A 360 DEGREE LOOK ON THE CONCEPT OF FINANCIAL PERFORMANCE

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Abstract

In the economic literature, several meanings can be found on performance, the subject being amply developed. In a general sense, the performance is associated with its positive result or associated to the success in a field; also, the performance can be seen as an action that leads to success. Performance can be regarded as a place of excellence being the result of a continuous effort, achieved in the competitive framework, commensurate through different methods. Performance always comes as a result of a comparison, based either an internal variable or an external one. From many angles of approach to the concept of performance, this paper focuses on issues of financial performance, addressing elements related to defining and measuring the performance and the study of various factors that influence it.

Keywords: *Financial performance, Profitability, Rates of Return*

JEL classification: *G10,G30, G32*

1. Introduction

Performance is neither the first, nor the last concept, that does not benefit from a unanimous opinion regarding its definition. Approaches of this concept are complex, vast, sometimes complementary, and sometimes contradictory and especially, the subject to a dynamic and temporal evolution of semantics.

1.1 Semantic explanation of the concept of performance

During the interwar period, in the Romanian Language Dictionary (Scriban, 1939), the performance represents *"the state of perfection of running*

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a horse, or another animal, or the functioning of a car". At the same time, the dictionary indicates the Latin origin of the term "per-training" and its meaning: *"to form everything"*. Although the origin of the term is Latin, its meaning comes from the English language: "to perform" and "performance" and from French: “performance”. Some essential attributes of the concept must be noted: the classification in the category of excellence and perfection, and the evolutionary character, determined by cultivation, functioning or running. Therefore, the performance is not a spontaneous state; it is obtained after an effort made over time and has a dynamic character. Latter, the explanatory dictionary of the Romanian language added a new dimension attached to the concept of performance: that of competition. Performance is not an isolated attribute, specific to an entity; it appears in a competitive context aiming excellence. Nowadays, when defining performance, a quantitative dimension is added, leading us to specific indicators of measuring it.

Concluding, performance can be considered a position of excellence that results from a continuous effort, realized in a competitive framework, which can be measured by various methods.

1.2 Economic approach to the concept of performance

The performance concept was also defined in the specialized literature, in the economic field.

During the period 1950-1980, when defining performance, in economic theory are frequently associated concepts as: maximization, organizational efficiency, efficiency, productivity, and effort. The criteria for its appreciation refer to productivity, flexibility, adaptability, capacity, sensitivity, achievement, growth, survival, environmental control, turnover, production costs, productivity, profitability, employee satisfaction, initiative, cooperation, communication, creativity, adaptability, staff stability, growth, profit margin, profitability of shares, activity rate, and solvency. As a practical tendency (Jianu, 2007), it seems to be easier to measure and evaluate the performance based on certain criteria, than to provide a unitary definition of the concept.

Over the years 1890-1890, performance is defined in economic literature according to the level of achieved objectives (Jianu, 2007), thus subject to the procedure and the level of establishing them, which determines the relative nature of the concept.

The period 1995 - 2000 addresses the performance in terms of efficiency and efficiency of the economic entity, and later, the value creation approach. Approaching performance in relation to productivity and efficiency (Nicolescu, 2005) prints a highly subjective character, being perceived differently, depending on the specific interest of each business partners: shareholders, employees, creditors, suppliers, state.

The modern approach of performance, developed after 1995, introduces the idea of creating value, as a defining attribute of performance. Performance is viewed from the perspective of all the actors involved in the life of a company, evolving towards the concept of sustainable development, where performance combines the holistic effect of increasing financial performance, environmental protection and social development, leading to the concept of total performance.

Thus, the performance represents the capacity of the company to ensure a sufficient remuneration of the interest holders, based on its ability to allocate and use optimally the limited resources, while ensuring an adequate sustainable development.

This temporal approach to the evolution of the performance concept has a relative character, sometimes encountering a translation from one period to another.

1.3 Financial performance

The concept of "financial performance", when not considered axiomatic or subjected exclusively to measurements, does not have a single definition.

The equivalence relation between performance, profitability and return, approached from a financial perspective, is questioned.

Profitability is the fundamental condition for ensuring the economic success of a business entity (Balteș, 2010), measured based on the positive result of the difference between the financial involved effects and efforts. The profit is often used as a measure of performance, or as a baseline for the same category indicators, such as Return on Investment, or Return on Equity. In absolute size, the net profit is a representation of what was obtained in addition to the expenses. When a company registered losses, there is a violation of the principle of profitability and economic growth (Bistriceanu, 2001). Thus, we can consider that there is a direct relationship between financial performance and profitability.

Financial performance (Feleaga, 2002) is defined by accounting according to the specific objectives of each information users, and shouldn't be sought exclusively in the profit and loss account. In the same context, I. Stancu considers that financial performance, identified by the profit and loss account, is overwrought (Stancu, 2007).

B. Colasse associates the notion of profitability with that of profit, as an ability of an enterprise to express a result in monetary terms.

V. Robu (Vâlceanu, 2005) approaches the performance of the company based on return, considered one of the most synthetic forms of expressing the efficiency of the economic-financial activity of a company. For measuring the return, the profit is indicated, as an absolute size of the profitability, and the Rates of Return, in order to appreciate the degree in which the used capital brings profit.

Ratability is seen as the potential of a company to create added value, the product obtained based on account of resources worth more than the sum of the consumed resources (Petcu, 2009).

Quoted by Iulia Jianu, M.Ristea appreciates performance in terms of efficiency, economics and efficiency. Called "*the equation of the three E's*", the performance is obtained by combining them, and is real, if maintained over the long term (Jianu, 2007).

Therefore, it is relevant to approach the financial performance from the perspective of all categories of persons interested in the good progress of the activity of an economic entity: shareholders, managers, creditors, customers, suppliers, potential investors, employees and other third parties (Balteș;Vasiu, 2015).

2. Approaching financial performance from different perspectives

2.1 Approaching financial performance based on the Profit and Loss Account

The Profit and Loss Account represents a component of the annual financial statements. It includes the patrimonial flows that allow the creation of wealth, starting from the total expenses and incomes. On its bases, can be computed the Intermediate Management Balances (IMB) (Ciuhureanu , 2017), which represents a cascade of financial indicators, by which management has the possibility of assessing financial performance: Profit margin, Production of the Financial Year, Value Added, Gross Operating Surplus, The Operating Result, Gross Profit, The Net Result. Offering a first clue in assessing financial performance, the indicators calculated based on the income statement, called synthetically results, are used in further the calculation of other indicators.

This financial indicator represents classic performance indicators, known, accepted and understood by most of financial information users. Explaining the way the net result was obtained at different stages, they allow a rapid assessment of the level of performance during the financial year.

On the other hand, the results can be influenced by the depreciation and stock valuation policy, the way of carrying out the inventory and by the age of owned assets. Also, they don't allow comparisons between economic entities of different sizes, which operate in different fields.

2.2 Financial performance analysis based on rates of return

Financial rates of return are mostly used indicators in performance tests. Performed analyses aim the dynamic evolution of Rates of Return and the identification of the factors which influenced the variation of values of indicators. This kind of analysis brings additional usefulness for financial information consumers, offering the possibility to make comparisons in time and space, or with internal or external standard values, accepted or elaborated by specialized bodies. It also allows the comparison of the entities that obtained the same results, but with different efforts.

There is a great variety of rates, generally determined as a ratio between the economic and financial obtained effects and the efforts made to achieve them (Vintila, 1997).

The classification of the Rates of Return varies from author to author, being possible to determine a large variety of indicators (Niculescu, 2005). The main categories of rates, computed at national and international levels are (Halpern, 1998):

- Liquidity Rates, which measures the company's ability to meet its short-term payment obligations
- Debt Management Rates, which measures the company's ability to meet its long-term payment obligations
- Rates on Asset Management, which measures the efficiency of the assets utilization
- Profitability Rates, which shows the holistic effect of liquidity, asset management and credit on operating results
- Growth Rates

- Market Value Rates, reflecting the joint influence of financial risk, profitability and return rates

The main rates used in financial performance analysis are Commercial rate, Return on Consumed Resources, Return on Total Assets and Return on Equity.

Even if these rates represents classic performance indicators, unanimously accepted by all financial-accounting information users, who know the general calculation model, the existence of a large number of calculating models for each rate may confuse the user in selecting the most relevant method. Their informational content is limited to historical results and makes no sense in the case of losses recording. Moreover, the calculation method can lead to false positive results. For example, reporting a loss to a negative own capital may generate a positive Return on Equity. As a result, professional reasoning is required to be applied in order to avoid a pure mathematical result (Vasiu; Baltes, 2015).

2.3 Appreciation of financial performance from creditor's perspective

It is a quick method of assessing the way the economic entity ability to deal with outstanding debts. The main rates are Liquidity Indicators (Current rate, Quick rate, Cash rate); Solvency Indicators (Equity Solvency Rate, General Solvency Rate); Indicators of appreciation of the Degree of Indebtedness (Rate of Global Indebtedness, Financial leverage, Rate of Financial Autonomy). They may indicate the occurrence of future problems and even the incidence of insolvency. The high values of the indicators do not necessarily indicate a high financial performance. This situation may occur in the case of debts accumulation or when an increase in stocks value is registered.

2.4 Assessing the financial performance of the capital market

For companies listed and traded, financial performance analysis from the perspective of classical indicators must be accompanied by performance analysis in terms of indicators specific to the capital market to capture the external perception of third parties, adding the market perspective to the internal performance indicators.

The main indicators are (Hurduzeu, 2009): Stock Market Indicators (Earnings per Share - EPS; Dividend per Share; Sales per Share (SPS); Dividend distribution rate) and Stock Rates (Stock Market Capitalization

Coefficient (Price-Earnings Ratio); Price to Earnings Ratio - PER Price per Book Value; Price to Sales Ratio- PSR; Price to Cash-flow; Dividend Yield-Divy; Net Profit Yield (EPS Yield, Earnings Yield).

Even if these indicators can provide valuable insights for buying or selling shares, understanding them requires specialized knowledge which isn't available to all financial information users. Must be considered that the indicators calculated on the basis of the stock exchange rate are related to the chosen time for the rate, and furthermore, the exchange rate may be affected by speculative actions.

2.5 Assessing the financial performance from the perspective of shareholders

The pressure of the financial markets forces the company to pay back its own capital, the shareholders being no longer satisfied only with the remuneration through a residual income, which sometimes has an uncertain character.

The value creation for the enterprise occurs when the company obtains a Return Rate on the Invested Assets that excess of the cost of the resources mobilized to finance them (Petrescu, 2008). Equity remuneration must be made at an attractive rate for investors, higher than the one offered by lower risk investments. Compared to other investment opportunities, this avoids capital outflows to more "tempting" entities and justifies risk taken (Petcu, 2009).

The value creation is, in the case of the listed company, the major criterion by which the shareholders evaluate the performances, starting from the strategic objective of maximizing the present and future profits. The main used indicators are: Economic Value Added (EVA) Market Value Added (MVA), Cash Value Added (CVA), Total Shareholder Return (TSR), Return on Investment (ROI).

Even if this modern indicator, based on value creation, modifies the traditional optics of approach to performance through net accounting profit, they are difficult to be used, requiring specialized and complex knowledge for calculation and interpretation.

3.Conclusions

Given the advantages, disadvantages, limits and opportunities of approaching financial performance from various angles, it is recommended to use a set of indicators, from each category, according to the specific activity of the economic entity. These indicators shouldn't be affected by financial-accounting techniques in order to reflect a true image of financial performance. Approaching financial performance from a profit perspective should be coupled with the analysis of entity's ability to generate cash flow. Further, it should be validated by analysis of liquidity, solvency and indebtedness.

Even if the financial performance indicators have satisfactory values, beyond the recommended limits, dynamic analysis is imperative. Made on sufficient time horizons, it helps to identify trends in the evolution of the company's activity and provides a basis for predictions.

But the performance does not have only quantitative valences. The financial performance can also be appreciated from the perspective of the value created by the company, granting to a quantitative dimension a qualitative one, promoting the sustainable development of the company, by creating value and not by consuming the existing one, even if the performance indicators have satisfactory values.

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