

CIS SEPTEMBER 2010 Exam Diet

Examination Paper 1.1:

Financial Accounting and Financial Statement Analysis

Economics and Financial Markets

Quantitative Analysis and Statistics

Level 1

SECTION A

Financial Accounting and Financial Statement Analysis (Questions 1 to 20)

1. Which of the following statements are true regarding the share premium account?
 - (I) It constitutes part of the shareholders' funds of a company.
 - (II) It can be paid out as dividend.
 - (III) It will increase if and when new shares are issued at a price above par value.
 - (IV) It can be used to write off preliminary expenses.
 - A. (I) and (II) only
 - B. (III) and (IV) only
 - C. (I), (III) and (IV) only
 - D. (I), (II), (III) and (IV)

2. Other things held constant, which of the following will not affect the quick ratio? (Assume that current assets equal current liabilities.)
 - A. Fixed assets are sold for cash.
 - B. Cash is used to purchase inventories.
 - C. Cash is used to pay off accounts payable.
 - D. Accounts receivable are collected.

3. The rules for the preparation of financial statements are governed by the following broad sets of codes except:
 - A. Laws governing corporate reporting.
 - B. Regulations of the body controlling the securities market.
 - C. Accounting Standards of the professional accounting bodies
 - D. Operating Procedures

4. According to IAS 1 Presentation of Financial Statements, which of the following items could appear in the statement of changes in equity:
 - (I) Total comprehensive income for the year
 - (II) Dividends
 - (III) Loss on sale of investments.
 - (IV) Issue of share capital
 - A. I, II and IV only
 - B. I, III and IV only
 - C. I and III only
 - D. I, II, III and IV

5. When calculating a company's gearing ratio which of the following factors would cause it to fall?
 - (I) A rights issue of ordinary shares.
 - (II) An issue of loan notes.
 - (III) An upward revaluation of non-current assets.
 - A. I only
 - B. I and II
 - C. II and III
 - D. I and III

6. Which of the following statements (in general) is correct?
- A low receivables turnover is desirable.
 - The lower the total debt-to-equity ratio, the lower the financial risk for a firm.
 - An increase in net profit margin with no change in sales or assets means a poor ROI.
 - The higher the tax rate for a firm, the lower the interest coverage ratio.
7. Failure to record the receipt of a utility bill for services already received will result in:
- An overstatement of assets.
 - An overstatement of liabilities.
 - An overstatement of equity.
 - An understatement of assets.
8. The trading securities owned by a company are:
- reported on the balance sheet as a current asset.
 - reported on the balance sheet as a noncurrent asset.
 - reported on the balance sheet as a contra-equity account.
 - reported on the balance sheet as a reduction of liabilities.
9. Which of the following statements regarding changing inventory methods is true?
- A change in inventory methods can be justified if the change is made to better match profits with revenue.
 - The effect of changing inventory method does not need to be disclosed.
 - Tax advantages are valid justification for changing inventory methods.
 - One place that the reader of an annual report would be able to identify that a company changed inventory methods is the footnotes to the financial statements.
10. Which of the following entries made to record the payment of N2,500 on account will cause the trial balance to be out of balance?
- No entry is recorded.
 - Cash is debited for N2,500 and Service Revenue is credited for N2,500.
 - Cash is debited for N250 and Accounts Payable is credited for N250.
 - Both Cash and Accounts Payable are credited for N2,500.
11. Which of the following indicators is **not** a measure of liquidity?
- Debt-to-equity ratio.
 - Quick ratio.
 - Current ratio.
 - Working capital.
12. Payment of dividend to shareholders is classified as a cash flow from
- Operating activities
 - Investing activities
 - Financing activities
- Either (I) or (II).
 - Either (I) or (III).
 - Either (II) or (III).
 - Either (I), (II) or (III).
13. Which of the following conditions is not necessarily true for an item to qualify as an asset?
- There should be probable future benefits from it.
 - It represents the claim of other entities.
 - It should be under the control of the firm.
 - It should have been bought or created by past events or transactions.

14. Which is the most appropriate stage in the transaction cycle at which revenue be recognized?
- A. When the product is delivered to the customer.
 - B. When the invoice is sent to the customer.
 - C. When the seller receives the payment from the customer.
 - D. None of the above answers is correct.
15. The cost of a tangible non-current asset should include which of these?
- A. Only the amount invoiced by the supplier of the asset.
 - B. The amount invoiced and additional expenses that occur until the asset can be used.
 - C. The amount invoiced and additional expenses that occur until the asset can be used, except import duties.
 - D. The amount invoiced and a part of general overhead costs of the company.
16. An allowance for doubtful debts is created:
- A. when debtors become bankrupt.
 - B. when debtors cease to be in business.
 - C. to provide for possible bad debt.
 - D. to write off bad debt.
17. Which of the following should not be called sales?
- A. Office fixtures sold
 - B. Goods sold on credit
 - C. Goods sold for cash
 - D. Sale of item previously included in ' purchases'
18. A firm bought a machine for N320,000. It is to be depreciated at the rate of 25 per cent using the reducing balance method. What would be the remaining book value after two years?
- A. N160,000
 - B. N240,000
 - C. N180,000
 - D. None of the above
19. A company has capital of 1 million ordinary shares of N1 each. It pays dividend of 6% of its profits after tax of N4,800,000, on sales of N40,000,000. The market price of the shares is N2.40. Compute the earnings per share
- A. 28.8k
 - B. N4.8
 - C. N8.33
 - D. N40
20. An investor who was worried that a company might go bankrupt would most likely examine it's:
- A. Current ratio
 - B. Return on equity
 - C. Debt-to-equity ratio
 - D. Price-earnings multiple

Economics and Financial Markets (Questions 21 to 40)

21. Why do price floors tend to cause persistent imbalances in the market?
- A. Quantity demanded exceeds quantity supplied but price cannot rise to remove the shortage.
 - B. Quantity demanded exceeds quantity supplied but price cannot fall to remove the surplus.
 - C. Quantity supplied exceeds quantity demanded but price cannot rise to remove the shortage.
 - D. Quantity supplied exceeds quantity demanded but price cannot fall to remove the surplus.
22. The law of diminishing marginal utility explains why
- A. most individual demand curves are straight lines.
 - B. the consumer's optimal purchase is at the tangency of an indifference curve and the budget line.
 - C. most individual demand curves slope downward.
 - D. marginal utility falls when total utility falls.
23. The price of an airline ticket rises as the amount of time between purchase and flight departure gets smaller. The airlines base the policy on the assumption that
- A. consumers are not aware of airline prices.
 - B. consumer demand is unrelated to prices.
 - C. consumer demand becomes more elastic as departure time approaches.
 - D. consumer demand becomes less elastic as departure time approaches.
24. To find its profit-maximizing output level, a firm should operate where
- A. $AVC = MC$.
 - B. $MC = MR$.
 - C. $TFC = TVC$.
 - D. $AFC = AVC$.
25. Economists object to monopoly because
- A. monopoly profits go to the rich.
 - B. monopolies overproduce to maximize profits.
 - C. monopolies are usually polluters.
 - D. monopolists keep output below efficient levels.
26. A common characteristic in oligopolistic markets is
- A. consideration of rivals' reactions.
 - B. standardized products.
 - C. high profits.
 - D. unused capacity.
27. Gross Domestic Product is defined as:
- A. disposable income + taxes + investment spending + exports + imports.
 - B. consumer spending + government purchases + financial spending + exports – imports.
 - C. consumer spending + government purchases + investment spending + exports – imports.
 - D. consumer spending + government transfers + investment spending + exports – imports.
28. Expansionary monetary policy
- A. tends to lead to an appreciation of a nation's currency.
 - B. usually has no effect on a currency's exchange value.
 - C. tends to lead to a depreciation of the currencies of other nations.
 - D. tends to lead to a depreciation of a nation's currency.

29. If the number of people classified as unemployed is 20,000 and the number of people classified as employed is 230,000, what is the unemployment rate?
- A. 8%
 - B. 8.7%
 - C. 9.2%
 - D. 11.5%
30. If an individual who cannot find a job because his or her job skills have become obsolete this is an example of
- A. frictional unemployment.
 - B. structural unemployment.
 - C. cyclical unemployment.
 - D. seasonal unemployment.
31. Banks can create money
- A. only by illegally printing additional dollar bills.
 - B. by paying interest to their depositors.
 - C. by making loans that result in additional deposits.
 - D. by offering financial services, such as stock market brokerage.
32. Which of the following represents an action by the Bank of Canada that is designed to decrease the money supply?
- A. an increase in federal tax rates
 - B. selling government securities in the open market
 - C. a decrease in the Bank rate
 - D. a transfer of government funds from the Bank of Canada to private banks
33. If the interest rate falls, then
- A. bond prices will remain the same
 - B. bond prices will rise
 - C. bond prices will fall
 - D. none of the above
34. If the quantity of money demanded is less than the quantity of money supplied, then the interest rate will
- A. either increase or decrease, depending on the amount of excess demand.
 - B. increase.
 - C. decrease.
 - D. not change.
35. An increase in total production (real GDP) causes the demand for money to _____ and the interest rate to _____.
- A. increase; increase
 - B. increase; decrease
 - C. decrease; decrease
 - D. decrease; increase
36. Which of the following actions is an example of expansionary fiscal policy?
- A. a decrease in welfare payments
 - B. a purchase of government securities in the open market
 - C. a decrease in the Bank rate
 - D. a decrease in the companies income tax rate

37. Which of the following components of government spending can be categorised as a consumption expenditure (CE) and which can be categorized as an investment expenditure (IE) respectively?
- A. CE: spending on unemployment payments; IE: salaries of the soldiers in peace-keeping operations in Sudan.
 - B. CE: paying gardeners to maintain the Presidential House grounds; IE: construction of a library
 - C. CE: construction of new conference halls; IE: research and development expenditure
 - D. CE: senators' fringe benefits; IE: purchase of consumables for defense
38. One possible explanation for involuntary unemployment is
- A. the wage rate does not adjust immediately to changes in the labor demand
 - B. the labor market is perfectly competitive
 - C. the firms, knowing the supply and demand curve for labor, implement the equilibrium wage, which happens to be so low that many people prefer to stay at home
 - D. maximum wages which are implemented
39. As the economy nears full capacity, the short-run aggregate supply curve
- A. becomes flatter.
 - B. becomes steeper.
 - C. shifts to the right.
 - D. shifts to the left.
40. The current account in a country's balance of payments accounting includes the sum of the country's:
- A. balance of trade and its capital account.
 - B. statistical discrepancy and its flows of funds.
 - C. net flows of payments for services and its balance of trade.
 - D. net currency flows and its capital account.

Quantitative Analysis and Statistics (Questions 41 to 60)

41. Two local football teams, Rangers United and Jos United, will be playing other teams tomorrow. Rangers United has a 30% chance of winning, and Jos United has a 40% chance of winning. If these two events are independent of each other, what is the probability that both teams will win tomorrow?
- A. 10%
 - B. 12%
 - C. Between a 30% and a 40% chance
 - D. 70%

42. You expect GTC Stock to have the following potential returns over the next year:

| <u>Scenario</u> | <u>Return</u> | <u>Probability</u> |
|-----------------|---------------|--------------------|
| Recovery | 22% | 40% |
| Status quo | 11% | 35% |
| Recession | -7% | 25% |

Which of the following would best estimate the expected variance for GTC Stock?

- A. 0.1353385
- B. 52.4654
- C. 12.845764
- D. 0.0129391

43. FBN Stock has an expected rate of return of 15% and a standard deviation of 6%, whereas UTB Stock has an expected return of 7% and a standard deviation of 4%. Which stock's return is relatively more uncertain?
- FBN Stock's returns are relatively more uncertain because its coefficient of variation is 2.5, whereas for UTB Stock it is only 1.75.
 - FBN Stock's returns are relatively more uncertain because its standard deviation is higher than that of UTB.
 - UTB stock's returns are relatively more uncertain because its coefficient of variation is 57%, whereas for FBN Stock it is only 40%.
 - In general, stocks that have a higher expected return bear more risk. Therefore, FBN Stock must be relatively more uncertain.

44. A portfolio manager examines the following return possibilities of Stock A and Stock B:

| State of Economy | Probability | Stock A | Stock B |
|------------------|-------------|---------|---------|
| Recession | .20 | -12% | 3% |
| Neutral | .70 | 8% | 5% |
| Boom | .10 | 20% | 9% |

What is the covariance between these two stocks?

- 28.49
 - 11.08
 - 17.27
 - 86.51
45. Which of the following statements with respect to hypothesis testing is (are) correct?
- The null hypothesis is the rejection of the hypothesis that is being tested.
 - The alternative hypothesis is the new hypothesis that may be tested if the original hypothesis was rejected.
 - A two-tailed test may be used when the null hypothesis is set to equal some fixed point.
 - A one-tailed test may be used when the null hypothesis is set to be greater than or equal to some particular outcome.
- I, II and IV only
 - I and II only
 - III and IV only
 - IV only
46. Which of the following statements least accurately interprets the IRR rule?
- The IRR could be interpreted as the expected return on an investment.
 - It is possible for an investment to have multiple IRRs.
 - If the required return is equal to the IRR, then the project's NPV will also be equal to zero.
 - If a project has a positive IRR, it should be accepted.
47. On average, there is a 60% chance that the economy will expand in any given year. What is the expected number of years that the economy is expected to expand in a 10-year period?
- Greater than six years
 - Less than six years
 - Six years
 - Insufficient information

48. The probability that ABC stock will experience a positive earnings year is 32%. What is the probability that this stock will experience two positive earnings years over a five-year period?
- 18.4%
 - 40.0%
 - 32.2%
 - 32.0%
49. Which of the following statements least accurately describes the information that may be obtained from an analysis of variance (ANOVA)?
- The confidence interval of the mean of the dependent variable
 - The regression sum of squares
 - The variance of the dependent variable
 - The sum of squares of the error terms
50. If a mutual fund bought for N200,000 three years ago was worth N251,200 two years ago, N191,200 last year, and N169,200 today, what would be the best estimate of its annual geometric rate of return?
- 3.3%
 - 5.4%
 - 9.8%
 - 7.0%
51. Which of the following hypothesis statements would not entail a two-tailed test?
- The mean difference of two populations is greater than 2.3%.
 - The variance of a population is equal to 14.5%.
 - The variances of two populations are equal.
 - The population average return equals 15.4%.
52. Which of the following test statistics should be used when conducting a hypothesis test for the mean of a population whose variance is known and the sample size is large?
- F-distribution
 - Chi-square
 - Z-distribution
 - T-distribution
53. Which of the following statements is incorrect with the following regression equation: $y = a + bx$?
- "y" is the dependent variable.
 - "a" is what the outcome is expected to be when the independent variable is zero.
 - "x" is the slope of the equation.
 - The error term can be measured as the difference between an actual outcome and the "y" value for that specific situation.
53. Which of the following is true with respect to the nature of statistics?
- Descriptive statistics is the process of summarizing large quantities of data.
 - Statistics refers to parameters that are specific to a population.
 - Statistical inference is a form of regression analysis.
 - Sample size should have no impact on the accuracy of statistical findings.

54. List the following steps in hypothesis testing in their proper order:
 I. Collect the data and perform the relevant calculations.
 II. Select the test statistic that will test the hypothesis.
 III. State the decision rule.
 IV. State the hypothesis.
- A. I, IV, III, II
 B. II, I, IV, III
 C. III, IV, I, II
 D. IV, II, III, I
55. How much will \$5,000 deposited today be worth in seven years if the bank is paying an interest of 9% compounded quarterly?
- A. \$9,323
 B. \$5,843
 C. \$9,140
 D. \$55,836
56. A cost function is: $C(N) = Q^2 - 40Q + 250$; Where, Q = quantity of units produced. What quantity will minimize cost?
- A. 32
 B. 20
 C. 30
 D. 40
57. One of the following statements about the linear programming model is wrong:
- A. Linear programming is applied strictly to maximization problems.
 B. One of the assumptions of the linear programming model is non-negativity.
 C. Simplex and graphical methods are the two approaches to solving linear programming problems.
 D. There could be 'slack variables' available at the optimum point in a linear programming solution.
58. What is a zero matrix?
- A. A matrix in which every element is zero
 B. A matrix in which one column is zero
 C. A matrix that has one of its elements as zero
 D. None of the above
59. The least squares regression line is the line:
- A. which is determined by use of a function of the distance between the observed Y's and the predicted Y's.
 B. which has the smallest sum of the squared residuals of any line through the data values.
 C. for which the sum of the residuals about the line is zero.
 D. which has all of the above properties
60. If the base year for an index is 2005 and the value of the index in 2008 is 156.1, by what percent has the measure grown over those 3 years (in total)?
- A. 156.1 %
 B. 100 %
 C. 5.61 %
 D. 56.1 %

SECTION B

Question 2 - Financial Accounting and Financial Statement Analysis

- 2(a) Explain the accounting concept of going concern. *(1 mark)*
- 2(b) List three categories of users of financial ratio and the primary purpose they use ratios for. *(2 marks)*
- 2(c) List three possible components of equity in the balance sheet of a reporting entity. *(1 mark)*

Question 3 - Economics and Financial Markets

- 3(a) Distinguish clearly between GDP and GNP in national income accounting. *(1 mark)*
- 3(b) At what point does a firm in perfect competition maximize profit? *(1 mark)*
- 3(c) What is the relationship between inflation and employment with reference to the modern version of Phillip's curve? *(1 mark)*

Question 4 - Quantitative Analysis and Statistics

- 4(a) Explain briefly the concept of 'time value of money' *(1 mark)*
- 4(b) Find the expression for dQ/dP , for the supply function $Q = P^2 + P + 1$ *(1 mark)*
- 4(c) What does 'coefficient of determination' measure? *(1 mark)*

SECTION C

Question 5- Financial Accounting and Financial Statement Analysis

Egoh Ibrahim is considering investing a substantial sum in the ordinary shares of Jalingo Limited. Having some accounting knowledge he has extracted the following information from the accounts for the last two financial years.

| | As at 31 March 2008 N'000 | As at 31 March 2009 N'000 |
|--------------------------------|---------------------------------|---------------------------------|
| ISSUED SHARE CAPITAL | | |
| N1 Ordinary Shares, Fully Paid | 100,000 | 150,000 |
| RESERVES | | |
| Share premium | 10,000 | 60,000 |
| Retained earnings | 140,000 | 160,000 |
| LOAN CAPITAL | | |
| 10% Loan Notes 2015-2016 | 40,000 | 40,000 |
| | For Year Ended 31 March 2008 | For Year Ended 31 March 2008 |
| | N'000 | N'000 |
| Net profit after tax | 60,000 | 70,000 |

Because he was disappointed with the result he obtained when he calculated the return on the equity capital employed, Egoh Ibrahim has asked for your advice.

Required:

- 5(a) Calculate the figures which prompted Egoh Ibrahim's reaction.

- 5(b) Prepare a memorandum to Egoh Ibrahim pointing out other information to be considered when comparing the return on equity capital employed over two years as a basis for his investment decision.

- 5(c) Explain why a company builds up and maintains reserves.

Question 6 - Economics and Financial Markets

The Nigerian economy is currently in equilibrium. The following figures refer to elements in its national income accounts:

| | <u>N' trillion</u> |
|------------------------|--------------------|
| Consumption (total) | 60 |
| Investment | 5 |
| Government expenditure | 8 |
| Imports | 10 |
| Exports | 7 |

6(a) What is the current equilibrium level of national income? *(4 marks)*

Assume that the Nigerian government wants to stimulate the economy by increasing government spending from the current N8 billion to N15 billion.

6(b) Using the IS-LM model, with appropriate graphs, briefly analyze the impact of this policy on the Nigerian economy. *(6 marks)*

Question 7 - Quantitative Analysis and Statistics

An investment of N100,000 yields returns of N25,000, N35,000, N30,000 and N15,000 in each of the subsequent four years.

7(a) Calculate the present value of the income stream and compare to the initial outlay, using an interest rate of 10% per annum.

7(b) Calculate the internal rate of return on this investment.