Our blog articles cover the P&L and the balance sheet individually. This e-book puts all three core statements side by side, explains how they connect to each other, and adds a chapter on the ratios worth tracking that neither blog article gets into.

Chapter 1: The Three Statements and How They Connect

The profit and loss statement, balance sheet, and cash flow statement are often reviewed separately, but they are really three views of the same underlying business. Net income from the P&L flows into retained earnings on the balance sheet. Depreciation on the P&L reduces the value of fixed assets on the balance sheet. Every cash movement on the cash flow statement eventually shows up as the cash balance on the balance sheet.

Reading all three together, rather than picking a favourite, is what turns financial statements from a compliance requirement into an actual decision-making tool.

Chapter 2: Reading Your P&L Like an Investor Would

An investor reviewing a P&L is not just checking whether the business made money. They are looking at the trend in gross margin over several periods, whether operating expenses are scaling sensibly with revenue, and whether profit is coming from the core business or from one-off items that will not repeat.

- Is gross margin stable, improving, or quietly eroding over the last six to twelve months?
- Are operating expenses growing in a way that matches revenue growth, or outpacing it?
- How much of net profit, if any, came from something outside normal operations?

Chapter 3: Reading Your Balance Sheet Like a Lender Would

A lender cares less about how much profit you made last month and more about whether you can cover your obligations if revenue slows down. That means close attention to the current ratio, the proportion of assets tied up in inventory or receivables versus cash, and how much of the business is funded by debt versus owner equity.

- Current ratio: current assets divided by current liabilities, generally healthier well above 1.0
- Debt-to-equity ratio: total liabilities divided by total equity, a measure of how leveraged the business is
- Quality of assets: how much of total assets are cash versus receivables or inventory that still needs to convert

Chapter 4: The Cash Flow Statement, the Reality Check

If the P&L and balance sheet tell you what the business earned and what it owns, the cash flow statement tells you whether any of that actually showed up as usable cash. A business can report a profitable P&L and a healthy-looking balance sheet while its operating cash flow is negative, usually because growth is tying up cash in receivables or inventory faster than it is generating it.

Operating cash flow is the number to watch most closely. Consistently negative operating cash flow, even alongside reported profit, is one of the clearer early warning signs available in a set of financial statements.

Chapter 5: Ten Ratios Worth Tracking Every Month

None of these require complex modelling. A simple spreadsheet updated monthly, alongside your financial statements, is enough.

- **Gross margin.** Gross profit divided by revenue. Shows the underlying profitability of what you sell before overhead.
- **Net margin.** Net profit divided by revenue. Shows what actually reaches the bottom line.
- **Current ratio.** Current assets divided by current liabilities. A quick check on short-term solvency.
- **Quick ratio.** Cash and receivables (excluding inventory) divided by current liabilities. A stricter version of the current ratio.
- **Days Sales Outstanding.** Average number of days it takes to collect a receivable. Rising DSO signals slowing collections.
- **Days Payable Outstanding.** Average number of days it takes to pay a vendor. Useful for understanding your own cash cycle.
- **Debt-to-equity ratio.** Total liabilities divided by total equity. A measure of leverage.
- **Operating cash flow margin.** Operating cash flow divided by revenue. Shows how much of revenue actually converts to usable cash.
- **Revenue growth rate.** Period-over-period change in revenue. Best read alongside margin trends, not alone.
- **Burn rate and runway.** Monthly net cash outflow, and how many months of cash on hand that outflow supports.

None of this is useful without financial statements you can actually trust, which starts with books that are reconciled and accurate every month. Collar Assist delivers all three statements monthly, on schedule, with senior professional review before they reach you. A free assessment is a good place to start if your current statements raise more questions than they answer.