

RATIO ANALYSIS

The following are the summarised results for Ginger Motor Sales Limited for the year ended 31st October 2003 and 2002:

PROFIT AND LOSS ACCOUNT	2003 €	2002 €
Sales	840,000	612,000
Cost of Sales	638,400	428,400
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Gross Profit	201,600	183,600
Overhead Expenses	175,350	156,060
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Net Profit	26,250	27,540
Bal. On Profit & Loss b/fwd	103,550	76,010
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Bal. on Profit & Loss c/fwd	129,800	103,550
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BALANCE SHEET					
	2003 €	2002 €		2003 €	2002 €
SHARE CAPITAL	50,000	50,000	FIXED ASSETS	175,000	100,000
BAL ON P&L A/C	129,800	103,550			
TERM LOAN	30,000	-			
CURRENT LIABILITIES:			CURRENT ASSETS:		
Creditors	79,800	53,550	Stocks	53,200	35,700
Bank Overdraft	36,600	-	Debtors	98,000	68,000
			Bank	-	3,400
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	326,200	207,100		326,200	207,100
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a. Compute for each year:-

- i. Current Ratio
- ii. Acid Test Ratio
- iii. Period of Credit Allowed
- iv. Period of Credit Taken
- v. Stock Turnover
- vi. Gross Margin
- vii. Net Margin

(16 Marks)

b. Using your computations at a. above, comment on the profitability and solvency of the company (9 Marks)

TOTAL 25 MARKS.

SOLUTION

GINGER MOTORS 2003

2002

Current Ratio $\frac{CA}{CL}$ (ideal 2:1)	$\frac{151200}{116400} = 1.30$	$\frac{107100}{53550} = 2:1$
Acid Test Ratio $\left(\frac{CA - \text{stock}}{CL}\right)$ ideal 1:1	$\frac{98000}{116400} = 0.84$	$\frac{71400}{53550} = 1.33$
Credit Allowed $\left(\frac{\text{Debtors}}{\text{Sales}} \times 365\right)$	$\frac{98000}{840000} \times 365 = 43 \text{ days}$	$\frac{68000}{612000} \times 365 = 40 \text{ days}$
Credit Taken $\left(\frac{\text{Creditors}}{\text{Cos}} \times 365\right)$	$\frac{79800}{638400} \times 365 = 46 \text{ days}$	$\frac{53550}{428400} \times 365 = 46 \text{ days}$
Stock T/o $(\text{Cos} / \text{Stock})$	$\frac{638400}{53200} = 12 \text{ times}$	$\frac{428400}{35700} = 12 \text{ times}$
Gross Margin $(\text{Gp} / \text{Sales} \%)$	$\frac{201600}{840000} \times 100 = 24\%$	$\frac{183600}{612000} \times 100 = 30\%$
Expenses per month $(9/12)$	14600 p.m.	13000 p.m.
Net Margin $\left(\frac{\text{Net}}{\text{Sales}} \times 100\right)$	$\frac{26250}{840000} \times 100 = 3.1\%$	$\frac{27540}{612000} \times 100 = 4.5\%$

Comments

- Decline in solvency as indicated by CR & ATR ratios.
- made profit, yet now running at a loss.
- Increase in fixed assets, not matched by similar increase in long term sources.
- Debtors Days have increased. Credit control procedures should be reviewed & bad debts should be identified, if any.
- overheads have increased by 10%. Sales have increased by 37%. Company is enjoying economies of scale.
- no change in stock turnover & creditors day and are consistent with expectations / prior years.
- REMEDY: Company should borrow long term & replenish bank.
- Gross Margin down 6%. Likely that sector is more competitive & to generate more sales, the company reduced prices.

CASH FLOW STATEMENT

Profit For Year	26,250
CHANGES IN WORKING CAPITAL	
Increase in stocks	-17,500
Increase in Debtors	-30,000
Increase in Creditors	26,250
Source from OPERATIONS	5,000
OTHER SOURCES	
Increase in loans	30,000
OTHER USES	
Increase in fixed assets	-75,000
NET SOURCE / USE OF FUNDS FOR YEAR	-40,000
Opening bank balance	+ 3600
Closing bank balance	- 36600
Adverse movement on bank	-40000