

Monyetla Project – Accounting Gr 12

Lesson 5: Companies: Analysis and Interpretation, Audit Report and Corporate Governance

ACTIVITY 1: MORE LIMITED

COMPANIES – AUDIT REPORT AND CORPORATE GOVERNANCE

(15 marks; 12 minutes)

1.1

1.1.1	D ✓
1.1.2	A ✓
1.1.3	B ✓
1.1.4	C ✓

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1.2 AUDIT REPORT

1.2.1

Where, why and when is this audit report expected to be presented?	
Where	<p>Any one valid answer ✓</p> <p>At the Annual General Meeting (AGM) On the Annual Report to shareholders On financial publications and newspapers On the internet</p>
Why	<p>Any one valid answer ✓</p> <ul style="list-style-type: none"> • Inform shareholders/potential investors about the performance/progress of the company. • If there is any compliance with the IFRS. • Transparency • Public company financial statement needs to be published (requirement of Companies Act) • Independent/External Auditors, appointed by shareholders, are answerable to them.
When	<p>Any one valid answer ✓</p> <p>At the end of the financial period Upon completion of the independent audit process On the date of the AGM and thereafter</p>

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1.2.2

Provide TWO points why the independent auditors make reference to pages 12 – 30 of the Annual Report.

Any two valid points ✓✓ ✓✓ **part marks for incomplete / partial answers**

- The financial statements are contained in those pages of the Annual Report; other reports are also included in the Annual Report, which were not prepared or inspected by them.
- The auditors are responsible for a certain part of the report.
- Directors are responsible for parts of the report as prepared by them.

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1.2.3

Explain TWO points on the impact of this report on the company.

Any two valid points ✓✓ ✓✓ **part marks for incomplete / partial answers**

- Prospective investors **may** no longer be interested to this company **(impact on demand for shares / market price)**
- Existing shareholders may want to sell their shares.
- It will ruin the reputation/image of the company.
- Will reduce the value of shares on the JSE **(1-mark option)**

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TOTAL MARKS		15
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ACTIVITY 2: HADLEY LTD

COMPANIES: ANALYSIS AND INTERPRETATION

(40 marks; 32 minutes)

2.1 Calculate the missing figures indicated by (a) – (e) in the Fixed Asset Note.

	CALCULATIONS	AMOUNT
(a)	$R6\ 800\ 000 - R5\ 800\ 000$	R1 000 000 ✓✓
(b)	$R840\ 000 + R960\ 000$	R1 800 000 ✓✓
(c)	$R850\ 000 - R180\ 000$	R670 000 ✓✓
(d)	<p>Previous years: $10/100 \times R150\ 000 = R15\ 000$ $10/100 \times R150\ 000 = R15\ 000$</p> <p>Current year: $10/100 \times R150\ 000 \times 6/12 = R7\ 500$</p> <p>Total depreciation: $R30\ 000 \checkmark + R7\ 500 \checkmark \checkmark$ $R150\ 000 \checkmark - R37\ 500$</p>	R112 500 ☑
(e)	<p>R7 500 See (d)</p> <p>Old: $10/100 \times R700\ 000 = R70\ 000$</p> <p>New: $10/100 \times R400\ 000 \times 6/12 = R20\ 000$</p> <p>$R7\ 500 \checkmark + R70\ 000 \checkmark \checkmark + R20\ 000 \checkmark \checkmark$ Sold old / remaining new</p>	R97 500 ☑

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2.2 Calculate the Debt-Equity ratio for 2019.

2 100 000 ✓ : 11 000 250 ✓

0,19 : 1 ✓

3

2.3

The directors decided to increase the loan during the current financial year. Explain TWO financial indicators to indicate why this was a good decision. Quote figures.

Financial indicator ✓✓ Trend and figures ✓✓ Comment ✓✓ ✓✓

ROTCE

This has decreased from 21,3% to 20.9%.

Positively geared as ROTCE is higher than the interest rate of 12%

Debt-Equity

This has increased from 0,13 : 1 to 0,19 : 1.

Low financial risk / not making use of loans / relies more on own capital

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2.4

The board of directors is of the opinion that the shareholders should be happy with their percentage return and the market price of their shares. Quote and explain TWO financial indicators with figures to support their opinion.

Financial indicator ✓✓ Trends and figures ✓✓ Comments ✓✓

ROSHE

Improved from 12,3% to 15,7% and it is 8,2% more than the interest (7,5%) in alternative investments.

NAV

NAV per share of 1 608 cents is less than the market price of 1 680 cents.

6

2.5

The Cash Flow Statement reflects some important decisions taken by the Directors.

Apart from the loans, identify TWO good decisions. Explain the effect of this decision on the company. Quote figures.

DECISION Decision ✓✓ Figures ✓✓	EFFECT ON COMPANY ✓✓
Sale of land and building, R1 000 000 / Selling of fixed assets R1 112 500	Increased the cash flow. / Used funds to buy other fixed assets.
Issue of shares R1 800 000 /	Increased the cash flow. / Used funds to buy assets.
Purchase of fixed assets 900 000 + 400 000 = R1 300 000	Leads to capital growth (future productivity). / More assets in the company. / Generates more income.

6

TOTAL MARKS	
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40

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ACTIVITY 3: LOCK LTD & DOWN LTD

COMPANIES – INTERPRETATION OF COMPANY INFORMATION

(35 marks; 25 minutes)

3.1 Compare the liquidity position of both companies and comment on the company that is managing the short term assets more effectively.

Financial indicators (with figures and trend) ✓✓ ✓✓
 Comment on **one** company ✓✓

-1 for additional irrelevant financial indicators

LOCK LTD

Although current ratio decreased from 2,1 : 1 to 1,9 : 1, the acid test ratio remains fairly consistent at 1,3 : 1 compared to 1,4 : 1 the previous year.

DOWN LTD

The acid test ratio is consistent at 1,5 : 1 whilst the current ratio increased from 2,8 : 1 to 3,6 : 1

COMMENT

Marks for only ONE company

Lock Ltd appears to control working capital more efficiently by ensuring that stock is moving. They also have enough current assets (cash) to meet short term liabilities

OR

Down Ltd is not managing stock effectively. Whilst they would not experience cash flow problems, they are holding too much stock which may contribute to low profitability.

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3.2 Compare the dividend pay-out policy of each company.

LOCK LTD

Dividend pay-out rate is 52% (45/86) compared to 81% (65/80) in 2019 ✓✓

DOWN LTD

Dividend pay-out rate is 86% (60/70) in 2020 and 86% (62/72) in 2019. Down Ltd has maintained the dividend pay-out rate at 86% ✓✓

4

Provide TWO possible reasons why one company decided to change their policy.

Any **TWO** reasons ✓✓ ✓✓ **part marks for incomplete / partial answers**

They are retaining earnings to concentrate on growth

They want to ease cash-flow problems and continue managing expenses to improve profitability

They want to sustain the trend of increasing profitability and return on equity so shareholders can see the long-term prospects of the company

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3.3

Lock Ltd decided to increase their loans during the current financial year, whilst Down Ltd decided to maintain their existing loans. Comment on the decisions of both companies. Make reference to the degree of risk and gearing.

LOCK LTD
Financial indicator with figures & trend ✓✓
Comment explaining gearing effect ✓✓

Debt/ equity ratio increased from 0,3 : 1 to 0,6 : 1 **one mark**

ROTCE increased from 12% to 15% **one mark**

Although the business is now highly geared the loan is being effectively used to improve profitability. Business is positively geared so the decision was appropriate **two marks**

DOWN LTD
Financial indicator with figures & trend ✓✓
Comment explaining gearing effect ✓✓

Debt/ equity ratio remained constant at 0,4 : 1 **one mark**

ROTCE decreased from 13% to 11,7% **one mark**

Although the business is low geared the loan is not being effectively used as the business is negatively geared so it would be wise to start paying back the loan, or improve strategies to improve profitability. **two marks**

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3.4

A shareholder of Down Ltd is concerned about the drop in the market price of the shares. Explain why they feel this way. Provide TWO points.

Any **TWO** valid points ✓✓ ✓✓ **part marks for incomplete / partial answers**

This reflects **that** public demand for shares is low/ public confidence in company has decreased

Shareholders want capital growth on their investment

Directors will be judged on the performance of the shares

The market price dropped below the net asset value

4

3.5 M. Mtolo owns 576 000 shares in Down Ltd, which represents 48% of the total issued shares. He wants to purchase another 25 000 shares.

Do a calculation to show how this would change his % shareholding in the company.

(576 000 + 25 000) two marks (576 000 ÷ 48%) two marks 50,08% accept
 601 000 ✓✓ ÷ 1 200 000 ✓✓ x 100 = 50,1% one part correct
 Must be 50,1% (not 50%)

5

Provide TWO reasons why you think he is specifically interested in increasing his shareholding in Down Ltd.

TWO points ✓✓ ✓✓ accept short statements for two marks
 He wants to be the majority shareholder
 He wants to influence strategic decisions
 He is aware of the poor performance of the business and thinks that he can make a difference.
 He sees potential in the company and wants to be part of the future growth
 He wants to implement corrective measures to address the downward trends in many of the financial indicators.

4

TOTAL MARKS		35
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