Cambridge

AS - Level

Business studies

CODE: (9609)

Unit 05- Chapter 30

Accounting fundamentals

Introduction

Accounts are monetary records of transactions, essential for businesses to track purchases, sales, and other financial transactions. They help identify spending habits and budgeting decisions. Without accounting records, businesses face problems and stakeholder groups need accounting information. Accounts provide essential information to both internal and external groups, ensuring that businesses are operating efficiently and effectively.

Management and financial accounting

There are several different branches of accounting. Two of the most important types of accountants are financial and management accountants. In general terms, the work of financial accountants is to prepare the published accounts of a business in keeping with legal requirements

Foundations of accounting – accounting concepts and conventions

It is important for accountants all over the world to base business accounts on the same basic principles. If they did not do this, it would never be possible to compare accounts from companies based in different countries. It would also cause huge problems for multinational companies if some of their accounts based on activities in foreign countries were recorded using different concepts and conventions to those in the home country.

The double-entry principle

Every time a business engages in a transaction, for example buying materials or selling goods to a customer, there are two sides to the transaction. Th is means that the accounts of the business must include it twice to ensure that the accounts balance.

Accruals

Accruals arise when services have been supplied to a business but have not yet been paid for at the time the accounts are drawn up, such as an electricity bill. If no adjustment was made for this accrued expense, then the profits in the current accounting period will be overstated.

The money-measurement principle

Accountants need a common form of measuring the wealth and performance of the businesses they work for. All accounting data are converted into money – hence the principle of money measurement. Only items and transactions that can be measured in monetary terms are recorded in a business's account books and not, for example, the skills and experience of the company's directors.

Conservatism – also known as the prudence concept

Accountants are trained to be realistic about the values used in accounts. Th e conservatism principle states that accountants should provide for and record losses as soon as they are anticipated. Profits, on the other hand, should not be recorded until they have been 'realised' – that is, until it is certain that goods or services have been sold at a profit.

The realisation concept

T h e realisation concept states that all revenues and profits should be recorded in the accounts 'when the legal title to the goods is transferred'. Th is means when the customer is legally bound to pay for them, unless they can be proven to be faulty. So sales are not recorded when an order is taken or when payment is actually made – but when the goods or services have been provided to the customer.

Recent changes – International Financial Reporting Standards (IFRS)

T h e IFRS aims to ensure that accounts produced by companies all over the world conform to similar terminology and layout. This is to try to avoid confusion when analysing accounts from companies based in diff erent countries. Recently, many changes to the names of the main accounts, the layout of them and the terminology to be used in them have been made by IFRS.

The income statement – what it shows about a business

T h is account used to be known as the profit and loss account. In old examination papers or company accounts drawn up some years ago, this term may be used.

KEY TERM

Income statement: records the revenue, costs and profit (or loss) of a business over a given period of time.

The account	What it shows
Income statement (formerly known as profit and loss account)	The gross and operating profit of the company. Details of how the operating profit is split up (or appropriated) between dividends to shareholders and retained earnings (profit).
Statement of financial position (formerly known as the balance sheet)	The net worth or equity of the company. This is the difference between the value of what a company owns (assets) and what it owes (liabilities).
Cash-flow statement	Where cash was received from and what it was spent on.

Table 30.3 Final accounts of limited companies – what they contain

■ A detailed income statement is usually produced for internal use because managers will need as much information as possible. It may be produced as frequently as managers need the information – perhaps once a month.

■ A less-detailed summary will appear in the published accounts of companies for external users. It will be produced less frequently, but at least once a year. The content of this is laid down by the Companies Acts and provides a minimum of information.

The sections of an income statement

Income statements have three sections. Each one gives a different total profit figure.

The trading account

This shows how **gross profit** (or loss) has been made from the trading activities of the business. It is most important to understand that, as not all sales are for cash in most businesses, the **revenue** figure is not the same as cash received by the business

	Revenue	3,060	
(minus)	Cost of sales	(1,840)	Trading account
(equals)	Gross profit	1,220	
(minus)	Overheads/expenses	(580)	Profit and loss section
(equals)	Operating profit (formerly net profit)	640	
(minus)	Interest	(80)	
(equals)	Profit before tax	560	
(minus)	Tax @ 20%	(112)	
(equals)	Profit for the year	448	
(minus)	Dividends to shareholders	200	Appropriation account
(equals)	Retained earnings	248	

Table 30.4 Income statement for Energen plc for the year ended 29 March 2013

Only the goods used and sold during the year will be recorded in cost of sales.

T h e formula used is: cost of sales = opening stocks plus purchases minus closing stocks

KEY TERMS

Gross profit: equal to sales revenue less cost of sales.

Revenue (formerly called sales turnover): the total value of sales made during the trading period = selling price × quantity sold.

Profit and loss account section

T h is section of the income statement calculates both the operating profit (or profit before interest and tax) and the profit for the year (profit aft er tax) of the business.

Appropriation account

T h is final section of the income statement (which is contained in the IFRS 'statement of comprehensive income') shows how the profit for the year of the company is distributed between the owners – in the form of **dividends** to company shareholders – and as **retained earnings** or profit.

KEY TERMS

Operating profit (formerly referred to as net profit): gross profit minus overhead expenses.

Profit for the year (profit after tax): operating profit minus interest costs and corporation tax.

KEY TERMS

Dividends: the share of the profits paid to shareholders as a return for investing in the company.

Retained earnings (profit): the profit left after all deductions, including dividends, have been made, this is 'ploughed back' into the company as a source of finance.

The uses of income statements

T h e information contained in income statements can be used in a number of ways:

■ It can be used to measure and compare the performance of a business over time or with other firms – and ratios can be used to help with this form of analysis

■ The actual profit data can be compared with the expected profit levels of the business.

■ Bankers and creditors of the business will need the information to help decide whether to lend money to the business.

■ Prospective investors may assess the value of putting money into a business from the level of profit being made.

A high profit figure resulting from the sale of a valuable asset for more than its expected value might not be repeatable and is, therefore, said to be **low-quality profit.**

High-quality profits because these are likely to be a continuous source of profit for some time to come.

KEY TERMS

Low-quality profit: one-off profit that cannot easily be repeated or sustained.

High-quality profit: profit that can be repeated and sustained.

The Statement of financial position – what it shows about a business

The **Statement of financial position** is still sometimes referred to as the balance sheet but IFRS rules led to a name-change for this important account.

Th e aim of most businesses is to increase the **shareholders' equity** by raising the value of the businesses assets more than any increase in the value of **liabilities**. Shareholders' equity comes from two main sources:

■ The first and original source was the capital originally invested in the company through the purchase of shares. This is called **share capital.**

■ The second source is the retained earnings of the company accumulated over time through its operations. These are sometimes referred to as reserves, which is rather misleading as they do not represent reserves of cash.

Points to note:

■ Companies have to publish the income statement and the Statement of financial position for the previous financial year as well in order to allow easy comparison. These have not been included in the above examples for reasons of clarity.

■ The titles of both accounts are very important as they identify both the account and the company.

■ Whereas the income statement covers the whole financial year, the Statement of financial position is a statement of the estimated value of the company at one moment in time – the end of the financial year.

Non-current or fixed assets

Th e most common examples of fixed assets are land, buildings, vehicles and machinery. These are all tangible assets as they have a physical existence. Businesses can also own intangible assets – these cannot be seen but still have value in the business.

Th ese items make up what is known as the '**intellectual property'** of the business. They can give a business a greater market value than the total value of its tangible assets less its liabilities. Th ese intangible assets can be very important for an IT-based or knowledge-based business.

Th e reputation and prestige of a business that has been operating for some time also give value to the business over and above the value of its physical assets. This is called the **goodwill** of a business and should normally only feature on a Statement of financial position just aft er it has been purchased for more than its assets are worth, or when the business is being prepared for sale.

Current assets

T h ese are very important to a business, as will be seen when liquidity is assessed later in this chapter. Th e most common examples are inventories, trade receivables (debtors who have bought goods on credit) and cash/bank balance.

KEY TERMS

Statement of financial position (balance sheet): an accounting statement that records the values of a business's assets, liabilities and shareholders' equity at one point in time.

Shareholders' equity: total value of assets – total value of liabilities.

Asset: an item of monetary value that is owned by a business.

Liability: a financial obligation of a business that it is required to pay in the future.

Share capital: the total value of capital raised from shareholders by the issue of shares.

KEY TERMS

Non-current assets: assets to be kept and used by the business for more than one year. Used to be referred to as 'fixed assets'.

Intangible assets: items of value that do not have a physical presence, such as patents, trademarks and current assets.

Current assets: assets that are likely to be turned into cash before the next balance-sheet date.

Inventories: stocks held by the business in the form of materials, work in progress and finished goods.

Trade receivables (debtors): the value of payments to be received from customers who have bought goods on credit.

Current liabilities: debts of the business that will usually have to be paid within one year.

Accounts payable (creditors): value of debts for goods bought on credit payable to suppliers; also known as 'trade payables'.

Non-current liabilities: value of debts of the business that will be payable after more than one year.

KEY TERMS

Intellectual capital or property: the amount by which the market value of a firm exceeds its tangible assets less liabilities – an intangible asset.

Goodwill: arises when a business is valued at or sold for more than the balance-sheet value of its assets.

Current liabilities

Typical current liabilities include accounts payable (suppliers who have allowed the business credit), bank overdraft and unpaid dividends and tax

	$m	$m	Notes
ASSETS			
Non-current (fixed) assets:			
Property	300		
Vehicles	45		
Equipment	67		
Intangible assets	30		
	442		
Current assets:			
Inventories	34		
Trade receivables (formerly debtors)	28		
Cash	4		Also called 'cash and cash equivalents'.
	66		
TOTAL ASSETS		508	This total will balance with equity and liabilities – hence the original term 'balance sheet'.
EQUITY AND LIABILITIES			
Current liabilities:			
Accounts payable (or creditors)	42		
Short-term loans	31		These loans will include the company's overdraft with the bank. Other current liabilities might include provisions to pay tax and dividends.
	73		
Non-current liabilities:			These used to be referred to as 'long-term liabilities'.
Long-term loans	125		Other non-current liabilities might include debentures issued by the company.
	125		
TOTAL LIABILITIES	198		If these actually equalled total assets, there would be no shareholders' equity in the company at all.
Shareholders' equity:			
Share capital	200		
Retained earnings reserve	110		The cumulative value of the company's annual 'retained earnings/ profits'.
	310		
TOTAL EQUITY AND LIABILITIES		508	This does balance with total assets!

Table 30.5 Example of a Statement of financial position with some explanatory notes

Working capital

You will recall this concept from Chapter 28 and it can be calculated from the Statement of fi nancial position by the formula: current assets – current liabilities. It can also be referred to as net current assets.

Shareholders' equity

Shareholders' funds, also known as shares, represent the capital paid into a business when shareholders bought shares. They are also known as reserves, which represent retained earnings or profits that shareholders have accepted should be kept in the business. These reserves can appear on the financial position statement if a company believes its fixed assets have increased in value or sells additional shares for more than their nominal value.

Non-current liabilities (long-term liabilities)

T h ese are the long-term loans owed by the business. These are due to be paid over a period of time greater than one year and include loans, commercial mortgages and debentures.

Other information in published accounts

Apart from the three main accounting statements, other information is required by law to be included in company published accounts. Some of the most important sections are:

1 The cash-flow statement

This is the third and final main account published in the annual report and accounts. As its name suggests, it focuses not on profit or net worth but on how the company's cash position has changed over the past year.

> **KEY TERM**
>
> **Cash-flow statement:** record of the cash received by a business over a period of time and the cash outflows from the business.

2 The Chairman's Statement

This is a general report on the major achievements of the company over the past year, the future prospects of the business and how the political and economic environment might affect the company's prospects.

3 The Chief Executive's Report

This is a more detailed analysis of the last financial year, often broken down by area of main product divisions. Major new projects will be explained and any closures or rationalisation that occurred will also be briefly referred to.

4 The Auditors' Report

This is the report by an independent fi rm of accountants on the accuracy of the accounts and the validity of the accounting methods used. If there are no problems with the accounts, the auditors will state that the accounts give a 'true and fair view' of the business's performance and current position.

5 Notes to the accounts

T h e main accounts contain only the basic information needed to assess the position of the company. Th ey do not contain precise details, such as the types of individual fixed assets, the main long-term loans or the depreciation methods used. Th ese and other details are contained at the end of the annual report and accounts in the 'notes to the accounts'.

Introduction to accounting ratio analysis

How much can we tell about a company's performance by studying the published accounts? It is easy to compare one year's profit figure with the previous year. Changes in sales revenue can also be identified – so too can differences from one year to the next in current assets, current liabilities and shareholders' equity. Similar comparisons can be made between different companies too.
However, in making these comparisons, one essential problem arises. Look, for example, at these company results from two printing fi rms:

	2013 Operating profit ($000)
Nairobi Press Ltd	50
Port Louis Press Ltd	500

The performance of Port Louis Press and Nairobi Press is unclear from the given information. While Port Louis Press made an operating profit ten times greater than Nairobi Press, the managers of Nairobi Press may not be more effective, and their strategies may not be more successful.

Now look at other information about these two businesses:

	2013 Revenue ($000)
Nairobi Press Ltd	250
Port Louis Press Ltd	3,200

Accountants make this assessment by relating two accounting results to each other in the form of a ratio. T h ese ratios are grouped into five main groups, but at AS Level only two of these groups of ratios are studied:

1 Profitability ratios: These include the profit margin ratios, which compare the profits of the business with revenue (AS Level), and the return on capital employed ratio, which compares operating profit with capital employed in the business (A Level).

2 Liquidity ratios: These give a measure of how easily a business could meet its short-term debts or liabilities.

Profit margin ratios

These are used to assess how successful the management of a business has been at converting sales revenue into both gross profit and operating profit.

	Gross profit $000	Revenue $000	Gross profit margin
Nairobi Press Ltd	125	250	$\frac{125}{250} \times 100 = 50\%$
Port Louis Press Ltd	800	3,200	$\frac{800}{3,200} \times 100 = 25\%$

Points to note: Port Louis Press's gross profit margin may be lower due to its low-price strategy or higher sales costs, possibly due to higher material or direct labor costs. To increase it, it could reduce sales costs while maintaining revenue, or increase revenue without increasing sales costs.

KEY TERM

Gross profit margin: This ratio compares gross profit (profit before deduction of overheads) with revenue.

$$\text{gross profit margin \%} = \frac{\text{gross profit}}{\text{revenue}} \times 100$$

The gross profit margin is a good indicator of how effectively managers have 'added value' to the cost of sales.

Using the same two businesses (all figures for 2013):

	Operating profit $000	Revenue $000	Operating profit margin
Nairobi Press Ltd	50	250	$\frac{50}{250} \times 100 = 20\%$
Port Louis Press Ltd	500	3,200	$\frac{500}{3,200} \times 100 - 15.6\%$

Points to note: The profitability gap between these two businesses has narrowed. Whereas the difference in gross profit margins was substantial, the **operating profit margins** are much more alike.

KEY TERM

Operating profit margin: This ratio compares operating profit (formerly this ratio was referred to as the net profit margin) revenue.

$$\text{operating profit margin \%} = \frac{\text{operating profit}}{\text{revenue}} \times 100$$

Liquidity ratios

Th ese ratios assess the ability of the fi rm to pay its short term debts. They are an important measure of the short term financial health of a business. They are not concerned with profits, but with the working capital of the business.

KEY TERM

Liquidity: the ability of a firm to pay its short-term debts.

Current ratio

Th is compares the current assets with the current liabilities of the business

KEY TERM

$$\textbf{Current ratio} = \frac{\text{current assets}}{\text{current liabilities}}$$

A firm's liquidity can be measured using a ratio or number, but no universally reliable result exists. Accountants recommend a 1.5-2 result, depending on industry and recent current ratio trends. A higher result may indicate concern.

All figures as at 31 December 2013 ($000)			
	Current assets	Current liabilities	Current ratio
Nairobi Press Ltd	60	30	$\frac{60}{30} = 2$
Port Louis Press Ltd	240	240	$\frac{240}{240} = 1$

Method to increase profit margins	Examples	Evaluation of method
Increase gross and operating profit margin by reducing direct costs	**1** Using cheaper materials, e.g. rubber not leather soles on shoes. **2** Cutting labour costs, e.g. relocating production to low-labour-cost countries, such as Dyson making vacuum cleaners in Malaysia. **3** Cutting labour costs by increasing productivity through automation, e.g. Hyundai's production line uses some of the most labour-saving robots in the world. **4** Cutting wage costs by reducing workers' pay.	**1** Consumers' perception of quality may be damaged and this could hit the product's reputation. Consumers may expect lower prices, which may cut the gross profit margin. **2** Quality may be at risk; communication problems with distant factories. **3** Purchasing machinery will increase overhead costs (gross profit could rise but operating profit fall), remaining staff will need retraining – short-term profits may be cut. **4** Motivation levels might fall, which could reduce productivity and quality.
Increase gross and operating profit margin by increasing price	**1** Raising the price of the product with no significant increase in variable costs, e.g. Mauritius Telecom raising the price of its broadband connections. **2** Petrol companies increasing prices by more than the price of oil has risen.	**1** Total profit could fall if too many consumers switch to competitors – this links to price elasticity. **2** Consumers may consider this to be a 'profiteering' decision and the long-term image of the business may be damaged.
Increase operating profit margin by reducing overhead costs	Cutting overhead costs, such as rent, promotion costs or management costs but maintaining sales levels, for example: **1** Moving to a cheaper head office location. **2** Reducing promotion costs. **3** Delayering the organisation.	**1** Lower rental costs could mean moving to a cheaper area, which could damage image. **2** Cutting promotion costs could lead to sales falling by more than fixed costs. **3** Fewer managers – or lower salaries – could reduce the efficient operation of the business.

Table 30.6 Evaluation of ways to increase profit margins

Points to note

Nairobi Press has a more liquid position with twice as many current assets as current liabilities, ensuring it can pay for $1 of short-term debts. Port Louis Press has a more worrying current ratio of $1 for each $1 of short-term debt, potentially causing trouble if all short-term creditors demand repayment simultaneously. Low current ratios may indicate a lack of proper management, such as selling redundant assets, cancelling capital spending plans, and taking long-term loans, which could lead to increased cash holding.

Acid-test ratio

Also known as the quick ratio, this is a stricter test of a fi rm's liquidity. It ignores the least liquid of the fi rm's current assets – inventories (stocks). Inventories, by definition, have not yet been sold and there can be no certainty that they will be sold in the short term.

KEY TERMS

Acid-test ratio: $\frac{\text{liquid assest}}{\text{current liabilities}}$

Liquid assets: current assets – inventories (stocks) = liquid assets.

All figures as at 31/12/13 ($000)	Liquid assets	Current liabilities	Acid-test ratio
Nairobi Press Ltd	30	30	1
Port Louis Press Ltd	180	240	0.75

Points to note:

■ Results below 1 are oft en viewed with caution by accountants as they mean that the business has less than $1 of liquid assets to pay each $1 of short-term debt. Therefore, Port Louis Press may well have a liquidity problem. 456

■ The full picture needs to be gained by looking at previous years' results.

■ Firms with very high inventory levels will record very different current and acid-test ratios. This is not a problem if inventory levels are always high for this type of business, such as a furniture retailer. It would be a cause for concern for other types of businesses, such as computer manufacturers, where stocks lose value rapidly due to technological changes.

■ Whereas selling inventories for cash will not improve the current ratio – both items are included in current assets – this policy will improve the acid-test ratio as cash is a liquid asset but inventories are not

Limitations of ratio analysis

T h e benefits of using ratio analysis for investigating fi rms' profitability and liquidity have been explained. Th ere are some limitations to using these ratios – especially if not combined with other data – to assess business performance in these important areas, however:

1 The four ratios studied give an incomplete analysis of a company's financial position.

2 One ratio result on its own is of very limited value – it needs to be compared with results from other similar businesses and with results from previous years to be more informative.

3 Comparing results with those of other businesses should be done with caution. Different businesses may have slightly different ways of valuing assets and some accounts may have been window-dressed.

4 Poor ratio results only highlight a potential business problem – they cannot by themselves analyse the cause of it or suggest potential solutions to the problem.

5 As noted earlier in the chapter, financial statements can only measure quantitative performance and this is true of the ratios based on them. Other information of a qualitative nature is necessary before the full picture of a company's position and performance can be fully judged.

Internal and external users of accounting information

It is usual to divide the users of accounting information into internal and external users

Method to increase liquidity	Examples	Evaluation of method
Sell off fixed assets for cash – could lease these back if still needed by the business	■ Land and property could be sold to a leasing company.	■ If assets are sold quickly, they might not raise their true value. ■ If assets are still needed by the business, then leasing charges will add to overheads and reduce operating profit margin.
Sell off inventories for cash (note: this will improve the acid-test ratio, but not the current ratio)	■ Stocks of finished goods could be sold off at a discount to raise cash. ■ JIT stock management will achieve this objective.	■ This will reduce the gross profit margin if inventories are sold at a discount. ■ Consumers may doubt the image of the brand if inventories are sold off cheaply. ■ Inventories might be needed to meet changing customer demand levels – JIT might be difficult to adopt in some industries.
Increase loans to inject cash into the business and increase working capital	■ Long-term loans could be taken out if the bank is confident of the company's prospects.	■ These will increase the gearing ratio (see Chapter 35). ■ These will increase interest costs.

Table 30.7 Evaluation of ways to increase liquidity

Business managers:

■ to measure the performance of the business to compare against targets, previous time periods and competitors

■ to help them take decisions, such as new investments, closing branches and launching new products

■ to control and monitor the operation of each department and division of the business

■ to set targets or budgets for the future and review these against actual performance.

Banks:

■ to decide whether to lend money to the business

■ to assess whether to allow an increase in overdraft facilities

■ to decide whether to continue an overdraft facility or a loan.

Creditors, such as suppliers:

■ to see if the business is secure and liquid enough to pay off its debts

■ to assess whether the business is a good credit risk

■ to decide whether to press for early repayment of outstanding debts.

Customers:

■ to assess whether the business is secure

■ to determine whether they will be assured of future supplies of the goods they are purchasing

■ to establish whether there will be security of spare parts and service facilities.

Government and tax authorities:

■ to calculate how much tax is due from the business

■ to determine whether the business is likely to expand and create more jobs and be of increasing importance to the country's economy

■ to assess whether the business is in danger of closing down, creating economic problems

■ to confirm that the business is staying within the law in terms of accounting regulations.

Investors, such as shareholders in the company:

■ to assess the value of the business and their investment in it

■ to establish whether the business is becoming more or less profitable

■ to determine what share of the profits investors are receiving

■ to decide whether the business has potential for growth

■ if they are potential investors, to compare these details with those from other businesses before making a decision to buy shares in a company

■ if they are actual investors, to decide whether to consider selling all or part of their holding.

Workforce:

■ to assess whether the business is secure enough to pay wages and salaries

■ to determine whether the business is likely to expand or be reduced in size

■ to determine whether jobs are secure

■ to find out whether, if profits are rising, a wage increase can be afforded

■ to find out how the average wage in the business compares with the salaries of directors.

Local community:

■ to see if the business is profitable and likely to expand, which could be good for the local economy

■ to determine whether the business is making losses and whether this could lead to closure

Limitations of published accounts

What they do not contain

Business published accounts are useful for stakeholders, but they only provide the minimum required accounting information as per company law. Companies like sole traders may not disclose information to the public, but may provide accounts to bankers and tax authorities. Obtaining a copy of a public limited company's published accounts helps determine legal disclosure requirements and exemptions.

■ details of the sales and profitability of each good or service produced by the company and of each division or department

■ the research and development plans of the business and proposed new products

■ the precise future plans for expansion or rationalisation of the business

■ the performance of each department or division

■ evidence of the company's impact on the environment and the local community – although this social and environmental audit is sometimes included voluntarily by companies

■ future budgets or financial plans.

Are the published accounts really accurate?

Stakeholders often worry about the accuracy of published accounts, as accounting is not as objective as some may believe. Companies cannot publish accounts that they know to be deliberately and illegally misleading, as they are checked by auditors. However, accounting decisions are not always based on exact science, and there are instances where accountants may use judgement and estimates to present accounts in a favorable way. This could lead to accusations of 'window-dressing' the accounts, which could influence banks to lend more money or encourage investors to buy shares. Common ways of window-dressing include selling assets, reducing depreciation, ignoring bad debts, giving stock levels a higher value, and delaying bills or incurring expenses. Therefore, published accounts should be used with caution and not all stakeholders want answers to.

KEY TERM

Window-dressing: presenting the company accounts in a favourable light – to flatter the business performance.

Revision questions

Q1 Case Study 141: Clothing Line (CL) 9609/22/O/N/18/Q1 (c)
Refer to Fig 1. Calculate the current ratio as at 31 December 2017. [2]

Q2: Case Study 9: (Mat pack Packaging pick) 9707/02/M/J/05/Q1 (c)
(i) Calculate the forecast net profit for 2006 if the new product is introduced. [2]
(ii) Calculate the net profit margin if the product is introduced. [2]
(iii) How might john use the result in (ii). [2]

Q3: Case Study 145: Jim's Farm (JF) 9609/22/F/M/19/Q1 (a) (ii)
(i) Calculate JF's forecast gross profit margin for option 1. [3]
(ii) Explain one reason why JF might aim for a high gross profit margin. [3]

Q4: Case Study 148: Planet Internet (PI) 9609/21/M/J/19/Q2 (a) (ii)
Refer to table 2.1. Evaluate the financial performance of PI compared to its competitors. [3]

Q5: Case Study 27: (Medlqulp) 9707/21/O/N/09/Q1 (c)
(i) Calculate the current ratio for 2009. [2]

(ii) The current ratio for 2008 was much higher. Briefly comment on the significance to MQ of the change in the current ratio. [2]

(iii) With reference to the data provided by the finance director, briefly explain one reason for the change in the current ratio. [2]

Q6: Case study 29: (phone quip) 9707/22/O/N/09/Q1 (b)
(i) Calculate the acid test ratio for 2009. [2]

(ii) The acid test ratio for 2008 was 1.5. Briefly comment on the significance to PQ of the change in the acid test ratio. [2]

(iii) With reference to the data provided by the finance director in table 1, briefly explain one reason for the change in the acid test ratio. [2]

Q7: Case Study 36: (Vegetables Soup) 9707/23/M/J/10/Q2 (a)
Calculate the annual revenue per member for EGC (Y in table 2). [2]

Q8: Case Study 62: Best move partnership (BM) 9707/21/O/N/12/Q2 (a) (i)
Refer to table 1. Calculate the net profit margin for the first year. [2]

Q9: Case Study 63: Burbank (BB) 9707/22/O/N/12/Q1 (c)
Calculate the forecast net profit for BB for year 2. Use table 1 in your answer. [2]

Q10: Case Study 106: Prestige Jeweler (P J) 9609/21/M/J/16/Q2 (a) (ii)
Define the term ‘income statement’ (line 13). [2]

Q11: Case Study 115: Exam Success (ES) 9609/23/O/N/16/Q1 (c)
Refer to Fig. 1 and other information on the lines 10-11. Calculate the forecast revenue for year 6. [2]

Q12: Case Study 118: Clean and Tidy (CT) 9609/22/F/M/17/Q2 (b) (ii)
Define the term ‘profit margin’ (line 5). [2]

Q13: Case Study 151: (First Nature) 9609/22/M/J/19/Q1 (a) (ii)
(i) Refer to table 1.1. Calculate the value of X in quarter 4. [2]
(ii) Explain two benefits to FN of cash flow forecasting. [4]

Q14: Case Study 4: The Akshay Company (TAC) 9707/02/O/N/03/Q2 (b)
(i) Calculate the return on capital employed for 2002. [2]
(ii) Using your answer to (c) (i) and other data, analyze the performance of the business between 1999 and 2002. [6]

Q15: Case Study 12: (The Sun Hotel Ltd) 9707/02/O/N/05/Q2 (a) (i)
(i) Calculate the current ratio. [4]
(ii) Briefly explain the significance of your result. [2]

Q16: Case study 5: (candy shows Ltd) 9707/02/M/J/04/Q1 (b)
Define the following term: sales revenue (line 6). [3]

Q17: Case Study 5: (Candy Shows Ltd) 9707/02/M/J/04/Q1 (d)
(i) Using information from text and table 1, calculate the forecast profit for a large event. [5]
(ii) Comment on your result. [3]

Q18: Case study 8: (Rite on clothes Ltd)
(i) Using the figures from table 1, calculate the missing value of X in table 2. [3]
(ii) Using your answer to (b)(i) and other information, comment on trends in ER’s profits. [3]

Q19: Case Study 3: (Round Pick) 9707/02/O/N/03/Q1 (a) (ii)
(i) Capital employed is $40 million for both years. Calculate return on capital employed for both 2002 and 2003. [3]
(ii) Briefly comment on your result. [3]

Q20: Case Study 28: (Joe’s world) 9707/21/O/N/09/Q2 (d)
Explain the following terms: profit margin. [3]

Q21: Case Study 28: (Joe’s world) 9707/21/O/N/09/Q2 (d)
(i) Calculate the price that CA would have to charge business customers to achieve the same operating profit per flight as for low cost flights. [3]
(ii) Briefly comment on your answer to (b)(i). [3]

Q22: Case Study 28: (Joe's world) 9707/21/O/N/09/Q2 (d)
Explain the following terms: net profit. [3]

Q23: Case Study 33: (Sassy Suits) 9707/22/M/J/10/Q1 (c)
(i) Calculate the net profit margin for SS in 2010. [3]
(ii) The net profit margin for ss in 2008 was 50% and for 2009 was 33%. Using table 1 and your answer to part (i), briefly comment on the trend in net profit margin for SS. [3]

Q24: Case Study 39: (Big Boxes) 9707/22/O/N/10/Q1 (a) (ii)
(i) Calculate the forecast gross profit margin for 2011. [3]
(ii) The gross profit margin for 2010 is 50%. Using table 1 and your answer to part (i), comment on the trend in gross profit margin. [3]

Q25: Case Study 45, Case Study 37: (Big Bags) 9707/21/O/N/10/Q1 (b)
(i)Calculate the forecast gross profit margin for 2011. [3]
(ii)The gross profit margin for 2010 is 50%. Using table 1 and your answer to part (i), comment in the trend in gross profit margin. [3]

Q26: Case Study 47: Quality Coaches (QC) 9707/23/M/J/11/Q1 (c)
Explain the following terms: retained profit. [3]

Q27: Case Study 31: (Taylor's Tables) 9707/21/M/J/10/Q1 (a) (i)
(i) Calculate the return on capital employed (ROCE) for TT in 2010. [3]
(ii) The ROCE for 2008 was 12% and for 2009 was 10%. Using your answer to part (i) briefly comment on the trend in ROCE. [3]

Q28: Case Study 35: (Classy Clocks) 9707/23/M/J/10/Q1 (c)
(i) Calculate the gross profit margin for CC IN 2010. [3]
(ii) The gross profit margin for CC in 2008 was 40% and for 2009 was 30%. Using your answer to part (i) and table 1 briefly comment on the trend in gross profit margin for CC. [3]

Q29: Case study 45: Turbo tractors (TT) 9707/22/M/J/11/Q1 (a) (ii)
Explain the following terms: cost of goods sold. [3]

Q30: Case Study 45: Turbo Tractors (TT) 9707/22/M/J/11/Q1 (d)
Explain the following terms: revenue (sales turnover). [3]

Q31: Case Study 43: Loader Lorries (LL) 9707/21/M/J/11/Q1 (a) (i)
(i) Using the information in table 1, calculate LL's gross profit margin for 2010. [3]
(ii) The gross profit margin for 2009 was 70. Using table 1, comment on the usefulness of the gross profit margin figures to the management of LL. [3]

Q32: Case Study 45: Turbo Tractors (TT) 9707/22/M/J/11/Q1 (d)
(i) Using the information in table 1, calculate the net profit margin for TT in 2011. [3]

(ii) The net profit margin in 2009 was 40% and in 2010 it was 25%. Briefly comment on the trend in the net profit margin. [3]

Q33: Case Study 47: Quality Coaches (QC) 9707/23/M/J/11/Q1 (c)
(i) The net profit margin for 2010 was 20%. Using this information and the data in table 1, calculate the revenue (sales turnover) in 2010. [3]
(ii) Using your calculation in (i), comment on the trends shown in Table 1. [3]

Q34: Case Study 48: Eldorado Gold (EG) 9707/23/M/J/11/Q2 (a) (ii)
(i) Using the information in table 3, calculate the value of X (the sales gold for 2016). [2]
(ii) Comment on the usefulness to EG of this cash flow forecast. [6]

Q35: Case Study 52: (Rex Cinema) 9707/22/O/N/11/Q2 (c)
Explain the following term: profit before tax (net profits). [3]

Q36: Case Study 52: (Rex Cinema) 9707/22/O/N/11/Q2 (c)
Explain the following terms: profits. [3]

Q37: Case Study 55: Advanced Control System (ACS) 9707/21/M/J/12/Q1 (a) (i)
(i) Calculate the current ratio with the contract (X in table 1). [3]
(ii) Briefly comment on the impact on ACS's financial situation if ACS gets the contract. Use information in table 1 and your answer to (b) (i). [5]

Q38: Case Study 68: Bright Glass (BG) 9707/21/M/J/13/Q2 (c)
(i) Calculate BG's current ratio for May 2013. [3]
(ii) BG's current ratio for 2012 was 1.5. Comment on the change in BG's liquidity. [3]

Q39: Case Study 73: Clare's Clothes (CC) 9707/21/O/N/13/Q1 (a) (i)
(i) Refer to table 2. Calculate the current ratio. [3]
(ii) Using your answer from (b)(i), comment on the liquidity of CC. [3]

Q40: Case Study 77: Charlie's Chocolates (CC) 9707/23/O/N/13/Q1 (a) (ii)
(i) Refer to table 1. Calculate the gross profit margin of CC. [3]
(ii) Last year CC's gross profit margin was 63%. Using your answer to (b)(i), comment on the trend in the gross profit margin. [3]

Q41: Case Study 75: Fizzy Drinks (FD) 9707/22/O/N/13/Q1 (a)
Explain the following terms: non-current assets. [3]

Q42: Case Study 75: Fizzy Drinks (FD) 9707/22/O/N/13/Q1 (a)
Refer to table 2. Calculate the acid test ratio. [3]

Q43: Case Study 34: (Sheep Stew) 9707/22/M/J/10/Q2 (a)
(i) Using the information in table 2, calculate the retained profit for EE at 30 April 2014. [3]

(ii) Retained profit for the year ending 30 April 2013 was $10m. Comment on the trend in retained profit. [3]

Q44: Case Study 85: Classic Cars (CC) 9707/21/O/N/14/Q1 (a) (ii)
(i) Calculate the value of X in table 1. [3]
(ii) Briefly explain two reasons for the trend in CC's net profit margin. [3]

Q45: Case Study 87: Best Bakery (BB) 9707/22/O/N/14/Q1 (d)
(i) Using table 1, calculate the value of gross profit for bakery Y in September. [2]
(ii) Explain one way that bakery Y could increase its gross profit margin. [4]

Q46: Case Study 89: Classic Clothes (CC) 9707/23/O/N/14/Q1 (d)
(i) Calculate the value of X in table 2. [3]
(ii) Using your answer to (b)(i) and table 2, comment on the trend in CC's net profit margin.[3]

Q47: Case Study 89: Classic Clothes (CC) 9707/23/O/N/14/Q1 (d)
Explain the following terms: balance sheet (line 14). [3]

Q48: Case Study 91: (Best Books) 9707/21/M/J/15/Q1 (a) (ii)
(i) Calculate the forecast current ratio with e-books. [3]
(ii) Comment briefly on the difference between the liquidity forecasts, with and without e- books. [3]

Q49: Case Study 95: Enterprise Electricals (EE) 9707/23/M/J/15/Q1 (b)
Analyze EE's financial problems. [3]

Q50: Case Study 99: Popular Presents (PP) 9707/22/O/N/15/Q1 (b) (ii)