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CA INTERMEDIATE

SUBJECT- F.M.

Test Code – CIM 8622

BRANCH - () (Date :)

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ANSWER 1

Income Statement

Particulars	Amt. (Rs.)
Sales	75,00,000
Less : Variable cost (56% of 75,00,000)	(42,00,000)
Contribution	33,00,000
Less : Fixed costs	(6,00,000)
Earnings before interest and tax (EBIT)	27,00,000
Less : Interest on debt @ 9% on Rs. 45 lakhs)	(4,05,000)
Earnings before tax (EBT)	22,95,000

(2 MARKS)

(i) ROI = $\frac{\text{EBIT}}{\text{Capital employed}} \times 100 = \frac{\text{EBIT}}{\text{Equity+Debt}} \times 100$

$= \frac{27,00,000}{55,00,000+45,00,000} \times 100 = 27\%$

(ROI is calculated on Capital Employed)

(1 MARK)

(ii) ROI = 27% and Interest on debt is 9%, hence, it has a favourable financial leverage.

(1 MARK)

(iii) Capital Turnover = $\frac{\text{Net Sales}}{\text{Capital}}$

OR = $\frac{\text{Net Sales}}{\text{Capital}} = \frac{\text{Rs.}75,00,000}{\text{Rs.}1,00,00,000} = 0.75$

Which is very low as compared to industry average of 3.

(1 MARK)

(iv) Calculation of Operating, Financial and Combined leverages

(a) Operating Leverage = $\frac{\text{Contribution}}{\text{EBIT}} = \frac{\text{Rs.}33,00,000}{\text{Rs.}27,00,000}$ = 1.22 (approx.)

(b) Financial Leverage = $\frac{\text{EBIT}}{\text{EBT}} = \frac{\text{Rs.}27,00,000}{\text{Rs.}22,95,000}$ = 1.18 (approx.)

(c) Combined Leverage = $\frac{\text{Contribution}}{\text{EBT}} = \frac{33,00,000}{\text{Rs.}22,95,000}$ = 1.44 (approx.)

Or = Operating Leverage × Financial Leverage = 1.22 × 1.18 = 1.44 (approx)

(1.5 MARKS)

(v) Operating leverage is 1.22. So if sales is increased by 10%. EBIT will be increased by 1.22 × 10 i.e. 12.20% (approx.)

(1 MARK)

(vi) Since the combined Leverage is 1.44, sales have to drop by 100/1.44 i.e. 69.44% to bring EBT to Zero

Accordingly, New Sales = Rs. 75,00,000 × (1 – 0.6944)

= Rs. 75,00,000 × 0.3056

= Rs. 22,92,000 (approx.)

Hence at Rs. 22,92,000 sales level EBT of the firm will be equal to Zero.

(1.5 MARKS)

(vii) Financial leverage is 1.18. So, if EBIT increases by 20% then EBT will increase by 1.18 × 20 = 23.6% (approx.)

(1 MARK)

ANSWER 2

Net worth = Capital + Reserves and surplus

= 4,00,000 + 6,00,000 = Rs. 10,00,000

$$= \frac{\text{Total Debt}}{\text{Networth}} = \frac{1}{2}$$

∴ Total debt = Rs. 5,00,000

Total Liability side = Rs. 4,00,000 + Rs. 6,00,000 + Rs. 5,00,000

= Rs. 15,00,000

= Total Assets

Total Assets Turnover = $\frac{\text{Sales}}{\text{Total assets}}$

$$2 = \frac{\text{Sales}}{\text{Rs.15,00,000}}$$

∴ Sales = Rs. 30,00,000

Gross Profit on Sales : 30% i.e. Rs. 9,00,000

∴ Cost of Goods Sold (COGS) = Rs. 30,00,000 – Rs. 9,00,000

= Rs. 21,00,000

Inventory turnover = $\frac{\text{COGS}}{\text{Inventory}}$

$$3 = \frac{\text{Rs.21,00,000}}{\text{Inventory}}$$

∴ Inventory = Rs. 7,00,000

Average collection period = $\frac{\text{Average debtors}}{\text{Sales / day}}$

$$40 = \frac{\text{Debtors}}{\text{Rs.30,00,000/360}}$$

∴ Debtors = Rs. 3,33,333.

Acid test ratio = $\frac{\text{Current Assets} - \text{Stock (Quick Asset)}}{\text{Current Liabilities}}$

$$0.75 = \frac{\text{Current Assets} - \text{Rs.7,00,000}}{\text{Rs.5,00,000}}$$

∴ Current Assets = Rs. 10,75,000.

∴ **Fixed Assets** = Total Assets – Current Assets

= Rs. 15,00,000 – Rs. 10,75,000 = Rs. 4,25,000

Cash and Bank Balance = Current Assets – Inventory – Debtors

= Rs. 10,75,000 – Rs. 7,00,000 – Rs. 3,33,333 = Rs. 41,667

(7 MARKS)

Balance Sheet as on March 31, 20X8

Liabilities	Rs.	Assets	Rs.
Equity Share Capital	4,00,000	Plant and Machinery and Other Fixed Assets	4,25,000
Reserves & Surplus	6,00,000	Current Assets :	
Total Debt :		Inventory	7,00,000
Current liabilities	5,00,000	Debtors	3,33,333
		Cash	41,667
	15,00,000		15,00,000

(3 MARKS)