INTERPRETATION OF ACCOUNTS

POOR SOLVENCY

Indicated by
- ↓ Working Capital
- ↓ Current Ratio
- ↓ Acid Test Ratio

Causes:

(i) ↑ in Fixed Assets not matched by ↑ in
- Share Capital
- Bal on P&L a/c
- Term Loans

} Long Term Liabilities

(ii) Poor Credit Control (cf: Debtors Days)

(iii) Build-up in Stocks (cf: Stock T/O)

Remedies:

(i) Borrow long term & replenish bank account

(ii) Improve credit control procedures
- sending statements
- evaluating new customers.

(iii) Identify slow moving stocks.

↑ Debtors Days :-
- might be expected if Sales have increased by offering better terms to customers.
- if not expected, review credit control procedures. Review Debtors balances to determine if there exists any bad debts.

↑ Creditors Days :-
- this is always desireable.
- Creditors may not be getting paid if solvency is poor
- should review Creditors balances if there exists any legal action pending.

PROFITABILITY

↓ Gross Margin :
- might be expected if market is more competitive &
- prices reduced to generate more Sales
- if not expected :
  - review procedures over recording of Sales (partic. cash business)
  - review controls over custody of stocks (labelling etc)

↓ Net Margin
- review overheads to identify any costs that have increased unexpectedly.
- If overheads have not increased substantially (relative to any ↑ in Sales) then economies of Scale are being derived.

↓ Stock Turnover
- may indicate that some stock items are obsolete or slow moving. Put a stop on any further orders.