An Analysis of the Financial Performance of Larsen & Toubro Limited-Critical Evaluation of the Various Financial Ratios of the Company

[1]Mala.K.M, [2]Dr. Raghu.G.Anand
[1]Research Student, Bangalore
[2]Jain University- Center for Management Studies, Bangalore, India

Abstract
Indian mining and construction equipment industry has made substantial growth and investment over the last few years in the country. The growth of this sector is interlinked with the growth of the Indian economy and indirectly with the growth of infrastructure. The prime driver for construction equipment is mining activities and construction industry. Within these industries, the key demand drivers going forward are likely to be road construction, urban infrastructure, irrigation, real estate, construction and mining. Ratio Analysis is a form of Financial Statement Analysis that is used to obtain a quick indication of a firm's financial performance in several key areas. Ratios can be used to compare a firm's financial performance with industry averages. In addition, ratios can be used in a form of trend analysis to identify areas where performance has improved or deteriorated over time. This research intends to study the working capital management at Larsen and Toubro (L&T) and interpret various ratios so as to analyze the performance of various departments in the organization. This study attempts to provide an insight into financial soundness of the company.

Keywords
Ratios, Financial Performance, Liquidity, Working Capital Management, Profitability.

I. Introduction
Finance studies and addresses the ways in which individuals, businesses, and organizations raise, allocate, and use monetary resources over time, taking into account the risks entailed in their projects. Financial management involves managerial activities concerned with the acquisition of fund for business purpose. The finance function does with procurement of money taking into consideration today as well as future needs and finance is required to purchase a machinery and raw materials, to pay salaries and wages and also for day-to-day expenses. Corporate finance is an area of finance dealing with the financial decisions corporations make and the tools and analysis used to make these decisions. The primary goal of corporate finance is to enhance corporate value while reducing the firm's financial risks.
Ratio Analysis is a form of Financial Statement Analysis that is used to obtain a quick indication of a firm's financial performance in several key areas. The ratios are categorized as Short-term Solvency Ratios, Debt Management Ratios, Asset Management Ratios, Profitability Ratios, and Market Value Ratios. It's a tool possesses several important features. The data, which are provided by financial statements, are readily available. The computation of ratios facilitates the comparison of firms which differ in size. Ratios can be used to compare a firm's financial performance with industry averages. In addition, ratios can be used in a form of trend analysis to identify areas where performance has improved or deteriorated over time. It helps in analyzing financial statements, judging efficiency, locating weakness, formulating plans and comparing performance.
Working capital management is the most important fact of the total financial management of any concern. It is that portion of the assets of the business, which are used in relation to current operations and representations at any one time by the operating cycle of such items such as against receivables, inventory, bills receivables and cash. Its effective inefficient management can lead not only to loss of profits but also to the ultimate downfall of what otherwise might be concerned as a promising concern.
Larsen & Toubro Limited is the biggest legacy of two Danish Engineers (who took refuge in India), who built a world-class organization that is professionally managed and a leader in India's engineering and construction industry. Together, Holck-Larsen and S.K.Toubro, founded the partnership firm of L&T in 1938, which was converted into a limited company on February 7, 1946. Today, this has metamorphosed into one of India's biggest success stories. The company has grown from humble origins to a large conglomerate spanning engineering and construction. Larsen & Toubro Limited, also known as L&T, is an Indian Multinational Conglomerate headquartered in Mumbai, Maharashtra, India. L&T has delivered Engineering, Procurement and Construction (EPC) services for many projects in the upstream hydrocarbon sector over the last two decades, in India, Middle East, Africa, South-East Asia and Australia.
L&T has formed a joint venture with SapuraCrest Petroleum Berhad, Malaysia for providing services to offshore construction industry worldwide. It has made presence in various sectors that include Solar, Electrical and automation, information technology, machinery and industrial products, alloys, etc.
This study attempts to provide an insight into financial soundness of the company. It also highlights the significant relationships of the financial statements through analysis. It would also help the company in planning future financial decisions by improving the current financial position and soundness. The study has been restricted to data available between years 2011-2014.

II. Literature Review
Following were the major efforts at research in the subject, which have been referred for this study purpose.
Appavadhanulu (1971)- Recognizing the lack of attention being given to investment in working capital, analyzed working capital management by examining the impact of method of production on investment in working capital. He emphasized that different production techniques require different amount of working capital by affecting goods-in-process because different techniques have differences in the length of production period, the rate of output flow per unit of time and time pattern of value addition. Different techniques would also affect the stock of raw materials and finished goods, by affecting lead-time, optimum lot size and marketing lag of output disposals. He, therefore, hypothesized that choice

of production technique could reduce the working capital needs. He estimated the ratio of work-in-progress and working capital to gross output and net output in textile weaving done during 1960, on the basis of detailed discussions with the producers and not on the basis of balance sheets which might include speculative figures. His study could not show significant relationship between choice of technique and working capital. However, he pointed out that the idea could be tested in some other industries like machine tools, ship building etc. by taking more appropriate ratios representing production technique correctly.

Agarwal (1983)-Also studied working capital management on the basis of sample of 34 large manufacturing and trading public limited companies in ten industries in private sector for the period 1966-67 to 1976-77. Applying the same techniques of ratio analysis, responses to questionnaire and interview, the study concluded the although the working capital per rupee of sales showed a declining trend over the years but still there appeared a sufficient scope for reduction in investment in almost all the segments of working capital. An upward trend in cash to current assets ratio and a downward trend in cash turnover showed the accumulation of idle cash in these industries. Almost all the industries had overstocking of raw materials shown by increase in the share of raw material to total inventory while share of semi-finished and finished goods came down. It also revealed that long-term funds as a percentage of total working capital registered an upward trend, which was mainly due to restricted flow of bank credit to the industries.

Vedavinayagam Ganesan- analyzed the working capital management efficiency of firms from telecommunication equipment industry. The relationship between working capital management efficiency and profitability is examined using correlation and regression analysis. ANOVA analysis is done to study the impact of working capital management on Profitability. Using a sample of 443 annual financial statements of 349 telecommunication equipment companies covering the period 2001-2007, this study found evidence that even though “days working capital” is negatively related to the profitability, it is not significantly impacting the profitability of firms in telecommunication equipment industry.
Shin H. H. and Soenen L (1998) - highlighted that efficient working capital management (WCM) was very important for creating value for the shareholders. The way working capital was managed had a significant impact on both profitability and liquidity. The relationship between the length of net trading cycle, corporate profitability and risk adjusted stock return was examined using correlation and regression analysis, by industry and capital intensity. They found a strong negative relationship between lengths of the firm’s net trading cycle and its profitability. In addition shorter net trade cycles were associated with higher risk and adjusted stock returns.

Md. Sayaduzzaman - The major objective of the study is to examine and evaluate the working capital management in BATBCL over a period of 5 years (1999-2000 to 2002-2003). The efficiency of working capital management of British American Tobacco Bangladesh Company Ltd. is highly satisfactory due to the positive cash inflows, planned approach in managing the major elements of working capital. Applications of multi- dimensional models of current assets mix have positive impact on the continuous growth and development of this multinational enterprise. This depends on co-operation of the stakeholders and business environment in the context of globalization.

III. Research Methodology

A. Objectives of the Study:

- To critically evaluate the various financial ratios of L&T.
- To understand the working capital management of the company.
- To provide an insight about the financial soundness of the company.
- To provide suggestions on better working capital management based on the findings.

B. Tools for Analysis

Ratio Analysis are is the financial tool that has been used for the study.

C. Data Collection Method

Secondary data has been used for the research. The annual reports of LARSEN & TOUBRO Limited and company websites, financial websites, and company’s reports available in periodicals, journals and books are used to obtain secondary data. The research undertaken is mainly based on secondary data. The relevant financial details were collected from the accounting and finance wing of the company. The data collected is measured in crores of rupees.

D. Plan of Study

The data has been collected and represented in the form of table and graphs for the purpose of analysis. Inferences have been drawn and suggestions have been given based on findings.

E. Reference Period

Data of Larsen & Toubro for a period of 3 years, between 2011-2012 and 2013-2014, has been collected and analyzed for the purpose of the research.

IV. Data Analysis and Interpretation

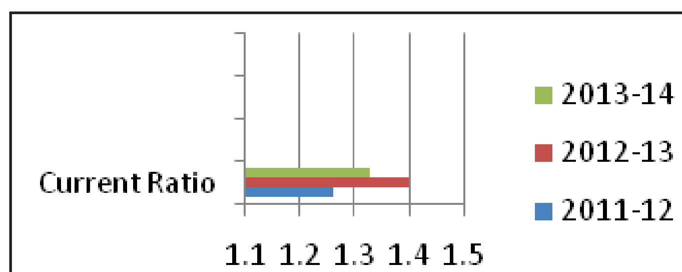
A. Financial Ratios

1. Current Ratio

Current Ratio=Current assets/Current liabilities

	2011-12	2012-13	2013-14
Current assets	46074.65	49247.96	56391.42
Current Liabilities	36355.80	34980.11	38361.51
Current Ratio	1.26	1.40	1.47

Analysis: From the above table it can be seen that the current ratio is 1.26, 1.40, and 1.47 for the years 2012, 2013 and 2014 respectively, where 2014 has the highest ratio of 1.47 The Higher the current ratio, the more capable the company is of paying its current obligation.



Interpretation: This ratio measures the short term solvency of the firm. The ideal current ratio of a company is 2:1, it implies

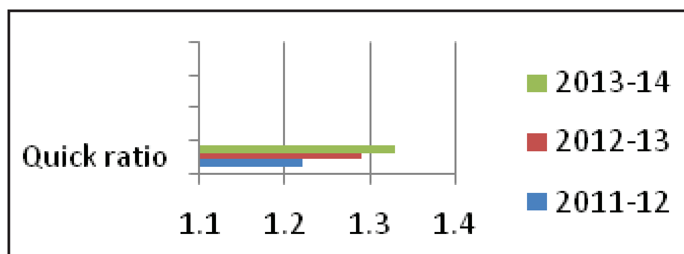
that for every one rupee of current liability, current assets of two rupees are available to meet them. The current ratio is lower in 2014, when compared to the previous year. The current assets are more than current liabilities in 2014, which is a good sign for company.

2. Quick Ratio (Acid Test Ratio)

Quick ratio=Quick assets/Current liabilities

	2011-12	2012-13	2013-14
Quick assets	44354.07	45124.34	51114.61
Current Liabilities	36355.80	34980.11	38361.51
Quick Ratio	1.22	1.29	1.33

Analysis: It can be seen that the quick ratio of the firm is 1.22, 1.29 & 1.33, where year 2014 has the highest ratio. Higher the Ratio, easier it is for the firm to meet its financial demand. Rule of thumb for quick ratio is 1:1.



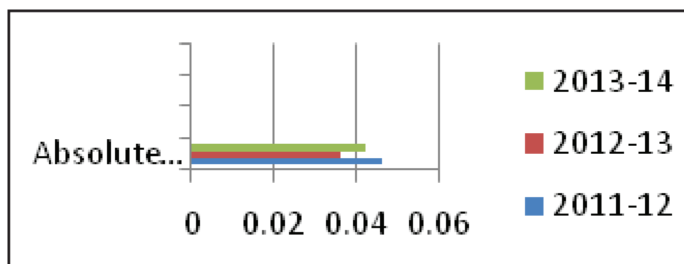
Interpretation: This ratio measures for every rupee of current liability, how much quick assets is available to meet them. It is an important indicator of firm's liquidity position. A quick ratio of 1:1 is an ideal one. The ratio of the company has been above 1.0 in the 3 years. This implies that the company does not depend on inventory to pay its short term liability. In 2012, the company's quick ratio is comparatively less owing to increased sundry creditors.

3. Cash/Absolute Liquid Ratio

Absolute liquid ratio=Cash & Cash equivalents/Current liabilities

	2011-12	2012-13	2013-14
Cash & cash equivalents	1688.11	1279.52	1622.96
Current Liabilities	36355.80	34980.11	38361.51
Absolute liquid Ratio	0.046	0.036	0.042

Analysis: It can be observed that the absolute liquid ratio is 0.046, 0.036, and 0.042 for the year 2012, 2013 and 2014 respectively, where it explains the relationship between liquid assets and current liabilities. Rule of thumb for this ratio is 0.5:1.



Interpretation: The ratio is low in the 3 years compared to the standard ratio which is 0.5:1. This indicates that the L&T does not have enough cash available to satisfy its short term liability. This low ratio indicates immediate problem with paying the bills of the company.

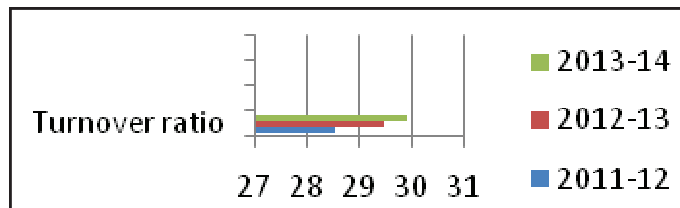
B. Turnover Ratios

1. Inventory Turnover Ratio:

Inventory turnover ratio=Net sales/Average inventory

	2011-12	2012-13	2013-14
Net sales	53170.52	51610.96	56598.92
Average inventory	1862.36	1750.11	1891.04
Turnover ratio	28.55	29.49	29.93

Analysis: From the above table it can be seen that the inventory turnover ratio of the firm are 28.55, 29.49 & 29.93 for the years 2012, 2013 and 2014 respectively. This ratio indicates the number of times the stock has been turned over during the period. Higher the Ratio better efficient management of inventory.



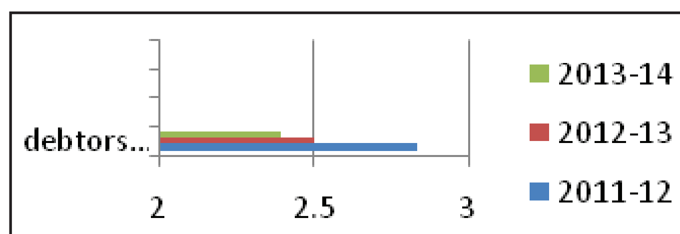
Interpretation: This ratio indicates how fast the inventory of the company is sold. The ratio is high, which signifies more profit to the firm and efficient management of inventory, indicating that stocks have been sold frequently. The ratio is low in the year 2012 which shows that the inventory has not been fast moving.

2. Debtors Turnover Ratio

Debtors turnover ratio=Credit sales/Sundry debtors

	2011-12	2012-13	2013-14
Credit sales	53170.52	56598.92	51610.96
Sundry debtors	18729.84	22613.01	21538.76
Debtors Turnover ratio	2.83	2.50	2.39

Analysis: It can be seen that the firm has 2.83, 2.50 and 2.39 inventory turnover ratio for the year 2012, 2013, and 2014 respectively. It indicates the velocity of debt collection. Higher the Debtor Turnover ratio more efficient is the management of debtors in the firm and vice versa.



Interpretation: This ratio indicates how rapidly receivables are collected. A higher ratio indicates shorter time-lag between credit sales and cash collection and lower ratio shows debts are not collected rapidly. The ratio of the company is very good thus indicates a good liquidity position.

3. Creditors Turnover Ratio

Creditors turnover ratio= Credit purchases/ Sundry creditors

	2011-12	2012-13	2013-14
Credit purchases	430681.82	468133.68	489382.77
Sundry creditors	15752.81	16345.45	16345.45
Creditors Turnover ratio	27.34	28.64	29.94

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Analysis: It can be seen that the firm has a creditor's turnover ratio of 27.34, 28.64 & 29.94 for the years 2012, 2013 and 2014 respectively. The Ratio indicates the velocity of debt payments. Higher the Ratio better is the firm's position in paying debts, maintaining liquidity and procuring credit from the market and vice versa.

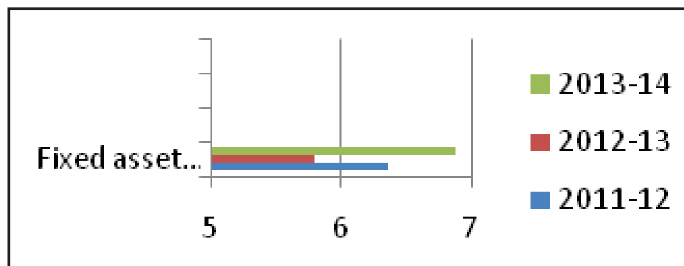
Interpretation: A higher ratio shows the accounts are to be settled rapidly. It measures the extent to which trade creditors are willing to wait for payment. The turnover of L&T is increasing rapidly in the last few years which show that the firm is able to pay back its creditors on time. The ratio of 29.94 in 2014 indicates that company on an average gets 12 days (assuming 365 working days in a year) to settle its creditors which is quite good.

4. Fixed Asset Turnover Ratio

Fixed asset turnover ratio=Sales/Total assets

	2011-12	2012-13	2013-14
Sales	53170.52	51610.96	56598.92
Total assets	8363.66	8901.98	8237.21
Fixed asset turnover ratio	6.35	5.79	6.87

Analysis: From the above table it can be seen that the firm has a total asset turnover ratio of 6.35, 5.79, and 6.87 respectively for the year 2012, 2013, and 2014. It explains the velocity of utilization of net fixed assets.
Higher the ratio better it is for the firm in managing its assets for sales.



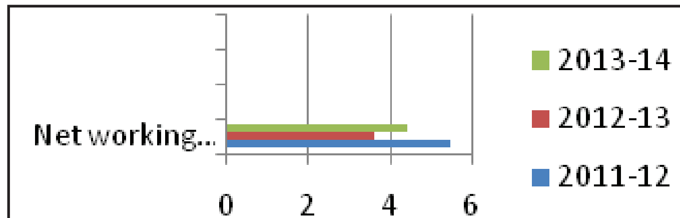
Interpretation: This ratio shows the firm's ability to generate sales from all financial resources committed to total assets. It is the amount of sales generated for every rupee worth of assets. Company's ratio is low in the last 3 years. The companies with low profit margin tend to have high asset turnover while those with high profit margins tend to have low asset turnover. The low ratio of Company shows that the profit margin is reasonably good since they are able to sell more products at reasonable prices.

5. Net Working Capital Turnover Ratio

Net working capital turnover ratio=Total sales/working capital

	2011-12	2012-13	2013-14
Total Sales	53170.52	51610.96	56598.92
Working capital	9718.85	14267.85	12753.10
Net working capital turnover ratio	5.47	3.61	4.43

Analysis: It can be seen that the firm has 5.47, 3.61 and 4.43 ratios for the year 2012, 2013 & 2014 respectively.
It indicates the velocity of utilization of net working capital, and measures the efficiency with which the working capital is being used by the firm. Higher the ratio better utilization of working capital.



Interpretation: It measures how effective the working capital is being used by the firm. As the ratio has increased drastically in the recent year it shows that they are effectively using their working capital in the day to day business operations.

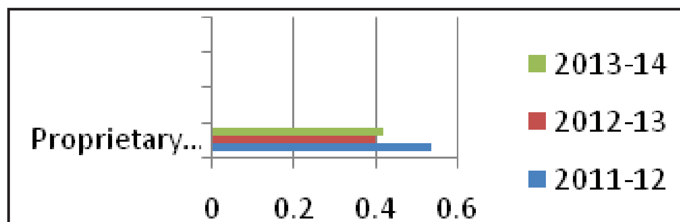
C. Solvency/Leverage Ratios

1. Proprietary Ratio

Proprietary ratio=Shareholders' fund/ Total assets

	2011-12	2012-13	2013-14
Shareholders' fund	25223.02	29142.72	33661.83
Totals assets	46074.65	72424.03	78304.58
Proprietary ratio	0.54	0.40	0.42

Analysis: It can be seen that the firm has 0.54, 0.40 and 0.42 ratios for the year 2011, 2013 & 2014 respectively. It indicates the long term solvency of the finance. Higher the Ratio better is the long term solvency position of the company.



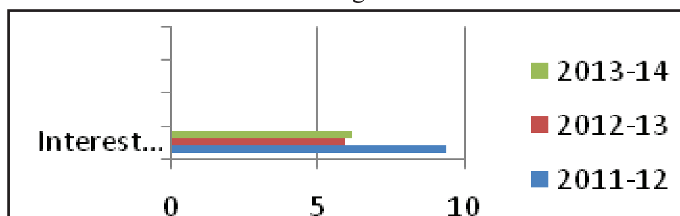
Interpretation: It indicates what portion of the total assets is financed by the owner's capital. This helps the creditors to know whether the capital or loans given them to the company are safe or not. Since the ratio of the company is very low in the three years, it shows poor long term solvency position of the company because of too much usage of debt or trade payables rather than equity to manage their daily operations. Thus it is a great risk to the creditors.

2. Debt Service/ Interest Coverage Ratio

Interest coverage ratio= Earnings before Interest and tax (EBIT)/ Interest charges

	2011-12	2012-13	2013-14
EBIT	6255.33	5677.94	6679.41
Interest charges	666.10	954.75	1076.08
Interest coverage ratio	9.39	5.94	6.21

Analysis: It is observed that the firm has 9.39, 5.94 and 6.21 for the year 2012, 2013 and 2014 respectively. It indicates the number of times interest is covered by the profits. If the ratio is 6 to 7 times then it is considered to be good.



Interpretation: It measures the firm's ability to make contractual payments. It is used to determine how easily a firm can pay interest on outstanding debts. The ratio in 2013 is low; this indicates that the firm is not able to cover the fixed interest liability of the firm. Hence the company is poor in the interest coverage in the year 2013.

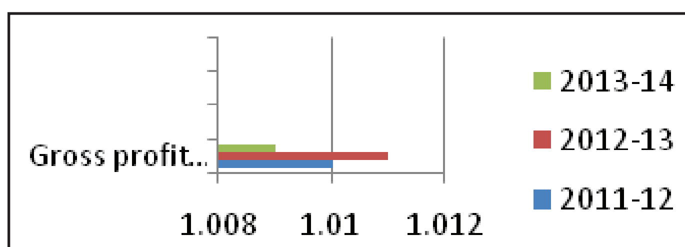
D. Profitability Ratios

1. Gross Profit Ratio

Gross Profit ratio=Gross profit/Net sales

	2011-12	2012-13	2013-14
Gross Profit	53737.78	52195.70	57163.85
Net sales	53170.52	51610.96	56598.92
Gross Profit Ratio	1.010	1.011	1.009

Analysis: It can be inferred that the firm has a gross profit of 1.010, 1.011 and 1.009 for the year 2012, 2013 & 2014 respectively. This ratio shows the relationship of gross profit to net sales and is represented as a percentage. Higher the ratio better is the result.



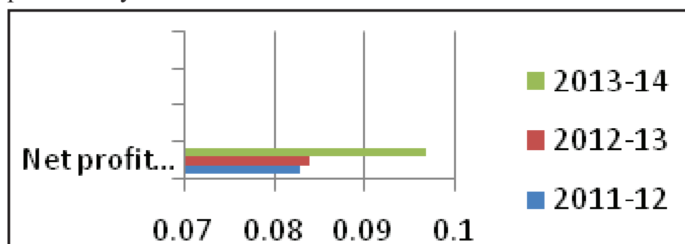
Interpretation: Gross profit margin measures the percentage of each sales rupee remaining after the firm has paid for his goods. The ratio of the company is not good which indicates the efficiency with which the company is producing its products. L&T is unable to maintain good distribution and manufacturing efficiency during its production process. This shows that the company has a poor profitability position, probably due to the fact that the industry is facing major problems due to high input cost, changing government policies and other political conditions in the economy.

2. Net Profit Ratio

Net Profit Ratio=Net Profit/Net sales

	2011-12	2012-13	2013-14
Net Profit	4456.50	4384.49	5493.13
Net sales	53170.52	51610.96	56598.92
Net Profit Ratio	0.083	0.084	0.097

Analysis: It is seen that the firm has a net profit ratio of 0.083, 0.084 and 0.097 for the year 2012, 2013 and 2014 respectively. It establishes a relationship between net profits and indicates the efficiency of management. Higher the ratio better is the profitability.



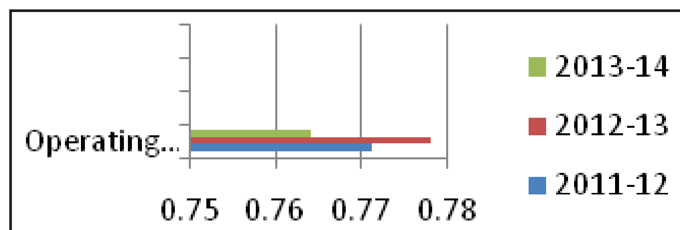
Interpretation: The net profit margin measures the percentage of sales rupee remaining after all the costs and expenses including interest and taxes have been deducted. It is an indication of how effective the company is at cost control. Since the ratio is low, the company's performance has come down. Hence it shows that the company was less efficient in converting sales into actual profits.

3. Operating Ratio

Operating ratio=Operating cost/Net sales

	2011-12	2012-13	2013-14
Operating cost	41020.18	40204.83	43346.45
Net sales	53170.52	51610.96	56598.92
Operating Ratio	0.771	0.778	0.764

Analysis: It is observed that the firm has operating ratio of 0.771, 0.778 and 0.764 for the year 2012, 2013 & 2014 respectively. It indicates the percentage of net sales that is consumed by operating cost. Higher the ratio the less favorable it is.



Interpretation: This ratio indicates the percentage of net sales that is consumed by operating Cost, it is favorable that the ratio should remain low but in the year 2013 the ratio is comparatively high, yet the company has managed to reduce the same in the year 2014 because of increased sales.

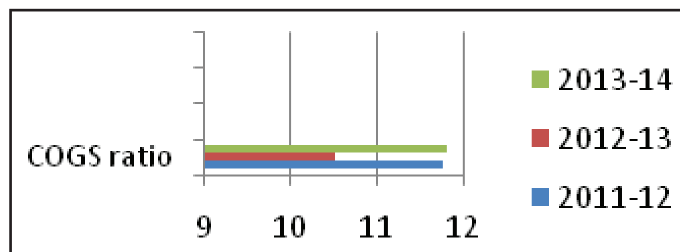
E. Expenses Ratio

1. Cost of Goods Sold Ratio

Cost of Goods sold ratio=Cost of goods sold (COGS)/ Net sales

	2011-12	2012-13	2013-14
COGS	625817.02	542947.29	668499.24
Net sales	53170.52	51610.96	56598.92
COGS Ratio	11.77	10.52	11.81

Analysis: It is inferred that the COGS ratio of the firm is 11.77, 10.52 & 11.81 for the year 2012, 2013 and 2014. It shows the amount of net sales consumed by cost involved until goods are sold.



Interpretation: This ratio indicates the relationship of various expenses to net sales, it is favorable if the ratio is lower which indicates greater profitability and vice versa in case of this company it had a high % of ratio compared to the 2013 in 2012 and 2014 but the company is trying to reduce its direct expenses which gives a good sign of more profitability.

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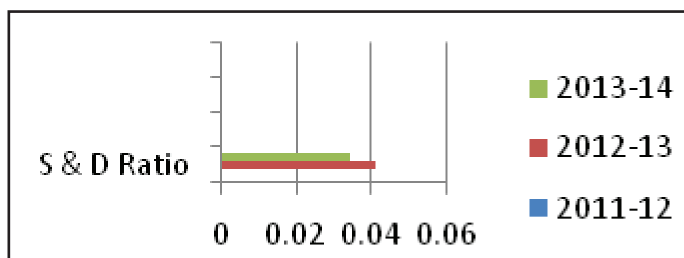
2. Selling & Distribution Expenses Ratio

Selling & Distribution expenses ratio=Selling & Distribution (S & D) Expenses/Net sales

	2011-12	2012-13	2013-14
COGS		2085.66	1932.03
Net sales	53170.52	51610.96	56598.92
COGS Ratio		0.041	0.034

Analysis: It can be seen that the firm has 0.041 and 0.034 of selling and distribution ratio expenses. It indicates the amount consumed of net sales for selling and distribution expenses. Lower the ratio better it is for the firm.



Interpretation: This ratio indicates the relationship of various expenses to net sales, it is favorable if the ratio is lower which indicates the greater profitability and vice versa in case of this ratio, company has a high percentage compared to other years in 2014 because of high sales, but the company is trying to reduce its direct expenses which gives a good sign of more profitability as it had low expenses in 2013.

V. Recommendations

- The company should try and increase its liquidity position so that it will be able to meet short term- debt obligations and has enough resources to pay its debt over next 12 months.
- The Operating cash flow should generate sufficient positive cash flow to maintain its operations and also to be able to meet its interest expenses.
- The company has good earning capacity by reducing cost of sales and should try to increase its Sales at a greater pace.
- The company has higher net income, to attract more investors and also to grow its operations the company needs to generate more EPS.
- As the company has performed very well in the year 2012 overall, the company needs to focus on future as the results of 2013 and 2014 are not good when compared to 2012.
- The company needs to focus and watch on its competitor's activities and strategies which help to make new strategies for the better and overall performance of the firm throughout the year.
- The company should follow a strict procedure in the sales and ratios techniques which would ensure a proper control on the funds.
- Overall the company is performing well and consistently on an average.

VI. Conclusion

Based on the overall study of the company's performance and position, the project study has been concluded as follows:

In this company every individual is committed; they plan on providing quality service to each and every company/customer regardless of the size of the business. The company treats everyone as individual and special.

To provide quality service the company has adopted modern technology. By adopting modern technology the company aims to deliver quality products and services for an effective long term relationship to the other company.

The financial performances shows the overall performance of the company is improving and can build a strong entity in the emerging market.

The employees and the workers of the company need to work hard to achieve their goals and meet the demand for the people in the markets to achieve good and high amount of profit.

From my research as indicated, the sales of LARSEN AND TOUBRO LTD. has been increasing over the years which show that the company is in a good position in the industry, thus it can be said that LARSEN AND TOUBRO LTD. has been working towards a progressive and healthy future.

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Mala.K.M received her BBM(Bachelor of Business Management) from Mount Carmel College, Autonomous, Bangalore University in 2012, securing the first rank and gold medal. She has received a post graduate degree in MBA(Master of Business Administration) from Pondicherry University in 2015. She has a corporate experience in the research and development wings, and is a research enthusiast. She is currently a full time research student in Bangalore. Her research interests include finance and stock markets, financial management of companies, Financial and accounting software and their need in SME's.

Dr. Raghu G Anand received his B.Com degree in Accounting and Taxation from MES College, Bangalore University in 1993, the M.Com degree in Costing and Taxation from Bangalore University in 1993, and the Ph.D. in Computerization of SME and the challenges in the dynamic scenario, from Golden State University UK/USA in 2005. He is the head of value addition department of Jain University – Center for Management Studies, Bangalore, where he is the interface for several international/chartered programs. His research interests include computerization of accounting, challenges faced, SAP and IFRS.