MACHAKOS UNIVERSITY

University Examinations for 2018/2019 Academic Year

SCHOOL OF BUSINESS AND ECONOMICS

DEPARTMENT OF BANKING, ACCOUNTING & FINANCE

FOURTH YEAR SPECIAL/SUPPLEMENTARY EXAMINATION FOR

BACHELOR OF ECONOMICS

BACHELOR OF COMMERCE

BAC 407: FINANCIAL STATEMENT ANALYSIS

DATE: 26/7/2019 **TIME: 2.00-4.00 PM**

INSTRUCTIONS: Attempt Question One and any other Two Questions

1. a) In stock valuation, state two ways in which errors may occur if statements are not audited and not necesarrily prepared in accordance with IFRS or GAAP (2 marks)

b) When collecting data for financial statements analysis how can you conclude that financial statements have been distorted. (4 marks)

c) A company is capitalised as follows:

Sh. 600,000 7% preference shares of sh. 1 each

Sh. 1,600,000 7% ordinarysharesof sh. 1 each

The following information is relevant for the year just ended dec 2017.

Profits after taxation @ 40% sh. 42,000

Ordinary dividend paid 20 %

Market price of ordinary share sh. 4

Required.

(i) The divdned yeild onordianry shaes (2 marks)

(ii) Divident covers (4 marks)

(iii) The earnngs yeld (2 marks)

(iv) The price earnings ratio (2 marks)

(d) Distingish between on operating lease and a financing lease (2 marks)

(e) When analyzing finacial statements, what should you confirm about management systems on (3 marks)

(i) Good debtors

(ii) Bad debts

(iii)Douubtful debts

(g) State and briefly explain three tools used for financial analysis (8 marks)

2. (a) The following is a summarised balance sheet at XYZ Co. Ltd. As of Dec 31st 2014 and 1st Dec 2015.

Balance sheet of XYZ Ltd.

	31st Dec 2015	**31st Dec 2014**
Assets	**Sh "000"**	**Sh "000"**
Plant and equipment	2000	1030
Land and buildings	1000	1000
Short tem investments	560	600
Sundry debtors	2200	2500
Inventories	1500	1300
Interest receivable	100	60
Cash in hand	300	500
Cash at bank	1290	780
	8950	**7770**
Liabilities	**Sh "000"**	**Sh "000"**
Contributed capital	2600	2200
Reserve and surplus	660	100
15% debentures	2000	1800
Deffered tax liability	600	500
Sundry creditors	400	600
Wages outstanding	40	20

Income Tax Payable	400	450
Accumulated depreciation on		
Plant and equipment	900	800
Land and buildings	600	100
Provision for dividend	800	800
	8,950	**7,770**

Income statement for XYZ Ktd for the year ended 31/12/2015

	Sh "000"	
Sales revenue	45,000	
Less: cost of goods sold	**(38,920)**	
Gross profit	6,580	
Less: **Expenses**		
Depreciation	570	
Selling and administration expenses	3200	
Interest expense	300	(4070)
		2510
AAdd:Income from tax expenses		80
Dividend income		100
Insurance settlement received		10
Profit on sale of equipment		20
Profit before tax		2720
Less: Income tax expenses		(600)
Net profit	2120	

Additional information

a) 15 % of sh.200 was redeemed during Year 2015
b) Equipment costing Sh.500 having an accumulated depreciation of sh.420 was sold for sh.100

c) During the year 2015 sh 1560 (including interim dividend of sh.760) was distributed as divindends

Required:

Prepare a cash flow statement as required under IAS7 using indirect method (15 marks)

b) when doing financial statement analysis, how can you conclude the financial statement have been compromised (5 marks)

QUESTION THREE

The following are the financial statements of Kakamega Ltd. For the year ended 31st December, 2005.

Statement of Financial Position as at 31st December,2005:

	Sh.		Sh.
Cash.	480,000	Trade creditors	860,000
Debtors	640,000	Short-term notes Payable	840,000
Stock	2,080,000	Long-term debt	1,600,000
Equipment	1,600,000	Shareholders' equity	1,500.000
	4,800,000		4,800,000

Income Statement for the year ended 31st December,2005

	Sh.	Sh.
Sales		6,000,000
Less: Cost of sales		3,600,000
Gross profit		2,400,000
Deduct: Selling expenses	600,000	
Administrative& gen. Expenses	1,120,000	
Interest charges	235.600	
Profit before taxation	444,400	
Taxation	177,760	
Net profit	266,640	

The following industry ratios are also provided to you:

Industry Averages

Current ratio	2.5 times
Acid test ratio	1.1 times
Stock turnover ratio	2.4 times
Total assets turnover ratio	1.4 times
Times interest earned ratio	3.5 times
Net profit margin	4.0 %
Return on investment	5.6 %
Total assets to shareholders equity	3.0 %

Return on shareholders equity 16.8 %

Required:

a) Calculate the ratios shown above for Kakamega Ltd.(14 marks)

b) Comment upon the following about Kakamega Ltd averages(6 marks)

i) Liquidity position

ii) Financial risk

iii)Overall performance

QUESTION FOUR (20 MARKS)

The following information relates to Laki Manufacturing Company for the month of September 2013.

Opening stock were 500 units at £ 100 each

Purchases	Sales
6th Sep 100 units @ 105 each	9th Sep 100 units @ £ 108 each
20th Sep 600 @ £ 110 each	15th Sep 300 units @ £ 110 each
21st Sep 400 @ £ 108 each	22nd Sep 400 units @ £ 106 each
23rd Sep 1000 units @ £ 112 each	24th Sep 250 units @ 115 each
30th Sep 200 units @ 110 each	28th Sep 200units @ £ 114 each
	29th Sep 200 units @ £116 each

Required

i. Record the above transactions assuming the business uses continuous records under LIFO c and weighted average methods. (12 marks)

ii. Using the two methods above, prove that different stock valuation methods have different impact on profit. (5 marks)

iii. As per the international financial reporting standard No 2 (MRS 2), explain how the stocks are valued. (3 marks)

QUESTION FIVE

a) one of the major concerns in amalysis of financial statements is adentifying whether the institution has any asset that ia potentially impairred.explain how you Can identify a potentially impairred asset (5 marks)

b) Explain the statement that different stock valuation methods result to a different value of profit. Give atleast one example . (5 marks).

c) Explain the following terminologies as used in the preparation of cashflow statements.Give examples in each case. (10 marks)

- Cash flow from operating activities
- Cashflow from investing activities
- Cash flow from financing activities.