PROJECT UNDERDOGS FOUNDER LIBRARY · MONEY BASICS · M-05

READING A BALANCE SHEET

What your business owns, what it owes, and what's left for you, on a single day.

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AT A GLANCE

- A **balance sheet** is a snapshot of the business on one date. It shows **assets** (what you own), **liabilities** (what you owe), and **owner's equity** (what's left for the owners).
- It always balances: **Assets = Liabilities + Owner's equity**.
- Lenders use it to see whether you can handle more debt. Investors use it to see what they'd be buying a share of.

Why it matters

Your profit and loss statement shows how you did over time. Your balance sheet shows where you stand today. A business can be profitable but carry too much debt, or have plenty of cash but owe most of it to suppliers. The balance sheet shows those risks.

How it works

Section	What's in it	Examples
Assets	Things the business owns that have value	Cash, money customers owe you, inventory, equipment, vehicles
Liabilities	Money the business owes	Credit card balances, bills you haven't paid, loans
Owner's equity	What's left for the owners	Money owners put in, plus profits kept in the business, minus draws

Assets and liabilities are split into **current** (turning into cash or due within a year) and **long-term** (longer than a year).

Assets = Liabilities + Owner's equity

Example: Rosa's Cleaning Co., December 31

Assets	Amount
Cash in the bank	$12,500
Accounts receivable (customers who owe her)	$3,000
Current assets	**$15,500**
Van and equipment	$22,000
Total assets	**$37,500**

Liabilities and equity	Amount
Business credit card	$1,500
Current liabilities	**$1,500**
Van loan	$14,000
Total liabilities	**$15,500**
Owner's equity	**$22,000**
Total liabilities and equity	**$37,500**

What Rosa learns

- **She can pay her short-term bills.** Her current assets of $15,500 are more than 10 times her current liabilities of $1,500.
- **Her debt is modest.** She owes $15,500, compared with $22,000 in equity.
- **It balances.** $15,500 owed plus $22,000 equity equals $37,500 in assets.

> KEY POINT
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> Two quick checks lenders often use: **current assets divided by current liabilities** (above 1.0 means you can cover short-term bills), and **total liabilities divided by owner's equity** (lower means less debt compared with what you own).

Step by step: reading your own

1. Run the balance sheet for the last day of last month.
2. Check that assets equal liabilities plus equity. If not, there's a bookkeeping error.
3. Compare current assets with current liabilities.
4. Look at how much you owe in total and whether it's growing.
5. Check that the cash on the report matches your bank statement.

Common mistakes

- **Ignoring it entirely.** Many owners only look at the P&L.
- **Not recording loans.** Every loan belongs here, including loans from family.
- **Letting "accounts receivable" grow.** Money customers owe you isn't cash yet. Chase it.
- **Mixing in personal assets.** Your home or personal car don't belong on the business balance sheet unless the business owns them.

Your checklist

- ☐ Run your balance sheet for last month-end
- ☐ Confirm it balances
- ☐ Calculate current assets divided by current liabilities
- ☐ List every loan and check it's recorded
- ☐ Follow up on any customer payments more than 30 days late

Key words, explained

Word	What it means
Asset	Something the business owns that has value.
Liability	Something the business owes.
Owner's equity	What's left for owners after subtracting what's owed.
Accounts receivable	Money customers owe you.
Accounts payable	Money you owe suppliers.
Current	Due or turning into cash within a year.

Where to go next

- **M-04 Reading a Profit and Loss Statement**
- **M-06 Cash Flow: Why Profitable Businesses Still Run Out of Money**
- **M-17 Profit and Loss and Balance Sheet Templates**

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