Analysis of Financial Statements

Standard difficulty · 20 questions · 40 marks · Time: 43 minutes

Name: _____ Date: _____ Score: ____ / 40

Show your working for Sections B and C. Answers are on the last page — try every question first!

Section A — Choose the correct answer — 8 × 1 = 8 marks

1. Comparing the same item over several years is:
(a) ratio analysis **(b)** cash flow analysis
(c) vertical analysis **(d)** horizontal analysis

2. What is meant by "cash flow analysis"?
(a) studying the inflows and outflows of cash and cash equivalents
(b) comparing items of one period with each other or with a total
(c) studying the statements to judge profitability and financial position
(d) percentages of each year's figures to a base year's figure

3. Which of these is a limitation of analysing financial statements?
(a) to judge short-term solvency
(b) to compare with other firms in the industry
(c) to judge the earning capacity of the business
(d) it is affected by personal judgement

4. In financial analysis, what interests short-term creditors most?
(a) the firm's ability to pay current debts (liquidity)
(b) profitability and stability, for wages and bonus
(c) long-term solvency and the cover for interest
(d) efficiency of operations and overall performance

5. Other income was ₹2,23,000 last year and ₹2,34,150 this year. What is the absolute change?
(a) increase of ₹11,150 **(b)** increase of ₹22,300
(c) decrease of ₹11,150 **(d)** increase of ₹2,34,150

6. In a comparative statement, advertisement expense was ₹3,46,000 last year and ₹2,94,100 this year. What is the percentage change?
(a) −30% **(b)** +15% **(c)** −15% **(d)** −17.65%

7. Silverline Ltd has revenue from operations of ₹6,80,000 and cost of materials consumed of ₹2,65,200. In a common-size statement of profit and loss, what percentage is shown for cost of materials consumed?
(a) 39% **(b)** 49% **(c)** 61% **(d)** 19.5%

8. Riverstone Ltd's balance sheet total is ₹4,30,000. Its non-current assets are ₹2,27,900. What percentage is shown for them in a common-size balance sheet?
(a) 53% **(b)** 58% **(c)** 47% **(d)** 48%

Section B — Short answer — 8 × 2 = 16 marks

9. What is meant by analysis of financial statements?

10. Explain each term: (a) trend analysis (b) horizontal analysis

11. Employee benefits expense was ₹2,82,000 last year and ₹3,52,500 this year. In a comparative statement, find (a) the absolute change (b) the percentage change.

12. Sunrise Ltd has revenue from operations of ₹3,80,000, cost of materials consumed of ₹1,48,200 and employee benefits expense of ₹38,000. Find each expense as a percentage of revenue from operations: (a) materials (b) employee benefits.

13. Advertisement expense this year is ₹2,86,800, which is 20% more than last year. Find last year's figure.

14. Trade payables fell from ₹1,12,000 to ₹98,000. Find the percentage change.

15. Greenleaf Ltd has revenue from operations of ₹2,50,000 and a profit before tax of ₹42,500. Find the profit before tax as a percentage of revenue from operations.

16. A company's revenue from operations was ₹3,90,000 in the base year, ₹4,48,500 in the next year and ₹6,82,500 in the year after. Find the trend percentages for the second and third years (base year = 100).

Section C — Word problems — 4 × 4 = 16 marks

17. Explain the significance of financial analysis to different users.

18. Prepare a comparative statement of profit and loss for Riverstone Ltd: revenue from operations ₹25,71,000 last year and ₹26,99,550 this year; cost of materials consumed ₹3,80,000 and ₹5,32,000; employee benefits expense ₹3,56,000 and ₹5,34,000. Show the absolute and percentage change for each item, and for revenue less these two expenses.

19. Prepare a common-size statement of profit and loss for Brightway Ltd: revenue from operations ₹6,10,000, other income ₹18,300, cost of materials consumed ₹2,92,800, employee benefits expense ₹79,300, other expenses ₹54,900.

20. Prepare a common-size balance sheet for Sunrise Ltd: shareholders' funds ₹1,37,200, non-current liabilities ₹67,200, current liabilities ₹75,600, non-current assets ₹1,84,800, current assets ₹95,200.

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Answer key

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Q	Answer	Working
1	**(d) horizontal analysis**	—
2	**(a) studying the inflows and outflows of cash and cash equivalents**	—
3	**(d) it is affected by personal judgement**	—
4	**(a) the firm's ability to pay current debts (liquidity)**	—
5	**(a) increase of ₹11,150**	₹2,34,150 − ₹2,23,000
6	**(c) −15%**	−₹51,900 ÷ ₹3,46,000 × 100
7	**(a) 39%**	₹2,65,200 ÷ ₹6,80,000 × 100
8	**(a) 53%**	₹2,27,900 ÷ ₹4,30,000 × 100
9	**Studying the relationships among items of the financial statements to judge the firm's profitability and financial position.**	—
10	**(a) percentages of each year's figures to a base year's figure (b) comparing the same item over several periods**	—
11	**(a) ₹70,500; (b) 25%**	(a) ₹3,52,500 − ₹2,82,000 (b) ₹70,500 ÷ ₹2,82,000 × 100
12	**(a) 39%; (b) 10%**	(a) ₹1,48,200 ÷ ₹3,80,000 × 100 (b) ₹38,000 ÷ ₹3,80,000 × 100
13	**₹2,39,000**	₹2,86,800 ÷ 1.2
14	**−12.5%**	(₹98,000 − ₹1,12,000) ÷ ₹1,12,000 × 100
15	**17%**	₹42,500 ÷ ₹2,50,000 × 100
16	**115%; 175%**	each year ÷ ₹3,90,000 × 100
17	**Management judges efficiency; shareholders judge profitability; creditors judge liquidity; lenders and debentureholders judge solvency; employees judge stability; government judges growth and tax.**	—
18	**Revenue from operations: ₹25,71,000 → ₹26,99,550, change ₹1,28,550 (5%)** **Cost of materials consumed: ₹3,80,000 → ₹5,32,000, change ₹1,52,000 (40%)** **Employee benefits expense: ₹3,56,000 → ₹5,34,000, change ₹1,78,000 (50%)** **Revenue less these expenses:**	change = this year − last year; % = change ÷ last year × 100

Q	Answer	Working
	₹18,35,000 → ₹16,33,550, change − ₹2,01,450 (−10.98%)	
19	**Revenue from operations 100%; Other income 3%; Materials 48%; Employee benefits 13%; Other expenses 9%; Profit before tax ₹2,01,300 = 33%**	each item ÷ ₹6,10,000 × 100
20	**Shareholders' funds 49%; Non-current liabilities 24%; Current liabilities 27%; total 100%** **Non-current assets 66%; Current assets 34%; total 100%**	each item ÷ ₹2,80,000 × 100