



(Knowledge for Development)

# **KIBABII UNIVERSITY**

**UNIVERSITY EXAMINATIONS**

**2021 / 2022 ACADEMIC YEAR**

**THIRD YEAR SECOND SEMESTER**

**MAIN EXAMINATION**

**FOR THE DEGREE OF BACHELOR OF COMMERCE**

**COURSE CODE: BCF321 / BBF322**

**COURSE TITLE: FINANCIAL STATEMENT ANALYSIS**

**DATE: 31<sup>ST</sup> AUGUST, 2022      TIME: 9.00AM - 11.00AM**

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## **INSTRUCTIONS TO CANDIDATES**

1. Answer Question One in Section A and Any other TWO (2) Questions in Section B
2. Question one carries 30 marks and each of the other two questions carry 20 marks each.

**TIME: 2 Hours**

**KIBU observes ZERO tolerance to examination cheating**

**This Paper Consists of 6 Printed Pages. Please Turn Over.**

## SECTION A

### QUESTION ONE (COMPULSORY)

- a) Accounting information is produced in terms of financial statements. This information aids the decision-making process to various interested parties. Justify looking at FIVE users why Financial statements are important (10 marks)
- b) Evaluate five objectives of financial statement analysis (10marks)
- c) Justify the importance of common size analysis (5marks)
- d) Examine some of the indicators of financial distress. (5 Marks).

## SECTION B

### QUESTION TWO

The following Financial statement has been extracted from the books of ABC Ltd and XYZ Ltd for the year ended 31/12/2005.

Balance sheet as at 31/12/2005

	Ksh. "000"	Ksh."000"
<b>Assets</b>	<b>ABC LTD</b>	<b>XYZ LTD</b>
Cash and marketable securities	21.2	216.5
Debtors	37.63	285.78
Inventories	112.89	298.77
Other current assets	6.36	97.26
Plant property and equipment	340.26	3,204.20
Other assets	11.66	229.49
<b>Total assets</b>	<b>530.00</b>	<b>4,330.00</b>
<b>Liabilities and Equity</b>		
Accounts payable	84.27	329.08
Other current liabilities	53.00	394.03
Long-term debt	95.40	961.26
Preferred credit	58.30	571.56
Preference shareholders	-	307.43
Shareholders' equity	293.03	1,766.64
<b>Total Liabilities and Equity</b>	<b>530.00</b>	<b>4,330.00</b>

Income statement for the year ended 31/12/2005

	Ksh."000"	Ksh."000"
<b>Revenues</b>	<b>ABC LTD</b>	<b>XYZ LTD</b>
Sales	1,325.99	6,657.658
Other revenues	8.004	13.342

<b>Expenses and Net Income</b>		
Excise taxes	174.754	620.403
Cost of goods sold	823.078	4,116.007
Administrative expenses	220.110	1,220.793
Interest expense	9.388	80.052
Other expenses	-	20.013
Current taxes	29.348	133.420
Deferred taxes	20.010	133.420
<b>Net income</b>	<b>57.362</b>	<b>346.892</b>
	1,334.00	6,671.000

**Required:**

- a) Prepare common size statements for both companies (15marks)
- b) Compare the performance of both companies (5marks)

**QUESTION THREE**

- a) You are provided with extracts from the financial statements of ABC Ltd for the year ended 31<sup>st</sup> December 2011.

ABC Ltd  
Statement of Financial Position

	Kshs.
Net equipment	1,610,000
Cash	480,000
Debtors	650,000
Stock	2,080,000
	<b>4,820,000</b>
Long term debt (10%)	1,610,000
Shareholders' equity	1,500,000
Trade creditors	870,000
Notes payable (9%)-short term	840,000
	<b>4,820,000</b>

Statement of incomes

	Kshs.
Sales	6,100,000
Less: cost of sales	3,600,000
<b>Gross profit</b>	<b>2,500,000</b>
Less: expenses	
Selling expenses	650,000
Administration expenses	1,120,000
Interest charge	235,600
	<b>2,005,600</b>
Profit before tax	494,400
Taxation	177,760

Net profit	316,640
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**Additional Information:**

- i. The market price per share of ABC Ltd is kshs. 5, Par value kshs. 1
- ii. Retained earnings are kshs. 467,640
- iii. Shareholders equity comprises only of share capital and retained earnings

**Required:**

Calculate the Altman Z-score for ABC Ltd and interpret it (15marks)

- b) You have just been appointed as the finance director at a newly established commercial bank. You reckon that the firm's financial plans must be anchored on a good forecasting system. What characteristics or features would you incorporate in designing your financial forecast (5marks)

**QUESTION FOUR**

- a) Examine the usefulness of financial ratios in predicting business failure of corporate firms. (10 Marks).
- b) The following are the Income Statement and balance Sheet in respect of Sameer Company Ltd based in Nairobi for the year 2014.

**Income Statement for period ended December 31<sup>st</sup>, 2014 – Shillings Millions.**

	<u>Shillings</u>
Net Sales	10,171
Cost of goods sold	7,621
Other Expenses	689
Depreciation	<u>514</u>
Earnings before Interest and Tax	<b>1,347</b>
Net Interest	260
Tax	<u>426</u>

<b>Net Profit</b>	<b>661</b>
Dividends	130
<b><u>Balance Sheet as at 31<sup>st</sup> December, 2014.</u></b>	
Cash and short term securities	62
Receivables	905
Inventories	892
Other Current Assets	<u>33</u>
<b>Total Current Assets</b>	<b>1,892</b>
Plant and Equipment	5,012
Other long-term assets	<u>211</u>
<b>Total Assets</b>	<b><u>7,115</u></b>
Debt due	210
Payables	404
Other Current Liabilities	<u>399</u>
<b>Total Current Liabilities</b>	<b>1,013</b>
<b>Long-term debt and Capital leases</b>	<b>953</b>
Common Share holders' equity	<u>2,635</u>
<b>Total Liabilities</b>	<b><u>7,115</u></b>

**Required.**

Calculate the following financial ratios:

- (i) Debt Ratio
- (ii) Times Interest ratio
- (iii) Current ratio
- (iv) Quick ratio
- (v) Net Profit ratio
- (vi) Return on equity ratio
- (vii) Inventory turnover

**(14 Marks).**

(c) The industry financial ratios in (b) above are as follows: current ratio=1.7 times, Inventory turnover= 7.0 times, Days sales outstanding = 45 days, Return on Assets (ROA)= 9.1% and Return on Equity(ROE) = 18.2%.

**Required.**

Analyze the Company's performance against the Industry benchmarks indicated and give your comments.

**(6 Marks).**

### **QUESTION FIVE**

Management Discussion and Analysis, provides a context within which to analyze and interpret the statements of financial position, financial performance and the statement of changes in equity of a firm.

#### **Required.**

Asses the principles for the presentation of management reports. **(10 Marks).**

(b) At the end of the year 2016, Western Financials ltd. reported the following Income Statement in (Kshs).

Sales	3,000,000
Operating costs excluding depreciation	2,450,000
EBITDA	550,000
Depreciation	250,000
EBIT	300,000
Interest	125,000
EBT	175,000
Taxes( 40%)	70,000
Net Income	105,000

The company's CFO has assembled the following information from projections:

- i. Sales for the year 2017 are expected to grow by 10% than last year
- ii. Depreciation is expected to increase at the same rate
- iii. Interest costs are on fixed income securities issued that shall in five years.
- iv. Tax rates are expected to remain at 40%

On the basis of that information your are required to construct forecasted income statement for the year ending 31<sup>st</sup> December 2017. **( 10 Marks)**