

FINANCIAL STATEMENTS: A TOOLS TO EVALUATE BUSINESS PERFORMANCE

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Abstract

Introduction: The study's main objective is to assess a company's performance by looking at its financial statements. Financial statements provide information on profitability, stability, and liquidity.

Literature Review: Financial statements involve “cash flow statements, balance sheets, and income statements”. It is possible to pinpoint areas for improvement in cash management, revenue development, and spending control by analysing trends in these statements.

Methodology: The research has selected the “primary quantitative research method” through the survey process. The analysis of the data has been performed through SPSS software. The distribution of respondents by age, gender, and level of education is displayed by demographic data. Significant relationships between variables can be found through correlation analysis.

Findings: The results show how crucial financial statements are for evaluating a company's performance. They give stakeholders a thorough understanding of a company's financial situation, enabling them to make wise decisions.

Discussion: The study emphasises how important financial statements are for assessing a business's success, assisting in data-driven decision-making, and promoting long-term expansion.

Conclusion: The study emphasises how crucial it is to use caution when guaranteeing the accuracy of financial data to preserve confidence and dependability in financial statement analysis.

Keywords: *Financial statements, Business performance, financial analysis, Performance indicators, Data manipulation*

Introduction

Financial statements are the performance indicators of a company that also helps to measure financial performance. The income statement shows the earnings for a given period as well as the company's expenses and profit or loss. This aids in evaluating the profitability and operational effectiveness of the company. A organisation's “assets, liabilities, and shareholders' equity” are shown in a balance sheet, which gives an overview of the business's financial situation and liquidity (Mosteanu & Faccia, 2020). Therefore, the cash flow statement also aids in determining the capacity of the business to manage working capital, create cash, and pay its debts.

It is possible to identify areas that may require improvement, such as expense control, revenue development, or cash management, by analysing trends in these statements over time. As illustrated by Ichsan et al. (2021), the analysis of financial statements is an essential instrument for assessing the past and present performance of a company, facilitating decision-

making, and serving as a foundation for projecting its future financial stability. A firm's long-term viability and growth can be ensured by stakeholders making well-informed decisions about lending, investment, and strategic planning based on an evaluation of the financial statements of the organization. However, the possibility of data manipulation or misrepresentation is a problem when examining financial accounts since it might mislead stakeholders and skew the evaluation of a company's performance. As illustrated by Devi et al. (2020), inaccurate performance evaluations brought about by manipulated financial data influence investment choices. Therefore, independent audits, regulatory supervision, and more openness through standardized reporting can all aid in ensuring the dependability and correctness of financial statements to address this problem.

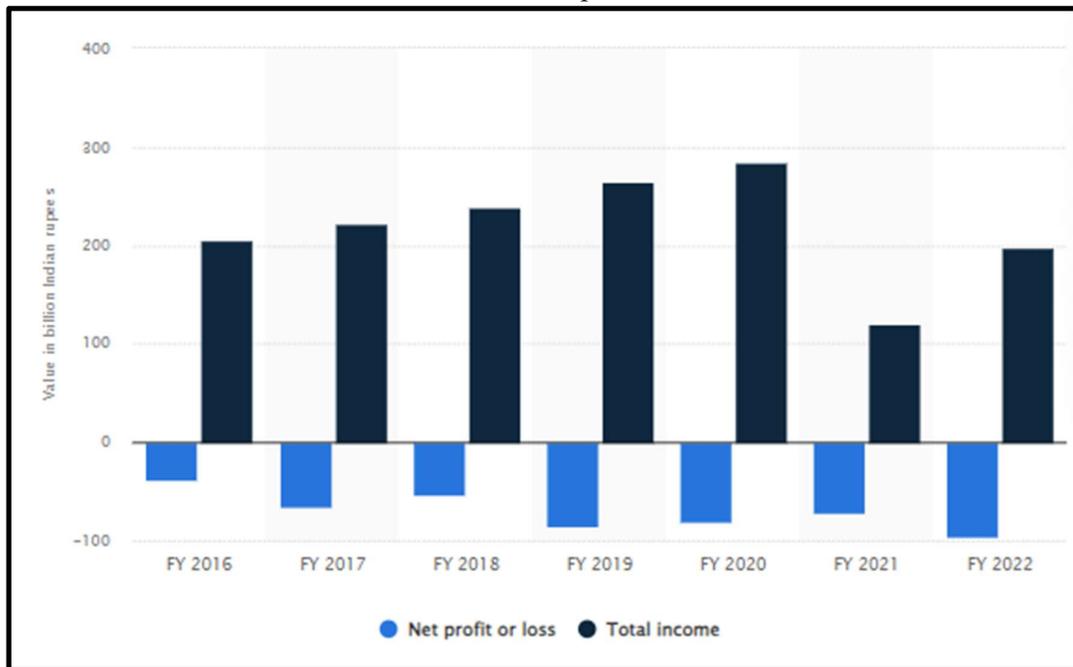


Figure 1: Business performance of Air India Limited from the year of 2016 to 2022
(Source: Statista, 2023)

Figure 1 illustrates the financial performance of Air India Limited from the year of 2016 to 2022. The “balance sheet, income statement, and statement of cash flows” are examples of financial statements that are crucial instruments for assessing overall financial performance (Ratmono, Darsono & Cahyonowati, 2020). Quantifiable measurements known as financial performance indicators are used to evaluate the success and well-being of a corporation.

Aim

The study's goal is to illustrate how financial statements can be used to evaluate a company's success.

Research Objectives

RO1: To comprehend how financial statements affect the functioning of businesses

RO2: To analyse past financial data to spot performance patterns that allow for the forecasting of future financial results

RQ3: To determine the components of financial statements that improves stability

RO4: To ascertain financial ratios and measures to appraise profitability and liquidity to appraise the financial well-being of the enterprise

Research Questions

RQ1: How do financial statements evaluate the performance of a company?

RQ2: How can performance trends that allow for the prediction of future financial outcomes are found using historical financial data?

RQ3: What aspects of the financial statements have impacted the stability of the financial system?

RQ4: How do financial ratios and metrics for assessing profitability relate to liquidity for evaluating the financial health of the company?

Hypothesis

H(1): There is a correlation between Return on Equity and business performance.

H(2): There is a relationship between liquidity and the business performance of an organization.

H(3): There is a general relation between net margin and organizational business performance.

H(4): There is a relationship between cash flow and the business performance of an organization.

Literature Review

Role of financial statements in measuring business performance

Financial statements offer a thorough and organised summary of a company's financial operations, which makes them essential tools for evaluating performance. As suggested by Gartenberg, Prat & Serafeim (2019), financial statements such as the “cash flow statement, income statement, and balance sheet” are essential instruments for evaluating the strength, effectiveness, and general performance of an organization. An important source of information about a company's profitability is the income statement. It shows the income received and the costs incurred over a given time frame, eventually indicating whether the company is profitable or losing money. Contrastingly, as argued by Kliestik et al. (2020), stakeholders also evaluate the company's capacity to turn a profit from its main business, measure its cost control, and spot long-term trends in profitability by examining financial statements. Therefore, a steadily rising profit is an indication of a successful company, but falling or negative earnings point to problems that need to be addressed, including better cost management, pricing, or operational efficiency.

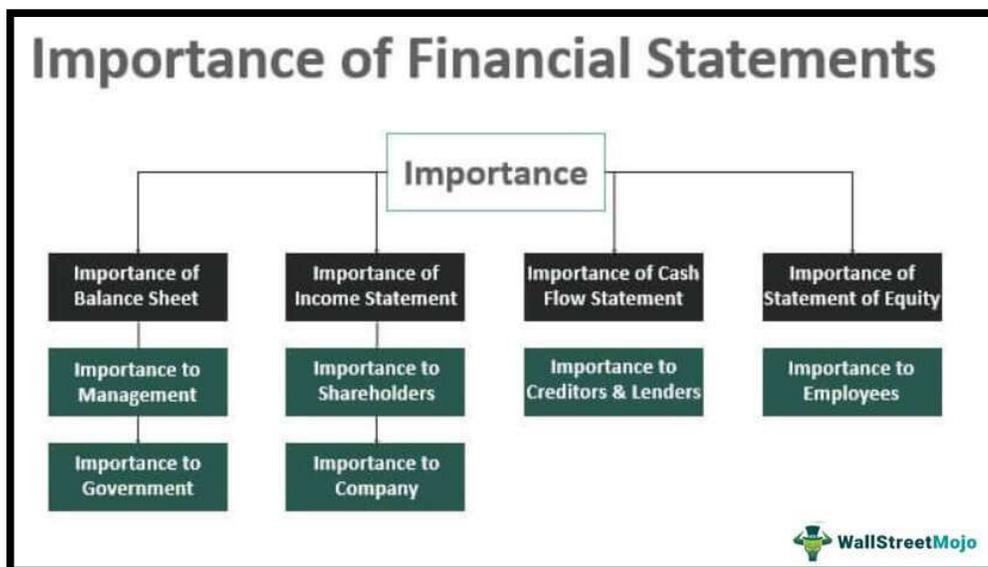


Figure 2: Financial statements in assessing business performance

(Source: Influenced by Tien et al. 2020)

An instantaneous view of a company's financial situation is provided by the balance sheet. As illustrated by Tien et al. (2020), a balanced sheet displays the assets, liabilities, and equity held by shareholders of a corporation. This data is essential for evaluating the company's solvency and financial stability. Sufficient assets and controlled debt on a robust balance sheet demonstrate sound financial standing and the capacity to fulfil both immediate and long-term commitments. Conversely, a high debt-to-equity ratio or insufficient liquidity may indicate financial risk and could make it more difficult for the business to grow or weather downturns in the economy.

Financial statements are essential tools for evaluating the success of businesses. As described by Alabdullah & Ahmed (2020), financial statements help stakeholders assess a company's profitability, financial stability, and liquidity by offering an organized, numerical depiction of its financial activities. Businesses, investors, and creditors all make well-informed decisions, evaluate risk, and establish creditworthiness by examining these statements. Therefore, financial statements are a crucial instrument in the continual evaluation of a company's performance and potential for sustainable long-term growth.

Identification of the factors of financial statements in enhancing financial stability

Improving financial stability is a top priority, and financial statements are essential to reaching this goal for organizations. As mentioned by Le, Chuc & Taghizadeh-Hesary (2019), a company's financial stability is greatly impacted by a number of the elements listed in financial statements. Additionally, an essential document that lists a company's earnings and outlays is the income statement. In contrast to that, as contradicted by Shad et al. (2019), strong profitability and steady sales growth are signs of sound financial standing. Companies are better able to pay debt, cover operating expenses, and reinvest in their operations when their revenues are rising and their profit margins are strong. Therefore, to evaluate a company's long-term financial stability, trends in revenue and profitability need to be identified, which is done by analysing the income statement.

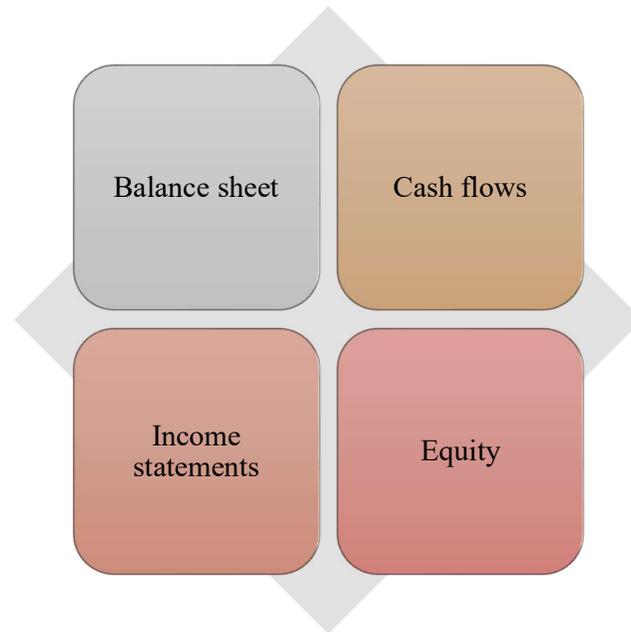


Figure 3: Factors of financial statements

(Source: Influenced by Shad et al. 2019)

The balance sheet offers information on the working capital and liquidity of a business. Short-term financial stability depends on having enough liquidity, which is indicated by a strong current ratio (Kliestik et al. 2020). Good working capital management guarantees that a business can pay its bills on time every day. A business that has enough cash and liquid assets is better able to handle unforeseen financial difficulties without having to take on more debt or sell assets at a loss. On the contrary, as argued by Ozili (2021), the company's debt levels are also shown on the balance sheet. Because high-interest rates can make cash flow difficult, having too much debt might undermine financial stability. Therefore, a better financial situation is indicated by a reduced debt-to-equity ratio and a comfortable interest coverage ratio. Effective debt management and the ability to pay off debt are prerequisites for businesses to stay solvent even in recessionary times.

Improving financial stability requires addressing the elements included in financial statements, such as revenue growth and profitability, liquidity and working capital management, debt levels and debt servicing capacity (Alsayegh, Abdul Rahman & Homayoun, 2020). These variables not only show a company's present financial situation but also provide information on how resilient it is to future downturns and maintain long-term stability. Therefore, businesses looking to improve their financial stability and make plans for long-term growth regularly evaluate these variables through financial statement analysis.

Methodology

The researchers in this study adopt the primary quantitative approach for data collecting, which focuses on obtaining numerical information to create a solid and impartial basis for the investigation. This study is a good fit for the primary quantitative technique since it seeks to reduce subjectivity and bias in the data collection. Here, positivism is the research approach used, emphasising the gathering of current, trustworthy data. As suggested by Flick (2020), positivism philosophy is helpful for quantitative research to prove the hypothesis.

Additionally, with this method, the researchers collected data on the study in real-time, which is very useful when it comes to financial statements that are used to evaluate business performance.

The research has been performed by following a descriptive research design. As illustrated by Kothari (2017), descriptive research design is useful to explain a whole population. The study also followed a deductive research approach to filter the data. A sample of 55 participants has been selected for the survey. The researchers developed a questionnaire with ten survey questions to gather data. These questions, which include three questions about demographics and seven questions about specific subjects, make it possible to get information from a wide range of respondents. In addition to being valuable, the data gathered using the primary quantitative approach also meets the study needs by being dependable, standardizable, and generalizable (Kumar, 2018). Therefore, it helps to guarantee that the data collected is correct and useful for deriving insights into financial statements' impacts in assessing financial performance, maintaining authenticity is essential.

Several statistical tests have been used in the study to gather and examine data. As per the view of Mazhar et al. (2021), the statistical analysis is performed using the “Statistical Package for the Social Sciences (SPSS) software”, which helps the researchers interpret the data they have gathered. Numerous statistical tests, such as tests relevant to variables and demographics, were employed in this research. Therefore, a comprehensive analysis of the data was made possible by these tests, which include descriptive statistics, linear analysis, ANOVA testing, coefficient tests, and correlation tests.

Hypothesis testing is important to this study to better understand how financial statements can assess business performance. As illustrated by Saunders & Bezzina (2015), to inform data-driven conclusions and scientific discoveries, hypothesis testing is essential to research since it impartially assesses the significance of links or effects. The researchers also determined the usefulness and relevance of these financial statements in the context of business performance measurement by formulating hypotheses and putting them to the test with real-time data. Moreover, the research study employs a rigorous technique for data collecting and analysis, integrating statistical tests, hypothesis testing, and quantitative data collection to investigate the financial statements aspects in the context of financial performance evaluation of organizations.

Findings and analysis

Demographic analysis

Gender

		gender			
		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Male	28	50.9	50.9	50.9
	Female	24	43.6	43.6	94.5
	Prefer not to say	3	5.5	5.5	100.0
	Total	55	100.0	100.0	

Table 1: Gender of the respondents

(Source: SPSS)

Gender-specific demographic data are shown in Table 1, wherein 24 female and 28 male individuals were involved in the data collection process. Furthermore, nine responders declined to reveal their gender. This data sheds light on how the statistical analysis's participants were distributed.

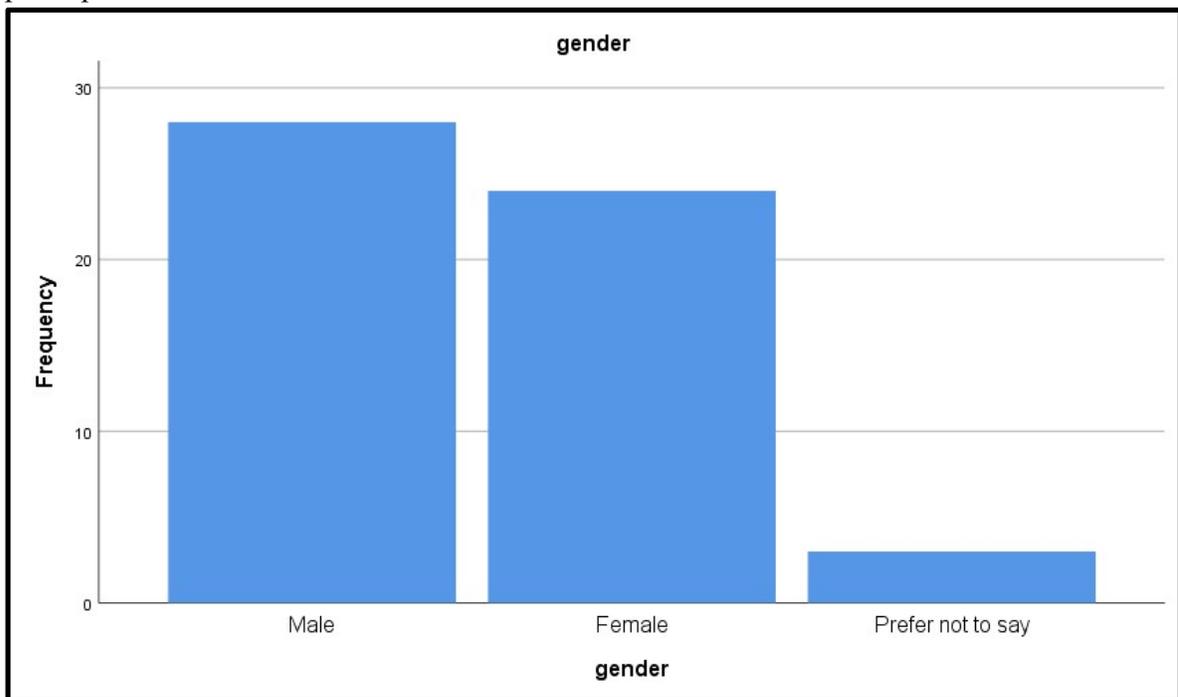


Figure 4: Gender

(Source: SPSS)

The gender-specific response rates are shown in Figure 4. The data collection revealed that 50.9% of men and 43.6% of women took part, with men having the greatest response rate. With 5.5% of responses, the "preferred not to say" group had the lowest response rate. The data reveals that respondents who choose not to identify their gender were less likely to participate and that male respondents predominate.

Age

		age			
		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	22-25 years	23	41.8	41.8	41.8
	26-30 years	20	36.4	36.4	78.2
	31-35 years	7	12.7	12.7	90.9
	More than 35 years	5	9.1	9.1	100.0
	Total	55	100.0	100.0	

Table 2: Age of the respondents

(Source: SPSS)

A breakdown of respondent frequencies by age group is given in Table 2. “23 responders are between the ages of 22 and 25, and 20 participants are between the ages of 26 and 30”. In addition, 7 participants are between the ages of 21 and 35, and 5 respondents are more than 35 years old. This information provides insight into how respondents are distributed throughout various age groups.

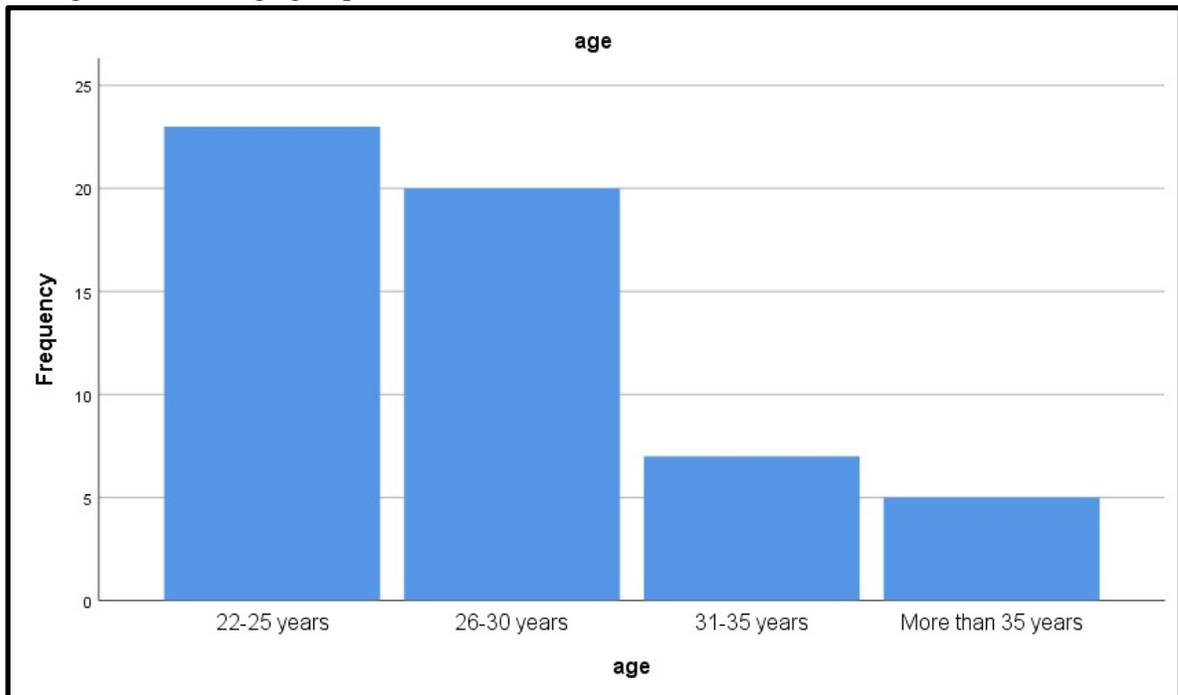


Figure 5: Age

(Source: SPSS)

Age-group-specific response rates are shown in Figure 5. The group aged 22 to 25 exhibits the highest response rate of 41.8%, indicating that they are the most responsive participants. The next group, aged 26 to 30, had a response rate of 36.4. A significant 12.7% of respondents are between the ages of 31 and 35, while participants between the ages of more than 35 years have a response rate of 9.1%. This data demonstrates how different age groups have varying degrees of engagement.

Education

		educational background			
		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Graduation	33	60.0	60.0	60.0
	Post Graduation	15	27.3	27.3	87.3
	PhD	7	12.7	12.7	100.0
	Total	55	100.0	100.0	

Table 3: Educational background of the respondents

(Source: SPSS)

Table 3 illustrates the educational background of the participants. 33 graduates, 15 post-graduates, and 7 PhD students have participated in the survey.

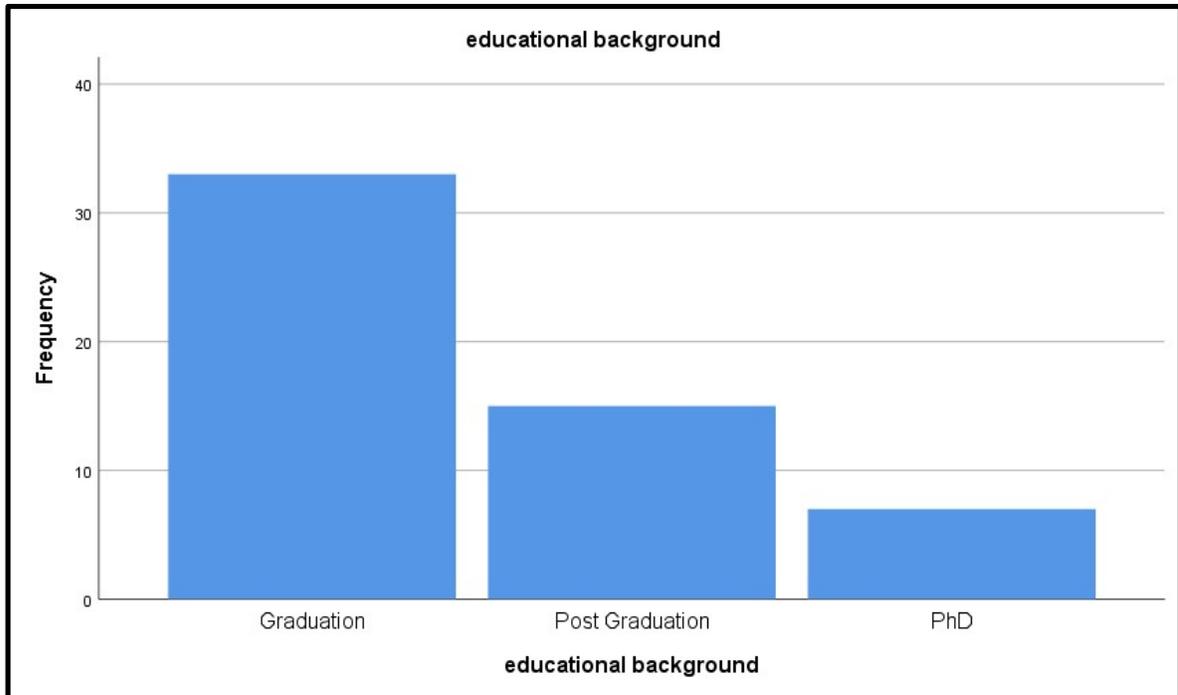


Figure 6: Educational background

(Source: SPSS)

Figure 6 illustrates the educational background in which 60% of the respondents are graduates, 27.3% are post-graduates, and 12.7% are PhD students.

Statistical analysis

Descriptive tests

Descriptive Statistics								
	N	Minimum	Maximum	Mean	Std. Deviation	Kurtosis		
	Statistic	Statistic	Statistic	Statistic	Statistic	Statistic	Std. Error	
DV	55	1	5	1.47	.920	7.187		.634
IV1	55	1	4	1.42	.786	4.523		.634
IV2	55	1	5	1.44	.977	8.016		.634
IV3	55	1	5	1.53	1.034	5.559		.634
IV4	55	1	5	1.47	.879	5.502		.634
Valid N (listwise)	55							

Table 4: Descriptive analysis of the variables
(Source: SPSS)

Descriptive data for four distinct variables are shown in Table 4. 1.42 is the mean value, 0.634 is the standard error, and 0.786 is the standard deviation for the first variable. As suggested by Denis (2018), insights into central patterns, variability, and distributions are provided by descriptive statistics, which can help with data analysis and decision-making by summarizing and simplifying complex data. The mean, standard deviation, and standard error of the second variable are 1.44, 0.634, and 0.977, respectively. “The mean of the third variable is 1.53, and its standard deviation is 1.034, with a standard error of 0.634”. The standard deviation is 0.879 and the mean value is 1.47 for the fourth variable. These statistical measures provide information about each variable's central tendency (mean), data dispersion (standard deviation), and accuracy of the mean estimate (standard error). Therefore, with this knowledge, researchers can better grasp the distribution and traits of various variables, facilitating data analysis.

Regression analysis

Hypothesis 1

Model Summary									
Model	R	R Square	Adjusted R Square	Std. Error of the Estimate	R Square Change	Change Statistics			Sig. F Change
						F Change	df1	df2	
1	.208 ^a	.043	.025	.908	.043	2.398	1	53	.007

a. Predictors: (Constant), IV1

ANOVA ^a						
Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	1.979	1	1.979	2.398	.007 ^b
	Residual	43.730	53	.825		
	Total	45.709	54			

a. Dependent Variable: DV
b. Predictors: (Constant), IV1

Coefficients ^a						
Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	1.127	.254		4.432	.000
	IV1	.243	.157	.208	1.549	.007

a. Dependent Variable: DV

Table 5: Regression for Hypothesis 1
(Source: SPSS)

The outcomes of a linear regression analysis are shown in Table 5. The correlation between the variables is represented by the R-value, which is 0.208. “The percentage of

variance in the dependent variable that is explained by the independent variable is shown by the R square value (0.043)”. A significant link between the variables is indicated by the ANOVA table's F value of 2.398, which is less than 0.05 and has a significance value of 0.001. In the linear regression model, these statistics aid in determining the “significance and strength of the link between the independent and dependent variables”.

Hypothesis 2

Model Summary									
Model	R	R Square	Adjusted R Square	Std. Error of the Estimate	R Square Change	F Change	df1	df2	Sig. F Change
1	.075 ^a	.006	-.013	.926	.006	.302	1	53	.005

a. Predictors: (Constant), IV2

ANOVA ^a						
Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	.259	1	.259	.302	.005 ^b
	Residual	45.450	53	.858		
	Total	45.709	54			

a. Dependent Variable: DV
 b. Predictors: (Constant), IV2

Coefficients ^a						
Model		Unstandardized Coefficients		Standardized Coefficients		
		B	Std. Error	Beta	t	Sig.
1	(Constant)	1.371	.223		6.135	.000
	IV2	.071	.129	.075	.550	.005

a. Dependent Variable: DV

Table 6: Regression test
 (Source: SPSS)

The findings of a linear regression analysis for the variables in question are presented in Table 6. As illustrated by Shrestha (2020), regression analysis examines the connections between variables to forecast results and establish causality. They provide future projections, model validation, and decision-making across a range of domains. A moderate correlation is shown by the R-value of 0.075, and the R-square value of 0.006. “There is a significant association between the variables in the ANOVA table, as indicated by the significance value of 0.001, which is less than 0.05”. The coefficient table shows a beta value of “0.071 and a t value of 0.550”, confirming the considerable correlation between financial statements that can assess the financial performance of a business.

Hypothesis 3

Model Summary										
Model	R	R Square	Adjusted R Square	Std. Error of the Estimate	R Square Change	F Change	df1	df2	Sig. F Change	
1	.033 ^a	.001	-.018	.928	.001	.059	1	53	.009	
a. Predictors: (Constant), IV3										
ANOVA ^a										
Model		Sum of Squares	df	Mean Square	F	Sig.				
1	Regression	.051	1	.051	.059	.009 ^b				
	Residual	45.658	53	.861						
	Total	45.709	54							
a. Dependent Variable: DV										
b. Predictors: (Constant), IV3										
Coefficients ^a										
Model		Unstandardized Coefficients B	Std. Error	Standardized Coefficients Beta	t	Sig.				
1	(Constant)	1.518	.225		6.756	.000				
	IV3	-.030	.122	-.033	-.242	.009				
a. Dependent Variable: DV										

Table 7: Regression for Hypothesis 3
(Source: SPSS)

The results of a linear regression analysis are shown in Table 7. “While the R square value of 0.001 indicates that variance in the dependent variable is explained by the independent variable, the R-value of 0.033 indicates a moderate correlation”. The number of respondents is taken into consideration by the adjusted R square value (-0.018). A significant link between the variables is indicated by the F value in the ANOVA table, which is 0.059, and the significance value, which is less than 0.05, which is 0.009. The substantial link between “the dependent and independent variables” is confirmed by the coefficient table, which shows a beta value of -.030 and a t value of -.242. These figures shed light on the linear regression model's capacity for prediction.

Hypothesis 4

Model Summary										
Model	R	R Square	Adjusted R Square	Std. Error of the Estimate	R Square Change	F Change	df1	df2	Sig. F Change	
1	.007 ^a	.000	-.019	.929	.000	.002	1	53	.001	
a. Predictors: (Constant), IV4										
ANOVA ^a										
Model		Sum of Squares	df	Mean Square	F	Sig.				
1	Regression	.002	1	.002	.002	.001 ^b				
	Residual	45.707	53	.862						
	Total	45.709	54							
a. Dependent Variable: DV										
b. Predictors: (Constant), IV4										
Coefficients ^a										
Model		Unstandardized Coefficients B	Std. Error	Standardized Coefficients Beta	t	Sig.				
1	(Constant)	1.483	.246		6.028	.000				
	IV4	-.007	.144	-.007	-.049	.001				
a. Dependent Variable: DV										

Table 8: Regression for Hypothesis 4
(Source: SPSS)

Table 8 represents the regression test for hypothesis 4, the R-value for the fourth variable is 0.007, and the R-Square value is 0.000.

Correlation analysis

		Correlations				
		DV	IV1	IV2	IV3	IV4
DV	Pearson Correlation	1	.208	.075	-.033	-.007
	Sig. (2-tailed)		.127	.585	.009	.961
	N	55	55	55	55	55
IV1	Pearson Correlation	.208	1	.457**	.088	.218
	Sig. (2-tailed)	.127		.000	.522	.110
	N	55	55	55	55	55
IV2	Pearson Correlation	.075	.457**	1	.043	.187
	Sig. (2-tailed)	.585	.000		.755	.172
	N	55	55	55	55	55
IV3	Pearson Correlation	-.033	.088	.043	1	.128
	Sig. (2-tailed)	.809	.002	.755		.351
	N	55	55	55	55	55
IV4	Pearson Correlation	-.007	.218	.187	.128	1
	Sig. (2-tailed)	.961	.110	.172	.351	
	N	55	55	55	55	55

** . Correlation is significant at the 0.01 level (2-tailed).

Table 9: Correlation test analysis

(Source: SPSS)

Table 9 displays the results of a correlation study for the variables. As viewed by Makowski et al. (2020), in research and data analysis, correlation tests evaluate “the strength and direction of the relationship between variables”, which helps uncover relationships, recognise patterns, and direct decision-making. There is a significant association between the first, second, third, and fourth variables, as shown by their significance values of 0.001, which is less than 0.05. With a significance value of 0.005, the fourth variable likewise exhibits a significant association with the dependent variable. Strong correlations between the variables are suggested by these data, corroborating the idea that they are related and have an impact on one another. The degree and direction of these correlations can be determined with the use of correlation analysis, which offers insightful information for additional data interpretation and decision-making.

Discussion

Examining financial statements is an essential part of assessing the performance of a company. As suggested by Roychowdhury, Shroff & Verdi (2019), a financial statement helps stakeholders make decisions by providing insights into various financial parameters. Additionally, analysing the profitability of a company is one of the main methods used to evaluate its performance using financial statements. As illustrated by Thottoli (2023), the income statement shows the company's potential to turn a profit by giving a quick overview of its revenues and costs. Therefore, growing earnings over time indicate a sound, profitable company, while diminishing profits may indicate other problems that need to be looked at further, such as pricing, demand in the market, or cost control.

Financial statements also aid in evaluating the liquidity and financial status of an organization. As per the view of Cho, Chung & Young (2019), the balance sheet shows the assets, liabilities, and shareholders' equity of the business, providing insight into its entire

financial situation. Stability in finances is demonstrated by a robust balance sheet with plenty of assets and reasonable debt. On the other hand, a high debt-to-equity ratio or insufficient liquidity may be signs of financial risk. They may make it more difficult for a company to weather downturns in the economy or take advantage of expansion possibilities.

A fundamental component of analysing financial statements comprehends the cash flow of a business. The cash inflow and outflow from financing, investing, and operating operations are shown on the cash flow statement (Putra, 2019). A company's ability to generate cash from its primary business activities is shown by positive cash flows from operations. This is essential for funding growth and fulfilling immediate responsibilities. Negative operating cash flows could be a sign of deeper problems in the company, such as low sales or inefficient operations. Ratios are an effective tool for analysing financial statements (Tsalis et al. 2020). They offer a means of evaluating a company's performance on historical data or industry standards. Common ratios that provide useful information about a company's financial structure, short-term liquidity, and profitability are the debt-to-equity ratio, current ratio, and return on equity. Therefore, a high debt-to-equity ratio could be a sign of financial risk, and a sliding return on equity might be a sign of declining profitability and call for additional research.

Moreover, trend analysis is critical to evaluating the success of a firm. As demonstrated by Safari Gerayli (2020), finding patterns and trends in financial statements across several periods is made possible by this comparison. For instance, sustained revenue growth over several years points to a successful company, but gradually dropping profit margins could be a sign of cost-cutting measures or competitive challenges. Moreover, recognizing these trends helps stakeholders anticipate potential issues or opportunities and make proactive decisions. One of the core components of evaluating the operation of a corporation is financial statement analysis (Gomez & Bernet, 2019). However, when paired with ratio and trend analysis, these statements' insightful data on profitability, financial health, cash flow, and other areas provide a complete picture of the company's financial situation. Therefore, understanding the information offered by these financial reports can help stakeholders identify development potential, reduce risks, and make well-informed decisions.

Conclusion

From the above study, it has been concluded that analysing financial accounts is a crucial part of assessing the performance of a company. These financial statements provide a thorough diagram of the profitability, cash flow, and overall situation of a company's finances. Stakeholders can obtain deeper insights and make wise decisions about lending, investments, and strategic planning by utilising ratios and trend analysis. On the other hand, it is critical to be mindful of any possible problems relating to data falsification or manipulation. Ensuring the truth of financial statements and addressing these risks require independent audits, regulatory monitoring, and transparency. Therefore, the capacity to evaluate a company's performance using financial records is essential for seeing possibilities, flaws, and strengths. It also facilitates efficient decision-making and helps the organization succeed in the long run.

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