UNIVERSITY OF BRADFORD

FINANCIAL STATEMENT ANALYSIS & VALUATION (MSc)

MAN4270M

7th May 2014 **16:00 – 17:30 hours**

Main

This is a **CLOSED BOOK** examination

Answer any **two** questions.

All questions carry equal marks

Answer any two of the following questions

Question 1

AHM ltd produces and sells a single product. The following accounts are expected for the 6 months Jan to June 2015.

	Jan £	Feb £	Mar £	April £	May £	June £
Sales	10,000	30,000	20,000	10,000	30,000	30,000
Cost of sales:						
Direct materials	8,000	12,000	15,000	6,000	4,000	12,000
Direct wages	2,000	3,000	2,000	2,500	3,000	1,800
Utility bills	1,000	1,000	1,000	900	900	700
Other expenses	500	400	200	350	400	230
Depreciation	900	900	1,800	1,800	1,800	1,800

Additional information:

1. All sales are made on credit. The business offers a cash discount (of 2% of the amount owed) to those customers who pay by the end of the month of sale. Half of all units sold qualify for the discount. For the remaining half of the units sold, 95% are paid during the next month. The remainder are bad debts. Total sales of December 2014 are expected to be £20,000.
2. Material purchases are made on credit; creditors allow one month's credit. When material costs exceed £10,000 a discount of 2% is available if payment is made within one month. AHM ltd will take up any discounts where available. The discounts have not been included in the P & L figures yet. The Purchases for the month of December 2014 are expected to total £7,000.
3. Wages, Utility and Other expenses are paid in the month in which they are incurred.
4. Equipment will be replaced in Feb 2015. The new machine costs £50,000 and the old machinery will be sold for a cash scrap value of £5,000 in Feb. Payment for the new machine is to be made in two equal instalments in April and June 2015.
5. A loan of £15,000 is due for repayment in March 2015.
6. In April the proceeds from a new share issue will be received totalling £100,000.
7. A taxation payment of £20,000 is due in April.
8. Opening cash balance on 1 Jan 2015 is expected to be £10,000 in hand.

Requirements:

- **a.** Prepare a monthly cash budget for January to June 2015. **(15 marks)**
- **b.** Advise the management on possible actions they might take to overcome any cash deficit. Use the monthly cash budget you have prepared in (a) to illustrate the advice and to emphasise the importance of preparing cash budgets. **(4 marks)**
- **c.** Critically discuss the purpose of budgeting in organisations and its limitations

(6 marks)

<u>Total 25 marks</u>

Question 2

AVD Limited is an engineering company that produces sets of specialised components that are currently only sold nationally. The company has been offered the opportunity to bid for a special contract of 5000 sets of this component. These would be manufactured during a slack period and would not affect normal production. The standard cost schedule and other information is set out below.

Standard cost schedule for one set

		£
Materials –	1 component A	5·00
	1 component B	4·00
	1 component C	4·00
	Packaging	1·00
		14·00
Direct labour – 2 hours at £5 per hour		10·00
Supervisor's labour at 20% of direct labour		2·00
Overheads – depreciation		2·00
Other general fixed costs		2·00
Total cost		30·00

The price is set by adding a further 10% on cost. The amount of the profit margin is £3.00 and a current price of £33.00.

<u>The following information may help in setting a price for this contract:</u>

1) Component A is in general use and its price is expected to remain unchanged in the coming year.
2) Component B is no longer used and there are currently at least 2,000 components in stock, for which there will be no other use. It can be sold by maximum £2 per unit.
3) Component C, which is widely used elsewhere, will be replaced shortly by a new component but the large stocks remaining at that date can be converted to the new component at a cost of £1 per unit. The new component itself will cost £4 per unit.
4) The usual packaging will not be required for this order, but special bulk packaging will be needed and will cost £8,000.
5) The direct labour needed for this order would normally be engaged in maintenance during the slack period and paid anyway. To complete the necessary maintenance, if the contract were accepted, overtime costing £10,000 will have to be paid.
6) Depreciation is a factor of time rather than use.
7) Additional overheads caused directly by this order will be £3,000.

Requirements:

- **a.** Describe what is meant by the terms 'relevant cost' and 'opportunity cost' **(6 marks)**
- **b.** Calculate the minimum price for this 5000 units' contract that AVD Limited could make with no loss on the contract. Suggest with reasons the price that you would bid. **(13 marks)**
- **c.** Discuss any factors, other than price, that should be considered before accepting this contract. **(6 marks)**

<u>Total 25 marks</u>

Question 3

A. Discuss the main characteristics that should be considered in providing financial information for decisions makers. Explain the importance of each characteristic for different kinds of user.

(12 marks)

B. Class ltd company makes two products, the cd and the dvd. The company has made the following sales and cost information available for each product:

	CD £	**DVD £**
Direct Materials	2	6
Direct Labour (£6 per hour)	12	6
Variable Overhead	2	2
	16	**14**

The selling price per unit is £28 per CD and £22 per DVD. During June, the company experiences a lot of holiday requests. As a result, they only have 16,000 hours of direct labour available for production.

Sales demand during the month of July is expected to be 6,000 units for CDs and 10,000 units for DVDs.

Requirements:

1. Calculate the product mix that will maximise profit and profit earned, assuming that fixed costs are £40,000 and there is no opening inventory. **(6 marks)**
2. Explain the meaning of "limiting factor" and discuss its limitations providing illustrative examples. State the rule that is used when activity is restricted by the presence of a limiting factor**.**

(7 marks)

Total 25 marks

Question 4

A. Distinguish between financial accounting and management accounting. **(7 marks)**

B. Storage NGS ltd manufactures three types of filing cabinet – F1, F2 and F3. The budgeted costs per unit are provided below:

	F1	F2	F3
	£9	£	£
Metal Cost (£2 per kg)	5	15	10
Direct Labour Cost (£4 per hour)	4	10	8
Variable Overhead Cost	3	7.50	6
Fixed Overhead Cost	4.5	11.25	9
Additional Information			
Selling Price Per unit	20	50	40
Budgeted Volumes Per Annum	4,000	2,000	1,500

The budgeted volume for each product is predicted to be equal to market demand. The fixed overhead costs are based on direct labour hours.

The company's products are in demand due to the hard wearing and long lasting nature of their cabinets. The procurement manager has recently discovered that there will be a problem with accessing raw material of metal in the coming period. He has predicted that the maximum amount of metal he will be able to access in the coming year is 20,000 kg. He is aware that included in the budgeted volumes of sales predicted is a special order that the company has already accepted.

This special order includes 500 F1 cabinets, 100 F2 cabinets and 150 F3 cabinets. The company will incur a financial penalty of £2,000 if they are unable to fulfil the order requirements within this period.

Requirements:

1. Determine the optimum production plan and state the total net profit that this should yield for each product in the current year. **(6 marks)**
2. Calculate and explain the maximum prices which should be paid per kg to obtain extra supplies of metal. **(2 marks)**
3. The company is considering outsourcing the remainder of the production to another firm. Discuss the benefits and limitations of outsourcing. What are the main stages of making an outsourcing decision. Make reference to the above company. **(10 marks)**

<u>Total 25 marks</u>