CHAPTER 3

Financial Analysis and Planning – Ratio Analysis

MULTIPLE CHOICE QUESTIONS

1. Ratio Analysis aid in ___________.
(*a*) Financial accounting
(*b*) Cost accounting
(*c*) Decision making
(*d*) None of the above

2. Which of the following is not the advantage of ratio analysis?
(*a*) Forecasting
(*b*) Inter-firm Comparison
(*c*) Historical analysis
(*d*) Clues to further investigation

3. Which of the following is not the limitation of ratio analysis?
(*a*) Not free from bias
(*b*) Only symptoms and not cure
(*c*) Only quantitative analysis and not qualitative analysis
(*d*) Simplicity

4. Ratio analysis facilitates ___________ comparisons.
(*a*) Inter-firm
(*b*) Intra-firm
(*c*) Pattern
(*d*) All of the above

5. Liquidity ratios measures ___________ obligations.
(*a*) Short - term
(*b*) Long - term
(*c*) Very short - term
(*d*) Both (*a*) & (*b*)

6. A very high current ratio will:
(*a*) increase the profitability
(*b*) have adverse impact on profitability
(*c*) not affect the profitability
(*d*) None of the above

7. A very high current ratio may be due to:
(*a*) pilling up inventory
(*b*) inefficiency in collection of debtors
(*c*) high balances in cash and bank without proper investment
(*d*) all of the above

8. Traditionally, a current ratio of __________ is considered to be a satisfactory ratio.

(*a*) 2:1
(*b*) 1:1
(*c*) 1:2
(*d*) None of the above

9. A firm seeks to increase its current ratio from 1.5 before its closing date of the accounts. The action that would make it possible is:

(*a*) Delaying payment of salaries
(*b*) Increase charge for depreciation
(*c*) Making cash payment to creditors
(*d*) Selling marketable securities for cash at book value

10. Which one of the following is not a quick assets:

(*a*) Debtors
(*b*) Marketable securities
(*c*) Cash at bank
(*d*) Prepaid expenses

11. The ratio which measures the average period for which quick assets are available to meet average daily operating expenses is:

(*a*) Absolute cash ratio
(*b*) Current ratio
(*c*) Quick ratio
(*d*) Interval measure ratio

12. A low interval measure ratio is indicator of:

(*a*) Short term profitability
(*b*) Short term liquidity
(*c*) Long term profitability
(*d*) Long term liquidity

13. Fixed assets ratio is __________.

(*a*) Liquidity ratio
(*b*) Activity ratio
(*c*) Solvency ratio
(*d*) Profitability ratio

14. Debt-service coverage ratio is __________.

(*a*) Liquidity ratio
(*b*) Activity ratio
(*c*) Solvency ratio
(*d*) Profitability ratio

15. Proprietory ratio is __________.

(*a*) Liquidity ratio
(*b*) Activity ratio
(*c*) Solvency ratio
(*d*) Profitability ratio

16. Interest coverage ratio is __________.

(*a*) Liquidity ratio
(*b*) Activity ratio
(*c*) Solvency ratio
(*d*) Profitability ratio

17. Return on total assets is __________.

(*a*) Liquidity ratio
(*b*) Activity ratio
(*c*) Solvency ratio
(*d*) Profitability ratio

18. Dividend payout ratio is __________.

(*a*) Liquidity ratio (*b*) Activity ratio

(*c*) Solvency ratio (*d*) Profitability ratio

19. Capital gearing ratio is __________.

(*a*) Liquidity ratio (*b*) Activity ratio

(*c*) Solvency ratio (*d*) Profitability ratio

20. Solvency ratio measures __________ obligations.

(*a*) Short-term (*b*) Long-term

(*c*) Very Short-term (*d*) None of the above

21. A __________ debt-equity ratio indicates a high safety margin for creditors.

(*a*) high (*b*) low

(*c*) very high (*d*) nil

22. __________ ratio measures the proportion of total assets financed by the equity.

(*a*) Capital gearing ratio (*b*) Debt-equity ratio

(*c*) Total assets to debt ratio (*d*) Proprietory ratio

23. A __________ proprietory ratio indicate that the firm is not taking benefit of trading on equity.

(*a*) high (*b*) low

(*c*) very low (*d*) nil

24. If the capital gearing ratio is less than 1, the company is said to be __________ geared.

(*a*) Highly (*b*) Lowly

(*c*) Either of the above (*d*) None of the above

25. __________ measures the efficiency with which fixed assets are being utilized.

(*a*) Current ratio (*b*) Fixed assets ratio

(*c*) Fixed assets turnover ratio (*d*) Debt-equity ratio

26. A low debtors' turnover ratio may involve risk of __________.

(*a*) Bad debts (*b*) High interest cost

(*c*) Both (*a*) & (*b*) (*d*) None of the above

27. Gross profit ratio may increase due to which of the following factor:

(*a*) higher sales price with constant cost of goods sold

(*b*) lower cost of goods sold with constant sales price

(*c*) A combination of (*a*) & (*b*)

(*d*) All of the above

28. The operating profit ratio may increase due to which of the following factor:

(*a*) Higher gross profits

(*b*) Lower operating expenses

(*c*) A combination of (*a*) & (*b*)

(*d*) All of the above

29. ___________ ratio indicate what portion of sales is left to pay dividend and to create reserves.

(*a*) Net profit

(*b*) Gross profit

(*c*) Expense

(*d*) Operating profit

30. A highly geared company is exposed to:

(*a*) Business risk

(*b*) Financial risk

(*c*) Interest risk

(*d*) Inflation risk

31. The industries where demand is volatile and profits subject to fluctuation should have:

(*a*) high level of gearing

(*b*) low level of gearing

(*c*) any level of gearing

(*d*) None of the above

32. A longer creditors payment period as compared to industry indicates:

(*a*) suppliers are willing to supply on too long credit period

(*b*) operating in sellers market

(*c*) operations are being financed by suppliers free of interest

(*d*) damages credit rating and relationship with suppliers

33. If a firm's total debt-to-equity ratio is higher than the industry average but the long-term debt-to-equity ratio is lower than the industry average, this suggests that the firm:

(*a*) has a higher level of short-term liabilities than the industry

(*b*) is less profitable than the industry

(*c*) is unable to make its interest payments

(*d*) is holding a larger amount of current assets

34. Return on investment can be increased by:

(*a*) Increasing the profit margin

(*b*) Reduction of invested capital

(*c*) Increasing the investment turnover

(*d*) All of the above

35. Four companies have the following P/E Ratios:

Company	A	B	C	D
P/E Ratio	17	24	12	8

Which of the following statement about the companies is true?

(*a*) B's share price must be twice that of C

(*b*) A's share price is 17 times of its earnings

(*c*) D has the lowest share price relative to its earning growth

(*d*) B has the high expectations of future earnings growth

36. Ratio of Net sales to Net working capital is a:

(*a*) Profitability ratio
(*b*) Liquidity ratio
(*c*) current ratio
(*d*) Working capital turnover ratio

37. Long-term solvency is indicated by:

(*a*) Debt/equity ratio
(*b*) Current ratio
(*c*) Operating ratio
(*d*) Net profit ratio

38. Ratio of net profit before interest and tax to sales is:

(*a*) Gross profit ratio
(*b*) Net profit ratio
(*c*) Operating profit ratio
(*d*) Interest coverage ratio

39. Observing changes in the financial variables across the year is:

(*a*) Vertical analysis
(*b*) Horizontal analysis
(*c*) Peer-firm analysis
(*d*) Industry analysis

40. The Receivable-Turnover ratio helps management to:

(*a*) Managing resources
(*b*) Managing inventory
(*c*) Managing customer relationship
(*d*) Managing working capital

41. Which of the following is a liquidity ratio?

(*a*) Equity ratio
(*b*) Proprietary ratio
(*c*) Net Working capital
(*d*) Capital gearing ratio

42. Which of the following is not a part of Quick assets?

(*a*) Disposal investments
(*b*) Receivables
(*c*) Cash and cash equivalents
(*d*) Prepaid expenses

43. Capital Gearing ratio is the fraction of:

(*a*) Preference share capital and debentures to Equity share capital and reserve & surplus
(*b*) Equity share capital and reserve and surplus to preference share capital and debentures
(*c*) Equity share capital to total assets
(*d*) Total assets to equity share capital

44. From the following information, calculate P/E ratio:

Equity share capital of ₹10 each	₹8,00,000
9% Preference share capital of ₹10 each	₹3,00,000
Profit (*a*fter 35% tax)	₹2,67,000
Depreciation	₹67,000
Market price of equity shares	₹48

(*a*) 15 times
(*b*) 16 times
(*c*) 17 times
(*d*) 18 times

45. Equity multiplier allows the investor to see:

(*a*) What proportion of interest on debt can be covered from earnings available to equity shareholders?

(*b*) How many times preference share interest be paid from earnings available to equity shareholders?

(*c*) What portion of return on equity is the result of debt?

(*d*) How many times equity is multiplied to get the value of debt?

46. A company has average accounts receivable of ₹10,00,000 and annual credit sales of ₹60,00,000. Its average collection period would be:

(*a*) 60.83 days (*b*) 6.00 days

(*c*) 1.67 days (*d*) 0.67 days

47. A company has net profit margin of 5%, total assets of ₹90,00,000 and return on assets of 9%. Its total asset turnover ratio would be:

(*a*) 1.6 (*b*) 1.7

(*c*) 1.8 (*d*) 1.9

48. What does Q ratio measures?

(*a*) Relationship between market value and book value per equity share.

(*b*) Proportion of profit available per equity share

(*c*) Overall earnings on average total assets

(*d*) Market value of equity as well as debt in comparison to all assets at their replacement cost

49. Calculate operating expenses from the information given below:

Sales	₹75,00,000
Rate of income tax	50%
Net profit to sales	5%
Cost of goods sold	₹32,90,000
Interest on debentures	₹60,000

(*a*) ₹41,00,000 (*b*) ₹8,10,000

(*c*) ₹34,00,000 (*d*) ₹33,90,000

50. Which of the following is not a profitability ratio?

(*a*) P/E Ratio (*b*) Return on capital employed (ROCE)

(*c*) Q Ratio (*d*) Preference Dividend Coverage Ratio

51. Profit margin (net) of B.S. Ltd. is 7% while turnover is 3 times of its capital. The return on investment of the concern is ___________.

(*a*) 18% (*b*) 19%

(*c*) 20% (*d*) 21%

52. If current ratio is given as 2.5, liquid assets are ₹60,000, then the value of the stock will be:

(*a*) ₹20,000 (*b*) ₹30,000

(*c*) ₹40,000 (*d*) ₹50,000

53. SK Ltd., has sales of ₹7,74,000 with after-tax profit of ₹93,000. If the company's asset turnover is 2.55, its return on assets (ROA) is:

(*a*) 11.83% (*b*) 26.54%

(*c*) 30.64% (*d*) 21.69%

54. For the financial year ended as on March 31, 2023 the figures extracted from the balance sheet of SK Ltd. is as under:

Opening stock ₹29,000; Purchases ₹2,42,000; Sales ₹3,20,000; Gross profit 25% of sales; Stock turnover ratio will be:

(*a*) 8 times (*b*) 6 times

(*c*) 9 times (*d*) 10 times

55. If credit sales for the year is ₹5,40,000 and debtors at the end of year is ₹90,000, the average collection period will be:

(*a*) 30 days (*b*) 61 days

(*c*) 91 days (*d*) 120 days

56. What will be the effect on present current ratio of 2, if there is bills payable discharged?

(*a*) Improve (*b*) Decline

(*c*) No effect (*d*) None of the above

57. What will be the effect on present current ratio of 0.7:1, if there is payment of final dividend already declared?

(*a*) Improve (*b*) Decline

(*c*) No effect (*d*) None of the above

58. What will be the effect on present debt-equity ratio of 2, if there is redemption of debentures for cash?

(*a*) Improve (*b*) Decline

(*c*) No effect (*d*) None of the above

59. What will be the effect on present gross profit ratio of 20%, if there is purchase of goods of ₹25,000?

(*a*) Improve (*b*) Decline

(*c*) No effect (*d*) None of the above

60. Calculate the quick ratio from the following data:

Current liabilities – ₹2,40,000; Working capital – ₹7,20,000; Creditors – ₹40,000; Inventory – ₹2,40,000;

(*a*) 2:1 (*b*) 3:1

(*c*) 2.5:1 (*d*) 3.5:1

61. SK Ltd. has a current ratio of 5:1. Its stock is ₹1,60,000 and its current liabilities are ₹1,60,000. Calculate the liquid ratio.

(*a*) 1.5:1 (*b*) 2.5:1

(*c*) 3:1 (*d*) 4:1

62. ABC Ltd. has a current ratio of 2:1 and quick ratio of 1.5:1. Its current liabilities are ₹40,000. Calculate the value of stock.

(*a*) ₹22,000 (*b*) ₹20,000

(*c*) ₹18,000 (*d*) ₹16,000

63. AB Ltd. has a current ratio of 3:1. Its net working capital is ₹2,00,000 and its inventory is ₹2,20,000. Calculate quick ratio.

(*a*) ₹1,00,000 (*b*) ₹90,000

(*c*) ₹80,000 (*d*) ₹70,000

64. Calculate capital gearing ratio from the following information:

15% long term debts – ₹4,00,000; 18% Preference share capital – ₹50,000; Equity share capital – ₹1,00,000; Reserve & Surplus – ₹75,000; Preliminary expenses – ₹25,000.

(*a*) 2:1 (*b*) 2.5:1

(*c*) 3:1 (*d*) 3.5:1

65. Calculate the interest coverage ratio form the following information:

Net profit after interest and tax ₹60,000; Interest on long-term debt ₹30,000; Tax @ 50%

(*a*) 4 times (*b*) 5 times

(*c*) 6 times (*d*) 7 times

66. Calculate the preference dividend coverage ratio from the following information:

15% Debentures ₹8,00,000; Net profit before interest and tax ₹6,00,000; Tax @ 50%;
16% ₹1,00,000 Preference shares of ₹100 each.

(*a*) 13 times (*b*) 14 times

(*c*) 15 times (*d*) 16 times

67. Fixed assets (at cost) ₹6,00,000; Accumulated depreciation till date ₹1,00,000; Trade investments ₹50,000; Current assets ₹2,20,000; Current liabilities ₹1,70,000; Cash sales ₹2,00,000; Gross credit sales ₹8,50,000; Sales return ₹50,000. Calculate capital turnover ratio.

(*a*) 1.5 times (*b*) 1.67 times

(*c*) 1.75 times (*d*) 1.87 times

68. Earning per share ₹20; Dividend per share ₹10; Market price per share ₹200. Calculate Earning Yield.

(*a*) 10% (*b*) 100%

(*c*) 20% (*d*) 5%

69. Market value of an equity share ₹40; Book value of an equity share ₹25; Calculate the market response ratio.

(*a*) 160% (*b*) 62.50%

(*c*) 50% (*d*) 75%

Answer Key

1. (*c*)	**2.** (*c*)	**3.** (*d*)	**4.** (*d*)	**5.** (*a*)	**6.** (*b*)	**7.** (*d*)	**8.** (*a*)	**9.** (*c*)	**10.** (*d*)
11. (*d*)	**12.** (*b*)	**13.** (*c*)	**14.** (*c*)	**15.** (*c*)	**16.** (*c*)	**17.** (*d*)	**18.** (*d*)	**19.** (*c*)	**20.** (*b*)
21. (*b*)	**22.** (*d*)	**23.** (*a*)	**24.** (*b*)	**25.** (*c*)	**26.** (*c*)	**27.** (*d*)	**28.** (*d*)	**29.** (*a*)	**30.** (*c*)
31. (*b*)	**32.** (*a*)	**33.** (*a*)	**34.** (*d*)	**35.** (*b*)	**36.** (*d*)	**37.** (*a*)	**38.** (*c*)	**39.** (*b*)	**40.** (*d*)
41. (*c*)	**42.** (*d*)	**43.** (*a*)	**44.** (*b*)	**45.** (*c*)	**46.** (*a*)	**47.** (*c*)	**48.** (*d*)	**49.** (*c*)	**50.** (*d*)
51. (*d*)	**52.** (*c*)	**53.** (*c*)	**54.** (*a*)	**55.** (*b*)	**56.** (*a*)	**57.** (*b*)	**58.** (*b*)	**59.** (*c*)	**60.** (*b*)
61. (*d*)	**62.** (*b*)	**63.** (*c*)	**64.** (*c*)	**65.** (*b*)	**66.** (*c*)	**67.** (*b*)	**68.** (*a*)	**69.** (*a*)	