	
Owner's capital	22,350
Total liabilities & OE	30,100

Finance and Accounts Notes by Akshansh

* Note : Type of Question on Ratios :
If the ratio is ___ . What does it mean?

→ NOT COMING FOR COMPRE : RATIOS

✡ PROFITABILITY EVALUATION RATIOS.

> Gross profit percentage / gross margin percentage :

$$= \frac{\text{Gross Profit}}{\text{Net Sales}}$$

Gross Profit ≡ Sales − Cost of goods sold

Net Sales ≡ Sales Revenue ≡ Sales ≡ Revenue

→ a part of INCOME Statement (or Profit & loss stmt)

eg :- $$\frac{6336.3 - 1617.4}{6336.3}$$

$$= 0.7447$$

[We will be asked analysis : why is cost of goods sold higher? Why this trend changed over the years? etc]

> Return on sales / ~~Net~~ Operating Profit margin

$$= \frac{\text{Operating Net Income}}{\text{Net Sales}}$$

Operating Net Income → Revenue − Expense

→ how much is a company earning from its sales
→ again, see Income statement

eg : $$\frac{406.1}{6336.3} = 0.064$$

→ This value is used to analyse the trend.

Finance and Accounts Notes by Utsarsh

classmate
Date
Page

* > Return on assets :

= Net Income / Total Assets

eg: 406.1 / 3885.8 → given the data in a table, put values to evaluate

> Return on equity :
(looked by investors)

= Net Income / Shareholder's equity

* LIQUIDITY RATIOS

> Current ratio / Working Capital Ratio

= Current assets / Current liabilities.

(≡ 2:1 for any organizⁿ
↳ generally accepted
But, varies with the type of industry [eg. fashion vs steel industry])

* For creditors expecting to be paid in next 12 months, look for HIGHER current ratios

> Quick ratio / Acid test ratio

= Current Assets − Inventory / Current Liabilities

* Quick ratio should be compared b/w companies in the same industry.

Finance and Accounts Notes
Akshansh

Gross Income
- Operating Expense
Operating Profit

★ FINANCIAL RATIOS

- Earnings per share.

$$\frac{\text{Net Income} - \text{Dividends on Preferred Stock}}{\text{Average Outstanding Shares}}$$

- Price earnings ratio
- Dividend yield ratio → $= \frac{\text{Annual Dividends per share}}{\text{Price per share}}$

for long term investor

Relation b/w dividends per share and the market value of shares.

- Dividend payout ratio

for short term investor

How quickly do I pay back my dividends

$$= \frac{\text{Yearly dividend per share}}{\text{Earnings per share}} = \frac{\text{Dividends}}{\text{Net Income}}$$

→ CAPITAL Structure

§ COST OF CAPITAL

↳ owner's / shareholder's investment

- Ideal sources of financing: debt & equity
- Company's primary aim is to maximize its shareholder's value
- Reward shareholders with outstanding returns

⇓

good company

Finance and Accounts Notes Akshansh

Interests, taxes, rates : Non Operating Expense

EBIDTA : Earning Before Interest Depreciation Taxes Amortization

- Capital is obtained in three forms

Debt → Advantage: No voting rights to anyone (they dont interfere)

Preferred Stock → divided on the basis of order of paying dividends (priority to them)

Equity → Shareholder's share profit & loss

Debt → Short term, Long term

Preference → Stock, Share

Debt Instruments → Bonds, Debentures

Only Theory Ques will come

Weighted Average Cost of Capital (WACC)

for compare only

* Why cost of debt is cheaper?
  - We get rid of investor in terms of fixed amount

- r_d : interest rate on firms new debt (before tax)
- $r_d(1-T)$: after tax component of debt
- r_p : component cost of preferred stock
- r_s : cost of common equity raised by retained earnings (internal equity)
- r_e : cost of external equity
- w_d, w_p, w_s, w_e : target weights of debt, preferred stock, RE (internal equity) & new common stock (external equity)

Finance and Accounts Notes Akshansh

• Only Debt is tax deductable (not preference, not equity)

• Cost : $k_e > k_s$

V.V. Imp

$$WACC = w_d k_d(1-T) + w_p k_p + w_c k_s$$

Type of Q: → one of the terms might be missing

- w_d → % of debt
- $k_d(1-T)$ → after tax cost of debt
- w_p → % of preferred stock
- k_p → cost of preferred stock
- w_c → % of common equity
- k_s → cost of common equity

~~P_{ce}~~

- Preferred stock (P_p)
- Preferred dividend (D_p)

• Component cost of preferred stock, $k_p = D_p / P_p$

• $(k_s) = k_{RF} + RP = D_1/P_0 + g = (\hat{k}_s)$

k_s → Req^d rate of return

$\hat{k}_s$ → expected rate of return

- k_{RF} : risk free rate
- RP : risk premium
- D_1/P_0 : Dividend yield
- g : expected growth
- $\hat{k}_s$: expected rate of return
- k_s : req^d rate of return

eg You were hired as a consultant to ABC company, whose target capital structure is 40% debt, 10% preferred and 50% common equity. After tax cost of debt is 6%, cost of preferred is 7.5% and cost of RE is 13.25%. The firm will not be issuing any new stock. What is its WACC?

Finance and Accounts Notes Arjun Singh

Sol^n:- Given :- $W_d = 40\%$
$W_p = 10\%$
$W_e = 50\%$
} Weights

$k_d(1-T) = 6\%$
$k_p = 7.5\%$
$k_s = 13.25\%$
} Costs

$\therefore$ WACC $= W_d k_d(1-T) + W_p k_p + W_e k_s$

$\Rightarrow$ WACC $= 9.78\%$

Finance and Accounts Notes Akshansh

* Mortgage : Long term liability

Date 19/11/14
Page

ANALYSE TRANSACTIONS.

* OS : Over Statement
US : Under Statement
NE : No Effect

eg ① Given a trial balance. Depreciation of equipment was not included.
Where will it have effect?

Soln : Balance Sheet — OS [long term assets are over stated]
Income Statement — OS

eg ② Not accounting interest received (due to marketable securities)
Impact?

Soln Balance Sheet — US
Income Stmt — US
(Breakup → Capital — NE
→ RE — US)

eg ③ Services provided
→ Uncollected & remain unrecorded
→ Balance Sheet (A/c receivable) — US
→ Income Stmt — US
→ Collected but remain unrecorded
→ Balance sheet (cash) — US
→ Income Stmt — US

eg ④ Mortgage (Interest Payable) — not mentioned.
→ Assets — OS] Balance Sheet — NE
→ Liabilities — US]
→ Income Stmt — NE

Finance and Accounts Notes Aishani

* When you can't find probability ⇒ Uncertainty
* Standalone risk : Investment on only one asset

RISK AND RATE OF RETURN

* High returns ⇒ high risk

* Investment Alternatives

Imp. ex

		①	②	③	④	⑤
Economy	Prob.	T-Bill	HT	Collateral	USR	MP
Recession	0.1	5.5%	-27%	27%	6%	-17%
Slow	0.2	5.5%	-7%	13%	-14%	-3%
normal	0.4	5.5%	15%	0%	3%	10%
strong	0.2	5.5%	30%	-11%	41%	25%
boom	0.1	5.5%	45%	-21%	26%	38%

Above is an investment split into 5 situations. See who has higher risk?

Idea: Find rate of return

- $\hat{r}$ = expected rate of return $= \sum_{i=1}^{N} r_i P_i$
- $\frac{\text{Dividend} + P_E - P_B}{P_B}$; P_E: Price ending, P_B: Price beginning
- Standalone risk : Single
- Portfolio risk : Combination of 2 or more.

* • Ways to avoid RISK :
1) Hedging
2) Portfolio → Business Risk & Market risk
3) Insurance
4) Diversification

After finding $\hat{r}$ for ① — ⑤, we find:
HT (12.4%), Market (10.5%), USR (9.8%), T-bill (5.5%), Coll. (1%)

* Higher the rate of return → better (but more risk)

Finance and Accounts Notes by Akshansh

eg: A & B
both with low risk, but diff^{t} rate of return. Then, VARIANCE is useful

✱ Standard Deviation & Variance

✓ Importance

✱ Note:

✓ Risk is omnipresent

✓ personality of people matters

↳ I can't take much risk : see low rate of return

↳ I don't mind taking risk : see high rate of return

eg

Stock	Expected Returns	Investments
AA	31.2 %	$190,000
BB	24.0 %	$350,000
CC	18.6 %	$200,000
DD	11.9 %	$500,000

Find: expected rate of return

Idea: Add all the investments (= $1,240,000)

Take percentage of those investments

↳ $\frac{31.2}{100}(1240,000), \frac{24}{100}(1,240,000)$

• Standard deviation$^{(\sigma)}$ ∝ Risk.

Q.

Economic Condition	Probability	Returns of VCC Ltd	Returns of LCC Ltd
High Growth	0.3	100	150
Low Growth	0.4	110	130
Stagnation	0.2	120	90
Recession	0.1	140	60

Which of the two companies is risky investment?

Finance and Accounts Notes Akshansh

KNOW • Define: Risk free
Risk Premium
Risk Market
} Imp:

Idea :- VCC Ltd.

Economic Condⁿ	Prob. (P)	Rate of Return (R)	$\bar{R} = P \times R$	$\Sigma(R-\bar{R})$	$[\Sigma(R-\bar{R})]^2$	$P[\Sigma(R-\bar{R})]^2$
High Growth	0.3	100	30	-12	144	43.2
low Growth	0.4	110	44	-2	4	1.6
Stagnation	0.2	120	24	8	64	12.8
Recession	0.1	140	14	28	784	78.4
			112			

Variance (V) = 136

Expected Return = 112%

Risk = Standard deviation = $\sqrt{V} = \sqrt{136} = 11.66\%$.

Why, LCC Ltd :- Expected Rate = 121%.

Risk = Std. Deviation = $\sqrt{V} = \sqrt{849}$
= 29.14%

Observation :-

Risk : LCC > VCC

Investor Chooses accordingly

- RISK AVERSION
  - Don't want to take risk (they want/require higher rate of return to take risk)
- RISK PREMIUM
  - Diff b/w return on a risky asset and a risk free asset, which serves as compensation for investors to hold riskier securities.

→ Investor says: I'm taking extra risk → give me premium

Finance and Accounts Notes Akshansh

→ Not for compse.

TALK

LEGAL ASPECTS OF SETTING UP A BUSINESS IN UNITED ARAB EMIRATES.

(Consultant : Adam Consulting)

☆ Overview

UAE Companies Law
↳ Introduced by ~~venture of~~ virtue of Federal Law no. 8 in 1984

☆ 7 types of legal entities.
① Main : LLC.

☆ Category of Licenses

1) Commercial ~~Lic~~ License : Trade locally.

2) Professional License : Provide service locally

3) Industrial License : Produce locally

4) To establish branch office / foreign company.

☆ Jurisdiction

> Mainland Company (eg: anything in Sheik Zayed Road)
> Free Zone Company (eg: Academic city, Knowledge Village)
> Offshore Company

Finance and Accounts Notes by Akshansh

MAINLAND

Ownership :-

Commercial
Expatriate 49% max
UAE National 51% min.

Industrial
same as commercial

Professional
Expatriate : 100%.

Branch / Representative
Parent Company

FREE ZONE

- All 100% owned by Expatriates
  - i.e, don't share with UAE nationals.
- ∃ trade barriers

OFFSHORE

- People looking for international trade

- Currently : 7 mainland jurisdictions (all 7 emirates)
  : 37 free zone jurisdictions.
  : 4 offshore jurisdictions

✡ PROTECTION OF BUSINESS.

- Intellectual Property
  - In UAE : whoever is first to get trademark, is the owner.
- Insurance and Professional Indemnity
- Minimizing Liabilities.
  - real estate brokerage : can only be done by Emirati
  - Partner with UAE nationals : liabilities decrease
- Subsidiaries
  - ★ Shadya law : wealth gets transferred to family

Finance and Accounts Nitesh Ahinash

- Control and Brand Reputation

- For mainland & free zone companies, information about owners and shareholders is publicly available.

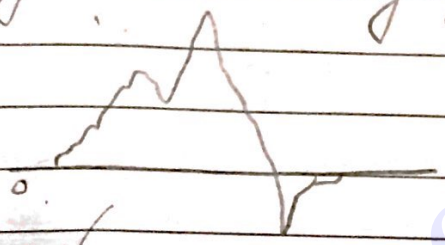
Finance and Accounts Notes Akshansh

→ Investment in two or more assets

PORTFOLIO RISK

- Diversifiable Risk + Market Risk
- Portfolio Risk $\propto \frac{1}{\text{No. of Stocks}}$
- WW Approach : +vely correlated
- WM Approach : -vely correlated

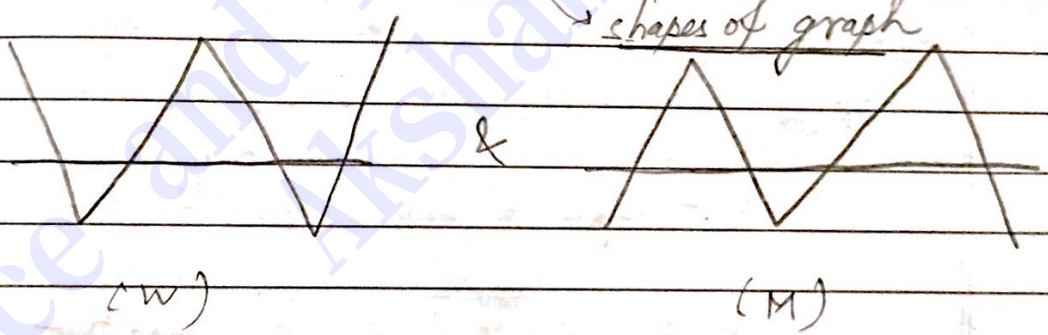
eg:- If I have a graph like :-



combination of 2 : (W & M)

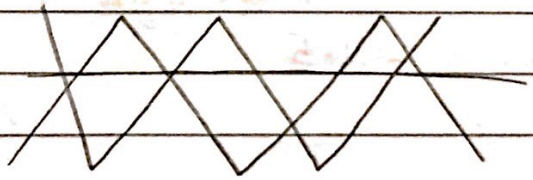
eg. Given a scenario. Kind of gives : would you be interest to invest in WW Approach stock ?

shapes of graph



(W) (M)

⇒



WM Approach (calculated from 8)

- Market Risk (β) → beta

Keeps track of movement of stock alongwith market conditions.

↳ β = 1 Ideal.
< 1 Less Risky
> 1 Higher Risk

Finance and Accounts Notes Akshansh

§ Capital Asset Pricing Model (CAPM) Approach

eqn :-

$$k_s = k_{RF} + (RP_M) b_i$$

$$= k_{RF} + (k_M - k_{RF}) b_i$$

- k_s : Reqd rate of return on stock i
- k_{RF} : Risk free
- RP_M : Market risk premium

Q. Risk free rate of return of stock X is 4.3%, expected return on market is 15.7% & reqd rate of return is 21.5%. What is beta (b)

$$k_s = k_{RF} + (k_M - k_{RF}) b$$

$$\Rightarrow b = \frac{k_s - k_{RF}}{k_M - k_{RF}} = \frac{21.5 - 4.3}{15.7 - 4.3} = 1.5$$

$$\Rightarrow b = 1.5$$

★ Coefficient of variation = $\frac{\text{Std. deviation}}{\text{Expected return}} = \frac{\sigma}{\hat{r}}$

Finance and Accounts Notes Akshansh

classmate
Date 3/12/14
Page

WORKING CAPITAL

- Capital reqd for general & day to day activities
- Originated with Yankee Peddler
- Includes management of what I have, how much I will require in future and so, how do I plan my expenses

Q. Which is more beneficial?
Merchandise on credit ⟶ better (no interest)
Merchandise borrowed from bank → has interest payable also

- Working capital measures liquidity of the company.

Gross Working Capital

Net Working Capital
* NWC = Current Assets
− Payables
+ Accruals

- Cash conversion cycle
  - Short : eg: grocery
  - Long : eg: automobile industry

- Asset holding
  - More : eg: hotel industry (investment in fixed assets)
  - Less : eg: food industry

Finance and Accounts Notes Akshansha

- Current Asset Investment Policies
  - Restricted (lean and mean)
  - Moderate
  - Relaxed / Liberal policy

- Current Asset Financing Policy
  Primary sources: bank loans, credit from supplies, accrued liabilities, long term debt, common equity

* Cash Conversion Cycle (CCC)
  Length of time b/w paying for working capital & retrieval/collecting cash from sale of working capital
  - Operating Cycle: Inventory period + A/c receivable period
  - Cash Operating Cycle: Operating − A/c payable period

→ Divided in 3 periods:
  - Inventory conversion period (ICP)
    eg: fashion industry — winter comes, change material (related with when merchandise was sold)
  - Average collection period (ACP)
    - how much time you get back
  - Payables deferral period (PDP)
    - length of time suppliers give to corporate to pay back its purchases.

V. Imp
* CCC = ICP + ACP − PDP

Finance and Accounts Notes Akshansh

eg Xavier Ltd for year end 2013

Income Statement (AED in 0000)

Sales	80
COGS	56
Inventory	(Beginning 9, Ending 12)
A/c receivable	(Beg 12, End 16)
A/c payable	(Bg 7 - End 10)

} Take Average ((Beg. + Ending)/2)

Formulae :

$$ICP = \frac{\text{Inventory}}{\text{COGS per day}} = \frac{(9+12)/2}{56/365}$$

$$ACP = \frac{\text{Receivables}}{\text{Annual sales}/365} = \frac{(12+16)/2}{80/365}$$

$$PDP = \frac{\text{Payables}}{\text{Purchases per day}} = \frac{(7+10)/2}{56/365}$$

$$= \frac{\text{Payables}}{\text{COGS}/365}$$

⇒ ICP = 68.4375

ACP = 63.875

PDP = 55.4017857

⇒ CCC = ICP + ACP − PDP

CCC = 76.9107143

Finance and Accounts Notes Akshaish

CASH FLOW STATEMENT

↳ Tells liquidity & solvency of a company.
↳ long term liability

Note :-

- Equipment has depreciation associated with it (done when we made financial statements)
- Assets like PATENTS & COPYRIGHTS also get depreciated but, the term is AMORTIZATION*

Current Asset

↙ Permanent

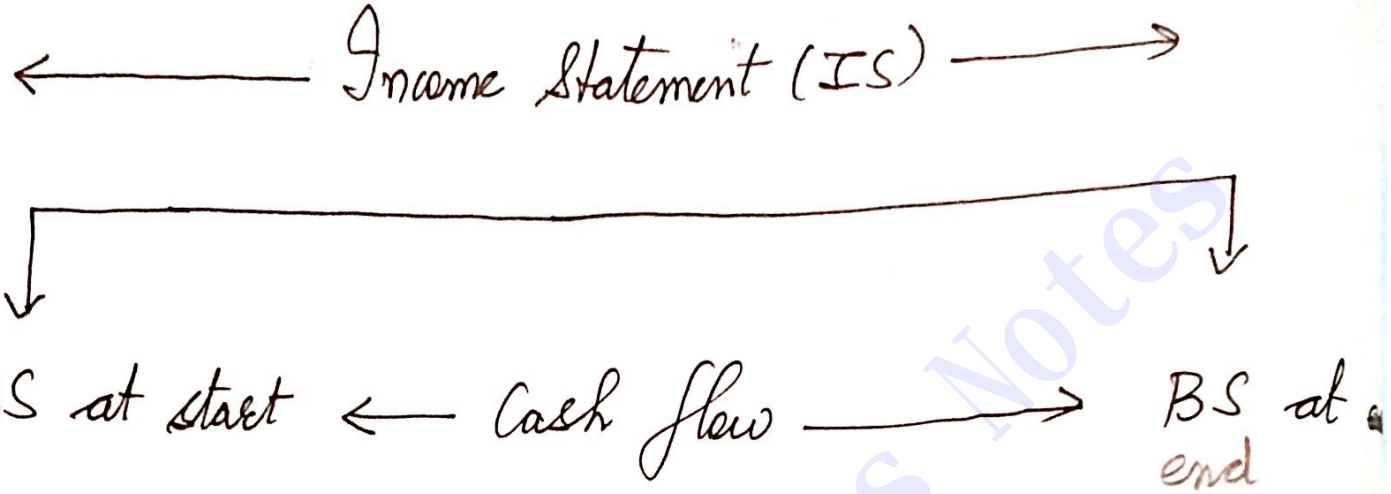
↘ Temporary
- To meet any temporary needs of, some assets are allocated.

Importance of Cash Flow Statement

↳ A conjunction between income statement and balance sheet
↳ Essential input for economic decision models.
↳ Reflects total changes of cash position in the organization.

Finance and Accounts Notes Akshansh

* Relationship with BS & IS



* General Idea :

Note where cash is going.

* Types of Activities

→ OPERATING

Income Statement

- like : payment to suppliers, employees, taxes, income tax; receipts from fees, sale of goods etc and rendering services etc.

→ INVESTING

- Fixed assets (investment done in these)
- Payments of interest & dividend (these days taken as operating)
- Receipts from bank loans, payment of stocks.

→ FINANCING

- like, loans taken from bank.
- Shareholder's Equity and Dividends

Finance and Accounts Notes Akshansh

* Note:

Cash flow statement = Operating + Investing + Financing

- Inflow $\xrightarrow{\text{Notation}}$ Operating
- Outflow $\xrightarrow{\text{Notation}}$ (Operating)

[Put Brackets to denote outflow]

---

* Note:

Deferred : Delayed

Accrued : Accumulated

---

* Methods for writing Cash Flow Statement

- Direct
- Indirect (more detailed: considering change from one account to the other)

* Note:

↑ A/c Receivable ⇒ ↑ Revenue ⇒ ↑ Sale on credit.

↓ Inventory ⇒ ↑ Sale of Goods

Finance and Accounts Notes Akshansh

↑ Inventory ⇒ ↓ Cash or ↑ in credit
↓ A/c receivable ⇒ ↑ Cash

✡ FORMAT & STRUCTURE : Cash flow Statement

	Cash flow from Operating Activities	(2M)
+	" Investing "	(2M)
+	" Financing "	(2M)
	Net Change in cash during period	
+	Beginning cash balance	
	Ending Cash Balance	

Q. Use this info. to calculate the amounts to report on the CF statement for investing activities :

1) Beginning plant assets	$76,000
2) Beginning accumulated depreciation	5,200
3) Depreciation for the year	1,300
4) Purchases of new assets	4,200
5) Ending new plant assets	72,850
6) Loss of sale on plant assets	150

Sol'n : Idea : Prepare investing activities
⇒ Inflows − Outflows

Finance and Accounts Notes Akshansh

Note: See the format of activities in CF statement (Direct & Indirect)
↳ SLIDES

classmate Date Page

- We are given beginning and ending "net plant assets". So, we can say,

Beginning plant asset + Purchase of new asset − Sales = Ending net plant asset

⇒ 76,000 + 4,200 − Sales = 72,850

Sales = 7350

Now, reduce value of accumulated depreciation (Or, reduce it directly from 76000)

⇒ 7350 − 5200

= 2150.

Reduce Depreciation expense from this

= 2150 − 1300.

⇒ Book value of plant assets sold = 850.

Now,

As the assets were sold at loss, the cash received from sale = 850 − 150

= 700

(loss ⇒ subtract 150. gain ⇒ add 150)

Notes

- HISTORICAL COST

The cost at which equipment was purchased

- BOOK VALUE

What is its ~~we~~ value after depreciation is included

- MARKET VALUE

What is its value when sold

Type of Ques. for compre.

☆ Note: Solve an accounting question. Use finance to comment on results.

Finance and Accounts Notes Akshansh

DIRECT METHOD

Q. Prepare Cash Flow Statement

Idea: Diff. in CF statement over the years, is the answer.

The following info is available for Zenith Co ended Dec 31, 20Y4. Its cash & cash equivalents on Jan 1st 20,000 while closing cash balance on Dec 31st is $55,000.

(⇒ Ans = 55000 − 20000)

① The company issued bonds payable for $100,000 cash.
② Cash received from sales to customers $870,000
③ Suppliers and employees were paid $764,000 cash during the year.
④ Marketable securities worth $45000 were sold for a loss of 5000
⑤ Borrowed $45000 by issuing short term notes payable to banks
⑥ Paid income tax $38,000
⑦ loan collections during the year $12,000

What has to be done?

Given transactions → see the type of activity & tell inflow or outflow of cash.

{( ) ⇒ outflow}

Operating		Investing		Financing	
Inflow	Outflow	Inflow	Outflow	Inflow	Outflow
② 870,000	③ (764,000)	④ 40,000		① 100,000	
	⑥ (38,000)	⑦ 12,000		⑤ 45,000	

↓ can be financing activity also.

Finance and Accounts Assignment Notes

(8) Interest and dividends received from external investments during the year amounted to 10,000.

Operating		Investing		Financing	
In	Out	In	Out	In	Out
		(8) 10,000			

→ can be in operating / financing also
(Just make sure inflow, outflow is right)

(9) Repaid 55000 due on short term loans

(9) (55000)

(10) Paid 28000 interests on loans borrowed

(10) (28000)

(11) Plant assets having a book value of 50000 were sold for a profit of 25000

(11) 75000

(12) Cash loaned to borrowers 17000 → I'm giving loan i.e, I'll get interest

(12) (17000)

(13) Company purchased plant assets and paid 160,000 for it

(13) (160,000)

(14) Cash paid for purchase of marketable securities 65000

(14) (65000)

(15) Cash dividends declared & paid to stockholders 40000

(15) (40000)

(16) Issued 1000 shares with par value $10, capital stock for cash at a price of $50 per share

(16) 50,000

New, Do, Inflows − Outflows

= 1,202,000 − 1,167,000

= $35,000 (Net change in cash during period)

+ $20,000 (Beginning cash balance)

= $55,000 (Ending Cash Balance)

Finance and Accounts Notes by Arsalan

• Indirect method: Best method
Followed everywhere
Easiest

☆ INDIRECT METHOD

Add when ∃ ↑ in cash → ↓ in asset or ↑ in liability

Subtract ↓ in cash

Net Income +

Depreciation
↓ in A/c receivable
↓ in inventory
↓ in prepaid expense
↑ in payable
↑ in deferred taxes
Loss in disposal

→ doesn't include notes payable, short term borrowings, current pos^n of long term debt

− ↑ in A/c receivable
↑ in inventory
↑ in prepaid expense
↓ in payables
↓ in deferred tax
Net cash provided by or used in operating activities
Gain in disposal
Cash payment for purchases

= Net Cash flow from Operating Activities

Q.

KOSINSKI MANUFACTURING COMPANY
Income Statement
For the year ended Dec. 31, 2012

	(000's)	(000)
Sales Revenue		6583
Operating expenses (excluding depreciation)	4920	
Depreciation expense	880	5800
Income before income tax		783
Income tax expense		353
Net Income		430

Included in operating expense is $24000 loss resulting from sale of machinery for 270,000 cash. Machinery was purchased at a cost 750000

Finance and Accounts Akshansh Notes

The following balances are reported on Kosinski's comparative balance sheets at Dec 31

KOSINSKI MANUFACTURING COMPANY
Comparative Balance Sheets (partial)

	2012 (000's)	2011 (000's)
Cash	672	130
A/c receivable	775	610
Inventory	834	867
A/c payable	521	501

Now, Make CF statement using indirect method

Sol^n Idea : See Net Income from Income Stmt = 430,000
Add Depreciation +880,000
Add loss +24,000
Deduct ↑ in A/c receivable (775000 - 610000)
Add ↓ in inventory + 33,000
→ 867000 - 834000
Add ↑ in A/c payable + 20000
→ 521000 - 501000
Deduct income tax expense (353,000)

So, cash provided by operating activities =
430,000
880000
+ 24000
- 165000
+ 33000
+ 20000 792,000
⇒ Cash from Operating Activities = 1,222,000

Finance and Accounts Notes Ayshansh

Indirect Method Format for Making CF Statement

Note: The question does not give the complete balance sheet. So, here, all activities mentioned are Operating Activities. But, in general, investing & financing activities can also be present. Then, they have to be included.

KOSINSKI MANUFACTURING COMPANY
Cash Flow from Operating Activities
Indirect Method

Net Income	$ 430000
Adjustment:	
Depreciation	880,000
Loss	24,000
Increase in A/c receivable	(165,000)
Decrease in inventory	33,000
Increase in A/c payable	20,000
Net Cash Flow from Operating Activities	1,222,000

Note: Format of Investing & Financing Activity (Indirect)

XYZ Comp.
Cash Flow From Investment Activities
Indirect Method

Cash from sale of land	xxxx
- - - -	xxx
- - - -	
Cash flow from Investing Activity	xxxx

XYZ company
Cash Flow from Financing Activities
Indirect Method

Cash dividend	xxx
- - - -	xxx
Cash flow from Financing Activity	xxxx

Finance and Accounts Akshansh Notes

used to see increase/decrease

Q. Prepare CF Statement (5-6 Marks)

INCOME STATEMENT

	2006		2005	
Revenues		191,400		182,600
Operating Expenses:				
Depreciation	26,400		26400	
Fuel	77,000		46,200	
Driver's salaries	44,000		35,200	
Tax and licenses	22,000		17,600	
Repairs	30,800		19,800	
Miscellaneous	2,200	202,400	1,100	146,300
Income (loss)		(11,000)		36,300

BALANCE SHEET

	12/31/2006	12/31/2005
Cash	22,000	4,400
A/c receivable	8,800	26,400
Net fixed assets	198,000	224,400
Total assets	228,800	225,200
A/c payable	30,800	22,000
Accrued salaries	8,800	5,500
Other accruals	3,300	1,100
Long term debt	100,100	129,800
Comp. capital	85,800	96,800
Total liabilities and Capital	$228,800	$225,200

use of 2006

Sol^{n}: See the net income from income statement = (11,000)
Add depreciation to this = + 26,400.
Now, add/deduct changes in balance sheet to this to get final cash flow due to operating activities.
(Note: Finial answer = 22,000 − (4,400 = 17,600)

Finance and Accounts Notes Akshansh

XYZ Company

Cash flow Statement (---th ---)

Operating Activities		
Net Income		$ (11,000)
Adjustments		
Depreciation		26400
Decrease in A/c receivable		17,600
Increase in A/c payable		8,800 → 30800 - 22000
Increase in accrued salaries		3300
Increase in other accruals		22,000
Investing Activities		
Cash Flow from Investing activities		NIL
Financing Activities		
Decrease in long term debt		(29700)
Net Increase in cash		17,600
Beginning cash balance	4400	
Ending cash balance	22000	17,600

Finance and Accounts Notes Akshansh

Revisit : CAPITAL BUDGETING

✱ Net Present Value (NPV)

$$NPV = \sum_{t=1}^{n} \frac{CF_t}{(1+r)^t} - CF_0$$

Q. Identify the amount and time period of each cash flow associated with a potential investment

1) Initial cash outlay : $70,000
2) Year 1 → 4 net cash savings : $21,000 per year
3) Year 5 net cash savings : $26,000
4) Reqd rate of return : 12 %.

Soln Cash outflow : (70000)

Cash Inflow :- 21,000 Yr 1
21,000 Yr 2
21,000 Yr 3
21,000 Yr 4
26,000 Yr 5

21000 ← 21000

$$NPV = \left\{ \frac{CF_{1st\ Yr\ Inflow}}{(1+12\%)^1} + \frac{CF_{2nd\ Yr\ Inflow}}{(1+12\%)^2} + \frac{CF_3}{(1+0.12)^3} + \frac{CF_4}{(1+0.12)^4} + \frac{26000}{(1+0.12)^5} \right\} - 70,000.$$

Finance and Accounts Notes

$$\Rightarrow NPV = [18750 + 16741.0714 + 14947.3852 + 13345.87965 + 14753.098] - 70,000$$

$$= 78537.43 - 70,000$$

$$\Rightarrow NPV = 8,537.43$$

Q2) With different interest rates for every year.

Given:-

Cash Outflow :- (12,000)

Cash Inflow	Rate	
4000	14%	Yr 1
5000	15%	Yr 2
7000	16%	Yr 3
6000	18%	Yr 4
5000	20%	Yr 5

Find NPV.

Sol^n

$$NPV = \left[\frac{CF_{1st}}{(1+0.14)} + \frac{CF_2}{(1+0.14)(1+0.15)} + \frac{CF_3}{(1+0.14)(1+0.15)(1+0.16)} + \frac{CF_4}{(1+0.14)(1+0.15)(1+0.16)(1+0.18)} + \frac{CF_5}{(1.14)(1.15)(1.16)(1.18)(1.20)} \right] - 12,000$$

Finance and Accounts Notes Akshansh

$$\Rightarrow NPV = \frac{4000}{1.14} + \frac{5000}{(1.14)(1.15)} + \frac{7000}{(1.14)(1.15)(1.16)} + \frac{6000}{(1.14)(1.15)(1.16)(1.18)} + \frac{5000}{(1.14)(1.15)(1.16)(1.18)(1.20)} - 12000$$

$$= 3508.77193 + 3813.882 + 4602.9616 + 3343.555 + 2321.913 - 12000$$

$$\Rightarrow NPV. = 5591.08353.$$

Ans

Note :- How it comes in exam?

Q: Story - - - - - - - - - - - - } just see the interest value from here.

Year	Project 1	Project 2
1	Value 1a	Value 1b
2	Value 2a	Value 2b.
⋮	⋮	⋮

See them and find similarly

Finance and Accounts Notes Akshansh

✡ IRR (Internal Rate of Return)

eg: Calculate IRR.

Year	Cash flows
0	(100,000)
1	30,000
2	30,000
3	40,000
4	45000

* If asked 14% to 18%, find for 14%, 15%, 16%, 17% and 18%

Rate of return, R = 15% to 16%.

Ans: For R = 15%,
IRR = (100,802)
For R = 16%.
IRR = (98,641)

Sol^n: Idea:- There are sequence of steps that need to be followed

Now,

Step 1) find NPV with R=15% initially.

$$NPV = \left[\frac{30000}{(1+0.15)^1} + \frac{30000}{(1+0.15)^2} + \frac{40000}{(1+0.15)^3} + \frac{45000}{(1+0.15)^4} \right]$$

$$+ (100,000)$$

$$= [26086.95 + 22684.31 + 26300.64 + 25728.89]$$

$$+ (100,000)$$

Finance and Accounts Notes Akshansh

Note: + (value) ≡ − Value
↳ outflow.

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⇒ $NPV\big|_{R=15\%}$ = 100800.79 − 100,000.

⇒ $NPV\big|_{R=15\%}$ = 800.79

[Similarly, find NPV for R = 16%.]

$NPV\big|_{R=16\%}$ = 1359

Step 2) Sum absolute values $|NPV_{15\%}| + |NPV_{16\%}|$

= 802 + 1359 = 2161

S3) Calculate ratio of NPV of smaller discount rate, identified in Step 1 to the sum obtained in step 2

⇒ $\frac{802}{2161} = 0.37$

S4) Add the no. obtained in S3 to the smaller discount rate

15 + 0.37 = 15.37 %

↳ Put in formula

↳ At this rate, NPV = 0!

Thus, IRR, calculated in this manner is very close approxim^{n} to true internal rate of return.

General Idea :-

If IRR > Cost of Capital : Accept Project

IRR < Cost of Capital : Reject Project

↳ will be given in Question

Finance and Accounts Notes by Akshansh

NON DISCOUNTING CRITERIA

Payback Period Method Accounting Rate of Return (ARR)

eg: Find ARR.

Given :-

Year	Book value of investment	Income
1	100.00	14.00
2	80.00	17.5
3	65.00	20.12
4	53.75	22.09
5	45.31	23.57

ARR = 28.31 %

$$ARR = \frac{\text{Avg of Income}}{\text{Avg of Investment}}$$

$$= \frac{\frac{14 + 17.5 + 20.12 + 22.09 + 23.57}{5}}{\frac{100 + 80 + 65 + 53.75 + 45.31}{5}}$$

$$\Rightarrow ARR = 28.31\ \%$$

Finance and Accounts Notes Akshansh

eg Find Payback Period

Yr	Investment
0	(100,000)
1	30,000
2	40,000
3	20000
4	25000
5	30,000

Idea: I Invested 100,000 initially. I want to see in how much time I will get my investment back.

Yr 1 (30000) + Yr 2 (40,000) + Yr 3 (20,000)
= 90,000

I need 10,000 more to cover my initial investment
So, mid of 4th year will give me 10,000.

So, Total Payback Period = $3 + \frac{10,000}{25000}$.

= 3.4 years. Ans

* Note:

Sales done on accounts ⇒ On credit

⇓

A/c receivable

↳ If we are not get cash back (or some %age)

⇓

Bad Debt

↳ Credit A/c receivable } when we close
Debit Bad Debt Expense } Balance sheet

end of Course

Finance and Accounts Notes Afghanistan

Merchandising activity { Material + Value addition → Selling

2-3 Marks → Mostly abbreviations

INDIAN FINANCIAL SYSTEM

§ 1. After 1947 : See details of Post Independence era.

- Around 1950s : Constitution comes
  RBI (Reserve Bank of India) comes

[Read : Diff. b/w cooperative bank, merchandising bank & investment bank]

- NEP (New Economic Policy) : Promotes private sector business, banks
  ↳ 3 types of banks : A, B, C.
  Run by govt. { Housing ; ICICI → Promoting Industrial sector
  Cooperative → Promoting Agricultural sector

[Read : Diff b/w current & saving account
current → no interest got
saving → gets interest]

- 1990s : Financial liberalization
  ↳ Concept of Universal Banking came
  (All types of services came in for every bank)
  (foreign banks could come)
- FERA (Foreign Exchange Regulation Act)
  ↳ Say of Central Bank
  ↳ SEBI comes (Stock Exchange Board of India)
  ↳ Herd Behavior : fall ⇒ sell shares by everyone herd

[Read : Diff b/w fiscal policy & monetary policy]

Finance and Accounts Notes