South Tuen Mun Government Secondary School
Business, Accounting and Financial Studies
Financial analysis Quiz #1

Name:____ Class: ______ No(____)

1. What is the ultimate goal of a firm or listed company? (2 marks)

2. Describe the FOUR major kinds of financial decisions of a firm? (4 marks)

3. Name THREE kinds of short-term assets? (3 marks)

4. What are operating expenses? (2 marks)

5. What are operating profit? (2 marks)

6. Define accounting/financial ratios. (2 marks)

7. What are the functions of financial ratios? (4 marks)

8. What are the limitations of ratio analysis? (4 marks)

Financial analysis Quiz#1

1) The ultimate goal of a listed company isto maximise stockholders' wealth.Stockholders' wealth can be measured by the market value of the shares they hold. Therefore, in order to maximize stockholders' wealth, a listed company should maximise its stock price. As a result, the ultimate goal of a listed company is to maximise its stock price.

2) Financial management refers to the management of the financial resources and financial obligations of a firm in order to achieve the firm's goals.

The four major kinds of decisions involved in the financial management in a firm include:

• Investment decisions: (where to invest) to identify good investment projects in order to maximize owners' wealth.

• **Financing decisions: (how to obtain funding)** chooses the right capital structure to reduce the overall cost of capital in order to engage in more profitable projects.

• **Dividend decisions:** determines the amount and form of dividends a firm should pay.

• **Working capital decisions:** involves the management of firm's short-term assets and liabilities.

3) **Short-term assets:** cash, inventory, account receivable

4) **Operating expenses**: refer to expenses that arise during the operation of a business

5) **Operating profits:** is the profit left after deducting all types of operating expenses, but no interest expenses and tax, from gross profit

6) **Accounting /financial ratios** express relationships between different financial statements.

7) **the functions of financial ratios** is to measure a firm's **profitability** (earning power of a firm), **liquidity** (a firm's ability to repay its short-term liabilities when due), **solvency** (the ability of a firm to repay its liabilities, both short-and long term when due) and **management efficiency** (measure how efficiently a firm utilizes its assets).

8) **Limitations of ratio analysis:**

- Accounting ratios cannot capture certain **quantitative information** about a firm.
- As ratios analysis is based on a firm's past data, it may not be able to **reflect the firm's future** financial condition.
- If firms have chosen **different accounting practices**, it would be difficult to compare their ratios
- It is difficult to **identify industrial norms** for firms with a unique mix of businesses
- Ratio analysis only helps reveal the source of a potential problem/success on the surface.