Monyetla Project – Accounting Gr 11

Lesson 3: Analysis and Interpretation of Financial Statements

QUESTION 1: SWEET AND SPICY	(25 marks, 20 minutes)

ANALYSIS AND INTERPRETATION

1.1	**The acid test ratio for 2018 is 1,3 : 1. Calculate the missing Inventory figure for 2018.** Acid test ratio = 1,3 : 1 = **X** : 22 520 **X** = 22 520 x 1,3 √ = 29 276 = Debtors control and Cash equivalents Inventory = 52 580 √ – 29 276 ☑ = R23 304 ☑	4
1.2	**Calculate the rate of stock turnover for the year. Use the Inventory amount calculated in question 4.1.** **Cost of sales for 2018 is R720 000.** Rate of stock turnover = Cost of Sales / Average trading stock = 720 000 √ / ½ (23 304 ☑ + 35 700 √) = 720 000 / 29 502 = 24,4 <u>times per year</u> ☑	4
1.3	**"Sweet and Spicy" deals in all kinds of spices, condiments and flavourings for cooking. Comment on the rate of stock turnover.** The rate of stock turnover of 24,4 times show that the stock will be sold out 24,4 times per year, which means twice a month. Therefore, the business will hold stock for about 15 days. √√ This is what you want from a shop selling stock which does not have a long shelf life. It means the products are always fresh. √√	4
1.4	**Calculate the return on average owner's equity for 2018. Is it satisfactory?** Return on owner's equity = Net profit / Average owner's equity = 225 000 √ / ½ (564 300 √ + 588 720 √) x 100/1 = 225 000 / 576 510 x 100/1 = 39% ☑ Yes, they would be satisfied. This return is much higher that what they would earn on alternative investments and therefore is sufficient compensation for the risk and hard work of owning a business. √√	6

1.5	**Calculate the debt/equity ratio for 2018. Is it satisfactory?** Debt/equity ratio = Non-current liabilities : Owner's equity = 125 000 √ : 564 300 √ = 0,2 : 1 ☑ Yes, they should be satisfied. For every R1 the partners have invested, they have borrowed 20 cents. This means that the business is creditworthy and will be able to borrow more money if they need to. √√	5
1.6	**According to the partnership agreement share Sucrose and Curry the remaining profits equally. Explain why the distribution of the net profit between them is not equal.** As the two partners share remaining profits equally, and Curry's interest on capital would have been less than Sucrose, the difference in earnings can only be caused by Curry earning a bigger salary then Sucrose. √√	2

TOTAL MARKS		**25**

Lesson 3: Analysis and Interpretation of Financial Statements

QUESTION 2: KATZ & RABINOWITZ	**(14 marks, 12 minutes)**

RATIO CALCULATIONS AND ANALYSIS

2.1	**Calculate the current ratio on 30 June 2019.** 122 512 √ : 58 344 √ = 2,1 : 1 ☑ one part correct	3
2.2	**Calculate the amount that will appear next to inventory in the Balance Sheet on 30 June 2019, if the Acid test ratio on this date is 0,75 : 1.** Acid test ratio = 0,75 : 1 Current assets – Inventories = 58 344 x 0,75 = R43 758 √ Current assets = 122 512 Thus Inventories = 122 512 √ – 43 758 ☑ = R78 754 ☑ one part correct	4
2.3	**Calculate the actual mark-up achieved on 30 June 2019.** Gross profit = 2 825 550 – 2 093 000 = 732 550 $\frac{732\ 550\ √}{2\ 093\ 000\ √} \times \frac{100}{1}$ = 35% ☑ one part correct	3
2.4	**Give TWO possible reasons why the business operated below the intended mark-up of 40%.** *Any TWO valid reasons* √√ √√ - Regular sales at discount prices took place – seasonal sales. - Too much trade discount was given for buying in bulk. - Cost of sales could have increased due to an increase in prices from suppliers. - Mistakes could have been made in calculating prices. - It can be due to normal stock losses, such as theft and damage. - The business lower the mark-up because of competitors.	4

TOTAL MARKS		**14**

Lesson 2: Asset disposal and Fixed assets

QUESTION 3: NZ TRADERS	**(22 marks, 18 minutes)**

ANALYSIS AND INTERPRETATION

3.1.1	**Calculate the percentage net profit on sales** 152 000 √ / 745 500 √ x 100/1 = 20,4% ☑	3
3.1.2	**Calculate the current ratio** 113 560 √ : 66 800 √ = 1,7 : 1 ☑	3
3.1.3	**Calculate the debt/equity ratio** 94 840 √ : 473 710 √ = 0,2 : 1 ☑	3
3.1.4	**Calculate the percentage return earned by Nkosi on his average equity** 103 000 √ / ½ √ (275 000 + 200 000 – 24 690 + 2 350) √ x 100/1 = 103 000 / 226 330 x 100/1 = 45,5% ☑	4
3.2	**Use the acid-test ratio to calculate the amount of trading stock on hand on 28 February 2017.** Acid test ratio = 0,6 : 1 = **X** : 66 800 **X** = 66 800 x 0,6 √ = 40 080 Thus, Current assets – Inventory = 40 080 Inventories = 113 560 √ – 40 080 ☑ = 73 480 ☑√	5

3.3	**Will partners Nkosi and Zama be satisfied with their returns in 2017? Give a reason for your answer.** Nkosi's return increased from 34,4% to 45,5%. ☑ He will be very satisfied, because his return is very high and much higher than alternative investments. √ Although Zama's return decreased from 33% to 28,2%, it is still better than alternative investments. So she will be satisfied. √√	4

TOTAL MARKS		**22**

Lesson 3: Analysis and Interpretation of Financial Statements

QUESTION 4: PETER AND PAULA	**(53 marks, 43 minutes)**

4.1 GAAP PRINCIPLES [10]

4.1.1	C √√
4.1.2	E √√
4.1.3	B √√
4.1.4	F √√
4.1.5	A √√

10

4.2 ANALYSIS AND INTERPRETATION [43]

4.2.1	**Calculate the mark-up % achieved by the business.** Gross profit = R2 400 000 – R1 600 000 = R800 000 $\frac{\text{Gross profit}}{\text{Cost of sales}} \times \frac{100}{1}$ $= \frac{800\ 000\ \surd}{1\ 600\ 000\ \surd} \times \frac{100}{1}$ = 50% √	3
4.2.2	**Should the owners be happy with the mark-up achieved? Why? Give 2 reasons that could account for the difference.** Reasons: - Too much **trade discount** to loyal customers / **Too much discount x** - Sales at special prices - Miscalculation of selling prices - Theft, errors - Lower the selling price because of competition - Old stock are too long on the shelves and is not part of the sales amount *Any two* √√ √√ No √ The mark-up is less than the 60% desired mark-up. √ **OR** Yes √ By offering trade discount he might have increased his total sales – depends on previous year's sales. √	6

4.2.3	**Calculate the cash and cash equivalents figure if the acid test ratio is 1,6 : 1.** Acid test ratio = 1,6 : 1 = x : 160 000 √ R160 000 x 1,6 = R256 000 √ Thus Debtors + Cash = R256 000 Debtors = R210 000 √ Therefore Cash = R256 000 – R210 000 = R46 000 √	4
4.2.4	**Calculate the current ratio.** Current assets : Current liabilities (420 000 + 256 000) √√ : 160 000 √ = 676 000 : 160 000 = 4,2 : 1 ☑	4

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<tr><td>4.2.5</td><td>

Calculate the stock holding period, debtor's collection period and creditor's payment period in days – use averages in your calculations.

Stock holding period = $\frac{\text{Average stock}}{\text{Cost of sales}} \times \frac{365}{1}$

$= \frac{½(400\,000 + 420\,000)}{1\,600\,000} \times \frac{365}{1}$

$= \frac{410\,000\ √}{1\,600\,000\ √} \times \frac{365}{1}$

= 93,4 / 94 days ☑

Debtor's collection period = $\frac{\text{Average debtors}}{\text{Credit sales}} \times \frac{365}{1}$

$= \frac{½(250\,000 + 210\,000)}{80/100 \times 2\,400\,000} \times \frac{365}{1}$

$= \frac{230\,000\ √}{1\,920\,000\ √} \times \frac{365}{1}$

= 43,7 / 44 days ☑

Creditor's payment period = $\frac{\text{Average creditors}}{\text{Credit purchases}} \times \frac{365}{1}$

$= \frac{½(140\,000 + 160\,000)}{90/100 \times 1\,600\,000} \times \frac{365}{1}$

$= \frac{150\,000\ √}{1\,440\,000\ √} \times \frac{365}{1}$

= 38 days ☑

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<tr><td>4.2.6</td><td>

Is the business exercising good liquidity control? Use your calculations in question 4.2.5 to answer the question.

No √ **OR** Yes – the reasons must fit the yes.

- Holding stock for 94 days, which is 3 months – this prevents the business from buying and selling new stock. Old/obsolete stock can easily be damaged or stolen.
- Debtors are not paying within the credit term of 30 days – charge interest on overdue accounts to make sure that you receive the money in time.
- Creditors are being paid before the terms of 45 days. Use the full credit term.
- The business can experience cash flow problems because the creditors are being paid before money are received from debtors.

Any three explanations according to Yes/No √√ √√ √√

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4.2.7	**Calculate the ratio of the final profit sharing between the partners.** 15 000 : 35 000 = 3 : 7 √√	2
4.2.8	**Calculate the return on average owner's equity earned by the business.** $\frac{\text{Net profit}}{\text{Average owner's equity}} \times \frac{100}{1}$ $= \frac{87\,000 + 113\,750 \ \surd\surd}{½([100\,000 + 120\,000 + 140\,000 + 110\,000] \surd + [10\,000 - 5\,000 + 85\,000 + 94\,750] \surd)} \times \frac{100}{1}$ $= \frac{200\,750}{327\,375} \times \frac{100}{1}$ = 61,3% ☑	5
4.2.9	**Do you think the partners should be happy with this return? Motivate your answer.** Yes √ The return is way above current interest rates on alternative investments. √√ **OR** *No* √ *The partners must consider that their salaries are included in this calculation. They might be able to earn a higher salary working for another business.* √√	3

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TOTAL MARKS		**53**