

# FINANCIAL STATEMENT ANALYSIS

## Lecture 6

### COMPARATIVE FINANCIAL STATEMENT ANALYSIS

Lecturer; **DR. Stephen Ndung'u**

#### MID SEMESTER ASSESSMENT

### FINANCIAL STATEMENT ANALYSIS

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**Instructions:**

Answer **ALL** questions

**Question one**

Superior Office Supply Company financial statements are presented below for the year 2019 and 2020;

**Superior Office Supply Company  
Consolidated statement of comprehensive income  
For the Years Ended December 31**

	<b>2020</b>	<b>2019</b>
Sales	2,198,600	2,114,100
Less: Returns and allowances	<u>(98,900)</u>	<u>(90,900)</u>
Net sales	2,099,700	2,023,200
Cost of goods sold	<u>(1,364,800)</u>	<u>(1,294,800)</u>
Gross profit	734,900	728,400
Selling expenses	(252,000)	(222,600)
Administrative expenses	(283,500)	(293,400)
Total operating expenses	<u>(535,500)</u>	<u>(516,000)</u>
Operating income	199,400	212,400
<b>Other revenue and gains</b>		
Interest and dividends	2,900	2,100
<b>Other expenses and losses</b>		
Interest expense	<u>(34,800)</u>	<u>(39,900)</u>
Net income	<u>167,500</u>	<u>174,600</u>

**Superior Office Supply Company  
Consolidated statement of financial position  
As at December 31**

	<b>2020</b>	<b>2019</b>
<b>Assets</b>		
<b>Noncurrent assets</b>		
Property, plant, and equipment	990,500	945,500
Less: Accumulated depreciation	365,000	306,800
Net property, plant, and equip.	625,500	638,700
Intangible assets	<u>110,000</u>	<u>100,000</u>
Total noncurrent assets	<u>2,091,000</u>	<u>1,991,000</u>

**Current assets**

Cash and cash equivalents	455,200	414,200
Short-term investments	35,500	36,900
Accounts receivable, net	286,200	255,800
Inventory	492,100	456,900
Prepaid expenses	<u>52,300</u>	<u>50,500</u>
Total current assets	<u>1,321,300</u>	<u>1,214,300</u>
Total assets	<u>2,056,800</u>	<u>1,953,000</u>

**Liabilities and Owner's Equity****Current liabilities**

Accounts payable	414,700	388,900
Short-term notes payable	50,000	24,500
Other current liabilities	<u>185,600</u>	<u>215,400</u>
Total current liabilities	<u>650,300</u>	<u>628,800</u>

**Long term liabilities**

Long-term debt	<u>551,400</u>	<u>581,600</u>
Total liabilities	1,201,700	1,210,400
Capital	<u>855,100</u>	<u>742,600</u>
Total liabilities and owner's equity	<u>2,056,800</u>	<u>1,953,000</u>

Required

- Prepare the following comparative financial statements showing the percentage increase or decrease in the various items.
  - Consolidated Statement of comprehensive income. (8 marks)
  - Consolidated Statement of financial position. (11 marks)
- Which items increased with the highest margin in both the income statement and the balance sheet? (2 marks)
- Comment on the performance of the business over the two years. (4 marks)

**Question two**

Neema incorporated has been in business for the past ten years. The finance director has come to your bank for a \$70 million loan. Neema incorporated has been a long-time customer of the bank. You are a member of the loan committee reviewing the loan application. The loan officer dealing with the customer is recommending that the full \$70 million loan be made because the business has been consistently profitable, maintains a good amount of working capital, has good current and acid-test ratios.

**Neema Incorporated**  
**Income Statement**  
**For the Years Ended May 31**

	2020 (000)	2019 (000)	2018 (000)
Net sales	456,000	397,000	344,000
Cost of goods sold	<u>214,000</u>	<u>188,000</u>	<u>158,000</u>
Gross profit	242,000	209,000	186,000
<b>Operating expenses</b>			
Selling	(37,000)	(28,000)	(24,000)

General and administrative	<u>(161,000)</u>	<u>(141,000)</u>	<u>(124,000)</u>
Income from operations	44,000	40,000	38,000
Loss on sale of land	(2,000)		
Interest expense	<u>(1,000)</u>	<u>(2,000)</u>	<u>(1,000)</u>
Net income	<u>41,000</u>	<u>38,000</u>	<u>37,000</u>

**Neema Incorporated**  
**Balance Sheet**  
**For the Years Ended May 31**

	<b>2020</b>	<b>2019</b>	<b>2018</b>
	<b>(000)</b>	<b>(000)</b>	<b>(000)</b>
<b>Fixed assets</b>			
Land		10,000	10,000
Property, plant, and equipment	125,000	125,000	118,000
Less: Accumulated depreciation	<u>(44,000)</u>	<u>(28,000)</u>	<u>(12,000)</u>
Total fixed assets	<u>169,000</u>	<u>163,000</u>	<u>140,000</u>
<b>Current assets</b>			
Cash	37,000	70,000	86,000
Accounts receivables	119,000	62,000	49,000
Supplies	2,000	2,000	3,000
Inventory	<u>127,000</u>	<u>78,000</u>	<u>51,000</u>
Total current assets	<u>285,000</u>	<u>212,000</u>	<u>189,000</u>
Total assets	<u>366,000</u>	<u>319,000</u>	<u>305,000</u>
<b>Liabilities and Equity</b>			
Total current liabilities	123,000	106,000	97,000
Long-term notes payable	47,000	58,000	48,000
Shareholders capital	<u>196,000</u>	<u>155,000</u>	<u>160,000</u>
Total liabilities and owner's equity	<u>366,000</u>	<u>319,000</u>	<u>305,000</u>

**Required**

a. Using the following ratios for the past three years, evaluate the loan application.

1. Current ratio (3 marks)
2. Acid test ratio (3 marks)
3. Accounts receivable turnover ratio (3 marks)
4. Inventory turnover ratio (3 marks)
5. Debt ratio (3 marks)
6. Capital gearing ratio (3 marks)

b. Do you agree with the loan officer's recommendation? (7 marks)

**Question three**

Big Mac ltd has been in operation for the past four years. The management of the company has requested you to evaluate the performance of the company over the four years of existence. Its financial statements are presented below;

**Income statement summary**

2017	2018	2019	2020
(000)	(000)	(000)	(000)

Turnover	<u>2,007,476</u>	<u>1,785,888</u>	<u>1,583,291</u>	<u>1,917,445</u>
Operating Profit	403,747	328,521	208,578	266,388
Taxation	<u>(128,208)</u>	<u>(127,918)</u>	<u>(65,826)</u>	<u>(76,553)</u>
Profit after taxation	275,539	200,603	142,752	189,835
Dividends	<u>(355,110)</u>	<u>(641,550)</u>	<u>(135,240)</u>	<u>(185,640)</u>
Retained profit	<u>(79,571)</u>	<u>(440,947)</u>	<u>7,512</u>	<u>4,195</u>
Earnings per share	1,313	955	680	904
Dividend per share	1,691	3,055	644	884

### Balance sheet summary

	<b>2017</b>	<b>2018</b>	<b>2019</b>	<b>2020</b>
	<b>(000)</b>	<b>(000)</b>	<b>(000)</b>	<b>(000)</b>
Fixed assets	126,336	102,585	97,368	87,898
Noncurrent assets	<u>21,347</u>	<u>22,584</u>	<u>30,699</u>	<u>38,932</u>
	147,683	147,683	128,067	126,830
Current assets	696,216	529,857	511,138	571,586
Current liabilities	<u>(120,239)</u>	<u>(368,092)</u>	<u>(327,364)</u>	<u>(371,141)</u>
Net current assets	<u>575,977</u>	<u>161,765</u>	<u>183,774</u>	<u>200,445</u>
NET ASSETS	<u>723,660</u>	<u>286,934</u>	<u>311,841</u>	<u>327,275</u>

### Financed by:

Share capital	210,000	210,000	210,000	210,000
Reserves	464,606	23,659	31,171	35,366
Shareholders' funds	674,606	233,659	241,171	245,366
Noncurrent liabilities	<u>49,054</u>	<u>53,275</u>	<u>70,670</u>	<u>81,909</u>
Shareholders' funds and liabilities	<u>723,660</u>	<u>286,934</u>	<u>311,841</u>	<u>327,275</u>

### Required

1. Calculate the trend percentages of the company income statement, by taking 2017 as base year. (8 marks)
2. Calculate the trend percentages of the company balance sheet, by taking 2017 as base year. (13 marks)
3. Analyze and comment on the statements of financial performance and trend percents from above. (4 marks)

### Question four

- a. Distinguish between technical analysis and fundamental analysis using appropriate examples. (9 marks)
- b. Business and financial statement analysis are important to different groups or situations. Explain eight groups or situations that may require such information. (16 marks)