ROLE OF FINANCIAL STATEMENT AS A TOOLS FOR EFFECTIVE BUSINESS DECISION MAKING

(A CASE STUDY OF UNION BANK PLC, ILORIN)

BY

BOLAKALE AMINA

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BEING A RESEARCH PROJECT SUBMITTED TO DEPARTMENT OF ACCOUNTANCY, INSTITUTE OF FINANCE AND MANAGEMENT STUDIES, KWARA STATE POLYTECHNIC, ILORIN.

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CERTIFICATION

This is to certify that this research work conducted byBOLAKALE AMINA with matric number HND/23/ACC/FT/541 has been read and approved as meeting the requirements of the Department of Accountancy, Institute of Finance and management Studies, Kwara State Polytechnic, Ilorin for the award of Higher National Diploma (HND).

______________________	______________________
MR. AZEEZ, Y.O.	**DATE**
(***PROJECT SUPERVISOR***)	
______________________	______________________
MRS. ADEGBOYE B.B	**DATE**
(***PROJECT COORDINATOR***)	
______________________	______________________
MR. ELELU M.O	**DATE**
(***HEAD OF DEPARTMENT***)	
______________________	______________________
MR. IKHU MOMREGBE SUNDAY (FCA)	**DATE**
(***EXTERNAL EXAMINER***)	

DEDICATION

This research work is dedicated to Almighty Allah, for making it possible for me from the inception to the completion of this program, the Author and Finisher, the Alpha and Omega, the most merciful.

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All praise, honour, glory and adoration goes to almighty Allah. The omnipotence and omniscience for his guidance and everlasting protection through the duration of my programs (ND & HND) in accountancy.

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CHAPTER ONE

INTRODUCTION

1.1 BACKGROUND OF STUDY

A financial statement refers to a summary explaining or providing a picture of the financial position/business performance (Atrill & Mclaney 2015) and or activities of a business during a certain period. Generally accepted accounting principles (GAAP) require a company to prepare a full set of financial statements that conform to regulatory guidelines and should be accurate. A full set of financial reports include statements of retained earnings, cash flows and the statement of a financial position (balance sheet). A good financial statement should document information such that it is easy to read and understandable. Presenting a financial statement clearly and professionally helps companies interpret results and thus plan for a more profitable future. Growth in a business refers to a company expanding its business using its own resources and assets. This growth also depends on the financial statement of the organization.

Similarly, a financial statement is a summarized report (Benedict & Elliott 2011) that indicates a cooperation's operating data during a period or its economic standing at a giving period. Financial statement preparations in a company are usually done by internal accountants, who are directly influenced by the management of the company. Companies make certain decisions based on information from financial statem ents. Thus, a fraudulent or an erroneous financial statement implies a risk possibility which can cause wrong investment decisions making in an organization.

Financial statements of companies are prepared either using generally accepted accounting principles (GAAP), defined by the law on accounting and the law on financial statements, or using international financial reporting standards (IFRS) and international accounting standards (IAS), issued by the international accounting standards board. These standards are not enforceable together; therefore, companies choose one of them for reporting purposes. Investment decisions can be explained as the determination made by directors or management body as to when and how much capital can be spent on investment opportunities. The decision often follows research on financial statements.

1.2 STATEMENT OF THE RESEARCH PROBLEM

It is observed that the role of financial statements as a tools for effective business organization in decision making in Nigeria has some problems to both customers and managers of business organizations who are either not aware of the importance of interdependence relationship that exist between customers and business organizations.

As a current situation in the society of Nigeria, customer's decisions in the Union Bank of Nigeria have been very slow due to the negligence on the use of financial state ment and other important financial records. Most organizations are still ignorant of the benefits of financial statement, thereby limiting their knowledge about their fina ncial position and above all their ability to use financial statements to make import ant investment decisions. For this reason, it was very important for the researcher to carry out a proper study and research on this issue, to point out the alarming si gnal on the role of financial statement as a tool for effective business decision mak ing in banking industry. Incidentally, bookkeeping as a practice is a necessary point er of strength and weakness in a business entity, however, the level of business man agement expertise and financial reporting skills necessary for sound decision maki ng has been way below the conventional standards expected.

Also, most Banking Industry complying with the bookkeeping principles have fallen short of living up to the laid down standards, but to satisfy the mandatory and statu tory requirement. Subsequently, this has further raised the urgency to provide techni cal support and management training needs, to the operators in this sector to cope with the ever-growing demand for new and existing players in the industry because of competition, creativity and innovation. Financial statements hold the potential of unraveling the future of Banking Industry as an integral driver of economic growth a nd development in economies.

1.3 RESEARCH QUESTIONS

To attain the objectives of this study, the researcher had the main research question;

i. To what degree does financial statement help managers make investment decisions in an organization?

ii.To what degree is financial statement analysis important or necessary in every organization?

iii. What are the various tools used for the presentation of the financial statements.

iv. To what extent does financial statement minimize business failures and facilitate achieving corporate objectives.

1.4 OBJECTIVES OF STUDY

On noting that most investments made by firms end in failure, it is the overall objective of this study to determine how firms can use financial statement analysis and interpretation to aid management decisions. Specifically, the study is designed to:

i. Find out the degree to which financial statement help managers make investment decisions in an organization?

ii. Find out the degree to which financial statement analysis is important or necessary in every organization?

iii. Investigate various tools used for the presentation of the financial statements.

iv. Find out the extent to which financial statement minimize business failures and facilitate achieving corporate objectives.

1.5 RESEARCH HYPOTHESIS

To aid the achievement of the desired objectives aforementioned, the following hypot heses are formulated:

H_0: Represents Null hypothesis

H_1: Represents Alternative hypothesis

Research hypothesis 1

H_0: There is no significant relationship between financial statement analysis and inter pretation and management decision making in an organization

H_1: There is significant relationship between financial statement analysis and interpre tation and management decision making in an organization

Research hypothesis 2

H_0: There is no significant relationship between a firm's profitability and financial stat ement analysis and interpretation.

H_1: There is a significant relationship between a firm's profitability and financial state ment analysis and integration.

1.6 SCOPE OF THE STUDY

The study is conducted to cover selected firms both in Ilorin but Union bank Plc, Ilorin was taken as a case study.

However, this study is conducted to cover the use of financial statement which includ es; (Balance sheet, income statement, statement of cash flow and statement of retain ed earnings) of the organization

1.7 LIMITATIONS OF THE STUDY

The research work has some limitations due to some problems encountered from the sources of collecting useful materials also some unforeseen circumstances which posted as a threat during preparation of this research project includes:

i. **Time:** A research of this kind would require enough time to cover many areas of activity effectively, but since the researcher is a student with other classroom works to do, the time allocated for the study was limited.
ii. **Finance:** During the course of this research, another stumbling block. Judgment financial resources were encountered. The researcher has to make due with little financial provision available to achieve a qualitative and acceptable research finding.
iii. **Transportation:** The source of collecting useful material or information is far and the transport logistics expensive, in some cases, the journey was fruitless if the staff was not available.

1.8 SIGNIFICANCE OF THE STUDY

This study will be useful to all financial statement of bank as this research will enable the current and prospective user of financial statement, both external and internal users be acquainted with the knowledge of analytical tools in making decision.

Serve as relevant guide for future researchers in the area of the users of financial statements. Help to supplement the existing knowledge of users of financial ratios as a guide towards determine the banks achievement as well as to show how financial ratio analysis can identify this strength and weakness of the bank both a day and in the future.

Enable the intending investors who are not well raised in accounting to be able to appreciate how to critically evaluate financial statement or organization of interest to them before making investment decision

1.9 DEFINITION OF KEY TERMS

i. **Ratios:** A ratio is the relationship between two amounts that results from dividing one by the other. It is an accounting term used to describe the financial index which compares two financial variables such as current assets and current liabilities. Examples of ratios are quick ratio, and test etc.

ii. **Accounting Ratios:** "they are the relationship between figures expressed as ratios"

iii. **Investment Decisions:** This relates to allocation of capital and involves decisions to commit funds to long term assets, which will yield benefits in future.

iv. **Ratio Analysis:** It is an analytical tool designed to identify significant relationships between two financial statement amounts.

v. **Security:** Security is a financial asset which earns a fixed and/or variable periodic income till terminal maturity period if any.

CHAPTER TWO

LITERATURE REVIEW

2.1 INTRODUCTION

This chapter considers basic concepts outlined in the study, a review of theoretical literature which gives us an understanding of the basis of the study, and finally links literature to current study by considering what authors have written with the conclusions arrived at as far as this study in concerned.

Investment decision enables corporate leadership to analyze various investment opportunities and to show how departments should make good commercial bets. This chapter therefore seeks to show the views relating to the role of financial statements as a tools for effective business decision making in an organization. A business financial health is reported in three financial statements.

The balance sheet, which shows a record of the business assets and liabilities at a point in time. The income statement or the profit and loss statement shows a record of its income and expenses for a given period. The cash flow statement describes the effect of its operations on the cash balances. Each of this required to make informed business investment decisions.

1.2CONCEPTUAL FRAMEWORK

Damodaran (2013) points out that, when evaluating a company's profitability and potential return in investment, there are several questions that the financial statement when used in conjunction with one another answers. Thus, the amount of debt the b usiness has or can take, the operating cash the business has, and the value of its products and investment can all be found in the balance sheet, income statement, and cash flow. However to some extent, since managers are shareholders or owners of organization, the preparation of financial statements is very important for investment decisions.

2.2.1 Financial statements

To make well-informed decisions, a company's management gleans data from various sources amongst which are financial statements. Financial statements therefore are a formal record of the financial activities of a business, person or other entity. Another name for financial statements is also known as financial report. Information on this report is presented in a structured manner and in a form easy to under- stand. Given the importance of financial statement in investment decisions, a lot of strategy goes into how a company must present its financial data and use such information to win economic competition. Most often the goal of financial statements is to steer the minds of the senior officers to combine their business acumen to find the best ways to drive the company towards profitability. Financial statement has specific effects on investment decisions.

1.1.2 Types of Financial Statements

There are basically 4 main types of financial statements. They include:

Balance sheet

While the income statement is essential to understanding the business, it doesn't contain all the information needed for a thorough analysis. The balance sheet provides the readers with data concerning the business debt loads and the value of assets such as real estate. While a business's revenue might be very healthy and increasing, if its burdened with too much debt, or many outstanding invoices that its clients haven't paid, they may not be clear on the income statement. It will be apparent on the balance sheet, however. Alternatively, a business with significant real estate or other assets that aren't monetized on the income statement will appear here; for example, if the business owns its own building, land, or plant, these values will be listed in the balance sheet. Thus, the balance sheet comprises of:

Assets: Refer to the thing owned by the business

Liabilities: Something the business owes it owners and represent the amount of capital that remains in the business after the asset are sold to pay its outstanding invoices. Thus, the difference between assets and liability equals equity. That is:

Assets – liability = equity

Income statements

The income statement tells the reader how much money the company made from and spent over a certain period, usually a month, quarter or a year. Subtracting the total expense from total revenue reveals the business's margin. Higher margins are better because it means the business can spend less and keep a greater percentage of r evenue as profit. It is best to analyze income statement from several consecutive years because it reveals what direction the business is heading to. As such with income statement often asked:

- Are margins growing smaller or larger?
- Is revenue growing along with the expenses or are only expenses growing while the revenues remain flat?

All these questions are answered by reading the income statements.

Cash flow statements

Another piece of the puzzle when evaluating a business's worth is the cash statement. This statement shows the flow of cash in and out of the business account. Actual deposits and payment activity of account payable, payroll, revenue is reflected here. A business that's running low on cash but has adequate income and asset to fund operation may have an account receivable problem or may need to re- finance debts. On the other, a company statement that show too much cash may indicate that the business is not putting enough resources back into its operations. As a result, using the cash flow statement and performing calculation on operating, investment and financing activities. This hence brings us to what operating, investing and financing activities are;

Operating activities: It represents the cash flow from short term operating and primary activities of a business that is its current assets and current liabilities. This secti on evaluates net income and loses of a business. By assessing sales and business expenditure, all income from non-cash items is adjusted to incorporate inflows and out flows of cash transactions determine a net figure.

Investing activities: Represents cash flow from the purchase and sale of goods, this section reports inflow from purchase and sales of long-term business investment such as property, assets, equipment, and securities. Increase in investment indicates a cash outflow (use of fund) and decrease in investment signals a cash inflow.

Financing activities: Represents cash flow generated or spend on raising share capital and debt together with the payment of interest and dividends. It also accounts for all money that is related to financing your business. For example, if you received a loan from your organization, the loan itself will be considered as an inflow of cash. Loan repayment will be considered as an out flow of cash and both will be recorded in this part of the cash flow analysis statement making cash flow projections and computing cash flow statement can be confusion if you have never managed these types of finances before.

1.1.3 Statement of Retained Earnings or Equity

Finally, the last main financial statement is the statement of retained earnings also known as the equity statement. It shows the movement in owners' equity over a period which is mostly determined from the company's share capital issued; net profit and loss as reported for the year. Most organizations will use the first two financial st atements to make investment decisions. Thus, it is only from reviewing the financial statement that can they perform a reasonable investment decision.

1.1.4 Use and Users of Financial Statement

Yuh (2013) points out, the main group users of financial statement include investor s, employees, customers, government and public. What then are the needs of this gr oup and how would they use these financial statements? They include the followin g:

Investor group: This group comprises of both existing and potential shareholders. T hey would consider either investing or disinvesting in the business. Equity investors consider two elements to their investment, gain and income: income in the form of dividends and gain in the form of share prices.

Employees: It is encouraging to note that some companies produce a separate emp loyee report. Employees and their representatives require information on business p erformance for two principal reasons:

- For wage and salary negotiation
- Assessment of current and forward opportunities in terms of employment.

They would be interested in both the current financial stability of the busines s in terms of cash flow and the organizations ability to meet its short-term liabilitie s.

Customers: This group is interested in the business short and long term financial st ability and its potential to supply quality goods and services. They may also have in terest in the environmental policy of the business.

Governments: The government department uses financial statement for the purpos es of taxation, which is the company's taxation and VAT. The government therefore are decision makers and their forward economic plan is influenced by the performa nce of all businesses within the various sectors in the econ omy.

Public: Most often, public is been referred to "shareholders" and business that do no t exist solely in isolation. Businesses are part of society at large and as such genera te much public interest.

At local and national levels factor such as employment and environment are often ke y interest.

1.1.5 Qualification on the Usefulness of Financial Statements

Although financial statements provide information useful to decision makers, there i s much relevant information that they omit. Factors of the market demand, technolo gical developments and price of raw materials, subsidies, competitors' actions, wars and nature can be a dramatic effect on a company's prospects in a firm investment decision making.

2.2.6 Features of a Good Management Decision Technique

According to Mabt (2001), investment decisions concern allocation of funds to appro priately select investment opportunities to maximize profit as well as sustain the orga nization as a gong concern. According to him, investment decision techniques involve sequential stages of opportunity assessment. The stages are as follows:

i. The review of a firms operating objectives and goals as well as the identification of possible constraints, which can inhibit goal achievement; this can be found in the director's report and the financial statements in the company's annual report or in the form 10-k from Security and Exchange Commission (SEC).
ii. Identification of various investment opportunities which are likely to enhance corporate goal achievement.
iii. Estimation of the amount of financial outlay required for each investments opportunity, timing of cash flow requirement and determination of the level of risk associated with each investment opportunity.
iv. Franking of all investment opportunities assessed in terms of the levels of contribution to goal achievement.
v. Selection of investment opportunity of opportunities that best enhance the achievement of operational objectives and
vi. Regularly assessing the detection to identity possible weaknesses in order to adopt corrective measures.

Generally, information from the financial statements can enable the efficiency of the above technique, hence, the great need for financial statement analysis in investment decisions.