FINANCIAL RATIO ANALYSIS:

ITS ROLE AND RELEVANCE TO THE

MANAGEMENT AND INVESTORS

BY

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A P P R O V A L S H E E T

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D E D I C A T I O N

To my beloved late Father Wayo,

My beloved Mother and my family

A C K N O W L E D G E M E N T

Thanks be to God for making it possible to contribute to the literary development of this country. I thank my supervisor, Mr. Silva, a senior lecturer in the Department of Accounting, for the necessary corrections and suggestions made in this project.

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Finally, the entire members of Kure's family need to be praised for their numerous contributions.

A-B 3 T R A C T

This project was written on the basis of the data gathered, interpreted and evaluated on four manufacturing companies in Nigeria such as Nigerian Breweries Limited (NBL) Guiness Nigeria Limited (GNL), United Nigerian Textiles Limited (UNTL) and Arewa Textiles Limited (ATL).

The uses of financial ratios be investors, management, workers and government were stressed. The ratio selection for thia analysis inoludes liquidity profitability, debt and activity ratios.

The literature review of financial ratios such as Predictive Ability of financial ratios. Rapid Growth Firms, Profitable firms and their relations to financial ratios, Bond rating and Default Detecting Ability of Financial Ration etc - has been carried out and incorporated in this project. Literature review provider, information as to how an attempt could be made to predict the success or failure of selected firms.

Analysis and comparison were made between Nigerian Breweries Limited (NBL) and Guinness Nigeria Limited (GNL) which produce similar products and a similar effort was made on United Nigerian Textiles Limited (UNTL) and Arewa Textiles Limited (ATL).

These companies had similar problems duo to **the** general recession in the economy during the period reviewed by the analyst.

It has been possible to conclude that efficient management is necessary in all business units to improve their performance and progress.

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CHAPTER ONE

INTRODUCTION

In every society, finance is very important for its daily transactions and business activities. In the very early period of man's existence on earth, transactions were carried out by what is commonly called 'trade by barter'. Trade by barter was, however found to be very crude and difficult. But later, man developed money to ease the problems of financial transactions and business activities.

The survival of a business organization depends on finance, which is its backbone. Before the word "finance" was brought into its logical use, it was mixed up with the words "accounting" and economics". Later on, it was separated and was developed as a special field of study. Therefore, 'finance' has changed from descriptive study of procuring funds, which lays emphasis on external analysis of firms, to a more rigorous and in-depth study. The changing role of finance has made the financial manager feel the necessity of using several tools successfully to manage a firm's finances.

This chapter discusses the purpose, scope, methodology and limitations of the study.

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1.1 Purpose of the Study.

The purpose of this study is to emphasize the importance of ratio analysis as one of the instruments for measuring the performance of Nigerian firms.

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Financial ratios can be used to evaluate, interpret and compare the performance of a particular company over many years, or those of one company with another, or the performance of a particular company over many years, or those of one company with another, or the performances of firms in the same industry or of firms in different industries. This is done to measure the changes that do occur from time to time in a business establishment. If the changes have a favourable impact, they will be noted as a positive sign. If the changes are unfavourable, prompt action should be taken to correct the situation.

1.2 Uses of Financial Ratios.

Analysed financial ratios give detailed information about a firm's financial position and performance. This is due to the fact that two or more items of a firm's financial data are compared in each financial ratio. "Ratio is the relationship, or proportion that one amount bears to another and is expressed as a percentage or a fraction". The analysis of ratios can disclose relationship as well as basis of comparison which reveal conditions and trends that cannot be detected by an inspection of the individual components of the ratio. Comparison of a firm's financial ratios over a period of time enables one to know the improvement, uniformity, or deterioration in its financial operations. It also helps in forecasting the future financial position of the firm.

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Financial ratios also measure the risks and returns on investments such as in common stocks, and pin-point firms that need quotation.

The above uses of financial ratios are meant for various parties both within and outside an organization as described below:-

1.2

(a) Financial Investors:

People invest their money so that they can get adequate return on their investments. Investment always involves the risk that the actual returns may not match the anticipated returns. Therefore, investors require accounting reports about the enterprises in which they have invested their money. They evaluate the risk and potential earnings, compare the investment alternatives and choose the best suitable alternative. Investors and or creditors use financial ratios to appraise the performance of management in a firm. Managers in business organizations are responsible to financial investors for efficient administration of the assets placed in their care - corporate management, in particular owe investors and society a report on how successfully they have discharged their responsibilities.

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(b) The Beneficial Relationship:

Groups such as trade creditors, employees, bondholders, analysts, governments, potential investors, shareholders

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and so on have different interests and, therefore, analyse financial ratios differently. Trade creditors, for instance, have a short-term claim and as such, are concerned with short-term liquidity of the firm. They use only those ratios that can provide them with such information. Long-term creditors are concerned with those ratios that measure the long-term capability of the firm to repay debts, as they fall due for payment. The governments are concerned with the imposition and collection of taxes from business organisations whenever profit is declared. The taxation issue is complicated because most business organizations are taxed by the Federal Government as well as respective state governments.

Any party aiming towards analysing the financial position of any firm has to make use of its financial statements which usually give the necessary financial information. Balance sheets, and profit and loss accounts (income statements) provide financial data for ratio analysis. "A balance sheet is a statement which purports to show the financial position of a business at a particular date". It shows the sources of finance obtained by the business and the uses to which these resources have been put". It is known as entity concept because it always balances.

"Profit and loss account (income statements) consists of the profit a company has made and retained which has not been transferred to reserves or capitalized. It is, therefore, a statement of a firm's operating performance that has taken place during a financial period.

In addition to a balance sheet and income statements,

a statement which assists financial analysis, is the Sources and Application of Funds Statement or fund statement. A fund statement shows the sources from which funds have flowed into a company during a defined period. It also shows the uses of these funds.

1.3 Nature of the Study.

The aim of this research is to analyse and interpret the performance of four sets of manufacturing companies in two industries. These are brewery and textile industries. Each company's performance over a period of five years is compared. The industry averages are also used to measure the performance of each company. Later on, two companies within an industry are compared.

1.4 Research Methodology.

For purposes of this study, data covering a period of five years (ie 1982 to 1986) have been obtained from the four manufacturing companies. The data obtained from each company would also be analysed. Where the data are not available, the period considered will, however, not be changed. All these companies are public limited companies and three of them are quoted in the Nigerian Stock Exchange. The four companies are drawn from two industries. The first two are from the textiles industry and the last two are from the brewery industry. For the purpose of comparison, the two companies from each industry will be analysed and compared.

A brief history of the four selected companies is given below.

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1.4.1 United Nigerian Textiles Limited (UNTL)

UNTL was incorporated on 7th May, 1964 and got listed on the Nigerian Stock Exchange in December, 1971. The company is a public limited liability company with its registered office in Kaduna. The company was one of the pioneer industrial establishments in the former Northern Region (now the eleven Northern States).

At the moment, the company has acquired interest in four other textile manufacturing companies which comprise the Zamfara textiles in Gusau Sokoto State; Funtua Textiles Limited in Katsina State and Unitex and Supertex Limited all located in Kaduna, Kaduna State. The acquisition was made as part of its expansion programme efforts in order to achieve the business objectives which included profit maximisation. The summary of its investment in subsidiary companies is as follows:

Company	No. of shares held	Percentage	Year
Zamtex Limited	1,670,500	50.35	1976
United Nigeria-Textile Limited	3,000,000	100	1981
Funtua Textile-Limited	4,335,000	51	1978
Supertex Limited	1,350,000	45	1983

The nature of financing the group of companies is through owners' equity and long-term and short-term secured loans. The number of shares of UNTL and its groups stood at 34 million ordinary shares at 50 Kobo each, capital reserves of ₦0.65 million and ₦182 million revenue reserve. The long-term financing is made up of various categories of debenture stocks and long-term loans as specified in Appendix "D".

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The short-term financing consists of secured bank overdraft and debenture payable within one year. Most of the loans obtained were used in financing acqusitions of subsidiaries and expansion programmes of the subsidiaries.

The company is the largest employer of labour in the textile manufacturing business in Nigeria. The company had up to 6,000 workers in its employment in 1976. This number rose to 8074 by 1979. The number later dropped to 6,562 at the end of 1981. The reduction was as a result of retrenchment carried out since 1980 in order to equate its staff strength to its production capacity. Retrenchment was necessitated by low production which arose from low demand for company's products, acute shortage of raw materials and implementation of ₦125.00 minimum wage introduced by the Shagari administration.

1.4.2 Arewa Textiles Limited (ATL).

This company was established in 1963 as a joint venture between International Finance Corporation, Barclays Overseas Development Corporation, Overseas Spinning Investment Company Limited (headed by nine leading Japanese Spinners) and the New Nigerian Development Company Limited (NNDC).

Production of finished textile goods started in April, 1965. The company obtains its funds through cash generated from operations and sale of fixed assets. The application of funds is mainly on the purchase of fixed assets, payments of dividends, payments of loans and company tax.

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The labour force of the company has increased tremendously over the years. As at November, 1986 the company had a total workforce of 2,800, permanent employees and 191 casual workers. The company, located at Kaduna is not quoted on the Nigerian Stock Exchange.

1.4.3 Nigerian Breweries Limited (NBL).

NBL, a public limited liability company, was registered on 16th November, 1946. It was registered with a capital of ₦8 million which was subject to increases in due course. The head office is located at Iganmu House, Lagos. There are other branches of the company at Apapa Lagos, Aba, Kaduna and Ibadan.

The company has 42,000 shareholders and had 4,000 employees in 1981. The number of employees went up to 4,400 in 1983 as a result of opening its branch in Ibadan.

NBL are brewers, bottlers and marketers of beer and allied products. It produces star, Gulder, Maltina and Green Sands Shandy. (Its stock exchange listings include food, beverages and tobacco.)

In a nut-shell, although the NBL was established in 1946, its operations started in 1949, when the nation's first brewery was commissioned in Lagos to produce Star lager beer. This was followed by the establishment of a brewery at Aba in the present Imo State in 1957 and the third Brewery was established in 1963 in Kaduna. The brewery, commissioned in Ibadan in 1983, is the fourth and biggest brewery which is even said to be the largest in West Africa.

1.4.4 Guinness Nigeria Limited (GNL).

Guinness Nigeria Limited was incorporated in Nigeria in 1950 and initially imported Dublin-brewed Guinness stout for distribution and sale in Nigerian markets. The company has its registered office at Oba Akran Avenue at Ikeja, Lagos.

The company is jointly owned by Nigerians and foreigners. The two foreign shareholders Guiness Overseas Limited and Atlanta Limited own 38,250,000 shares and 21,750,000 shares respectively, which represent ₦30 million or 40% of the company's authorized, issued and paid up capital. The Nigerian directors share among themselves 38,560,000 shares or 26% of the total shares and the Nigerian public hold the remaining 34%. The company's authorized share capital of ₦75 million is divided into shares of 50 Kobo each.

The first brewery was built at Ikeja and commissioned in 1962.. In 1974 and 1978 the second and third breweries to produce Harp Larger and Guinness Stout beer, respectively, were commissioned in Benin City. The fourth brewery was built at Ogba in Oyo state in 1983.

The company's employees were 4,000 in 1985, 311 of these were in the management cadre. The company is totally committed to the training and development of its staff as a means of increasing efficiency, productivity and continued mutual trust and cooperation. It has a training school in Benin City for the training of the staff locally.

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The company has intensified efforts to develop local alternative sources of raw materials and reduce its reliance on imported raw materials. It is now developing a farm at Kudu in Niger State, to obtain raw materials for its use.

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1.5 RATIO SELECTION

For the purpose of financial analysis many ratios are made use of. But, for the purpose of this study, four main ratios are selected:

(a) Liquidity ratio,
(b) Profitability ratio,
(c) Debt ratio and
(d) Activity ratio.

Under each of the four slected major ratios, three to five sub-ratios are discussed. Only a few ratios were selected from each category because the more the ratios selected, the more difficult the analysis becomes. Apart from this, some ratios provide the same information as others and no analyst can claim that he knows all the financial ratios.

The explanation of the ratios selected from the four groups are given in section I of chapter II.

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1.6 LIMITATIONS OF THE STUDY

The limitations of financial ratios generally apply to this study too. The limitations found in financial ratios are numerous.

One of the limitations is that there is no acceptable standard on ratios to be used by all firms. Each firm can decide on the ratios it deems fit to use. The analysts can decide on what ratios to be used.

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Another limitation of ratio is that it cannot be used in assessing any organization's financial position and when too many ratios are used, they lead to confusion and waste of time. A good analysis of financial position must include balance sheets, profit and loss accounts as well as the sources and applications of funds.

In financial analysis, conditions of economy, competitors' activities, state of industrial relations and the quality of potential workforce have to be considered because they are usually neglected in financial statement preparation. Some facts which are important for the organization and which are material in value are usually not available for the analyst.

Many large firms actually operate a number of different divisions in quite different industries, making it difficult to develop a meaningful set of industry averages for comparison purposes. This tends to make ratio analysis more useful for small firms than for large firms.

Some financial statements do not contain enough information for computing certain ratios. In this research, some ratios were left out because certain information relevant for the purpose was not available.

A few financial data are grouped together in financial statements and this makes it difficult to get the actual figure for some items.

Other limitations of this research are:

Firms are compared mainly on what they manufacture.

Some essential factors like the age of the asset, size of assets etc are not used in the analysis of these four companies due to non-availability of adequate data.

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The financial data of these four companies are analysed on group basis and they include the subsidiaries. Industry averages which are used by the analysts as basis for favourable or unfavourable performance of firms are used only when available.

1.7 METHOD OF PRESENTATION.

This study is divided into five chapters. Chapter one deals with the introduction of the subject matter. Chapter two gives a conceptual frame work of the selected four companies, while chapter three deals with the financial analysis and comparison of Nigerian Breweries Limited (NBL) and Guinness Nigeria Limited (GNL).
Chapter four deals with the financial analysis and comparison of United Nigerian Textiles Limited (UNTL) and Arewa Textiles Limited (ATL).
Chapter five deals with conclusions and recommendations.

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CHAPTER TWO

A CONCEPTUAL FRAMEWORK OF FINANCIAL RATIOS

SECTION I

2.0 TYPES OF RATIOS.

Ratios may be categorised into four groups.

(1) Liquidity

(2) Profitability

(3) Debt Management

(4) Activity

These ratios are useful and each of these major groups of ratios has many sub-divisions under each. They are discussed below:

2.1 LIQUIDITY RATIOS.

Liquidity ratios are divided into two parts, namely

(1) Short-term and

(2) Long-term liquidity ratios.

Short-term liquidity ratio determines a firm's ability to meet its short-term obligations. It measures and sees if the firm has enough cash at its disposal for its day-to-day requirements. These ratios are as follows:

(a) Current ratio

(b) Acid test ratio

(c) Liquidity of inventories

(d) Average collection period and so on.

They are discussed in detail below.

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2.1(i) CURRENT RATIO.

The current ratio is computed by dividing current assets by current liabilities. Current assets normally include cash, marketable securities, accounts receivable, and inventories. Current liabilities, on the other hand, consists of accounts payable, short-term note payable, current maturities of long-term debt, accrued income taxes and other accrued expenses (principally wages). The current ratio is the most commonly used measure of short-term solvency, since it provides the best single indicator of the extent to which the claims of short-term creditors are covered by the assets that are expected to be converted to cash in a period roughly corresponding to the maturity of the claims. The formula is:

$$\text{Current Ratio} = \frac{\text{current assets}}{\text{current liabilities}}$$

The industry average for current ratio is 2:1 and it is expressed in "times" rather than in "percentage".

2.1(ii) QUICK RATIO OR ACID TEST

Quick ratio is commonly used in manufacturing companies where inventories are found in large quantities. This ratio is considered a better measure than the current ratio. It measures the firm's ability to pay off short-term obligations without relying on the sale of inventories. Inventories or stocks are not easy to convert to cash and are excluded in Acid Test. It is computed as follows:

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$$\text{Acid Test} = \frac{\text{Current Assets - Inventory}}{\text{Current Liabilities}}$$

An Acid Test ratio of 1:1 is considered appropriate for an industry.

2.1(iii) Liquidity of Inventories .

This ratio shows the cost of goods sold to average inventory. The average inventory is the opening inventory plus closing inventory divided by two. The figures for cost of goods sold is not usually made available in financial statements; and as such, analysts divide sales by stocks to get the liquidity of inventories which is also called stock turn-over ratio or stock turnover rate. This gives a rough idea of the number of times a firm sells its stocks in a financial year. This ratio also shows the cause of a firm's financial imbalance that is whether the problem is slow or questionable inventory. This is also known as 'activity ratio'. The formula is

$$\text{Inventory utilization (or turnover)} = \frac{\text{Sales}}{\text{Inventory}}$$

2.1 (iv) Average Collection Period.

The average collection period is used to appraise the accounts receivable. It is computed by dividing debtors or accounts receivable by credit sales per day. It is expressed in "days" in most cases. The average collection period represents the average waiting time for a firm to collect its receivables after it has made credit sales.
The formula is as follows:

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$$\text{Sales per day} = \frac{\text{Annual Credit Sales}}{360 \text{ days}}$$

$$\text{Average Collection Period} = \frac{\text{receivables}}{\text{Sales per day.}}$$

This ratio also indicates a probable cause for a company's financial problem, for instance, slow or uncollectable receivables. It is also a measure of performance. This ratio is not computed by the analyst as the credit sales figures are not available in financial statements. Usually, some analysts divide debtors by total sales per day to get an idea of the collection period.

2.2 PROFITABILITY RATIOS.

Profitability ratios are divided into two different types. The first measures the effectiveness of the firm at utilizing its assets (activity ratios) and the second one measures the firm's effectiveness with respect to returns generated on sales and capital invested. Profitability ratios considered here include:

(i) dividend yield on Book value,

(ii) earnings per share,

(iii) earning power,

(iv) net profit margin and

(v) capital employed.

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2.2(i) DIVIDEND YIELD ON BOOK VALUE.

The profit distributed to shareholders is known as dividend.. The dividend shared is based on the Book Value of the shareholders' investment and it is expressed in percentage.

2.2(ii) EARNINGS PER SHARE.

This is calculated by dividing net profit after taxes by the total number of shares outstanding.

$$\text{Earnings per share} = \frac{\text{Net profit after taxes}}{\text{Shares outstanding.}}$$

2.2(iii) NET PROFIT MARGIN.

This ratio is also called operating profit margin or profit margin on sales. This ratio shows whether or not the cause of financial problem of a firm is operating loss.

$$\frac{\text{Net Profit}}{\text{Sales}}$$

2.2(iv) RETURN ON CAPITAL EMPLOYED.

There are three definitions here:-

2.2(iv) (a) The capital invested by shareholders or net worth is considered to be the capital employed by some people. It is called the shareholder's capital. This ratio is calculated as:

$$\frac{\text{Net profit after taxes} \times 100}{\text{Net worth.}}$$

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2.2(iv) (b) Return on Gross Capital Employed.

This is the ratio of net profit before interests and taxes to total assets (networth plus all liabilities). Some analysts use average total assets minus intangible assets instead of total assets as the denominator. The return on gross capital employed is expressed in percentage and it is called return on investment (ROI) or net operating profit rate of return. It is calculated as:

$$\frac{\text{Net profit before interests and taxes}}{\text{Total Assets.}}$$

2.2(v) (c) Return on net capital employed.

The return on net capital employed is defined as net profit before interests and taxes divided by networth plus long-term debt, (total assets less current liabilities). It is also expressed in percentage. It is calculated as:

$$\frac{\text{Net profit before interests and taxes}}{\text{Networth + long-term debt.}}$$

2.2(v) Earning Power.

The 'earning power' or return on total assets is the product of net profit margin and the turnover ratio which ignore the way assets are utilized and the profitability on sales, respectively. The earning power takes care of the deficiencies of these two ratios. It is calculated as:

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$$\text{Return on total assets} = \frac{\text{Sales}}{\text{Total assets}} \times \frac{\text{Net profit after taxes}}{\text{Sales}}$$

$$= \frac{\text{Net profit after taxes} \times 100}{\text{Total assets}}$$

The problem with this ratio is that it does not take interest charges into consideration. However, net operating profit rate of return is used when financial charges like interests, and dividends on preference shares are of substantial amount. The formula used by some analysts when financial charges are significant is the same as the formula for gross capital employed or return on investment (ROI).

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2.3 ACTIVITY RATIOS

Activity ratios measure the firm's performance by indicating how effectively it utilizes its resources. Assets are resources of a firm and are compared with sales to evaluate the rate at which they are turned over or number of times they are sold in a year. The activity ratios are as follows:

(a) average collection period,
(b) stock turnover ratio,
(c) current assets turnover ratio,
(d) Fixed assets turnover ratio,
(e) Total assets turnover ratio,
(f) sales to networth,
(g) miscellaneous assets to networth.

The average collection period and stock turnover ratio have already been discussed under liquidity ratios. The remaining ratios in the above list are discussed below:

2.3(i) Current Assets Turnover Ratio.

This is the ratio that describes the relation of sales to current assets and is usually expressed in "times". This tells the number of times current assets are turned over. It is calculated as:

$$\text{Current Assets Turnover Ratio} = \frac{\text{Sales}}{\text{Current Assets}}$$

2.3(ii) Fixed Assets Turnover Ratio.

It It is calculated using the following formula:

$$\text{Fixed Assets turnover ratio} = \frac{\text{Sales}}{\text{Net fixed assets.}}$$

Net fixed assets indicate that depreciation has been charged on fixed assets.

2.3(iii) Total assets Turnover Ratio.

This ratio is calculated by dividing sales by total assets (fixed and current assets).

$$\frac{\text{Sales}}{\text{Average total assets-intangible fixed assets}}$$

The higher the current, fixed and total assets turnover ratios the more efficient the firm is at utilizing them.

2.3(iv) Sales to Networth Ratio.

Here the ratio is calculated by dividing sales by equity capital. $\frac{\text{Sales}}{\text{Networth}}$

Equity capital is also called networth or shareholders' funds. It includes the capital invested and all reserves (revenue reserve or retained earnings, and capital reserves). A higher the ratio shows over-trading and a lower one shows under-trading.

Over-trading is the situation where excessive sales are made on limited networth. It is caused by inflation, taxation (on which no adjustment for inflation is made by government), depletion of working capital or or over-expansion.

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Its effects include:-

(1) difficulty in finding liquid cash for payment of wages and salaries,

(2) difficulty in paying taxes,

(3) increased cost of purchases and

(4) reduction in effective sales figure caused by accumulated stock of unsold goods.

Under-trading is the situation where a company does not make enough sales to cover its equity capital. In other words, it is an over capitalized business or business that fails to utilize its invested capital (networth) to the fullest extent. An under-trading company has the following characteristics.

(1) slow paying records,

(2) inadequate working capital,

(3) high debt,

(4) declining bank balances.

2.3(v) Fixed Assets to Networth.

This ratio gives the percentage of owners' capital invested in fixed assets. It is calculated as follows:

$$\frac{\text{Fixed Assets}}{\text{Networth}} \times 100$$

When a high percentage is recorded as owner investment capital in fixed assets, the investment is said to be excessive.

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It is an indication that fixed assets have a large share of owners' invested capital. The current and miscellaneous assets share only the remaining portion of the capital.

However, this does not mean that networth is the only capital invested because borrowed funds are also invested in business.

2.3(vi) Miscellaneous Assets to Networth.

Miscellaneous assets are divided by networth to get this ratio.

It is calculated as follows:

$$\frac{\text{Miscellaneous Assets}}{\text{Networth}}$$

It measures the extent to which networth is invested in miscellaneous assets. These assets are not fixed, nor current, and nor intangible ones. Such assets include loans given to officers and directors, prepayments, value of life insurance and so on. This ratio explains one of the causes of a company's financial problem. Here funds are diverted into miscellaneous uses instead of investing them profitably in the business.

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2.4 Debt Ratios.

Debt ratios deal with solvency. They indicate the long-term liquidity of the firm, that is, its ability to meet long-term obligations. Debt ratios are called gearing ratios and give information on the amount provided by shareholders and creditors in financing the firm. If creditors provide a larger portion of the amount invested, they bear the risks of the organization and the owners in such a case lose control partly to the creditors. Raising funds through 'debt' may mean an opportunity for magnifying shareholders earnings if returns on borrowed funds are greater than interest paid on them.

The management of companies that have large portions of total invested capital provided by creditors are not free to take decisions without being bothered about creditors' bill. When shareholders' provide higher per centage of the invested capital, it denotes strong ownership position and freedom of operation by management. Debt or risk ratios included here are:-

(a) Debt to networth,

(b) Long-term capitalization,

(c) Debt ratio,

(d) Times interest earned,

(e) Fixed charge coverage.

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2.4(i) Debt to Networth Ratio.

The debt to networth ratio gives the relative proportion of capital contributed by the creditors and by the owners. It shows the balance that the management of a company has struck between total debts and shareholders' equity. It measures the relative claims on the company's assets. A firm with a higher percentage of debt has more financial problems than the one that has a lower percentage.

Debt to networth is calculated using the following formula:

$$\text{Debt to networth ratio} = \frac{\text{Total Debt x 100}}{\text{Networth.}}$$

2.4(ii) Long-term Capitalization.

Long-term capitalization indicates the relative importance of long-term debts in the capital structure of the portion of the firm's assets financed by creditors. This ratio is calculated by dividing long-term debt by total capitalization. Long-term debt includes debentures and mortgaged loans while total capitalization or capital structure consists of long-term debt plus shareholders' funds. It is expressed in "percentage" and calculated as follows:

$$\frac{\text{Long-term Debt x 100}}{\text{Total Capitalization}}$$

2.4(iii) Debt Ratio.

This ratio shows the financial structure of the firm and the way the firm is financed. The ratio is obtained by dividing total debt by total assets.

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The total assets constitute the financial structure of a firm. The ratio is expressed in "percentage" and shows the percentage of the total financing provided by all creditors (long-term and short-term creditors).
It is calculated as follows:

$$\frac{\text{Total Debt} \times 100}{\text{Total Assets.}}$$

2.4(iv) Times Interest Earned.

This ratio measure the extent to which a firm's earnings can decline without the firm being able to pay interest on creditors' bills. It is calculated as:

$$\text{Times Interest Earned} = \frac{\text{Gross Income}}{\text{Interest charges}}$$

The gross income is the profit before taxes and interest charges of the organization. This ratio is usually expressed in "times". Profit before tax is used in this formula because tax is charged after interest on long-term debt is deducted.

2.4(v) Fixed Charge Coverage.

This ratio recognises that firms lease assets and incur long-term obligations under contract lease. The ratio is preferred to the times interest earned for this reason and it is computed as follows:

$$\text{Fixed charge coverage} = \frac{\text{Gross income}}{\text{Interest charges + lease obligation}}$$

This ratio is expressed in "times". Fixed charges have as their components interest plus long-term lease obligations.

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SECTION II

2.5 LITERATURE REVIEW.

The study of financial ratios did not originate in Nigeria. It was introduced into Nigeria by foreigners who operated business enterprises. It has become widespread in the country. Accounting, finance and business students started using financial ratios to determine the performance of certain companies in Nigeria for academic purposes. Financial ratio is just one of the tools used by students in their analyses. Many researches have been done on the topic, but most of the publications in this field were made mainly in advanced countries like America, United Kingdom and Australia as far back as the 1930's. Researches on financial ratios also include bond rating, corporate risk determination, rapid growth firms, firm failure, and so on.

2.5.1 Researches on the Predictive Ability of Financial Ratios.

In a sample study carried out by one hundred and eighty-three firms which had difficulties between 1923 and 1931 and failed, Smith and Winakor (1935), analysed a trend of twenty-one ratios for ten years prior to failure. They observed deterioration in the average value of those firms that failed and concluded that good indicators of approaching distress were long-term solvency. Also, working capital to total assets ratio, which declined from the beginning to the end of the period studied, was considered as the best indicator of approaching failure.

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Fitz Patrick (1931) studied three to five year conditions of twenty firms that failed between 1920 and 1929. The condition prior to their failure were analysed using thirteen ratios for each of them separately. He compared each of the firms with 19 other firms which did not fail and concluded that all ratios were capable of predicting failure to a certain extent. According to the researcher, the best failure predictors among them were net profit to networth, and networth to total assets ratio.

Merwin (1942) examined 939 small firms in the period 1926 to 1936. He analysed the data for those firms for six years prior to failure after dividing his sample into "continuing" (successful) and "discontinuing" (unsuccessful) firms. He compared the industry average ratios of unsuccessful firm with their estimated "normal" ratios. He observed that the current ratios, networking capital to total assets and networth to total debts were the best indicators of discontinuity as early as five years prior to failure. Merwin believed that these three ratios were always below the estimated normal ratios and they showed declining trends before discontinuity in all cases.

Altman (1968) tested a sample of 33 United States Corporations that failed and 33 firms that were successful. The firms also had assets of similar size and belonged to the same industry.

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He developed a discriminant model formula (Z) which consisted of five ratios of different weights drawn from twenty-two variables he originally selected. The discriminant model tested whether a firm could go bankrupt or not, or whether it was possible to state from the results obtained that it would or would not become bankrupt. He predicted bankruptcy in the 3rd, 2nd, and final years prior to failure with 50, 72, and 95 percent accuracy, respectively.

The Z is calculated as follows:

$$Z = .012x_1 + .014x_2 + .033x_3 + .006x_4 + .099x_5$$

Where:

X_1 = Working capital to total assets.

X_2 = Retained earnings to total assets.

X_3 = Earnings before interest and taxes to total assets.

X_4 = Market value of equity to book value of total debt.

X_5 = Sales to total assets.

(1) Daniel (1968) also found discriminant function capable of predicting failure.

(2) Beaver (1967) who researched on univariate analysis predicted bankruptcy.

(3) Lev (1971), selected a sample of thirty-seven failing firms and selected non-failing firms of similar asset size and in the same industry. He measured the information decomposition measure of balance sheets of

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his sample companies and found that the balance sheet decomposition measure (BSDM) was not consistently different between failed and non-failed firms.

(4) Like Altman(1968), Deakin (1972), used multivariate analysis to predict failure. He measured the significance of each of the fourteen variables used by Beaver using Wilks' Lambda and also used discriminant analysis in conjunction with these ratios on each of his thirty-two failed and thirty non-failed firms. Unlike Beaver, Deakin excluded firms that defaulted in loan obligation and those that had preferred stock arrear ages in his definition of failure. As a result of such exclusion, he had less data available on failed firms than Beaver.

The 32 failed firms examined by Deakin were selected from a population that experienced failure between 1964 and 1970. The validating sample was selected at random from Moody's Industrial (Manual of 1962 - 1966). However, the data collected by Deakin on the non-failed firms were from 1964 to 1970. He concluded that statistical techniques, particularly from the discriminant analysis could be used to predict financial distress with a high degree of accuracy three years prior to failure.

(1) Wilcox (1973) tested a paired sample of fifty non-failed and failed firms for the period 1949 to 1971 after adjusting the cash position and cash flow of each of the firms. He was able to rank the bankruptcy risk of each firm. He ranked the bankruptcy risk of each of the firms for five years prior to their failure using gambler's run model.

(2) Another research by Edminster(1972) was on predictive ability of financial ratios. He concentrated on small business. He analysed fifteen ratios and found that the following ratios, incorporated in a discriminant function, predicted failure for up to three years on cumulative data analysis, quick assets to current liabilities, working capital to sales, net income plus depreciation -depletion, armortization to current liabilities, networth to current liabilities to networth and inventory of sales.

(3) Altman, et al (1977) reviewed Altman's model and updated its application from 1969 to 1975. In doing this, 53 failed and 53 non-failed firms including retailing firms were studied. Of the twenty-seven ratios they started with, they ended with seven, which were incorporated in a discriminant function which was found to predict correctly 96% and 70% respectively of the failure in the first and fifth years before bankruptcy.

2.5.2 Studies on Corporate Risk Determination of Financial Ratios.

Studies were conducted in this area in the 1970's Orgler (1970) developed a credit scoring model for commercial bank

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loans using twenty-one ratios selected from all but valuation ratio category. He discovered that he could predict good loans with some degree of success using a six variable model which contained working capital to current assets in addition to others. This model was developed to distinguish between good and bad loans. This could be considered a risk measure for investors using financial ratios.

Similarly, Altman, et al (1974) developed a model using data on one hundred and thirty firms, and a discriminant analysis on forty-one financial ratios. They found the model to be a useful predictor of risky loans ie those loans with repayment problems. The research was on French commercial bank loans.

Martin (1971);
Deakin (1972) and
Breen and Lerner (1973)

agreed that financial ratios could be used to determine how risky a company was.

Falk and Heintz (1975) employed average total assets to sales; total assets to working capital; and average accounts receivable to sales as a composite risk index for each of the forty-one industries they analysed for two years (1971-1972). They were aimed at analysing characteristics of each industry as reflected in its financial ratios so as to be able to rank them according to this risk. They succeeded in grouping a significant number of industries based on the above-mentioned facts.

2.5.3 Works on Rapid Growth Firms, Profitable Firms, and their Relations to Financial Ratios.

A research was done on related area to rapid growth firms, where profit and non-profit firms were distinguished by Chudson (1945). He discovered that short-term liquidity and long-term solvency were the two factors that could be used to differentiate profitable from non-profitable firms. According to him, firms had all ratios (he studied) but capital turnover ratios are high.

2.5.4 Researches on Bond Rating and Default Detecting Ability of Financial Ratios

(1) Hickman, in 1958, studied the result, of bonds issued from 1900 to 1943 and found that firms with high ratios (times interest earned and / or net profit to sales ratios) went into default less frequently than those with low ones. Based on this, the two ratios were paired to be good default predictors whether they were studied jointly or individually.

(2) Wojinlower (1962) examined the quality of bank loans and analysed such loans critiz by banks in 1957 for three federal districts in United States. His findings indicated that two-thirds of the firms whose loan schemes were critized had networth to total debt ratio below industry average (each firm's performance was compared with general performance of the industry to which it belonged). He further found that critized firms in every industry had current ratio below the industry average.

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Jen (1964) found out that the 'total debt to total asset ratios' as well as 'net profit to total assets' were the principal determinants of credit availability after he had analysed the availability of bank credit to a sample of small firms.

(3) Pogue and Soldosky (1969) developed a regression model with dichotomous (0-1) dependent variables so as to predict whether a bond should be classified as having Aaa or Baa rating. The model, which succeeded in classifying a number of bonds, had five variables:

Net income to total assets, debt to total capital,

Co-efficient of variation to total assets,

Net income plus interest to interest, and net profit to assets.

Pogue and Soldosky's analysis was limited to investment bonds as in Moody's rating.

(4) Pinches and Mingo (1973) analysed 180 bonds for the whole of 1967, collected financial data on thirty-five variables, and developed a model that employed six variables using M-group Multiple Discriminant Analysis, and factors analysis. The six variables contained in the model were:

(1) Subordination (legal status of the bond);
(2) Issue size (that is, bond ratings and the size of bond issue were related);
(3) Years of consecutive dividends (indicating ability to pay cash dividends);
(4) Five - years long-term debt to total assets - (measure of capital structure);
(5) Net income plus interest to interest(coverage ratio);
(6) And net income to total assets.

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Pinches and Mingo's model obtained 69.7% success of Moody's actual bond rating when they grouped one hundred and thirty-two bonds.

2.5.5 Financial Ratios and Other Studies.

There are certain categories of studies that cannot fit into any of the above classification.

(1) Lev (1966) analysed the following ratios for 245 United States firms from 1947-1966: acid test, sales to inventory, sales to total assets, equity to total debt, current ratio, and net income to total assets. He concluded that the analysed ratios were periodically adjusted with industry average of each firm by each of them.

(2) O'connor (1973) studied five ratios: total liabilities to networth; working capital to sales; cash flow to number of common stocks; current liabilities to inventory; and earnings per share to price per share and found them to be poor predictors of rates of return on common stock. He concluded that ratio analysis is of low value to investors in common stock. Abdel-Khalik (1974) noted that the regression equation and the parameters estimated were not valid for predictive purposes for three primary reasons.

(i) the issue of ratios multi-collinearity;
(ii) the choice of the explanatory ratio was peculiar;
(iii) the use of unadjusted R2 as a measure of explanatory "power" and objected the conclusions of O'connor.

O'connor (1974) agreed and said his findings were tentative.

(3) Pinches, et al (1973) and Pinches, et al (1975) classified 48 ratios into seven factors using R.factor analysis and showed the ratios that correlated with the factors as well as their loading the factors. The seven factors the authors used were: inventory intensiveness, space-return on investment, capital intensiveness, receivable intensiveness, financial coverage, cash position and short-term liquidity.

Deakin (1975) examined 1,114 companies for nineteen fiscal years (1955-1973) and attempted to determine the statistical distributions of financial ratios. He believed that "if emperical distributions of financial ratios were known, then a distribution function could be found for the Linear combinations of ratios that would be used in a classification model". He examined the emperical distribution of various financial ratios like current ratios; current assets to sales; quick assets to sales; working capital to sales; cash flow to debt net income to total assets; and total debt to total assets. He found that assumptions of normality may hold for only total debt to total assets. He assigned Chi-square values for seven of the ratios, except for current assets to total assets; working capital to total assets; total debt to total assets. He suggested distribution free probability statements for financial ratios.

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In a study on the effect of capitalised leased data on the predictive ability of financial ratios; Elam (1975) concluded that the "exclusion or addition of capitalized leased data from a firm's financial statements, does not significantly increase the predictive power of affected financial ratios to predictive failure.

(1) Chudson (1937) classified firms into profitable and non-profitable ones and he found two factors:

short-term liquidity and long-term solvency significantly differentiating between profitable and non-profitable firms with the profitable ones showing higher ratios, except for capital turnover ratio.

(2) Jackendoff (1962) also found financial ratios clearly and consistently distinguished between profitable and non-profitable firms. The ratios such as current ratio, working capital to total asset and networth to total debt were consistently higher for profitable firms.

CONCLUSION: In this chapter, section I considered financial ratios generally. In section II, a review was made of various researches done on financial ratios by different experts in the field.

A review was also made of financial ratios as important tools in determining firms' bankruptcy and firms' growth and non-growth. Chapter three discusses, interpretes and compares the performance of each firm over the five-year period from the selected sample companies.

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CHAPTER THREE

FINANCIAL ANALYSIS OF NIGERIAN BREWERIES LIMITED (NBL) AND GUINNESS NIGERIA LIMITED (GNL).

3.0 INTRODUCTION

The analysis of the financial ratios for NBL and GNL is for the five-year period ie 1982-1986. On account of non-availability of data, analysis of debt ratios has not been made for the two companies ie NBL and GNL.

3.1 Liquidity Ratios

Liquidity is defined as "the ability to realise value in money in the shortest time and with certainty of the price realised". The liquidity ratios relate to the ability to meet a firm's immediate obligations and avoid the possibility insolvency. In other words, they provide a quick and easy-to-use measure of a firm's ability to meet its current liabilities as they become due for payment. Liquidity ratios contain many ratios that inform the users of the competitive position and financial structure of a company. The examples of liquidity ratios are current ratio, acid test, liquidity of inventories and the average collection period.

3.1.1 Current Ratio.

This is also called the working capital ratio and is computed by dividing current assets by current liabilities. The ratio tests the short-term solvency of a company and it is the most commonly used measure of short-term solvency.

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It provides a general picture of adequacy of working capital and the ability to meet daily cash obligations of a company. The ratio indicates the strength of the working capital. In other words, it shows the extent to which the claims of short-term creditors are covered by assets that are converted to cash in a period roughly corresponding to the maturity of the claims.

Current assets normally include cash, marketable securities, accounts receivables and inventories, while current liabilities consist of accounts payable, short-term notes payable, current maturity of long-term debt, accrued income taxes, and other accrued expenses principally wages.

The traditionally accepted standard for current ratio measurement is 2:1. However, this ratio is not to be strictly relied upon because it is often found to be conservative under modern conditions.

But, whenever this ratio is much higher than 2:1, it could indicate unused cash (large holding of cash not put into profitable and productive use), slow paying debtors, or excessive stocks. However, when there is decline in this ratio, it shows an over-trading (excessive sales not accompanied by adequate working capital), fixed assets purchasedat the expense of working capital (excessive fixed assets), diversion of funds into miscellaneous assets (assets that are not fixed, not intangible, and not current,

e.g., officers' loans, prepayments), and so on. However, when there is a depression in current ratio, it indicates a sign of existence of financial problem.

3.1.2 Acid Test Ratio or Guide Ratio.

This measures the instant debt paying ability of a company and reveals the extent to which liquid resources are readily available to meet current obligations. Quick ratio is calculated by deducting inventories from current assets and dividing the remainder by current liabilities. Inventories have to be deducted because they are typically the least liquid of a firm's current assets and the assets on which losses are most likely to occur in the event of liquidation. Therefore, this measures the firm's ability to pay off short-term obligations without relying on the sale of inventories.

The acid test ratio of 1:1 or above is generally believed to be favourable. When the ratio is 1:1 or above, it could consist of large number of debtors who may be slow in paying their debts or who may not pay at all. For this reason, the fatio is also criticised because a firm with 1:1 or above acid test-ratio may turn out illiquid because of such a problem. However, when there is a decline on this ratio, it could be viewed as a likelihood of the company facing liquidity problems in future. A low acid test ratio does not mean the company will definitely liquidate because a lot depnds on the state of the economy and the buying and selling terms of the company.

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A high acid test ratio, whether it allows for liquidity or not (depending on the percentage of debtors) indicates financial stability both at present and in the near future. Acid test ratio can also be called liquid asset ratio.

3.1.3 Inventory Turnover Ratio.

This is the ratio of cost of goods sold to average inventory. It is also known as stock turnover ratio. This ratio serves as a useful technique for ascertaining slow- moving and fast-moving items, for the purpose of comparing the present performance with that of the past. Inventory turnover ratio measures the velocity with which merchandise moves through a business within a given period. It indicates efficiency in the control of stocks of materials, finished goods and work-in-progress. It is also an effective tool for analysing price changes.

However, most financial statements do not usually contain data on the cost of goods sold. Analysts use the relation of sales to stocks as a substitute for liquidity of inventories formula. The ratio of sales to stocks thus gives only a rough idea to analysts because the actual physical measure is difficult to compute. The higher this ratio, the more efficient the management because there are risks and costs involved with piling stocks. These costs include insurance costs, interests on amount borrowed to finance stock,

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interests on loss incurred on resources that are tied to stocks, costs of store-keeping and so on. There are also risks involved which include obsolence, pilferage, deterioration, change in customer preferences, seasonal influence, purchase or retention of unusable materials, overvaluation, and so on. Low turnover ratio could indicate the possibility of including unsaleable materials in the inventory figure and the possibility of writing them off in future. A decline in the 'stock turnover rate' could be due to overstocking which adversely affects cash flow because of slowing down rate of converting stocks to cash either directly or first through debtors.

Table 3.1 contains the liquidity ratios of the sample companies analysed below:

3.2 NIGERIAN BREWERIES LIMITED (NBL): LIQUIDITY RATIOS.

An attempt is made in this section to make an analysis of the financial data applicable to NBL for the period 1982to 1986. The analysis is made first with the use of liquidity ratios based on data as shown on table 3:1.

3.2(a) Current Ratio.

This is also called the working capital ratio. The current ratio for NBL from 1982 to 1986 is considered in this discussion. Traditionally, current ratio is recognized as standard when it is 2:1. This means that the assets must exceed liabilities two times.

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The current ratio for the past five years, as indicated on the average was poor. It has an average of 1.0.

Generally, the current ratio for NBL has been on the increase right from 1982 to 1986. However, in 1982 and 1983, the current ratio was very poor which indicates that there was no margin of safety for the creditors. Hope started rising when current ratios started to improve from 1.1 in 1984 to 1.2 in 1985 and 1986. The improvement in the last three years showed only little margin of safety for the creditors.

The current assets of the NBL include stocks, debtors and pre-payments, cash and bank balances. The current liabilities include trade creditors and other creditors for accrued expenses, taxation and dividends. In the above analysis, the current ratio of NBL is not good enough to attract investors to the company. This is because the company cannot meet its short-term obligations. This discourages investors from going into investment in such companies which have weak current ratios.

3.2. (b) N B L:

Acid Test Ratio:

A quick ratio of 1:1 is generally considered satisfactory as satisfactory. The average acid test ratio for NBL for the five years under consideration is 0.70 which did not meet the acceptable average of 1:1. The NBL can pay more than half of the current liabilities without touching its inventories. However, quick ratio offers a better

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way of assessing the short-term debt-paying ability of NBL. Acid test ratio increased gradually from 1982 to 1984 and dropped in 1985 and 1986 to 0.81 and 0.72, respectively.

3.2. (c) N B L:

Inventory turnover Ratio.

To calculate this ratio, the average intentory must be obtained by adding the opening and closing stock and then dividing the total by two. In this analysis, special care is given to the different inventory procedures such as LIFO, FIFO and so on which are employed by the firm.

The inventory turnover for NBL was generally good for 1982, 1983 and 1985. This is because the ratios were very high and showed how efficient and effective the company was in reducing risks and costs. In 1984 the ratio was 2.9. The year 1986 had a ratio of 2.8 which was the lowest ratio for the period under consideration.. The lowest turnover ratio could indicate that some items in the inventory figure were written off. The higher the inventory turnover ratio, the better the financial position of NBL, provided such factors as level of inventory, clearance sales, stockouts, orders for inventory replacement and so on remain positive. However, a low inventory turnover for NBL is considered to be unfavourable. The years 1984 and 1986 do not appear to be good for investors and creditors who might have sought information through this ratio. However, the overall average performance for the period of five years is reasonably good, that is, 3.6.

rising cost of production or decline in demand for its products.

The return on capital employed is divided into three categories: ie

shareholders' capital employed,
gross capital employed and
net capital employed.

Shareholders' Capital Employed:- is the ratio of net profit after taxes to networth.

Gross Capital Employed:- Shows the relationship of net profit before interests and taxes to total assets. It is also called return on investment (ROI).

Net Capital Employed: relates to net profit after interest, and taxes divided by networth plus long term debt (total assets less current liabilities).

A firm has to measure its management efficiency at using all types of capital available for it. Therefore, gross capital employed is a more appropriate figure, particularly in this case. An abnormally high ratio of return on capital employed indicates inadequate capital but usually, the higher it is, the financially stronger the organization is termed.

The return on total assets or earning power relates to net profit after taxes to total assets. This ratio provides a measure of profitability of all financial resources invested in the firm's assets.

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3.3 Profitability Ratios:

Profitability ratios have assumed prominence in the financial management of enterprises as important parameters for indicating the firm's profit trends. They are particularly very important tools being used by financial analysts for investigating the effectiveness and efficiency of the operations of a firm. Profitability is the net result of claims of polices, decisions and actions of the management. It measures how effectively a firm is managed and includes profit margin on sales, ratios that determine return on capital employed earning power and so on. The profit margin on sales is the only profitability ratio that yields information about a cause of financial distress, that is, it indicates the cause of strength or weakness of a firm. All others indicate the financial structure and/or competitive position of the firm.

Profit margin ratio is obtained when operating expenses and income tax are subtracted from the gross profit. It is calculated by dividing net profit by sales. Under normal circumstances, any percentage increase on or decrease in sales is accompanied by a greater increase or decrease in net profit, as the case may be. This ratio indicates the firm's capacity to withstand adverse economic condtions. If the net profit margin is inadequate, the firm faces difficulty in achieving satisfactory return on owners' equity. A firm with high net profit margin would be in an advantageous position to survive when there is decline in selling prices,

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It evaluates the use of total funds without any regard to the sources of funds. The higher this ratio, the better for the company as it indicates an increase in turnover of assets or increase in net profit margin or both.

3.4 N B L.

Profitability Ratios.

A few of the profitability ratios are calculated and analysed in this section as shown in Table 3:2. Due to non-availability of data, it has not been possible to analyse all the ratios stated in chapter 2.

3.4 (a) NBL: The Net Profit Margin:

The net profit margin of NBL in terms of the average performance was fairly good. It was calculated as follows:

$$\frac{\text{Net Profit}}{\text{Sales.}}$$

The highest percentage of net profit margin was recorded in 1983 and 1984 with 16% and 17% respectively. The performance of 1982 and 1986 was not impressive for the company. This could be as a result of general slump in the economy.

3.4 (b) Return on Capital Employed

It was calculated using the following formula:

$$\frac{\text{Net profit after taxes x 100}}{\text{Networth}}$$

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The performance of NBL in 1982, 1983, and 1984 was very good and had ratios of 26%, 36% and 35%, respectively. The unfavourable periods were 1985 and 1986 which had a ratio of 16% each. The implication of these figures is that for every ₦1 invested, there was a return of 26K, 36K, 35K, 16K and 16K respectively, for the stated periods.

3.4 (c) Return on Total Assets:

It was calculated susing the following formula:

$$\frac{\text{Net profit after taxes} \times 100}{\text{Total assets.}}$$

The return on total assets of NBL for the five-year period was the highest in 1984, with a figure of 18%. In fact, starting from 1982 to 1984, there was a gradual increase during the three-year period. The worst return on total assets was in 1985 and 1986 with 10% and 9%, respectively. The average for the five-year period was 14%.

N B L: Debt Ratio: The debt ratio of NBL is not analysed here because relevant data was not included in the annual reports of the company. Therefore, debt ratio analysis is not done for the five-year period under review.

3.5 ACTIVITY RATIOS.

Activity ratios measure a firm's affectiveness at employing its resources. It includes:

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(a) current assets turnover ratio,

(b) Fixed assets turnover ratio,

(c) Total assets turnover ratio,

(d) Ratio of fixed assets to networth.

(e) Sales to networth ratio.

The stock turnover ratio is grouped under liquidity ratios. It has already been discussed under 3.2.1(c). Earning power has already been analysed under the heading profitability ratios. It is very important to note that certain activity ratios are highly informative and show the actual causes of a firm's problems. They indicate financial strength or weakness of the firm.

3.5.1 The Activity Ratios or Performance Ratios.

These ratios measure firm's effectiveness at employing its resources. The activities to be analysed are discussed below:

3.5.1 (a) Current Assets Turnover Ratio:

This shows the relation of sales to current assets:

$$\frac{\text{Sales}}{\text{Current Assets.}}$$

A decline in this ratio from one period to another could indicate an increase above the desired level of current assets like stocks, debtors, or unused assets. It could also indicate reduction in sales that is unaccompanied by decrease in current assets. However, it is affected by problems faced by any of the current assets and shows

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signs of the problems without specifying the actual problem through its expression.

3.5.1 (b) Fixed Assets Turnover Ratio.

This ratio shows how effectively a firm uses its fixed assets for producing goods that are to be sold.

$$\frac{\text{Sales}}{\text{Net fixed assets.}}$$

The more effectively the fixed assets are utilised the more efficient the company is. That is, the higher the ratio the more competent the company is termed to be. However, an unsually high ratio indicates, that some or all of the company's fixed assets are leased or rented. This ratio also tests the adequacy of sales volume. It, therefore, has the symptom of excessive fixed assets; expansion of sales without adequate owner's capital, etc by its definition.

3.5.1 (c) Total Assets turnover ratio.

This ratio is calculated as follows:

$$\frac{\text{Sales}}{\text{Average total assets - Intangible fixed assets}}$$

A decline in this ratio indicates dis-utilization capacity to the optimum due to inefficiency. Increase in total assets is not justified by sales made. This ratio not only indicates the actual problem, but it is also symptomatic of various problems.

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3.5.1 (d) Ratio of Fixed Assets to Networth

This ratio measures the extent to which the net capital employed (networth) of a company is tied up in permanent, depreciable, and non-liquid assets.

$$\frac{\text{Fixed Assets}}{\text{Networth}}$$

It measures the amount of shareholders' capital that remains in business and as such shows whether too much capital is invested in fixed assets or not. Almost every company has limited amount of capital with which to operate. Excessive investment in any area including fixed assets will result in problems like additional borrowing, inadequate profit, loss etc. A high ratio indicates the actual cause of a company's problem like inadequate working capital.

3.5.1 (e) Sales to Networth Ratio.

This is sometimes called trading ratio. It is calculated as follows:

$$\frac{\text{Sales}}{\text{Networth}}$$

It shows whether a company is over-trading or under - trading. A high trading ratio indicates an over-trader while a low trading shows an under-trader. Overtrading is indicated by sales being more than the amount invested by shareholders while under-trading is when sales do not cover networth. Where sales and networth are the same or when the difference between the two is insiginificant, the company is neither an over-trader nor an under-trader.

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3.6 N B L : Activity Ratios:

The activity ratios of NBL are analysed in this section.

3.6 (a) N B L : Current Assets Turnover Ratio

$$\frac{\text{Sales}}{\text{Current Assets}}$$

This ratio was high in 1982, 1983 and 1984, and the figures showed 2.8, 2.3 and 2.1, respectively. But the period 1985 and 1986 recorded the least ratios of 1.3 and 1.13, respectively. The decline in current assets turnover shows that this company faced problems of increase above the desired in any of its components of current assets or a reduction in sales that followed decline in current assets.

3.6 (b) Fixed Assets Turnover Ratio.

$$\frac{\text{Sales}}{\text{Net fixed assets}}$$

This ratio was high in 1983 and 1984, with the figures 2.0 and 2.2, respectively. The higher ratio shows how competent the company was in using its fixed assets in the production of beer. The lower ratios were found in 1982, 1985 and 1986 with figures 1.5, 1.3 and 1.3 respectively.

3.6 (c) N B L Total Assets Turnover Ratio.

$$\frac{\text{Net Profit after taxes}}{\text{Total assets}}$$

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This ratio was not significantly high over the stated period. The ratios 1.0,1.1, and 1.1 for 1982, 1983 and 1984, respectively, were moderately high. There was a decline in total assets turnover in 1985 and 1986 with the ratios of 0.63 and 0.64, respectively. The decline in total assets turnover ratio indicates that NBL did not utilize the total assets to its maximum capacity.

3.5 (d) N B L: Fixed Assets to Networth.

This ratio was high in 1982 and 1983 with figures 1.4 and 1.2, respectively.

$$\frac{\text{Fixed Assets}}{\text{Networth}}$$

The higher ratio of NBL showed that the company lacked current assets which could easily be converted in cash. It was a problem for the NBL. This indicates the excessive assets NBL had during 1982 and 1983. The company had lower ratios of 0.92, 0.87 and 0.82 in 1984, 1985 and 1986, respectively.

3.6 (e) N B L : Sales to Network Ratio

$$\frac{\text{Sales}}{\text{Networth}}$$

This ratio for NBL, in 1982, 1983 and 1984 shows high trading of an over-trader. Over-trading for the period just mentioned above was 2.1 for 1982, 2.34 for 1983, and 2.0 for 1984,. There was under-trading in 1985 and 1986 with the ratios of 1:1 and 1:2, respectively. This means that NBL was neither under-trader nor over-trader.

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3.7 Guinness Nigerian Limited (GNL): Liquidity Ratios.

As in the case of NBL, an attempt is made in this section to make an analysis of financial data applicable to GNL for the period 1982 to 1986. The analysis follows the same order as in NBL. The data is given in Table 3.1.

The liquidity ratios of GNL are calculated and analysed here.

3.7.1(a) GNL: Current Ratio.

This ratio increased gradually from 1982 to 1986. As the acceptable ratio is 2:1, throughout the period the ratio was unsatisfactory for this company, 1982 and 1983 were the most

The low current ratio suggests that this company had working capital problem during the period.

3.7 (b) G N L : Acid Test Ratio:

The ratio increased gradually from 0.23 in 1982 to 0.91 in 1986. The acid test ratio for GNL during the first three years that is 1982, 1983 and 1984 was much below the acceptable level. During 1985 and 1986, it was nearly satisfactory. It means the company could never pay her liabilities without touching her stocks.

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The acid test ratio of GNL as it affects debt paying ability of the company is poor.

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3.7. .(c) G N L : Inventory Turnover Ratio.

This ratio was 20 times in 1982 which means that it took 18 days to realise cash from sales made on credit. The inventory turnover ratio of 31 times in 1983 was the highest during the five-year period. This ratio indicates that 'receivables' were generated through sales and collected during the year for 31 times, or that it took about 12 days only to collect cash from sales made on credit. The figures for 1984, 1985 and 1986 were 23 times, 26 times and 6 times, respectively. The inventory turnover ratio of GNL was very high during the first four years and dropped to very low level during the last year ie 1986.

3.8 G N L: Profitability Ratios.

The profitability ratios of GNL are analysed in this section. The data is shown in Table 3.2.

3.8.1 G N L: Net Profit Margin.

In 1982 the net profit margin for the company was 14.5% which was very good. The net profit margin started to decline in 1983 and 1984 to 13.2% and 12.5% respectively. The decline in net profit margin may be due to increase in operating and manufacturing costs. The net profit margin increased in 1985 to 14.7%, being the highest in the five-year period. There was a sharp decline in net profit margin in 1986 to 12.6% which was as a result of additional costs incurred in operation and manufacturing. The major cause for the relatively poor performance in 1986 can be traced to the difficult times the company faced due to shortage of raw materials.

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In general, given the prevailing economic recession, the company's net profit margin is very commendable.

3.8.2 G N L: Return on Capital Employed.

This ratio increased from 22.6% in 1982 to 24.5% in 1983. It later on decreased sharply in 1984 to 16%. Return on capital employed in 1985 increased to 21%, but dropped in 1986 to 17.4%. Generally, capital employed during the five-year period was very high. This means that GNL was actually utilizing its assets to generate net profit. The assets were under utilized in 1986. This is because of general recession in the economy which affected the company by way of shortage of raw materials as a result of stringent measures introduced by the Federal Military Government on importers. But still the performance has been satisfactory over the years.

3.8.3. G N L: Return on Total Assets.

This ratio was generally satisfactory over the years. In 1982, the rate of return was 26%, which obviously was as a result of the high net profit earned by the Company. An impressive return of 28% was recorded in 1983. The return on total assets fell to 18% in 1984 which was the lowest for the five-year period. There was an increase in 1985 to 23% and also a decrease in 1986 to 19%. In fact, there was fluctuation in the rate of return over the five-year period. It could be either due to change in the value of the total assets or due to the general recession

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in the economy.

G N L: DEBT RATIO.

Data for debt ratio was not available in the annual reports. As a result the debt ratio could not be analysed.

3.9 G N L: ACTIVITY RATIOS.

The activity ratios of GNL are analysed in this section. The data is shown in Table 3. 3.

3.9 (a) G N L: CURRENT ASSETS TURNOVER.

This ratio decreased gradually from 1982 to 1986. This could shows an increase above the desired level of current assets such as Stocks, debtors, cash and the unused assets. The highest ratio recorded for the five-years was in 1982 with a figure of 4. 0. In 1983 the ratio went down to 3. 0. The least figure was in 1985 and 1986 with a ratio of 1.6 each. The decline over the period also indicates reduction in sales which is as a result of decrease in Company's Stocks.

3.9 (b) G N L: FIXED ASSETS TURNOVER.

In 1982 this ratio was 1.4 which rose to 1.7 in 1983. In 1984, the ratio dropped to 1.3, an indication that the fixed assets that year were not properly utilized. In 1985, the ratio again rose to 1.6 and later to 1.7 in 1986. In 1985 and 1986, the Company utilized the fixed assets more efficiently than in the previous years with the exception of 1983.

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The higher the ratio the more competent the Company is termed to be.

3. 9 (c) G N L: TOTAL ASSETS TURNOVER.

The ratios of 1.0 and 1.1 in 1982 and 1983, respectively, were very high. The higher ratios show how efficiently the total assets are utilized to maximum capacity. The ratios in 1984, 1985 and 1986 were very low and this shows the disutilization capacity of the fixed and current assets. Therefore decline in the ratio indicates lack of proper utilization of the total assets.

3.9. (d) G N L: FIXED ASSETS TO NETWORTH

In 1982, this ratio was 3.4 which was high and it indicates the excessive fixed assets the Company had. This high ratio in 1982 also shows that the Company had inadequate working capital. The ratio started to decline in the following order: 1.3 in 1983, 1.1 in 1984, and 0.95 each in 1985 and 1986. This ratio shows the amount of share-holders' capital that remains in the business and the capital to be invested.

3. 9 (e) G N L: SALES TO NETWORTS RATIO.

In 1982 this ratio was 1.8. It rose to 2.1 in 1983. It shows that the company was over-trading. The cover ratio of 1984, 1985, and 1986 with 1.4, 1.6, and 1.5 respectively, shows that the sales of GNL has been fluctuating during the period. A firm that puts itself into a situation of excessive

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over-trading OR under-trading is bound to have finanacial problems.

3.10. COMPARISON OF NIGERIAN BREWERIES LIMITED (NBL) AND GUINNESS NIGERIAN LIMITED (GNL).

The financial statements of NBL and GNL from 1982 to1986 were used for the purpose of this comparison. The comparison of the two companies is based on the total average of the five-year period under consideration. The Company with the higher average ratio is regarded as better than the other Company in terms of performance. The industrial or traditional ratio standard was used in measuring the two Companies together.

The current ratio of NBL has an average of 1.0 and GNL has 1.03. Therefore, GNL has a slightely higher average than NBL. The average ratios of the two Companies were less than the standard traditional ratio of 2.1. In acid test ratio, the average of NBL was 0.46. The two averages for the Companies were less than the traditional ratio of 1.1. Despite that, the performance of NBL was higher than GNL. Both Companies performed poorly. It means that the two Companies hard to sell their inrentories before they could meet their immediate cash demand or payment.

The average net profit margin of NBL for the five-years was higher than that of GNL by 1.5 percent. Since NBL average was 15% and GNL was 13.5%, it showed that NBL was more efficient in generating net profit than GNL.

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The Return on Capital employed of NBL has an average of 26% while the average return in capital employed by GNL is 20.3%. With this comparison, we can conclude that NBL generated more return on capital employed than GNL during the five-years under consideration. The Return on total assets of NBL was very low on average for the five years. The average return on total assets was 14%. The return on total assets of GNL was 23% on average for the five years. In fact, GNL generated more return on total assets than NBL. It showsthat GNL can utilize her total assets more efficiently than NBL.

The Current assets turnover ratio of GNL was 2.5 on average for the five years. This was higher than the average current assets turnover ratio of NBL which was 1.9. The higher average ratio of 2.5 of NBL was as a result of reduction in current assets such as Stocks, Debtors, Cash or unused assets. The decline in the average ratio of NBL to 1.9 was due to increase in the current assets. With this comparison we know that GNL has less current assets or unused assets while NBL has more current assets than GNL.

The fixed assets turnover ratio of NBL on average is higher than that of GNL by 0.2. Having an average of 1.7 to its credit the past five years, NBL proved that it utilised its fixed assets more efficiently than GNL. GNL had on average only 1.5 which showed that it did not utilise its fixed assets in producing goods as efficiently as NBL.

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CHAPTER FOUR

FINANCIAL RATIO ANALYSIS OF UNITED NIGERIAN TEXTILES LIMITED (UNTL) AND AREWA TEXTILES LIMITED (ATL).

4. 0 The analysis of the financial ratios for UNTL and ATL is for the three year period, 1982 to 1984. The data for 1985 and 1986 were not made available to the analyst.

SECTION 1

4. 1 LIQUIDITY RATIOS OF UNTL.

Table 4.1 contains the liquidity ratios of the sample Companies. The ratios are analysed in this section.

4.1.1 UNTL: CURRENT RATIO.

For the UNTL, current ratio in 1982 was 1.3, indicating that the ratio is far below 2:1 which is accepted as a satisfactory figure. In that year, UNTL had little working capital to cover its current liabilities satisfactorily, and also to meet its day-to-day activities. In 1983, the ratio dropped further to 0.91, showing that the Company had serious liquidity problem. The company might have held Stock and working-in-process. There was a slight improvement in the current ratio in 1984 when the ratio went up to 1.06. The current assets were just enough to cover the current liabilities and service its debts.

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This development indicates that either UNTL had declining production due to shortage of raw materials or that stocks were held longer than necessary before being sold.

4.1.2 UNTL: ACID TEST RATIO.

This ratio was 0.27 in 1982. The general liquidity position of UNTL for 1982 to 1984 was very weak, especially in 1982 when the ratio was 0.27. There was a slight improvement in 1983 and 1984 when the ratios were 0.31 and 0.40, respectively. All these indicate that UNTL did not have enough liquidity ability to meet its creditors.

4.1.3 UNTL: Receivables Turnover Ratio.

It is calculated by this formula:

$$\frac{\text{Annual Credit Sales}}{\text{Receivables.}}$$

In calculating this ratio for 1982, Sundry debtors were not added to trade debtors to arrive at total receivables. This was not given in the balance sheet for that year. As a result the receivable turnover was higher in 1982 than in 1983 and 1984. In 1983 and 1984 both trade debtors and sundry debtors were added to get the total receivables. The 19.3 ratio recorded in 1982 was the highest, but it later dropped to 9.67 and 8.12 in 1983 and 1984, respectively. This indicates that either credit was not granted like the previous year, or that the Company did not produce enough products due to shortage of raw materials. 1983 and 1984 showed a good receivable

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turnover when compared to that of 1982. This may due to the fact that 1983 and 1984 figures included sundry debtors and trade debtors.

4.2 PROFITABILITY RATIOS OF UNTL.

These ratios are shown in table 4.2.

4.2.1 UNTL: NET PROFIT MARGIN.

In 1982, the net profit margin as a percentage figure was 0.6% and then it dropped to 0.01% in 1983 thus showing insignificant amount of net profits. In 1984, the figure rose to 4.7%. This indicates that as more of net profit was recorded within the year, the possibility of incuring losses was made more remote. These percentages indicate how much the profit margin can decline before the company can incur losses. In 1982 and 1983 the situation was worst. The net profit margin was not even up to 1%. In these two years, the shareholders might have expressed their dissatisfaction with the performance of the directors of the company. In order not to discourage the shareholders, the company declared dividends of 4 Kobo and 2.3 Kobo per share in 1982 and 1983, respectively. The problem of net profit margin over the two years was as a result of raw material shortages. The position really improved in 1984 because the company recorded a net profit which exceeded that of the previous years. Therefore, they declared a dividend of 6.25 Kobo per share in 1984.

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4.2.1 (b) U N T L: Return on Capital Employed.

For the company, in 1982 the return on capital employed was 1.5%. In 1983 it dropped to 0.2%. This was very poor and it suggests that the shareholders could not have even thought of investing in the company because they could not obtain any rate of return. In 1984, there was a great improvement because the company's return on capital rose.to 10.4%. This means that during this period the prospective shareholders were inclined towards investing in the company because they could obtain a reasonable return on their investment.

4.2.1(c) U N T L: Return on Total Assets:

The return on total assets of UNTL in 1982 was 1.5%. The return later dropped in 1983 to 0.27%. The year 1984 recorded a percentage of 11.7% which was the highest for the three-year period. The return on total assets that year could be as a result of proper utilization of the current and fixed assets of the company to generate higher returns. The position of UNTL indicates that the assets output in 1982 and 1983 was poor.

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4.3 Debt Ratios of UNTL:

The data is given in table 4.4. The debt ratios of UNTL analysed cover four years. The data for 1986 were not available for the analyst. Also total debt to total assets could not be analysed for the period as relevant data was not available.

UNTL: Debt to Networth:

This ratio was calculated using the following formula:

$$\frac{\text{Total Debt}}{\text{Networth}} \times 100$$

The highest debt to networth ratios of 1.95 and 1.7 were recorded in 1982 and 1983, while the lowest of 1.55 and 1.6 were in 1984 and 1985 respectively. The highest ratios showed that suppliers' funds were more than the shareholders' funds.

4.3.2 UNTL: Long-term debt to Capitalization.

This ratio was calculated using the formula

$$\frac{\text{Long-term debt}}{\text{Total Capitalization}}$$

Long-term debt to capitalization ratio was highest in 1982 at 0.19. In 1983 and 1984 it was 0.11 and 0.066 respectively. The lowest ratio was in 1985 at 0.06.

4.4 ACTIVITY RATIOS OF UNTL.

4.4.1. UNTL: Current Assets Turnover:

The activity ratios of UNTL are analysed in this section. The data is shown in Table 4.3. In 1982,

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the company recorded the highest ratio at 4.4. In 1983 and 1984 the ratio was 4.1 and 3.8 respectively. The company obviously was over-trading throughout the period.

4.4.2 UNTL: Fixed Assets Turnover.

In 1982 the company had the highest ratio at 2.3, followed by 2.0 in 1984 while the least figure was recorded in 1983 at 2.0. The fairly high ratio during the three year period indicates that the UNTL utilized its fixed assets efficiently in the production of goods.

4.4.3 UNTL: Total Assets Turnover.

In 1982 the ratio was 4.0 which indicates that the company utilized the current and fixed assets fairly well in the production of goods. Later on, the ratio dropped to 3.2 in 1983 and 2.7 in 1984. The drop in the last two years shows that the total assets were not efficiently utilized by the company. This could be due to the economic recession and the problem of procurement of raw materials and other numerous problems.

4.4.4 UNTL: Fixed Assets-to-Networth.

This ratio was highest in 1982 at 2.4. This shows that the investment of the company in fixed assets was very high. In 1983 and 1984, the company's fixed assets to networth ratio was 0.63 and 0.55, respectively. In these two years, the company invested less on fixed assets

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and more on liquid assets. Excessive investment on fixed assets leads to the problem of inadequate working capital, which can seriously hamper the company's ability to pay the immediate creditors.

4.4.5 UNTL: Sales to Networth Ratio.

In 1982, the company recorded the highest ratio of 5.6, followed by 1983 with 4.6 and 1984 with 4.0. Throughout the period spanning this analysis, the sales were far higher than the amount invested by the shareholders.

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SECTION II

AREWA TEXTILES LIMITED (ATL)

4.5 Liquidity Ratios of ATL: As in the case of UNTL, an attempt is made in this section to make an analysis of financial data applicable to ATL for the period 1982 to 1984. The analysis follows the same order as in UNTL. The data is given in Table 4.1.

4.5.1 ATL: Current Ratio.

The current ratio of ATL was on the increase during the three-year period. It increased from 1.02 in 1982 to 1.04 in 1983 and to 1.25 in 1984. This period characterised increase in inventory level coupled probably with adequate cash realization from sales. The figures for the three-year period under consideration were far less than the conventional standard for current ratio which is 2:1. This low ratio suggests that the company's working capital was very low and it might have discourage the short-term creditors to a considerable extent.

4.5.2 ATL: Acid Test Ratio.

This ratio was 0.20, 0.28 and 0.42 for 1982, 1983 and 1984 respectively. Throughout the period, the ratio was unsatisfactory. It can be observed that ATL had a higher proportion of inventories among the current assets. The inventories alone represented more than 70% of the total current assets. This shows that ATL hardly discharged its debts instantly without selling the inventories.

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There was not even a single year that meet the traditionally accepted standard for quick ratio of 1:1.

4.5.3 ATL: Receivable turnover Ratio.

This ratio increased from 13 times in 1982 to 26 times each in 1983 and 1984. The year 1982 showed that receivable turnover was lagging far behind the company's average. The years 1983 and 1934 each had receivable turnover ratio of 26 times which could be considered good. The receivable turnover is to measure the management performance and efficiency in collecting their credit sales made to customers during a specified period.

4.6 Profitability Ratio of ATL.

The Profitibility ratios of ATL are analysed in this section. The data is given in Table 4.2.

4.6.1 ATL. Net Profit Margin.

The net profit margin of ATL was 1.9% in 1982. It later dropped to 0.8% in 1983 and rose sharply to 3.9% in 1984. The year 1983 recorded a drastic decline in the net profit margin. The figure 0.8% was less than 1k margin per ₦1.00. The decline in net profit margin in 1983 can be attributed to increase in the expenses of the Company which invariabley reduced the net profit. However, a corrective measure was applied in 1984 and that led the net profit margin to rise to a satisfactory level of 3.9% (about 4k) which was the highest figure for the three year period.

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4.6.2 ATL: Return on Capital Employed.

In 1982 this return recorded 9% earning power which was not satisfactory. In 1983, the company experienced a serious decline in the earning power of the stock investment. The earning power dropped to 4% which was very poor in comparison with other years. It was only in 1984 that the company recorded a significant earning power on stock equity which could be considered as satisfactory. The management efficiency in 1984 result in satisfactory rate of return on capital employed.

4. 6. 3 ATL: Return on Total Assets.

For ATL the return on total assets was 3% in 1982 which regarded as unsatisfactory. The ratio for 1983 was 1%. This showed a serious decline relative to the proceeding year. After the drastic decline in 1983, the return of 6% obtained in 1984 could be considered quite impressive. The satisfactory performance for 1984 was a realistic challenge to 1983 downward trend. Generally, the return on total assets was satisfactory with the exception of 1983.

4.7 Debt Ratio of ATL.

Liquidity ratio discussed in 4.5 was to measure the liquidity position of the company. It is concerned with the ability of the company to meet its maturing

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short-term obligations, while the debt ratios deal with the ability of a firm to meet its long-term obligations. The debt ratios measure the funds supplied by owners as compared with the financing provided by the Company's creditors.

A Company's liabilities are normally divided into current liabilities and long-term liabilities. A company is said to be highly-geared (leveaged) when it has high proportion of long-term debts and lowly-geared when it has less proportion of long-term debts.

The following are the debt ratios to be discussed in relation to Arewa Textiles Limited for three years from 1982 to 1984.

(a) Debt to networth ratio

(b) Debt to total capitalization ratio.

(c) Debt to total assets.

The relevant data is given in table 4.4.

4.7.1 DEBT TO NETWORTH RATIO.

The debt to networth ratio of capital contributed by creditors and owners, which shows the balance the management of the company has struck between the total debts and owners' equity. The total debts of a Company consist of current and long-term liabilities. The ATL has only medium-term loans which have more than one year of maturity. They are regarded as long-term liabilities in this analysis.

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The networth on the other hand, comprises the portion of liabilities belonging to the owners of the company. There are the equity shares, preference shares, reserves and retained earnings. Sometimes intangible assets such as goodwill, patents, debenture discounts, trade mark and formation expenses might be included in the balance sheet If these appear and are valued very highly, they have to be deducted from the total networth of the company. To compute the debt to networth ratio, the total debts are divided by the networth. The higher the ratio, the greater the risk to debt-holders, while the lower the ratio, the less the risk.

The debt to networth ratio of ATL in 1982 and 1983 showed that the suppliers' funds were more than double the company's funds supplied by the owners. The ratios in 1982 and 1983 were 2.2 and 2.11, respectively. The ability of the company in raising these funds was prompted by its relatively moderate credit position of the previous years. However, these higher ratios for 1982 and 1983 reduced management's chances of obtaining more loans, because the creditors would be less willing to grant more credit for fear of losing in the event of adverse circumstances. Again, if economic depression forces the company to lose, it will find it difficult to pay for creditors' interests and funds supplied. In view of these, 1982 and 1983 credit position was unsatisfactory to the creditors.

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However, the high amount of credits for 1982 and 1983 yielded higher profit for the company.

The ratio of 1984 was 1.9. This position of the companys' debt was almost the same with the period 1982 and 1983 analysed above. The year 1984, experienced a downward trend of creditors' contribution relative to owners'. The higher credit position in 1982 and 1983 might have curtailed the ability of the company to obtain more loans, or possibly that more debts were charged within the period.

4.7.2 ATL: Long-term Debt to Total Capitalization Ratio.

The long-term debt to total capitalization measures the relative importance of long-term debts in capital structure of the company. Capitalisation refers to the total investment capital. It comprises owners' equity and non-current liabilities. Long-term debt to total capitalization ratio is computed by dividing the long-term liabilities by total capitalization.

Based on these data, it could be observed that ATL was not highly geared (coveraged) during the three-year period. In 1982, the long-term debt was 22% of the company's capital structure. In 1983 and 1984 it was 16% and 23% respectively. The situation in 1984 showed a remarkable increase over the preceding years.

Generally, the long-term debt to capitalization of ATL was very low and this position made the company

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attractive to creditors to grant loan on long-term basis. As long-term debts were relatively low during the period, the potential creditors were interested in granting loans to the company as chances of recovering such loans were bright due to the fact that creditors in the long-term category were few.

4.7.3 ATL: Debt to Total Assets Ratio.

Debt to total assets ratio measures the total funds provided by creditors in relation to the total assets of the company. The creditors normally prefer a moderate debt ratio because the lower the ratio, the greater the safety of their interests in the event of liquidation of the company. This ratio is computed by dividing the total debts by the total assets of the company.

The years 1982, 1983 and 1984 showed an alarmingly high ratio of 69%, 68% and 65%, respectively. The position cannot be regarded as satisfactory since creditors' funds showed a high margin. The interest charges were obviously correspondingly high. The years 1983 and 1984 recorded gradual decline in the creditors' funds. The downward trend indicated that the creditors, having realised that their funds were reaching a risky level, decided to reduce their supply of credit.

Normally, the creditors would prefer the ratio of their funds to total assets to be low.. The owners however, would want high debt to assets ratio so as to

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be able to trade on the equity especially if the loan consists more of long-term maturity period. Therefore, if the total debts of the company for the period comprised mainly long-term liabilities, it is evident that the company could trade on the equity and maximize earnings.

4.8 ACTIVITY RATIOS OF ATL:

The activity ratios of ATL are analysed in this section. The data is given in Table 4.3.

4.8.1 ATL: Current Assets Turnover Ratio:

This ratio was 2.5 in 1982, 2.7 in 1983 and dropped to 2.1 in 1984. The drop in sales to current assets ratio in 1984 was probably as a result of rise in current assets ratio in 1984 was probably as a result of rise in current assets such as stocks, debtors, or the assets were lying unused. The rise of ATL sales to current assets in 1983 was probably as a result of the drop in assets which also led to rise in sales. This made 1983 the year with the highest ratio of 2.7.

4.8.2 ATL: Fixed Assets Turnover Ratio.

This ratio was 3.8 in 1982 and the lowest during the three-year period under consideration. The ATL did not utilize its fixed assets properly in 1982 in production of textile materials as in other years. The fixed assets were better utilized in 1983 with a ratio of 4.8 the highest during the three-years. There was a slight reduction in the ratio 1984, which dropped to

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to 4.6 in 1984. Generally, the ratios for the three-year period were very high.

4.8.3 ATL: Total Assets Turnover Ratio.

This ratio was 1.5 in 1982, 1.7 in 1983 and 1.5 in 1984. It would appear that ATL did not utilize the current and fixed assets to their optimum capacity during the period under review. There was total rise in both the current and fixed assets which did not bring out any justifiable increase in sales made. Another reason could be the economic recession in the country. The ratio of 1.7 in 1983 was higher than that of the other years. It indicated that total assets were better utilized during the year 1983.

4.8.4 ATL: Fixed Assets to Networth.

During three-year period in question this ratio was 1.2 in 1982, 1.1 in 1983 and 1.1 in 1984. The ratios during the three years were virtually the same. By this analysis, it could be deduced that the company didn't invest much in fixed assets when compared to current assets. But the ratio was not so high during the period under discussion. The company probably realised the problem of investing huge amount of money in fixed assets. The company obviously gave more consideration to liquid assets than non-liquid assets.

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4.8.6 ATL: Sales to Networth Ratio.

This ratio otherwise called trading ratio, recorded a higher figure in 1983 when compared to 1982 and 1984. The ratio of 4.6 in 1982, 5.1 in 1983 and 4.2 in 1984 generally shows that the company had an over-trading throughout the three-year period. For a company to record under-trading, the sales must be less than the amount invested by shareholders. But in a situation where the sales and the maount invested by the shareholders are exactly equal, then the company is neither an over-trader nor an under-trader. In a nutshell, the ATL was an over-trader.

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SECTION III

4.9 COMPARATIVE STUDY OF UNTL AND ATL.

This comparative study of UNTL and ATL is based on the average ratio for the three-year period from 1982 to 1984. An analysis of the ratios for each company has aready been made in section I and II of this chapter. This section is section III makes a comparative study of the two companies on the basis of the ratios already analysed separately for each company.

The average current ratio of 1:1 for UNTL and ATL was exactly the same for the three years. The average for the three-year period was less than the traditional current ratio requirement of 2:1. Generally, the two companies could meet their current liabilities through the current assets at their disposal.

The Acid test ratio of UNTL and ATL on the average for the three-year period was 0.33 and 0.32, respectively. In fact, for the both companies the average ratio for the period under consideration is less than the traditionally accepted acid test ratio of 1:1. The low average ratio for the companies mean that the two companies could not meet their short-term cash requirements without touching their inventories which took a long time to yield cash. It also means that the two companies had more inventories than other liquid assets.

The receivable turnover ratio of UNTL and ATL on average were 12.4 and 21.6, respectively.

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In comparison, the UNTL was not efficient in its credit collection because on average collection for the three-years was 12.4, while ATL had an average collection period of 21.6. Generally, the higher the receivables turnover the more efficient the company is in collecting her credit and also lesser time was involved in the collection. So, while ATL took less time on average to collect her credit, UNTL took more time because the lesser the receivable turnover ratio, the longer the period involved in collecting the debts.

The net profit margin of UNTL on average for the three-year period from 1982 to 1984 was 18%, while that of ATL was 2.2%. This shows that the ATL had higher return on sales than UNTL on average for the three years under consideration. The performance of ATL was better than that of the UNTL, considering the two companies had the same sales and products.

The return on capital employed of UNTL was 4% on average for the three-year period under consideration while that of ATL was 9.7%. Thus, the UNTL had less return on capital employed than ATL. The ATL was more efficient in generating higher return on its capital employed than UNTL was. Despite the fact that the two companies produce the same products and use the same type of machinery, etcetera, still ATL performed better than UNTL.

The return on total assets of UNTL on average for the three-year period from 1982 to 1984 was 4.5%, while that of ATL was 3.3%.

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This indicates that UNTL was more efficient in generating returns from its current and fixed assets than ATL was. The efficiency in using the total assets by UNTL on average might be due to good management.

The fixed assets turnover ratio of UNTL was 2:1 on average for the three-year period under discussion while that of ATL for the same period was 4:4. Therefore, ATL had excessive fixed assets on average compared to UNTL. This also indicates that ATL invested more on fixed assets during the period, than on current assets. High investment on fixed assets create the problem of liquidity in the company which in fact cannot be avoided by ATL. ATL could be considered more efficient in using her fixed assets in the production of goods than UNTL.

The total assets turnover ratio of 3:3 of UNTL for the three years was very high on average, while that of ATL for the same period was 1:6. The average ratio of ATL did not utilise the total assets to capacity to generate sales like UNTL did.

The sales to networth ratio on average for the three-year period from 1982 to 1984 for UNTL and ATL were very high. On average, UNTL had a ratio of 4:7 while ATL had a ratio of 4:4. However, the average sales of the two companies were much higher than the amount invested by shareholders. Generally, the two companies had almost the same average ratio for the same period.

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DEBT RATIO OF UNTL AND ATL

In comparison, the debt to networth ratio of UNTL and ATL was 1.73 and 2.07 respectively on the average. However, the creditors of the two companies have nothing to fear about the safety of their money. Prompt payment can be made to them during the period of liquidation.

Long-term debt to capitalization - UNTL and ATL had on the average for three-year period of 0.122 and 0.20 respectively.
This means that UNTL and ATL acquired very little long-term loans for expansion during the period.

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CHAPTER FIVE

CONCLUSIONS AND RECOMMENDATIONS

5.1 CONCLUSIONS:

Financial ratios have been used to analyse and evaluate the performance of four manufacturing companies, three of which are quoted in the Nigerian Stock Exchange. Two manufacturing companies, Nigerian Breweries Limited and Guinness (Nigeria) Limited were analysed for a five-year period from 1982 to 1986. These two companies are brewers of beer. The other two are United Nigerian Textiles Limited and Arewa Textiles Limited; both are textiles manufacturing companies. The financial ratios of these two companies have been analysed for three-years only because the data for 1985 and 1986 were not available.

The computation of ratios is a rather simple arithmetical operations but its interpretation is a complex task. Ratios facilitate the evaluation of accounting information by reducing a large volume of data into a small set. The ratio analysis of these companies disclosed relationship as well as differences between them. The comparison was done by making use of the data obtained from these companies.

The financial analysis has examined the record of results of operations and financial position of the four companies. An analysis of this nature is an indispensable step in arriving at decisions by both the management and outsiders or investors.

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It has to be pointed out that information contained in annual reports accounts (the primary source of information) and the resulting ratio computation are not sufficient in most cases.

The NBL and GNL have unfavourable ratios in current and acid test ratios. Only inventory turnover ratio was favourable for the two companies reviewed. However, the liquidity ratios of the NBL and GNL for stipulated period were generally unsatisfactory that is, below the standard acceptable ratio during the period under consideration.

The profitability ratios for the two companies were a bit high during the period, but they still need improvement. This can make the shareholders and outsiders improve their investment in the business.

The activity ratios of the companies were exactly the same in terms of average computation during the period.

The ratios of the two textile companies, UNTL and ATL, have been computed and fully analysed in this study. It is necessary to further highlight the important facts contained in the analysis by way of summary. The liquidity ratio, especially the current ratio of both companies was the same but less than the conventional standard ratio of 2:1.

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The acid test ratio of the two companies showed that UNTL and ATL could hardly discharge their short-term debts instantly without selling their inventories. In fact, current assets for both UNTL and ATL consist mostly of inventories.

The receivables turnover of UNTL and ATL showed that the companies were efficient in obtaining cash receipts from credit sales within specified times.

The profitability ratios of the two companies were moderate and required improvement. The profit margin, return on capital employed and return on total assets of the two companies were almost the same. This is especially true when the profitability average for the three years under consideration was taken.

However, the financial difficulties of the four selected companies were both short and long-term in nature. The individual ratio analysis also shows the causes of financial difficulties of each firm. The causes of financial problems found in this study are:

too much of fixed assets,
slow-moving inventories,
over-trading and so on.

All four companies being analysed had excessive fixed capital and at the same time had been over-trading during the period covered by the study.

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5.2 RECOMMENDATIONS.

Based on the analysis made in chapters three and four, it is evident that the companies faced financial difficulties which were caused by various problems. In the light of this, the following solutions are recommended to remedy the financial difficulties:-

5.2.1 Companies With Excessive Fixed Assets.

Such companies can adopt one of or all the following steps to solve their problems.

5.2.1 (a) Excessive fixed assets such as machinery, unused parts, unused vehicles and equipment not required should be sold.

(b) Additional capital can be raised by selling stocks/shares to the existing shareholders or public through Stock Exchange Market. This will increase the networth and reduce excess of fixed assets.

(c) Excessive fixed assets should be leased or rented out.

(d) Investment on fixed assets should be restricted.

(e) Short-term loans can be obtained from creditors so as to increase the working capital, and reduce excessive investment on fixed assets.

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5.2.2 Remedies for Slow-Moving Inventories.

Companies that are very sluggish in changing their stocks into cash can use the following methods:-

(a) Inventory records should be established in order to make sure that parts or articles needed are not purchased in excessive quantities. At the same time, it is important to note that adequate supply of items should be available as and when required.

5.2.2(b) Inventory records should be examined so as detect those items of stock that are no longer used in the manufacturing or marketing programme. The identified items should be eliminated as soon as possible through sale even at low prices in the market.

5.2.2(c) The buying and inventory control function should be the responsibility of an individual or body. This is to avoid duplication of orders and promote inventory balance.

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5.2.2(d) Companies should review the rate at which each inventory component is individually turned over. This enables companies to know those items that cannot be easily sold in order to arrange to dispose of them, and reduce or even stop their production completely, if possible.

5.2.2(e) Another method of reducing inventory level is to purchase merchandise on consignment basis. Articles are made available to the company when there is a consignment agreement without immediate payment. Payment can be made after the items have been sold.

5.2.2(f) A company can arrange for loans on inventory. These loans are usually on short-term basis which cannot give lasting solution to sluggish inventory but can assist in revamping their procedures and speeding their sales.

5.2.3 Companies with Over-trading Problems.

Over-trading arises where there is excessive sales on limited networth.

Companies that have over-trading problems develop compensating advantages like better-than-average performance on receivables collection, fixed assets, investment, inventory turnover, miscellaneous assets

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control and so on, if they experience operating profits (net profits). When an over-trading company experiences operating loss, its cure is a careful analysis of each customer's account so that undesirable ones like those with slow-paying records are identified. Also freight costs, unattractive price levels for purchases and so on are looked for necessary action.

The temporary relief for an over-trader who makes either profit or loss is to borrow funds from financial institutions or secure special credit terms.

5.2.4 Those Companies that have Excessive Investments in Miscellaneous assets.

The assets that are neither current nor fixed are referred to as miscellaneous assets. These include loans and advances due from directors, employees, or officers or loans and advances to affiliated companies; prepaid expenses and deferred payments; cash value of life insurance; long-term receivables like mortgage receivables, investment in securities other than readily marketable securities, inventory suppliers (if they are distinguished from merchandise inventory, otherwise they are included among inventory under current assets; investments in or advances to subsidiaries, and so on. Pre-paid expenses and inventory of supplies are sometimes classified under current assets - depending on the accounting method used.

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Though inordinate investment in miscellaneous assets is rarely a factor faced by companies, it is difficult to correct because investment in such assets covers those made to highly placed personalities in the organization (like directors and/or managers). Here, the interests of these people are placed above that of the organization and care has to be taken to eliminate or reduce the problem of excessive investment in miscellaneous assets. Every component of miscellaneous assets has to be carefully analysed so as to ascertain the measure to be embarked upon. For instance, when a problem is found to be excessive loans made to officers, such loans should be collected back either in full or a substantial portion of it and the amount realised should be invested in business.

In fact, it should be noted that all the remedies mentioned above are directed at improving the position of a company which is in financial difficulties. However, when all efforts made to revamp a company fail, its management and/or directors (who act on owners' behalf) should, with the agreement of perhaps the creditors who are not yet paid, either amalgamate or liquidate the company as they think fit.

5.3 GENERAL RECOMMENDATIONS

(1) Directors and Auditors' Remuneration

In the analysis of the four different companies done so far, it was found out that most of their

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profits drop drastically as a result of heavy amount of money paid to directors and auditors. As the directors and auditors are not owners of the companies, they should not be paid so much at the expense of their owners.

(2) Financial and Lending Institutions.

Since Nigeria was so many financial and lending institutions, many companies borrow excessively from these institutions on a competitive basis. As a result, such companies accumulate excessive debts. At a later date, it becomes difficult when the loans are due for repayment. Such companies are, therefore, advised to operate or invest in viable projects within their means and learn to "cut their coats according to the cloth available".

(3) State of the Nigerian Economy.

Nigeria is witnessing high inflation as a result of the introduction of the Second-tier Foreign Exchange Market (SFEM) in 1986. The introduction of the market forced many companies which were depending on foreign sources of raw materials to wind up their business because they could not afford to get foreign exchange to import their raw material needs.

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The few companies that have survived, have raised prices of their goods to 600%, in some cases which is beyond the reach of the common man. This has made survival difficult for individuals and firms. However, to solve these problems, efficient management is necessary in all organizations.

If the quality and calibre of manngement required is improved, firms will survive.

Ratio analysis is an important tool for the manngement in its efforts to improve its operational efficiency.

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TABLE 3:1

LIQUIDITY RATIOS

NIGERIAN BREWERIES LTD	1982	1983	1984	1985	1986	Avera
Current Ratio	0.66	0.86	1.1	1.2	1.2	1.0
Acid Test Ratio	0.36	0.55	0.83	0.81	0.72	.70
Inventory Turnover	4.13	3.71	2.9	4.2	2.8	3.6

GUINNESS NIGERIA LTD	1982	1983	1984	1985	1986	Avera
Current Ratio	0.74	0.86	1.02	1.22	1.3	1.03
Acid Test Ratio	0.23	0.52	0.65	0.91	0.91	0.46
Inventory Turnover	20.25	30.8	23.0	26.3	5.7	21.2

TABLE 3:2

PROFITABILITY RATIOS

NIGERIAN BREWERIES LTD.	1982	1983	1984	1985	1986	Avera
Net Profit Margin	13%	16%	17%	15%	13%	15%
Return on capital employed	26%	36%	35%	16%	16%	2.6%
Return on total assets	15%	17%	18%	10%	9%	14.7%

GUINNESS NIGERIA LTD	1982	1983	1984	1985	1986	Avera
Net profit margin	14.5%	13.2%	12.5%	14.7%	12.6%	13.5%
Return on capital employed	22.6%	24.5%	16.2%	21%	17.4%	20.3%
Return on total assets	26%	28%	18%	23%	19.4%	23.0%

TABLE 3:3

Activity Ratios

NIGERIAN BREWERIES LTD	1982	1983	1984	1985	1986	Aver
Current Assets turnover	2.8	2.3	2.1	1.30	1.13	1.9
Fixed Assets turnover	1.5	2.0	2.2	1.3	1.45	1.7
Total assets turnover	1.0	1.1	1.1	0.63	0.64	0.9
Fixed Assets to networth	1.4	1.2	0.92	0.87	0.82	1.04
Sales to networth	2.1	2.34	2.0	1.1	1.2	1.75

GUINNESS NIGERIA LTD	1982	1983	1984	1985	1986	Average
Current Assets turnover	4.0	3.0	2.4	1.6	1.6	2.5
Fixed assets turnover	1.4	1.7	1.3	1.6	1.7	1.5
Total assets turnover	1.0	1.1	0.84	0.89	0.83	0.93
Fixed assets to networth	3.4	1.3	1.1	0.95	0.95	1.54
Sales to networth	1.8	2.1	1.4	1.6	1.5	1.7

TABLE 4:1

LIQUIDITY RATIOS

UNITED NIGERIAN TEXTILE LTD

	1982	1983	1984	1985	1986	Average
Current Ratio	1.3	0.91	1.06	-	-	1.1
Acid test ratio	0.27	0.31	0.40	-	-	.33
Receivable turnover	19.35	9.67	8.12	-	-	12.4

AREWA TEXTILES LTD	1982	1983	1984	1985	1986	Average
Current ratio	1.02	1.04	1.25	-	-	1.8
Acid test ratio	0.26	0.28	0.42	-	-	.32
Receivable turnover	13	26	26	-	-	21.6

TABLE 4:2

PROFITABILITY RATIOS

UNITED NIGERIAN TEXTILES LTD

	1982	1983	1984	1985	1986	Average
Net profit margin	0.6%	0.1%	4.68%	-	-	1.8%
Return on capital employed	1.5%	0.2%	10.4%	-	-	4%
Return on total assets	1.5%	0.27	11.7%	-	-	4.5%

AREWA TEXTILES LTD	1982	1983	1984	1985	1986	Average
Net profit margin	1.9%	0.8%	3.9%	-	-	2.2%
Return on capital Employed	.9%	4%	16%	-	-	9.7%
Return on total assets	3%	1%	6%	-	-	3.3%

TABLE 4:3

ACTIVITY RATIOS

UNITED NIGERIAN TEXTILES LTD

	1982	1983	1984	1985	1986	Average
Current assets turnover	4.4	4.1	3.8	-	-	4.1
Fixed assets turnover	2.3	2.0	2.1	-	-	2.13
Total assets turnover	4.0	3.2	2.7	-	-	1.2
Fixed assets to networth	2.4	0.63	0.55	-	-	1.2
Sales to networth	5.6	4.6	4.0	-	-	4.7

AREWA TEXTILES LTD	1982	1983	1984	1985	1986	Average
Current assets turnover	2.5	2.7	2.1	-	-	2.4
Fixed assets turnover	3.8	4.8	4.6	-	-	4.4
Total assets turnover	1.5	1.7	1.5	-	-	1.6
Fixed assets to networth	1.2	1.1	1.1	-	-	1.13
Sales to networth	4.0	5.1	4.2	-	-	4.6

TABLE 4:4

DEBT RATIOS

UNITED NIGERIAN TEXTILES LTD

	1982	1983	1984	1985	1986	Average
Debt to networth	1.95	1.7	1.55	-	-	1.73
Long-term debt to Capitalization	0.19	0.11	0.066	-	-	0.122
Total debt to total assets	-	-	-	-	-	-

AREWA TEXTILES LTD	1982	1983	1984	1985	1986	Average
Debt to networth	2.2	2.11	1.9	-	-	207
Long-term debt to Capitalization	0.22	0.16	0.23	-	-	0.20
Total debt to total assets	0.69	0.68	0.65	-	-	0.67

APPENDIX I

NBL: BALANCE SHEET.

As at 31 December, 1986

	Notes	1986 ₦'000	1985 ₦'000
Employment of Capital			
Fixed assets	2	141,752	141,004
Current assets	3	181,620	131,994
Total assets		323,372	272,998
Current liabilities	4	(150,524)	111,129
Gross Capital Employed		172,848	161,869
Sources of Capital			
Share capital	5	85,781	57,188
Capital reserve	6	45,499	45,616
Reserve for scrip issue	7	—	28,594
Profit undistributed		41,568	30,471
Shareholders' Funds		172,848	161,869

M. A. Makinde
J.P.C. Corlay } DIRECTORS

The notes on pages 11 to 15 form an integral part of these accounts.

APPENDIX II

NBL: PROFIT AND LOSS ACCOUNT.

For the year ended 31st December, 1986

	Notes	1986 ₦'000	198 ₦'00
Turnover	12	**205,476**	178,1
Profit before taxation	8	45,387	41,5
Taxation	9	(17,820)	(15,0
Profit after taxation		27,567	26,5
Profit undistributed brought forward		30,471	56,3
Profit attributable to shareholders		58,038	82,8
Dealt with as follows:-			
Contribution to National Economic Recovery Fund		—	8,0
Dividends	10	16,470	15,7
Reserve for scrip issue	7	—	28,5
Profit undistributed carried forward		41,568	30,4
		58,038	82,8

The notes on pages 11 to 15 form an integral part of these accounts.

NBL: SOURCE AND USE OF FUNDS.

		1986		1985
Source of funds:		₦'000		₦'000
Profit before taxation		45,387		41,566
Depreciation		15,859		16,175
Profit on disposal of fixed assets		(151)		(373
Total funds available		61,095		57,368
Use of funds:				
Cash spent on capital projects (net of disposal proceeds)	16,574		9,745	
National Economic Recovery Fund Contribution	8,054		—	
Tax paid	18,281		44,249	
Dividends paid	15,732		21,620	
		(58,641)		(75,614)
Increase/(decrease) in working capital and cash		2,454		(18,246)
Represented by movements in:-				
Stocks		30,482		5,856
Debtors		69,244		2,628
Creditors		(47,169)		3,767
Cash and bank balances		(50,103)		(30,497)
Net increase/(decrease) as above		2,454		(18,246)

NBL: FIVE YEAR FINANCIAL SUMMARY.

	AS AT 31st DECEMBER	1986 ₦000	1985 ₦000	1984 ₦000	1983 ₦000	198 ₦00
1.	**Turnover**					
	Including excise duty	205,476	179,109	322,125	317,387	241,09
	Excise duty	56,924	53,783	87,589	86,746	65,79
	Net proceeds of Sale	148,552	125,326	234,536	230,641	175,30
2.	**Capital employed**					
	Share capital	85,781	57,188	57,188	57,188	45,75
	Capital reserve	45,499	45,616	45,616	45,616	45,61
	Other reserves	41,568	59,065	56,302	32,969	24,57
	Shareholders' Funds	172,848	161,869	159,106	135,773	115,94
3.	**Represented by:**					
	Fixed assets	141,752	141,004	147,068	157,528	161,11
	Net current assets/ (liabilities)	31,096	20,865	12,038	(21,755	(45,17
	Net Assets	172,848	161,869	159,106	135,773	115,94
4.	**Profit before taxation**	45,387	41,566	104,158	95,652	53,88
5.	**Profit after taxation**	27,567	26,544	55,358	49,402	30,38
6.	**Dividends**	16,470	15,727	32,025	29,574	18,03
7	**Earnings per share ***	16.07k	15.47K	32.27K	28.80K	17.71
8.	**Dividends per share ***	9.60k	9.16K	18.67K	17.23K	10.51

**Based on issued share capital at 31st December, 1986.*

Profit and Loss Account

For the year ended 31st August, 1986

	Notes	1986		1985	
		₦'000	₦'000	₦'000	₦'000
TURNOVER	1		268,052		258,214
PROFIT BEFORE EXCEPTIONAL ITEM AND TAXATION	2		70,310		68,439
EXCEPTIONAL ITEM	3		(10,216)		—
PROFIT AFTER EXCEPTIONAL ITEM AND BEFORE TAXATION			60,095		68,439
TAXATION	4		(26,295)		(30,600)
PROFIT AFTER TAXATION			33,800		37,839
DIVIDENDS:	5				
1st Interim paid 21.7.86		(9,500)		(7,500)	
2nd Interim payable 6.1.87		(8,000)		(12,000)	
Proposed final		(2,780)		(3,200)	
			(20,280)		(22,700)
RETAINED PROFIT FOR THE YEAR			13,520		15,139
Earnings per share			17k		19k
Dividends per share			10k		11k

The accounting policies on page 17 and notes to the accounts on pages 21 to 24 form part of these accounts.

Report of the Auditors, page 16.

GNL

Balance Sheet

As at 31st August, 1986

	Notes	1986		1985	
		₦'000	₦'000	₦'000	₦'000
ASSETS EMPLOYED					
FIXED ASSETS	6		156,911		155,481
CURRENT ASSETS	7	164,336		135,739	
Less CURRENT LIABILITIES	8	127,303		110,978	
NET CURRENT ASSETS			37,033		24,761
TOTAL NET ASSETS			193,944		180,242
CAPITAL AND RESERVES					
SHARE CAPITAL	9		100,000		76,000
CAPITAL RESERVE	10		59,133		59,420
REVENUE RESERVES	11		15,011		29,822
SHAREHOLDERS' FUNDS			174,144		164,242
LOAN STOCKS	12		14,800		16,000
DEFERRED TAXATION			5,000		—
TOTAL CAPITAL EMPLOYED			193,944		180,242

DR. A. K. UBEKU, OFR
B. A. ARENYEKA
} *Directors*

The accounting policies on page 17 and notes to the accounts on pages 21 to 24 form part of these accounts.

Report of the Auditors, page 16.

GNL

Statement of Source and Use of Funds

For the year ended 31st August, 1986

	1986 N'000	1985 N'000
SOURCE OF FUNDS		
Profit before taxation	70,310	68,439
Adjustment for items not involving the movement of funds:		
Transfer from Revenue Reserve to Gratuity	(1,141)	(1,141)
Depreciation	10,623	10,721
Transfer of Maintenance Project Expenditure	82	547
(Profit)/Loss on disposal of fixed assets	(69)	22
Exceptional Item	(10,215)	—
Total generated from operations	69,590	78,588
Funds from other sources:		
Unclaimed Dividends from Registrars	767	2,029
Proceeds of sale of fixed assets	68	130
TOTAL	70,415	80,747
USE OF FUNDS		
Capital Expenditure	12,150	2,697
Income Tax paid during the year	25,111	26,410
Dividends paid during the year	20,480	18,012
National Economic Recovery Fund Contribution	2,190	—
Scrip Issue Costs	287	—
TOTAL	60,218	47,119
NET INFLOW OF FUNDS	10,197	33,628
REPRESENTED BY INCREASE IN WORKING CAPITAL		
Stocks	13,339	1,585
Debtors	1,342	436
Creditors	(18,400)	(10,475)
Movement in net liquid funds	13,916	42,082
	10,197	33,628

The accounting policies on page 17 and notes to the accounts on pages 21 to 24 form part of these accounts.

Report of the Auditors, page 16.

GNL

Financial Summaries

As at 31st August	1982 N'000	1983 N'000	1984 N'000	1985 N'000	1986 N'000
RESULTS					
Turnover	179,861	240,347	215,708	258,214	268,052
Profit before Taxation	35,782	54,724	50,356	68,439	60,095
Taxation	(9,681)	(23,000)	(23,378)	(30,600)	(26,295)
Profit after Taxation	26,101	31,724	26,978	37,839	33,800
Dividends	(15,661)	(19,034)	(16,187)	(22,700)	(20,280)
Retained Earnings	10,440	12,690	10,791	15,139	13,520
BALANCE SHEET					
Fixed Assets	132,306	143,092	164,205	155,481	156,911
Cash/Investments	2,536	49,414	49,126	91,208	105,124
Other Current Assets	42,955	32,593	42,510	44,531	59,212
Total Assets	177,797	225,099	255,841	291,220	321,247
Current Liabilities	(61,259)	(95,871)	(89,597)	(110,978)	(127,303)
Total Net Assets	116,538	129,228	166,244	180,242	193,944
Share Capital	50,000	50,000	75,000	75,000	100,000
Capital Reserves	32,166	32,166	59,420	59,420	59,133
Revenue Reserves	18,372	31,062	15,824	29,822	15,011
Shareholders' Funds	100,538	113,228	150,244	164,242	174,144
Debenture Stocks	16,000	16,000	16,000	16,000	14,800
Deferred Taxation	—	—	—	—	5,000
Capital Employed	116,538	129,228	166,244	180,242	193,944

SOURCE AND USE OF FUNDS

	1982 N'000	1983 N'000	1984 N'000	1985 N'000	1986 N'000
Funds generated from operations	40,737	64,003	59,801	78,588	69,399
Funds from other sources	130	369	732	2,159	1,016
Total Sources	40,867	64,372	60,533	80,747	70,415
Capital Expenditures	44,861	20,434	4,287	2,697	12,150
Income tax paid	8,234	12,673	16,278	26,410	25,111
Dividends paid	10,758	13,393	15,903	18,012	20,480
Other payments	94	—	2,323	—	2,477
Total Uses	63,947	46,500	38,791	47,119	60,218
Increase/(decrease) in funds	(23,080)	17,872	21,742	33,628	10,197

C. N. L.

Financial Summaries *(continued)*

STATEMENT OF VALUE ADDED	1982 N'000	1983 N'000	1984 N'000	1985 N'000	1986 N'000
Turnover	179,861	240,347	215,708	258,214	268,052
Bought-in Materials and services	61,780	83,532	69,507	67,796	78,128
Excise Duty	56,083	65,951	60,654	86,846	90,502
	61,990	90,864	85,547	103,572	99,422
Distribution:-					
For employees	20,218	24,506	27,084	23,032	27,324
Maintenance of Assets	5,040	9,365	10,096	10,721	10,623
To Government	9,681	23,000	21,327	30,600	26,295
To Providers of Capital	16,611	21,303	16,249	24,080	21,660
Re-investment in the business	10,440	12,690	10,791	15,139	13,520
	61,990	90,864	85,547	103,572	99,422

STATISTICS

	1982	1983	1984	1985	1986
Share price at 31st August	110k	111k	98k	114k	117k
Earnings per share (adjusted)	13k	16k	13k	19k	17k
Dividends per share (adjusted)	8k	10k	8k	11k	10k
Net Assets per 50k share (adjusted)	50k	57k	75k	82k	90k
Current Assets: Current Liabilities	0·74	0·86	1·02	1·22	1·29
Return on Capital Employed	22·4%	24·5%	16·2%	21·0%	17·4%
Return on Shareholders' Fund	26·0%	28·0%	18·0%	23·0%	19·4%
Return on Net Sales value	14·5%	13·2%	12·5%	14·7%	12·6%

Note: Bonus issues of 1 for 3, 1 for 2 and 1 for 3 were made on 25th February 1982, 15th March, 1984 and 13th March, 1986.

Dividends, Earnings and Net Assets per share have been adjusted to take account of these issues.

APPENDIX X

UNITED NIGERIAN TEXTILES LIMITED

BALANCE SHEET AT 31ST DECEMBER, 1984

	Notes	1984 ₦'000	1983 ₦'000
ASSETS EMPLOYED:			
Fixed Assets	2	16,267	17,453
Investments	3	10,356	10,356
Net Current Assets	4	17,129	12,568
		43,752	40,377
FINANCED BY:			
Share Capital	5	17,000	17,000
Reserves	6	12,762	10,835
Shareholders' Funds		29,762	27,835
Deferred Liabilities	7	13,990	11,542
Loans		-	1,000
		43,752	40,377

Mohammed Aminu Sanusi
Sing Fong Zao
} Directors

The notes set out on pages 18 to 24 form part of these accounts.

APPENDIX XI

UNITED NIGERIAN TEXTILES LIMITED

AND ITS SUBSIDIARY COMPANIES

CONSOLIDATED BALANCE SHEET AT 31ST DECEMBER, 1984

	Notes	1984 ₦'000	1983 ₦'000
ASSETS EMPLOYED:			
Fixed Assets	2	56,625	64,547
Investments	3	1,350	1,350
Net Current Assets/(Liabilities)	4	4,761	(5,626)
Preliminary and Preproduction Expenses		726	1,018
		63,462	61,289
FINANCED BY:			
Share Capital	5	17,000	17,000
Reserves	6	13,089	9,760
Shareholders' Funds		30,089	26,760
Deferred Liabilities	7	16,557	13,298
Minority Interest		7,571	6,800
Loans	8	9,245	14,431
Mohammed Aminu Sanusi, Sing Fong Zao — Directors		63,462	61,289

The notes set out on pages 18 to 24 form part of these accounts.

APPENDIX XII

UNITED NIGERIAN TEXTILES LIMITED

AND ITS SUBSIDIARY COMPANIES

FINANCIAL REVIEW

	1984	1983	1982	1981	1980
CAPITAL EMPLOYED	₦'000	₦'000	₦'000	₦'000	₦'000
Share capital	17,000	17,000	17,000	17,000	17,000
Capital Reserve	650	650	650	650	650
Revenue Reserve	12,439	9,110	9,211	9,041	8,027
Shareholders' Interest	30,089	26,760	26,861	26,691	25,677
Loans and Advances	9,245	14,431	24,028	16,622	10,275
Minority Interest	7,571	6,800	7,726	8,293	7,735
Deferred Liabilities	16,557	13,298	7,790	5,972	4,618
Total Capital Employed	63,462	61,289	66,407	57,578	48,305
REPRESENTED BY					
Fixed Assets	56,625	64,547	65,782	47,741	36,402
Investment	1,350	1,350	-	3,000	-
Net Current Assets/ (Liabilities)	4,761	(5,626)	(471)	5,377	11,143
Deferred Revenue Expenditure	-	-	-	-	234
Preliminary and Pre-Production Expenses	726	1,018	1,096	1,460	526
TURNOVER, PROFITS, TAXATION AND DIVIDENDS					
Turnover	141,356	136,809	152,861	139,501	136,053
Profit before Tax	11,568	2,378	4.133	4.740	4,321
Taxation	4,941	2,203	3,127	2,299	1,641
Profit After Tax	6,627	175	1,006	2,441	2,680
Profit Attributes to UNTL	5,454	798	1,360	2,204	2,379
Dividend	2,125	850	1,190	1,190	1,445
Profit/(Loss) for the year Retained	3,329	(52)	170	1,014	934
Dividend Per share	6.25k	2.5k	3.5k	3.5k	4.25k
Earnings per share	16.04k	2.35k	4.0k	6.48k	7.00k
Net Assets per share	184.52k	177.27k	192.09k	165.05k	139.84k

Note: Dividends, Earnings and Net Assets per share are calculated Paid-Up Capital of 34,000,000 Ordinary Shares of 50k each.

ARIA, NIGERIA.