



24th Comprehensive Examination

Saturday, the 23rd February 2013

Time Allowed – 2 Hours

Maximum Marks – 60

- (i) Attempt both the cases 1 and 2 carrying 30 marks each.
- (ii) Answers must be neat, relevant and brief.
- (iii) In marking the question paper, the examiners take into account clarity of exposition, logic of arguments, effective presentation, language and use of clear diagram or chart where appropriate.
- (iv) Read the instructions printed on the top cover of answer script CAREFULLY before attempting the paper.
- (v) Use of non-programmable scientific calculator of any model is allowed.
- (vi) DO NOT write your Name, Reg. No. or Roll No. anywhere inside the answer script.
- (vii) Multiple Choice Questions (MCQs) printed separately, is an integral part of this question paper.
- (viii) Question paper must be returned to the invigilator before leaving the examination hall.

CASE # 1

Marks

The Rural Education & Development (READ) Foundation is a private charity partly supported by government grants. Its centres are located in Northern areas of Pakistan. The READ Foundation has just finished its operations for the month, which was a particularly busy month due to heavy rain that hit the areas, causing damage to stationery and other supplies. Residents of neighbouring areas voluntarily donated stationery and other supplies to help the READ. As a result, the READ Foundation collected and used over 30% more units of supplies than had been originally planned for the month accommodating the students of other affected institutions of nearby locations.

A report prepared by a government official comparing actual costs to budgeted costs for the READ Foundation appears below. Continued support from the government depends on the READ Foundation's ability to demonstrate control over its costs.

**READ Foundation
Cost Control Report
for the month ended**

	Actual	Budget	Variance
Stationery and office supplies (units)	780	600	180 F
Variable costs:			Rs. '000'
Examination expenditures	18,504	14,220	4,284 U
Books/ stationery supplies	21,564	17,220	4,344 U
Transportation of material	2,372	1,920	452 U
Administrative supplies	378	300	78 U
Total variable costs	42,818	33,660	9,158 U
Fixed costs:			
Teachers and staff salaries	26,400	26,400	–
Depreciation	4,200	3,800	400 U
Rent for premises	3,000	3,000	–
Utilities	648	600	48 U
Total fixed costs	34,248	33,800	448 U
Total costs	77,066	67,460	9,606 U

The Managing Director of the READ Foundation was very unhappy with this report, claiming that his costs were higher than expected due to the emergency in the areas. He also pointed out that the additional costs had been fully covered by donations from generous individuals from the other areas.

The government official who prepared the report countered that all of the figures had been submitted by the READ Foundation to the government; the administrator of the READ Foundation was just pointing out that actual costs were a lot higher than promised in the budget.

Required:

(a) Prepare a new performance report for the month using the flexible budget approach. **25**

(b) Do you think any of the variances in the report you prepared should be investigated? Why? **05**

(Note: Even though some of these costs might be classified as direct costs rather than as overhead, the flexible budget approach can still be used to prepare a flexible budget performance report.)

CASE # 2

The sales of Gama Company have not been upto the desired level, costs have been higher than were projected, and a large loss occurred in 2012, rather than the expected profit. As a result, its managers, directors, and investors are concerned about the company's survival.

CFO of the company had the task of getting the company back into a sound financial position. The statement of financial position and income statement of 2011 and 2012 of the company, together with projections for the year 2013, are shown in the following tables showing the ratios of 2011 and 2012, along with industry averages. The projected financial statements represent best estimates of CFO and CEO for the year 2013, assuming that some new financing is arranged to overcome financial problem.

Statement of Financial Position

	Rupees		
	As at end of the year		Projected
	2011	2012	2013
Assets:			
Cash	27,000	21,846	42,000
Short-term investments	145,800	60,000	214,896
Accounts receivable	1,053,600	1,896,480	2,634,000
Inventories	2,145,600	3,862,080	5,149,440
Total current assets	3,372,000	5,840,406	8,040,336
Gross fixed assets	1,473,000	3,608,850	3,660,000
Less: Accumulated depreciation	438,600	789,480	1,149,480
Net fixed assets	1,034,400	2,819,370	2,510,520
Total assets	4,406,400	8,659,776	10,550,856
Liabilities and Equity:			
Accounts payable	436,800	972,000	1,079,400
Notes payable	600,000	2,160,000	900,000
Accrued expenses	408,000	854,880	1,140,000
Total current liabilities	1,444,800	3,986,880	3,119,400
Long-term debt	970,296	3,000,000	1,500,000
Ordinary shares (100,000 shares)	1,380,000	1,380,000	5,042,808
Retained earnings	611,304	292,896	888,648
Total equity	1,991,304	1,672,896	5,931,456
Total liabilities and equity	4,406,400	8,659,776	10,550,856

Income Statements

	Rupees		
	For the year end		Projected
	2011	2012	2013
Sales	10,296,000	17,503,200	21,106,800
Cost of goods sold	8,592,000	14,940,000	17,400,000
Other expenses	1,020,000	2,160,000	1,838,880
Depreciation	56,700	350,880	360,000
Total operating costs	9,668,700	17,450,880	19,598,880
EBIT	627,300	52,320	1,507,920
Interest expense	187,500	528,000	240,000
EBT	439,800	(475,680)	1,267,920
Taxes (40%)	175,920	(190,272)	507,168
Net income/ (loss)	263,880	(285,408)	760,752
Other Data			
Share price (Rs.)	25.50	18.00	36.51
Share outstanding (Nos.)	100,000	100,000	250,000
EPS (Rs.)	2.64	(2.85)	3.04
Dividend per share (Rs.)	0.66	0.33	0.66
Tax rate	40%	40%	40%
Book value per share (Rs.)	19.914	16.728	23.727
Lease payments (Rs.)	120,000	120,000	120,000

Ratio Analysis

	For the year end		Projected	Industry Average
	2011	2012	2013	
Current	2.3 x	1.5 x	—	2.7 x
Quick	0.8 x	0.5 x	—	1.0 x
Inventory turnover	4.8 x	4.5 x	—	6.1 x
Days sales outstanding	37.3	39.6	—	32.0
Fixed assets turnover	10.0 x	6.2 x	—	7.0 x
Total assets turnover	2.3 x	2.0 x	—	2.5 x
Debt ratio	54.8 %	80.7 %	—	50.0 %
Times interest earned	3.3 x	0.1 x	—	6.2 x
EBITDA* coverage	2.6 x	0.8 x	—	8.0 x
Profit margin	2.6 %	−1.6 %	—	3.6 %
Basic earning power	14.2 %	0.6 %	—	17.8 %
Return on assets	6.0 %	−3.3 %	—	9.0 %
Return on equity	13.3 %	−17.1 %	—	17.9 %
Price/ earnings (P/E)	9.7 x	−6.3 x	—	16.2 x
Price/ cash flow	8.0 x	27.5 x	—	7.6 x
Market/ book value per share	1.3 x	1.1 x	—	2.9 x

* EBITDA = Earnings before interest , taxes, depreciation and amortization

CFO examined monthly data for 2012 (not given in the case), and he detected an improving pattern during the year. Monthly sales were rising, costs were falling, and large losses in the early months had turned to a small profit by December. Thus, the annual data looked somewhat worse than data finalized in later month(s) of the year. Also, it appears to be taking longer for the advertising program to get the message across, for the new sales offices to generate sales, and for the new manufacturing facilities to operate efficiently. In other words, the lags between spending money and deriving benefits were longer than Gama Company's managers had anticipated. For these reasons, CFO and CEO are hopeful for the company – provided it can survive in the short run.

CFO must prepare an analysis of where the company is now, what it must do to regain its financial health, and what actions should be taken.

Required:

Your assignment is to help him answer the following questions providing him the comparative statement of ratios for the year 2013:

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| (a) Why are ratios useful? What are the five (05) major categories of ratios? | 03 |
| (b) Calculate the ratios for the year 2013 for comparison with previous years and industry norms. | 20 |
| (c) Indicate the company's major strengths and weaknesses, using the extended Du Pont equation to provide a summary and overview of Gama Company's financial condition as projected for the year 2013. | 07 |

THE END