

# Financials, decoded: Fundamentals of financial statement analysis

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One of the most important tasks for a credit professional is assessing a customer's creditworthiness. They need to figure out who their customer is and if they'll be able to fulfill their financial obligations. An essential part of the credit investigation is reviewing a customer's financials in a process called financial statement analysis.

**Why it matters:** Financial statement analysis turns numbers into knowledge, helping credit professionals protect their organizations from unnecessary risk while enabling business growth through well-managed credit. For those new to the process or just looking to strengthen their credit assessments, we've curated a list of essential knowledge and skills needed to effectively analyze financial statements.

**But first, what is financial statement analysis?** The answer will depend on who you ask. "What first comes to mind when hearing financial statement analysis is ratios, but it's so much more than that," said Franziska Thalmann, [CCE](#), specialist, credit management at SABIC (Houston, TX). "For me, it's putting the pieces together to tell a story. You start to recognize the different elements at play and how they interact to create an outcome."

By definition, financial statement analysis is the process of reviewing and analyzing the financial statements of a company in order to make a decision about its financial health and creditworthiness. To conduct a comprehensive financial statement analysis, credit professionals should be knowledgeable about the following:

- **Accuracy and competency of financial statements.** Be able to read and understand financial statements. What makes up a financial statement varies country by country, but generally, it's composed of the balance sheet, income statement (or profit and loss statement) and the statement of cash flow, also known as source and use of cash statement.
- **Ratio analysis.** This provides insights concerning the financial position and how well the business is performing. "You can determine a business's creditworthiness through key financial ratios—profitability, leverage, coverage and liquidity," said Chad Sivertson, credit analyst II at nVent Management Company (Anoka, MN).
- **Cash flow.** The source and use of the company's cash flow, the movement of money in and out of a business. It's a key indicator of a company's liquidity, or its ability to meet short-term obligations like paying suppliers, employees and debts.
- **Trend analysis.** Gain insight and interpret a company's financial performance over a specific historical period. "Ratios and trends year over year can help you predict the company's ability to service debt requirements, achieve growth objectives, satisfy customer needs and provide return to shareholders," said Erin Stammer, [CCE](#), vice president of credit at PNW Railcars, Inc. (Portland, OR).

- **Capital expenditures (CapEx).** Funds that a company uses to acquire, upgrade or maintain physical assets such as property, buildings, equipment or technology. It reflects a company's long-term investment strategy and growth potential.
- **External and internal conditions.** What has or could affect the financial soundness of a customer such as a merger and acquisition (M&A) or macroeconomic issue.
- **Obtaining financial statements.** Be able to obtain financials from the customer, credit agencies, lenders and public records.

"A financial statement is an essential tool to understand credit risk," said Ginny Overbeck, [CCE](#), director of financial services at William M. Bird & Co., Inc. (North Charleston, SC). "Customers may refuse to provide financials, saying that their payment history should speak for itself. I've learned from experience that analyzing their financial statement would've foretold the outcome."

### Key skills for effective financial statement analysis

To analyze financial statements effectively, credit professionals need a few core skills:

- *Analytical skills:* the ability to assess financial statements and understand the market context they operate in.
- *Attention to detail:* avoid overlooking critical information that could impact decisions.
- *Effective communication:* clearly present findings and recommendations to stakeholders at all levels.
- *Problem-solving mindset:* because the goal isn't just to say "no," but to find workable solutions that still protect the company from risk.

Accounting standards bring consistency and clarity to financial statements. They are a common set of rules that guide accounting practices and enhance transparency through required disclosures. Credit professionals can stay ahead by referencing the two main standards: the International Financial Reporting Standards (IFRS), used in over 110 countries, and the Generally Accepted Accounting Principles (GAAP), primarily used in the United States.

**The bottom line:** Financial statement analysis isn't just a task—it's a core component of what makes credit management valuable. "We provide judgment, risk coverage and communication and explain the "why" behind every decision, and that elevates the profession," Sivertson said. "My advice for credit professionals is to continue to sharpen their skills by reviewing financial statements of publicly traded companies and continuing to educate themselves through NACM and the [Credit and Financial Development Division](#) (CFDD) to stay ahead and thrive in their field."

*All the credit managers in this article are graduates of NACM's hybrid program, [Graduate School of Credit & Financial Management](#) (GSCFM), which covers four essential business and professional growth disciplines, including Advanced Financial Statement Analysis. Through the program, students gain a comprehensive view of each subject and real-world knowledge from peers to apply in their day-to-day job. Take control of your learning and register for the Spring GSCFM course by May 2. Click [here](#) for more information.*