

  
17 MAR 2017

**EASTERN UNIVERSITY, SRI LANKA**  
**FACULTY OF COMMERCE AND MANAGEMENT**

Final Year First Semester Examination in Bachelor of Commerce / Bachelor of  
Commerce (Specialization in Accounting and Finance)-2013/2014 (January 2016)  
(Proper/Repeat/Re-Repeat)

**DAF 4013 - Financial Reporting and Statement Analysis**

Answer All Questions

Time Allowed: 03 Hours

Non-Programmable Calculators are permitted.

---

01.

- (I) Explain why financial statements are important to the decision-making process in financial analysis.

(05 Marks)

- (II) CMA Plc a retailer dealing in a single product. Beginning inventory is zero at 1st of January and the operating expenses for the year are Rs.60000. The following purchases are made during the year:

Month	No. of Units	Per Unit (Rs.)	Total Cost (Rs.)
January	200	100	20000
March	300	110	33000
June	600	120	72000
October	400	140	56000
December	500	150	75000
<b>Total</b>	<b>2000</b>		<b>256000</b>

Ending inventory at December 31 is 800 units.

**Required:**

Determine net income for the year using each of the following inventory accounting methods. Assume a sale price of Rs.300 per unit and ignore income taxes.

- (i) First In First Out (FIFO)
- (ii) Last In First Out (LIFO)
- (iii) Average Cost (weighted average)

(15 Marks)

(Total 20 Marks)

02.

(I) Describe business analysis and identify its objectives.

(05 Marks)

(II) Comparative analysis is an important tool in financial analysis.

a. Explain the usefulness of comparative financial statement analysis.

b. Describe how financial statement comparisons are effectively made.

(05 Marks)

(III) Comparative income statements of a Company for the years 2013 and 2014 are as below:

	2014	2013
Net sales	Rs.600000	Rs.500000
Cost of goods sold	390000	280000
Gross Profit	210000	220000
Operating expenses	100000	130000
Income before taxes	110000	90000
Income taxes	30000	25000
Net income	80000	65000

**Required:**

a. Prepare a common-size statement showing the percentage of each item to sales for both years 2013 and 2014.

b. Interpret the trend shown in your percent calculations. What areas should management must concern?

(10 Marks)

(Total 20 Marks)

03.

(I) What is the meaning of the term "Cash Flow"? Why is this term subject to confusion and misrepresentation?

(05 Marks)

(II) What information can a user of financial statements obtain from the statement of cash flows?

**(05 Marks)**

(III) Discuss the importance of analysis of the statement of cash flows. Identify factors entering into the interpretation of cash flows from operations.

**(05 Marks)**

(IV) Describe the computation of free cash flow. What is its relevance to financial analysis?

**(05 Marks)**

**(Total 20 Marks)**

04.

(I) Discuss the motivation for excluding "nonproductive" assets from invested capital when computing return. What circumstances justify excluding intangible assets from invested capital?

**(05 Marks)**

(II) How is return on invested capital used as an internal management tool?

**(05 Marks)**

(III) Why is return on invested capital one of the most relevant measures of company performance? How do you use this measure in the analysis of financial statements?

**(05 Marks)**

(IV) Why is interest expense ignored when computing return on net operating assets (RNOA)?

**(05 Marks)**

**(Total 20 Marks)**



05.

(I) Calculate the weighted average number of shares for the followings,

- A corporation has 5,000 shares outstanding on 1 January 2014, the beginning of the fiscal year.
- On 31 March 2014, the conversion privilege on convertible bonds is exercised by the bond- holders, resulting in an additional 2,400 shares being issued.
- On 1 September 2014, the stock is split 2-for-1.
- On 1 October 2014, an additional 3,000 shares are issued for cash.

(05 Marks)

(II) MYLO Corp. reported net income of Rs.2,000,000 for 2014. As of 01/01/14, 400,000 shares of common stock were outstanding. On 1/10/14, 50,000 new shares were sold. There are no potentially dilutive securities outstanding at the beginning of the year. But MYLO has 5,000 shares of 6% cumulative preferred stock (Rs.10 par) which was outstanding all year. MYLO also has an issue of convertible preferred stock (cumulative) that was outstanding during the entire year. The preferred stock has Rs.100 par value and pays a Rs.10 annual dividend. The 6,000 shares were outstanding all year. Each share of preferred stock can be converted into 5 shares of common stock.

MYLO Corp. also has 50,000 stock options outstanding all year. At any time during the next five years, the option holders have the right to buy a share of common stock for Rs.10 per share. The average market price during 2014 was Rs.25.

Calculate the Basic Earning per Share and Diluted Earning per share

(10 Marks)

(III) Accounting income has elements of both permanent income and economic income. Explain this statement.

(05 Marks)

(Total 20 Marks)