



UNIVERSITY OF EMBU

2017/2018 ACADEMIC YEAR

SECOND SEMESTER EXAMINATIONS

THIRD YEAR EXAMINATION FOR THE DEGREE OF BACHELOR OF COMMERCE

DFI 306: FINANCIAL ANALYSIS AND FORECASTING

DATE: APRIL 11, 2018

TIME: 11:00 AM – 1:00 PM

INSTRUCTIONS:

Answer Question ONE and ANY Other TWO Questions.

QUESTION ONE (30 MARKS)

- a) Distinguish between financial analysis and business analysis (2 marks)
- b) Analysis of financial statements reveals important facts concerning managerial performance and the efficiency of the firm. Outline the objectives of analysis of financial statements (6 marks)
- c) Explain the three categories of techniques of analysis of financial statements (6 marks)
- d) Financial analysis is useful and significant to different users. Describe any six different users and how they use financial analysis (6 marks)
- e) Richardson et al (1994) provided an alternative method of classifying reasons of business failure using the analogy of frogs and tadpoles. Explain these classifications (6 marks)
- f) Describe the role of cash budgets in financial forecasting (4 marks)

QUESTION TWO (20 MARKS)

The following are the summarized financial statements of Deweto limited:

Trading and profit and loss account for the year ended 31 October.

	2016	2017
	Sh.'000	Sh.'000
Sales	93,500	11,350

Cost of sales	(55,120)	(72,970)
Gross profit	38,380	38,380
Expenses	(26,230)	(23,960)
Net profit before interest and tax	12,150	14,420
Loan interest	(450)	(375)
Net profit before tax	11,700	14,045
Taxation	(3,510)	(5,413.5)
Net profit after tax	8,190	8,631.5
Dividend	(6,000)	(6,000)
Retained profit	<u>2,190</u>	<u>2,631.5</u>

Statement of financial position as at 31 October

	2016		2017	
	Sh.'000	Sh.'000	Sh.'000	Sh.'000
Fixed assets:				
Freehold premises	10,500		10,500	
Plant and equipment	7,200		9,500	
Motor vehicles	<u>5,350</u>	23,050	<u>7,300</u>	27,300
Current assets:				
Stock	12,500		11,800	
Debtors	9,850		8,900	
Bank balance and cash in hand	<u>5,950</u>	28,300	<u>5,864.5</u>	26,564.5
Current liabilities:				
Creditors	8,350		7,830	
Taxation	3,510		5,413.5	
Dividend	<u>3,000</u>	(14,860)	<u>3,000</u>	(16,243.5)
		<u>36,490</u>		<u>37,621</u>
Ordinary share capital		30,000		30,000
Reserves		<u>3,490</u>		<u>5,121</u>
		33,490		35,121
15% loan		<u>3,000</u>		<u>2,500</u>
		<u>36,490</u>		<u>37,621</u>

Note:

- 80% of the sales are on credit
- The stock as at 31 October 2015 was valued at Sh.13,000,000

Required:

- a) Calculate two ratios for each classification identified below for the financial years ended 31 October 2016 and 2017:
- Profitability ratios (4 marks)
 - Liquidity ratios (4 marks)
 - Gearing ratios (4 marks)
 - Activity ratios (4 marks)

b) Comment on Deweto Ltd's profitability and liquidity positions.

(4 marks)

QUESTION THREE (20 MARKS)

You are provided with the following information in respect of four listed companies.

	Working Capital	Retained Earnings	Earnings Before interest and tax	Market value of equity	Total Assets	Liabilities	Sales
	Sh.'000'	Sh.'000'	Sh.'000'	Sh.'000'	Sh.'000'	Sh.'000'	Sh.'000'
A Ltd.	4,000	60,000	10,000	35,000	120,000	120,000	200,000
B Ltd.	2,000	20,000	0	5,000	100,000	80,000	120,000
C Ltd.	6,000	20,000	-30,000	48,000	800,000	740,000	900,000
D Ltd.	40,000	200,000	30,000	100,000	700,000	1,000,000	2,000,000

Required:

- a) Calculate the Altman's Z-Score for each company and interpret it (10 marks)
- b) List down the indicators of possible business failure. (4 marks)
- c) Highlight the options available to a firm during financial distress (6 marks)

QUESTION FOUR (20 MARKS)

- a) Briefly explain the most commonly used techniques of financial analysis (8 marks)
- b) Consider the Ondiek Company Ltd, which reports the following financial information

Year	2013	2014	2015	2016	2017
	Shs "000"	Shs "000"	Shs "000"	Shs "000"	Shs "000"
Cash	400	404	408	412	416
Inventory	1,580	1,620	1,676	1,727	1,778
Accounts receivable	1,120	1,140	1,165	1,189	1,212
Net plant and equipment	3,500	3,640	3,786	3,937	4,095
Intangibles	<u>400</u>	<u>400</u>	<u>404</u>	<u>406</u>	<u>408</u>
Total assets	<u>7,000</u>	<u>7,204</u>	<u>7,439</u>	<u>7,670</u>	<u>7,909</u>

- i) Undertake vertical common-size analysis for the Ondiek Company's assets.

(6 marks)

- ii) Create the horizontal common-size analysis for Ondiek Company's assets, using 2011 as the base year. (6 marks)

QUESTION FIVE (20 MARKS)

- a) Outline the steps followed in financial forecasting (6 marks)
- b) The following is the statement of financial position of Mawingu Ltd as at 31st December 2017:

	Sh.'000'
Noncurrent assets (net)	3,000
Current assets	<u>1,000</u>
	<u>4,000</u>
Financed by:	
Ordinary share capital	1,000
Retained earnings	700
10% debentures	1,500
Trade Payables	500
Accrued expenses	<u>300</u>
	<u>4,000</u>

Additional Information

- The sales for year 2016 amounted to Sh.5,000,000. The sales will increase by 15% during year 2018 and 10% during year 2019.
- The after tax return on sales is 12% which shall be maintained in future.
- The company's dividend payout ratio is 80%. This will be maintained during forecasting period.
- Any additional financing from external sources will be affected through the issue of commercial paper by company.

Required

- a) Determine the amount of external finance for 2 years upto 31st December 2019. (10 marks)
- b) Prepare a proforma statement of financial position as at 31 December 2019. (4 marks)

--END--