



Use financial ratios as a tool to evaluate performance efficiency

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Abstract

The subject of financial analysis is one of the important topics in the field of financial management and accounting Through which the management of the facility can diagnose the strengths and weaknesses in their internal environment and evaluate their financial and investment decisions and can be used as one of the important bases in determining their strategic options The importance of financial analysis has increased in recent decades due to several factors, including the high competition intensity between different economic projects , the increasing role played by the financial markets, and the tremendous development in information technology and its various uses, which requires increasing the importance of providing analytical tools and financial indicators appropriate to keep pace with the size and speed of the completion of various economic processes and the most used tools in financial analysis are the financial ratios. the research includes two chapters the first was devoted to the theoretical side while the second chapter devoted to the practical aspect of the research concluded with the necessary conclusions and recommendations.

Keywords : financial , ratios , tool ,evaluate , performance , efficiency



استخدام النسب المالية كأداة لتقييم كفاءة الأداء

ختم دخن حمزة

قسم التربية البدنية وعلوم الرياضة ، كلية التربية للبنات ،

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ملخص

يعد موضوع التحليل المالي من الموضوعات المهمة في مجال الإدارة المالية والمحاسبة والتي من خلالها يمكن لإدارة المنشأة تشخيص نقاط القوة والضعف في بيئتها الداخلية وتقييم قراراتها المالية والاستثمارية ويمكن استخدامها كأحد الأسس المهمة في تحديد خياراتهم الاستراتيجية: لقد ازدادت أهمية التحليل المالي في العقود الأخيرة بسبب عدة عوامل ، بما في ذلك كثافة المنافسة العالية بين المشاريع الاقتصادية المختلفة ، والدور المتزايد الذي تلعبه الأسواق المالية ، والتطور الهائل في تكنولوجيا المعلومات واستخداماته المتنوعة والتي تتطلب زيادة أهمية توفير الأدوات التحليلية والمؤشرات المالية المناسبة لمواكبة حجم وسرعة إنجاز العمليات الاقتصادية المختلفة وأكثر الأدوات المستخدمة في التحليل المالي هي النسب المالية. تضمن البحث فصلين ، الأول خصص للجانب النظري بينما خُصص الفصل الثاني للجانب العملي للبحث واختتم بالنتائج والتوصيات اللازمة.

الكلمات المفتاحية: المالية ، النسب ، الأداة ، التقييم ، الأداء ، الكفاءة

Research Methodology:

First: the issue of the research :

The data provided by the financial lists can not be used for the purposes of planning and evaluating the efficiency of performance without using one of the means of financial analysis, which is represented by using the financial ratios and comparing the financial lists of the current year with previous years, in which it enhances the detection of weaknesses and strength and achieving efficiency of performance.

Second: The hypothesis of research:

The use and analysis of financial ratios enhances the chances of reaching to an efficiency measurement of the Company's financial policy by comparing the financial ratios for the current year with those of previous years.

**Third: The aim of research**

The research aims at presenting a study represented by using the financial ratios for the purpose of evaluating performance efficiency.

Fourth: The importance of research

Most companies do not apply money management techniques. Therefore, it requires using financial analysis methods, including financial ratios for the purpose of planning and monitoring the efficiency of performance and to achieve the optimal use of available resources.

Fifth: Methods of data collection

The researcher adopted two methods of data collection

1. Official sources: All records of the company include the research sample.
- 2 - Oral interviews: in order to obtain some data not available in official sources.

the theoretical side**Performance assessment using financial ratios:**

1 - Financial analysis is considered one of the important tools in the business establishments and a basis of planning and control, which includes a detailed study of the data contained in the financial statements adopted by the project and the financial analysis by ratios is an important and fundamental means in the study of the financial position of the project in n light of the figures and data in its financial statements. The financial ratios were divided into a number of totals, each of which reflects specific aspects of the project. Some reflect the liquidity position of the enterprise, particularly the possibility of making long-term liabilities and the other reflects the efficiency of managing current and fixed conditions, which measures the degree of indebtedness of the project and the possibility of borrowing.

First: - types of Comparative financial analysis

There are two types of analysis used when comparing ratios

1-cross-sectional



2 -Time series analysis

1-CROSS-SECTIONAL ANALYSIS:

This analysis includes comparing the financial ratios of a number of different establishments at a specific time of year. The model establishments that seek to increase their share in the market are tasked with comparing their performance with the performance of other establishments in the same sector, and since the financial statements of the competing establishments are available and can be obtained and analyzed, there for ,the establishments usually compare their ratios with the financial ratios of the main competitors or the competing establishments that the facility wishes to compete with or surpass. This type of analysis is called BENCH MARKING and has become very common, By comparing the financial ratios of the facility with another facility or a number of identified facilities, bench marking can identify the strengths and weaknesses of the facility . . Another common type of comparison is the comparison with the industrial standard, which compares a set of ratios with the industrial standard, where this can reveal any deviation from the normal rate so it is very important to verify deviations from the standard of goods, whether negative or positive .

2- TIME SERIES ANALYSIS

This type of analysis evaluates the performance of the same facility over time by comparing the current performance with the past performance, allowing the facility to determine whether it is developing as planned or not, Trend indicators can be developed by comparing performance for a number of years and these indicators benefit enterprises in planning their future operations.

¹Alsamarraee , Adnan Hashim , financial management, Dar Zahran for publishing,Aman , 1997 .

²Lawrence J.Gitman , “ Principles of Managerial Finance “, Person Education Inc . 2003 ,p50



Second: Cautions About Ratio Analysis

There are some determinants that must be considered and taken into consideration when analyzing using financial ratios they are:

1- A single financial ratio can not be used to judge the performance of an enterprise because it does not provide effective information about the facility's position – thus a set of ratios must be used to judge the facility. However, if the financial analysis relates only to a particular part or an aspect of the financial position, one or two may be sufficient to give a picture of the situation

2-When comparing financial statements, they should be used by a particular date. If not, the comparison may lead to erroneous decisions and results.

3 - When performing ratios analysis, it is best to use audited financial statements because the information contained in unaudited financial statements may not reflect the true financial position of the facility.

4-When comparing the financial ratios of a particular facility with the financial ratios of another, it should be for the same period to limit the impact of economic inflation on the results.

Third: Categories of financial ratios

Financial ratios are classified into five groups

1: Liquidity ratios group

2: profitability ratios group

3: Activity ratios group

4: debt ratios group

5: Market ratios group

Where liquidity, activity and debt ratios measure risk, while measuring the ratios of profitability and market returns and since the period of liquidity and activity and profitability became more important because it provides us with information about the facility useful in short-term operations Each group of major groups includes



several types of financial ratios which reflect certain indicators that can be used in the analysis of the financial situation of the establishment and decision-making.

³previous source , Lawrence J. Gitman , p51

⁴Abud Alhadi , Mohamad Saaed , Financial Management, Investment and Finance Financial Analysis, Dar Hamel for publishing , Aman , 1999, p73

⁵Scott Besley And Eugene F . Brigham , “ Essentials of Managerial Finance “ .

First: liquidity ratios group:

Financial Liquidity of the facility can be measured by its ability to meet short-term liabilities as they mature and the major liquidity metrics are:

1-current Ratio

2-Quick Ratio

3-net working capital

1-Current Ratio:

Financial Liquidity of the facility can be measured by its ability to meet short-term liabilities as they mature therefore, it indicates the margin of safety through the ability of current assets to cover the current liabilities and the increase in the ratio is a good indicator of the liquidity of the company and is calculated as follows:

$$\text{Current Ratio} = \frac{\text{Total Current Assets}}{\text{Total current liabilities}}$$

1-we can notice that the ratio scale is (once) which means the number of times the current liabilities are covered with the margin of safety. If the trading ratio is equal to 2, it is described as acceptable but the acceptance of this value depends on the type of industry in which the company operates.



2. Quick liquidity ratio

This ratio is measured by dividing the current assets minus the inventory on the current liabilities and by the following rule:

$$\text{Quick liquidity ratio} = \frac{\text{total current assets} - \text{inventory}}{\text{total liabilities}}$$

The reason for the exclusion of stocks when calculating the liquidity ratio is due to two factors:

A- There are several types of inventory that can not be sold easily because they are complementary to other varieties.

B- Inventory is usually sold on term (or is converted into commodities ready for sale and then sold with debt) this means that it turns into debited pacts before it turns into cash and this percentage can be applied in Industrial and Commercial Companies

As for companies that do not deal with stocks (do not have stock), the ratio of liquidity is fast and equal to the proportion of trading as in the case of the banking sector.

Dryden Press 2000, p95

⁶ Stanley B. Bock And Geoffery A. Hirt “ Foundation of Financial

Management “ Micheal W. Junior , 1997 , p 59

⁷ Timothy R. Mayes And Todd M. Shank , ” Financial Analysis “ Harcourt Inc .2001 , p89

⁸ Eugene F. Brigham , Louis C . Gapenski And Phillip R . Daves , “ Intermediate Financial Management “ Dryden Press , 1999, p74

3 - Net working capital

Net capital can be measured using the following formula:



$$\text{Net working capital} = \frac{\text{Current assets}}{\text{Current liabilities}}$$

This measurement is useful for the internal observation purposes of the company and when obtaining a long-term debt, the loan agreement usually includes a minimum amount of working capital net that the facility must maintain. This condition protects the creditors by obliging the company to maintain good liquidity.

Second: - profitability ratios group:

There are more profitable metrics, which generally measure the profitability of the company taking into account the level of sales, volume of assets, owners' investments and equity and there is no doubt that when the company does not achieve profits, creditors and shareholders become concerned about the future of the company and about the recovery of their money so the creditor owners and the management of the company are interested in increasing profits as it protects the company from the risk of bankruptcy and one of the tools commonly used to assess the profitability of the company is Common-Size Income Statement.

Or relationship of elements ratios of the income list in sales and there is more than the proportion of profitability emanating from this group and the most used are:

1 - Gross of Profit Ratio:

This indicator measures the ratio of total profit to sales and the higher the percentage the better for the company

$$\text{Gross profit ratio} = \frac{\text{Gross profit}}{\text{Net sales}}$$

2: - Net profit ratio

This percentage measures the remaining amount of each JD of sales (as a percentage) after paying all costs including interest and taxes⁽¹⁰⁾. This percentage is a common and important measure to measure the success of the company in its operations, taking into account the consideration of the return on sales. The ratio varies from one industry to another and is calculated as follows

$$\text{Net Profit Ratio} = \frac{\text{Net profit}}{\text{Net sales}}$$



⁹ 2003: 61 , Gitman , previous source

¹⁰ ALnaaemee , Adnan taieh , Analysis and Financial Planning, Dar Al - Bazdari Scientific Publishing and Distribution , Jordan , 2008 , p 70

The applied approach to the use of financial ratios in evaluating performance efficiency

First: - Research sample:

The Industrial Bank is considered one of the specialized banks in Iraq. It was established in 1935 as an industrial agricultural bank and then became independent in 1940. It is currently practicing in accordance with the provisions of the Public Companies Law No. 22 of 1977, as amended, laws, regulations and instructions which are still valid. In a manner that does not interfere with and aims at growing and developing the national industry in the private, mixed and cooperative sectors within the framework of the economic development plan through the granting of loans of all types and bank facilities in addition to the business of commercial banking and mediation in the sale and purchase of financial securities based on the decision of the Revolution Command Council (dissolved) No. 1 on 14.1.1996

Second: the results of calculating the financial ratios of the bank

We have been relying on the final accounts for the five fiscal years ended December 31, 2009.

To prepare a table of the main figures contained in the final accounts mentioned above for the purpose of adopting them to calculate the financial ratios as explained in Table (1) while (6-2) were allocated for the purposes of calculating the different financial ratios. where as table (7) was allocated to present the results.

Calculating financial ratios for the ended five past years 31/December /2009



Table no.(1) A comparison of the main figures contained in the final accounts for the five years ended December 31, 2009 for the Industrial Bank / General Company Baghdad

Account name	Year 2005 Thousand dinars	Year 2006 Thousand dinars	Year 2007 Thousand dinars	Year 2008 Thousand dinars	Year 2009 Thousand dinars
Total current assets	99769443	105316401	156337105	197489013	178344400
Total current liabilities	68267462	72206689	122724831	163535647	145064200
Gross profit	1343587	2977668	5740049	3093621	642715
Net profit	379655	1117870	1261536	1475803	265489
Total revenue	4987068	7099730	10361901	8233231	5310001

1- The table prepared by the researcher

2- The source / final accounts of the bank for the five years ended December 31, 2009

3. The total revenue of the bank consists of (revenues from banking operations and investment income) corresponding to the net sales revenues of the industrial companies. For the purpose of calculating the financial ratios, a table was prepared for the results of calculating each ratio in which the percentage of trading was calculated as shown in Table (2).

Table (2) The trading ratio for the five years ended December 31, 2009

Account name	Year 2005 Thousand dinars	Year 2006 Thousand dinars	Year 2007 Thousand dinars	Year 2008 Thousand dinars	Year 2009 Thousand dinars
Total current assets	99769443	105316401	156337105	197489013	178344400
Total of current	68267462	72206689	122724831	163535647	145064200
	1.461	1.459	1.274	1.208	1.229



liabilities					
= Trading ratio / time	99769443	105316401	156337105	197489013	178344400
	68267462	72206689	122724831	163535647	145064200

$$* \text{Trading ratio} = \frac{\text{Total current assets}}{\text{Total current liabilities}}$$

1- The table prepared by the researcher

2- The source / final accounts of the bank for the five ended years December 31, 2009

The calculation of net capital is reflected in Table (3)

Table [3] Net working capital for the five ended years December 31,

Industrial Bank / General Company – Baghdad

Details	Year 2005 Thousand dinars	Year 2006 Thousand dinars	Year 2007 Thousand dinars	Year 2008 Thousand dinars	Year 2009 Thousand dinars
Total current assets	99769443	105316401	156337105	197489013	178344400
Total of current liabilities	68267462	72206689	122724831	163535647	145064200
= Trading ratio / time	31501981	33109712	33612274	33953366	33280200

$$* \text{Net working capital} = \text{Total current assets} - \text{Total current liabilities}$$

1. Table of the researcher's preparation

2. The source / final accounts of the bank for the five years ended December 31, 2009.



Table (4) Ratio of total profit for the five years ended December 31, 2009

Industrial Bank / General Company / Baghdad

Details	Year 2005 Thousand dinars	Year 2006 Thousand dinars	Year 2007 Thousand dinars	Year 2008 Thousand dinars	Year 2009 Thousand dinars
Gross profit	1343587	2977668	5740049	3093621	642715
Total revenue	4987068	7099730	10361901	8233231	5310001
Ratio of gross profit%	26.94	41.94	55.395	37.575	12.104

$$* \text{Ratio of total profit} = \frac{\text{Gross profit}}{\text{Total revenue}}$$

1. Table of the researcher's preparation

2. The source / final accounts of the bank for the five years ended December 31, 2009.

The ratio of the total profit was also calculated as shown in Table [5] the percentage of total profit and its relation to the expenses of the current activity and total revenues for the five years ended December 31, 2009

Details	Year 2005 Thousand dinars	Year 2006 Thousand dinars	Year 2007 Thousand dinars	Year 2008 Thousand dinars	Year 2009 Thousand dinars
Total Revenues (Thousand dinars)	4987068	7099730	10361901	8233231	5310001
Current - activity expenses (thousand dinars)	3643481	4122062	4621852	5139610	4667286

1. Table of the researcher's preparation



2. The source / final accounts of the bank for the five years ended December 31, 2009.

The net profit ratio was also calculated in Table (6)

Table [6] Net profit for the five years ended December 31, 2009

Industrial Bank / Baghdad General Company

Details	Year 2005 Thousand dinars	Year 2006 Thousand dinars	Year 2007 Thousand dinars	Year 2008 Thousand dinars	Year 2009 Thousand dinars
Net profit	379655	1117870	1261536	1475803	265489
Total revenue	4987068	7099730	10361901	8233231	5310001
X Net profit ratio	7.613	15.745	12.175	17.925	5

$$* \text{Net Profit Ratio} = \frac{\text{Net Profit}}{\text{Total Revenue}}$$

1. Table of the researcher's preparation

2. The source / final accounts of the bank for the five years ended December 31, 2009.

The results obtained from the ratios were also consolidated in Table (7). Table of results for the five years ended December 31, 2009

Table (7): Table of results of calculating the financial ratios for the five years ended December 31, 2009

Industrial Bank / Public Company _ Baghdad

Financial ratio	Unit of measurement	Year 2005	Year 2006	change	Year 2007	change	Year 2008	Change	Year 2009	change	Notes
trade rate	Once	1.461	1.459	0.0014 (1.274	(0.128)	1.208	(0.173)	1.229	(0.153)	Decrease in ratio
Quick Ratio	Once	1.461	1.459	0.0014 (1.274	(0.128)	1.208	(0.173)	1.229	(0.153)	Decrease in ratio
Percenta	%	26.94	41.9	15	55.39	28.455	37.57	10.635	12.10	14.863	High in



ge of total profit			4		5		5		4		proportion
Net profit ratio	%	7.613	15.745	8.135	12.175	5.132	17.925	10.312	5	(2.613)	A decrease in the percentage in 2009
Net working capital	Thousand dinar	19813150	33109712	1607731	33612274	2110293	33953366	2451385	33280200		High net working capital

Notes :

1. Table of the researcher's preparation.
- 2- The source / final accounts as in the annex in Table 1_8 of the Bank for the last five years ending 31 December 2009 with the adoption of 2005 as the base year.
- 3- The rest of the financial ratios were not adopted due to their non-conformity with the nature of the work of the Industrial Bank
- 4- The trading ratio = the rapid percentage due to the lack of inventory

Third: Analyzing the results of using financial ratios

Third: Analysis of the results of using financial ratios

For the purposes of analyzing the results of the use of financial ratios, a set of tables (1_7) were presented in the research side of the applied side. The results of the analysis in light of this were as follows:

First: Analysis of the trading ratio

The general trend of the bank's trading ratio is a continuous decline, with a ratio of 1.461% ,1.459%,1.274%,1.208%,1.229%

(Once) for the five years ended December 31, 2009

The decrease is due to:

The increase in current liabilities compared to the basic rate which reached 145064.200,163535.647,122724.831,72206.689.68267.462 (thousand dinars) for the last five years 31 December 2009



The increase in current liabilities compared to the base year was as follows:

57.77%, 79.77%, 139.55%, 112.48% and for the years 2009, 2008 and 2007 respectively

As shown in Table (1)

B- Despite the increase in the current assets compared to the base year, which reached 17834440,194,489,013,156337105,105316401,99769443(thousand dinars) for the last five years ended 31 December/2009

The increase in current assets for the base year was as follows: 5.55%, 58.70%, 97.95%, 78.76% for the years 2009, 2008 and 2007 respectively, as shown in Table (1). However, the increase In current assets and the accompanying increase in current liabilities has led to a decrease in the trading rate.

The treatment requires an increase in assets against a reduction in current liabilities and this will increase the ratio of future trading in order to enhance the ability of the financial exchange.

Analyzing ratio of total profit:

Through the results of the table (4) Table of calculation of the total profit for the last five years ended 31/12/2009 we clarify the following:

- 1- The general trend of the ratio of total profit in the bank is increasing and compared to the base year, where the percentage was 26.74%, 41.94%, 55.395% 37.575% for the four years ended 31/12/2008, the ratio for 2009 was 12.104%, which is lower compared to the base year and in the general trend, it is due to the following:

A-The clear increase in expenses of the current activity of the bank (banking expenses, depreciation and administrative expenses) reached 4667,286,5139,610,462,182,412,202,364,348 thousand dinars for the five years ended December 31, 2009.

As shown in Table (5). The increase compared to the base year is as follows: 13.14%, 26.85%, 41.06% and 28.10% for the years 2008,2007,2006. It is also



increasing with the general trend line for the years of the research sample except 2008, Which was characterized by a decline.

The results of Table (5) show the table of the calculation of the total profit and the relation of the expenses of the current activity and the total revenues.

B-The clear increase in the total annual revenues ended on 31 December 2009 compared to the base year, except for the decrease in the total revenues achieved for the year 2008 and for the year 2009 compared to the general trend line of revenues for the years of the research sample where the total revenue as shown in Table (5) is the table of the calculation of the total profit and its relation to the expenses of the current activity and the total revenues. The revenues amounted to 53,100,008,823,321,1036,191,7099,730,498,706 thousand dinars for the five years ended December 31, 2009 .The increase in total revenues for the base year is as follows:

6.4%, 65.1%, 107.78% and 42.36% for the years 2009, 2008 and 2007, where we notice that the percentage is increasing significantly with the general trend line of total revenues except for 2009, where the increase rate is not in line with the general trend line.

Based on points (A and B) mentioned above, the impact of these clear and direct points on the years 2009 and 2008 is shown. This resulted in a clear decrease in the total profit as a result of the increase in the current activity expenses by a clear decrease in total revenues compared with the general trend line of revenues during the years of sample search .

Third: Analysis of net profit ratio:

Based on the data of Table (6) The table of net profit ratio for the five years ended 31 December 2009 is as follows:

1-The net profit for the five years ended 31 December 2009 is as follows: 265489,1476803,1261536,1117870,379655 (thousand dinars)

Note that net profit compared to the base year was on a continuous rise except for the year 2009, which was characterized by a clear decrease in the net profit as the increase compared to the base year according to the following



percentages for the years 2008,2007,2006 respectively 194.44%, 232.28%, 288.72% 2009 was characterized by a decrease of (30%) from the base year.

2- Net profit reached 7.613%, 15.746%, 12.175% and 17.925% for the five years ended 31 December 2009. The analysis showed the slight increase in net profit during the four years of the research sample compared to the base year it is also in line With the general trend line of the ratio except for the year 2009, which showed a clear decline compared to the base year and the general trend line where the net profit was 5%. The decrease in the net profit during 2009 is due to the decrease in total revenues.

During the two years above compared to the general trend line. Total revenues for the five years ended 31 December 2009 were as follows:

5310001,8233231,10361901,7099730,4987068 ,

which is in constant increase except for the year 2009, which was characterized by a clear decrease in the total amount of revenues. This resulted in a decrease in the net profit and net profit for 2009 in particular. The net profit amounted to JD (265,489) with a decrease by 30% from the base year while the net profit ratio was 5%, which is a decrease from the base year 2.613%.

Conclusions:

The research hypothesis is achieved by not using the industrial bank for financial ratios. The low financial ratios listed in table (7) the table of using the financial ratios and the table of analysis of ratios for the five years ended 31 December 2009 which require reconsideration of the use of these ratios in the future by the bank.

2 - Table (7) results table of the use of financial ratios for the five years ended 31 December 2009 and analysis of the results of financial ratios show: -

A) A clear decline in the ratio of trading and the rapid rate, due to the increase in current liabilities during the five years ended.

(B) The clear decline in the percentage of total profit for the year 2009 reaching 12.104%.



(C) The clear decline in the net profit for 2009, which reached 5%.

3-through analyzing the financial ratios and relying on the final accounts for the five years ended 31 December 2009, the decrease in financial ratios was attributed to:

A) There is a large increase in current activity expenses, especially administrative expenses for the five years.

(B) A decrease in total revenues (investment income, income from banking operations) for 2009.

C- Despite the increase in the capital of the Industrial Bank, this increase did not lead to an increase in profits which commensurate with the size of the increase in capital. This subject requires the management of the bank to develop plans and policies that will increase revenues and maximize profits.

Recommendations:

Through the findings of the researchers recommend the following:

1 - Use the financial ratios in the research to achieve an assessment of the efficiency of performance in the Industrial Bank

Studying all ways to increase investment revenues and revenues of banking operations in order to achieve better profitability for the bank as well as studying the reduction of expenses related to these revenues.

2 - Study and develop a new policy for the granting of loans for the industrial sector and increase investment opportunities and develop procedures for banking operations in the coming period to achieve the benefits to the bank and encourage the national industry after the stability of the security situation.

3 - Evaluation of a study by the Industrial Bank for the purpose of establishing a mechanism for the protection of national products to support of the Iraqi economy and in cooperation with the Ministry of Industry and to the benefit of both the industrial and the bank sectors.

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