

Studies on the Role of Financial Communication in Presenting the Financial Sustainability of a Company

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Abstract—In a world where digitalization and globalization are two very strong phenomena, the modernization of a common language used in the preparation, presentation and especially in the communication of the information provided by the annual financial statements acquires a primary role. The acute need for truthful financial communication of economic and business-specific information within the digital age is forcing the International Financial Reporting Standards to try to provide a richer portfolio of information on a company's intellectual assets and sustainability. Financial communication must be based on transparent and accurate information regarding the assets, financial situation, and stability of a company. Within the new business economy environment, which is a digital one, an efficient financial communication will ensure the performance architecture of any company. Organizations with substantial financial and material resources and rigorous financial management have an increased chance of survival and development. That is why financial sustainability must be seen in terms of financial autonomy. In this paper the authors tried to combine the theoretical elements with the practical ones necessary to diagnose financial sustainability and the way of efficient and correct communication of financial information, reputation and trust of the company. In the paper, the authors focused on the theoretical issues of financial communication by reviewing the literature and tried to achieve a crystallization of financial information necessary for economic analysis. Emphasis was placed on accurate financial information from the annual financial statements.

Keywords—financial communication, financial sustainability, economic information, digital economy

I. INTRODUCTION

The diversity of the problems related to the economic-financial activity of a company requires the need of an economic-financial diagnosis in the form of a study through

the prism of the cause-effect relationship, which would analyze and interpret the facts[1]. The purpose of any business is to maximize profit, but the factors that determine its evolution could easily be changed by the internal and external environment of the business. [1], [2], [3], [4],[5].

The role of financial communication is to increase the company's notoriety and credibility in order to attract potential investors [2], [6].

Financial communication is based on both transparency and credibility. On these grounds, we focused our work on the role of financial communication, and more specific on financial reporting and the ongoing concern for the image of the entity that has become an increasingly important element even for companies that have not yet granted due attention to this aspect. [7], [8] Financial communication does not only refer to financial data, but also has a specific role in building the company's image, reputation and trust. In this article we focused our attention on the theoretical issues of financial communication by reviewing the existing specialized literature and trying to condense and outline the financial information necessary for an economic analysis. [9], [10], [11], [12], [13], [14], [15]. We have mainly used primary data such as truthful financial information that comes from annual financial statements as it reflects the reality. The quality of financial reporting and especially financial communication requires that companies to voluntarily expand the volume and improve the quality of information they report, to ensure that all users of that information are fully informed in order to make investment decisions, loans, etc. [3], [16]. Taking into consideration the concerns of the IASB's international regulatory body about the updating accounting standards and also about the quality of existing IFRS standards, the process of financial reporting in accordance with IFRS should become more relevant and credible. In terms of financial sustainability,

it could be argued that it is shaped by a series of actions and advisory activities which seek more than an immediate profit and leave a legacy to future generations of a sustainable economic environment. Authors such as [17], [18], [19], [20], [21], consider that sustainability has three dimensions that are constantly interacting between themselves, namely environmental, social and economic sustainability. The financial sustainability of the company represents the power to make a profit in order to survive and benefit from the economic systems [20], [18], [22], [23].

II. METHODS

This paperwork combines theoretical research with empirical research, as the theoretical aspect is defining the conceptual features, and the empirical aspect aims to analyze the financial and non-financial elements presented by the winemaking company under study from Iasi County, Romania.

III. RESULTS

The necessary primary data were taken from the annual financial statements for the period 2017-2019 of a winemaking company from Iasi County. The financial communication was based on the information provided by the analysis of the liquidity indicators, solvency and management indicators (efficiency ratios) situations.

IV. DISCUSSION

Having a quick overview, in 2017 the current liquidity rate is good, showing a financial security (177.94%). In 2018 the current liquidity rate is better, demonstrating a good ability to pay short-term debts (244.82%) and at the end of 2019 the rate level is also good, showing a financial security (189%). (fig. 1).

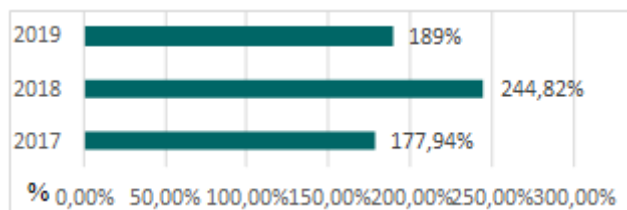


Fig. 1. Evolution of the current liquidity rate

In relation the Quick Liquidity Ratio, at the end of the 3 years we can say the following:

In 2017, the data seems good, showing financial security (122.8%) At the end of 2018 the data is very good, demonstrating a good capacity to pay short-term debts from the immediate liquidities of the company (207.67%). In 2019 the provided data is 117%, therefore this shows a good financial security. (fig. 2)

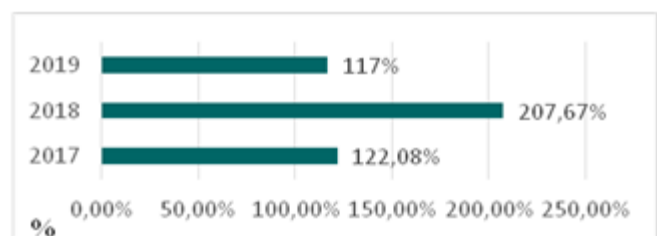


Fig. 2. The evolution of the immediate liquidity rate

Based on the global indebtedness rate, the share of debts in total liabilities was presented as such:

- 2017 RIG = 63.84% below standard, but in good parameters
- 2018 RIG = 60.20% below standard, but in good parameters
- 2019 RIG = 64.42% below standard, but in good parameters.

The company has an acceptable degree of indebtedness and it is able to pay its obligations (fig.3)

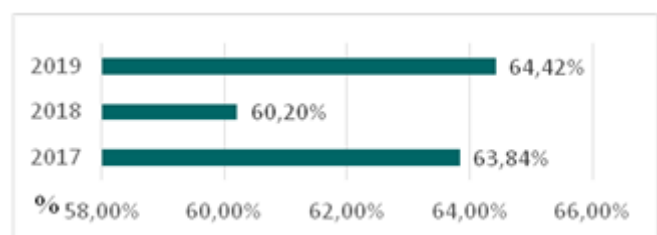


Fig. 3. Evolution of the global debt ratio

The equity borrowing rate, RICpr, must be below 8.5 or 85%, preferably below 5 or 50%. So the total debts represent a maximum of 50% of the own capital.

- 2017 RICpr = 179.71% - shows a high indebtedness compared to the company's equity.
- 2018 RICpr = 152.69% - shows a high indebtedness compared to the company's equity.
- 2019 RICpr = 181.98% - shows a high indebtedness compared to the company's equity. (fig. 4)

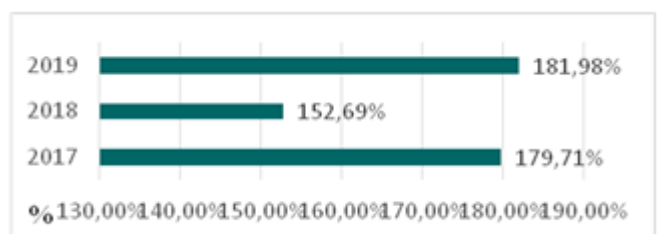


Fig. 4. Evolution of the equity borrowing rate

As for the solvency ratio, it must have a value below 0.3 or below 30%. During the analyses period, a weak level is registered for the whole period

- 2017 RS = 112.57% weak solvency ratio

- 2018 RS = 111.92% weak solvency ratio
- 2019 RS = 122.43% weak solvency ratio (fig. 5)

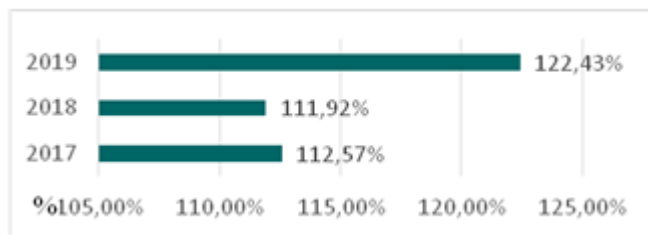


Fig. 5. Evolution of the solvency rate

Management indicators (Efficiency Ratios), show the efficiency of a company in managing resources and carrying out agricultural and non-agricultural activities. The following were analyzed: The turnover rate of total $VrCA / AT$ assets which shows how many times the total assets are rotated in turnover. The number of rotations must be increasing from one period to another to reflect the increase in the efficiency of the use of total assets in the production of turnover.

- 2017 $VrCA / AT = 2.32$ rotations
- 2018 $VrCA / AT = 1.97$ rotations
- 2019 $VrCA / AT = 1.29$ rotations

The number of rotations is decreasing, which reflects a degradation of the indicator. The decrease is largely due to the transfer of a part of the activity to a new company in the group. (fig. 6)

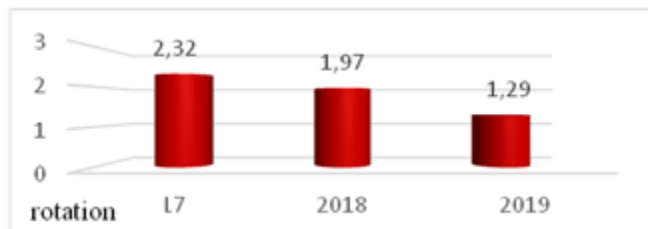


Fig. 6. Rotation speed of total assets

Rotation speed of current assets (the number of rotations must be increasing from one period to another to reflect the increase in the efficiency of the use of current assets in achieving turnover.

- 2017 $VrCA / AC = 5.47$ rotations
- 2018 $VrCA / AC = 5.01$ rotations
- 2019 $VrCA / AC = 3.23$ rotations

The turnover rate decreased, which indicates a worsening of the indicator from year to year. The decrease is largely due to the transfer of part of the activity to a new company in the group. (fig. 7)



Fig. 7. Rotation speed of current assets

Regarding the turnover rate of fixed assets in turnover, $VrCA / AI$, it is good that the number of rotations is increasing from one period to another to reflect the increase of an efficient use of fixed assets in the production of turnover.

- 2017 $VrCA / AI = 4.03$ rotations
- 2018 $VrCA / AI = 3.25$ rotations
- 2019 $VrCA / AI = 2.14$ rotations (fig. 8)



Fig. 8. Rotation speed of fixed assets

The number of rotations has a decreasing trend, which theoretically is not a good indicator. The evolution of this indicator was influenced by the following aspects:

- Transfer of a business line from this company to a group company
- New investments made between 2018 and 2019

Regarding the indicator duration in days of a rotation of stocks in turnover, $Dz St / CA$, we can say that stocks must be rotated as soon as possible, because their storage can lead to loss, degradation, theft, moral wear, and tear. We are looking for a reduction in the duration in days of a stock rotation from one period to another. During the analyzed period, the indicator is strongly influenced by the value of stocks at the end of the year. A more accurate calculation of the indicator would be done using a monthly arithmetic average of the value of stocks.

- 2017 $Dz St / CA = 20.9$ days (optimal duration).
- 2018 $Dz St / CA = 11.04$ days (optimal duration).
- 2019 $Dz St / CA = 42.64$ days (a month and a half, increasing). (fig. 9)

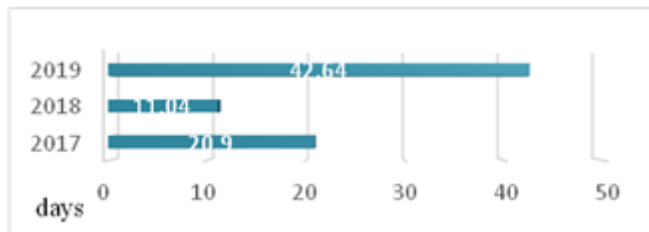


Fig. 9. Duration in days of a stock turnover (St) in turnover (CA)

For the indicator Duration in days of a turnover of current assets in turnover, $Dz AC / CA$, it must be followed that the current assets are rotated as soon as possible, thus trying to reduce the duration in days of a turnover from a period to period. (fig. 10)

- 2017 $Dz AC / CA = 66.67$ days (approximately 2 months, indicator with optimal value).
- 2018 $Dz AC / CA = 72.78$ days (approx. 2.5 months, optimal value).
- 2019 $Dz AC / CA = 112.67$ days (approx. 4 months, weaker). (fig. 10)

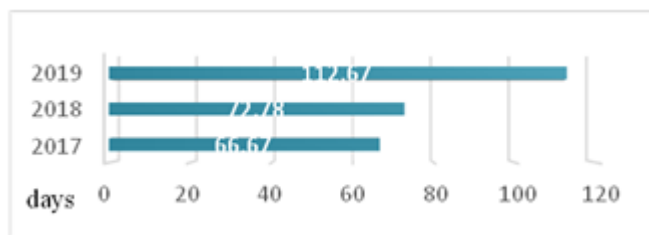


Fig. 10. Duration in days of a turnover of current assets (AC) in turnover (CA)

For the indicator Duration in days of a rotation of receivables in turnover $Dz Cr / CA$, it is necessary to follow the increase of the number of days of receivables collection showing the existence of uncertain, frivolous, insolvent or bad paying clients, the appearance of problems in the cash flow, which we need for the company to carry out its activity.

- 2017 $Dz Cr / CA = 44.41$ days (about 1.5 months - good).
- 2018 $Dz Cr / CA = 61.15$ days (about 2 months - good).
- 2019 $Dz Cr / CA = 69.55$ days (about 2.5 months - good). (fig.11)

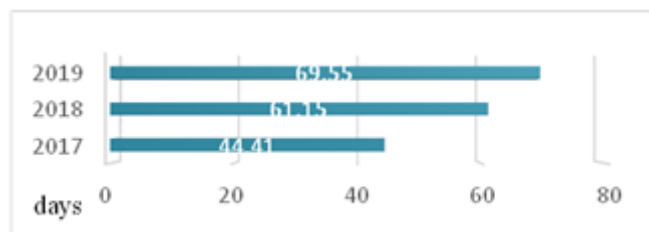


Fig. 11. Duration in days of a turnover of receivables (Cr) in turnover (CA)

The rate of return on working capital, $RrCperm$, shows the share of gross profit realized on the use of employed or permanent capital. The share of profit in working capital must increase from one period to another to denote the increase in profitability. The rate of return on capital employed fluctuates from one year to another depending on the gross result obtained. (fig. 12)

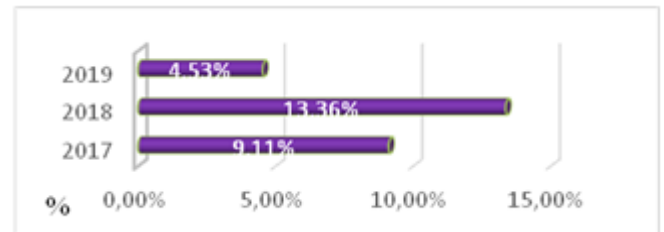


Fig. 12. Rate of return on employed capital

The rate of return on equity, $RrCpr$, (The rate of financial return) shows the share of net profit realized on the use of equity. The share of net profit in equity must increase from one period to another to denote increased profitability. The rate of return is fluctuating, but above the rate of inflation which denotes the profitability of the business (fig. 13)

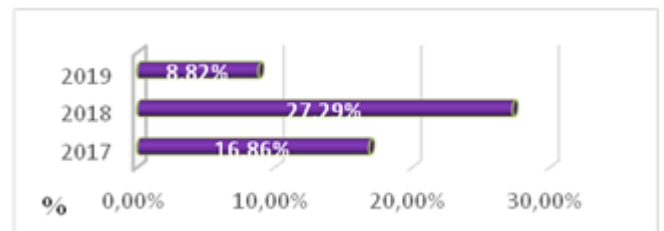


Fig. 13. Rate of return on equity

The gross sales margin, MBv , shows the ratio between the gross profit resulting from sales and the turnover. It must increase from one year to another in order to highlight the increase of profitability. Gross margin fluctuates depending on market conditions. The year 2018 was an exceptional one for the company, managing to sell the production at a very good price. (Fig 14)

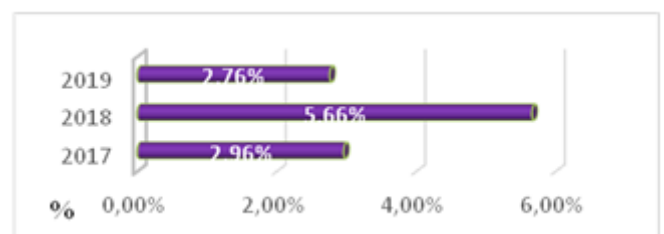


Fig. 14. Gross sales margin

The rate of economic profitability shows the ratio between gross porphyry and total assets or, in other words, the capacity of total assets to produce profit. It must increase from one period to another to reflect increased profitability. In the last two years, according to the evolution of this indicator, the profitability of the assets used decreased.

But, we must analyze this evolution in the context of the investment effort made by the company in 2018 and 2019. Given that such an investment is made over a period of about a year, the fruits of the new investment will be seen in the results of future years. (fig. 15)

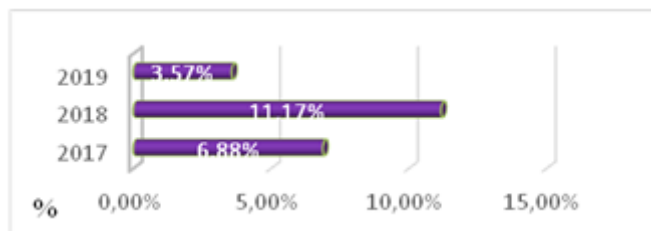


Fig. 15. Economic profitability rate

The rate of return on resources consumed, $RrCht$, shows the ratio between the net profit and the total expenses incurred. It must increase from one year to another to reflect the increase in the return on total expenses incurred. The rate of return is low in 2019. But, again, we must take into account the investment made in 2019. (Fig. 16)

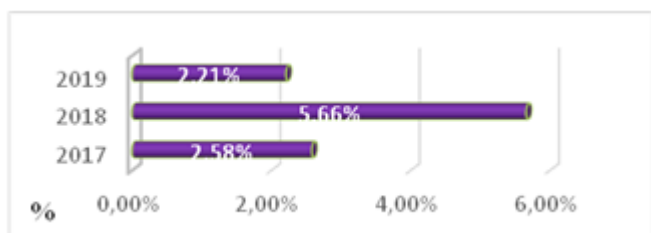


Fig. 16. Rate of return on resources consumed

V. CONCLUSIONS

The financial situation of the company under study is average, but with real possibilities for improvement. The economic indicators calculated in evolution are influenced by the following:

a. Market situation. For example, in 2018 the company had a favorable situation, managing to sell chickens raised at one of the slaughterhouses at a very good price.

b. The investment effort. In the second part of the years 2018 and 2019, the company invested in new patrimonial assets (led to the increase of fixed assets, but also to a decrease of the net profit related to 2019).

In the future, the unit manager should be more involved in the language of financial communication and look at the elements within each calculation formula of each creditworthiness indicator. In this way he will identify the directions of action on which he must intervene. For a true image of financial sustainability, the manager together with the team should act in the following directions:

- Optimizing the business by making the most of the available fixed assets.
- Increase in turnover:
- Increasing profitability by:

- Increased sales
- Better prices obtained from customers
- Reduction of operating expenses through negotiation with all suppliers
- Reduction of financial expenses by scheduled repayment of contracted bank loans.
- Reducing the volume of credit for working capital employed
- Improving solvency.

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