

THE ESSENTIALS | HOW TO READ FINANCIAL DOCUMENTS: ANNUAL REPORTS, BALANCE SHEETS & AUDIT REPORTS

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“Follow the money” is a common adage when it comes to investigative work. In this section we bring you a key document - the company annual report which contains all the financial statements of the company for one financial year. We then focus on one such document - the balance sheet. We also touch upon audit reports and external documents that are crucial to piecing together the money puzzle of a company.

Annual Report

An annual report is [a corporate document](#) disseminated to shareholders and it details out a company's financial condition and operations over the previous year. It contains information on financial statements, data on profit and loss, balance sheets and cash flow statements.


The report is [typically issued](#) to shareholders and other stakeholders so that they have the information they need to evaluate the firm's financial performance and to make investment decisions.

One will find all the information about the financial health of a company in these documents, from Balance sheets, to Profit and Loss statements.

“When I report on stories, the financial documents form a very strong base in terms of verifying the information that I have from other sources. The main documents that I look at are balance sheets and profit-and-loss accounts. These two documents give me a complete overview of how the money's flowing in and out of the company. Along with these there are auditors' reports, and cash flow statements, all of these combined give you a picture of the financial health of the company, as well as if there are any shady dealings or any kind of discrepancies in the transactions,” explains Sonal Matharu, senior journalist, *Confluence Media*.

How to access these documents:

- You can find the annual reports on the websites of companies.
- Look up the name of the company, go to their website.
- Since each website is different, the report could be found under a section for investors. However, this could vary by company.

 **Pro-tip:** *Since the reports are available in public domain, companies are mindful and may try to present them in ways to make them more marketing-friendly. So, be careful to read between the lines and with some scepticism (A reminder in case we have not stressed this part already.)*

However, while companies can try to present information with a marketing perspective, they cannot lie in these reports. These are considered to be official documents, and false information can be held against the companies.

In addition to financial statements, you can also find information on company composition and policies. For example, how many women sit on the company's board? Or what policies or measures does the company have in place for stakeholders who come from vulnerable and marginalised backgrounds? Do they have special training programmes for women, for people with disabilities? The Business Responsibility Reports which have a lot of valuable information are part of company annual reports. We explore the BRR in more detail [here](#).

Balance sheets

As mentioned above, annual reports contain a wealth of information about the financial performances of companies. They also contain balance sheets.

But first up, what is a balance sheet?

According to [Investopedia](#), a balance sheet is a financial statement that reports a company's assets, liabilities and shareholders' equity at a specific point in time, and provides a basis for computing rates of return and evaluating the company's capital structure.

Essentially, it provides a snapshot of what a company owns and owes, as well as the amount invested by shareholders.

How to read a balance sheet:

A typical balance sheet has two broad sections, assets and liabilities, and they both are equal to each other.

Assets = Liabilities

Assets: These are the resources that the company owns/controls. They have economic value. These include cash reserves, securities, inventory, and even fixed capital assets such as land and equipment.

Liabilities: Things that the company is liable for - what it owes to others. This could include the rent it owes, the bills, wages and even taxes it has to pay. The equity a company owes to its shareholders is also included in liabilities.

So, you can also write the formula as $\text{Assets} = \text{Liabilities} + \text{Equity}$.

Why is all this information important and how can you use it?

The balance sheet has a lot of information on a company's financial dealings - from what it owns to what it owes.

You can look at the situation of a company's liquidity, you can see its debts, you can also get a glimpse of how the situation changes over time. A balance sheet paints a picture of the company's finances at one point in time, so you can compare different time periods and map how different components have changed over time. And you can spot any sudden changes or anomalies and investigate them further.

In addition to the balance sheet, you should also look at the profit and loss (P&L) statements of the company.

P&L sheets provide information on revenue, expenses, depreciation, taxes etc. and give you a sense of whether a company is performing well or not. So, a company may have high revenues, but also high expenses, leading to low profits or even loss. While another may have lesser revenue but due to lower expenses, might be making profit.

"These sheets cannot be looked at in isolation," says journalist Sonal Matharu. While the balance sheet will give you a sense of the assets and liabilities, the P&L statements tell you about revenues and expenses. "That actually breaks down the whole system for you - it tells you where the money is coming from. Where is it going in the company?" Matharu adds.

And while these are documents prepared by companies, audit reports give an outsider perspective on company finance.


Audit Reports

Audit reports - typically independent and external - assess the company's financials to see if they are in line with the legal mandates and if there is any misrepresentation of the numbers. According to Investopedia, they are important

because banks and creditors require an audit of a company's financial statements before lending to them. In India, section 139 under Chapter X of the Companies Act 2013 mandates that “every company...appoint an individual or a firm as an auditor”.

Why should reporters know about audit reports?








While other financial reports such as the balance sheet, P&L statements are put together by the company, audits are done by independent auditors, who don't have vested interests in the company. So, these reports can flag any violations, misreporting, or even raise concerns about certain financial dealings. Audit reports can flag major violations and expose scams (see an example on the DHFL scam below), but sometimes, they can also point a reporter towards a possible scam.

 **Pro-tip:** *The trick lies in reading the fine print and reading between the lines.*

For example, while investigating a story on the Scania bus scam, Matharu observed a loan flagged in the audit report, one that the company could not explain to the auditor. Therefore, the auditor could not verify where that money had come from or for what it was being used.

Wrapping up, companies are required to put out information on their financial performance in the public domain. These are available in the annual reports. Companies are also required to get their finances audited. In between all these pages and tables, lie immense possibilities of research and reporting. While one sheet by itself will not necessarily lead to a story, if you spend enough time, and are able to read different documents together, it's only a matter of time when you'll run into something insightful. Get started now, we'd say.

Stories

-  The Golden Touch of Jay Amit Shah, Rohini Singh, [The Wire](#)
-  'No Link' to Scania Bus Said Gadkari, But Sons' Messages, Loan to Front Company Say Otherwise, Sonal Matharu, Joe Sperling, Hans Koberstein, [Confluence Media](#)
-  From 2014 to 2019: How the Adani Group funded its expansion, M. Rajshekar, [Scroll.in](#)
-  Forensic audit finds fraudulent transactions worth Rs 14,000 crore in DHFL, [Business Line](#)
-  Rs 7,926 crore loan fraud: Ex-TDP MP floats fake firms in name of maids, drivers, sweepers, [Times of India](#)
-  The big debts of Reliance Big: more thorns in Anil Ambani's bleeding crown, [Economic Times](#)
-  Profit and Gloss | Massive concealment of production and profits by the aluminium giants Hindalco and BALCO, Mahesh C Donia, [Caravan Magazine](#)

RESOURCES | INSPIRATIONS

- ◆ What is a balance sheet? | [Investopedia](#)
- ◆ Understanding Balance Sheet Statement | [Zerodha](#)

PEOPLE TO FOLLOW

- ◆ [M Rajshekhar](#)
- ◆ [Nitin Sethi](#)
- ◆ [Sonal Matharu](#)
- ◆ [N Sundaresha Subramanian](#)
- ◆ [Sucheta Dalal](#)
- ◆ [Morning Context](#)