ST. MARY'S UNIVERSITY COLLEGE

BUSINESS FACULTY

DEPARTMENT OF ACCOUNTING

ANALYSIS AND EVALUATION OF FINANCIAL PERFORMANCE ON CHECHELA MEDICAL SERVICE PLC

BY

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January, 2012

SMUC

Addis Ababa

AN ASSESSMENT OF ANALYSIS AND EVALUATION OF FINANCIAL PERFORMANCE IN CHECHELA MEDICAL SERVICE PLC

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CHAPTER ONE
INTRODUCTION

1.1 Background of the Organization

Health problem is one of the critical issues that need attention in developing countries. In this regard Ethiopia has formulated policies, regulations, and strategies that develop the health coverage of the country. These policies and strategies create conducive environment for private sectors to involve in the medical service sector. Using these opportunity private medical sectors is emerged to participate in resolving the medical problem of the country. Hence, Chechela Medical Service PLC becomes one of the important medical service sectors in the country.

The Chechela medical service PLC was established by Ethiopian proclamation 1952, article 514(2) and 515 in 1999 E.C. as PLC. The company is owned by three specialist Doctors and it has got legal entity and limited liability; registered according to the business proclamation and law of the country.

The company entered in to its initial operation, with very few medical equipments and offices in a building rented from private individual to give clinical services with these very minimum facilities. The current health services provided by the company are medical treatment and awareness creation on the pre protection of diseases.

Currently it is playing great role in the sector by modernizing the medical service through using high-technology medical equipments especially in the area of pathology, radiology cryptology including all laboratory services within the past five years.

The vision of the company is to have international standard medical institute and is working towards it. Accordingly, it has developed its own long and short term plan by developing business plan. In this regard the company designed its short term plan in a way that it will enhance its medical service provision by considering the interest of its customers. The long term plan of the company is to give standardized service so as to realize its vision.

1.2 Background of Study

The background of study is related to the company background is that, the company vision is to have international standard medical institute and is working towards it but, the company has few medical equipments and offices in a building rented from private individual to give clinical services with these very minimum facilities. For achieving this vision and improve their services capacity the company evaluates their finance performance because it is used to identify financial performance weakness and strength and to get decision improving finance for up grading the minimum services. According to different literatures we can see the usefulness of financial performance evaluation for anticipating the future.

According to Chandra (2004: 79), financial analysis depends primarily on the statements to diagnose financial performance; the reason is that (I) as long as the accounting biases remain more or less the same over time, meaningful in terms can be drawn by examining trends in raw data and in financial ratios (II) since similar biases characterize various firms in the same industry, inter firm comparison are useful (III) experience seems to suggest that financial analysis, works if one is aware of accounting biases and makes adjustments for the same.

A properly analyzed and interpreted financial statement can provide valuable insights in to a firm’s performance. Analysis of financial statements is of interest to lenders (short term as well as long term) investors, security analysis, managers, and others. Financial statement analysis may be done for variety of purpose, which may range from a simple analysis of the short term liquidity position of the firm to a comprehensive assessment of the strength and weakness of the firm in various areas. It is helpful in assessing corporate excellence, judging credit worthiness, valuing equity shares, forecasting financial situations, predicting bankruptcy, and assessing market risk.

According to Pandey (2005:114-115), financial analysis is starting point for making plans. Before using any sophisticated for casting and planning procedures; understanding the past is prerequisite for anticipating the future. Financial analysis is the process of identifying, the financial strength, and weakness of the firm by property establishing relationships between the items of the balance sheet and the profit and loss account. Financial analysis can be undertaken by management of the firm, or by parties outside the firm owners, creditors, investors and others. According to Chandra (2004) and Pandey (2005 analysis of financial statements is one of the influential criteria to determine financial position or over all financial performance of the company. On view of this concept ratio analysis such as liquidity ratio, leverage ratio, activity ratio, profitability ratio, time serious analysis and other related financial analysis were conducted for the study.

1.3 Statement of the Problem

The success or failure of any business organization, whether governmental or not depends on the level of its effectiveness and efficiency in utilizing its resources. Chechela Medical Service PLC as a business company runs its business by providing health service. More over as a business making company it focuses on profit maximization through efficient and effective utilization of financial resources.

Besides this the company is working hard to be a competent company in the country and beyond. For Chechela to be a sustainable and progressive competent in the business it has to conduct regular evaluation on its performance, efficiency, and effectives either internally by developing its own mechanism or by other external body. However, under our information the company has shown some losses and currently there is no trend of evaluating its financial performance.

Therefore, the purpose of this study is to analyze and evaluate the financial performance, the liquidity, and solvency, profitability, efficiency of financial resource utilization of Chechela medical service PLC and hence, to develop recommendation that will help the company adopted financial statements evaluation to improve its financial performance.

These research questions are based on solutions for the predefined problems, to get reliable information from concerned parties. The following questions are formulated in a way that it helps to sum up the assumptions so as to give recommendation to the company for further improvement.

1. What are the company's financial administration strategies to be a competent company in this business?
2. How the Company administers its financial resources?
3. How the company, evaluate its financial performance?

1.4 Objectives of the Study

The general objective of the study is to analyze and interpret the financial statements of the Chechela Medical Service PLC and to give recommendations.

The specific objectives are:

- To investigate the financial administration strategy of the company;
- To examine the efficiency of the company in managing and utilizing its financial resources;
- To assess the company's financial performance evaluation.

1.5 Significance of the Study

The major benefits of this study will be:

- It allows the researchers to practice a similar study that could be performed in other company
- It enables the manager of Chechela medical service to be aware the existing financial performance and its importance in achieving the vision and intended objectives
- Enriches the knowledge of the reader on financial performance
- It enables the lender concerned primarily about the company's ability to pay back a loan

1.6 Delimitation/Scope of the Study

The scope of the study will cover the financial performance in Chechela medical service PLC. Our selected company has two branches, hence, all financial documents are collected to headquarter office, and all financial documents are getting available in head office, due to this fact we bounded four years data, (Year 2008-2011). Because of the company has started effective Accounting system, since beginning of 2008. And try to explain the financial statement as an assistant to finance management and related staffs.

1.7 Definition of Terms

In this research there are words which will need some elaboration and definition based on operational concepts of research that help for readers to get enough idea. Those terms are:

- **Financial statements** are formats that indicate financial condition and financial position of the company (Pandey, 1999: 29).
- **Financial statement analysis** can also be defined as the process of giving meaningful interpretation to the figure in the financial statements so that every user could understand it easily and use it as a tool for decision making (Pandey, 1999: 30). Financial statement analysis allows managers, investors and creditors to reach conclusion about financial status of a firm. What is perhaps more important about financial statement analysis is forecasting outcomes about a firm's future financial performance (Pandey, 1999: 108).
- **Financial performance** is operationally defined as financial activities that indicate effectiveness or weakness of the company by evaluating, analyzing financial statements, and related financial documents (Pandey, 1999: 109).

1.8 Research Design and Methodology

1.8.1 Research Design

The researchers used descriptive research design method to evaluate and analyze the financial statements analysis ratios. This method is appropriate methods, because our research focused more on the secondary data to evaluate and analyze financial statement of the company.

1.8.2 Population and Sampling Technique

No sampling technique used due to nature of the research. But we used all data because of a viability of only four years formally recorded data. The researches focused on formally recorded data are used as secondary data for this research. Besides this, focus group discussion, interview, and personal observation are used for primary data collection.

1.8.3 Types of Data used

For this senior research paper, the data that are used primary and secondary data obtained from the company based on the research objectives as well as statements of the problems. The researches focused on the secondary data collected from financial statements as main data for analysis and focus group discussion, interview and personal observation as supplementary data for confirmation of the result of secondary data analysis.

1.8.4 Methods of Data Collection

Primary data was collected from employees of the company who have accounting knowledge and who are involved in the finance recording and financial statement analysis, through interview and focus group discussion. The secondary data was gathered mainly from the yearly un published audited financial statements of the company, and from some selected un a published financial reports.

1.8.5 Data Analysis Methods

The study used trend analysis which is also known as time serious analysis to compare financial ratios of the company successive financial statements. Moreover, theoretical rule of thumb or traditional opinions used to evaluate the company's financial ratios. Finally, the data processed and analyzed using descriptive analysis and presented using tables and charts.

1.9 Limitations of the Study

Busy schedule of the company personnel during group discussion and interview, absence of well organized referential documents and shortage of budget during data collection and analysis are the main limitations faced during conducting this research.

1.10 Organization of Study

This research have four chapters, the first chapter includes: Background of the organization, background of study, statement of the problem, objectives of the study, significance of the study, scope of the study, definition of terms, research design and methodology, limitation of the study and organization of study. Chapter two deals with related literature review and Chapter three includes data presentation, analysis, and interpretation. The fourth chapter includes summary, conclusion, and recommendation.

CHAPTER TWO
REVIEW OF RELATED LITERATURE

2.1 Financial Statement

Financial Statements provide the primary means for managers to communicate about the financial condition of their organization to outside parties. Managers, investors, lenders, and government agencies are among the users of financial statements. Substantial information is conveyed by financial statements about the financial strength and correct performance of an enterprise. Although financial statements are prepared primarily for users outside an organization, managers also find their organization's financial statements useful in making decisions. As mangers develop operating plans, they think about how those plans will affect the performance of the organization, as conveyed by the financial statements (Ronald, 1997: 915).

There are four primary financial statements.

- Balance Sheet
- Income Statement
- Retained earnings statement
- Statement of cash flows

The balance Sheet presents an organization's financial position at a point in time. It shows the balances in the organization's assets, liabilities and owners' equity, as of the balance sheet date (Ronald, 1997: 915).

The Income Statement reports the income for the period between two balance sheet dates. The Retained Earnings Statement shows how income and dividends for the period have changed the organization's retained earnings.

The Statement of Cash Flows shows how cash was obtained during the period and how was used.

2.2 Financial Statement Analysis

Financial statement analysis is an analysis which highlights important relationships in the financial statements. It focuses on evaluation of past operations as revealed by the analysis of basic statements. Financial statement analysis embraces the methods used in assessing and interpreting the results of past performance and current financial position as they relate to particular factors of interest in investment decision (Jawahar, 2001: 827).

Assessment of past performance and current position

Past performance is often a good indicator of future performance. Therefore, an investor or creditor looks at the trend of past sales, expenses, net income, cash flow and return on investment not only as a means for judging management's past performance but also as a possible indicator of future performance. In addition, an analysis of current position will fell; for example, what assets the business owns and what liabilities must be paid. It will also tell what the cash position is, how much debt the company has in relation to equity, and how reasonable the inventories and receivables are knowing a company's past performance and current position is often important in achieving the second general objective of financial analysis (Pandey, 2000: 81).

Assessment of future potential and related risk

Information about the past and the present is useful only to the extent that it has bearing on decisions concerning the future. An investor judges the potential earning ability of a company because that ability will affect the value of the market price of the company's stock and the amount of dividends the company will pay. A creditor judges the potential debt-paying ability of the company. The potentials of some companies are easier to predict than those of others and so there is less risk associated with them. The risk of the investment or loan depends on how easy it is to predict future profitability or liquidity (Pandey, 2000: 33).

2.3 Objectives of Financial Analysis

The objective of financial statement analysis is to use historical accounting data to help in printing how the firm will fare in the future. The aspects of an organization's future performance that are most interest depend on the needs of the user. A manager in the firm would be interested in the company's overall financial strength, its income and growth potential, and the financial effects of pending decisions. A potential lender, such as a bank loan officer, would be concerned primarily about the firm's ability to pay back to loan; potential investors would be interested not only in the company's ability to repay its loan obligations, but also its future profit potential. Potential customers would want to assess the firm's ability to carry out its operations effectively and meet delivery schedules (Ronald, 1997: 916).

2.4 Strategies of data analysis

Our strategies are based on interview, focus group, observation, and financial analysis. Interview is a formal meeting at which we are asked questions in order to find out if they are suitable for the research. While focus groups are the groups of individuals providing people through an open - in depth discussion rather than simply asking questions to solicit participant response. However, that we focus more on observation and financial analysis (Holt and David, 1992: 169).

The evaluation techniques are based on observing the ratios according to time trend and consistency of related four years financial statements. We will observe the techniques and procedures that the company adoption to administer its financial resources by looking through registration books, financial ledgers, and journals are the most our focal points, to make evaluation and fiscal assessment. Furthermore we will present the condition in tables and chart bars, to make easy comparison between ratios versus their financial years.

2.5 Tools and Techniques of financial analysis

Different methods are applicable to get a better understanding about financial status of the firm and operating results. The most frequently used techniques in analyzing financial statements are the following: (Pandey, 2005: 110)

2.5.1 Ratio Analysis

Ratio analysis is a powerful tool of financial analysis. A ratio is defined as "the indicated quotient of two mathematical expressions" and as "the relation between two or more things". In financial analysis ratio is used as a bench mark for evaluating the financial position arid performance of a firm. The absolute accounting figures reported in the financial statements do not provide a meaningful understanding of the performance and financial position of a firm. An accounting figure conveys meaning when it is related to some other relevant information. The relationship between two accounting figures, expressed mathematically is known as a financial ratio (or simply as a ratio). Ratio helps to summarize the large quantities of financial data and to make qualitative judgment about the firm's performance (Pandey, 2000: 109).

Ratio analysis is a widely-used tool of financial analysis. It can be used to compare the risk and return relationships of firms of different sizes. It is defined as the systematic use of ratios to interpret the financial statements so that the strengths and weakness of a firm as well as its historical performance and current financial condition can be determined. The term ratio refers to the numerical or quantitative relationship between two items/variables. This relationship can be expressed as percentages, fraction, and proportion of numbers. This alternative method of expressing items which are related to each other are, for purposes of financial analysis referred to as ratio analysis.

The rationale of ratio analysis lies in the fact that it maker related information comparable. A single figure by itself has no meaning but when expressed in terms of a related figure, it yields significant inferences (Khan and Jain, 2004: 72).

2.5.2 Types of Ratios

Several ratios, calculated from the accounting data, can be grouped into various classes according to financial activity or function to evaluate. As stated earlier, the parties interested in financial analysis in evaluating every aspects of the firm's Performance. In view of requirements of the several of ratios, they may be classified into the following four important categories (Pandey, 1999: 111).

- Liquidity Ratios
- Leverage Ratios
- Activity Ratios
- Profitability Ratios

2.5.2.1 Liquidity Ratios

Liquidity Ratios are used to measure a firm's ability to meet short-term obligations. They compare short-term obligations to short –term (or current) resources available to meet these obligations. (James and John, 2004: 134-136).

The importance of adequate liquidity in the sense of the ability of a firm to meet current/short-term obligations when they become due for payment can hardly be overstressed. In fact, liquidity is a prerequisite for the very survival of a firm. The short-term creditors of the firm are interested in the short-term solvency or liquidity of a firm. But liquidity implies, from the viewpoint of utilization of the funds of the firm that funds are idle or they earn very little. A proper balance between the two contradictory requirements, that is, liquidity and Profitability, is required for efficient financial management. The liquidity ratios measure the ability of a firm to meet its short-term obligations and reflect the short-term financial strength/solvency of a firm. The ratios which indicate the liquidity of a firm are: current ratios, quick ratios and net working capital ratios (Khan and Jain, 2004: 73).

- **Current Ratio:** One of the most general and frequently used of these liquidity ratios is the current ratio. It shows a firm's ability to cover its current liabilities with its current assets (James and John, 2004: 134-136).

It is also important to keep a reasonable amount of working capital to ensure that short- term obligations can be paid on time, opportunities for volume expansion can be seized, and unforeseen circumstances can be handled easily (Ronald, 1997: 919).

$$\text{Current ratio} = \frac{\text{Current Asset}}{\text{Current Liability}}$$

- **Acid-test (Quick) Ratio:** It shows a firm's ability to meet current liabilities with its most liquid (quick) assets.

$$\text{Quick Ratio} = \frac{\text{Current Asset} - \text{Inventories}}{\text{Current Liabilities}}$$

- **Net working Capital Ratio:** The difference between current assets and current liability excluding short term bank borrowing is called working capital. Net working capital represents the excess of current assets over current liabilities. The term current assets refers to assets which in the normal course of business get converted into cash without diminution in value over a short period, usually not exceeding one year or length of operating/cash cycle whichever is more. Current liabilities are those liabilities which at the inception are required to be paid in short period, normally a year. Although net working capital is really not a ratio, it is frequently employed as a measure of a company's liquidity position. An enterprise should have sufficient net working capital in order to be able to meet the claims of the creditors and the day-to-day needs of business. Accordingly, net working capital is a measure of liquidity (Khan and Jain, 2004: 74).

2.5.2.2 Financial Leverage (Debt) Ratio

Financial leverage refers to the use of debt finance. While debt capital is a cheaper source of finance, it is also a riskier source of finance. Leverage ratios help in assessing the risk arising from the use of debt capital (Chandra, 2004: 76).

Which is also known as debt solvency ratios, are designed to assist the decision maker in judging whether a firm has too little or much debt and then go on to explain the following debt ratios (James and John, 2004: 136).

- **Debt-to-equity Ratio:-**To assess the extent to which the firm is using borrowed money; we may use several different debt ratios. It shows the relative contributions of creditors and owners. The numerator of this ratio consists of all debt, short-term as well as long-term, and the denominator consists of net worth plus preference capital (Chandra, 2004: 76).

$$\text{Debt-to-equity Ratio} = \frac{\text{Total Debt}}{\text{Shareholder's equity}}$$

- **Debt-to-Total-Asset Ratio:-**It is derived by dividing a firm's total debt by its total assets (James and John, 2004: 136-137). It measures the extent to which borrowed funds support the firm's assets.

$$\text{Debt-to-Total-Asset Ratio} = \frac{\text{Total Debt}}{\text{Total Assets}}$$

2.5.2.3 Activity Ratio

Also known as efficiency or turnover ratios, measure how effectively the firm is using its assets. As we will see, some aspects of activity analysis are closely related to liquidity analysis. We will focus on how effectively the firm is managing two specific asset groups receivables and inventories and its total assets in general (James and John: 2004, 139).

- **Receivable turnover Ratio:** Provides insight into the quality of the firm's receivables and how successful the firm is in its collections.

$$\text{Receivable turnover Ratio} = \frac{\text{Annual net credit sales}}{\text{Receivables}}$$

- **Inventory turnover ratio:** To help determine how effectively the firm's managing inventory (and also to gain an indication of the liquidity of inventory).

  Inventory turnover or stock turnover, measures how fast the inventory is moving through the firm and generating sales (Chandra, 2004: 79).

$$\text{Inventory turnover ratio} = \frac{\text{Cost of Goods Sold}}{\text{Inventory}}$$

- **Total asset turnover Ratio:** This ratio measures how efficiently assets are employed, overall (Chandra, 2004: 81).

  As in to the output – capital ratio in economic analysis, the total assets turnover is defined as:

$$\text{Total asset turnover Ratio} = \frac{\text{Net sales}}{\text{Total Assets}}$$

2.5.2.4 Profitability Ratios

Profitability ratios are two types- those showing profitability in relation to sales and those showing profitability in relation to investment. Together, these ratios indicate the firm's overall effectives of operation (James and John, 2004: 146-148).

Profitability reflects the final result of business operations. These are two types of profitability ratios: Profit margin ratios show the relationship between profit and sales. Since profit can be measured at different stages, there are several measures of profit margin. The most popular profit margin ratios are: gross profit margin ratio and net profit margin ratio. Rate of return ratios reflect the relationship between profit and investment (Chandra, 2004: 81).

- **Profitability in relation to sales:**- It consider is the Gross profit Margin

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

- **Profitability in relation to Investment:**-It measures is the rate of return on investment or return on assets.

$$= \frac{\text{Net profit after taxes}}{\text{Total Assets}}$$

- **Return on Equity** $= \frac{\text{Net Profit after Taxes}}{\text{Shareholder Equity}}$

2.6 Standards of Comparison

The ratio analysis involves comparison for a useful interpretation of the financial statements. A single ratio in itself does not indicate favorable or unfavorable condition. It should be compared with some standard. (Pandey, 2000: 153) stated that standards of comparison may consist of:

- Past ratios i.e. ratios calculated from the past financial statement of the same firm;
- Projected ratios, i.e. ratios developed using the projected, or Performance of financial statements of the same firm;
- Competitors ratios, i.e. ratios of some selected firms, especially the most progressive and successful competitor, at the same point in time, and
- Industry standard, i.e. ratios of the industry to which the firm belongs (Pandey, 2000: 143).

But we are only interested to analyze ratios of financial statements of the company four years 2008-2011 including projected proforma financial statements of company to make comparison, due to difficulty of getting industrial standard average

2.7 Comparative Financial Statements

Comparative financial statements show the company's financial results for two successive years. These statements highlight the change in each financial item between different years (Ronald, 1997: 918).

- **Horizontal Analysis**

  It is an analysis of the year-to-year change in each financial statement item. The purpose is to determine how each item changed, why it changed, and whether the change is favorable or unfavorable.

- **Trend Analysis (Time series analysis)**

  When the comparison is expected to three or more years the technique is called trend analysis. It can be shown in birr or percentage or both form by designating the first year in the sequence as the base year.

- **Proforma Analysis**

Sometimes, future ratios are used as the standard of comparison. Future ratios can be developed from the projected or proforma, financial statements. The comparison of current or past ratios with future ratios shows the firms relative strengths and weaknesses in the past and future. If the future ratios indicate weak financial position, corrective actions should be initiated (Pandey, 2000: 146).

2.8 Advantages and Limitation of Ratio Analysis

- **Advantage**
  - ✓ Easy to compute
  - ✓ It allows industry comparison at point of time serious
  - ✓ To identify problem areas of firm
  - ✓ For prediction of net income and growth prospects
- **Disadvantage**
  - ✓ Easily misinterpreted
  - ✓ Provides little useful information
  - ✓ Ratios are based on accounting data that subject to different interpretation and manipulation
  - ✓ Very few or no standards exist that can be used to judge the adequacy of a ratio

CHAPTER THREE

DATA PRESENTATION, ANALYSIS, and INTERPRETATION

2.9 Financial Analysis of Chechela Medical Service PLC

This part of the study deals with the analysis and the interpretation of data gathered through surveying financial statements of Chechela medical service PLC. Financial statements are formatted reports that indicate financial performance of the company which this research focused on. This formatted company's annual report has been prepared for each year and each contains the balance sheet, the income statement, the cash flow statement.

2.10 Ratio Analysis

Ratio analysis is one of the most important tools to see all financial directions and status of the company. It helps to summarize the large quantities of financial data and to make qualitative judgments about the firm's performance. It provides clues to investigate those issues in detail. Ratio analysis is used to interpret the financial statements so that the strengths & weakness of a firm as well as its historical performance & current financial condition can be determined.

There are major groups of ratio that are used to evaluate financial performance of a company. Summary data and ratio analysis was presented with their interpretation as follows using appropriate ratio techniques for each of the financial situations.

2.11 Liquidity Ratios

Liquidity refers to the ability of company to meet its short term obligations and efficiency. It refers to how productive a company is, and also focuses on the total asset and total liability of a company.

2.11.1 Current Ratio

The current ratio indicates how many birr of short term assets are available for every birr of short term liability that the company owed.

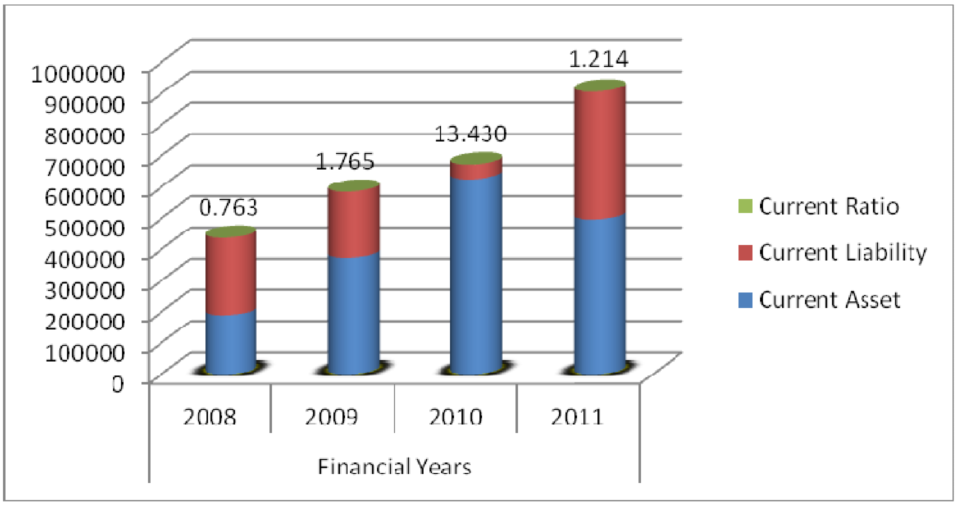
$$\textbf{Current Ratio} = \frac{\textbf{Current Assets}}{\textbf{Current Liabilities}}$$

Table 1 Current Ratio

Description	**Financial Years**			
	2008	**2009**	**2010**	**2011**
Current Asset	189,870.43	374,176.91	626,544.93	497480.54
Current Liability	248,779.90	212,050.89	46,652.63	409736.57
Current Ratio	0.763	1.765	13.430	1.214

Source: Financial statements of Chechela medical service PLC.

Figure 1 Current Ratio



Source: Financial statements of Chechela medical service PLC.

As shown in table 1 and figure 1 above Chechela medical service has higher current ratio in years 2009 and 2010 (1.765 and 13.43 respectively), where as in 2008 and 2011 it is relatively lower (0.763 and 1.214 respectively). This implies the company had fewer current assets for every birr of current liabilities in the two years i.e. 2008 and 211. On the other hand the current ratio represents margin of safety for creditors. The higher the current ratio the greater the margin of safety: the larger the amount of current assets in relation to current liabilities and the more the company is able to meet its current obligation.

2.11.2 Net Working Capital Ratio

Net working capital indicates how many birr of working capital are available to pay bills and current debts. Net working capital is really not a ratio; it frequently employed as a measure of company's liquidity position.

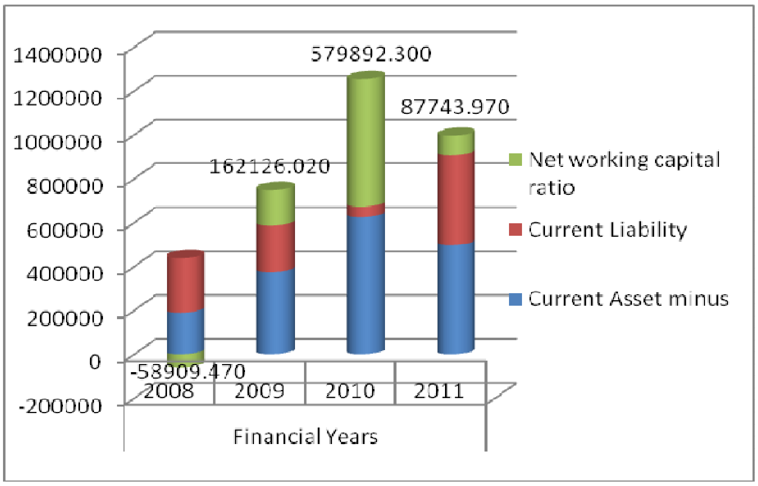
Net Working Capital = Current Asset – Current Liability

Table 2 Net Working Capital Ratio

Description	Financial Years			
	2008	2009	2010	2011
Current Asset	189,870.43	374,176.91	626,544.93	497480.54
Current Liability	248,779.90	212,050.89	46,652.63	409736.57
Net Working Capital	(58,909.47)	162,126.91	579,892.30	87743.97

Source: Financial statements of Chechela medical service PLC.

Figure 2 Net Working Capital Ratio



Source: Financial statements of Chechela medical service PLC.

The Net Working Capital ratio shows the company has no sufficient capital in relation to its size & working environment. As it shown in table 2 and fig 2 above in year 2008 the net working capital is negative i.e. -58909.470 this means the company cannot cover the current liability because current liability is greater than the working capital. However, in the other years (2009, 2010, & 2011) the net working capital is 162126.02, 579,892.30, and 87,743.97 respectively which is positive although the amount is higher in the year 2010.

2.11.3 Quick /Acid Test/Ratio

This ratio measures the company's ability to meet short-term obligation from its most liquid assets. In this case, inventory is not included with other assets because it is generally for less liquid than the other current asset.

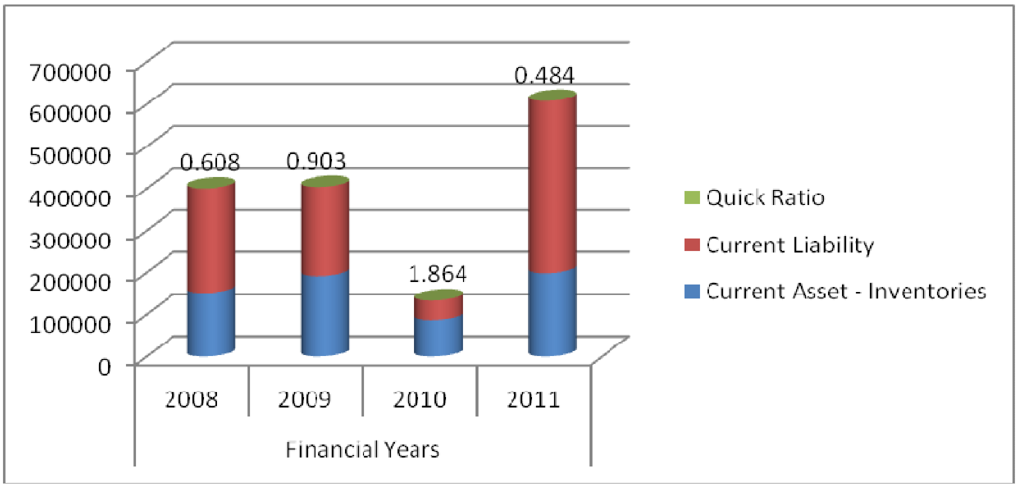
$$\text{Quick Ratio} = \frac{\text{Current Asset} - \text{Inventory}}{\text{Current Liability}}$$

Table 3 Quick Ratio

Description	Financial Years			
	2008	**2009**	**2010**	**2011**
Current Asset	1898,70.43	374,176.91	626,544.93	497480.54
Inventory	38,539.70	182,663.62	539,606.50	294107.50
Current Liability	248,779.90	212,050.89	46,652.63	409736.57
Quick Ratios	0.608	0.903	1.864	0.484

Source: Financial statements of Chechela medical service PLC.

Figure 3 Quick Ratio



Source: Financial statements of Chechela medical service PLC.

In year 2008, 2009 and 2011 shows numerical ratio values 0.608, 0.903 and 0.484 respectively indicating that, the company's, current asset were not sufficient enough after deduction of its inventory for each birr of its current liability. This shows stored inventories and receivables were very less compared to the current liability. As indicating in the table 3 and figure 3 above the company has less quick ratios in all succeeding analysis years except in year 2010 (i.e.1.864).

Beside this company should reduce and should pay its current liability according to time scheduled to have more net current asset after deduction of inventory for each birr of its current liability.

2.12 Activity Ratios

Activity ratio referred to as turnover ratios or asset management ratios measure how efficiently the assets are employed by a company. These ratios are based on the relationship between the lists of activities, represented by sales or cost of goods sold.

2.12.1 Receivable Turnover Ratio

This ratio indicates how the company collects its account receivables /revenue from customers or credit and show annual sales and inventory.

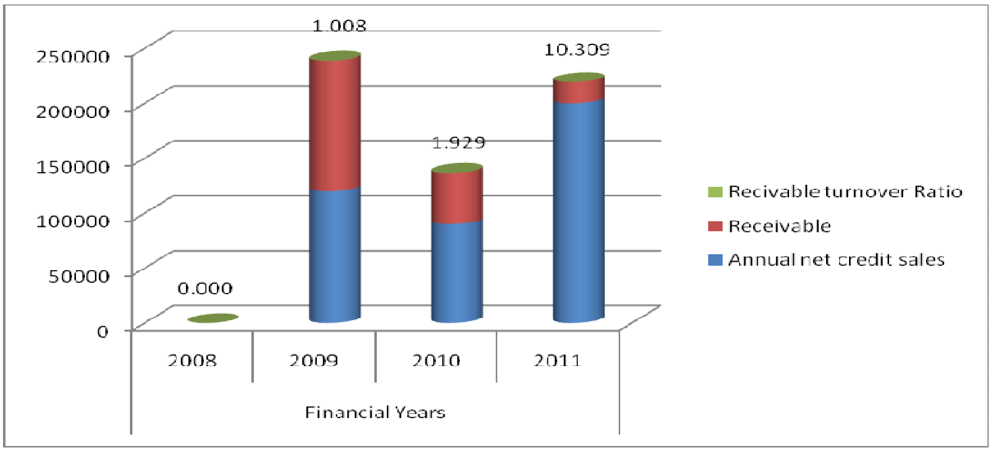
$$\textbf{Receivable Turnover Ratio} = \frac{\textbf{Annual Net Credit Sales}}{\textbf{Receivables}}$$

Table 4 Receivable Turnover Ratio

Description	**Financial Years**			
	2008	**2009**	**2010**	**2011**
Annual Net Credit Sales	0.00	0.00	0.00	0.00
Receivable	0.00	21000	46652.63	24359.75
Receivable Turnover Ratio	0.00	0.00	0.00	0.00

Source: Financial statements of Chechela medical service PLC.

Figure 4 Receivable Turnover Ratio



Source: Financial statements of Chechela medical service PLC.

As shown in table 4 and fig 4 above the receivable turnover ratio of year 2008, 2009, 2010 and 2011 was nil because credit sales not clearly stated on the financial statements of the company.

As facts showed due to numerical ratios calculated in all years was nil because of the credit sales were not collected clearly for our evidence in all years. Therefore, the company should stated and make credit term customers to increase its annual sales volume because revenue can be generated from both cash sales and credit sales to maximize company's profit margin and at the same time company should develop strong receivables collection policy by using receivables aging methods or by promoting giving discounts for quick payers for their receivable settlement and putting provision for bad debt expenses such as un collectability of receivables, due to unforeseen circumstances and contingences based on analysis and forecasting of environmental and market situations.

2.12.2 Inventory Turnover Ratio

This ratio measures how the inventory is moving through the company and generating sales. It reflects the efficiency of inventory management.

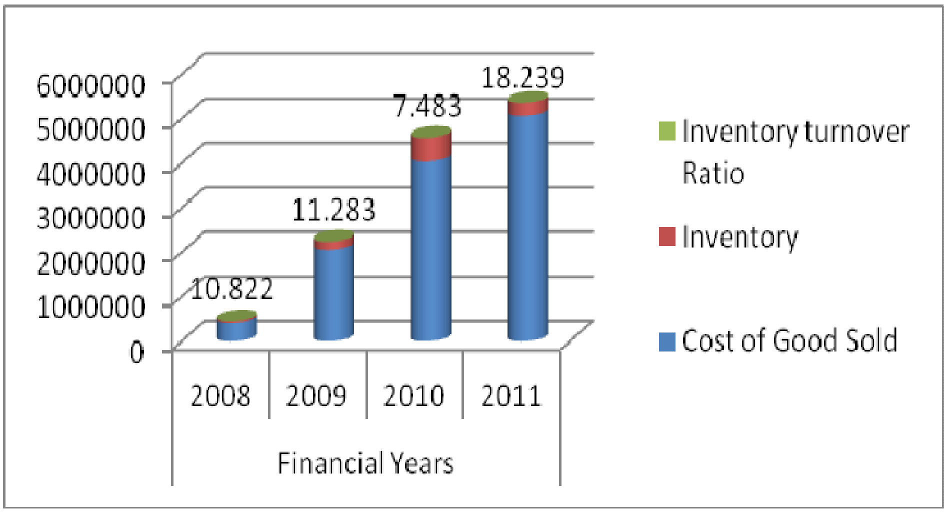
$$\text{Inventory Turnover Ratio} = \frac{\text{Cost of Goods Sold}}{\text{Inventory}}$$

Table 5 Inventory Turnover Ratio

Description	Financial Years			
	2008	**2009**	**2010**	**2011**
Cost of Goods Sold	0.00	0.00	0.00	2313358.57
Inventory	38539.7	182663.62	539606.5	294107.50
Inventory turnover Ratio	0.00	0.00	0.00	7.866

Source: Financial statements of Chechela medical service PLC.

Figure 5 Inventory Turnover Ratio



Source: Financial statements of Chechela medical service PLC.

The result shows year 2008, 2009, and 2010 has zero inventory turnover ratios as compared to year 2011 i.e.7.866. Zero inventory turnover ratios means the company has no turning over its inventory. T In year 2011 shows the company used inventories for sale. As it was confirmed during focus group discussion and interview low inventory turnover caused by a high level of inventory which is resulted in infrequent stock outs and loss of sale.

2.12.3 Total Asset Turnover Ratio

This ratio shows how efficiently the company is using its assets to support sales.

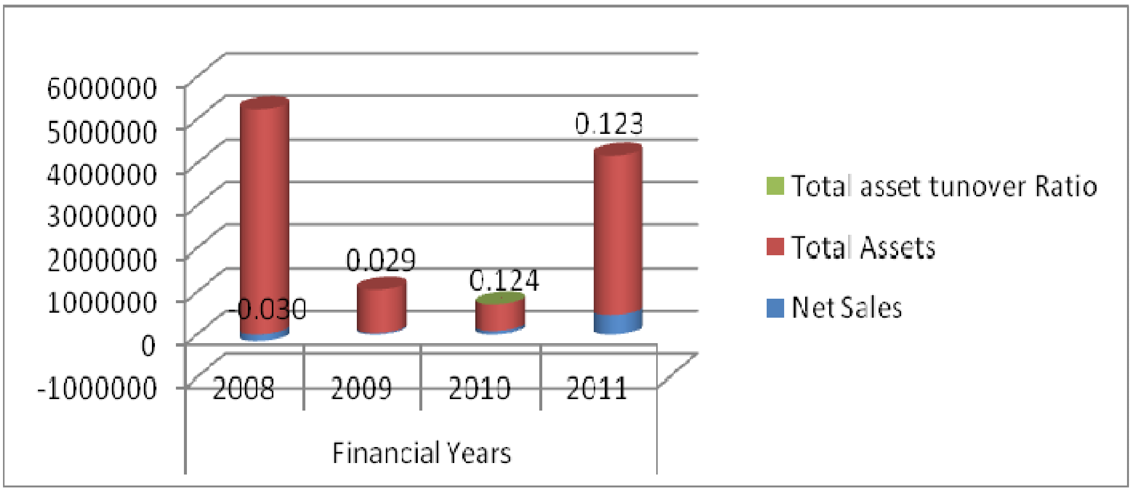
$$\text{Total Asset Turnover Ratio} = \frac{\text{Net Sales}}{\text{Total Asset}}$$

Table 6 Total Asset Turnover Ratio

Description	Financial Years			
	2008	2009	2010	2011
Net Sales	417064.97	1867814.03	4037886.89	5454688.88
Total Assets	5231871.4	1022334.56	626544.93	3719329.02
Total asset turnover Ratio	0.080	1.827	6.445	1.467

Source: Financial statements of Chechela medical service PLC.

Figure 6 Total Asset Turnover Ratio



Source: Financial statements of Chechela medical service PLC.

As shown in the Table 6 and Fig 6 above the total asset turnover of the year 2008 was 0.080; it is the worst as compared to the continuing consecutive years (year 2009, 1.827, year 2010, 6.445 and year 2011, 1.467).In year 2010 asset turnover ratio is higher compared to other years because more assets used to for sales. The lower asset turnover in the year 2008 indicates lower annual sales compared to its utilization of total assets, hence, sales are generated by using asset resources, and each birr of annual sales should shows incremental advantage for each birr of utilized total assets.

2.13 Leverage Ratios

This ratio refers to the use of debt finance. It helps to identify the cheaper source of finance as well as the riskier source of finance. It also helps in assessing the risk arising from the use of debt capital.

2.13.1 Debt to Equity Ratio

This ratio shows the relative contribution of creditors and owner.

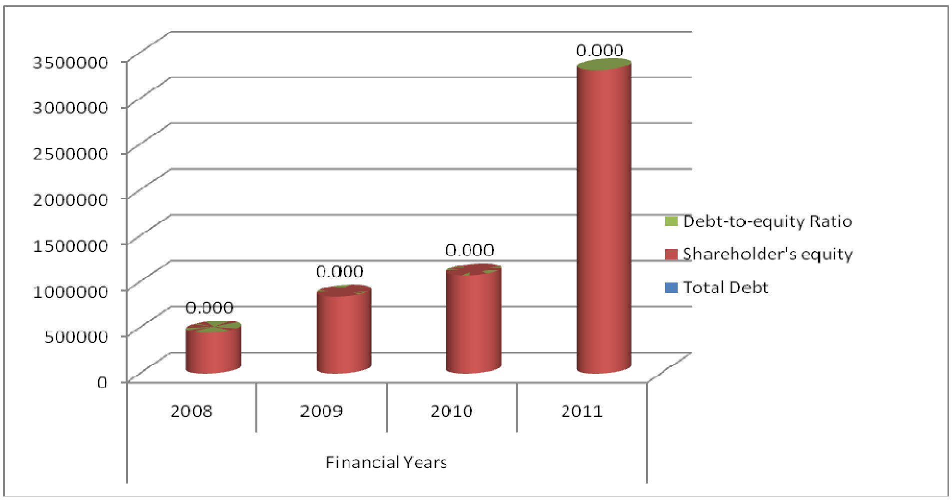
$$\text{Debt to Eqity Ratio} = \frac{\text{Total Debt}}{\text{Stock holder's Equity}}$$

Table 7 Debt to Equity Ratio

Description	Financial Years			
	2008	2009	2010	2011
Long Term Debt	0	0	0	0
Stock Holders Equity	445,291.50	810,283.68	3,420,000.00	3660310.82
Debt-Equity Ratios	0	0	0	0

Source: Financial statements of Chechela medical service PLC.

Figure 7 Debts to Equity Ratio



Source: Financial statements of Chechela medical service PLC.

As shown in the Table7 and Fig.7 above Chechela medical service owners have contributed more funds than lender. From the information gathered during focus group discussion and the interview conducted with the finance manager, it was understood that the owners of the company are not risk taker. Besides this, they explained during the discussion that they want to run the business using their own capital.

2.13.2 Debt to Total Asset Ratio

It measures the extent to which borrowed funds support the company assets.

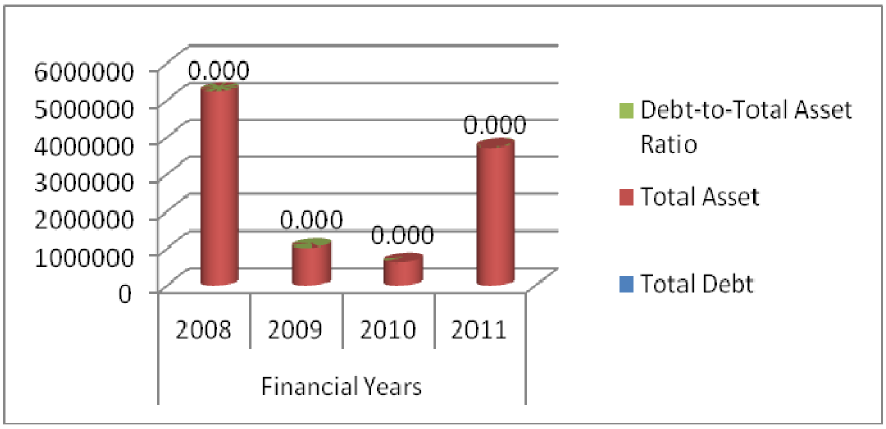
$$\textbf{Debt to Total Asset Ratio} = \frac{\textbf{Total Debt}}{\textbf{Total Asset}}$$

Table 8 Debt to Total Asset Ratio

Description	**Financial Years**			
	2008	**2009**	**2010**	**2011**
Total Debt	0	0	0	0
Total Asset	5231871.4	1022334.56	626544.93	3719329.02
Debt-to-Total Asset Ratio	0.000	0.000	0.000	0.000

Source: Financial statements of Chechela medical service PLC.

Figure 8 Debts to Total Asset Ratio



Source: Financial statements of Chechela medical service PLC.

According to the information gathered from the focus group discussion and the interview conducted with the finance manager of Chechela Medical Service PLC, they are not risk taker .Simply they want to run the company only their finance. Because of the company not adoption to work with financing agents to increase its capital and to make enhancement of its working environment in terms, technology, skilled manpower, modern buildings, and well organized medical facilities. Therefore, the company should look for its modernization in terms of its working aspects by working with these financing agents like banks.

2.14 Profitability Ratios

Profitability ratio indicates that, the amount of each birr of profit after tax to each birr of total income. It reflects the final result of business operations.

2.14.1 Profitability in Relation to Sales

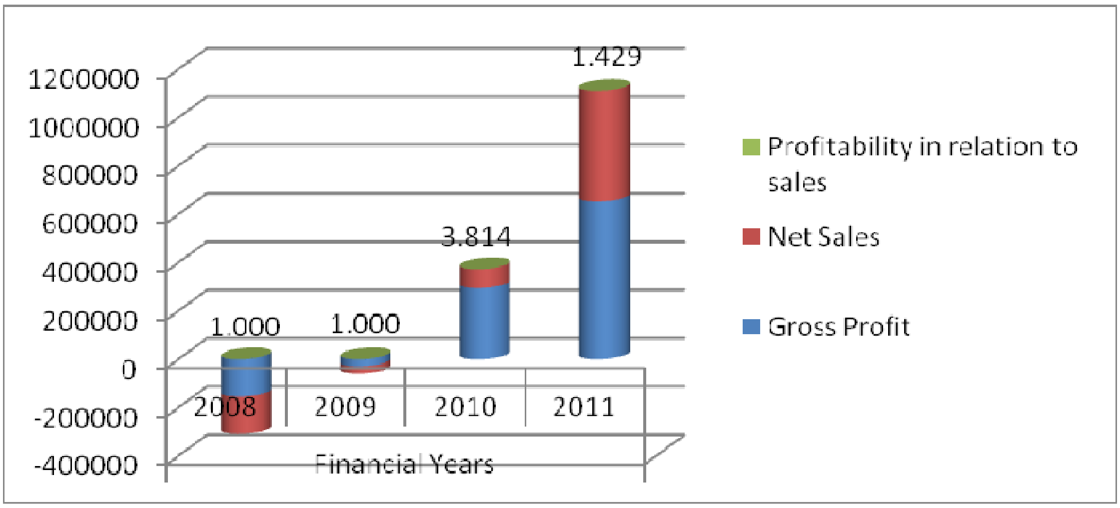
$$\textbf{Profitability in Relation to Sales} = \frac{\textbf{Gross profit}}{\textbf{Net Sales}}$$

Table 9 Profitability in Relation to Sales

Description	**Financial Years**			
	2008	**2009**	**2010**	**2011**
Gross Profit	417064.97	1867814.03	4037886.89	3141330.31
Net Sales	417064.97	1867814.03	4037886.89	5454688.88
Profitability in relation to sales	1.000	1.000	1.000	0.576

Source: Financial statements of Chechela medical service PLC.

Figure 9 Profitability in Relation to Sale



Source: Financial statements of Chechela medical service PLC.

As indicated above the profitability ratio in years 2008, 2009, and 2010 is 1. However, it is less in year 2011which is 0.576. Because from the table we can see the profit and sales ratios are the same. Besides this the result shows the gross profit and net sale of the first three years (2008, 2009and 2010) is equal. And even in year 2011 the result shows gross profit is greater than the net sales because of cost of income, but still it has lower ratio. The result shows the company's profit margin is not satisfactory.

2.14.2 Profitability in Relation to Investment

This ratio implies the amount of profit earned on each birr invested in assets. It helps to measure management efficiency in using assets.

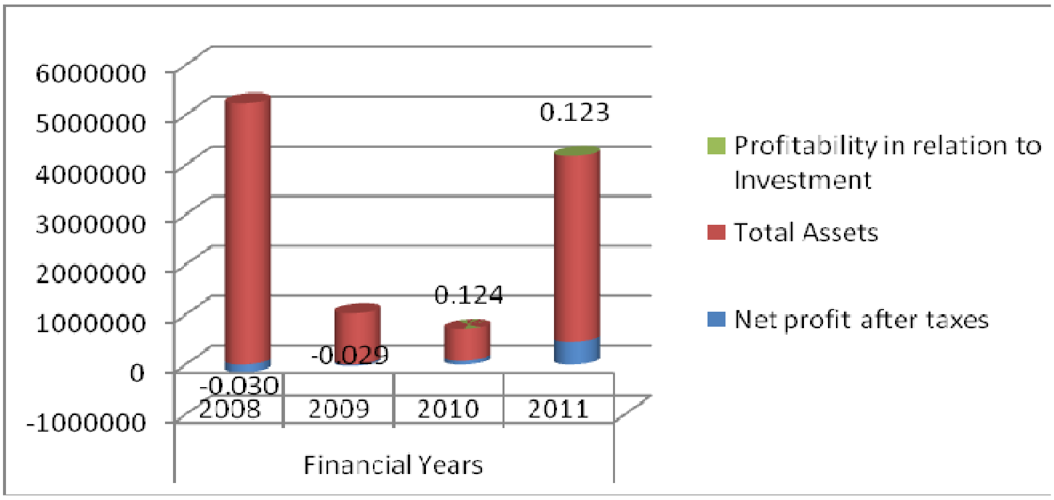
$$\textbf{Profitability in Relation to Investment} = \frac{\textbf{Net Profit after Taxes}}{\textbf{Total Assets}}$$

Table 10 Profitability in Relation to Investment

Description	**Financial Years**			
	2008	**2009**	**2010**	**2011**
Net Profit After Taxes	-154708.5	-30007.82	77432.59	457129.18
Total Assets	5231871.4	1022334.56	626544.93	3719329.02
Profitability in Relation to Investment	-0.030	-0.029	0.124	0.123

Source: Financial statements of Chechela medical service PLC.

Figure 10. Profitability in Relation to Investment



Source: Financial statements of Chechela medical service PLC.

From the above profitability Chechela Medical Service PLC in relation to investment on asset show positive ratio in years 2010 and 2011 where as in the first two years 2008 and 2009 it was negative. On the other hand the investment on asset is greater than the return. As it was confirmed during the group discussion and interview the cost of investment on fixed asset is higher because the company is in its infant stage in year 2008 and 2009 and also Sales are very little.

2.14.3Return on Equity

This ratio implies the amount of profit earned on each birr invested by stock holders. It measures management efficiency of using stakeholders’ equity.

Return on Equity = <u>Net Profit after Tax</u>

Stock Holder’s Equity

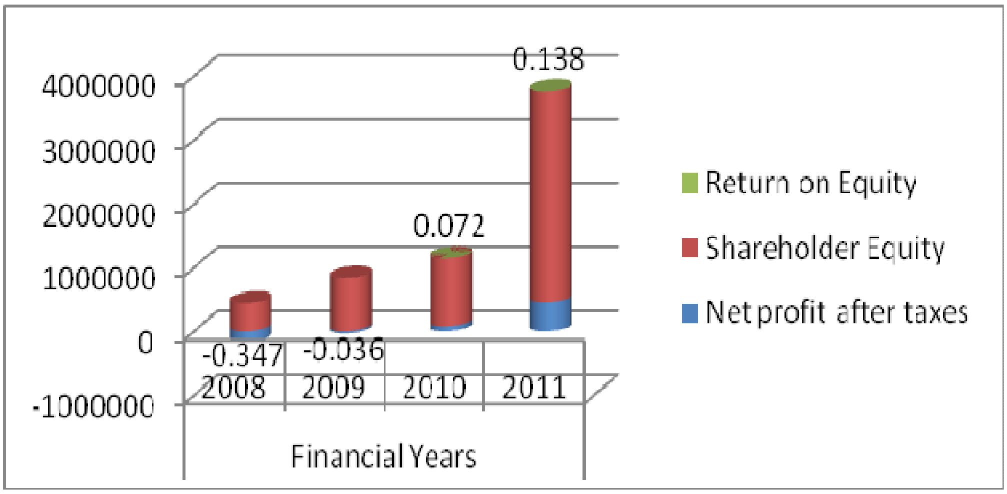
Table 11 Return on Equity

Description	**Financial Years**			
	2008	**2009**	**2010**	**2011**

Net Profit After Taxes	-154708.5	-30007.82	77432.59	457129.18
Shareholder Equity	445291.5	840291.5	1072432.59	3309592.45
Return on Equity	-0.347	-0.036	0.072	0.138

Source: Financial statements of Chechela medical service PLC.

Figure 11 Returns on Equity



Source: Financial statements of Chechela medical service PLC.

The result shows returns on equity ratio are negative for the years 2008 and 2009 (-0.347and -0.036 respectively) and lowest positive ratio for the next two years i.e. 2010 and 2011 (0.072 and 0.138 respectively). From this we can understand the company is at loss in the first two years. Even in the next two year the company's net profit is not promising.

2.15 Financial Resource Administration

From the discussion conducted with the company administrative staffs it was understood that the company used checking systems to control cash out lays and collection and petty cash system for its miscellaneous expenditures. Inventories are purchased following authorization procedure and financial administration techniques. All collections and payments are coded and referenced then journalized in computerized system and physical safeguarding and counting periodically.

However, our findings from interview and focus group discussions show that the company's finance administration strategies are weak. As it was understood from the explanation of the general manager there is no segregation of duties and responsibilities among the staffs where the General Manager Acts as a purchaser.

Moreover, the explanation of the finance manager confirmed that although the job discretion of the cashiers clearly indicates the duties and responsibilities of the cashier some times the accountant of the company accomplish the duties of the cashier. Furthermore, the finding from review of documents and interview shows the company has no cost section in order to evaluate inventory so as to use weighted average method, which is the requirement of Ethiopian tax low.

Besides this, in our observation the company structure is no well organized and developed, from farther discussion and proforma analysis it was confirmed that the company's planning is not based on the past performance. The absence of internal auditor section is another gap identified during the discussion. The financial manual also lack of policies and guidelines in the areas of liquidity management.

CHAPTER FOUR

SUMMARY, CONCLUSIONS AND RECOMMENDATIONS

2.16 Summary

This study focuses on the analysis of financial performance at the Chechela Medical Service PLC. The research has been conducted mainly to know the financial performance, financial resources administration, and strategies at the company. Above all factors financial performance analysis is the most important for the success or failure of the organization.

Chechela Medical Service PLC has been facing a problem of financial performance evaluation. It is obvious that the company performance were unsatisfactory. Realizing this problem, this study's main objective is to analyze and evaluate the financial performance; those findings are summarized as follows:

- The Liquidity ratio of Chechela Medical Service PLC indicates that the current ratio of the company had fewer current assets for every birr of current liabilities in the two years in 2008 and 2011 (0.763 and 1.214 respectively).Whereas in year 2009 and 2010 it is relatively higher i.e.(1.765 and 13.43 respectively). The net working capital ratio also the company cannot cover the current liability because current liability is greater than the working capital in year 2008 the net working capital is negative i.e. -58909.47. However, in the other three years in 2009, 2010 and 2011 the net working capital is positive (162126.91, 579892.30, and 87743.97 respectively). Whereas the quick ratio shows the company's current asset were not sufficient enough after deduction of its inventory for each birr its current liabilities in all years except year 2010 i.e. 1.864, in year 2008, 2009 and 2011 (0.608, 0.903 and 0.484 respectively). To sum up the company liquidity ratio shows less quick asset i.e. large current liability and large holding of the stock.

- The activity ratio indicates that the receivable turnover ratio of year 2008,2009, 2010 and 2011 is zero, it means the company do not have clearly stated credit customer for our evidence. The inventory turnover ratio shows the less efficiency of the management of inventory in year 2008, 2009, and 2010 has zero inventory turnover ratios as compared to year 2011 i.e. 7.866. This shows with in three year the company inventory management was poor. The total asset turnover ratio indicates in the year 2008, (0.080) lower annual sales compared to its utilization of total asset, hence the other three years in 2009, 2010 and 2011 (1.872, 6.445 and 1.467 respectively) shows improve ratio for contribution of each birr of annual sales for each birr of total asset.

- The leverage ratio of the Chechela Medical Service PLC in table 7, the debt to equity and table 8 the debt to total asset ratios shows zero in all four years i.e. year 2008 up to year 2011, it was understood that the owners of the company are not risk taker. Simply they run the business using their own contribution capital.

- The profitability ratios indicate in year 2008, 2009, and 2010 is 1. However, it is less in year 2011 which is .0.576. In relation to sales the company profit margin is not satisfactory to full fill all necessary finance contribution. In relation to investment show positive ratio in years 2010 and 2011 which is 0.124 and 0.123 respectively. But in years 2008 and 2009 it was negative (-0.030 and -0.029 respectively). In general the company’s investment on asset is greater than the return. The return on equity ratio shows negative for the years 2008 and 2009 which is -0.347 and -0.036 respectively. We understood the company is at loss in these two years. Even in the next two years 2010 and 2011 (0.072 and 0.138 respectively) the company’s net profit is not promising.

- In order to obtain the views and comments of the existing staff working at the General Manager and finance and administrations department were selected to discuss. Our findings on interview and focus group discussions evaluation are that the company finance administration strategies are weak. From the explanation of the general manager it was confirmed that there is no segregation of duties and responsibilities among the staffs.

- Moreover, the explanation of the finance manager witnessed that although the job discretion of the cashiers clearly indicates the duties and responsibilities of the cashier some times the accountant of the company accomplish the duties of the cashier. Absence of the cost section and internal audit is another gap of the company as understood during the discussion and document revision.

2.17 Conclusions

The objective of these studies is to analyze and evaluate the financial performance soundness; profitability and efficiency of the business and the financial resources administers under the study. With these areas the researcher used to different ratio analysis and the findings of the study are concluded as follows.

Chechela Medical Service PLC in the four year period 2008 up to 2011 may be interpreted as insufficiently liquid and more of the company shows. From the quick liquidity ratio result it was understood that the company has less quick asset. From this it is possible to conclude that the company has large holding of the inventory stocks which it does not sell. Moreover, an excessive investment in current asset is not an efficient use of funds.

In year 2010 was 1.864 however, better than other three fiscal years, but still the numerical ratio is very less. This implies holding of stock it has to pay its current liabilities, it may find it difficult to meet its obligation. So that, the company should increase availability cash at bank and other cash items and should clearly set credit sales policy to increase its account receivables and should make effective receivables collection policy such as sales terms.

Lower movement of inventories can cause additional costs for safeguarding and storage fees and inventory cost may affect by deletion and inflation situations. Besides to this inventory items are related to medical service, hence inventory may be affected by date of expiration and then fast movement of inventory is important for the company by initiating and treating its customers and making some more additional clients to increase its annual sales volume and by using purchase budget techniques to manage inventory on hand.

As shown in the table 7 and 8 it is clear that in the case of Chechela Medical Service owners have contributed more funds than lenders. It is an indication of the risk averse of a company interim of its long term liquidity or solvency.

Based on the profitability and peroforma ratios Chechela Medical Service exercised a lower profitability ratio and negative gross profit and net sale. From this we can conclude that the company's is not well organized to controlled costs and expenses. In general, the company profit margin is not satisfactory, to full fill all necessary capital and expenditures demands as well as for the finance contribution of the company's future modernization.

The company strategy and procedure for financial administration has some weakness. For example the company has financial resource manual. But it doesn't address all the financial resources requirements in the day to day activities of the company. The financial manual also lack of investment by debt. Moreover, the company does not have policies and guidelines in the areas of liquidity management. There is no segregation of duties and responsibilities

2.18 Recommendations

Based on the findings of the study the following recommendations are made for effective and efficient financial performance analysis of Chechela Medical Service PLC.

- Although net working capital ratio is not a good indicator of the company's performance, as it couldn't measure the liquidity of a firm for trend analysis, the result shows the net working capital of Chechela medical crevice PLC is very low even if it shows positive value in years 2009, 2010 and 2011. Therefore, Chechela medical service should have to have sufficient net working capital in order to be able to meet the claims of the creditors and the day-to-day needs of business.

Hence, the company should raise liquidity ratios or refund its own working capital and should reduce its current liability.

- The lower asset turnover in the year 2008 indicates lower annual sales compared to its utilization of total assets, hence, sales are generated by using asset resources, and each birr of annual sales should shows incremental advantage for each birr of utilized total assets. This can be obtained by increasing annual sales volume using different technique for instance, making advancement of quality of service for customers, using largest laboratory and other medical equipments to give sufficient service for customers, by organizing educated staffs and favorable working areas and clean working environment to satisfy customer quests, by making market research and market development mechanism, these enables to determine manageable service and medicine cost and to share more of market.

- In the leverage ratio analysis shown in table 7 and table 8, even though the finding shows zero numerical values, in year 2008-2011. As ratios indicated the company still not adapted to increase its finance by using short term or long term loans. Therefore, the company should see manageable finance form financing agents, such as banks to in hence its working environment and to penetrate the competitive market share.

- The result shows the company's profit margin is not satisfactory. Hence, the management should see and look for better profit margin; this can be achieved by well organized, open and manageable purchasing systems to reduce purchase related costs, and operating expense. Annual sales should increase using different attractive mechanisms, such as, availability of stocks, quality services for customers, skilled man power, and well organized medical equipments. And also the company has well organizational structure and segregation of duties and responsibilities.

- As it was understood from returns on equity ratio result the company is in loss in the first two years and even the result of the second two years is not satisfactory. However, the long rang survival of business depends on its ability to earn enough revenue to satisfy all obligations and provide a satisfactory return on the investment. Thus the management of the company has the responsibility of maximizing the owner's welfare. Because a potential lender also concerned about the company ability to pay back to loan. Therefore they have to continuously improve the efficiency of the company's operations in view of profits.

- The researcher strongly recommend the management of Chechela Medical Service PLC should perform a complete financial analysis of all aspects of the company financial condition to determine the firm's financial strengths and weaknesses and accordingly takes actions to improve the firm's position. The ratio of the company should compare with the past ratio. This comparison also reveals the firm's strength and weakness. Therefore the company finance manager should continuously improve the financial performance of the firm's operations by evaluation system.

- Chechela Medical Service PLC was no assessment to measure the financial performance. So according to our peroforma analysis the company develops their own liquidity management it helps to control and take a decision on time. Therefore the company should try its best to improve its image.

- We recommend that the case of financial resource administration strategies: the company manages and controls financial resources according to policies and procedure of Chechela Medical Service PLC.

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Appendix

Appendix 1: Summary Company Information

Appendix 2: Projected Peroforma Analysis

Declaration

We the undersigned, declare that this senior essay/project is our original work, prepared under the guidance of Ato Biruk G/Michael. All source of materials used for the manuscript have been duly acknowledged.

Name____________________ Signature ____________________

Name____________________ Signature ____________________

Name____________________ Signature ____________________

Place of Submission______________________

Date of Submission ______________________