CASH FLOW STATEMENT & RATIO ANALYSIS 25 APRIL 2013

Lesson Description

In this lesson we:

- Look at a question relating to Cash Flow Statement & Ratio Analysis.

Questions

Question 1

(Adapted from November 2009, NSC, Paper 1, Question 5)

The information given below was extracted from the financial statements of Manchester Ltd, distributors of exquisite perfumes.

REQUIRED:

1.1 Prepare the following:

a.) Complete the note for reconciliation between profit before taxation and cash generated from operations. (8)

b.) Prepare the Cash-Flow Statement for the year ended 28 February 2009. (28)

All workings must be shown in brackets to earn part-marks.

1.2 Calculate the following for 2009:

a.) Current ratio (3)

b.) Acid-test ratio (4)

c.) Net asset value per share (4)

d.) Debt/Equity ratio (Gearing ratio) (3)

1.3 Explain why the directors decided to reduce the long-term loan significantly during the current financial year. In your opinion, was this a wise decision? Explain, quoting evidence (figures/financial indicators) from the question. (6)

1.4 Comment on the return on shareholders' equity, earnings and dividends earned by the shareholders. Quote evidence (figures/financial indicators) from the question. (6)

1.5 Calculate the premium at which the new shares were issued. (5)

1.6 The existing shareholders are unhappy with the price at which the additional shares were sold. Discuss, quoting ONE figure or financial indicator to support your answer. (3)

INFORMATION:

1.	**Extract from the Income Statement**	**R**
	Depreciation	33 500
	Interest expense	164 450
	Net profit before tax	844 300
	Income tax (rate 30% of net profit)	?

2.	**BALANCE SHEET**	**28 February 2009**	**28 February 2008**
	ASSETS		
	Non-current assets	**3 490 885**	**3 017 500**
	Fixed/Tangible assets at carrying value	3 440 885	2 967 500
	Fixed deposit at PDV Bank	50 000	50 000
	Current assets	**320 000**	**231 250**
	Inventories	251 250	110 250
	Trade debtors	60 000	76 000
	Cash and cash equivalents	1 250	45 000
	SARS – Income tax	7 500	0
	TOTAL ASSETS	**3 810 885**	**3 248 750**
	EQUITY AND LIABILITIES		
	Capital and reserves	**3 120 000**	**1 443 000**
	Ordinary share capital (par value R5)	2 085 000	1 050 500
	Share premium	268 970	0
	Retained income	766 030	392 500
	Non-current liabilities	**300 000**	**1 525 000**
	Loan: Enid Bank at 15% p.a.	300 000	1 525 000
	Current liabilities	**390 885**	**280 750**
	Trade creditors	209 945	220 475
	Bank overdraft	47 500	0

	Shareholders for dividends	133 440		52 525	
	SARS – Income tax	0		7 750	
	TOTAL EQUITY AND LIABILITIES	**3 810 885**		**3 248 750**	

3. ADDITIONAL INFORMATION:

A. Additional new shares were issued at a premium halfway through the year on 31 August 2008. These shares did not qualify for interim dividends.

B. Fixed assets were sold for R100 000 cash at carrying value.

C. Earnings and dividends per share were as follows:

	2009	**2008**
Earnings per share	189 cents per share	135 cents per share
Total dividends	72 cents per share	105 cents per share
Interim dividends	40 cents per share	80 cents per share
Final dividends	32 cents per share	25 cents per share

D. You are also provided with the following financial indicators:

	2009	**2008**
% return on shareholders' equity	26%	21%
% return on capital employed (after tax)	24%	10%
Net asset value per share	?	687 cents

E. The price of the shares on the Johannesburg Securities Exchange (JSE) has fluctuated between 680 cents and 780 cents over the past year.

[70]

Answer Booklet

Question 1

1.1

a.)	**Reconciliation between profit before taxation and cash generated from operations**	
	Net profit before tax	844 300
	Adjustments:	
	Depreciation	33 500
	Interest on borrowed funds	164 450
	Operating profit before changes in working capital	**1 042 250**
	Changes in working capital	
	Cash generated from operations	

8

b.) **MANCHESTER LIMITED**
CASH-FLOW STATEMENT FOR THE YEAR ENDED 28 FEBRUARY 2009

	CASH FLOW FROM OPERATING ACTIVITIES	
	Cash generated from operations	
	Interest paid	
	Dividends paid	
	Taxation paid	
	CASH FLOW FROM INVESTING ACTIVITIES	
	Purchase of fixed assets	
	Proceeds from the sale of fixed assets	
	CASH FLOW FROM FINANCING ACTIVITIES	

	Proceeds of shares issued	
	Repayment of long-term loans	
	Net change in cash and cash equivalents	
	Cash and cash equivalents at the beginning of the year	
	Cash and cash equivalents at the end of the year	

28

1.2 Calculate the following for 2009:

a.)	**Current ratio**	**3**
b.)	**Acid-test ratio**	**4**
c.)	**Net asset value per share**	**4**
d.)	**Debt/Equity ratio (Gearing ratio)**	**3**

1.3	**Explain why the directors decided to reduce the long-term loan significantly during the current financial year. In your opinion, was this a wise decision? Explain, quoting evidence (figures/financial indicators) from the question.**	6

1.4	**Comment on the return on shareholders' equity, earnings and dividends earned by the shareholders. Quote evidence (figures/financial indicators) from the question.** **Return on shareholders' equity** **Earnings**	6

Dividends

1.5 **Calculate the premium at which the new shares were issued.**

5

1.6 **The existing shareholders are unhappy with the price at which the additional shares were sold. Discuss, quoting ONE figure or financial indicator to support your answer.**

3

TOTAL MARKS		**70**