

# 5: Financial information and decisions

## Paper 1 – Topic questions

The questions in this document have been compiled from a number of past papers, as indicated in the table below.

Use these questions to formatively assess your learners' understanding of this topic.

Question	Year	Series	Paper number
2d	2017	March	12
3e	2017	March	12
2e	2017	June	11
2e	2018	March	12

- 2 QAC uses batch production to make 70 different cleaning products including soap and polish. To meet increased demand for two of its products, X and Y, QAC could invest \$10m in flow production using new technology. The Finance Director is worried about QAC's cash flow position as shown in Table 1. He thinks it is important to have a high level of inventory but he also wants to improve the cash flow position.

**Table 1: QAC's cash flow forecast for April – June 2017 (\$000)**

	April	May	June
Cash in:	300	400	460
Cash out:			
Labour costs	140	140	140
Inventory costs	120	180	180
Fixed costs	100	100	100
Total cash out	360	420	420
Net cash flow	(60)	(20)	?
Opening balance	30	(30)	(50)
Closing balance	(30)	(50)	?

- (d) Identify and explain **two ways (other than reducing inventory)** that QAC could use to improve its cash flow position.

Way 1: .....

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Explanation: .....

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Way 2: .....

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Explanation: .....

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- 3 Dipta and Ravi are friends. They want to start up a business making chocolates to sell at local markets. Most ingredients such as cocoa beans will be imported. Ravi's primary market research shows that using ethical sources of supply for the ingredients will be popular with consumers. Ravi and Dipta have no business experience, but Dipta has written a business plan. They need \$500 for equipment, but they cannot decide which source of finance to use.

(e) Identify and explain **two** possible advantages of importing for Dipta and Ravi's business.

Advantage 1: .....

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Explanation: .....

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Advantage 2: .....

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Explanation: .....

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- 2 Josh owns an office cleaning business. He has a number of large and small business customers. Josh employs 6 full-time cleaners who are all given off-the-job training. Josh believes that using the latest cleaning equipment increases added value. He said: 'Customers are happy with the service. I am always sending text (SMS) messages to workers about additional work.' Josh has been looking at his balance sheet. He cannot decide if a bank loan is the best source of finance to use for new equipment. The new equipment will cost \$60 000.

**Table 1: Extract from Josh's balance sheet as at 30 April 2017 (\$000)**

Current assets		120
Trade receivables	90	
Cash	X	
Current liabilities		Y
Net current assets		70

- (e) Do you think a bank loan is the best source of finance for Josh to use for the new equipment? Justify your answer.

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- 2 Paul is the Managing Director of a private limited company called PShirts. It manufactures and sells men's and women's shirts in country Y. Its products are priced lower than most of its competitors. Sales have fallen recently even though there has been an economic boom. Paul is thinking about starting to sell shirts in other countries. One of the directors is worried about legal controls in other countries. A summary of the accounts is shown in Table 1.

**Table 1: Summary of financial statements**

	2016 (\$m)	2017 (\$m)
Revenue	500	350
Gross profit	210	120
Profit	160	60
Current assets	35	30
Current liabilities	15	15

- (e)** Do you think Paul should be worried about the change in the profit margins between 2016 and 2017? Justify your answer.

[illegible]

Question	Answer	Mark
2 (d)	<p><b>Identify and explain two ways (other than reducing inventory) that QAC could use to improve its cash flow position.</b></p> <p>Knowledge [2 × 1] award 1 mark for each relevant way identified</p> <p>Application [2 × 1] – award 1 mark for each way if relevant reference made to this business</p> <p>Analysis [2 × 1] – award 1 mark for each relevant explanation</p> <p>Relevant points might include:</p> <ul style="list-style-type: none"> <li>• Ask debtors to pay quicker/ reduce credit terms [k] if they pay sooner this will increase cash inflows [an]</li> <li>• Delay purchases [k] could decide not to buy as much equipment [app] so keeping cash in the business [an]</li> <li>• Delay inventory payments [k] as \$1 20 000 paid in May [app] lowering cash outflow [an]</li> <li>• Arrange a <b>short term</b> loan / overdraft [k]</li> <li>• Lower fixed costs [k]</li> <li>• Buy cheaper materials [k]</li> <li>• Sell (unwanted) non-current assets [k] so releasing cash tied up in the business [an]</li> <li>• Delay investment/ expansion plans [k] of \$10m [app]</li> </ul> <p>Accept practical suggestions for example:</p> <ul style="list-style-type: none"> <li>• Reduce range of products sold [k] this would reduce the cost of materials needed [app];</li> <li>• Sell more products [k]</li> </ul> <p>Application marks may be awarded for appropriate use of the following: correct use of data in table 1, \$10m, batch or flow production, reference to soap or polish, 70 products, cleaning products, increased demand for X and Y</p>	6

Question	Answer	Mark
3 (e)	<p><b>Explain two sources of finance Dipta and Ravi could use.</b></p> <p><b>Recommend which source Dipta and Ravi should choose. Justify your answer.</b></p> <p>Knowledge [1] – award 1 mark for identification of relevant source(s)</p> <p>Application [1] – award 1 mark for a relevant reference made to this business</p> <p>Analysis [2] – award up to 2 marks for relevant development of point(s)</p> <p>Evaluation [2] – award up to 2 marks for a justified decision as which is the best option to choose</p> <p>Relevant points might include:</p> <ul style="list-style-type: none"> <li>• Bank loan [k] would have time to repay [an] the \$500 [app] but would have to pay interest on amount borrowed [an]</li> <li>• Own savings [k] no need to repay [an] but may not have sufficient funds [an]</li> <li>• Leasing or hire purchase [k] as have no business experience [app] could return equipment in case of need [an]</li> <li>• Micro finance [k] as new start up [an]</li> <li>• Government grants/ subsidies [k]</li> <li>• Ask family/ friends for finance [k]</li> </ul> <p><b>Do not accept</b> issue shares, debentures, retained profits or sell existing assets as not appropriate for a start up business.</p> <p>Application marks may be awarded for appropriate use of the following: chocolate, \$500, equipment, primary market research, business plan, no business experience, new business, ingredients or cocoa beans, ethical (sources of supply)</p>	6

Question	Answer	Mark
2 (e)	<p><b>Do you think a bank loan is the best source of finance for Josh to use for the new equipment? Justify your answer.</b></p> <p>Knowledge [1] : award 1 mark for identification of relevant point (s)  Application [1] : award 1 mark if relevant reference made to this business  Analysis [2] : award up to 2 marks for relevant development of point(s)  Evaluation [2] : justified decision made as to whether a bank loan is the best source of finance for Josh to use for the new equipment</p> <p>Points might include:</p> <ul style="list-style-type: none"> <li>• Increased liabilities OR must be repaid [k] by \$60 000 [app]</li> <li>• Loan would give him time to repay [k]</li> <li>• Has cash available [k] of \$30 000 [app] so he would not need to borrow the full amount [an]</li> <li>• Doesn't have enough cash available [k] to pay the \$60 000 [app]</li> <li>• Cost of repayments OR interest [k]</li> <li>• Leasing is a method Josh can use [k] so the latest equipment is always available [app]</li> <li>• Banks may not be willing to lend the money [k]</li> </ul> <p>Application marks may be awarded for appropriate use of the following:  Service, cleaners, small / large businesses, \$60 000, correct use of table 1, added value, <b>latest equipment</b>, Josh has a small business.</p> <p>Candidates may analyse other suitable sources of finance.</p> <p><b>Do not award</b> overdraft as it is not a suitable source of finance to purchase fixed assets.</p>	6



Question	Answer	Mark
2 (e)	<p><b>Do you think Paul should be worried about the change in the profit margins between 2016 and 2017? Justify your answer.</b></p> <p>Knowledge [1] – award 1 mark for identification of relevant issue(s) (Max 1)</p> <p>Application [1] – award 1 mark for a relevant reference made to this business</p> <p>Analysis [2] – award up to 2 marks for each relevant explanation(s)</p> <p>Evaluation [2] – justified decision as to whether Paul should be worried by the change in profit margins</p> <p>Relevant points may include:</p> <ul style="list-style-type: none"> <li>• Gross profit margin <b>decreased</b> [k] from 42% to 34% [app + an] which is a decrease of 8% [an]</li> <li>• Profit margin <b>decreased</b> [k] from 32% to 17% [app + an] a decrease of 15% [an]</li> <li>• Revenue decreased [k] by \$150m OR to \$350m [app]</li> <li>• Cost of sales <b>decreased</b> [k] by \$60m OR to \$230m [app]</li> <li>• Expenses <b>increased</b> [k] by \$10m OR to \$60m [app]</li> <li>• Profit <b>decreased</b> [k] to \$60m OR by \$100m [app]</li> </ul> <p>Application marks may be awarded for appropriate use of the following:</p> <ul style="list-style-type: none"> <li>• private limited company</li> <li>• shirts</li> <li>• men and women</li> <li>• priced lower than competitors</li> <li>• sales have fallen</li> <li>• legal controls</li> <li>• relevant use of financial data in table</li> <li>• selling in other countries</li> <li>• economic boom</li> </ul>	6