MNGT5312
Financial Statement Analysis

Course Outline
Session 3, 2015

Part A: Course-Specific Information

Please consult Part B for key information on AGSM & Universities policies (including those on plagiarism and special consideration), student responsibilities and student support services.
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PART A: COURSE-SPECIFIC INFORMATION

1 STAFF CONTACT DETAILS

Lecturer-in-charge: Dr Jeff Coulton
Quadrangle Building Room 3061
Phone No: 9385 5811
Email: j.coulton@unsw.edu.au
Consultation Times – TBA in class and on Blackboard/Moodle (& also by appointment).

2 COURSE DETAILS

2.1 Teaching Times and Locations
Updated information about class times and locations can be found on the AGSM website and by logging in to the Google Calendar.

2.2 Units of Credit
The course is worth 6 units of credit

2.3 Summary of Course
Financial statement information is the basis for a wide range of business decisions. It is used by managers to monitor their firm's performance relative to competitors, to communicate with external investors, to help judge what financial policies they should pursue, and to evaluate potential new businesses to acquire. Securities analysts use it to rate and value companies they recommend to clients. Bankers use it in deciding whether to extend a loan to a client and to determine the loan's terms. Investment bankers use it to provide a basis for valuation and analysis of prospective buyouts, mergers and acquisitions, and consultants use it as a basis for competitive analysis for their clients. We will be covering the following topic areas:

Accounting Analysis
• Assessing quality of financial statements
• Potential accounting distortions
• Recasting financial statements

Financial Analysis
• Ratio analysis including the DuPont framework
• Cash flow analysis

Prospective Analysis
• Using accounting numbers in forecasting
• Forecasting for valuation / credit analysis

2.4 Course Aims and Relationship to Other Courses
The aim of this course is to present the tools necessary to undertake business analysis using financial statement information, and to show how these tools can be applied to a wide range of decision contexts.

The Core Finance and Core Accounting courses are prerequisites for this elective, and this course builds on and applies skills and knowledge from these courses, along with your prior analysis of business strategy.
2.5 Student Learning Outcomes

The Course Learning Outcomes are what you should be able to DO by the end of this course if you participate fully in learning activities and successfully complete the assessment items.

The Learning Outcomes in this course also help you to achieve some of the overall Program Learning Goals and Outcomes for all MBA students in the ASB. Program Learning Goals are what we want you to BE or HAVE by the time you successfully complete your degree (e.g. ‘be an effective team player’). You demonstrate this by achieving specific Program Learning Outcomes - what you are able to DO by the end of your degree (e.g. ‘participate collaboratively and responsibly in teams’).

### ASB Postgraduate Coursework Program Learning Goals and Outcomes

1. **Knowledge:** Our graduates will have current disciplinary or interdisciplinary knowledge applicable in local and global contexts.
   You should be able to identify and apply current knowledge of disciplinary or interdisciplinary theory and professional practice to business in local and global environments.

2. **Critical thinking and problem solving:** Our graduates will have critical thinking and problem solving skills applicable to business and management practice or issues.
   You should be able to identify, research and analyse complex issues and problems in business and/or management, and propose appropriate and well-justified solutions.

3. **Communication:** Our graduates will be effective communicators in professional contexts.
   You should be able to:
   a. Produce written documents that communicate complex disciplinary ideas and information effectively for the intended audience and purpose, and
   b. Produce oral presentations that communicate complex disciplinary ideas and information effectively for the intended audience and purpose.

4. **Teamwork:** Our graduates will be effective team participants.
   You should be able to participate collaboratively and responsibly in teams, and reflect on your own teamwork, and on the team’s processes and ability to achieve outcomes.

5. **Ethical, social and environmental responsibility:** Our graduates will have a sound awareness of ethical, social, cultural and environmental implications of business issues and practice.
   You should be able to:
   a. Identify and assess ethical, environmental and/or sustainability considerations in business decision-making and practice, and
   b. Consider social and cultural implications of business and/or management practice.

6. **Leadership:** Our graduates will have an understanding of effective leadership. (MBA and MBT programs only).
   You should be able to reflect on your personal leadership experience, and on the capabilities necessary for leadership.

For more information on the Postgraduate Coursework Program Learning Goals and Outcomes, see Part B of the Course Outline.

The following table shows how your Course Learning Outcomes relate to the overall Program Learning Goals and Outcomes, and indicates where these are assessed:
### Program Learning Goals and Outcomes

**This course helps you to achieve the following learning goals for all ASB postgraduate coursework students:**

<table>
<thead>
<tr>
<th>Course Learning Outcomes</th>
<th>Course Assessment Item</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>On successful completion of the course, you should be able to:</strong></td>
<td><strong>This learning outcome will be assessed in the following items:</strong></td>
</tr>
</tbody>
</table>
| 1 Knowledge Explain the role of financial statements in corporate performance analysis | • Class participation  
• Seminar Problems  
• Major Report  
• Exam |
| Use statistical skills to present data relevant to problems of financial statement analysis, and in particular in company valuation | |
| 2 Critical thinking and problem solving Explain factors leading to variation in ‘accounting quality’ and how this impacts on financial statement analysis | • Seminar problems  
• Major Report  
• Exam |
| 3a Written communication Construct written work which is logically and professionally presented. | • Case summaries  
• Major Report |
| 3b Oral communication Communicate ideas in a succinct and clear manner. | • Class participation  
• Major Report |
| 4 Teamwork Work collaboratively to complete a task. | • Case summaries  
• Major Report |
| 5a Ethical, environmental and sustainability responsibility Identify and assess environmental and sustainability considerations in problems in financial statement analysis | • Part of Seminar Problems and Major Report but not separately assessed |
| 5b Social and cultural awareness Not specifically addressed in this course. | |

### 3 LEARNING AND TEACHING ACTIVITIES

#### 3.1 Approach to Learning and Teaching in the Course

This course uses a combination of interactive classes based heavily on case analysis and reference to current business events to apply key concepts, theories and models, to practice.

This course will be conducted as a 2 x 1 hr 20 min class sessions run in intensive mode. The class sessions will also focus on a series of case studies and recommended readings which students are expected to complete prior to the commencement of the class. We will focus on Qantas as the ongoing ‘case study’ company. This will save you time in that your preparation for understanding Qantas’ business for the first week will be relevant for all remaining classes.

The course will develop four fundamental analysis skills - business strategy analysis, accounting analysis, financial ratio and cash flow analysis, and prospective analysis. We will practice using these tools in a variety of contexts e.g., security analysis, credit...
analysis and investor communications. In class, we will use cases as the primary vehicle for learning these skills. Cases have several advantages over lectures in this setting. They provide a “hands on” opportunity to apply and practise the concepts that we will discuss. This greatly enhances learning. They also present business analysis issues in a specific context, making learning more interesting. In order to derive maximum benefit from your classes, you will need to have read and tried your hand at working through the cases prior to the class.

4 ASSESSMENT

4.1 Formal Requirements

In order to pass this course, you must:
- achieve a composite mark of at least 50; and
- make a satisfactory attempt at all assessment tasks (see below).

4.2 Assessment Details

<table>
<thead>
<tr>
<th>Assessment Task</th>
<th>Weighting</th>
<th>Learning Outcomes assessed</th>
<th>Length</th>
<th>Due Date</th>
</tr>
</thead>
<tbody>
<tr>
<td>Class Participation</td>
<td>10%</td>
<td>1, 3b</td>
<td>N/A</td>
<td>Ongoing</td>
</tr>
<tr>
<td>Case summaries (x2)</td>
<td>20%</td>
<td>1, 2, 3a, 4</td>
<td>3 pages each</td>
<td>Wed 11 November, and Wed 18 Nov</td>
</tr>
<tr>
<td>Major project</td>
<td>30%</td>
<td>1, 2, 3a, 3b, 4</td>
<td>15 pages</td>
<td>End of class 5</td>
</tr>
<tr>
<td>Final Exam</td>
<td>40%</td>
<td>1, 2</td>
<td>TBA</td>
<td>Details announced in class 1</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>100%</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Class Participation

You need to prepare case summaries for each case used in the course – specific questions will be provided to assist and direct you in preparing these. Without adequate preparation you will find it difficult to contribute usefully in class and will risk a poor grade for class participation. I will also indicate opportunities for class participation through some minor research tasks to be discussed/presented in class.

The course will be taught in a discussion mode to facilitate thoughtful discussion of the cases. To get the most out of the course, you must be prepared for discussion every day. You should come to class with a list of questions on everything you do not understand, and you should be prepared to discuss your opinions on professional issues. In other words, you do not have to have a specific question in order to participate; I am very interested in your opinions.

You can participate in different ways. These include (but are not limited to):
- Identifying key issues in a case based on your reading of the materials provided
- Describing relevant personal experience
- Making comments linked to the comments of other students and to the basic topic of discussion
- Listening to the contributions of your classmates and engaging them in constructive dialogue
The quality of your contribution is far more important than the quantity. You should also use your name cards for the first six weeks of the course. You should be prepared for cold-calling in all class meetings, especially in class time devoted to discussion of the case studies and of the major project.

You will lose points for contribution if you use your phone in class, or use your computer other than for course-specific tasks.

**Case summaries**

Due date: Wed 11 November and Wed 18 November.

Please submit these to me at the start of the relevant class. No email or fax submissions will be accepted. The submitted case summaries must be 3 pages or less (including any supporting materials).

You need to prepare summaries on all cases to be covered in class. There will be specific questions provided for each case to guide you in your preparation. This will assist you in class participation and generating a lively discussion in class. Notice that there is a generous allocation of marks to class participation.

Please note that I will not be able to review or discuss any draft submissions. I will be able to answer questions that clarify what the case study requires. I will do this on Blackboard/Moodle so that all students have the same information to assist them in the preparation of their responses.

**Group Project**

The group project requires you to conduct a complete analysis and valuation of a publicly listed companies (from an industry sectors specified in class 2). Your company can be listed on an overseas exchange, or (preferably) on the Australian Securities Exchange. Meanwhile, you can find a list of all ASX sectors and constituent companies at the following website: http://www.asx.com.au/asx/research/companyInfo.do

The group project requires you to conduct a complete analysis and valuation of the businesses. A key feature of the project is that it requires you to identify and obtain the relevant, publicly available information. Thus, in addition to being evaluated on your ability to apply the tools of analysis described in the course, you will also be evaluated on your ability to identify and obtain the relevant information. Your analysis should provide solid support for the assumptions and forecasts that drive your valuation. (Your valuation should use only publicly available information. Do not use inside information obtained from personal company contacts etc.) Do not use brokerage house reports or other published sources that make investment recommendations.

**Choosing a Company:**

Selecting a company because you like its product or because you plan to work there is unlikely to identify a mis-valued stock. To increase the odds that your analysis will yield a viable investment opportunity, I will provide you with the output of some large-sample stock screens. Common indicators of mis-valued stocks are extreme fundamental-to-price ratios, a lack of consensus in analysts' forecasts, high stock price volatility, high trading volume, a large short position and other similar statistics. The stock screens search for companies that look promising on these dimensions. I will provide you with a list of companies based on these screens.
You need to clear your final selection with me before proceeding.

Your analysis should follow the steps described in the course.

1. Business Strategy: Briefly describe the industry and the company’s position within the industry and, most importantly, the sustainability of profits generated by the company’s strategy. Why do you think the firm’s return on equity will or will not revert to its cost of capital? Please do not simply repeat the company overview from the company’s website or Management Discussion and Analysis. (6 marks)

2. Accounting Analysis: Assess the degree to which the firm’s accounting reflects the underlying business reality. Identify accounting distortions and their impact on the sustainability of profits. For instance, R&D is sometimes expensed when incurred, but probably creates an economic asset. How will this affect your forecasts? You may also want to restate or rearrange the existing financial statements to make them easier to analyse and forecast. (6 marks)

3. Financial Analysis: Use ratio analysis and cash flow analysis to evaluate the current and past performance of the business and assess its sustainability. You should definitely compare your company to some peers in the same industry. (8 marks)

4. Forecasting: Forecast the firm’s future income statements and balance sheets. This is the heart of the project so provide specific justification for each major component of your forecasts. Is the forecast based on past trends, comparisons with other firms in the industry, an industry report, or your gut feel? How does your forecast for the next few years compare with analyst forecasts? Finding relevant data from outside the firm’s own financial statements to guide your forecasts is particularly valuable here, but please only access publicly-available data; do not use inside information that you may have gathered from personal contacts in the company. (12 marks)

5. Valuation: Use either the residual income (i.e. abnormal earnings) model or a discounted cash flow model to produce an estimate of firm value. Focus on the value per share of equity in the company and compare your valuation to the market valuation, providing possible explanations for any differences. You should also conduct a sensitivity analysis by varying your discount rate and other crucial assumptions. (8 marks)

Due date: TBA

Project Length:
Your report should be a readily comprehensible and condensed report of your work (i.e., not a detailed compilation of all the information you collected and all the various valuation scenarios you considered). Accordingly, your report is limited to 15 pages. Please site any sources for data used in your financial analysis or forecasts, such as industry reports. You are required to disclose all sources of information e.g., raw data, expert opinions, surveys, analyst reports etc.

Formation of Groups
You will form your own groups, or you can choose to do the assignment by yourself. You may change groups during the course.

Final exam:
The final exam will take place during the exam period. More details on the format of the exam will be provided in the first class.
4.3 Assessment Format

For guidelines on formatting and presenting your assignment, see http://www.asb.unsw.edu.au/currentstudents/agsmmba/academicinformation/assessmentsandexaminations/Pages/default.aspx

4.4 Assignment Submission Procedure

You should be reminded to keep a copy of all work submitted for assessment and to keep your returned marked assignments.

4.5 Late Submission

AGSM MBA Programs applies a daily penalty of 5% to late assignments. This policy was reviewed in October 2009 in light of the fact that certain schools within the Australian School of Business apply a 10% penalty. The decision of AGSM MBA Programs following this review was that current 5% penalty is appropriate to all of our programs and will remain unchanged.

Refer to policy at: http://www.asb.unsw.edu.au/currentstudents/agsmmba/academicinformation/assessmentsandexaminations/Pages/default.aspx

Quality Assurance

The ASB is actively monitoring student learning and quality of the student experience in all its programs. A random selection of completed assessment tasks may be used for quality assurance, such as to determine the extent to which program learning goals are being achieved. The information is required for accreditation purposes, and aggregated findings will be used to inform changes aimed at improving the quality of ASB programs. All material used for such processes will be treated as confidential.

5 COURSE RESOURCES

The website for this course is on UNSW Blackboard (or Moodle) at: http://lms-blackboard.telt.unsw.edu.au/webapps/portal/frameset.jsp

There is no prescribed textbook for this course. I will be putting (1) power point slides, (2) readings, and (3) problem sets on the course Moodle page.


If you wish to explore any topic in more detail, please let me know. I have a heap of material on each of the topics we cover.

6 COURSE EVALUATION AND DEVELOPMENT

Mid- and end-of-Semesr feedback is sought from students about the courses offered in the AGSM MBA Program, and continual improvements are made based on this feedback. The mid-Session feedback is collected in weeks 3 or 4, and communicated to students in the class following its collection. Significant changes to courses and programs within the Program based on end-of-Session feedback are communicated to subsequent cohorts of students.
### COURSE SCHEDULE

<table>
<thead>
<tr>
<th>Class</th>
<th>Date</th>
<th>Topic</th>
<th>Cases</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Wed 14 October (JBR)</td>
<td>Introduction to the Course&lt;br&gt;The role of earnings in the capital market&lt;br&gt;Strategy analysis and accounting</td>
<td>LinkedIn (Questions in coursepack)&lt;br&gt;Analysing Qantas (Questions in Coursepack)</td>
</tr>
<tr>
<td>2</td>
<td>Wed 21 October (HDR)</td>
<td>Accounting analysis:&lt;br&gt;i. Assessing earnings quality&lt;br&gt;ii. Disclosure vs recognition&lt;br&gt;iii. Capitalising vs expensing</td>
<td>Analysing Qantas (Questions in Coursepack)</td>
</tr>
<tr>
<td>3</td>
<td>Wed 11 Nov (JBR)</td>
<td>Using ratio analysis to understand the business</td>
<td>Qantas’ 2015 results*&lt;br&gt;&lt;em&gt;This is a hand-in case&lt;/em&gt;&lt;br&gt;Dupont analysis of Qantas versus Virgin Australia</td>
</tr>
<tr>
<td>4</td>
<td>Wed 18 Nov (JBR)</td>
<td>Forecasting techniques – developing expectations&lt;br&gt;Forecasting mechanics – estimating the impact of future business activities using pro forma financial statements</td>
<td>Forecasting for Qantas&lt;br&gt;&lt;em&gt;This is a hand-in case&lt;/em&gt;</td>
</tr>
<tr>
<td>5</td>
<td>Wed 25 Nov (JBR)</td>
<td>Accounting-based valuation&lt;br&gt;Valuation&lt;br&gt;i. Reverse engineering share price&lt;br&gt;ii. Market-based multiples&lt;br&gt;Equity analysis</td>
<td>Valuing Qantas</td>
</tr>
</tbody>
</table>

Course Review and wrap-up