

## Quadrant II – Notes

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**Fundamental analysis - Industry Analysis** The investor should consider the industries that promise the most favourable opportunities in the near future. Industries vary in their growth rates and their overall contribution to the economy. Successful investors are those who analyse the economic significance of industries and invest in the industries that promise success.

### **Major characteristics in industrial analysis**

#### **1. Sales Trends and Earnings Performance:**

The historical sales records and earnings performance play a very crucial role for forecasting future trends. Even though the past performance may not be repeated in future, the analyst needs to know how the industry has behaved in the past. The analyst will be able to judge the stability of the performance in terms of sales and earnings as well as the growth rates.

## 2. Cost Structure:

Cost structure is a factor related to the sales and earnings. This factor studies the relationship between sales and fixed costs. Higher the fixed costs, higher will be the break-even point and higher will be the sales volume to be achieved. However, lower the fixed cost, a firm will easily achieve and surpass its break-even point.

## 3. Labour Conditions:

The industry whether it is labour intensive or Capital intensive has to use labour of different categories and expertise. An analyst should examine the possible reasons that may halt the production process and its fall out on the profit of the industry. If there are problems of labour such as strikes, the industry would be unwelcome for the investors.

4. Competitive Pressure: The analyst must consider the type of competitive pressure that an industry faces in the country. Profits are expected to be more in an industry which has less pressures of competition.

## 5. Demand for the Product:

Industries in which demand is high will have good prospects of profitability. The supplier would be able to sell the products at growing rate. Along with domestic demand, there should be export demand for the product also.

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## 4. Future Prospects:

After a study of the past and present, the future prospects of the industry are to be assessed. Firms have to be assessed in terms of its strategies to meet the challenges as they emerge and its future prospects should be assessed before an investment is made.

**Fundamental Analysis – Company Analysis** The investor should identify the promising companies in the industry. In company analysis, all the factors affecting the earnings and growth of the company are considered. The important financial and non-financial indicators are as follows -

### **Financial Indicators**

Financial indicators provide a good source of information to evaluate the success of the company.

#### **1. Income statement –**

This includes earnings from regular operations. The company earns on a regular basis. The regular and stable earnings should be taken into consideration. The expenses should be reflected in the same year as revenues to which they are related.

#### **2. The balance sheet –**

The balance sheet is a statement indicating the financial position of the company on a given date. It shows the assets and liabilities of the company.

#### **3. Statement of changes in financial position –**

The statement of changes in financial position of a firm from beginning and end of an accounting year should be taken into consideration. This statement gives an idea of the changes in working capital of the firm.

It gives the sources of finance and takes into consideration the income.

It helps the investor to analyse the company's ability to generate cash flows in the future, pay dividends etc.

**Non financial indicators** In addition to the financial parameters, the investor has to analyse some non financial indicators also. Some important non financial indicators as explained as follows:

#### **1. Business of the Company:**

The investor should know whether the company is a well established one. The industry or industries in which the company is operating should have good growth prospects. The future outlook of the company and prospects of the industry are interlinked.

**2. Management:** The management should be efficient and experienced. They should have honesty, integrity and vision for expansion and growth. The

competence and commitment of the management, shapes the future of the company.

3. Market share of the Company:

The market share of the company should be substantial. The larger the share, the better the prospects of controlling the market this leads to high profits.

4. Product Range:

Progressive companies create competition for their existing products by launching new products. Investors must examine whether the company launches new products frequently.

5. Research and Development: Progressive companies spend substantial sums of money on Research and Development to upgrade their existing products, introduce new products etc. such companies have bright future prospects