International Journal of Social Sciences
Uluslararası Sosyal Bilimler Dergisi

Use Of Financial Analysis In Improving Financial Performance: A Case Study Of Industrial Company In Iraq

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Abstract

The study examined the Use of Financial Analysis in the Evaluation of Financial Performance: A Case Study of Fallujah Construction Materials Company. The financial analysis includes a detailed study of the data contained in the financial disclosures, a study of the results of the financial performance to be interpreted and the identification of weaknesses and strengths in the financial policies established at the facility. This conversion process requires the use of a range of methods, the most important of which are financial ratios and the financial analyst's best choices for the problems faced by financial management, and do everything he can to help the administration adopt right decisions that make actual performance as required. The lowest cost and there is no choice in front of us except profit or loss is the tool that can show how economically efficient industrial projects perform.

Fallujah Construction Materials Company was selected for the period (2007-2010) and we discussed, in our research, the key aspects and scientific as well as practical procedures through a set of financial ratios indicators to know the points of strength and weakness and the extent to which the objectives for which the project was established have been achieved.

Keywords: Financial Analysis, Financial Performance, Financial Ratios

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IJSS, 2019, Volume 3, Issue 15, p. 226-243.

Finansal Performansin Değerlendirilmesinde Finansal Analizin Kullanilmasi: Felluce İnşaat Malzemeleri Şirketi Üzerine Bir Vaka Çalişmasi

Özet

Çalışmada; Finansal Performansın Değerlendirilmesinde Finansal Analizin Kullanılması: Felluce İnşaat Malzemeleri Şirketi Üzerine Bir Vaka Çalışması incelenmiştir. Finansal analiz; finansal açıklamalarda yer alan verilerin ayrıntılı bir şekilde incelenmesini, yorumlanacak finansal performansın sonuçlarının incelenmesini ve tesiste kurulan finansal politikalardaki zayıflıkların ve güçlü yönlerin belirlenmesini içerir. Bu dönüşüm süreci; en önemliler arasında yer alan finansal oranları ve finansal analistin, finans yönetiminde karşılaştığı sorunlar için en iyi seçimi gibi bir dizi yöntemin kullanılmasını gerektirir ve yönetimin gerçek performansı için gereken doğru kararları benimsemesine yardımcı olmak amacıyla finansal analist elinden gelen her şeyi yapmasını kapsar. En düşük maliyet ve kar (tasarruf) veya zarar (açık) ki önümüzde bunlar dışında bir seçenek yoktur ve bunlar ekonomik olarak verimli endüstriyel projelerin nasıl performans gösterdiğini gösteren araçtırlar.

Felluce İnşaat Malzemeleri Şirketi 2007-2010 dönemi için seçilmiş olup araştırmamızda; bir dizi finansal oran göstergesiyle, güçlü ve zayıf noktalarını ve projenin kurulduğu hedeflerin ne ölçüde sağlandığını bilmek için temel yönlerini, bilimsel ve pratik prosedürlerini tartıştık.

Anahtar Kelimeler: Finansal Analiz, Finansal Performans, Finansal Oranlar

1. Introduction

Financial performance principally reflects business sector outcomes and results that shows overall financial health of the sector over a specific period of time. It indicates that how well an entity is utilizing its resources to maximize the shareholders wealth and profitability. This enables the facility to plan for the future in the light of past achievements, or it involves converting data obtained from its sources into information of particular significance. The performance evaluation process is a measure of the revenues achieved in the industrial company by maximizing the production as possible at the lowest cost and there is no choice in front of us except profit (savings) or loss (deficit) is the tool that can show how economically efficient industrial projects

perform, based on this the economic calendar should therefore be a set of operations by which the profit or loss of any company should be measured after subtracting the total costs of production verified by the company's revenues for a specified period of time or for previous periods.

Although a complete evaluation of a firm's financial performance take into account many other different kind of measures but most common performance measurement used in the field of finance and statistical inference is financial ratios.

2. Literature Review

Bhushan & Rai (2004) concludes that for purposes of Financial Decisions process exists different tool as Net Present Value (NPV), Internal Rate of Return (IRR), Benefit Cost Ratio (BCR), Total Cost of Ownership (TCO), Payback Period, Balanced Scorecard, Economic Value Added (EVA) and Return on Investment (ROI) (Bhushan & Rai, 2004, pp. 6-8). For calculating mentioned indicators, directly or indirectly, information from accounting system, i.e., annual financial statements are needed. "It is up to the decision-maker or makers to understand the context, underlying advantages and disadvantages of these tools prior to their deployment in the decision making process" (Bhushan & Rai, 2004, p. 6).

David (2011) states that assessment of business strategy should be conducted by using quantitative and qualitative criteria. "Quantitative criteria commonly used to evaluate strategies are financial ratios, which strategists use to make three critical comparisons: (1) Comparing the firm's performance over different time periods, (2) Comparing the firm's performance to competitors' and (3) Comparing the firm's performance to industry averages" (David, 2011, p. 293). The most often used instruments for conducting quantitative strategy assessment are Return On Investment (ROI), Return On Equity (ROE), profit margin, market share, debt to equity, earnings per share, sales and assets growth, and at the end, as a important tool for strategy assessment is financial statements audit (David, 2011, p. 293). Mentioned tools for strategy assessment are individual financial ratios calculated using data from annual financial statements. "Financial accounting information is designed for decision makers who are not directly involved

in the daily management of the company. These users of the information are often external to the company" (Lanen, et al., 2011, p. 6).

3. Methodology Of The Study

The study consisted of two theoretical and applied aspects, the theoretical one deals with scientific thoughts and views related to financial analysis where the researcher used the descriptive approach in presenting the data, and analytical approach in analysis of the results of the study, which aimed to identify the effectiveness of financial analysis at industrial companies.

4. The First Discourse

4.1. Concept of Financial Analysis

The analysis is defined as the sum of mathematical, statistical and technical methods and performed by the financial analyst on the data, reports and financial statements in order to assess the performance of institutions and organizations in the past and present and to anticipate what they will be in the future (Abdallah, 2008, p. 15).

He adds (Saada, 2008-2009, p. 3) the financial analysis is closely linked to the need of the different parties involved in the project, to learn about the economic changes that have occurred in its work during a certain period, and future trends of its development, and to know the historical variables and predictions for the future,the financial analysis is used to study the past and compare it to the present to predict future, which in this sense is a science which is relevant to the making of information in order to assist those involved in making decisions regarding the project.

4.2. Objectives of Financial Analysis

The overall objective of the financial analysis is to evaluate the performance of the institution from multiple aspects and how to achieve the goals of users of information who have financial interests in the institution, in order to identify strengths and weaknesses, thus, use the information provided by the financial analysis to rationalize their financial decisions related to the institution, and the objectives of financial analysis can generally be limited to the following aspects (Saada, 2008-2009, p. 3).

4.3. Uses of Financial Analysis

Financial analysis is used to identify and judge the level of performance of enterprises and make special decisions and financial analysis can be used for the following purposes (Al-Mutairi, 2011, p. 61):

1. Credit analysis: This analysis is performed by lenders in order to identify the risks they may be exposed to if the enterprises are unable to pay their obligations on time.

2. Consultative Analysis: This analysis is done by individual and corporate investors who are interested in the safety of their investments and the amount of revenues on them, and this type of analysis is used to assess the efficiency of management in creating new investment areas in addition to measuring the profitability and liquidity of the facility.

3. Merger and Acquisition Analysis: This type of analysis is used during the merger process between two companies that evaluate the current value of the company intended to purchase and determine the company future performance after the merger.

4. Financial Planning: Financial planning is one of the most important roles of the administrations and the planning process is represented by developing a vision of the expected performance of the future, and here the roles of financial analysis plays an important aspect in this process in terms of assessing past performance and estimating the expected performance in the future (Jerdawi, 2008, p. 31).

5. Performance Evaluation Analysis: The evaluation of performance in an enterprise is considered as one of the most important uses of financial analysis. Through the revaluation process, the following aspects can be judged on; level of profits, the capacity of the facility to liquidity, the repayment of obligations and its ability to credit, as well as the valuation of assets.

6. Parties Using and Benefiting from Financial Analysis: Various parties get benefit from the analysis information, as well as the purposes of their use of the information, which vary according to the diversity of their relations with the institution on the one hand and the diversity of their decisions based on this information on the other hand, and the parties that use and get benefit from financial analysis information are listed as following: (Saada, 2008-2009, p. 9-12):

1. Management of the enterprise,
2. Investors,
3. Clients,
4. Employees of the foundation,
5. Government entities,
6. Individuals and entities dealing with securities,
7. Institutions working in the field of financial analysis.

5. The Second Discourse

5.1. Financial Analysis Tools

The financial analysis of the published financial statements is considered as the means by which investors can develop a set of financial indicators for the activities of the facility and in this analysis various tools can be used as follows:

- **Vertical Analysis:** The vertical analysis is represented by studying the quantitative relationships between the items of the financial list at a certain time, and this type of analysis is characterized by inertia and persistence, although it helps to evaluate the performance of the facility in a given period and discover the strengths and limitations of it, however it still need to be supported by horizontal analysis and obtaining the sales center (Abdulhadi, 2000, p. 103).

- **Horizontal Analysis:** This type of analysis is represented by studying the behavior of each item of the financial lists over time, i.e., tracking the movement of the item, whether increase or decreaseover time, and thus it is a dynamic analysis because it shows the changes that have occurred in a relatively long period of time (Alkahlot, 2005, p. 31).

- **Analysis by Financial Ratios:** Analysis of financial ratios by finding the relationship between two variables with common properties to judge a particular status or activity of the facility. The financial ratios have become gained an increasing importance as these ratios became important financial indicators to be used by financial analysts in predicting financial failures of enterprises (Al-Sayahand & AL-Amiri, 2006, p. 52-33; Jaber, 2006, p. 8).

5.2. Financial Analysis Ratios

5.2.1. Liquidity Ratios

A. Trading ratio: Trading Ratio=Current Assets/Liabilities

This percentage reflects the number of times that current assets can cover current liabilities, and the higher this rate, the more the company's ability to meet the risk of sudden-onset current liabilities without the need to liquidate any fixed assets or obtain new borrowing (Ghussein, 2004, p. 44).

B. Quick repayment ratio: Cash Ratio=(Current Assets–Inventory)/Current Liabilities

This ratio illustrates the extent to which short-term liabilities can be repaid within a few days and the fair ratio in most industries is 1:1 (Sheikh, 2008, p. 31-35).

C. Cash ratio: Cash Ratio=Cash and Quasi-Cash Assets/Current Liabilities

This percentage illustrates the extent to which short-term liabilities can be repaid through a telephone call as they say (Ahmed & Al-Kassar, 2009, p. 8).

D. Ratio of debt to total assets: This ratio measures the extent to which the enterprise is relying on the funds of others to finance its needs and can be calculated by dividing the total debt (short and long term) on total assets (traded and fixed) (Akel, 2000, p. 390).

E. Debt-to-property ratio: Calculated by dividing the total debt (short and long-term) on property rights (capital, reserves and retained earnings) (Shamki & Aljazrawi, 1998, p. 66).

F. Ratio of capital structure: Calculated by dividing the total long-term debt into long-term sources of finance (long-term debt and property rights). This ratio is considered to be an indicator of financial risk judgment (Lutfi, 2006, p. 352).

J. Interest gain rate (coverage ratio): This ratio measures the extent to which the enterprise can pay the interests of the loans from realized profits, and is counted by dividingthe income before interest and taxes on paid annual benefits and the higher the rate, the greater the confidence in the enterprise ability to meet the loans interestsit is committed to (Al Ameri, 2001, p. 136).

5.2.2. Profitability Ratios

These ratios measure the company ability to generate profits from sales, assets, and property right. The most important and common ratios of this group are:

A. Gross profit margin ratio (total profit): This ratio indicates the efficiency of management in pricing and sales generation, and the control of costs and is calculated by the total profit (sales-the cost of goods available for sale) on net sales, and the higher the rate, the better it would be.

B. Operational profit margin ratio: This ratio measures the overall operational efficiency of the company and is calculated by dividing the operating profit on net sales and the higher the rate, the better it would be.

C. Ratio of net income: This ratio measures the sales capacity to generate net income and is calculated by dividing the net income on the net sales, and the higher the rate, the better it would be (Al-Shedifat, 2001, p. 130).

As the total profit represents the price of the sale that covers the cost and makes a profit, so this ratio will contribute to the pricing. Another researcher (Al-Shamma, 1992, p. 100) adds the following:

D. Rate of revenue on investment (assets): This ratio measures the overall efficiency of the management in achieving profits from its overall investment in assets and is calculated by dividing net income on total assets (traded and fixed). The higher the rate, the better it would be.

E. Rate of revenues on property right: Calculated by dividing net income on the right of property (paid-up capital+premiums+retained earnings). Higher rate is an evidence of efficient management, which is usually preferred by the owners.

F. Basic revenue capacity: This ratio reflects the extent to which the assets contribute to making the operational profit and is extracted by dividing the operational profit on the assets.

5.2.3. Activity Ratios (Assets Management)

This set of ratios measures the efficiency of enterprise resources management by comparing its net sales with investment in major groups of assets (Akil, 2000, p. 371).

These ratios assume an appropriate balance of company sales and assets such as inventory, debtors and total assets, and work to detect any defect and fixed assets may occur on this balance.

One of the most important and common ratios of this group is:

A. Property ratios: This ratio is used to determine the percentage that shareholders will get from the total assets in case of liquidation (Abdallah, 2008, p. 29).

B. Turnover of fixed assets: This index measures the efficiency of management in the use of its fixed assets for the making sales, if it is high "It indicates the effective use of available production capacity (the intensity of the facility's utilization of its fixed assets), but its decline indicates that the fixed assets are not used efficiently (Essam, 2012, p. 49).

C. Turnover of total assets: This ratio measures the management efficiency in managing total assets to make sales, higher percentage is indicative of efficient use of assets in making sales (Hassoun, 2007, p. 75). Another researcher (Al-Ameri and Al-Rakabi, 2007, p. 120) adds the following:

5.2.4. Rates of Assessment

The ratios of this group reflect the evaluation of the financial market for the performance of the enterprise, which is the most accurate criterion for the value of the enterprise. The most important and common rates of this group are:

A. The ratio of the price of one ordinary share to its book value: The share price of the ordinary share in the market is attributed to its book value (the right of property / number of ordinary shares), thereby understanding the market value of the share in relation to what is recorded in the books of the company.

B. The ratio of price of a single average share to its profitability: The ordinary market share price is attributed to its profitability (net income/number of ordinary shares) and this ratio measures the amount of profit that belongs to each share of the company at the end of the financial period.

6. Third Discourse

6.1. Performance Evaluation

6.1.1. The Concept of Performance Evaluation

It is defined as measuring the performance of the activities of an economic unit combined, based on the results achieved at the end of the accounting period, which is usually one calendar year, in addition to knowing the causes that led to the above results and proposing solutions to overcome those causes in order to achieve good performance in the future (Akil, 2000, p. 190).

It is also defined as all processes and studies that are designed to determine the level of relationship between available resources and the efficient use of them by the economic unit, while assessing the evolution of the relationship during successive periods of time or in a specific period by making comparisons between the targeted objectives and the achieved ones based on specific standards and criteria (Al-Shamki & Al-Jazrawi, 1998, p. 46).

6.1.2. Basic Rules of Performance Evaluation

6.1.2.1. Setting the Targets

For the purpose of evaluating the efficiency of the economic unit performance, it is necessary to identify the objectives that the unit intends to achieve, these objectives should be clearly and accurately identified using the numbers, ratios and appropriate description such as profitability, the added value to be achieved, the size and type of goods and services it produces, and so on. Economic unit, when it formulates policies on the overall objective of its activity, it must be expanded to include all its detailed objectives (Eid, 2009, p. 23).

6.1.2.2. Develop a Program Accomplish Businesses

In light of specific objectives, an integrated plan is developed to accomplish businesses in details for each area of activity in the economic unit; within this unit, the financial and human resources available to the unit are explained, in addition to identifying their sources and how to obtain them beside the technical, administrative and organizational methods that they follow in the management and use of these resources, the nature of the production, marketing techniques, the type of technology used and the methods of preparation and training of manpower (Abdallah, 2008, p. 39). Another researcher adds (Ahmed and Al-Kassar, 2009, p. 16) the following:

6.1.2.3. Determination of Responsibility Centers

The centers of responsibility mean that each organizational unit, which is competent to perform a particular function and has the authority to take decisions that, would manage part of the activity of the economic unit and determine the results that it will obtain. Therefore, the responsibility of each center of the production process must be defined for the purpose of accountability and to explain the causes of deviations that occur during the implementation process.

6.1.2.4. Defining Performance Standards

Performance evaluation procedures require the development of criteria for the purpose of comparison with the results achieved. The criteria are a set of measures, ratios and bases by which the achievements of the economic unit can be measured.

6.1.2.5. Availability of an Appropriate Apparatus to Execute the Performance Evaluation Process

This is the basis of the performance evaluation process and its existence should be assumed prior to the initiation of the process. It is assumed that there is a monitoring and information gathering system that records the results that originate from the implementation by using them in specific purposes that the management notes. Performance evaluation results depend on the accuracy of data collection and recording. Specialized training for the benefit of all executive and supervisory levels.

6.2. Stages in the Performance Evaluation Process

6.2.1. Collection of Statistical Data and Information

Statistical data and information are obtained from the financial statements, consisting of the financial position list, the income list, the cash flow list, the other lists and explanatory notes attached to the financial reports, as well as information of previous years, in addition to data related to activities of similar establishments.

6.2.2. Analysis and Study of Statistical Data and Information Related to the Activity

A level of reliability and independence should be provided in these data and some known statistical techniques may be used to determine the reliability of such data (Al-Tamimi, 2010, p. 39). Al Ameri adds the following (2001, p. 145):

6.2.3. Conducting the Assessment Process

By using the appropriate criteria and ratios for the activity carried out by the economic unit. The evaluation process should include the general activity of the economic unit in order to reach a reliable and objective judgment.

6.2.4. Determining the Deviations

This is done by comparing the results of the evaluation with the unit-planned objectives. The deviations in the activity have been limited and their causes determined. The solutions needed to address the deviations have been taken and the plans have been put in place to carry out the unit's activity for the better in the future.

6.2.5. Follow-up Correction of Deviations

This is by presenting the results of the evaluation to various departments within the unit to make use of them in the design of future plans and to enhance the effectiveness of follow-up and supervision.

7. Fourth Discourse

7.1. Applied Study

7.1.1. Introduction to Fallujah Company for the Manufacturing of Construction Materials

Fallujah is considered one of the most important industrial companies in Iraq and it is of a mixed type of contribution, the government (0.1825) and private sector contribution (0.8175), it is located in Anbar province, Fallujah district, near the Fallujah cement factories, short code is IFCM Fakashi.

7.1.2. What Are Its Activities

The company is specialized in manufacturing of block and concrete slabs (stagier) of all types, concrete pipes of various measurements, and the interlocked tiles of pavements with different types, in addition to concrete slab sand marble-inlaid mosaic.

7.1.3. Date of Incorporation and Listing in the Baghdad Stock Exchange

It has been decided to establish the company on (22/08/1989) according to the international numbering (IQ000A0M7TY6) with a founding capital of 10.000.000 Iraqi Dinars, date of listing it on the Baghdad Stock Exchange was on 14/08/2004 with a registered capital of 20.000.000). The following table shows the financial ratios of Fallujah Company for construction materials for the years 2007 to 2010.

Table 1. The Financial Ratios of Fallujah Company for Construction Materials for the Years 2007 to 2010

Year / Financial Ratios	2007	2008	2009	2010
Share Turnover Ratio	1.02	1.40	49.51	50.24
Revenues Per Share-ID	---	---	0.11	0.00
Property Ratio	57.38	47.02	61.90	77.83
Trading Rate (Times)	2.11:1	1.69:1	2.40:1	3.99:1
Rapid Liquidity Ratio	1.13:1	0.3:1	0.29:1	0.82:1

8. Conclusions

8.1. Share Turnover Ratio

It is noted that this ratio has risen from the year 2007 to 2008 by 0.38 and during the period 2008 and 2009 by 48.11, and from 2009 to 2010, it increased by 0.73. These ratios indicate an increased trading of the company's shares in the market and its close correlation with the profit. A proof to this is that the company in the year (2007 and 2008) had made a loss, and its shares trading rate was low compared to the years (2009 and 2010) when it made a profit.

8.2. Revenues Per Share

It is noted in the table above that in the years 2007-2008, the company did not make any profits. This is why the earnings per share ratio did not appear, as opposed to the year 2009 and 2010. In 2010, the company's policy necessitated not to distribute profits and keep them as reserves.

8.3. Property Ratio

It is noted from the above table that the company decided to liquidate in the year 2007 and that a shareholder with shares worth of 30 million would receive 17,214,000 through (30,000,000*%57.38). Whether this ratio is affected by the company's profits or not can be judged by noting the percentages in the table. In 2007, the percentage was %57.38, which was low due to a loss in this year. In 2008, we can note that the percentage dropped further more than the year 2007 and therefore to make a greater loss than it was, while in the year 2009-2010 we can notice that the percentages started to increase gradually and this was for a clear reason which as making a profit in these years on the contrary of the previous years.

8.4. Trading Rate

From the table above, we can notice which percentages are better and are closer to the fair ratio in 2007. Although they are larger than the fair ratio of 0.11, this indicates the strength of the company's financial position, which is better than the rest of the years, while in 2008, the ratio was lower than the fair ratio by 0.31. This was an indication of an increase in the item of liabilities on the assets, which indicates that the financial position of the company started to weaken. In 2009, the ratio increased by 0.40 and in the year 2010 it also increased by 1.99 above the fair value, which indicates that there was an increase in the current assets in comparison with the current liabilities (Abu Bakr, 2008, p. 23).

8.5. Rapid Liquidity Ratio

In the above table you can determine which financial ratios were closest to the fair ratio, in 2007, the rate of rapid liquidity was greater than the fair ratio by 0.13, this indicates a surplus in the current assets, which indicates the strength of the company's financial position, while in 2008, we can notice that there was a decrease in the rapid liquidity ratio by 0.70 from the fair ratio, which indicates a decrease in the current assets in comparison to the liabilities as evidenced by the weak financial position of the company. As in 2009, we can notice that the rapid liquidity ratio was lesser than the fair ratio by 0.71, as it is noted the ratio here was below the liquidity ratio for 2008, while in 2010 we can notice that the percentage started to rise although it did not reach the fair ratio but it was better than what it was in 2008-2009.

8.6. Recommendations

1. It is necessary to rely on the analysis techniques by using the financial ratios when evaluating the performance of companies and educate the affiliates on the importance of this method through conducting training and awareness-raising courses.

2. The main aspects of the performance evaluation process should be updated in line with the state of economic progress to serve the objectives and directions of the economic unit.

3. The need to maintain an appropriate and optimal commodity inventory limit to exceed any additional cost.

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