



Examiner's report

Foundation in Financial Management (FFM)

June 2016

General Comments

The examination consisted of ten objective testing questions in Section A, worth 20 marks overall and six questions in Section B, one worth 20 marks, three 10 mark questions and two 15 mark questions. All questions were compulsory.

Presentation varied from script to script, but generally layout and legibility was acceptable. Many candidates used the breakdown of the requirement to give structure to written answers.

Specific Comments – Section A

I reiterate here what I have said in past examiner's reports, that it is imperative that candidates practice the MCQ style questions, as a good mark here provides a solid base from which to attempt Section B.

Candidates are reminded that they do not lose marks for incorrect answers, and therefore, even if they are not sure what the answer should be, it is always worth 'taking a guess' and no question within Section A should be left unanswered.

The following question was not well attempted by the majority of candidates.

T Co has been asked to quote for a one-off project which will require 60 hours of skilled labour.

Skilled labour is currently fully utilised elsewhere in the company where it earns a contribution of \$5 per hour. Skilled labourers are paid \$6.40 per hour.

T Co can only hire an additional 30 hours of labour. The additional labour will be paid 25% more than T Co pays its own skilled labour.

Using relevant costing principles, what is the cost of skilled labour that should be included in the quotation?

- A** \$384
- B** \$582
- C** \$432
- D** \$684

Relevant costing techniques are regularly examined within both Section A and Section B questions, and the concept of having a scarce resource is an area which often causes candidates difficulty.

In this question, skilled labour is the scarce resource as it is fully used within the business. Although more labour can be hired in, only 30 hours is available for hire, and 60 hours are needed for the project. To fulfil the remaining 30 hours, labour will have to be taken away from its existing activities in the business.

This means that there are two elements to the calculation. Candidates need to calculate the cost of hiring in 30 hours of labour, and the cost of moving labour to the project from its existing activities.

The cost of hiring in labour is fairly straightforward as we are told that labour that is hired, costs 25% more than the internal pay rate of \$6.40. The cost of hiring in is therefore:

$$30 \text{ hours} \times \$6.40 \times 1.25 = \$240$$

We then move to the cost of moving labour from its current activities. The cost of moving the labour from its current activities is calculated as the hours required multiplied by (the cost per hour plus the contribution lost).

This would give us:

$$30 \text{ hours} \times (\$6.40 + \$5.00) = \$342$$

Adding the two elements together gives \$582 and the correct answer is B.

The majority of candidates opted for C as their answer. These candidates correctly calculated the cost of hiring the labour as \$240, but in calculating the cost of moving labour from its current activities, only took into account the cost per hour of \$6.40. Their calculation was:

$$\$240 + \$6.40 \times 30 \text{ hours} = \$432$$

Candidates need to remember to include the contribution that the organisation will lose from the current activities if labour is moved to work on the project in a calculation of this type.

Specific Comments – Section B

Candidates performance in section B was disappointing in comparison to previous sittings. The paper was set, as it always is, with easier marks to be gained from knowledge, and then the remaining marks required candidates to apply their knowledge to a scenario.

What seems to have let candidates down at this sitting was the lack of knowledge shown in some areas of the syllabus, and candidates not reading the requirement carefully and answering a different question to the one set.

There are three specific examples of where candidates showed a lack of knowledge:

- As part of a question looking at a company which has surplus cash, and the return that can be gained, candidates were asked to briefly explain the motives for holding cash according to Keynes. This is a requirement that is asked fairly regularly, but unfortunately a substantial minority of candidates did not know the motives and so did not gain three easy marks.
- A question set from the cash budgeting and forecasting area of the syllabus, required candidates to define sensitivity analysis and carry out simple sensitivity analysis on a cash budget. Candidates struggled with this, and seemed to have little knowledge of this area of the syllabus.
- A ten mark question asked candidates to describe four types of institutional investor. This was a test of knowledge, and should have provided some easy marks, but the majority of candidates did not score well in this question.

There are two question where candidates did not read the requirement carefully enough:

- As part of a question looking at assessing creditworthiness through ratios, candidates were asked to describe four limitations of using ratio analysis. Unfortunately a substantial minority described ratios that could be used to assess creditworthiness eg the current ratio, rather than looking at the limitations of ratio analysis.
- Part of a fifteen mark question examining working capital and credit management asked candidates about definition and explanation of invoice discounting. Some candidates talked about factoring, and some about a prompt payment discount, neither of which scored any marks.

The numerical questions were generally better answered, but candidates should ensure that they show all of their workings. An investment appraisal question required candidates to decide, on the basis of net present value calculations, whether existing equipment should be replaced with a more technically advanced version. This question could be approached in two ways:

1. Calculate the net present value of the existing situation, and the net present value if the new equipment is invested in, and compare the two net present values to make a decision.
2. Calculate the net present value of the incremental flows that arise if the new equipment is invested in.

Some candidates included some cash flows from approach one and some from approach two all in the same net present value calculation, and did not show how the cash flows had been calculated. It is very difficult to award method marks if workings are not shown. In future candidates are advised to use one approach they understand better rather than mix the two..

Conclusion

This was a paper that a candidate who had studied the whole syllabus and took care when reading the requirement could have passed. Those that did not pass showed a lack of knowledge, and did not gain the easier marks that were available in Section B.