

**ADVANCED GCE
BUSINESS STUDIES**

2875

Further Accounting and Finance

TUESDAY 17 JUNE 2008

Afternoon

Time: 1 hour 30 minutes

Additional materials (enclosed): Answer Booklet (8 page)

Additional materials (required):
Calculators may be used



INSTRUCTIONS TO CANDIDATES

- Write your name in capital letters, your Centre Number and Candidate Number in the spaces provided on the Answer Booklet.
- Read each question carefully and make sure you know what you have to do before starting your answer.
- Answer **all** the questions.
- If you use extra sheets of paper, fasten these sheets to the Answer Booklet.

INFORMATION FOR CANDIDATES

- The number of marks for each question is given in brackets [] at the end of each question or part question.
- The total number of marks for this paper is **60**.
- You will be awarded marks for the quality of written communication where an answer requires a piece of extended writing.

This document consists of **4** printed pages.

Weatherheads Waterproofs plc (WWP)

Henry Levinger is the Chief Executive of Weatherheads Waterproofs plc (WWP). The company manufactures a range of waterproof clothing designed to cater for all kinds of outdoor activity. It produces garments such as golf waterproof suits and orienteering protective clothing. Henry is keen to keep adding to WWP's range of clothing, bringing out new designs and styles to cater for the needs of the sporting and recreational market. "Such clothing is almost fashion wear these days," he often said. "It is certainly no longer simply a functional product." 5

Henry was in discussion with his financial accountant, Martin O'Neill. Martin was explaining to him the importance of identifying a breakeven volume when assessing the value of a product line to the business. He was using Fig. 1 to illustrate his point.

Fig. 1 Simplified breakeven chart

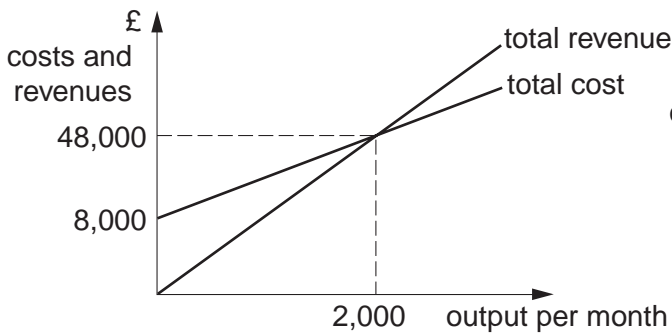
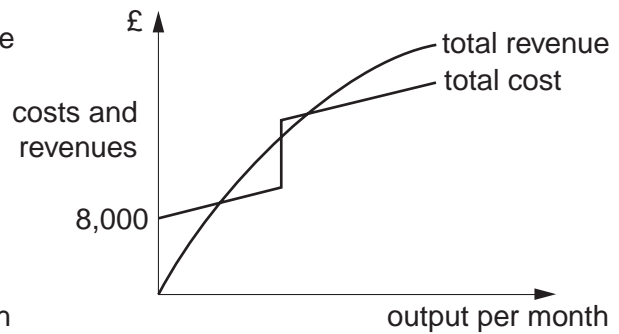


Fig. 2 Complex breakeven chart

10



"I based this chart on some data we had on a waterproof football training top," he said. "As you can see we need to sell 2,000 of these products every month to cover our costs. Unfortunately the chart is based on simplifying assumptions which rarely hold in practice. A more accurate picture is shown in Fig. 2."

Martin now turned to the financial data concerning a new range of rugby training suits which WWP had recently introduced. He explained to Henry that the production costs were determined by three major elements: 15

- the quality of the lining used;
- the breathability of the waterproof material;
- the trimmings used such as zips, pockets and design features.

20

"Customers are much more demanding these days," said Martin, "All customers, even rugby players, want to look good!"

Henry had recently signed a contract to supply 3,000 of these suits to MM Sports, a major retailer, for an agreed contract price of £50 each. He was confident that such a deal would be profitable for WWP. Martin then showed Henry a breakdown of the budgeted costs for this batch of 3,000 of these garments (see Fig. 3). 25

Fig. 3 Cost breakdown for training suits

	(£)	(£)	(£)	
	Lining	Waterproof	Trimmings	
Direct labour costs	20,000	15,000	12,000	30
Direct material costs	16,000	25,000	9,000	

Allocated overheads for the batch totalled £15 000.

Martin then went on to say that WWP usually added a 50% mark up to the full unit cost of such garments when selling to retail outlets.

Henry became alarmed when Martin told him that the company was now running at 20% over budget on materials for lining the training suits. Martin continued saying that labour costs were also significantly over budget. Henry wanted to know why this had happened. Obviously he had not had time to analyse the full impact on profits yet, but he knew it could be quite damaging. 35

Despite this, Henry was pleased with the performance of WWP over the last year. The company had been consistently profitable and its performance was regarded as good. A number of financial analysts in the newspapers had been recommending the shares as a 'buy' in their columns. 40
 Figs. 4 and 5 indicate perhaps why the shares are regarded as a good investment. Dividends per share have averaged 22p for each of the last three years.

Fig. 4 WWP's Share Price

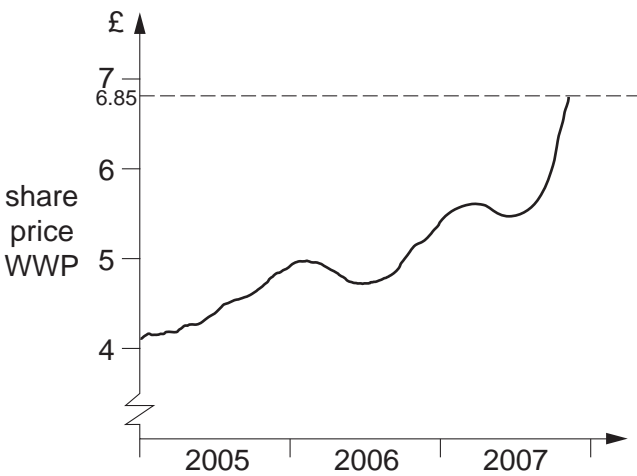
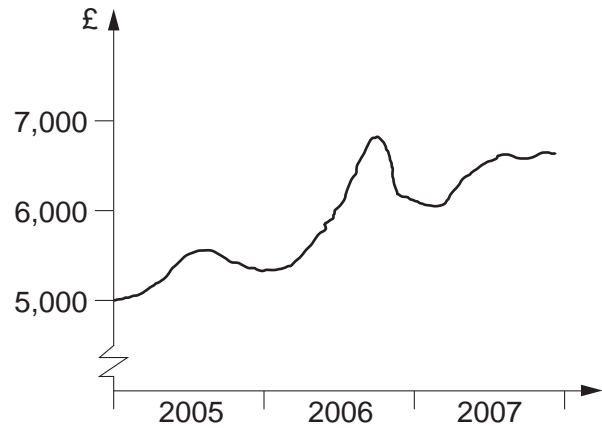


Fig. 5 F.T.S.E. Index



Figs. 6 and 7 show extracts from WWP's accounts for 2006 and 2007. 45

Selected extracts WWP's accounts

Fig. 6 WWP Profit and Loss account (Years ended 30 November 2006 and 2007)

	(£'000s) 2007	(£'000s) 2006	
Sales	1,900	1,400	50
Cost of Sales	1,100	850	
Gross Profit	800	550	
Net Profit before tax	550	350	

Fig. 7 WWP Balance Sheet Extracts (as at 30 November 2006 and 2007)

	(£'000s)	(£'000s)	
	2007	2006	
Fixed Assets	1,400	900	
Current Assets	900	850	
Current Liabilities	1,100	800	
Total Assets less Current Liabilities	1,200	950	55
Long-term Liabilities	700	500	
Net Assets	500	450	
Issued Share Capital	250	250	
Reserves	250	200	
Shareholders Funds	500	450	60
			65

Henry felt that these final account extracts showed a strong financial position and performance, although he was aware of a few worrying features.

“I believe that the company has excellent prospects,” he said. “We are one of the market leaders in a fast growing sector.”

Answer **all** the questions.

- 1 (a) Use Fig. 1 to calculate:
- (i) the selling price per unit; [2]
 - (ii) the variable cost per unit. [2]
- (b) Using the data presented in Figs. 1 and 2, analyse **two** benefits to WWP of using breakeven charts in its decision-making. [6]
- (c) The cost of MM Sports' order will exceed budget. Analyse the impact of this on WWP's budgeted profits. [6]
- (d) Evaluate the usefulness to WWP of budgeting as a management decision tool. [16]
- 2 (a) A shareholder bought 5,000 shares in WWP at £4.20 each in January 2005. Assess the performance of this investment to 31 December 2007. [10]
- (b) Using all the data available, evaluate the financial position and performance of WWP in 2007. [16]

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