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ACCOUNTING QUESTIONS ACCOUNTING QUESTIONS ANSWERS Task two Calculation of the cash flow for each ofthe five years   
Annual cash flow   
year 0   
-100, 000   
year 1   
20, 000   
year 2   
40, 000   
year 3   
60, 000   
year 4   
60, 000   
year 5   
40, 000   
Calculation of Cash Flows:   
Sale price per unit=£ 12   
Variable Cost per unit=£ 8   
Contribution=£ 4   
Cash flow of 1st Year=£ 4 \* 5, 000=£ 20, 000   
Cash flow of 2nd Year=£ 4 \* 10, 000=£ 40, 000   
Cash flow of 3rd Year=£ 4 \* 15, 000=£ 60, 000   
Cash flow of 4th Year=£ 4 \* 15, 000=£ 60, 000   
Cash flow of 5th Year=£ 4 \* 5, 000=£ 20, 000   
In 5th year, there is termination value of machine which is £20, 000, therefore there is additional cash flow of £20, 000 during 5th year.   
2. Using the investment appraisal methods to calculate the ARR, Payback, NPV and IRR   
2. 1 Calculation of Accounting Rate of Return (ARR)   
Accounting Rate of Return= Average Annual Cash Flow / Average Investment   
=[£ 24, 000 / £ 60, 000] \*100   
= 40%   
Average Investment = Cost of Machine + Disposal Value / by two   
Total Cash Flow during useful life of machine= £ 200, 000   
Average annual cash flow = £ 200, 000 / 5   
= £ 40, 000   
Average Investment = £ 100, 000 + £20, 000/2   
Average Investment = £ 60, 000   
2. 2 Calculating the payback   
Initial Investment   
100, 000   
Accumulative Cash Flow   
Cash Flow Year 1   
20, 000   
20, 000   
Cash Flow Year 2   
40, 000   
60, 000   
Cash Flow Year 3   
60, 000   
120, 000   
The Accumulative cash flow up to year 2 is £ 60, 000, initial investment required is £ 100, 000 thus cash flow required during year 2 is £ 40, 000. The cash flow during year 3 is £ 60, 000. Therefore calculation will be:   
Cash flow required during year 3= £ 60, 000   
Time required to generate required amount=£ 40, 000 / £ 60, 000   
= 0. 67 years i. e. 8 months (0. 67 \* 12)   
Therefore, the machine will take two years and 8 months to generate cash flow of amount equal to initial investment i. e. £ 100, 000.   
2. 3 Calculating the NPV   
Years   
Net Cash Flows   
PV   
0   
(100, 000)   
1   
20, 000   
17, 860   
2   
40, 000   
31, 880   
3   
60, 000   
42, 720   
4   
60, 000   
38, 160   
5   
40, 000   
22, 680   
Total   
153, 3000   
Sum of PV 1-5Yrs based on COC =£153, 3000   
Initial Investment required to get machine operational =£100, 000   
Net Present Value= £153, 3000 - £100, 000   
=£ 53, 300   
Therefore, the Net Present Value calculated is £ 53, 300, which is highly positive.   
2. 4 Calculating the Internal Rate of Return:   
Years   
Net Cash Flows   
0   
(100, 000)   
1   
20, 000   
2   
40, 000   
3   
60, 000   
4   
60, 000   
5   
40, 000   
The IRR calculated through MS Excel is 29. 16%. Calculations based on Trial & Error method is summarized as shown below   
Years   
Net Cash Flows   
PV @ 25%   
PV @ 30%   
PV @ 28%   
PV @ 29%   
1   
20, 000   
16, 000   
15, 385   
15, 625   
15, 504   
2   
40, 000   
25, 600   
23, 669   
24, 414   
24, 037   
3   
60, 000   
30, 720   
27, 310   
28, 610   
27, 950   
4   
60, 000   
24, 576   
21, 008   
22, 352   
21, 667   
5   
40, 000   
13, 107   
10, 773   
11, 642   
11, 197   
Total   
110, 003   
98, 144   
102, 643   
100, 355   
The table above is showing present value of estimated cash flows at different rates while it is clear that present value of estimate cash flows at 29 percent and 30 percent are respectively nearest greater and less to initial investment therefore the IRR will lie between 30% and 29%. Exact value will be calculated through interpolation, as below.   
Present Value of Estimated Cash Flows @ 30%=£98, 144   
Present Value of Estimated Cash Flows @ 29Nd%=£100, 355   
Initial Investment =£100, 000   
Internal Rate of Return = 29% + (100, 000 – 98, 144) / 100, 000   
= 29% + 0. 1656   
= 29. 165   
Therefore, the IRR calculated through Trial & Error method is 29. 165% approximately at which the present value of estimated cash flows is £99, 996 which is approximately equal to initial investment i. e. £100, 000   
3. Advising the client to either accept or reject the project   
The customer should take the project because the payback period is two years and eight months, besides, the IRR calculated through Trial & Error method is 29. 165% approximately at which the present value of estimated cash flows is £99, 996 that gives an approximately equal to initial investment i. e. £100, 000.   
Task three   
1. Cash budget for the months of august to November 2014   
Pedrosa Plc   
Cash Budget   
For the period from August 2014 to November 2014   
Opening Cash Balance   
August   
Sep   
Oct   
Nov   
15, 400   
37, 240   
43, 390   
48, 930   
Sales   
67, 650   
60, 400   
58, 500   
55, 500   
Cash Sales   
27, 060   
24, 160   
23, 400   
22, 200   
1 Month   
39, 180   
40, 590   
36, 240   
35, 100   
Rent Income   
9, 000   
9, 000   
9, 000   
9, 000   
Cash Receipt   
75, 240   
73, 750   
68, 640   
66, 300   
Net Cash Inflow   
90, 640   
110, 990   
112, 030   
115, 230   
Y   
Purchases   
33, 600   
32, 600   
34, 750   
35, 650   
Cash Payments   
35, 400   
33, 600   
32, 600   
34, 750   
Wages   
18, 000   
18, 000   
18, 000   
19, 080   
Dividend   
16, 000   
  
Machine   
  
  
12, 500   
6, 250   
Cash Payments   
53, 400   
67, 600   
63, 100   
60, 080   
  
  
  
  
  
Ending Cash Balance   
37, 240   
43, 390   
48, 930   
55, 150   
The ending cash balance during month of August is £37, 240 while the expected cash balance during September is £43, 390. Similarly the expected cash balance during October and November are £48, 930 and £55, 150 respectively as shown in the table above.   
2. Benefits of the budget to a business   
Organisations need budget to help in the evaluation of its performance. Without a financial planning that makes use of the budget, they would not be in a position to assess their progress and institute appropriate measures. Besides, they need budgeting for efficient coordination of the organisational activities. The budget acts like a blueprint that provides the roadmap and the expectation of the activities like sales, expenditures, and other costs. When organisations do not use budgets to address these issues, they are at risk of running down the organisation because of unplanned activities that are likely to exceed the expectations. Budgeting helps organisations to take control of their finances, hence keeping focused on the goals they laid down when beginning the financial year. A budget helps the organisation plan savings and makes decisions in advance when expecting or not expecting any costs related to the activity of the organisation hence controlling debts (Young, 2003).   
2. 1 What can be done to enhance budgeting process?   
Budgeting process can be very challenging especially when there is poor communication between the team tasked with the making of decisions. Therefore, enhancing communication and reducing the number of people involved in the making of budget will help improve the process (Young, 2003). Besides, it is important to have time and iterate the budget because handling the process at the last minute may hamper the process. It is also crucial to have time to review and improve areas that may not represent the expectations of the organisation (Young, 2003).   
BIBLIOGRAPHY   
Young, R. D. (2003). Performance-Based Budget Systems - Public Policy & Practice, p. 12, available online from ww. iopa. sc. edu/ejournal/assets/performance%20based%20budgets. pdf [21st June 2015)