To 259.55 times in juxtaposition to 2015

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To conclude, there is certainly some operational issues; both managerial and financial functioning in Benitez Plc which is resulting ina heavily decreased bank balance. As mentioned I think the main contribution toBenitez Plc's £140 million fall in bank balance is the increased debt ratiowhich is costing Benitez Plc a decrease in cash flow resulting in no rise inthe bank balance. Issues such as increased receivables collection period andinventory turn over period are also relevant factors but debt being the mainissue. As cited I do think Benitez financial directors should look at ways inmaximising its cash flow and sales as its one of the main steps to resolvingthe issue.

I think it is also very important to mention thatBenitez Plc's increased turnover period is also damaging the firms bank balance. Inventory turn over period is the measurement of times inventory is used or soldover a period of time, typically a year. Table 3 shows that in 2014 Benitez Plc'sturnover period was 259. 55 times in juxtaposition to 2015 which was 389.

33times. An Increased turnover period means higher cost of holding inventory asmore money is being utilised on labour to maintain it resulting in deduction inBenitez Plc bank balance. However, high inventory turnover period could suggeststronger sales for the firm, but this is not the case for Benitez Plc as there turnoverhas decreased by £300 million from the year ended 2014 to the year ended 2015 definininglysupporting the result of a reduced bank balance as there is lesser cash flowcoming to Benitez plc's bank balance Another contribution of Benitez Plc's reduced bankbalance is the increase in the receivables collection period. The receivablescollection period is efficiency ratio which measure the amount of time it takesfor a firm to collect money from its accounts receivables. In table above wecan see

that in the year ended 2014 Benitez Plc had a receivables collectionperiod was approximately 150 days and now has drastically increased in 2015 toapproximately 341 days. A high collection period shows Benitez inability andstruggle to convert receivables into cash, resulting in money that is owed tothe Benitez Plc taking much longer to actually be represented in the bank balance. In aid of improving their collection period Benitez Plc could apply morepressure and be more practical and forceful in invoicing or could also offerpayment plans to insure their guaranteed an ongoing source of income frompayments.

Alternatively, they could offer a small early payment discount meaningBenitez Plc will get money back quicker however that comes with a burden of losingout money. I think themain culprit of Benitez plc’s drastic decrease in bank balance is its large andincreased debt ratio. Debt ratio is the proportion of the firm’s assetsfinanced by debt, if you look carefully on table 3 we can see that in the yearended 2014 the percentage of assets financed by debt was only 58. 09% incomparison to the year ended 2015 which was 63. 21%. If most of a firm’s assets arefinanced by debt this means that they don’t completely own all there asset, resultingin bank loan being used to reimbursement liabilities meaning more of Benitez Plc’scash flow is going towards paying off liabilities instead of contributingtowards an increased bank balance.

In order for Benitez Plc to reduce theredebt ratio they could concentrate on sales and profit maximisation and attemptto reduce expenses which could potentially help their bank balance to raise. Having reading over your statement of financialposition and statement of profit and loss for both the

year ended 31stDecember 2014 and 31st December 2015, I believe your concerns for thesubstantial reduction in the Benitez plc's bank balance are certainly correct, from the year ended 2014 to 2015 the bank balance has decreased by £140 millionpounds. Subsequently reviewing both sources of financial information andcalculating efficiency; liquidity and probability ratios, I have come to theassumption that the reason why your firms bank balance has reduced sodrastically is because of its increased receivables collection period, additionally the high proportion of debt ratio is indirectly decreasing thebank balance and lastly the increased inventory turnover rate in comparison tothe year ended 2015. Dear Directors of Benitez Plc, To conclude I defiantly think GNCC Capital shouldreduce their weighted average cost by utilising more debt financing as it ischeaper and will allow GNCC Capital to obtain more ownership of the companyhowever they have to beware of not becoming too over geared as it can createrisk. With saying that I don't completely think GNCC Capital should stop usingequity financing, just reduce the amount as it could potentially create lowerrisk of GNCC Capital becoming bankrupt. Alternatively, if GNCC Capital decide they prefer touse equity capital over debt financing I think the company should firstly tryto increase their market share value by improving managerial decisions such asprofit maximisation and sales maximisation, as a higher market share price willpotentially lower their cost of equity capital and attract more and cheaperinvestors due to a lower risk associated with the firm's operations. However, too much debt financing can make the company overgeared and increase leverage creating some risk for GNCC Capital, because if thereis a change in the company's financial position for example the company'sprofit somehow reduces or interest rates suddenly increase, the company isobliged

to follow repayment schedules or could face bankruptcy. Regardless ofthe company’s financial position lenders will not change interest rates tocompensate which could potentially end a whole projectAdditionally, debt financing has the benefit ofallowing the GNCC to preserve full ownership without any outside interference ofmanagerial decisions made by GNCC which will reduce conflict within the firm.

It also means they don’t have to share as much of their profit withshareholders as lenders receive only the sum of interest agreed on, unlikeequity capital with profits being shared. Discovering that information has led me to theconclusion that for GNCC Capital to reduce their weighted average cost of capitalthey could should issue more debt financing and reduce the amount of equitycapital they use. The main reason why I suggest GNCC use more debt financing isbecause it is considerably cheaper than equity capital it also may help thefirm recollect more profit within the company as with debt financing GNCC Capital’sinterest payments are tax deductible reducing the firms net duty unlike equitycapital when dividends is paid out of profit after tax, beneficially fixedmonthly or annual payments make it easier for the firm to budget and plan theirfinances.

According to Arnold (2012 p 773) “ financing a businessthrough borrowing is cheaper than using equity capital. This if first becauselenders require a lower rate of return than ordinary shareholders” I found thisto be certainly true as when calculating the capital structure and the weightedaverage cost of capital for both GNCC Capital and Magnet Financial services asshow in table 1 and 2, I found the cheapest source of capital for both firmswas bank loan, (debt capital) costing only 7. 5% which was cheaper thanpreference shares

and considerably than equity capital. I think GNCC Capital should definitely aim at reducingtheir weighted average cost of capital and opting for a cheaper source ofcapital as it has benefits such as attracting investors as it increases thevalue and reputation of firm and furthermore will widen their businessopportunities by allowing them to accept low return projects and still increasevalue.

CHEAPER SOURCES OF FINANCEAND IDEAS ON REDUCING WEIGHTED AVERAGE COST OF CAPITAL   To conclude, aftermuch analysing it is almost certain that GNCC Capital, concerns for capital iscorrect and should immediately aim at changing their capital structure toreduce their weighted average cost of capital. The negatives of utilisingequity capital most defiantly outweigh the positive, such as issues likeconflict with in the firm due to outside forces influencing decisions also thehigher cost of burden and potential reduction in profits for GNCC Capital. However, having too much equity capital may not alsobe a completely bad idea for GNCC Capital, as a high amount of use of equitycapital ensures a lower risk of bankruptcy for GNCC Capital. This is becausedividends payments can be deferred if the firm is having some financialproblems and any form of cash flow can be directed into improving the firm'soperation to relieve themselves from a financial crisis. Your worries of Magnet financial services attractingcheaper sources of finance is very accurate. This is due to Company Capital'sweighted average cost of capital being 1.

34% higher than their competitorsMagnet financial services meaning there is a higher risk associated with thefirm's operation which may be deemed unattractive to investors and lead themmore towards their competitors.

Moreover, Magnet Financial Services may beattracting cheaper sources of finance because they have a higher market shareprice by £15 in comparison to GNCC Capital, meaning a lower risk is associatedwith Magnet Financial Services operation meaning the required rate of returnwill be significantly lower making there cost of equity capital cheaper andreducing the companies weighted average cost of capital. Additionally, an important disadvantage or equityfinancing is the share in profit. according to Modigliani and Miller (1958 p 263) " Inparticular, the use of debt rather than equity funds to finance a given venturemay well in- crease the expected return to the owners, but only at the cost ofin- creased dispersion of the outcomes." Which supports my theory that if the company has a great turnover and takesoff they will have to share a proportion of the earnings with its shareholderswhich could potentially lead to the dispersal of profits over the long termexceeding what GNCC Capital could have repaid on a loan.

Another flaw of GNCC Capital using equity capital as aform or capital financing is the expected pressure applied by shareholders. Asmentioned before because of the uncertainty and risk investors hold they mayapply pressure on the firm on achieving a high rate of return on thereinvestment which may cause conflict with management as it could affect GNCCCapital's goals and plan. I think the main cause of GNCC Capital's high weightedaverage cost of capital is there flawed capital structure, they are simplyusing way too much equity capital. Equity capital is money that is investedinto the business by investors in conversion of a share of the company with anexpected rate of return normally set by investors. If you look in table 1, wecan see that equity capital (earning shares and retained

earnings) is astaggering 64. 7% proportion of GNCC capital structure and cost the highestamount (14.

8%) in comparison to the other sources of capital in the structuresuch as bank loan (7. 5%) and preference shares (7. 62%). The reason why equitycapital is typically more expensive is because its holds a higher risk forshareholder, the definite return of the investment is uncertain for investorsin comparison to a fixed obligated amount earned by debt financers if GNCCCapital was to go bankrupt equity shareholders would be the last to get theirmoney back with debt lenders and preference shares being a priority. Furthermore, financing through equity also necessitates other expenditures such asunderwriting fees, brokerage and a merchant banker which just adds to GNCCCapital’s expenditures.