**AFB MOCK EXAM 1**

**ANSWER QUESTION 1 AND ANY TWO OTHER QUESTIONS**

**Section A: Compulsory question for 40 marks**

**Question** 1

The trial balance below is for ME1 plc for the y/e 31/12/2021 [in £000s]

|  |  |  |
| --- | --- | --- |
| Purchases and Sales | 700 | 1140 |
| Inventory 1/1/2021 | 50 |  |
| Receivables and payables | 87 | 70 |
| Selling & distribution expenses | 50 |  |
| Rent, rates and insurance | 40 |  |
| Staff salaries | 100 |  |
| Advertising | 20 |  |
| Gas & electricity | 25 |  |
| Audit fee | 10 |  |
| Bad debt | 4 |  |
| Directors’ remuneration | 34 |  |
| Debenture interest | 10 |  |
| Interest on bank loan | 7 |  |
| Cash | 4 |  |
| Bank | 9 |  |
| Premises at cost | 500 |  |
| Equipment at cost | 130 |  |
| Equipment – accumulated depreciation |  | 30 |
| Furniture & fittings at cost | 100 |  |
| Furniture & fittings – accumulated depreciation |  | 60 |
| £1 Ordinary share capital |  | 350 |
| 7% Long term bank loan |  | 100 |
| 11% Debentures |  | 100 |
| Share premium |  | 20 |
| Retained profits |  | 30 |
| Interim ordinary dividend | 20 |  |
| Totals | 1900 | 1900 |

**Additional information as at 31/12/2021**:

* Inventory was valued at £80,000.
* Rent prepaid £4000; Distribution expenses prepaid £3000;
* Accruals for rates £1000; Gas & electricity £1000; Audit fee £2000
* Debenture interest to be accrued
* The equipment to be depreciated by 20% on reducing balance
* The furniture & fittings to be depreciated by 20% on straight line.
* The directors wish to provide £26,000 for taxation.
* The directors propose a final ordinary dividend of 7p per share.

**Required:**

**a) Income Statement for the year ended 31/12/2021. [20 marks]**

**b) Statement of Financial Position as at 31/12/2021. [20 marks]**

**Section B: Attempt ANY Two questions – 30 marks each**

**Question 2**.

M plc requires your advice on the following investment potential to expand in Scotland. Its market research team has made the following five-year forecasts for the product to be produced and sold there.

* New equipment costing £150,000 (year 0) will be required immediately. This will have a residual value of £40,000 in year 5.
* The product’s selling price and variable costs are expected to be £25 per unit and £15 per unit respectively over the 5 years.
* Incremental fixed costs per annum specific to this investment potential is estimated to be £75,000 over the investment period.
* Sales volume in year 1 is expected to be 10,000 units. Forecasts for the remaining 4 years are: 12,000 units in year 2; 15,000 units in year 3; 14,000 units in year 4; 11,000 units in year 5.
* M plc’s cost of capital is 10 % and the payback required for the investment is 3 years.
* Discount factors @ 10 % are as follows:

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
| Year | 1 | 2 | 3 | 4 | 5 |
| Discount factors @ 10 % | 0.909 | 0.826 | 0.751 | 0.683 | 0.621 |

**Required for the above investment proposal:**

**a) The relevant annual cash flows for the proposal. [6 marks]**

**b) Payback and Net Present Value (NPV). [6 marks]**

**c) Advice the company. [5 marks]**

**d) State five other factors that require consideration before a final decision is**

**made.** **[5 marks]**

**e) The company’s finance director confidently stated that the proposal’s IRR would be “well over 10 % for the investment.” Explain what IRR is and why the finance director was so confident that the IRR would be well in excess of 10 %.** **[5 marks]**

**f) State the advantages of IRR. [3 marks]**

**Question 3**.

The latest financials [in £000s] of R plc are provided below.

|  |  |  |
| --- | --- | --- |
| Year ended 31st March | 2022 | 2021 |
| Sales | 120 | 105 |
| Gross profit | 50 | 45 |
| Profit before tax | 10 | 12 |

|  |  |  |
| --- | --- | --- |
| SOFP as at 31st March | 2022 | 2021 |
| Current assets: |  |  |
| Inventory | 14 | 10 |
| Receivables | 16 | 21 |
| Cash | 2 | 3 |
|  |  |  |
| Current liabilities: |  |  |
| Payables | 12 | 13 |
| Bank overdraft | 5 | 4 |
| Dividends | 7 | 7 |
| Corporation tax | 3 | 5 |

**Required:**

**a) Calculate the following ratios for both years: [14 marks]**

* **Gross profit ratio**
* **Net profit ratio [using profit before tax]**
* **Current ratio**
* **Quick ratio**
* **Inventory holding period in days**
* **Receivables ratio**
* **Payables ratio**

**b) Comment on the performance of the company over the two years using the above ratios [16 marks]**

**Question 4**

Salah Enterprises Ltd produces and sells a variety of frozen burgers and pizzas. One of these is a vegan pizza and the following relate to this product.

In the year ended 30/04/2022, the company sold 50,000 pizzas. The selling price was £5 per unit and its unit variable costs was £2. The annual fixed costs specific for this product line is £36,000.

For the next accounting year to 30/04/2023, the company expects to increase its selling price to £6 in an attempt to improve profitability. The annual fixed costs would increase by 5%. The company expects to reduce the variable costs by 20%. The sales volume is expected to remain the same at 50,000 pizzas.

**Required:**

**a) The profit for the year ended 30/04/2022. [6 marks]**

**b) The contribution to sales ratio for the year ended 30/04/2023. Explain the significance of your answer. [6 marks]**

**c) Prepare a statement to show the expected total contribution and the resulting net profit or loss for the year ended 30/04/2023. [7 marks]**

**d) The breakeven sales and margin of safety for the year ended 30/04/2023.**

**[6 marks]**

**e) State the limitations of breakeven analysis as an aid to decision-making.**

**[5 marks]**

**END OF EXAMINATION PAPER**

**[You should have answered Question 1 and any 2 other questions.]**