

Examiner's report

P4 Advanced Financial Management
September 2017



ACCA

General Comments

This exam paper is in two sections. Section A consisted of a compulsory question for 50 marks. Section B consisted of three questions of 25 marks each, from which candidates had to answer two questions. Two of the three questions in Section B for this examination consisted of a mixture of computational and discursive elements. The third optional question was wholly discursive. This is an advanced level option paper which builds upon the knowledge and skills examined in F9, Financial Management. At this advanced stage, candidates will be required to demonstrate their ability to read and digest quickly, comprehensive and detailed questions, apply relevant knowledge and skills and exercise the professional judgement expected of a senior financial person, in recommending or making financial management decisions that are likely to affect the entire business organisation. For example, Section A normally sets out a complex business scenario in the form of a case study that requires candidates to demonstrate their ability to understand, deal and communicate about strategic issues that a senior financial manager or advisor may be expected to encounter in his or her career.

Like a senior financial person at work, a candidate is expected to read a business brief in the form of an exam question here carefully and decide on a relevant methodical approach to achieve the brief's objectives. Senior management work under tight deadlines, and hence prioritising and managing your time is crucial to performing well under examination conditions.

In this exam, time management was essential as evidenced by a large number of candidates who did not fully attempt three questions. A candidate who leaves out parts of questions unanswered will be marked out of less than 100%, and therefore considerably reduces the chance of gaining a pass.

This examination included a significant amount of technical content to test a candidate's ability to perform them. Invariably, a candidate will be expected to assess the findings of the technical computations within the context of the question's scenario as for example in Question 1.

Answers that score high marks show a reasoned structure, appropriate narrative discussions that are succinct, clear and relevant to the question asked and easy to follow numerical workings supported where appropriate by brief notes. Achieving this in a P4 exam will ensure a candidate is on track to passing it.

The main reasons for candidates performing less well were:

- i) Not completing sufficient questions. In many instances, one of the optional questions was attempted very briefly or not at all. This is possibly the most common reason for not passing this exam;
- ii) Poor exam technique. Too much time was spent in attempting a question part that a candidate has prepared well, thus leaving insufficient time to attempt the remaining questions;
- iii) Lack of question practice under examination conditions. Candidates who have practiced attempting questions under examination conditions should be better prepared to manage their time more effectively;
- iv) Spending time on unnecessary introductions or definitions or reproducing figures

- already given in the question;
- v) Illegible scripts. Markers need to be able to read the answers and they will find it hard to award marks to answers that are very difficult to read either because of poor handwriting or have workings that have been crossed out and rewritten over;
- vi) Numerical answers that were poorly structured. It is difficult to award marks when a candidate's calculation does not indicate the relevant currency, for example in Question 1 b) or no workings were given as to how their figures were arrived at;
- vii) Written answers that were poorly structured. It was difficult to identify in some answers whether candidates were discussing advantages or disadvantages, assumptions or risks;
- viii) Focussing more on either the numerical or discursive parts of the exam paper. Candidates need to be aware that a balanced approach is required to achieve a pass;
- ix) Not carefully reading the requirements of a question and therefore not answering the question that was asked;
- x) Too much effort often being put into answering question parts worth only a few marks whilst less effort made in answering question parts worth more marks.

Specific Comments

Question One

This was a compulsory 50-mark question. It required candidates to provide reasoned advice supported by relevant workings, in evaluating the feasibility in manufacturing goods in a country that is close to the company's overseas export market, and being subject to a changing macroeconomic and trading environment.

The question's case scenario was complex and required candidates to undertake various calculations and discuss the issues therefrom. Thus, it was essential that the candidate managed the volume of information provided effectively, in order to provide coherent and detailed answers.

Part a) asked candidates to distinguish between free trade areas and customs unions, and the role of the World Trade Organisation.

Many candidates were not able to distinguish clearly between free trade areas and customs unions, and the World Trade Organisation was often given a role beyond its remit in real life. It is important to note that syllabus areas such as this, which may be overlooked in study and revision, will be examined and can be a source of relatively easy to earn marks.

Part b) required an evaluation based on a net present value analysis within an international investment appraisal context, and the implications when macroeconomic and trading environment change.

Candidates need to be aware that investment appraisal using net present value analysis is a progression from their knowledge of F9, and hence form a core element of this advanced syllabus. It was disappointing to find that many candidates were unable to apply the purchasing power parity theory to forecast exchange rates. Equally, many were unable to appropriately inflate sales revenues and costs. Furthermore, a significant number of candidates did not convert the plant and machinery investment into the local currency first before depreciating it annually.

It was also disappointing to find that many candidates were unable to perform the basic conversion

from one currency into another.

A project's net present value analysis should include all relevant free cash flows arising from undertaking it, not merely those cash flows remitted back to the parent company as a number of candidates erroneously believed.

Time management is important in this exam and markers were concerned to find that a fair proportion of candidates wasted time and earned no marks when they reproduced the same information that has already been provided in a table in the question itself.

This question part required a report based on an evaluation that covered three countries, three different currencies and two project proposals. Therefore, it certainly would have helped candidates to earn marks if their report had headings and sub headings, tables and calculations that were properly labelled, workings that showed intermediate steps and currencies that were clearly identified in the cash flow statements.

The report format should have an introduction; display a good structure and presentation with appropriate use of appendices, followed by a conclusion/recommendation that is relevant and meaningful to the foregoing discussion. Many candidates could have easily earned a professional mark available by providing an appropriate conclusion to the report.

A fair proportion of candidates showed a reasonably good level of theoretical knowledge and ability in this question part, but their answers often indicated a lack of commercial awareness and business sense. Candidates who demonstrated an awareness of the business environment that is relevant to the case study scenario often score good marks.

Part c) required a discussion about the composition of senior management strategy such that the board skills and experience can be utilised in an efficient, effective and transparent way.

Candidates who identified and then discussed the costs and benefits of different compositions of senior management teams, scored well in this question part.

Question Two

This question dealt with issues in raising various sources of finance for an acquisition.

Part a) required a discussion of the merits of specific sources of finance for an acquisition proposal and to recommend the most appropriate mode of financing.

Candidates scored well when they presented a good structure in their discussion with a clear reference to the specific financing sources. Candidates who discussed without focussing on the specific scenario in the question, or kept repeating points already discussed, received considerably less marks.

A common misconception by a significant number of candidates is that a rights issue will cause a dilution of control.

Part b) considered the regulatory and ethical issues when raising financing capital.

Candidates did reasonably well when they distinguished between ethical and regulatory issues and then organised their discussion points. The unsatisfactory answers were vague and repeated

information from the question. Also, a significant number of candidates scored low marks because they did not discuss each ethical or regulatory issue in enough depth when there were ten marks available in this question part.

Question Three

This question considered financial issues in a business re-organisation through an unbundling exercise.

Part a) required a calculation of how much an unbundled part of a company may be sold for and the impact of its sale on the company's financial structure and performance.

Many candidates scored high marks in determining the expected sale proceeds. However, the majority of candidates omitted to add back the interest saved from paying off the loan when calculating the adjusted earnings per share.

A large number of candidates erroneously either included the loan already repaid or ignored the bank loans in determining the company's weighted average cost of capital. Quite a few candidates made a basic error in using market return instead of market premium when calculating a company's cost of equity.

Part b) required an evaluation of the decision to sell off the unbundled part of the company. Most discussions were narrowly focused on the results from the calculations produced in part a) and ignored the important non-financial strategic factors relating to the scenario. Very few candidates made full use of the information given in the scenario to produce a balanced discussion, with points for and against the sale.

Question Four

This was the most popular optional question and it focussed on treasury and advanced risk management techniques.

Part a) asked for reasoned advice on the most appropriate strategy in using financial derivatives to hedge against interest rate risk.

This was an interest rate hedging question similar to those asked in previous diets, and it allowed well prepared candidates to demonstrate their knowledge which many did and generally scored highly. Some candidates omitted to identify which hedging instruments they had chosen for example, a buy vs sell futures or a put vs call options, making it difficult for markers to award marks. A number of candidates omitted to discuss their results and/or make a recommendation meaning that they could not be awarded these marks.

Part b) examined the role of the treasury function in different geographical locations, in managing risk exposure and maximising corporate value.

Candidates must read a question and its requirements carefully. In this question, many candidates misread the question and answered it in terms of national or global functions, some without even mentioning regional functions, which was asked for in the question. Their answers indicate that they reproduced their textbook knowledge of centralised (global) versus decentralised (country) treasury functions instead of applying their knowledge to the question asked.

