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ACCOUNTING FUNDAMENTALS

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Introduction

The financial statement has been prepared by following the guidelines of the account. It helps to provide an effective accounting system to record the transduction of the business. The generally accepted accounting principle has to be followed for elaborating the concept of accounting. The profit and loss, as well as the balance sheet help, analyze the position of the business.

Question 1

A) Prepare the statement of profit and loss as well as balance sheet

Profit and loss statement

Profit and loss of Kedison Plc	
Particulrs	Amounts (£)
Revenue	826650
Cost of sales	578650
Gross profit	248000
Distribution cost	28000
Adminitrative expenes	30000
Other income	nil
Operating profit	190000
Income from invetment	nil
Finance cost/ interst	2000
Profit before tax	188000
Taxation	68000
Profit for the period	120000

Figure 1: Computation of Profit and loss

(Source: Self-created)

In the above figure the profit and loss have been stated which involves the amount of revenue is £826650. The cost of sales amounted to £578650. The gross profit has been computed by deducting the cost of sales from the revenue and it amounts to £248000. The distribution cost amounted to £28000 and the administrative costs amounted to £28000. The amount has obtained operating cost which mounts is £190000. The interest paid amounted to £2000 and the profit before tax amounted to 188000. The profit after deducting the tax amounts to £120000.

Balance sheet

Balance sheet of Kedison Plc	
Assets	Amount £
Non-current assets	
Property, plant, equipment	632730
Intangible assets	nil
Current assets	
Inventories	330600
Trade recivables	170125
Cash	12900
Total assets	1146355
Liabilities	Amount £
Cuurent liability	171355
Non- current liability	nil
Total liabilities	
Equity	
Share capital	710000
Share premium	13000
Other reserves	
Retained earnings (profit at start + net pofit)	252000
Total Libilities	1146355

Figure 2: Computation of balance sheet

(Source: Self-created)

In the above figure, the statement of the balance sheet has been identified which involves assets and liability of Kedison Plc. The assets of the organization involve plant and machinery which amounts to £632730. The current assets involve inventories, trade receivables, and changes which amount to £330600, £170125, and £12900 respectively. The total assets amount to £1146355. The liability involves share capital, share premium, and retained earnings which amount to £710000, £13000, and £252000 respectively. The total liability amounts to £1146355.

B) Reasons for a statement of financial position balancing

The balance between the debit side which is involved with the balance of liabilities and the balance of the credit side which involves the balance of assets. The statement involves assets and liability which is known as a balance sheet. The significant reason for the balancing in both as it is in liability is due to the following accounting principle regarding double entry(Hussain *et al.* 2018, p.48). The system of accounting helps to record all the transactions in two different books of

accounts which therefore act to reflect the account on both sides of the statement. The effecting of the account on both sides of the statement leads to providing a balancing figure in the financial statement.

Question 2

A) Analyze and computation of ratios

1. ROCE

ROCE ratio		2019(£m)	2020 (£m)
Profit before interest and tax		539	620
Capital employed		300	300
Ratio		1.80	2.07

Figure 3: Calculation of ratios

(Source: Self-created)

Meaning

The ratio of return on capital employed is known as the profitability ratio and it provides various profits and interests to the stakeholders, potential investors, and financial managers.

Analyze

It helps to analyze the investment of a company by its capital efficiency. In the above figure, the ratio has been calculated which amounts to 1.80 in 2019 and in 2020 the ratio is 2.07.

Compare

In the above figure, the ratio of the year 2020 had been increased due to an increase in the profit of the year 2020 and the ratio amounted to 2.07.

Ways to improve

The ratio of return on capital employed can get improved by selling off all the outdated machinery, which will lead to lower the total base of assets and debts to increase the ratio.

2. ROE

ROE			
total equity		300	300
net profit		366	431
net income/total equity		1.22	1.44

Figure 4: Calculation of ratios

(Source: Self-created)

Meaning

The term return on the equity leads to measuring the performance of the financial part and it helps to calculate by dividing the total net income by shareholders equity.

Analyze

It has been calculated with the shareholder's equity because they quit is equal to the organizations as it minus debt. In the above figure, the total equity of both the years 2020 and 2019 has been presented.

Compare

In the above figure, the ratio of the year 2020 has been increased to 1.44. The ratio of the year 2019 is 1.22.

Ways to improve

The ratio can be improved by improving the net profit by decreasing the expenses of the organization of Chocco Plc.

3. Earnings per share

Earning per share		2019(£m)	2020 (£m)
Preference dividend		nil	nil
Net Income		366	431
Share Outstanding		1071	1071
EPS ratio [(Net income - Prefernce dividend)/ outstanding share]		34%	40%

Figure 5: Calculation of ratios

(Source: Self-created)

Meaning

The term earning per share has been calculated by dividing the profit of the organization with outstanding shares regarding the main common stock.

Analyze

The ratio serves as the indicator which shows that the company has profitability during the year. The net income in the year 2019 amounts to £366 and in the year 2020, the amount is £431.

Compare

The ratio of the year 2020 is increased from the year 2019 to 40%. In the year 2019, the ratio was 34%.

Ways to improve

The ratio can improve by increasing the net profit of the year with better efficiency.

4. Net profit margin

net profit margin		2019(£m)	2020 (£m)
net profit		366	431
sales		6441	6738
net profit/sales		6%	6%

Figure 6: Calculation of ratios

(Source: Self-created)

Meaning

The margin of net profit has been computed by using the financial issue and it helps to analyze the percentage of the profit of the company by estimating its total revenue and expenses.

Analyze

The net income in the year 2019 amounts to £366 and in the year 2020, the amount is £431. The sales amount to 6441 in the year 2019. The sales of the year 2020 amount to 6738.

Compare

The ratio has remained the same in both the years 2019 and 2020. The sales have been increased in the year 2020 to £6738.

Ways to improve

Its ratio can improve by increasing the net profit which has gained during the year and the net income has been divided by revenue to analyze the ratio.

5. Asset turnover

Assets turnover ratio		2019(£m)	2020 (£m)
current assets		2355	2303
inventory		659	708
current liability		3046	2511
Assets turnover ratio		37%	34%

Figure 7: Calculation of ratios

(Source: Self-created)

Meaning

The term acid turnover ratio leads to measuring the valuation of the revenue or sales of the organization to provide a relative value to the value of assets.

Analyze

The ratio regarding the asset's turnover is used as an indicator for the efficiency of the company.

Compare

In the above figure, the current assets of 2019 amount to £2355, and in the year 2020 the amount is £2303. The ratio will decrease in the year 2020.

Ways to improve

The organization can also delay the capital purchase which involves cash payments.

6. Stock holding days

stock holding period	2019(£m)	2020 (£m)
inventories	659	708
COGS(PURCHASE)	3096	3235
(inventory/purchase)*360		
	76.63	78.79

Figure 8: Calculation of ratios

(Source: Self-created)

Meaning

The stock holding this ratio can be calculated by analyzing the number of days of the business to hold inventory by dividing the inventory with the cost of sales and it has to be multiplied by 365 days to analyze the ratio during the period.

Analyze

In the above figure, the inventory of the year 2019 amounts to £659 and in the year 2020, the amount is £708.

The ratio of the year 2019 is 76.63 and in 2020 the amount is 78.79. The ratio will be increased in the year 2020.

Compare

Ways to improve

The resource and the ratio can also improve including the sales and reducing the price of the product in the organization.

7. Debtor's collection period

debtors collection period		2019(£m)	2020 (£m)
account receivable days		1287	1249
sales		6441	6738
(receivable/sales)*360		71.93293	66.73196794

Figure 9: Calculation of ratios

(Source: Self-created)

Meaning

The term data collection period indicates the average time for collecting the debts of the company.

Analyze

In the above figure, the amount of account receivables is £1287 in the year 2019, and in the year 2020, the amount is £1249.

Compare

The ratio has been decreed which helps to identify the efficiency of the company. The ratio has been decreased to 66 days in the year 2020.

Ways to improve

The ratio of debtors can be improved by providing a discount on early payments.

8. Current ratio

current ratio			
current assets		2355	2303
current liability		3046	2511
current assets/current liability		0.7731451	0.917164476

Figure 10: Calculation of ratios

(Source: Self-created)

Meaning

The current ratio indicates the liquidity of the organization and it also helps to analyze the capability of the company for paying its current liabilities and short-term obligations.

Analyze

In the above figure the current ratio has been stated, in the year 2019 the ratio amounts to 0.773 and in the year 2020, the ratio is 0.91.

Compare

In the above figure, the ratio of the year 2020 has increased to 0.917. The current liability of the year 2020 has decreased to £2511.

Ways to improve

The organization can lead to increase the liquidity ratio by sweeping the accounts, paying the liabilities, and cutting over its expenses.

9. Gearing ratio

Gearing ratio		2019(£m)	2020 (£m)
debt		242	255
equity		300	300
ratio (debt/equity)		81%	85%

Figure 11: Calculation of ratios

(Source: Self-created)

Meaning

The ratio regarding the grading is known as the financial ratio and it helps to compare the equity of Honor to the debt. The gearing ratio leads to measuring the financial leverage for better demonstrating the degree of the company's operation.

Analyze

The ratio of the year 2019 amounts to 81% and the ratio of the year 2020 is 85%.

Compare

The ratio has been incurred in the year 2020 to 85% and the debt has also been increased in the year 2020 to £255

Ways to improve

The gearing ratio can be improved by increasing the level of existing hearing and buying back the ordinary shares from the market which leads to a decrease of the net assets and this will help to increase their ratio.

10. Inventory cover ratio

inventor cover		2019(£m)	2020 (£m)
inventories		659	708
COGS(PURCHASE)		3096	3235
(inventory/purchase)*360			
		76.63	78.79

Figure 12: Calculation of ratios

(Source: Self-created)

Meaning

The ratio regarding inventory coverage is your finances of the ratio and it shows the resources which have been available with the organization for financing the forming of stock.

Analyze

In the above ratio, the inventories of the year 2019 amount to £659 and the amount for the year 2020.

Compare

In the figure, the ratio of the year 2020 has been increased by 78.79. The inventories will be increased to £708 in 2020.

Ways to improve

The ratio regarding inventory cost can be improved by better forecasting of the resources which have been needed during the organization according to the techniques.

B) Analyzing the final position of business

The use of the ratio is measured as the technique for analyzing the position of the organization. The investors are generally analyzing the ratios to evaluate the performance and the availability of liquidity with Choco Plc for spying on the creditors and the short-term obligations. The ratio helps to examine the current performance of the organization by evaluating the percentage of actions (Broadbent *et al.* 2019, p.39). It helps to ascertain the potential of the organization by understanding the efficiency ratio of the firm. The organization, Chocco Plc has been improving in the current ratio by increasing its current liabilities. The current ratio has to be high as it leads to analysis that the company has a sufficient amount to pay its creators.

Conclusion

The statement of the profit and loss helps to analyses the net profit of the year and it also helps to a certain the expenses of the year. The balance sheet provides various information about assets and liabilities. The ratio helps to calculate the efficiency and the ability of the profitability of the organization so that it can be helpful for the investors to invest in the organization.

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