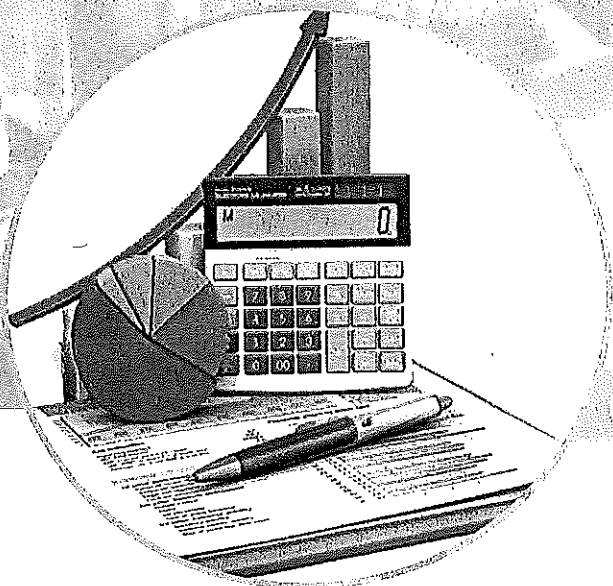


ACCOUNTING
Grade 12
REVISION BOOKLET



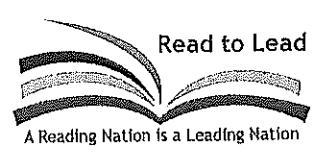
ACCOUNTING

CASH FLOW STATEMENT

GRADE 12



basic education
Department:
Basic Education
REPUBLIC OF SOUTH AFRICA



Foreword

In order to improve learning outcomes the Department of Basic Education conducted research to determine the specific areas that learners struggle with in Grade 12 examinations. The research included a trend analysis by subject experts of learner performance over a period of five years as well as learner examination scripts in order to diagnose deficiencies or misconceptions in particular content areas. In addition, expert teachers were interviewed to determine the best practices to ensure mastery of the topic by learners and improve outcomes in terms of quality and quantity.

The results of the research formed the foundation and guiding principles for the development of the booklets. In each identified subject, key content areas were identified for the development of material that will significantly improve learner's conceptual understanding whilst leading to improved performance in the subject.

The booklets are developed as part of a series of booklets, with each booklet focussing only on one specific challenging topic. The selected content is explained in detail and include relevant concepts from Grades 10 - 12 to ensure conceptual understanding.

The main purpose of these booklets is to assist learners to master the content starting from a basic conceptual level of understanding to the more advanced level. The content in each booklets is presented in an easy to understand manner including the use of mind maps, summaries and exercises to support understanding and conceptual progression. These booklets should ideally be used as part of a focussed revision or enrichment program by learners after the topics have been taught in class. The booklets encourage learners to take ownership of their own learning and focus on developing and mastery critical content and skills such as reading and higher order thinking skills.

Teachers are also encouraged to infuse the content into existing lesson preparation to ensure in-depth curriculum coverage of a particular topic. Due to the nature of the booklets covering only one topic, teachers are encouraged to ensure learners access to the booklets in either print or digital form if a particular topic is taught.

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1. How to use this study guide

The main intention of this study guide is to address challenges with specific areas of subject content that was poorly answered in past NSC papers. This is informed by the detailed analysis done on each question and the findings that were provided in the Diagnostic Report.

The material presented in this booklet focuses on the progression and content overlap across the FET phase, as illustrated in the table below.

Field	Grade 12	Grade 10 & 11
Financial	<p>Companies</p> <ul style="list-style-type: none"> • Concepts and bookkeeping • Financial Statements • Cash Flow, Ratios (analysis and interpretation) <p>Reconciliations analysis Bank, Debtors and Creditors VAT</p>	<p>Bookkeeping (sole trader)</p> <ul style="list-style-type: none"> • Adjustments • Financial Statements • Ratios/Interpretation <p>Reconciliations <i>prepare</i> VAT concepts and calculations</p>
Managerial	<p>Manufacturing concerns</p> <ul style="list-style-type: none"> • Production Cost Statement • Unit cost calculations and break-even analysis <p>Budgeting (analysis)</p> <ul style="list-style-type: none"> • Projected Income Statement • Cash Budget 	<p>Manufacturing</p> <ul style="list-style-type: none"> • Concepts and ledger accounts • Break-even analysis <p>Budgeting (prepare)</p> <ul style="list-style-type: none"> • Concepts and preparation • Basic calculations
Managing Resources	<ul style="list-style-type: none"> • Stock valuation FIFO, weighted average and specific identification • Fixed asset management (analysis) • Auditing, internal controls and ethics 	<ul style="list-style-type: none"> • Stock (clubs) Perpetual and periodic • Fixed assets (prepare) Depreciation, disposal • Auditing, internal controls and ethics

It is important to first address prior knowledge (concepts, calculations), before moving to the more challenging matters of analysing, interpreting and commenting. The next logical step is to tackle examination type questions with the knowledge that all questions will cater for the different cognitive levels.

This study guide provides:

- Notes on simple definitions, explanations, formulae and short-cuts (handy hints).
- Focus-activities to test specific skills.
- Application activities in the form of examination-type questions.
- Adapted questions from past examination papers.

Plan of action:

- Master the basic skills by using this manual, together with all other resources, if more practice is needed.
- Test your knowledge by attempting to do some examination questions.
- Make a note of your shortcomings and go back to the drawing board.

2. Study and Examination Tips

Know the paper: General structure and layout

- One 3-hour paper for 300 marks;
- The paper consists of 6 compulsory questions; the marks per question range from 30 to 80 marks. Each question will comprise a number of sub-questions that are set at different cognitive levels.
- The content covered must conform to the requirements of CAPS, as follows:

Financial Accounting	50% - 60%	150 – 180 marks
Managerial Accounting	20% - 25%	60 – 75 marks
Managing Resources	20% - 25%	60 – 75 marks

The trend in past papers was as follows:

- Question 1, 2 and 6 are generally shorter questions (30 – 45 marks).
- Question 3 and 4 are generally longer questions, comprising Financial Statements and the Cash Flow Statement.
- The question paper comes with a specially prepared ANSWER BOOK, which means you can answer the questions in any order.

Strategy:

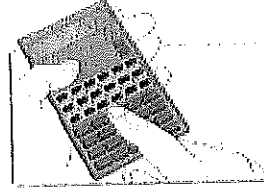
- ✓ **Cash Flow Statement** is part of Financial Accounting. Together with Income Statement, Balance sheet and Notes to the Financial Statement, it must constitute 50% – 60% of the paper.
- ✓ Past trends show that it is normally Question 4 or 5 and is 60 – 75 marks, together with analysis and interpretation.
- ✓ Examiners will sometimes ask you to complete the Cash Flow Statement, calculate some figures (like Tax Paid) and prepare some parts of the Cash Flow Statement. The past trend shows that it is seldom that you will be asked to do a full Cash Flow Statement.
(Detailed explanations are provided in Section 5 of this document).
- ✓ The Cash Flow Statement requires good knowledge and understanding of the principles of Inflows and Outflows, i.e. how these affect the cash movement in the company.
- ✓ These skills are developed in Grade 10, where Cash Receipts Journal (Inflow) and Cash Payments Journal (Outflow) are introduced
- ✓ Knowledge of the company as a form of ownership is important to understand the changes from other forms.

3. Overview of the Topic

LAYOUT - CASH FLOW STATEMENT

CASH FLOW FROM :

OPERATING ACTIVITIES



INVESTING ACTIVITIES

FINANCING ACTIVITIES

NET CHANGE IN CASH AND CASH EQUIVALENTS

4. What is a Cash Flow Statement?

A Cash Flow Statement (CFS) is one of the three key financial statements that reports the cash generated and spent during a specific period of time. The CFS acts as a bridge between the Income Statement and Balance Sheet, by showing how money moved in and out of the business.

The basic format of the CFS is provide below and please note that an outflow of cash will be shown in brackets to indicate a negative effect on cash:

CASH FLOW STATEMENT FOR THE YEAR ENDING	
Cash effect of operating activities	XX
Cash effects of investing activities	XX
Cash effects of financing activities	XX
Net change in cash and cash equivalents	XX
Cash and cash equivalents at the beginning of the year	XX
Cash and cash equivalents at the end of year	XX

Special notes:

- ← Should be positive at all times if the company is successful.
- ← Depends on decisions made by the directors.
- ← Depends on decisions made by the directors.
- ← Depends on the above points.
- ← A positive total will improve the liquidity of the company.

4.1 Cash effect from Operating Activities

Information:	
Extract from the Income Statement for the year ended 28 February 2018	
Net profit before tax	300 000
Income tax	135 000
Interest on loan	92 000
Depreciation	120 000

Extract from the Balance Sheet on 28 February 2018		
	2018	2017
Trading stock	600 000	520 000
Trade and other receivables	230 000	286 000
Trade and other payables	300 000	272 000
SARS (income tax)	12 000	16 000
Shareholders for dividends	60 000	45 000

Operating activities are the main income-earning activities of a company. They are directly related to the main objective of a company and must be considered in a broad sense. The cash generated by operating activities is perhaps the most significant indicator of a company's success, because this relates to the main purpose of establishing the company. **Examples of operating activities are:** buying and selling stock; paying creditors; receiving payment from debtors; paying all the expenses, e.g. wages, salaries, telephone, motor vehicle expenses; paying SARS the tax due; paying shareholders a dividend.

The items in the CFS are not cash flows, but "reasons why cash flow is different from profit."

Depreciation expense is a non-cash item that reduces profit, but does not impact cash flow. Hence, it is added back.

If the starting point profit is above interest and tax in the income statement, then interest and tax cash flows will need to be deducted if they are to be treated as operating cash flows.

CASH FLOW STATEMENT FOR THE YEAR ENDED		
Cash flow from operating activities		?
Cash generated from operations	Note 1	?
Interest paid		(?)
Dividends paid		(?)
Taxation paid		(?)
Cash flow from investing activities		XXX
Cash flow from financing activities		XXX
Net change in cash and cash equivalents		XXX
Note 1: Cash generated from operations		
Net profit for the year	xxx	← Start with this figure from IS.
+ Depreciation	xxx	← Add back non-cash item.
+ Interest expense	xxx	← Add back non-operating expense.
Sub-total	xxx	
Net change in working capital	xxx	
(Increase) / Decrease in inventory	xxx	← These amounts can be with or without brackets, depending on the effect on the cash of the business, i.e. whether there was an inflow or outflow of cash.
(Increase) / Decrease in receivables	xxx	
Increase / (Decrease) in payables	xxx	
Cash generated from operations	xxx	← This figure will be used in the CFS.

Example:

Information:	
Extract from the Income Statement for the year ended 28 February 2018	
Net profit before tax	300 000
Income tax	135 000
Interest on loan	92 000
Depreciation	120 000

Extract from the Balance Sheet on 28 February 2018		
	2018	2017
Trading stock	600 000	520 000
Trade and other receivables	230 000	286 000
Trade and other payables	300 000	272 000
SARS (income tax)	12 000	16 000
Shareholders for dividends	60 000	45 000

Total dividends for the year amounts to R100 000, as per the note to Retained Income.

Solution

Note 1: Cash generated from operations	
Net Profit <i>before tax</i>	300 000
Add: Depreciation	120 000
Add: Interest expense	92 000
Sub-total	512 000
Net changes in working capital	(4 000)
Change in inventory	(80 000)
(600 000 – 520 000) - outflow	
Change in receivables	56 000
(286 000 – 230 000) - inflow	
Change in payables	28 000
(300 000 – 272 000) - inflow	
Cash generated from operations	508 000

We can use the following table to calculate dividends paid and tax paid:

	Taxation
Amount in financial statements	135 000
+ Amount owing at beginning of year	16 000
- Amount owing at end of year	(12 000)
= Amount paid	139 000

	Dividends
Amount in financial statements	100 000
(Total dividends for the year)	
+ Amount owing at beginning of year	45 000
- Amount owing at end of year	(60 000)
= Amount paid	85 000

CASH FLOW STATEMENT FOR THE YEAR ENDING	
Cash flow from operating activities	225 000
Cash generated from operations	Note 1 508 000
Interest paid	(92 000)
Dividends paid (100 000 + 45 000 – 60 000)	(85 000)
Taxation paid (135 000 + 16 000 – 12 000)	(139 000)

Let us practice

The information relate to Dean Ltd for the year ended 28 February 2018.

REQUIRED:

- Complete the note for "Cash generated from operations".
- Complete the section on "Cash flow from operating activities".

INFORMATION:

A. Extract from the Income Statement for the year ended February 2018:

Interest expense	R12 500
Depreciation	R29 000
Income Tax (30% of Net Profit before tax)	R87 000

B. Extract from the Balance Sheet:

	2018	2017
Inventory		
Trading stock	R200 000	R230 000
Consumable stores on hand	R3 000	R5 000
	R203 000	R235 000
Trade and other receivables		
Trade debtors	R41 000	R25 000
Prepaid expenses	R1 500	R1 500
	R42 500	R26 500
Trade and other payables		
Trade creditors	R35 000	R46 500
Shareholder dividends	R110 000	R54 000
SARS (income tax)	R8 500	R5 000
Accrued expenses	R4 000	R5 500
Income received in advance	R3 500	R7 500
	R161 000	R118 500

C. The Retained Income note showed total ordinary share dividends of R180 000.

Note 1: Cash generated from operations	
Net Profit <i>before tax</i>	
Add: Depreciation	
Add: Interest expense	
Sub-total	
Net changes in working capital	
Change in inventory	
Change in receivables	
Change in payables	
Cash generated from operations	

CASH FLOW STATEMENT FOR THE YEAR ENDING	
Cash flow from operating activities	
Cash generated from operations	Note 1
Interest paid	
Dividends paid	
Taxation paid	

Solution

Note 1: Cash generated from operations	
Net Profit <i>before tax</i>	290 000
Add: Depreciation	29 000
Add: Interest expense	12 500
Sub-total	331 500
Net changes in working capital	(1 000)
Change in inventory (235 000 – 203 000) - inflow	32 000
Change in receivables (42 500 – 26 500) - outflow	(16 000)
Change in payables (59 500 – 42 500) - outflow	(17 000)
Cash generated from operations	330 500

CASH FLOW STATEMENT FOR THE YEAR ENDING	
Cash flow from operating activities	110 500
Cash generated from operations	Note 1
Interest paid	(12 500)
Dividends paid (54 000 + 70 000)	(124 000)
Taxation paid (87 000 + 5 000 – 8 500)	(83 500)

4.2 Cash Flow from Investing Activities

Investing activity involves the establishment of the infrastructure of a company in order for it to be in a position to earn income. **Examples of investing activities include:** investing in land and buildings (e.g. shop premises, which results in earning income because of having a place for customers to buy goods or services); fixed deposit (generates income through interest).

CASH FLOW STATEMENT FOR THE YEAR ENDING	
Cash flow from operating activities	XXX
Cash flow from investing activities	?
<i>Purchase of fixed assets</i>	<i>?</i>
<i>Proceeds from sale of assets</i>	<i>?</i>
<i>Increase / Decrease in investments</i>	<i>?</i>
Cash flow from financing activities	XXX
Net change in cash and cash equivalents	XXX
Cash and cash equivalents at beginning of year	XXX
Cash and cash equivalents at end of year	XXX

Use the following format to identify changes to fixed assets (summary of note):

FA = Fixed Assets; BS = Balance Sheet; IS = Income Statement.

FA at beginning of year	XXX	← This figure comes from the BS Year 1.
+ FA purchased	Add: XXX	← You will be able to calculate one of these figures as a missing figure needed for the preparation of the CFS.
- FA sold (at book value)	Less: XXX	
- Depreciation for the year	Less: XXX	← This figure comes from the IS.
= FA at end of year	XXX	← This figure comes from the BS - Year 2.

*Can be shown in the form of an equation.

Example:

You are provided with the following information from the financial statements.

Complete the appropriate extract from the Cash Flow Statement.

NON-CURRENT ASSETS

Fixed Assets
Investment in fixed deposit

	Year 2	Year 1
	770 000	480 000
	650 000	430 000
	120 000	50 000

Note:

- The Income Statement reflects depreciation of R35 000.
- Fixed assets were sold at carrying value for R22 000.

Solution:

Calculate the amount for fixed assets purchased, as follows:

Fixed assets at beginning of year	430 000
+ Fixed assets purchased	<i>missing figure</i>
- Fixed assets sold (carrying value)	(22 000)
- Depreciation	(35 000)
- Fixed assets at end of year	650 000

Calculation of the missing figure:

Extract from Cash Flow Statement

Cash flow from investing activities	net cash outflow	(325 000)
Purchase of fixed assets	outflow	(277 000)
430 000 – 22 000 – 35 000 – 650 000		
Proceeds from sale of assets	inflow	22 000
Increase / Decrease in investments		(70 000)
(120 000 – 50 000) outflow		

Let's practice

You are provided with the following information from the financial statements.

Complete the extract from the Cash Flow Statement.

	2017	2016
NON-CURRENT ASSETS	323 000	505 000
Fixed Assets	83 000	205 000
Investment in fixed deposit	240 000	300 000

Note:

- The income statement reflects depreciation of R44 000.
- Fixed assets of R52 000 were bought during the 2017 financial period.

Answer

Cash flow from investing activities	
Purchase of fixed assets	
Proceeds from sale of assets	
Decrease in investments	

Solution:

Cash flow from investing activities	net cash outflow	138 000
Purchase of fixed assets	outflow	(52 000)
Proceeds from sale of assets	inflow	130 000
<i>(205 000 + 52 000 – 44 000 – 83 000)</i>		
Decrease in investments		60 000)
<i>(300 000 – 240 000)</i>		inflow

4.3 Cash Flow from Financing Activities

Financing activities are the activities involved in funding the infrastructure of the company. They result in a change in the size and composition of the debt and the capital funding. **Examples of financing activities include:** new issue of shares; repurchasing of shares; raising a loan; repayment of a loan.

CASH FLOW STATEMENT FOR THE YEAR ENDING	
Cash flow from operating activities	XXX
Cash flow from investing activities	XXX
Cash flow from financing activities	?
<i>Proceeds from shares issued</i>	<i>?</i>
<i>Repurchasing of shares</i>	<i>?</i>
<i>Loans received/repaid</i>	<i>?</i>
Net change in cash and cash equivalents	XXX
Cash and cash equivalents at beginning of year	XXX
Cash and cash equivalents at end of year	XXX

Example

Study the given information to complete the table that follows.

	Year 2	Year 1
SHAREHOLDERS' EQUITY	XXX	XXX
Ordinary share capital	1 579 500	900 000
Retained income	XXX	XXX
NON-CURRENT LIABILITIES	330 000	210 000
Loans	330 000	210 000

Note:

- At the end of Year 1, there were 150 000 shares in issue.
- During Year 2, 100 000 shares were issued at a price of R8,55 per share.
- During Year 2, 25 000 shares were repurchased from a disgruntled shareholder at a price of R12,00 each.

CASH FLOW STATEMENT FOR YEAR ENDED.....	
Cash effects of operating activities	XXX
Cash effects of investing activities	XXX
Cash effects of financing activities inflow	675 000
Proceeds of shares issued	855 000
100 000 shares x R8,55 per share inflow	
Shares repurchased	(300 000)
25 000 shares x R12,00 per share (outflow)	
Loans received/repaid	120 000
(330 000 – 210 000) inflow	
Net change in cash & cash equivalents	XXX
Cash & cash equivalents at beginning of year	XXX
Cash & cash equivalents at end of year	XXX

Explanations

Proceeds of shares issued:

You can't just subtract the figures of year 1 from year 2 to get this figure. You must read the additional information to determine how many shares were issued during the year and at what price.

In some instances, you must be able to complete the note of Ordinary Share Capital in the financial statements to calculate this figure.

Shares Repurchased:

This is the total amount that the business has paid to repurchase the shares from shareholders.

If you are only given the above average amount per share, you must calculate the average price of these shares on the day of repurchasing and add the above average amount, then multiply by the number of shares repurchased.

Let's practice

Use the given information to complete the table that follows, by substituting the "?" with the correct figures.

You are provided with the following information from the financial statements:

	Year 2	Year 1
SHAREHOLDERS' EQUITY	XXX	XXX
Ordinary share capital	1 575 000	2 800 000
Retained income	XXX	XXX
NON-CURRENT LIABILITIES	870 000	1 590 000
Loans	870 000	1 590 000

Note:

- At the end of Year 1, there were 200 000 shares in issue.
- During Year 2, one of the shareholders passed away. The directors decided to buy-back his 50 000 shares at R1,50 above the average price.
- No further shares were issued during the year.

Answer

CASH FLOW STATEMENT FOR YEAR ENDED.....	
Cash effects of operating activities	XXX
Cash effects of investing activities	XXX
Cash effects of financing activities	?
Proceeds of shares issued	?
Shares repurchased	?
Loan received/repaid	?
Net change in cash & cash equivalents	XXX
Cash & cash equivalents at beginning of year	XXX
Cash & cash equivalents	XXX

Solution:

CASH FLOW STATEMENT FOR YEAR ENDED.....	
Cash effects of operating activities	XXX
Cash effects of investing activities	XXX
Cash effects of financing activities	(1 495 000)
Proceeds of shares issued	0
Shares repurchased $2800\ 000/200\ 000 = R14 + R1,50 =$ ($R15,5 \times 50\ 000$)	(775 000)
Loan received/repaid ($1590\ 000 - 870\ 000$)	(720 000)
Net change in cash & cash equivalents	XXX
Cash & cash equivalents at beginning of year	XXX
Cash & cash equivalents	XXX

4.4 Cash and Cash Equivalents (Balance Sheet note)

Cash: Cash on hand (Petty cash and cash float)

Cash equivalents: Includes cash held as bank deposits in the current account, deposits in a savings account (short term investments) and short-term maturities (fixed deposits that will mature within the next 12 months).

CASH FLOW STATEMENT FOR THE YEAR ENDING	
Cash effect of operating activities	XXX
Cash effect of investing activities	XXX
Cash effect of financing activities	XXX
Net change in cash and cash equivalents	XXX
Cash and cash equivalents at beginning of year	XXX
Cash and cash equivalents at end of year	XXX

Example 1 - (an increase in cash balances - inflow)

	2017	2016
Current assets	xxx	Xxx
Inventory	xxx	Xxx
Trade and other receivables	xxx	Xxx
Cash and cash equivalents	48 200	18 600

Solution (Example 1)

Complete the appropriate section in the Cash Flow Statement	
Net change in cash and cash equivalents (48 200 – 18 600) – an inflow of cash	29 600 [#]
Cash and cash equivalents at beginning of year	18 600
Cash and cash equivalents at end of year	48 200

Note that an inflow of cash constitutes an amount without brackets.

Example 2 - (a decrease in cash balances - outflow)

	2017	2016
Current assets	XXX	XXX
Inventory	XXX	XXX
Trade and other receivables	XXX	XXX
Cash and cash equivalents	13 700	135 800

Solution (Example 2)

Complete the appropriate section in the Cash Flow Statement	
Net change in cash and cash equivalents (135 800 – 13 700) – an outflow of cash	(122 100) ^{##}
Cash and cash equivalents at beginning of year	135 800
Cash and cash equivalents at end of year	13 700

Note that an outflow of cash constitutes an amount between brackets.

Example 3 - (what to do in the case of an overdraft)

You are provided with the following information from the financial statements:

	Year 2	Year 1
Current Assets	xxx	xxx
Inventories	xxx	xxx
Trade & other receivables	xxx	xxx
Cash & cash equivalents	6 000	9 000
	Year 2	Year 1
Current Liabilities	xxx	xxx
Bank overdraft	xxx	180 000
Trade & other payables	xxx	xxx

Complete <i>the appropriate section</i> in the Cash Flow Statement	
Net change in cash and cash equivalents $(171\ 000 + 6\ 000)$ - inflow	177 000###
Cash and cash equivalents at beginning of year $(-180\ 000 + 9\ 000)$	(171 000)
Cash and cash equivalents at end of year	6 000

We must first deposit the R171 000 to make the bank balance R0, and then a further R6 000, i.e. $(R171\ 000 + R6\ 000 = R177\ 000)$.

Let us practice 1: You are provided with the following information:

	Year 2	Year 1
CURRENT ASSETS	XXX	XXX
Inventories	XXX	XXX
Trade & other receivables	XXX	XXX
Cash & cash equivalents	225 000	90 000

Complete the following by providing a figure in each cell indicated with a "?"

CASH FLOW STATEMENT FOR YEAR ENDED....	
Cash effect of operating activities	XXX
Cash effect of investing activities	XXX
Cash effect of financing activities	XXX
Net change in cash and cash equivalents	?
Cash and cash equivalents at beginning of year	?
Cash and cash equivalents at end of year	?

CASH FLOW STATEMENT FOR YEAR ENDED....	
Cash effect of operating activities	XXX
Cash effect of investing activities	XXX
Cash effect of financing activities	XXX
Net change in cash and cash equivalents	135 000
Cash and cash equivalents at beginning of year	90 000
Cash and cash equivalents at end of year	225 000

Let us practice 2

Refer to the given information and complete the table below by substituting each "?" with the correct figure.

	Year 2	Year 1
CURRENT ASSETS	xxx	xxx
Inventories	xxx	xxx
Trade & other receivables	xxx	xxx
Cash & cash equivalents	18 000	27 000
	Year 2	Year 1
CURRENT LIABILITIES	XXX	XXX
Bank overdraft	xxx	147 000
Trade & other payables	xxx	xxx

CASH FLOW STATEMENT FOR THE YEAR ENDED.....	
Cash effect of operating activities	XXX
Cash effect of investing activities	XXX
Cash effect of financing activities	XXX
Net change in cash & cash equivalents	?
Cash & cash equivalents at beginning of year	?
Cash & cash equivalents at end of year	?

CASH FLOW STATEMENT FOR THE YEAR ENDED.....	
Cash effect of operating activities	XXX
Cash effect of investing activities	XXX
Cash effect of financing activities	XXX
Net change in cash & cash equivalents	(102 000)
Cash & cash equivalents at beginning of year (147 000 – 27 000)	120 000
Cash & cash equivalents at end of year	18 000

4.5 Activities

ACTIVITY1: CASH FLOW STATEMENT

The following information was obtained from the accounting records of DBE Ltd on 31 December 2018, which is its financial year-end. The company has an authorised share capital of 750 000 ordinary shares.

REQUIRED:

- 1.1 Complete the Cash Flow Statement for the year ended 31 December 2018. Show all workings to obtain part-marks.

(27)

INFORMATION:

A. Extract from the Income Statement for the year ended 31 December 2018:

Interest on loan	27 000
Interest on overdraft	380
Depreciation	58 000
Income tax	23 000
Net profit before income tax	100 000

B. Information from the Balance Sheet:

	2018 R	2017 R
Ordinary share capital	678 000	440 000
Retained income	73 000	56 000
Loan: TK Bank	130 000	170 000
Fixed assets (carrying value)	549 000	420 000
Inventory	61 000	73 000
Trade and other receivables	214 320	150 600
Bank (favourable)	30 130	-
Bank overdraft	-	10 000
Cash float	1 000	1 000
Trade and other payables	158 400	152 550
SARS: Income tax*	4 000 (Dr)	10 000 (Cr)
Shareholder dividends*	28 000	22 000

*Included above in Trade and other receivables and Trade and other payables.

- C. Total dividends for the year amounted to R60 000.
 D. New equipment was purchased, and a vehicle was sold during the year, at its carrying value of R17 000.
 E. Shares to the value of R400 000 were repurchased during the year. This transaction was recorded.

ACTIVITY 2

You are provided with information from the records of Pretoria Ltd for the financial year ended 29 February 2016. This is a public company listed on the JSE.

REQUIRED:

- 2.1 Calculate the missing figures indicated by **A to F** on the Cash Flow Statement. Show workings to earn part-marks.

INFORMATION:

- A. The company was registered with an authorised share capital of 1 000 000 ordinary shares.

On 29 February 2016, after all movements to the share capital account were recorded, the issued share capital comprised 625 000 ordinary shares.

- B. Information extracted from the Income Statement on 29 February 2016:

Sales	6 200 000
Depreciation	425 000
Interest on loan	188 000
Net profit before tax	1 600 000
Net profit after tax	1 120 000

- C. Information extracted from the Balance Sheet:

	2016	2015
Fixed Assets (carrying value)	7 350 000	6 931 000
Current Assets	610 000	422 000
Inventories	235 000	90 000
Trade and other receivables	262 000	330 000
SARS (Income tax)	14 000	-
Cash and cash equivalents	99 000	2 000
TOTAL ASSETS	7 960 000	7 353 000
Shareholders' Equity	5 503 000	4 023 000
Ordinary share capital	4 700 000	3 800 000
Retained income	803 000	223 000
Non-current Liabilities: Venus Bank	2 100 000	2 800 000
Current Liabilities	357 000	530 000
Trade and other payables	132 000	180 000
SARS (Income tax)	-	28 000
Shareholder dividends	225 000	200 000
Bank overdraft	-	122 000
TOTAL EQUITY AND LIABILITIES	7 960 000	7 353 000

- D. 150 000 new shares were issued during the year, at R8 each.
- E. On 26 February 2016, the company bought back 57 500 shares from disgruntled shareholders, at 600 cents each.
- F. An interim dividend of R270 000 was paid on 30 June 2015.
- G. Fixed assets were sold during the year, at a carrying value of R86 000. Additional equipment was purchased to replace the assets sold.
- H. **CASH FLOW STATEMENT FOR YEAR ENDED 29 FEBRUARY 2016**

CASH EFFECT OF OPERATING ACTIVITIES	
Cash generated from operations	
Interest paid	A
Income tax paid	B
Dividends paid	C
CASH EFFECT OF INVESTING ACTIVITIES	
Fixed assets purchased	D
Proceeds from sale of fixed assets	E
CASH EFFECT OF FINANCING ACTIVITIES	
Proceeds of shares issued	F
Repurchase of shares	G
Increase/ Decrease in loans	H
NET CHANGE IN CASH AND CASH EQUIVALENTS	I
Cash and cash equivalents at beginning of year	J
Cash and cash equivalents at end of year	K

ACTIVITY 3

The information below was extracted from the books of Mpumalanga Ltd. Study the information and answer the questions that follow.

REQUIRED:

- 3.1 Prepare the reconciliation between net profit before tax and cash generated from operations. (Show workings in brackets)
- 3.2
 - 3.2.1 Calculate the figure for Income Tax that appeared in the Cash Flow Statement on 30 June 2018.
 - 3.2.2 Calculate the figure for Dividends that appeared in the Cash Flow Statement on 30 June 2018.
- 3.4 Complete the 'Cash Flow from investing activities' section of the Cash Flow Statement on 30 June 2018.
- 3.5 Complete the 'Cash Flow from financing activities' section of the Cash Flow Statement on 30 June 2018.

INFORMATION

1.

EXTRACT FROM THE BALANCE SHEET (Statement of Financial Position) ON 30 JUNE 2015		
	2018	2017
ASSETS		
NON-CURRENT ASSETS		
Fixed assets	1 039 500	774 800
Financial assets	140 000	190 000
CURRENT ASSETS		
Inventory	1 145 000	1 150 000
Trade and other receivables	1 143 000	1 139 000
CAPITAL AND RESERVES		
ORDINARY SHAREHOLDERS' EQUITY	2 500 000	1 285 100
Ordinary share capital	2 160 000	1 200 000
Retained Income	340 000	85 100
LOAN	450 000	970 000
CURRENT LIABILITIES		
Trade and other payables	1 185 000	929 000

2. Notes to the Balance Sheet

(Statement of Financial Position)

	2018	2017
1. FIXED ASSETS	1 039 500	774 800
Land and Buildings	950 000	700 000
Equipment (book value)	89 500	74 800
2. TRADE AND OTHER RECEIVABLES	1 143 000	1 139 000
Debtors' Control	1 115 000	1 130 000
Prepaid Expenses	10 000	9 000
SARS: Income Tax	18 000	-
3. TRADE AND OTHER PAYABLES	1 185 000	929 000
Creditors Control	955 000	850 400
SARS: Income Tax	-	5 000
Shareholders for Dividends	230 000	74 000

ADDITIONAL INFORMATION

3.1 **Ordinary share capital:**

- 1 July 2014: 120 000 shares issued @ R10 each.
- 1 January 2015: 80 000 new shares issued @ R15 each.
(These shares did not qualify for interim dividends.)
- 30 June 2015: repurchased 20 000 shares @ R14 each.

3.2 **Depreciation**

- Total depreciation for the year amounted to R18 500.

3.3 **Sale of equipment**

- Equipment was sold at carrying value of R19 430.

3.4 **Net Profit before tax**

- Net Profit before tax amounted to R625 000.

3.5 **Dividends**

- The interim dividend of 80 cents per share was declared and paid on 3 January 2018. The final dividend was declared on 30 June 2018.

3.6 **Loan**

Interest capitalised for the year was R115 000.

ACTIVITY 4

The following information relates to Tambo Ltd. The financial year ends on 31 May each year.

4.1 CASH FLOW STATEMENT

REQUIRED:

4.1.1 Calculate the following amounts for the Cash Flow Statement:

- Taxation paid (4)
- Dividends paid (4)

4.1.2 Prepare the following note to the Cash Flow Statement:

- Prepare the cash generated from operations (14)

4.1.3 Complete the following from the Cash Flow Statement:

- Cash flow from investing activities (9)
- Cash flow from financing activities (5)
- Net change in cash equivalents (4)

INFORMATION:

A. Share capital and dividends:

Additional shares were issued on 1 November 2016 for R383 000.

The company bought 10 000 shares back from a shareholder on 31 March 2017, at R2,50 per share.

The Interim dividend paid on 30 November 2016 was R72 000.

B. Fixed assets :

- Equipment was disposed of at carrying value during the year.
- New fixed assets were purchased at R680 000 during the year.

C. Extract from the Income Statement for the year ended 31 May 2017:

Depreciation	R135 700
Interest expense	76 500
Income tax	303 880
Net profit before tax	995 900

D. Extract from the Balance Sheet of Celine Ltd. on 31 May 2017

	2017	2016
Fixed assets at carrying value	R1 584 190	R1 101 500
Financial Assets:		
Investments	750 000	960 000
Current assets	376 000	335 400
Inventories	112 000	174 000
Trade and other receivables:	128 000	156 000
Trade debtors	119 600	122 000
SARS: Income tax	8 400	0
Expenses prepaid	0	34 000
Cash and cash equivalents	136 000	5 400
Long-term liabilities: Loan	500 000	580 000
Current liabilities	233 600	479 300
Trade creditors	94 600	144 000
SARS: Income tax	0	33 800
Shareholder dividends	130 000	98 000
Income received in advance	9 000	0
Bank overdraft	0	203 500

ACTIVITY 1 (Answer sheet)

Note 1: Cash generated from operations	
Net Profit <i>before</i> tax	
Add: Depreciation	
Add: Interest expense	
Sub-total	
Net changes in working capital	
Change in inventory	
Change in receivables	
Change in payables	
Cash generated from operations	

1.1 CASH FLOW STATEMENT FOR THE YEAR ENDED 31 DECEMBER 2018

CASH EFFECTS OF OPERATING ACTIVITIES	
Cash generated from operations	
Interest paid	
Dividends paid	
CASH EFFECTS OF INVESTING ACTIVITIES	
Fixed assets purchased	
CASH EFFECTS OF FINANCING ACTIVITIES	
NET CHANGE IN CASH AND CASH EQUIVALENTS	
Cash and cash equivalents at beginning of year	
Cash and cash equivalents at end of year	

27

ACTIVITY 2 (Answer sheet)

2.1

Provide the missing figures indicated by A to F in the Cash Flow Statement. Show workings to earn part-marks.

A	
B	
C	
D	
E	
F	
G	
H	
I	
J	
K	

ACTIVITY 3 (Answer sheet)

MPUMALANGA LIMITED

NOTES TO THE CASH FLOW STATEMENT	
	RECONCILIATION BETWEEN NET PROFIT BEFORE TAXATION AND CASH GENERATED FROM OPERATIONS
	Net Profit before tax
	Adjustment in respect of:
	Depreciation
	Interest on Loan
	Operating profit before change in working capital
	Net change in working capital
	Cash generated from operations

	Calculate the figure for Income Tax that appeared in the Cash Flow Statement on 30 June 2018

	Calculate the figure for Dividends that appeared in the Cash Flow Statement on 30 June 2018

	Cash flow from investing activities	

	Cash flow from financing activities	

ACTIVITY 4

TAMBO LIMITED

4.1 Calculate the following amounts for the Cash Flow Statement:

4.1.1

Taxation paid

--

4

4.1.1

Dividends paid

--

4

4.1.2

Prepare the following note to the Cash Flow Statement

Net profit before tax	995 900
Adjustment for :	
Depreciation	135 700
Interest on loan/expense	
Profit before changes in working capital	
Change in Working capital	
Cash generated from operations	

14

4.1.2	Cash flow from investing activities	

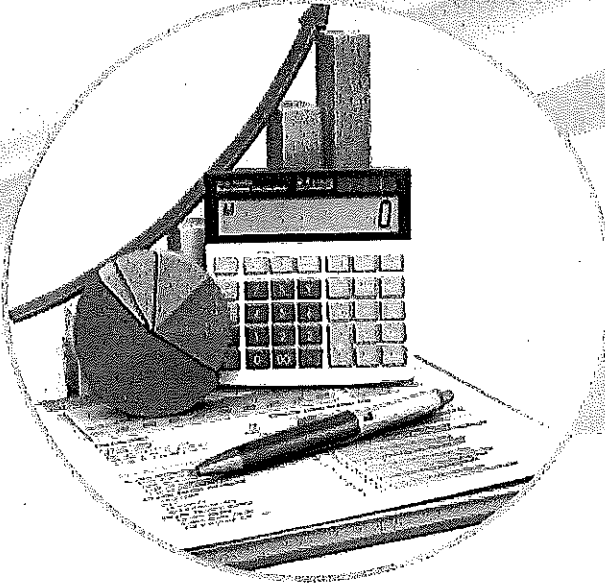
5

4.1.3	Cash flow from financing activities	

5

4.1.4	Net change in cash and cash equivalents	

4



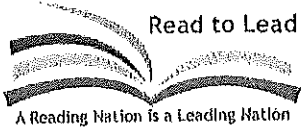
ACCOUNTING

ANALYSIS AND INTERPRETATION OF FINANCIAL INFORMATION

GRADE 12



basic education
Department:
Basic Education
REPUBLIC OF SOUTH AFRICA



Foreword

In order to improve learning outcomes the Department of Basic Education conducted research to determine the specific areas that learners struggle with in Grade 12 examinations. The research included a trend analysis by subject experts of learner performance over a period of five years as well as learner examination scripts in order to diagnose deficiencies or misconceptions in particular content areas. In addition, expert teachers were interviewed to determine the best practices to ensure mastery of the topic by learners and improve outcomes in terms of quality and quantity.

The results of the research formed the foundation and guiding principles for the development of the booklets. In each identified subject, key content areas were identified for the development of material that will significantly improve learner's conceptual understanding whilst leading to improved performance in the subject.

The booklets are developed as part of a series of booklets, with each booklet focussing only on one specific challenging topic. The selected content is explained in detail and include relevant concepts from Grades 10 - 12 to ensure conceptual understanding.

The main purpose of these booklets is to assist learners to master the content starting from a basic conceptual level of understanding to the more advanced level. The content in each booklet is presented in an easy to understand manner including the use of mind maps, summaries and exercises to support understanding and conceptual progression. These booklets should ideally be used as part of a focussed revision or enrichment program by learners after the topics have been taught in class. The booklets encourage learners to take ownership of their own learning and focus on developing and mastery critical content and skills such as reading and higher order thinking skills.

Teachers are also encouraged to infuse the content into existing lesson preparation to ensure in-depth curriculum coverage of a particular topic. Due to the nature of the booklets covering only one topic, teachers are encouraged to ensure learners access to the booklets in either print or digital form if a particular topic is taught.

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1. How to use this booklet

The main intention of this study guide is to address challenges with specific areas of subject content that was poorly answered in past NSC papers. This is informed by the detailed analysis done on each question and the findings that were provided in the Diagnostic Report. The material presented in this booklet focuses on the progression and content overlap across the FET phase, as illustrated in the table below.

Field	Grade 12	Grade 10 & 11
Financial	Companies <ul style="list-style-type: none"> • Concepts and bookkeeping • Financial Statements • Cash Flow, Ratios (analysis and interpretation) • Reconciliations analysis • Bank, Debtors and Creditors • VAT 	Bookkeeping (sole trader) <ul style="list-style-type: none"> • Adjustments • Financial Statements • Ratios/ Interpretation • Reconciliations prepare • VAT concepts and calculations
Managerial	Manufacturing concerns <ul style="list-style-type: none"> • Production Cost Statement • Unit cost calculations and break-even analysis Budgeting (analysis) <ul style="list-style-type: none"> • Projected Income Statement • Cash Budget 	Manufacturing <ul style="list-style-type: none"> • Concepts and ledger accounts • Break-even analysis Budgeting (prepare) <ul style="list-style-type: none"> • Concepts and preparation • Basic calculations
Managing Resources	<ul style="list-style-type: none"> • Stock valuation FIFO, weighted average and specific identification • Fixed asset management (analysis) • Auditing, internal controls and ethics 	<ul style="list-style-type: none"> • Stock (clubs) Perpetual and periodic • Fixed assets (prepare) Depreciation, disposal • Auditing, internal controls and ethics

It is important to first address prior knowledge (concepts, calculations), before moving to the more challenging matters of analysing, interpreting and commenting. The next logical step is to tackle examination type questions with the knowledge that all questions will cater for the different cognitive levels.

This study guide provides:

- Notes on simple definitions, explanations, formulae and short-cuts (handy hints).
- Focus-activities to test specific skills.
- Application activities in the form of examination-type questions.
- Adapted questions from past examination papers.

Plan of action:

- Master the basic skills by using this manual, together with all other resources, if more practice is needed.
- Test your knowledge by attempting to do some examination questions.
- Make a note of your shortcomings and start the process over again until you get the activity right.

STUDY AND EXAMINATION TIPS

KNOW THE PAPER: GENERAL STRUCTURE AND LAYOUT.

- One 3-hour paper for 300 marks;
- The paper consists of 6 compulsory questions; the marks per question range from 30 to 80 marks. Each question will comprise a number of sub-questions that are set at different cognitive levels.
- The content covered must conform to the requirements of CAPS, as follows:

Financial Accounting	50% - 60%	150 - 180 marks
Managerial Accounting	20% - 25%	60 - 75 marks
Managing Resources	20% - 25%	60 - 75 marks

• PAST TREND:

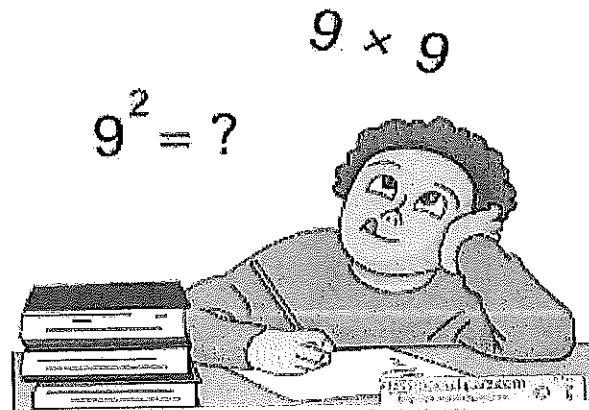
- Question 1, 2 and 6 are generally shorter questions (30 - 45 marks).
- Question 3 and 4 are generally longer questions, comprising Financial Statements and the Cash Flow Statement.
- The question paper comes with a specially prepared ANSWER BOOK, which means you can answer the questions in any order.

• STRATEGY:

- **Analysis and interpretation of financial information** cuts across all three fields of Accounting and constitutes a sizable portion of the marks in the examination paper.
- Past trends show that the topics normally asked in all questions, but it is concentrated on more in questions 3 to 6. The questions require calculations as well as analysis and interpretation.
- Examiners always set this topic and you must be well prepared on all sections of the work. Detailed explanations on this topic are provided in Section 5 of this document.
- The calculations require strong mathematical ability, which is developed over a period of time, starting in Grade 7.
- These skills must include calculating percentages, increases, decreases or specific amounts, using equations.
- Interpretation and analysis requires good comprehension ability.
Be mindful of the language of the paper, and practice using many past papers.

3. OVERVIEW OF ANALYSIS AND INTERPRETATION

USE OF FINANCIAL INFORMATION

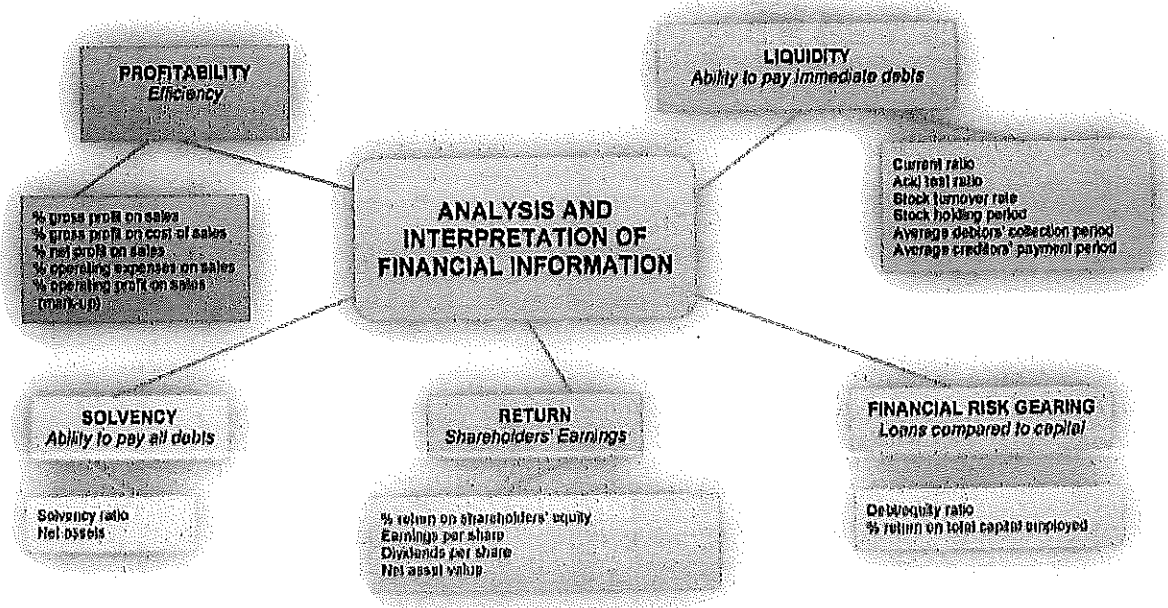


WHAT TO DO

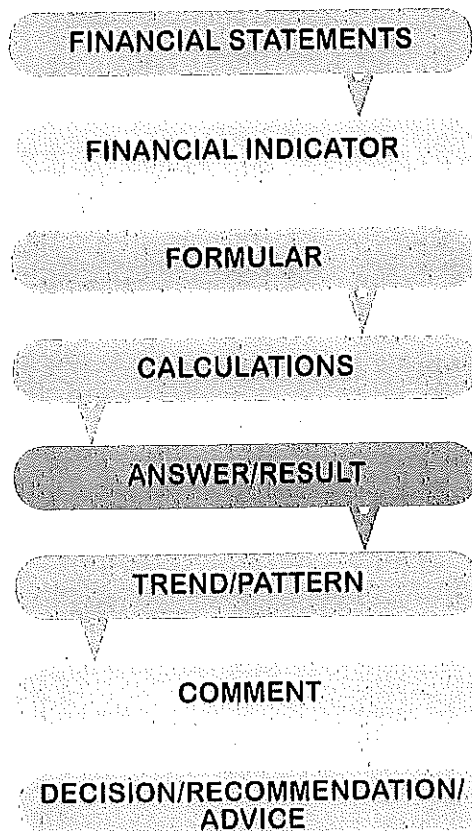
- Identify the relevant financial indicators to comment on specific questions.
- Extract the appropriate information from the financial information given, to calculate financial indicators.
- Understand the requirements of the question, such as comment, give advice, provide the trend, justify his action, etc.
- Be knowledgeable, so that it is easy to work backwards using the given information.
- Don't rely on rote learning or mindless memorising without insight.
- Assess the length of the answer expected by the question.

**PLEASE PAY MORE ATTENTION
FROM NOW ON.**

OVERVIEW OF ANALYSIS AND INTERPRETATION



OVERVIEW OF ANALYSIS AND INTERPRETATION



5. FINANCIAL ANALYSIS AND INTERPRETATION

5.1 CONCEPTS AND RELATED INFORMATION

Q: What is analysis and interpretation?

A: A process that extracts relevant information from a company's Financial Statements, which are interpreted to meet a particular need at a particular point in time.

Q: Why It is done?

A: Financial analysis and interpretation is done to provide information that is useful for the purpose of decision making.

Q: Who uses it?

A:

Users	Reasons
Shareholders	Current and future profitability.
Financial institutions (suppliers of short-term credit)	Will business be able to pay its debt?
Financial institutions (suppliers of long-term credit)	Will business be able to pay a long-term loan and interest?
South African Revenue Services	To know whether the correct tax is paid.
Management	To evaluate their performance.
Customers	To establish the staying power of a business.
Auditors	Does the financial statements fairly present the results of the business?
Employees or unions	Long-term growth prospects to ensure continued employment.

Q: How is it done?

A: Use the information from the Financial Statements to calculate the required ratio.

After calculating, interpret the result by comparing it to:

- Financial indicators of the same business in previous years (meaningful)
- Competitors
- Generally accepted norms and standards

FINANCIAL INDICATORS

AREA OF ANALYSIS	DESCRIPTION	RELATED FINANCIAL INDICATORS
Profitability	How efficient is the company in its normal operating activities?	% gross profit on sales % gross profit on cost of sales % net profit on sales % operating expenses on sales % operating profit on sales (mark-up)
Liquidity	The ability of a company to pay off its immediate (short-term) debts.	Current ratio Acid test ratio Stock turnover rate Stock holding period Average debtors' collection period Average creditors' payment period
Solvency	The ability of a company to pay off all its debts.	Solvency ratio Net assets
Return	Are the shareholders earning a fair amount on their investment?	% return on shareholders' equity Earnings per share Dividends per share Net asset value
Financial risk gearing	To what extent is the company financed by loans (borrowed money) compared to its own capital?	Debt/equity ratio % return on total capital employed
Share price and market prospects	To determine whether the business is in a sound economic/financial position and if it is viewed as an investment opportunity.	Net asset value (NAV) Issue price Share price Average share price Market price (Securities Exchange)

INFORMATION FOR PRACTICE EXERCISES

ZAMA LTD FOR THE FINANCIAL YEAR ENDED 28 FEBRUARY 2018.

INFORMATION:

A. Share Capital

The business has an authorised share capital of 750 000 ordinary shares.
The total issued share capital on 28 February 2018 was 400 000 ordinary shares.
50 000 ordinary shares were issued on 2 March 2017.

B. Extract from the Income Statement on 28 February 2018:

Sales	5 152 000
Cost of sales	3 220 000
Gross profit	1 932 000
Operating income	257 600
Operating expenses	1 004 640
Operating profit	1 184 960
Interest expense	133 960
Net profit before income tax	1 051 000
Income tax	315 300
Net profit after income tax	735 700

C. Information from the Balance Sheet on 28 February

	28/02/2018	28/2/2017
Non-current assets	6 947 700	6 377 400
Fixed assets	6 747 700	6 177 400
Financial assets	200 000	200 000
Current assets	973 200	1 058 700
Inventories	418 000	321 700
Trade debtors	550 000	475 000
Cash and cash equivalents	5 200	262 000
Shareholders' equity	6 224 000	5 058 300
Ordinary share capital	5 827 500	4 960 000
Retained income	396 500	98 300
Non-current liabilities	1 000 000	1 600 000
Current liabilities	696 900	777 800
Trade creditors	411 200	621 600
Shareholders for dividends	220 000	120 000
Bank overdraft	52 200	0

D. An Interim dividend of R180 000 was paid and a final dividend was declared.

E. Credit sales amount to 30% of total sales.
Credit purchases amounted to R2 415 000.

5.2 PROFITABILITY

5.2.1 Gross profit on sales (gross margin)

$$\frac{(\text{Gross Profit})}{\text{Sales}} \times \frac{100}{1} = \%$$

It indicates the percentage by which the total selling price is greater than the cost price.
Decrease in this ratio indicates:

- Pressure on Selling Price as a result of competition.
- Upward pressure on costs as a result of inflation or other cost factors.
- Reduced SP to sell products.

5.2.2 Gross profit on cost of sales (gross mark-up)

$$\frac{\text{Gross Profit}}{\text{Cost of Sales}} \times \frac{100}{1} = \%$$

Mark-up on Cost Price should equal this %; if not, it could be the result of:

- Shrinkage
- Products not correctly marked
- Theft
- Discounts

5.2.3 Net profit on sales (net margin)

$$\frac{\text{Net Profit}}{\text{Sales}} \times \frac{100}{1} = \%$$

- If the ratio is 10%, this means that for every R1 of sales, 10 cents is profit.
- The faster the turnover, the greater the accumulation of 10 cents and the larger the ultimate net profit.

5.2.4 Operating expenses on sales

$$\frac{\text{Operating Expenses}}{\text{Sales}} \times \frac{100}{1} = \%$$

- This indicates how much of the sales price is used to cover running expenses.
- The trend is favourable if this is dropping or at least consistent.

5.2.5 Operating profit on sales

$$\frac{\text{Operating Profit}}{\text{Sales}} \times \frac{100}{1} = \%$$

- Indicates how much of the sales price ends up as profit.
- The trend is favourable if profit is increasing or at least consistent.

LET'S PRACTICE PROFITABILITY RATIOS

Use the practice information on page 7 to calculate the following ratios.
Round off your answers to one decimal point.

- Gross profit percentage on sales
- Operating expenses on sales
- Operating income on sales
- Net profit after tax on sales
- Gross profit percentage

a. **Gross profit percentage on sales**

$$\frac{1932\ 000}{5152\ 000} \times 100 = 37,5\ %$$

b. **Operating expenses on sales**

$$\frac{1004\ 640}{5152\ 000} \times 100 = 19,5\ %$$

c. **Operating income on sales**

$$\frac{1004\ 640}{5152\ 000} \times 100 = 19,5\ %$$

d. **Net profit after tax on sales**

$$\frac{735\ 700}{5152\ 000} \times 100 = 14,3\ %$$

e. **Gross profit percentage**

$$\frac{1932\ 700}{3220\ 000} \times 100 = 14,3\ %$$

5.3 LIQUIDITY RATIOS

5.3.1 Current Ratio

Current Assets: Current Liabilities

- This indicates whether or not the business can meet its short-term obligations.
- It should not be too high, as that means that funds are tied up, instead of being used more effectively.

5.3.2 Acid Test Ratio

Current Assets - Inventory: Current Liabilities

- If this is too low, the business will not be able to meet its short-term obligations.
- It should not be too high, as that will mean that funds are tied up, instead of being used more effectively.

5.3.3 Stock turnover rate

$$\frac{\text{Cost of Sales}}{\text{Average Inventories}} = \text{_____ times per year}$$

- Stock is turned over a number of times per year.
- This also depends on the type of goods being sold.
- The business needs to look at ways to increase its sales, in order to create a higher rate of stock turnover.

5.3.4 Stock holding period

$$\frac{\text{Average Inventories}}{\text{Cost of Sales}} \times \frac{365}{1} = \text{_____ days}$$

- The faster the sales occur, the fewer number of days stock is kept.
- This is also influenced by the type of goods being sold.

5.3.5 Average debtors' collection period

$$\frac{\text{Debtors}}{\text{Credit Sales}} \times \frac{365}{1} = \text{_____ days}$$

This indicates how long debtors will take to settle their accounts. It is informed by the credit terms of the business. A generally accepted period is 30 days. It is the final test of liquidity.

5.3.6 Average creditors' payment period

$$\frac{\text{Creditors}}{\text{Credit Purchases}} \times \frac{365}{1} = \text{_____ days}$$

This indicates how long the business takes to pay its creditors. It is informed by the credit terms of the supplier. A generally accepted period is 90 days.

LET'S PRACTICE LIQUIDITY RATIOS

Use the practice information on page 7 to calculate the following ratios. Round off your answers to one decimal point.

- i. Current ratio
- ii. Acid test ratio
- iii. Stock turnover rate
- iv. Average stock holding period
- v. Average debtors' collection period
- vi. Average creditors' payment period

i. Current ratio

$$973\ 200 : 696\ 900 \quad 1,4 : 1$$

ii. Acid test ratio

$$\frac{555\ 200}{(973\ 200 - 418\ 000) : 696\ 900} \quad \text{Or} \quad \frac{555\ 200}{(550\ 000 + 5\ 200) : 696\ 900}$$

$$= 0,8 : 1$$

iii. Stock turnover rate

$$\frac{3\ 220\ 000}{\frac{1}{2}(321\ 700 + 418\ 000)} = 41,9 \text{ times}$$

iv. Average stock holding period

$$\frac{\frac{1}{2}(321\ 700 + 418\ 000)}{3\ 220\ 000} \times 365 = 41,9 \text{ times} \quad \text{Or} \quad 365/8,7$$

v. Average debtors' collection period

$$\frac{512\ 500}{\frac{1}{2}(475\ 000 + 550\ 000)} \times 365 = 121 \text{ days}$$

$$\frac{30\% \ 5\ 15200}{1\ 545\ 600}$$

vi. Average creditors' payment period

$$\frac{516\ 400}{\frac{1}{2}(621\ 600 + 411\ 200)} \times 365 = 78 \text{ days}$$

$$\frac{2\ 415\ 000}$$

5.4 SOLVENCY

5.4.1 Solvency ratio = Total Assets : Total Liabilities

- It indicates whether or not the business can meet (pay) its liabilities.
- A business is solvent if its assets exceed its liabilities.

5.4.2 Net Asset = Total Assets - Total Liabilities

LET'S PRACTICE SOLVENCY RATIOS

Use the practice information on page 7 to calculate the following ratios.
Round off your answers to one decimal point.

1. Solvency ratio
2. Solvency

1. Solvency ratio

$$\frac{7\,920\,900}{(6\,947\,700 + 973\,200)} : \frac{1\,696\,900}{(1\,000\,000 + 696\,900)} = 4,7 : 1$$

2. Solvency

$$7\,920\,900 - 1\,696\,900 = 6\,224\,000$$

5.5 RETURN

5.5.1 Return on Shareholders' Equity

$$\frac{\text{Net Profit}}{\text{Average Owner's Equity}} \times \frac{100}{1} = \text{---} \%$$

- It indicates the return the owners' have received on their investment in the business.
- Should the owners rather have invested elsewhere?
- Compare it to returns achieved at financial institutions.

5.5.2 Earnings per share

$$\frac{\text{Net Profit}}{\text{Number of Shares issued}} \times \frac{100}{1} = \text{---} \text{ cents}$$

- Establish if purchasing the shares was worthwhile and whether or not the company has long-term sustainability and growth potential.

5.5.3 Dividends per share

$$\frac{\text{Ordinary Share Dividends}}{\text{Number of Shares issued}} \times \frac{100}{1} = \text{---} \text{ cents}$$

- Earnings are distributed to shareholders as dividends, but some earnings are retained to ensure future growth.

5.5.4 Net Asset value per share

$$\frac{\text{Ordinary Shareholder's Equity}}{\text{Number of Shares issued}} \times \frac{100}{1} = \text{---} \text{ cents}$$

This represents the intrinsic value of the share, i.e. a more realistic value, based on the performance of the undertaking over the years and the growth of the business, including acquisition of assets and additional shares being issued.

LET'S PRACTICE RETURN RATIOS

Use the practice information on page 7 to calculate the following ratios. Round off your answers to one decimal point.

- a. Return on shareholders' equity
- b. Earnings per share (EPS)
- c. Dividends per share (DPS)
- d. Net asset value per share (NAV)

a. **Return on shareholders' equity**

$$\frac{735\,700}{\frac{1}{2}(6\,224\,000 + 5\,058\,300)} \times 100 = 13\%$$

$$5\,641\,150$$

b. **Earnings per share (EPS)**

$$\frac{735\,700}{450\,000} \times 100 = 163,5 \text{ cents}$$

c. **Dividends per share (DPS)**

$$\frac{180\,000 + 220\,000}{450\,000} \times 100 = 89 \text{ cents}$$

d. **Net asset value per share (NAV)**

$$\frac{6224\,000}{450\,000} \times 100 = 1383 \text{ cents}$$

5.4 FINANCIAL RISK/GEARING

5.6.1 Debt-equity ratio (gearing)

Non-Current Liabilities: Shareholders' Equity

- It provides insight into the **capital structure** of the business.
- A ratio of 0,52:1 indicates that for every R1 of capital invested by the shareholders, 52c was raised through long-term loans.
- It also indicates the ability of the business to raise additional capital through long-term loans.
- A lower ratio indicates that the business has a higher creditworthiness and that it should therefore be able to obtain additional financing easily.
- It is favourable for the business to make use of borrowed capital when interest rates are lower than the return that can be earned by the business in using those funds.

5.6.2 Return on total capital employed

$$\frac{\text{Net Profit Before Tax}}{\text{Average Shareholders + Average Loans}} \times \frac{100}{1} = \text{---} \%$$

- Compare the figure to last year and indicate whether it has improved or deteriorated.
- Is it above or below the interest rate on loans?
- If it is above, it indicates positive gearing; therefore, it is favourable to use loans.
- If it is below, it indicates negative gearing; therefore, it is unfavourable to use loans and the business should consider paying loans off quickly.

LET'S PRACTICE FINANCIAL RISK/GEARING RATIOS

Use the practice information on page 7 to calculate the following ratios. Round off your answers to one decimal point.

- Debt/equity ratio
- Return on average capital employed (ROTCE)

i. **Debt/equity ratio**

$$1\,000\,000 : 6\,224\,000 = 0,2 : 1 \quad (0,16 : 1)$$

ii. **Return on average capital employed (ROTCE)**

$$\frac{1\,051\,000 + 133\,960}{(6\,224\,000 + 1\,000\,000 + 5\,058\,300 + 1\,600\,000)} \times 100 = 17,1\%$$

5.7 COMMENTING ON FINANCIAL INDICATORS

Steps to follow when you are required to comment on financial indicators:

- Consider what the question is asking you to analyse (e.g. liquidity).
Decide on the relevant financial indicator(s).
- Name the financial indicator(s), giving figures or ratios or percentages.
- Compare the current year's indicator(s) with that of the previous year.
Say whether it has increased or decreased.
- *If possible, provide a general comment.

Hint: Use short sentences and point form when commenting.

EXAMPLE 1

Financial indicator	2016	2017
Current ratio	1,6 : 1	2,3 : 1
Acid test ratio	0,7 : 1	1,5 : 1

- Current ratio has improved from 1,6 : 1 to 2,3 : 1
- Acid test ratio has improved from 0,7 : 1 to 1,5 : 1
- This company is in a good liquidity position and should be able to pay its short-term debt easily.

EXAMPLE 2

Financial indicator	2016	2017
Earnings per share (EPS)	85c per share	55c per share
Dividends per share (DPS)	75c per share	60c per share

- EPS has declined from 85c to 55c per share.
- DPS has declined from 75c to 60c per share.
- In 2016, the EPS was 85c, while the DPS was 75c per share. This means that the company retained 10c per share for future growth.
- In 2017, the company earned 55c per share, but gave the shareholders 60c per share; therefore none of this year's profits were retained.

5.8 ACTIVITIES

ANALYSIS AND INTERPRETATION ACTIVITIES

ACTIVITY 1

CONCEPTS

Required:

Complete the following sentences using the words in the list below. Write only the word next to the question number. (5)

liquid; profitable; solvent; return; risk/gearing

- a) A company with total assets exceeding total liabilities is.....
- b) A company that relies heavily on loans will have high.....
- c) A company that controls its income and expenses properly will be.....
- d) The percentage net income on equity indicates the earned by shareholders.
- e) A company that is able to settle its immediate debts is.....

ACTIVITY 2

(Modified from Nov 2014 DBE QP)

(32 Marks; 19 Minutes)

REQUIRED

SMITH TRADERS

- 2.1 Calculate the following financial indicators for the financial year ended 28 February 2014:
- 2.1.1 Solvency ratio (4)
 - 2.1.2 Net asset value per share (3)
 - 2.1.3 Debt-equity ratio (3)
- 2.2 Comment on the liquidity position of the company. Quote THREE relevant financial indicators (actual figures/ratios/percentages) and their trends. (9)
- 2.3 The directors decided to increase the loan during the current financial year. Quote TWO financial indicators (actual figures/ratios/percentages) that are relevant to their decision. Explain why this was a good decision, or not. (8)

2.4 The Bakker family owns 740 000 shares in this company.
Explain the effect that the repurchase of shares on 31 December 2013
had on their control of the company.
Give a calculation to support your answer.

(5)

INFORMATION:

A. Extract from the Income Statement for the year ended 28 February 2014:

Interest on loan (all capitalised)	88 500
Net profit before tax	1 575 000
Income tax	441 000

B. Extract from the Balance Sheet as at:

	28 Feb. 2014	28 Feb. 2013
Current assets	3 337 300	4 641 000
Inventories	818 200	641 000
Trade debtors	2 377 600	1 512 000
SARS: Income tax	128 000	-
Cash and cash equivalents	13 500	2 488 000
Shareholders' equity	8 839 000	7 400 000
Ordinary share capital	8 700 000	6 600 000
Retained income	139 000	800 000
Mortgage loan: Excel Bank (interest rate: 12,5% p.a.)	908 000	508 000
Current liabilities	2 063 700	1 302 000
Trade creditors	678 700	700 000
Shareholders' for dividends	870 000	480 000
Bank overdraft	515 000	-
SARS: Income tax	-	122 000

C. Shareholders' register:

DATE	DETAILS
1 March 2013	1 200 000 shares in issue.
31 March 2013	300 000 shares issued at R8 each.
31 December 2013	The company bought back 50 000 shares from a dissatisfied shareholder, S Smit, at R9,50 each. The average price of all shares issued to date was R6 per share.
28 February 2014	1 450 000 shares in issue.

D. Dividends for the financial year ending 28 February 2014:

Interim dividends paid on 31 August 2013	R750 000
Final dividends declared on 28 February 2014	R870 000

E. Financial indicators:

	28 Feb. 2014	28 Feb. 2013
Debt-equity ratio	?	0,1 : 1
Net asset value per share (NAV)	?	617 cents
Current ratio	1,6 : 1	3,6 : 1
Acid-test ratio	1,2 : 1	3,1 : 1
Stock turnover rate	6,8 times p.a.	5,1 times p.a.
Debtors' collection period	40 days	35 days
% return on average capital employed	18,8%	16,4%

ACTIVITY 3

(Modified from Nov 2015 DBE QP)
REQUIRED

(38 Marks; 23Minutes)

3.1 CONCEPTS

Give ONE term for each of the descriptions below. Choose a term from the list below.
Write only the term next to the question number.

**directors' report; Balance Sheet; shareholder; director;
internal auditor; Cash Flow Statement; independent auditor**

- 3.1.1 A person employed by a company to check and advise management on the financial control systems. (1)
- 3.1.2 A person appointed by the shareholders who expresses an unbiased opinion on the financial statements of a company. (1)
- 3.1.3 A person appointed to manage a company and make decisions to ensure it runs smoothly. (1)
- 3.1.4 The financial statement that shows the financial position of a business on a certain date. (1)

3.2 CEBO LTD

The information below relates to CEBO Ltd.

REQUIRED:

- 3.2.1 Calculate the following for the financial year ended 28 February 2015. (4)
- Acid-test ratio
 - Return on shareholders' equity (ROSHE)
(Use average equity in your calculation.) (5)
 - Net asset value (NAV) per share. (3)

INFORMATION:

A. Figures from the Balance Sheet and notes:

	28 FEBRUARY 2015	28 FEBRUARY 2014
Fixed assets (carrying value)	R4 137 700	R2 598 300
Financial assets (fixed deposit)	350 000	600 000
Current assets	662 300	575 500
Inventory	322 000	345 000
Trade and other receivables	245 000	228 000
SARS: Income tax	6 400	–
Cash and cash equivalents	88 900	2 500
Shareholders' equity	3 439 500	2 718 000
Ordinary share capital	2 967 000	2 520 000
Retained income	472 500	198 000
Non-current liabilities	1 200 000	500 000
Current liabilities	510 500	555 800
Trade and other payables	323 000	285 000
Shareholders' dividend	187 500	108 000
SARS: Income tax	–	9 800
Bank overdraft	–	153 000

B. Extract from the Income Statement for the year ended 28 February 2015:

Gross profit	R2 040 000
Depreciation	215 100
Operating profit	1 300 000
Interest expense	132 000
Net profit before tax	1 175 000
Net profit after tax	846 000

C. Share capital:

- Authorised share capital consists of 800 000 ordinary shares.
- 150 000 new ordinary shares were issued on 1 October 2014.
- 60 000 ordinary shares were repurchased on 1 January 2015 at 90 cents above the average issue price of R4,30.
- On 28 February 2015, the share register reflected that a total of 690 000 shares had been issued to date.

D. Fixed assets:

- Additional property was purchased for R2 100 000. No other fixed assets were purchased.
- Equipment was sold at carrying value.

3.3 DON LTD AND LAKA LTD

You have R50 000 to invest in a listed company.

You choose to focus on two companies in the same industry.

NOTE: When answering the questions below, compare the information given and quote the relevant financial indicators of both companies (percentages, ratios and/or amounts).

REQUIRED:

- 3.3.1 Comment on the value of the shares of the two companies listed on the Johannesburg Securities Exchange (JSE). Explain how this will influence your choice of company. (6)
- 3.3.2 Compare and comment on the dividend pay-out policies of the two companies. (6)
- 3.3.3 Comment on the degree of risk and gearing. Explain how this will influence your choice of company. (6)
- 3.3.4 Apart from the points mentioned above, what other factors would you consider before deciding in which company you are going to invest? Explain TWO points. (4)

INFORMATION:

	DON LTD	LAKA LTD
Current ratio	4,3 : 1	1,5 : 1
Acid-test ratio	2,8 : 1	0,8 : 1
Stock turnover rate	4 times	6 times
Stock-holding period	90 days	62 days
Average debtors' collection period	54 days	26 days
Average creditors' payment period	59 days	62 days
Debt-equity ratio	0,3 : 1	1,6 : 1
Return on total capital employed (ROTCE)	15,6%	10,2%
Return on shareholders' equity (ROSHE)	17,2%	9,1%
Earnings per share (EPS)	420 cents	980 cents
Dividend per share (DPS)	360 cents	490 cents
Net asset value per share (NAV)	310 cents	750 cents
Market price of shares on JSE	400 cents	645 cents
Interest rate on loans	11,5%	11,5%

ACTIVITY 4

(Modified from Feb 2016 DBE QP)

(28 Marks; 17Minutes)

PILLAY LTD

You are provided with information for the financial year ended 28 February 2016, taken from the books of Pillay Ltd. It is a listed public company.

4.1 Calculate the following financial indicators for the financial year ended 28 February 2016. (Round off your calculation to ONE decimal point or the nearest cent, where applicable.)

4.1.1 Net asset value per share (3)

4.1.2 Return on average shareholders' equity (5)

4.1.3 Debt-equity ratio (3)

4.2 Refer to Information E.

4.2.1 The directors are not satisfied with the liquidity position. Quote and explain THREE relevant financial indicators (with figures) to support this statement. (6)

4.2.2 The directors decided to increase the loan during the current financial year. Explain why this was a good decision. Quote and explain TWO financial indicators (with figures) in your answer. (8)

4.2.3 The directors were pleased with the price that the company paid to buy back the 40 000 shares. Give a suitable reason why the directors felt that way. Quote relevant financial indicators (with figures) to support your answer. (3)

INFORMATION:

- A. Extract from the Income Statement for the year ended 28 February 2016:

Sales	R2 800 000
Net profit before tax	1 240 000
Income tax	?
Net profit after tax	892 800

- B. Extract from the Balance Sheet on 28 February 2016:

	2016	2015
Fixed assets (carrying value)	?	?
Fixed deposit: FS Bank	1 450 000	1 200 000
Current assets	1 944 280	1 010 000
Inventory	975 700	345 000
Debtors and other receivables	419 000	629 600
SARS (Income tax)	0	17 400
Cash and cash equivalents	549 580	18 000
Shareholders' equity	5 950 800	4 345 000
Share capital	5 402 000	4 200 000
Retained income	548 800	145 000
Mortgage loan: TKO Bank	1 950 000	400 000
Current liabilities	587 200	555 000
Creditors and other payables	437 800	165 000
Accrued expenses	8 700	5 000
SARS (Income tax)	35 700	0
Shareholders' dividend	105 000	275 000
Bank overdraft	0	110 000

C. Share Capital

- Authorised share capital is 3 000 000 ordinary shares.
- In 2012, 1 200 000 ordinary shares had been issued at R3,50 per share.
- On 1 November 2015, 300 000 ordinary shares were issued at R4,50 each.
- On 28 February 2016, 40 000 shares were repurchased at R0,60 more than the average price per share.

D. Dividends

The directors declared a final dividend of 7 cents per share.
The shares bought back on 28 February 2016 also qualify for the final dividend.

E. Financial indicators on 28 February:

	2016	2015
Net profit after tax on sales	31,9%	24,5%
Current ratio	3,3 : 1	1,8 : 1
Debtors' collection period	36 days	28 days
Creditors' payment period	45 days	80 days
Acid-test ratio	1,7 : 1	1,2 : 1
Rate of stock turnover	3 times	5 times
Return on shareholders' equity	?	17,5%
Return on total capital employed	24,2%	21,2%
Debt-equity ratio	?	0,09 : 1
Interest rate on loans	10,5%	10,5%
Net asset value per share	?	362 cents
Market value per share	505 cents	480 cents

ACTIVITY 5

(Modified Nov 2016 DBE QP)(49 Marks; 29 Minutes)

REQUIRED

- 5.1 Choose a term from COLUMN B that matches the description in COLUMN A. Write only the letter (A–D) next to the question number (5.1.1– 5.1.4).

COLUMN A	COLUMN B
5.1.1 Ability of the business to pay off all its debts.	A gearing
5.1.2 Ability of the business to pay off its short-term debts.	B return on equity
5.1.3 The benefit that shareholders receive for investing in the company.	C solvency
5.1.4 The extent to which a company is financed by loans.	D liquidity

(4 x 1)

5.2 **REID LTD**

You are provided with information relating to Reid Ltd for the financial year ended 30 June 2016.

Where financial indicators are required to support your answer, name the financial indicator, the actual figure/ratio/percentage and the trend.

REQUIRED:

5.2.1 Calculate the following financial indicators on 30 June 2016:

- Acid-test ratio (4)
- Debt-equity ratio (3)
- % return on average shareholder's equity (ROSHE) (5)
- Net asset value per share (NAV) (3)

5.2.2 The liquidity of the company has improved.
Quote THREE financial indicators to support this statement. (6)

5.2.3 Dividend policy:

- Provide calculations to show the change in the dividend pay-out policy. (4)
- Explain why the directors decided to change the policy.
State ONE point with figures. (2)

5.2.4 Mary is the CEO of the company. Her shareholding is as follows:

NUMBER OF SHARES	DATE PURCHASED	% SHAREHOLDING
420 000	10 January 2015	46,7%

- (a) Calculate Mary's % shareholding on 1 October 2015, after the repurchase of shares. (4)
- (b) Explain how Mary has benefitted from the decision to repurchase the shares. (2)
- (c) The independent auditor discovered that Mary had made the decision to repurchase the shares without informing the board of directors. Why should the independent auditor be concerned about this? (2)

5.2.5 The Financial Statements reflected fixed assets purchased in the amount of R4,5 million.

- Name TWO major sources of funding for these fixed assets and provide the figures (over R1 000 000 each). (4)

- State for EACH source whether it was a good or bad decision. Explain your choice. Quote relevant financial indicators/figures to support your opinion. (6)

INFORMATION:

A. Share capital and dividends:

- 900 000 shares were in issue on 1 July 2015.
- 75 000 ordinary shares were repurchased from the estate of a deceased shareholder at R10,70 per share on 1 October 2015.
- The company issued 125 000 ordinary shares at R10,80 per share on 1 April 2016.
- The 2016 Cash Flow Statement reflected dividends paid of R434 250.

B. Extract from Income Statement for the year ended 30 June 2016:

	R
Sales	5 220 000
Cost of sales	3 600 000
Operating profit	1 295 000
Income tax	190 500
Net profit after tax	444 500

C. Extract from Balance Sheet on 30 June:

	2016	2015
	R	R
Fixed assets (carrying value)	17 420 950	14 683 300
Fixed deposit: Ken Bank	250 000	380 000
Current assets	1 015 000	456 000
Inventories (only trading stock)	564 000	281 500
Trade and other receivables (debtors)	246 000	167 000
Cash and cash equivalents	205 000	7 500
Shareholders' equity	10 050 750	9 540 000
Ordinary share capital	?	9 180 000
Retained income	?	360 000
Loan: Barbie Bank	8 000 000	4 500 000
Current liabilities	635 200	1 479 300
Trade and other payables	420 000	683 400
Shareholders' dividend	209 000	162 000
SARS: Income tax	6 200	23 400
Bank overdraft	-	610 500

D. The following financial indicators were calculated on 30 June:

	2016	2015
Current ratio	1,6 : 1	0,3 : 1
Acid-test ratio	?	0,1 : 1
Stock turnover rate	8,5 times	10 times
Debtors' collection period	36 days	43 days
Creditors' payment period	63 days	63 days
Solvency ratio	2,2 : 1	2,6 : 1
Debt-equity ratio	?	0,5 : 1
Return on total capital employed (ROTCE)	8,2%	9,5%
Return on shareholders' equity (ROSHE)	?	6,2%
Earnings per share (EPS)	51 cents	58 cents
Dividends per share (DPS)	55 cents	35 cents
Net asset value per share (NAV)	?	1 060 cents
Market price	1 000 cents	1 030 cents
Interest rate on loans	12%	12%

ACTIVITY 6**(Modified Nov 2017 DBE QP)****(50 Marks; 30Minutes)****REQUIRED**

- 6.1 Choose a term to complete each of the following statements.
Write only the term next to the question number (6.1.1– 6.1.4).

shareholder(s); external auditor(s); director(s); internal auditor(s)

- 6.1.1 are appointed by the shareholders to manage the company.
 6.1.2 The is employed by the company to set up functional internal control processes.
 6.1.3 A is a person who invests in a company by buying shares.
 6.1.4 are appointed by shareholders to give an unbiased opinion on the financial statements. (4 x 1) (4)

6.2 FINE LTD

The given information relates to Fine Ltd for the financial year ended 31 August 2017.

REQUIRED:

- 6.2.1 Calculate the following financial indicators on 31 August 2017:
 · Percentage operating profit on sales (3)
 · Debt-equity ratio (4)
- 6.2.2 Calculate the dividends per share (DPS) of a shareholder who owned the same number of shares for the entire financial period. (4)

INFORMATION:

- A. Information from the Income Statement for the financial year ended 31 August 2017:

	R
Sales	8 652 000
Operating expenses	1 760 000
Depreciation	320 000
Interest expense	86 100
Operating profit	697 000
Income tax	187 770
Net profit after income tax	438 130

B. Information from the Balance Sheet on 31 August:

	2017 (R)	2016 (R)
Fixed assets (carrying value)	6 177 000	4 975 000
Fixed deposits	220 000	300 000
Loan: Dolphin Bank	985 000	450 000
Current assets	619 600	663 300
Current liabilities	490 000	614 300
Shareholders' equity	?	?
Ordinary share capital	5 292 000	?
Retained income	?	147 370
Cash and cash equivalents	23 400	2 500
Bank overdraft	-	65 100
Shareholders' dividend	168 000	120 000
SARS: Income tax	11 800 (Cr)	2 400 (Dr)

C. Share capital and dividends

- The authorised share capital comprises 1 200 000 ordinary shares.
- 900 000 ordinary shares were in issue on 1 September 2016.
- The company issued 150 000 ordinary shares at R6,30 per share on 1 May 2017.
- 70 000 ordinary shares were repurchased from shareholders on 30 August 2017. A cheque for R437 500 was issued for these shares. These shareholders qualify for a final dividend.
- An interim dividend of 12 cents per share was paid on 1 February 2017.
- A final dividend was declared on 30 August 2017.

6.3 CASTRO LTD AND PETER LTD

You are provided with information relating to two companies.

BACKGROUND INFORMATION:

- Henry Harries owns 300 000 shares in each company.
- **Castro Ltd** issued 200 000 new shares to existing shareholders at the average issue price (R9,10). These funds were used to establish a new branch. No new loans were raised.
- **Peter Ltd** paid R4 800 000 to repurchase 320 000 shares.

REQUIRED:

NOTE: Where comments or explanations are required, quote financial indicators and figures to support your answer.

CASTRO LTD

- 6.3.1 Comment on the price of R9,10 charged by Castro Ltd for the new shares issued. (3)
- 6.3.2 Explain how the issue of new shares has affected the financial gearing and risk of Castro Ltd. Quote TWO financial indicators. (6)
- 6.3.3 Henry had the option to buy some of the new shares issued by Castro Ltd. He had saved sufficient funds (interest rate 5% p.a.) for this purpose.
 - If Henry wanted to retain his 60% shareholding in the company, how many shares would he have had to buy and how much would he have had to pay? (5)
 - Henry decided NOT to buy these shares. Apart from the % shareholding, explain TWO reasons why he has made a mistake by not taking up this option. (6)

PETER LTD

- 6.3.4 Comment on the liquidity of Peter Ltd. Quote TWO financial indicators. (6)
- 6.3.5 Comment on the price paid by Peter Ltd for the repurchase (buy-back) of shares. (3)
- 6.3.6 Explain THREE ways in which Henry has benefited from the repurchase of shares by Peter Ltd. (6)

ADDITIONAL INFORMATION:

Financial indicators and additional information from annual reports:

	CASTRO LTD		PETER LTD	
	2017	2016	2017	2016
Debt-equity ratio	0,5 : 1	0,8 : 1		
Current ratio			1,9 : 1	3,5 : 1
Acid-test ratio			1,1 : 1	1,7 : 1
Stock-holding period			54 days	54 days
Number of shares in issue	700 000	500 000	580 000	900 000
Average share issue price	R9,10		R10,20	
Price paid for share repurchase			R15,00	
Price of share on JSE	R12,00		R15,00	
Net asset value per share	R10,73	R11,38	R13,30	R13,22
% return on shareholders' equity	23%	17%	16%	13%
% return on total capital employed	20%	15%		
Earnings per share	140 cents	196 cents	266 cents	171 cents
Total dividends	R357 000	R325 000	R928 000	R928 000
Dividends per share	51 cents	65 cents	160cents	103 cents