

REVISION: INTERPRETATION OF FINANCIAL STATEMENTS

27 MARCH 2014



Lesson Description

In this lesson we revise:

- Companies: Income Statement
- Companies: Cash Flow
- Companies: Interpretation of Financial Statements



Improve your Skills

Companies: Income Statement

Read the information below and show the necessary adjustments that need to be made to the Income Statement.

Question 3

Extract of the Trial Balance before taking into account the adjustments below: (28 February 2013 – end of financial year)

Sales	R100 000
Cost of sales	R60 000
Trading stock	R25 000

Adjustment

- A dissatisfied customer was issued with a credit note, R400. The credit note was omitted from the relevant journal. The business uses a mark-up of 100% on cost.
- Due to heavy rains in February, stock with a value of R2 000 was damaged. The insurance company decided to pay 50% of the loss, however no payment has yet been received. The bookkeeper did not make any entries for the above transactions.
- A physical stock take at year end showed that the business has stock to the value of R21 300. (this was after taking into account the above adjustments)

Extract of Income Statement

Sales	
Cost of sales	
Gross Profit	
Operating expenses	

Companies: Cash Flow

Question 1

You have been presented with the following financial information for Posh Limited for the year ended 30 June 2013.

- 1) Extract of balances from the post-closing trial balance of Posh Limited as at 30 June 2013. (Comparative figures have been given).

	2013 R	2012 R
Ordinary share capital	3,100,000	2,740,000
Retained income	677,000	403,720
Loan: Generous Bank	2,700,000	1,980,000
Vehicles	2,450,000	2,780,000
Accumulated depreciation on vehicles	836,000	481,000
Equipment	5,302,000	3,980,000
Accumulated depreciation on equipment	1,974,000	1,613,000
Inventories	513,000	546,000
Net trade debtors	1,988,000	1,524,000
Bank (favourable)	?	155,500
Cash float	3,500	4,500
Trade creditors	1,315,000	1,183,000
SARS – income tax (Dr)	256,280	0
SARS – income tax (Cr)	0	188,000
Shareholders for dividends	31,000	238,000

- 2) Extract from the notes to the financial statements as at 30 June 2013.

Ordinary share dividends	302,000
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- 3) Additional shares were issued during the year.
- 4) Interest on the loan is NOT capitalised.
- 5) Some of the vehicles were sold during the year at carrying value. No new vehicles were purchased.
- 6) No equipment was disposed of during the year.
- 7) Income tax is calculated at 28% of net profit.

Answer Sheet

Notes to the Cash Flow Statement for the year ended 30 June 2013

1. Reconciliation between profit before taxation and cash generated from operations	R
Profit Before tax	
Adjustment in respect of	
Depreciation	
Interest expense	
Operating profit before changes in capital	
Changes in working capital	
_____ in inventory (
_____ in debtors (
_____ in creditors (
Cash generated from operations	

You can use this information to prepare the full Cash Flow Statement as well!

Prepare the cash flow statement with notes for Posh Limited for the year ended 30 June 2013.

	Note	R
Cash flows from operating activities		
Cash generation from operations	1	
Interest paid		(468 000)
Dividends paid	2	
Normal tax paid	3	
Cash flows from investing activities	4	
Purchase of non-current assets		
Proceeds of sale of non-current assets		
Cash flows from financing activities		
Proceeds from issue of share capital		
Proceeds from long-term loan		
Net change in cash and cash equivalents		
Cash and cash equivalents: beginning of year		160 000
Cash and cash equivalents: the end of year		

notes for...

3. Taxation paid	R

3

4. Cash flows from investing activities	R
Purchase of non-current assets	
Proceeds of sale of non-current assets	

6

Companies: Interpretation of Financial Statements

Question 1

(Adapted from November 2009, Question 5)

CASH-FLOW STATEMENT AND RATIO ANALYSIS

The information given below was extracted from the financial statements of Sports Ltd, distributors of various sporting equipment.

Required:

- 1.1 Calculate the following for 2009:
 - 1.1.1 Current ratio (3)
 - 1.1.2 Acid-test ratio (4)
 - 1.1.3 Net asset value per share (4)
 - 1.1.4 Debt/Equity ratio (Gearing ratio) (3)
- 1.2 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)

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	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

Additional Information:

- A. 206 900 shares were sold during the financial year at R6,30.
 B. 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

- C. 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	?	

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