

Examiner's Report

AA3 EXAMINATION - JULY 2016

(AA32) MANAGEMENT ACCOUNTING AND FINANCE

OVERVIEW:

This paper has three sections covering 100 marks,

1. Section A includes four compulsory questions for 20 marks
2. Section B includes three compulsory questions for 30 marks.
3. Section C includes two compulsory questions for 50 marks.

General Comments:

Candidates' overall performance for this paper was not satisfactory. Some of the candidates have scored fairly good marks for this paper.

Candidates' performance for **Section A** was satisfactory.

Candidates' performance for **Section B** was found to be unsatisfactory despite similar questions have been shown as examples in the study pack.

Candidates' performance was satisfactory for **Section C**.

SECTION A

Question No. 01

This question tested the knowledge of personal financial planning. It was required to explain the term "Personal Budget" and state two (02) advantages of "Personal Financial Planning" for 5marks.

Performance:

Overall performance for this question is satisfactory.

Most of the candidates had attempted and scored more than half of the marks allocated.

Common mistakes are:

Some candidates had not mentioned that savings and debt repayment also covered under the definition of personal budget as answers to part (a).

Examiner suggestions:

Read the Self-study Text and other related materials such as business news in the newspapers and business magazines to update the knowledge.

Question No. 02

This question tested on the ability to identify possible reasons for the cash deficit from part (a) and strategies / methods to achieve a cash surplus from part (b).

Performance:

This was a simple question based on theory and overall performance for this question was satisfactory. Some of the candidates were not able to identify the strategies / methods to achieve a cash surplus although they had stated possible cause for the cash deficit.

Common mistakes are:

- Writing vague and incomplete answers.
- Explaining the term “cash surplus” instead of explaining strategies / methods to achieve a cash surplus for part (b).

Examiner suggestions:

- Practice past papers and read the Self-study Text and other related materials.
- Candidates should be aware of the methods of improving short term working capital requirements such as factoring of debtors, leasing of fixed assets etc.

Question No. 03

This question tested knowledge on calculation of optimal production mix to maximize the profit when there is a limiting factor.

Performance:

The performance for this question is average. Many candidates do not possess the knowledge on how to calculate the optimal product mix when there is a limiting factor.

Common mistakes

- Some candidates were not aware that fixed overhead should not be taken into account when calculating the contribution.
- In calculating the contribution some of the candidates have copied incorrect figures from the question paper (Eg: Entered 225 instead of 255) and some have made arithmetical errors.

Possible reason for these mistakes would be lack of understanding the concept/theory and not reading the question carefully.

Examiner suggestion:

- Practice similar type of questions available in the Self-study Text.
- Read the question properly before attempting and be extra cautious when copying the figures from the question paper for the calculations in the answer scripts.
- Show your workings clearly.

Question No. 04

This question tested on the knowledge of calculating Return on Capital Employed (ROCE) for part (a) and stating advantages of using ROCE for part (b). ROCE should be calculated as follows:

$$\text{ROCE} = \frac{\text{PBIT}}{\text{Equity} + \text{Non-current Liabilities}}$$

Performance:

Candidates' performance is average for this question. Most of the candidates do not possess the knowledge on how to arrive at the capital employed i.e. they do not know whether to include retained earnings, other reserve and long term loans.

Common mistakes:

- For part (a), when calculating ROCE some have taken profit after tax while some have taken profit before tax for the numerator. Some have taken only stated capital as capital employed for the denominator.
- For part (b) most of the candidates have given irrelevant answers.

Examiner suggestion:

- Practice similar type of past paper and other practice questions
- Study and get clear and conclusive knowledge about the ROCE and other ratios.

SECTION B

Question No. 05

It was required to prepare a table showing the current profit and estimated profit at each given price and demand level from part (a). From part (b) it was required to identify the appropriate price level for the company.

Performance:

The candidates' performance is not satisfactory for the question.

Common mistakes are:

- Most of the candidates had not calculated the expected demand and had calculated the profit based on 70,000 and 90,000 units.
- Some of the students had not calculated the profit for the current situation although in the question it has specifically stated to show the current profit.
- A considerable number of candidates have not recognized the appropriate price level for the company and just prepared the calculations, although question has clearly indicated to identify the appropriate price level for the company from the part (b).

Examiner suggestions:

- Practice past papers and other practice questions especially in the self-study pack.
- Always show your workings.
- Avoid the simple arithmetical errors and double check the calculations.

Question No. 06

It was required to prepare an operating statement (a budgetary control statement) using marginal costing format for the given month based on the flexible budget from part (a) and state two limitations of budgetary control from part (b).

Performance:

The performance for this question was not satisfactory.

Common mistakes:

- Majority of the candidates didn't have the theoretical knowledge about the flexible budget and how to prepare an operating statement.
- Most of the candidates have copied the budgeted and actual figures from the question and tried to find the variance without preparing the flexible budget.
- Although some students have mentioned the variance, they have not properly identified whether the variance is favorable or adverse.
- Some of the students have used variance analysis method to calculate the variances without preparing the flexible budget.

Examiner suggestions:

- Study the relevant content and the questions thoroughly in the self-study pack regarding budgetary control.
- Practice the past papers and other practice questions - similar type of questions were repeatedly tested in exams.
- Should improve the knowledge about budgeting and relevant formats.
- Be mindful about using (+) / (-) and the arithmetical accuracy when calculating variances.

Question No. 07

This question tested on the knowledge about the calculation of cost of equity, cost of debt, and calculation of Weighted Average Cost of Capital (WACC) from part (a). It was required to state two (02) advantages of financing the project from the bank loan from part (b) and factors to be considered when choosing long term funding source from part (c).

Performance:

The performance of the candidates for this question is poor as a whole.

For part (a) The computations related to Cost of capital of Ordinary Share Capital, Debt Capital, and overall WACC needs only substitution of figures to the relevant formula. But candidates' performance was not satisfactory. Only few candidates did the calculation of cost of equity using dividend growth model and answered well. Although some candidates have written the formulae, they have not substituted the figures correctly or were found weak in solving the formula arithmetically.

The performance for part (b) and (C) are also poor and it was observed that some candidates have not even attempted the same.

Common mistakes:

- Some of the students had not used dividend growth model for the calculation of the cost of equity.
- Instead of adding the growth rate, some of the students have used wrong formulae by multiplying and subtracting the growth rate.

$$\text{Eg:- } r_e = \frac{d_0(1+g)}{P_0} - g$$

$$r_e = \frac{d_0(1+g)}{P} * g$$

- Some of the candidates had calculated IRR and NPV, instead of WACC.
- Instances were observed where candidates have calculated WACC using book value.
- Some candidates have not applied the dividend growth % to the formula totally.
- Candidates did not know how to solve the formula and arrive at figures accurately, even when they have written the formulae correctly. This is because they are weak in mathematics.
- Several candidates have provided irrelevant and vague answers for part (b) and part (c).

Examiner suggestions:

- Practice past paper questions since similar types of questions were repeatedly tested in every exam.
- Apply the formulae correctly for the cost of equity, cost of debt, WACC.
- Be mindful about using (+) / (-) and the arithmetical accuracy.
- Have a sound knowledge regarding the theoretical aspects of Sources of Capital and Cost of Capital.
- State specific and relevant answer for theory question after reading and understanding the question carefully.

Section C**Question 08**

Part A of the question tested on evaluating a proposal to purchase a new machinery to replace an existing old machinery by using NPV calculations and IRR computation.

Part B of the question tested on accepting a special order.

Performance:

The candidates' performance for this question is satisfactory. Majority of the candidates have correctly identified the cash flows. However, calculation of depreciation and identification of fixed cost were done incorrectly.

Common mistakes:

- Some candidates have not excluded the scrap value when calculating the depreciation.
- Some of the candidates didn't have any idea about how to treat the depreciation for the cash flow. Some have fully deducted 40 million erroneously as annual fixed cost.

- Although some have correctly calculated the depreciation value of 17.2 million they have deducted both depreciation value 17.2 and the fixed cost of 22.8 million separately in arriving at the cash flow.
- Some candidates have used incorrect signs for initial investment and for scrap value in the calculations.
- When calculating the IRR some candidates have not correctly applied the figures to the formula.
- In the case of part (B) most of the candidates have done only the calculations and have not assessed the decision with reasons although question has specifically stated the requirement of assessing the decision.

Examiner suggestions:

- Be careful in showing the cash out flows and inflows signs in project calculation (Cash outflows to be shown within brackets or as negative figures and cash inflows without brackets).
- Always show your additional workings and clearly state the assumptions if there are any.
- Practice past papers and other practice questions.
- When the question specifically required to “assess” the decision or financial viability, determine the value, nature or ability of the scenario based on the calculations.
- It is worthwhile for candidates to read the question carefully while paying proper attention to action verbs.

Question No. 09

This question tested the knowledge on application of Standard absorption costing method, and Variance analysis from part (A). From part (B), it was required to analyze the option on discontinuation of manufacturing.

Performance:

The performance was satisfactory for this question.

Common mistakes:

- Some students have calculated contribution instead of actual profit for part (a) in sub section (A).
- Some students have applied the answers arrived from variance analysis to find out the profit.
- Few students have calculated per unit profit.
- Few students have ended up with the mathematical errors in summing up even though the application is correct.
- Forgetting to show Adverse (A) / Favourable (F) in calculating variances for the part (b) in sub section (A).
- Majority of the students have done various calculations without stating assumptions clearly for sub section (B) of the question.

Examiner suggestions:

- Candidates should practice on formulas of variances in different scenarios.
- Candidates must be encouraged to show all the workings especially on options analysis to score high marks.
- Candidates should state assumptions clearly along with the workings.
- Presentation of formulas with the correct application of figures in variance analysis.
- Practice past papers and other practice question.
- Improve the theoretical knowledge regarding the variances and relevant costing.

It is essential to practice past papers, the practice questions in the study pack to understand the patterns and the formats of the questions. Candidates should be extra conscious in writing formulas, substituting figures for them and about the arithmetical accuracy. It is also required to show the workings pertaining to the questions with clarity and state any related assumptions very clearly if there are any.

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General points to be considered in developing the level of Understanding of candidates

1. Studying well the full contents of the syllabus completely and develop a thorough understanding about the level of knowledge expected for the each unit or area.
2. Candidates should read the question carefully a several times and should show all the relevant workings related to the computations with clarity.
3. State the assumptions clearly if there are any assumptions involved in answering the questions.
4. Handwriting should be legible and the numbers of questions should be correctly written. Re-checking of question numbers etc. before handing over answer scripts is a must.
5. Following correctly the instructions given in the question paper.
6. Perusal of past question papers and suggested answers would help sharpening of knowledge, skills and experience. It is always advantageous because the similar patterns and the structures may repeat in the real examination papers.
7. Referring the **self-study text** is essential and practicing the examples of the **self-study text** is also vital.
8. Refer books, articles, magazines in relation to this subject and other reading materials related to the relevant subject areas.
9. Time Management is crucial in the examination. By looking at the marks allocated to the each question candidates can make an estimation of the time they require to spend in answering.
10. Appearing for the examination with a firm determination of passing the examination with due preparation.

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