Financial statements and financial performance analysis: Implementation in an Indonesian MSME-based aesthetic beauty clinic

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ABSTRACT: The aim of this study is to make financial statements and conduct financial performance analysis of one of the micro, small, and medium enterprises (MSMEs) in Indonesia, namely, Luxe Dental and Aesthetic Center, which is engaged in the aesthetic beauty clinic industry. This study was conducted by using gap analysis and Pareto analysis. The results show that the financial statements consisted of income statement, balance sheet, and cash flow statement. Financial performance analysis was performed using common-size financial statements and profitability ratios. Creating financial statements and conducting financial performance analysis are useful to map and describe the condition of an MSME financial performance and to increase its ability to evaluate its performance against competitors.

1 INTRODUCTION

Micro, small, and medium enterprises (MSMEs) around the globe significantly contribute to the economy. They contribute to around 90% of the businesses around the world and are responsible for 60%–70% of employment and up to 50% of the gross domestic product (GDP) of the countries (United Nations Year 2018 about MSMEs). However, in running their business, many MSMEs often face obstacles in terms of financial management. This brings up some constraints associated with the development of MSME financial strategies, such as difficulty in raising capital (Auken & Lema, 2003).

Financial arrangements need to be made so that the company can survive, avoid bankruptcy, compete with other companies, maximize sales, minimize costs, maximize profits, and maintain a steady increase in income. One of the things that need to be done to make it easier to manage finances is to make financial statements (Ross et al. 2013). The ease of making financial statements is important for MSMEs (Halabi et al. 2010).

Moreover, a company needs to analyze its financial performance to assess its current performance and compare it with that of other companies to help it find best practices to improve its performance (Weygandt et al. 2012). The purpose of financial performance analysis is to evaluate the financial performance of the company by studying the relationship between operational decisions and financial performance (Higgins, 2016).

One of the micro, small, medium enterprises (MSMEs) in Indonesia, namely, Luxe Dental and Aesthetic Center, which is engaged in the aesthetic beauty clinic industry, faced problems regarding creating financial statements and conducting financial performance analysis. With the availability of the financial statements and by conducting financial performance analysis, it can clearly understand its financial performance and find best practices to support its growth.

2 LITERATURE REVIEW

The purpose of financial statements is to provide information on the financial position and financial performance of an entity, and they help a large number of users make economic decisions, particularly those who are not in a position to request specific financial reports to obtain the information needed. Financial statements also show the accountability of the management for the resources entrusted to it (Weygandt et al. 2012).

The balance sheet is a report that captures the position of the assets, liabilities, and equity of a company for a specific time period (Higgins, 2016). The income statement is a report that contains a summary of the income and expenses of a company (Ross et al. 2013). The cash flow statement is a statement that provides information about the cash position that results from cash inflows and cash outflows, which are usually grouped into operating, investing, and financing activities for a certain period (Ross et al. 2013).

The purpose of financial performance analysis is to evaluate the financial performance of the company by studying the relationship between the company's operational decisions and its financial performance (Higgins, 2016). In this study, there are two tools performed, namely, common-size analysis and financial ratio analysis.

The common-size analysis is used to describe each account in the financial statements using a percentage as the basis value. This standardized financial statement describes the accounts in the statement of financial position as a percentage of assets and describes the accounts in the income statement as a percentage of sales (Higgins, 2016). The advantage of the common-size analysis is that it allows a company to compare its performance with other companies of different sizes. The results of this financial statement analysis are called common-size financial statements, consisting of common-size balance sheet and common-size income statement.

Financial ratio analysis is done by comparing a company's financial ratios, which are calculated based on the financial figures reported by the company. Financial ratios are calculated to obtain comparable results for different companies and over time, regardless of size. The financial ratio analysis used in this study was profitability ratios. Profitability ratios measure the income or operating success of a company for a given period of time (Eklund et al. 2003).

Profitability ratios used in this study are profit margin, return on assets (ROA), and return on equity (ROE). Profit margin is obtained by dividing sales by net income. This ratio is particularly important to calculate because it reflects the company's pricing strategy and its ability to control operating costs. ROA is obtained by dividing net income by total assets. ROA is a basic measure of the efficiency with which a company allocates and manages its resources. ROE is obtained by dividing net income by total equity (Higgins, 2016).

3 RESEARCH METHODS

This study is a descriptive and qualitative study and was conducted through a business coaching method. The data were obtained using both primary and secondary data from MSME business process including marketing, finance, operation and human resources from 2018 to 2019. The data were acquired from interviews, observations, and desk research.

The data were analyzed through gap analysis and Pareto analysis. Gap analysis was conducted to compare the level of mismatch between ideal conditions and actual conditions by using analysis tools such as Business Modal Canvas (BMC), PESTEL, five forces model of competition, service marketing mix, segmenting, targeting, and positioning (STP), SWOT, and TOWS.

Pareto analysis is a priority scale carried out based on the level of urgency and significance of its impact on problems in an MSME.

The threshold for the accumulated problems is 80%. The result of Pareto analysis shows that creating financial statements and conducting financial performance analysis are the most significant and most feasible for an MSME to carry out under current conditions. Upon this result, it is agreed

that the implementations to be executed are as follows: (1) creating financial statements and (2) conducting financial performance analysis.

4 RESULTS AND DISCUSSIONS

The MSME's financial statements taken from the MSME financial data from 2018 to 2019 are given. The income statement consisted of sales, operating expenses, and tax expenses. The balance sheet consisted of cash, prepaid rent, equipment, and accumulated depreciation in the assets side and equity and retained earnings in liabilities and equity. The cash flow statement consisted of sales, operating expenses, and tax expenses in operating activities, purchase of equipment and payment of rent in investing activities, and issuance of equity in financing activities.

The following is the result of the comparative common-size financial statements. The result of the common-size income statement shows that the MSME had an increase in financial performance, as indicated by an increase in the net income from 2018 to 2019 by 11.2%. Meanwhile, its competitor had a decrease in financial performance, as indicated by a decrease in the net income from 2018 to 2019 by 0.3%. This shows that the operational efficiency of the MSME had increased compared to its competitor from 2018 to 2019.

The result of the comparative profitability ratio is as follows. The result shows that the MSME had a better financial performance compared to its competitor with an increase in profit margin from 2018 to 2019, greater by 10.9%. This shows that the operational performance of the MSME was increasing from 2018 to 2019, greater than its competitor. Return on assets (ROA) and return on equity (ROE) from 2018 to 2019 were greater by 10.4% compared to its competitor. Increase in the company's ROA shows that there was an increase of 12.7% in the efficiency of using its assets to generate profits, which was greater than its competitor. Increase in ROE shows that the MSME was generating greater return on investment (by 1.7%) from 2018 to 2019 from the equity invested by the owner than its competitor.

The results of this study confirm the benefits of financial statements to reduce information asymmetry of financial information provided by MSMEs. It is believed that creating financial statements will increase MSMEs' access to funding through harmonious and quality financial information (Parera & Chand, 2015).

The results also show that financial ratio analysis is important. This shows whether a company is on the path of improvement. An increase in a company's profitability ratio indicates a better financial performance. A high profit margin means that the company has the ability to absorb cost increases without passing it on to consumers at an increased price. Return on assets (ROA) measures the success of a company in converting its assets into profit. Return on equity (ROE) measures the success of a company in generating returns on investment that has been issued by shareholders (Mahajana & Sarkar, 2017).

Financial performance comparisons are used to map information from economic events to financial statements and thus capture similarities in how two firms explain similar transactions (De Franco et al., 2011). Comparability has the potential to expand company information because companies often rely on information from financial reports when formulating their own strategies. Comparability is believed to enhance the characteristics of financial information that differ from other qualitative characteristics, such as representativeness, relevance, and timeliness.

5 CONCLUSIONS

This study was conducted to create financial statements and to perform financial performance analysis for Luxe Dental & Aesthetic Center. This is used as a basis for the company to assess its financial performance and to compare it with its competitors. The study was conducted through a business coaching method. The data obtained were analyzed with gap analysis and Pareto analysis. The implementation was done by doing common-size analysis for balance sheet, income statement,

and profitability ratio analysis, consisting of profit margin, return on assets (ROA), and return on equity (ROE). The results of this study indicate that creating financial statements and conducting financial performance analysis are useful to describe the condition of the MSME's financial performance and can increase its ability to evaluate its performance against its competitor.

The scope of this study, which was carried out through the business coaching method, is limited to the field of financial management of the service company. The results reported herein suggest the need for more analyses and comparable financial information. Finally, this study provides a baseline for additional research. For example, future studies may examine how to evaluate the result of financial performance analysis for future investment in competitive markets.

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