

Examiner's report

P4 Advanced Financial Management June 2016

The ACCA logo consists of the letters 'ACCA' in a bold, white, sans-serif font, centered within a solid black square.

General Comments

This exam paper consisted of two sections. Section A contained a compulsory 50-mark question. Section B contained three 25-mark questions each, from which candidates had to answer two questions. All questions in the examination consisted of both computational and discursive elements.

This is an advanced level optional paper which builds upon the knowledge and skills examined in Paper F9, Financial Management paper. At this advanced stage, candidates are required to demonstrate their ability to read and digest quickly, comprehensive and detailed questions, apply relevant knowledge and skills, and to exercise the professional judgement expected of a senior financial adviser, 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 which 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. As an illustration, the Section A question one on this exam paper tests a candidate's ability to provide sound advice supported by relevant workings, in a coherent report, of a potential international investment decision, and to consider risks, assumptions made and issues such as environmental and ethical behaviour.

Like a senior financial person at work, a candidate is expected to read a business brief in the form of an exam question carefully, take notes and decide on a relevant methodical approach to meeting the brief's objectives. Senior management work under scheduled deadlines, and hence prioritising and good time management is crucial to performing well under examination conditions. Business reports and proposals are expected to be succinct, professionally written and easy to read with clear headings and conclusions. A candidate, who does not demonstrate this approach, will fail to earn the full professional marks that are easily available in question one.

The hallmark of a good piece of written work is evidenced by a reasoned structure, narrative discussions that are relevant and in sufficient detail, and clear and easy to follow numerical workings supported where appropriate by brief notes. Achieving it in this exam will ensure a candidate is on track to passing it.

This examination also includes a significant amount of technical content dispersed across the questions, 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.

The overall performance of the candidates was better than the previous few sittings, and in line with the overall trend of recent examinations. The main reasons for candidates performing less well were:

- i) Lack of detailed knowledge of parts of the syllabus areas and leaving whole or parts of questions unanswered because of this;
- ii) Poor time management. Too much time spent in carrying out relatively simple calculation tasks;
- iii) Inability to perform basic arithmetic calculations;
- iv) Not structuring question one, part (a) in a report format and thereby not gaining all the professional marks;
- v) Presenting the discursive answers in brief bullet-point format, often in incomplete sentences, as statements and not as discussion-based, analytical or evaluative narrative;

- vi) Focussing more on either the numerical parts or the discursive parts of a question, instead of a balanced approach;
- vii) Not reading the requirements of the question and therefore answering the question incorrectly. This was particularly relevant to questions 3(b), 3(c) and 4(a);
- viii) Not using the reading time effectively to plan a strategic approach to tackling the paper and to choose the optional questions wisely.

Specific Comments

Question One

This was the 50-mark compulsory question where the case study scenario asked candidates to consider an international capital investment decision and an adjusted present value in part (a). The calculations were to be presented within a report, and the better answers included these as appendices. The report also asked for discussions and evaluation of assumptions, non-risk related issues and the impact of a possible joint venture **after** the initial project has finished.

On the whole, this part was done well by many candidates. Common calculation errors included:

- Not able to inflate cash flows correctly;
- Not translating cashflows between currencies correctly;
- Not being able to calculate tax allowable depreciation correctly;
- Not able to deal with additional tax payable, additional contribution earned and adjusted present value calculations where investments were made in two years instead of just one year.

Some candidates caused time-pressure problems for themselves by presenting relatively simple calculations as separate workings. For example, the question contained a simple requirement to inflate fixed costs and this task could have been accomplished easily without a separate working. Common discursive errors included articulating very simplistic assumptions, whereas at the professional level candidates need to be able to demonstrate a clear link with the scenario instead of just repeating a pre-prepared list of assumptions.

A significant minority of candidates misread the question and assumed that the current project could be done using a joint venture relationship. The joint venture related to investments made after the initial project investment. It is important that the candidates read and understand the question scenario fully.

Four professional marks were available for the report for part (a). It was disappointing that many candidates did not draft their answers in a report format, with a brief introduction, appendices and conclusion. Some candidates did not follow any report format and the overall structure and presentation was not neat and therefore these candidates gained few or no professional marks.

Question one, part (b) was unsatisfactorily attempted by the majority of candidates. It asked candidates to discuss the impact of undertaking the project on environmental and corporate objectives, and how this impact could be mitigated. Most answers were very general and did not relate well to the scenario. It appeared either that candidates had considered this to be a minor area of the syllabus and therefore not worthy of detailed study, or they repeated previously prepared answers with little or no attempt to make the discussion relevant to the scenario. Very few answers attempted to offer mitigations.

Question Two

This was a 25-mark optional question. In part (a) candidates were required to undertake interest rate hedging using FRAs, futures and options. Well-prepared candidates earned the majority of the marks for this part of question two. However, less well prepared candidates struggled with it and gained few marks. Although the question asked for costs in amounts and as percentages, and for candidates to show appropriate calculations, a few candidates tried to just show percentages and/or costs for a single contract, which was less than what the requirement asked for.

Part (b) asked candidates to use the value-at-risk methodology to estimate and comment on the level of confidence that the net present value of the project will not be negative. This part was not done well by many candidates. Similar to question one, part (b) it seems that candidates considered this part of the syllabus to be a minor area and had not studied it in detail. They therefore did not know how to approach answering this question.

Part (c) asked candidates to consider the factors which would determine the degree to which a treasury department is centralised. Many candidates did this part well and gained the majority of marks. Weaker answers just provided lists of advantages and disadvantages without considering the responses in terms relevance to the question scenario.

Question Three

This was a 25-mark optional question on mergers and acquisitions. Part (a) was a discursive question which asked candidates to discuss the advantages and disadvantages of an acquisition from the viewpoint of the acquirer. The majority of candidates did this part well, with many of the candidates providing a balanced discussion between advantages and disadvantages. Stronger responses related the advantages and disadvantages to the question scenario and weaker responses did not.

The responses to part (b) were mixed. Candidates who understood how to calculate PE ratios and understood the factors leading to their change, produced clear succinct answers and earned all the related marks. However, many candidates did not either read the requirement of the question, did not understand what was required or did not know how to calculate PE ratios. These candidates provided computations which were not relevant to the question and gained few marks.

Few candidates achieved high marks for part (c) because either they did not know what was required or did not know how to calculate the revised EPS figures and gearing figures. A number of candidates also decided to calculate the gain/loss of the acquisition, although this was not asked for in the question.

Question Four

Part (a) asked candidates to perform relatively simple valuation calculations to estimate the value of various divisions of a company and then candidates were asked to discuss which parts of the business they would consider disposing. A significant number of candidates had difficulty undertaking the valuation calculations and a sizable number attempted to value the entire company instead of parts of the company. The discussion tended to be quite general and not targeted specifically to requirement of the question or to the narrative of the question. It also appeared that many candidates were not well-prepared for this type of question, but were attempting to answer it. General and/or weak discussions did not gain many marks.

Part (b) asked candidates to consider staff reduction proposals in terms of the impact on relations with shareholders, with employees and to discuss the ethical implications thereon. This part was answered quite well by many candidates and the answers provided a good and wide-ranging discussion. However, a sizable number of responses did not consider the ethical implications of the proposals in any/sufficient depth.

Conclusion

To sum up, candidates need to be able to apply their understanding and knowledge of advanced financial skills to pass the P4 examination. Sustained study, over a long period of time, is an essential pre-requisite for success. In this paper, successful candidates demonstrated this clearly, while candidates, who did not achieve a pass, did not demonstrate sufficient understanding and knowledge of all the topics in the Advanced Financial Management syllabus. In addition to this, well-presented and well-structured answers, directly addressing the requirements of the question, and using the reading time appropriately, are essential requirements for success.