Index Number.................................Signature...Date..............

CHRISTIAN SERVICE UNIVERSITY COLLEGE
KUMASI, GHANA
CSUC SCHOOL OF BUSINESS
DEPARTMENT OF ACCOUNTING AND FINANCE

END OF SECOND SEMESTER EXAMINATIONS – 2018/19 ACADEMIC YEAR

LEVEL 500

MACF 506: FINANCIAL STATEMENT ANALYSIS

MAY, 2019 **60 MARKS** **TIME ALLOWED: 3 HRS**

GENERAL INSTRUCTIONS TO CANDIDATES:

- Attempt all the four questions.
- Write your index number on top of the question paper and every page of the answer booklet used.

Examiner: Abraham Osei-Wusu (CA)

Index Number.................................Signature...Date..............

QUESTION 1

Below are the separate financial statements of Mike Ltd, and two investee companies which also operate in the same industry as the investor entity.

Income Statements and Other Comprehensive Income for the year ended 31 December 2018.

	Mike Ltd	Frank Ltd	Collins Ltd
	GH¢'000	GH¢'000	GH¢'000
Revenue	92,500	45,000	30,000
Cost of Sales	(70,500)	(36,000)	(18,000)
Gross profit	22,000	9,000	12,000
Distribution expenses	(2,500)	(1,200)	(1,000)
Administrative expenses	(5,500)	(2400)	(2,000)
Finance cost	(100)	-	-
Profit before tax	13,900	5,400	9,000
Corporate tax	(3,900)	(1,500)	(2,200)
Profit for the year	10,000	3,900	6,800
Other comprehensive income:			
Gain on revaluation of land	500	-	-
Total comprehensive income	10,500	3,900	6,800

Statements of financial position as at 31 December 2018

	Mike Ltd	Frank Ltd	Collins Ltd
	GH¢'000	GH¢'000	GH¢'000
Assets			
Non-current assets			
Property, plant and equipment	25,500	13,900	15,000
Investments	5,400	-	-
	30,900	13,900	15,000
Current assets	12,500	2,400	3,000
Total assets	43,400	16,300	18,000
Equity and liabilities:			
Equity:			
Equity shares of GH¢1 each	15,000	5,000	6,000
Land revaluation reserve	2,000	-	-
Other equity reserve	500	-	-
Retained earnings	12,900	4,500	5,000
	30,400	9,500	11,000
Non-current liabilities:			
20% loan notes	3,000	-	-
Current liabilities	10,000	6,800	7,000
Total equity and liabilities	43,400	16,300	18,000

The following additional information is relevant:

1. On 1 September 2018, Mike Ltd acquired 80% of the equity share capital of Frank Ltd. The consideration consisted of two elements: a share exchange of three shares in Mike Ltd. for every five acquired shares in Frank Ltd. and the issue of a GH¢100 6% loan note for every 500 shares

acquired in Frank Ltd. The share issue has not yet been recorded by Mike Ltd., but the issue of the loan notes has been recorded. At the date of acquisition, shares in Mike Ltd. had a market value of GH¢5 each and the shares of Frank had a stock market price of GH¢3.50 each.

Mike Ltd. had earlier, on 1 July 2018, acquired 2.4 million shares in Collins Ltd. on the stock market at a price of GH¢1.50 per share.

2. At the date of acquisition, the fair values of Frank Ltd's assets were equal to their carrying amounts with the exception of its property. This property has a fair value of GH¢1.2 million below its carrying amount. The effect of the fair value would lead to a reduction of the depreciation charge (in cost of sales) of GH¢50,000 in the post acquisition period. Frank Ltd. has not incorporated this value change into its separate financial statements.

3. Sales from Frank Ltd. to Mike Ltd. throughout the year ended 31 December 2018 was GH¢12 million. Frank made a mark-up on cost of 25% on these sales. Mike Ltd. had GH¢2 million (at cost to Papa Ltd.) of inventory that had been supplied in the post acquisition period by Frank Ltd. as at 31 December 2018.

4. In December 2018, Collins Ltd. sold goods to Mike Ltd. for GH¢2million achieving a profit mark-up of 25%. The entire consignment remained unsold and was included in the inventory of Mike Ltd. as at 31 December 2018.

5. Mike Ltd's investments included some available-for-sale investments that have increased in value by GH¢300,000 during the year. The other Equity Reserve relates to these investments and is based on their value as at 31 December 2017. There were no acquisitions or disposals of any of these investments during the year ended 31 December 2018.

6. Mike Ltd's policy is to value the non-controlling interest at fair value at the date of acquisition. For this purpose Frank Ltd's share price at that date can be deemed to be representative of the fair value of the shares held by the non-controlling interest.

7. Goodwill was tested at the end of the year. 10% of the Goodwill related to acquisition of Frank Ltd. was found to be impaired.

Required:

i. Prepare the consolidated statement of comprehensive income for Mike Ltd. Group for the year ended 31 December 2018.

(10 marks)

ii. Prepare the consolidated statement of financial position for Mike Ltd. Group as at 31 December 2018 **(10 marks)**

(Total: 20 marks)

Index Number.................................Signature......................................Date..............

QUESTION 2

Philo Ltd has incurred losses for many years. However, the company is developing a new product, which is expected profits of GH¢400,000 per annum in anticipation of an immediate capital injection of GH¢2,000,000. The company's Statement of Financial Position as at 31st December, 2017 is as follows:

ASSETS	GH¢
Property, plant and equipment	3,250,000
Inventories	1,000,000
Accounts receivables	500,000
	4,750,000
LIABILITIES & EQUITY	
Ordinary share capital (GH¢1.00)	2,000,000
10% Preference shares	750,000
15% Debentures (unsecured)	1,000,000
Accounts payables	1,000,000
Bank overdraft	750,000
Income surplus	(750,000)
	4,750,000

The bank overdraft is secured against the property, plant and equipment.

In the event of a forced sale the assets would probably raise the following amounts.

	GH¢
Property, Plant and Equipment	1,500,000
Inventories	400,000
Account Receivables	350,000

The Directors are therefore proposing a capital re-organisation of the company on the following basis:

i) The ordinary share capital should be written down to 200,000 share of GH¢1.00 each.
ii) The 10% preference shares are to be converted into 150,000 ordinary shares valued at GH¢1 per share.
iii) GH¢650,000 of the 15% debenture should be converted into GH¢350,000 10% Debentures.
iv) Trade creditors to accept a moratorium of six (6) months in payment of amounts currently due them. New supplies will be paid for on delivery.
v) A two for-one rights issue will be made at a price of GH¢1 per share for cash after the above conversions.
vi) Property, plant and equipment are to be revalued at GH¢2,250,000, inventories at GH¢600,000 and account receivables at GH¢450,000.
vii) The accumulated losses are to be written off.
viii) The corporate tax rate is 25%.
ix) Liquidation expenses will amount to GH¢10,000.

Index Number..................................Signature..Date..............

Required:

a) Prepare a statement of financial position after reconstruction on the assumption that the capital injection takes place.

(8 marks)

b) Prepare a statement of distribution if the company were to be liquidated now.

(7 marks)

(15 marks)

QUESTION 3

In June 2018, the shareholders of Vero Ltd decided to sell their equity stake in the company. The company is not listed and the new shareholders plan to prepare the company for listing once the acquisition was completed. The summarized financial statements of Vero Ltd for the year ended 30th June, 2018 are stated below:

Statement of income for the year ended 30th June, 2018

	GH¢
Profit before tax	24,800,000
Taxation	(8,000,000)
Profit after tax	16,800,000
Dividends	(3,200,000)
Retained Earnings	13,600,000

Statement of Financial Position as at 30th June, 2018

	GH¢
Non-Current Assets	62,400,000
Current Assets	21,400,000
	83,800,000
Current Liabilities	12,800,000
Long Term Liabilities	35,000,000
	47,800,000
Net Assets	36,000,000
Stated Capital	20,000,000
Retained Earnings	16,000,000
	36,000,000

The following additional information is provided;

1. The discounted present value of future cash payments in respect of the long term loan is GH¢48,800,000.
2. The stated capital of Vero Ltd is made up of 25,000,000 ordinary shares of no par value.

3. Current Assets include inventory of GH¢6,600,000 representing goods received from a major supplier on "not for sale but display only" basis.

4. The fair value of the tangible non-current assets was GH¢116,000,000.

5. The profit for the current year includes VAT of 17.5% on turnover of GH¢8,500,000 being invoice amount sold to a customer.

6. The discount rate of Vero Ltd is 10% per annum.

7. Warehouse Ltd, a major competitor of Vero Ltd is listed with a P/E ratio of 9 and dividend yield of 5.2.

8. Profits after tax over the 4 years were as follows;

	GH¢
30th June 2017	12,000,000
30th June 2016	14,400,000
30th June 2015	6,400,000
30th June 2014	11,200,000

Required:
Compute the value to be placed on the ordinary shares using three methods of valuation and advise the Directors accordingly.

(15 marks)

Index Number................................Signature.......................................Date..............

QUESTION 4

Honourable Co is considering acquiring an interest in its competitor Gabby Co LTD. The managing director of Honourable Co has obtained the three most recent statements of financial position of Gabby Co Ltd as shown below.

Gabby CO Ltd- Statement of financial position at 31st December

	2013	2014	2015
	GH¢'000	GH¢'000	GH¢'000
Non – current assets			
Land and buildings	11,460	2,121	11,081
Plant and equipment	8,896	9,020	9,130
	20,356	**21,141**	**20,211**
Current Assets			
Inventories	1,775	2,663	3,995
Trade receivables	1,440	2,260	3,164
Cash	50	53	55
	3265	**4,976**	**7,214**
Total Assets	**23,621**	**26,117**	**27,425**
Equity			
Share capital	8,000	8,000	8000
Retained earnings	6,434	7,313	7,584
	14,434	15,313	15,584
Non – current liabilities			
12% debentures 2015 – 2018	5,000	5,000	5,000
Current liabilities			
Trade payable	390	388	446
Bank	1,300	2,300	3,400
Income taxes payable	897	1,420	1,195
Dividend payable	1,600	1,696	1,800
	4,187	5,804	6,841
	23,621	**26,117**	**27,425**

Required:

Prepare a report for the managing director of Honourable Co. commenting on the financial position of Gabby Co Ltd. and highlight any areas that require further investigation (using gearing and liquidity ratios only).

(10 marks)