



Type exercises: value an
organisation for investment
purposes

Assessment one

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- ✓ Following the use of the notions learned in the "Accounting Fundamentals" course and the online resources offered by "UWTSD", we analyzed the following:

Answer for: first question

Statement of Financial Position

FIRST STEP :

I consider it always good (like a first step) to identify each subject in which class it belongs (for example "if X" is "assets, liabilities or capital/equity"), then to identify if it is a decrease or an increase (for example, "if X" is "debit or credit").

	DEBIT £	CREDIT £
<u>ASSETS</u>		
Non-current assets		
Plant and equipment	632,730	
Total non-current assets		<u>x</u>
Current assets		
Sale		(826,650)
Cost of sale	578,650	
Cash and bank	12,900	
Administrative expenses	30,000	
Stock at 31st December 2020	330,600	
Debtors	170,125	
Total current assets		<u>x</u>
TOTAL ASSETS		<u>x</u>
<u>LIABILITIES</u>		
Non-current liabilities		
4% Debentures		(100,000)
Total non-current liabilities		<u>x</u>
Current liabilities		
Trade creditors		(171,355)
Corporation tax for the year		(68,000)
Owed commission/Salesmen		(3,000)
Good Value		(980)

Total current liabilities		<u>x</u>
TOTAL LIABILITIES		<u>x</u>
<u>EQUITY</u>		
£1 ordinary shares		(310,000)
10% £1 preference shares		(300,000)
Retained profits at 1st January 2020		(132,000)
Ordinary dividend paid	20,000	
Preference dividend paid	30,000	
Interest paid	2,000	
Directors remuneration	5,000	
Distribution costs	28,000	
TOTAL EQUITY		<u>x</u>
TOTAL LIABILITIES AND EQUITY		<u>x</u>

SECOND STEP:

The account is created with the information obtained above and also taking into account:

- "net current assets" must be extracted (the amount of money to be held for the payment of current liabilities), ie "current assets - current liabilities".
- required "net assets" (which is like a total of the values of a business, ie "net current assets – total current assets").
- for an accounting equation : important also the fact that "capital = assets" and "capital + liabilities = assets".

➤ STATEMENT OF FINANCIAL POSITION AS AT 31ST DECEMBER 2020

	£	£
<u>ASSETS</u>		
Non-current assets		
Plant and equipment	632,730	
Total non-current assets		632,730
Current assets		
Cash and bank	12,900	

Stock at 31st December 2020	330,600	
Debtors	170,125	
Total current assets		513,625
TOTAL ASSETS		1,146,355
<u>LIABILITIES</u>		
Non-current liabilities		
4% Debentures	100,000	
Total non-current liabilities		100,000
Current liabilities		
Trade creditors	171,355	
Corporation tax for the year	68,000	
Owed commission/Salesmen	3,000	
Goods value	980	
Total current liabilities		243,355
TOTAL LIABILITIES		343,355
Net current assest		270,270
Net assest		243,355
<u>EQUITY</u>		
£1 ordinary shares	310,000	
10% £1 preference shares	300,000	
Retained profits at 1st January 2020	132,000	
Total equity		742,000
Total equity and liabilities		1,085,355

Profit and loss statement

In the following table the target is to find out if the business has profit or loss. It is calculated from the company's income, then the costs incurred. After they are found, a subtraction must be made between them to find out the result that denotes if there is a profit / loss.

- “gross profit – total expenses = operatin income => profit/loss”

➤ **PROFIT AND LOSS STATEMENT FOR THE YEAR ENDED AT 31ST
DECEMBER 2020**

	£	£
INCOME		
Sales	826,650	
Cost of sales	578,650	
Goods valued	980	
Distribution costs	28,000	
Gross profit		276,980
EXPENSES		
Ordinary dividend paid	20,000	
Preference dividend paid	30,000	
Interest paid	2,000	
Administrative expenses	30,000	
Corporation tax for the year	68,000	
Owed commission	3,000	
Total expenses		153,000
Operating income		123,980

“Why does the statement of financial position balance?”

- *"Balance sheet" is another name for "statement of financial position".*

The first step in identifying something, regardless of any subject, is to understand the meaning of words, such as:

- *"balance" in its natural meaning, means "equality", and in finance it has the same meaning. In finance "balance" is used to produce "equality" in calculations. That is, the amount offered to be equal to the one received (I have the share, I must also have the reward, ie assets = capital + liabilities).*

- *this "statement" helps the "balance sheet" to represent these "equalities".*

- *financial position refers to the inputs and outputs of a business (calculated to reach the above equality).*

- *all three related show the balance of a company to check the consistency of some actions.*

(Frank & Alan, 2012)

Answer for : second question

Accounting ratios

I chose to calculate the ratios incorporated in a table as simple as possible, but still explicit.

- Desired model :

RATIO	FORMULA AND CALCULATION	YEARS
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- I will add a few abbreviations, namely:

- a) Return on capital employed – “ROCE”
- b) Earnings per share – “EPS”
- c) Return on equity – “ROE”

➤ ACCOUNTING RATIOS :

INVESTMENT RATIOS		2020	2019
1. ROCE	$\frac{\text{Profit before interest}}{\text{Assets employed}} \times 100\%$ Calculation : 2020 : $\frac{805}{9,736 - 2,511} \times 100 = \frac{805}{7,225} \times 100 = 0,1114 \times 100 = 11,14$ 2019 : $\frac{699}{10,087 - 3,046} \times 100 = \frac{699}{7,041} \times 100 = 0,0992 \times 100 = 9,92$	11,14 %	9,92 %
2. ROE	$\frac{\text{Earnings}}{\text{Ordinary share capital and reserves}} \times 100\%$ Calculation : 2020 : $\frac{431}{3,088} \times 100 = 0,1395 \times 100 = 13,95$ 2019 : $\frac{366}{2,912} \times 100 = 0,1256 \times 100 = 12,56$	13,95 %	12,56 %
3. EPS	$\frac{\text{Earnings}}{\text{Number of ordinary shares}}$ Calculation : 2020 : $\frac{431}{300} = 1,43(6)$ 2019 : $\frac{366}{300} = 1,22$	1,43p	1,22p
PROFITABILITY RATIOS			

4. Net profit margin	$\frac{\text{Net profit}}{\text{Sales}} \times 100\%$ Calculation : 2020 : $\frac{805}{6,738} \times 100 = 0,1194 \times 100 = 11,94$ 2019 : $\frac{699}{6,441} \times 100 = 0,1085 \times 100 = 10,85$	11,94 %	10,85 %
EFFICIENCY RATIOS			
5. Asset turnover	$\frac{\text{Turnover}}{\text{Assets employed}}$ Calculation : 2020 : $\frac{6,738}{9,736 - 2,511} = \frac{6,738}{7,225} = 0,9325$ 2019 : $\frac{6,441}{10,087 - 3,046} = \frac{6,441}{7,041} = 0,9147$	0,93	0,91
6. Stock holding days	$\frac{\text{Inventory}}{\text{Cost of sales}} \times 365$ Calculation : 2020 : $\frac{708}{3,235} \times 365 = 0,2188 \times 365 = 79,88$ 2019 : $\frac{659}{3,096} \times 365 = 0,2128 \times 365 = 77,69$	80 days	78 days
7. Debtors collection period	$\frac{\text{Trade receivables}}{\text{Credit sales}} \times 365$ Calculation : 2020 : $\frac{1,249}{6,738} \times 365 = 0,1853 \times 365 = 67,65$ 2019 : $\frac{1,287}{6,441} \times 365 = 0,1998 \times 365 = 72,93$	68 days	73 days
LIQUIDITY RATIOS			
8. Current ratio	$\frac{\text{Current assets}}{\text{Current liabilities}}$ Calculation : 2020 : $\frac{2,303}{2,511} = 0,9171$ 2019 : $\frac{2,335}{3,046} = 0,7665$	0,9	0,7
FINANCING RATIOS			
9. Gearing ratio	$\frac{\text{Debt}}{\text{Debt} + \text{equity}} \times 100\%$	57,25 %	58,64 %

	Calculation: 2020 : $\frac{4,137}{(4,137 + 3,088)} \times 100 = \frac{4,137}{7,225} \times 100 = 0,5725 \times 100 = 57,25$ 2019 : $\frac{4,129}{(4,129 + 2,912)} \times 100 = \frac{4,129}{7,041} \times 100 = 0,5864 \times 100 = 58,64$		
10. Interest cover	<u>Profit before interest</u> Interest charges Calculation : 2020 : $\frac{805}{226} = 3,5619$ 2019 : $\frac{699}{181} = 3,8618$	3,5 times	3,8 times

Comment on the financial performance and position

Due to the above calculations we can see how in the case of "ROCE" and "ROE" there is a rather considerable improvement in 2020 in percentage. More precisely, an increase of: 1,22 % for ROCE (2020) and 1,39 % for ROE (2020).

There is a profit margin that increased by 1.09%, which induces the stability of the company.

Interest is stable (has not improved), even if there is a decrease of 0.3%

References

Frank, W. & Alan, S., 2012. *Frank Wood's business accounting 2*. 12th ed. Essex: Pearson Prentice Hall.