

THE INSTITUTE OF CHARTERED ACCOUNTANTS OF PAKISTAN
CERTIFIED FINANCE AND ACCOUNTING PROFESSIONAL (CFAP) EXAMINATION
EXAMINERS' COMMENTS

SUBJECT Business Finance Decisions	SESSION Winter 2020
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Passing %

Question-wise					Overall
1	2	3	4	5	
65%	51%	32%	51%	47%	49%

General comments

Overall performance of the examinees was satisfactory. The performance in the numerical parts of the questions was much better as compared to below average performance in those parts that required interpretation of numerical results, evaluation of the existing or proposed strategies and recommendation on future course of action.

Question-wise common mistakes observed

Question 1(a)

Good performance was observed in this part.

Question 1(b)

Good performance was observed in this part.

Question 1(c)

Examinees correctly agreed with the statement regarding the role of WACC as 'minimum average rate of return' but they were not able to produce appropriate justifications to support the agreement.

Question 1(d)

Examinees restricted their answers by discussing the circumstances under which current WACC can be used as the discount rate for new project investment appraisal. However, they failed to indicate other methods to determine a discount rate that could be adopted when it is not appropriate to use the current WACC.

Question 1(e)

While calculating cost of equity for determining risk adjusted discount rate, most of the examinees either skipped or incorrectly computed the re-gearing of asset beta to KPL's gearing level. Some examinees applied the formula incorrectly.

Question 2(a)

- While calculating the net present value of the new project:
 - entire sales revenue (existing and new customers both) was taken.
 - cash outflow related to working capital was started from year 1.
 - cash inflow related to working capital at end of the project was ignored.
 - capital allowance was calculated on Rs. 125 million.
 - loss on disposal of fixed asset at the end of the project was ignored.
- Calculation of MIRR was either ignored or worked-out incorrectly.

Question 2(b)

- Examinees evaluated the project by considering financial factors only and ignored non-financial factors altogether. Those who discussed non-financial factors confined their answers by mentioning the purpose of sensitivity analysis only and ignored its weaknesses.
- Benefits of simulation and other non-financial factors such as resource requirements, impact on existing customers, issues related to employees' redundancy and reactions of competitors were not discussed.

Question 3(a)

- While computing free cash flows:
 - Year 5 onwards cash flows were discounted by using discount rate based on 5th year.
 - Interest on loan was not deducted.
- In net asset valuation, brand value was not taken.
- In price to earnings valuation, price earnings ratio was not adjusted.

Question 3(b)

- Almost 46% examinees did not attempt this part of the question.
- Examinees who attempted this part were only able to comment on the suitability of two or three assumptions.

Question 4(a)

- In no hedge, selling rates were used for calculating expected exchange rate.
- In forward contract hedge, forward premium was added in current spot rate.
- In money market hedge, loan rates and deposit rates were used interchangeably.
- In over-the-counter option hedge, exercise price based on call option was taken.

Question 4(b)

Examinees drew conclusion by considering the amount of receipts under each option and ignored following issues in their discussion:

- Probability about expected exchange rate may not hold.
- Lack of flexibility in forward contract hedge.
- Borrowing requirement and its impact on gearing of the company in money market hedge.
- Impact of paying premium on company's cash flows in over-the-counter option.

Question 5(a)

Good performance was observed in this part.

Question 5(b)

Good performance was observed in this part.

Question 5(c)

- Almost 43% examinees did not attempt this part of the question.
- Examinees who attempted this part were only able to reproduce the variance amounts computed in part (a) by stating that such variances were favorable or adverse without explaining their impact to the board and actions to be taken by the board.

(THE END)