CBSE Test Paper 02

Ch-10 Statement Analysis Tools and Accounting Ratios

1. Which of the following is not a part of Long Term Borrowings?
   a. Debentures
   b. Mortgage Loan
   c. Bank Overdraft
   d. Public Deposits
2. Accounting Ratio is
   a. Based on cash transactions only
   b. It is arithmetical relationship between two accounting variables
   c. Based on credit transactions only
   d. tool used by individuals to conduct a quantitative analysis of information
3. Debt to Equity Ratio of Vinod Limited is 2:1. Company purchased a Machinery of Rs.2,00,000 by taking a long term loan. What will be the effect on ratio?
   a. Decrease
   b. No Effect
   c. Increase
   d. Increase and decrease in debt and equity
4. Which of the following is not a Quick Asset_______
   a. Trade Receivables
   b. Loose Tools
   c. Cheques in hand
   d. Bank Balance
5. Liquidity ratios are expressed in
   a. Pure ratio form
   b. Rate or time
   c. Percentage
   d. None of these

6. What is meant by ‘Net Profit Ratio’?

7. Is a higher debt-equity ratio acceptable?

8. The Gross Profit Ratio of a company is 50%. State with reason whether the decrease in rent received by Rs. 15,000 will increase, decrease or not change the ratio.

9. The current ratio of Vinod Textiles Ltd. is 0.8 at present. In the future, it wants to improve this to 2. Suggest any two accounting transactions for improving the current ratio.

10. What is Stock Turnover Ratio?

11. The quick ratio of a company is 2 : 1. State with giving reasons, (for any four) which of the following would improve, reduce or not change the ratio

    i. Purchase of machinery in cash.
    ii. Purchase of goods on credit.
    iii. Sale of furniture at the price at which it is purchased.
    iv. Sale of goods at a profit.
    v. Cash received from debtors.

12. i. From the following, calculate 'Trade receivables turnover ratio'.

Total revenue from operations for the year	Rs. 8,40,000
Cash revenue from operations	40% of credit revenue from operations
Closing trade receivables	Rs. 2,00,000
Excess of closing trade receivables over opening trade receivables	Rs. 80,000

ii. From the following information calculate 'Interest coverage ratio'

Profit after interest and tax	Rs. 4,97,000
Rate of income tax	30%
12% debentures	Rs. 6,00,000

13. The current ratio of a company is 2.1 : 1.2. State with reasons which of the following transactions will increase, decrease or not change the ratio.

    i. Redeemed 9% debentures of Rs. 1,00,000 at a premium of 10%.

ii. Received from debtors Rs. 17,000.
iii. Issued Rs. 2,00,000 equity shares to the vendors of machinery.
iv. Accepted bills of exchange drawn by the creditors Rs. 7,000.

14. From the following information, prepare a summarised Balance Sheet as at March 31, 2019.

Working capital	2,40,000
Bank Overdraft	40,000
Fixed Asset to Proprietary Ratio	0.75
Reserve & Surplus	1,60,000
Current Ratio	2.5
Liquid Ratio	1.5

CBSE Test Paper 02
Ch-10 Statement Analysis Tools and Accounting Ratios

Answer

1. c. Bank Overdraft, **Explanation:** Borrowings for more than one year validity can be termed as long term borrowings. Bank overdraft is meant for a short period and therefore will be treated as current liability.
2. b. It is arithmetical relationship between two accounting variables
   Explanation: Accounting Ratio is also called financial ratios provide a way of expressing the relationship between one accounting data point and another which is intended to provide a useful comparison.
3. c. Increase, **Explanation:** Debt Equity ratio will increase because long term debts will increase but there is no change in equity.
4. b. Loose Tools, **Explanation:** Assets which can be easily converted into cash can be termed as quick assets. Loose tools having least liquidity
5. a. Pure ratio form, **Explanation:** Pure ratio form

6. Net Profit Ratio indicates the relationship between 'Net Profit' and 'Net Revenue from Operations' (sales). It helps in determining the overall efficiency of the business operation. An increase in the ratio over the previous year shows improvement in the overall efficiency and profitability of the business.

7. **No**, because it represents more risk on the financial stability of an enterprise.

8. Not change the ratio:- Rent received Rs. 15,000 does not affect the gross profit. Because rent received is a indirect income and it is not a part of gross profit.

9. The current ratio is a liquidity ratio that measures whether or not a firm has enough resources to meet its short-term obligations. It compares a firm's current assets to its current liabilities.

   i. Payment of current liabilities,
   ii. The issue of share capital or raising a long-term loan.

10. Stock Turnover Ratio = $\frac{\text{Cost of Goods Sold}}{\text{Average Stock or Inventory}}$

It reflects the relationship between the cost of goods sold and the average amount of inventory carried during that period.

11. i. **Purchase of Machinery for Cash**

Effect <u>Reduce</u>

Reason Purchase of machinery for cash will decrease the quick assets because there is a cash outflow in the business, but the current liabilities will remain unchanged.

ii. **Purchase of Goods on Credit**

Effect <u>Reduce</u>

Reason Purchase of goods on credit will increase the current liabilities because we have to pay it afterwards, but the quick assets will remain unchanged

iii. **Sale of Furniture at Cost at which it is purchased**

Effect <u>Improve</u>

Reason Sale of furniture at cost price at which it is purchased will increase the quick assets because there is an inflow of cash in the business, but the current liabilities will remain unchanged

iv. **Sale of Goods at a Profit**

Effect <u>Improve</u>

Reason Sale of goods at a profit will increase the quick assets because by sale quick assets will increase, but the current liabilities will remain unchanged.

v. **Cash Received from Debtors**

Effect <u>No change</u>

Reason Cash received from debtors will not change the quick assets because the quick assets are increased and decreased with the same amount as the cash recieved added in cash and the same amount is subtracted from debtors, and the current liabilities remain unchanged.

12. i. Trade Receivables Turnover Ratio $= \frac{\text{Credit Revenue from Operations *}}{\text{Average Trade Receivables *}} = \frac{6{,}00{,}000}{1{,}60{,}000}$ = 3.75 times

Let, credit revenue from operations be x

Cash revenue from operations be x $\times$ 40% = 0.4x

Total Revenue from Operations = Cash Revenue from Operations + Credit Revenue from Operations

8,40,000 = 0.4x + x

8,40,000 =1.4x

*Credit revenue from operations $\Rightarrow$ x $\Rightarrow$ 6,00,000

**Average Trade Receivables $= \frac{\text{Opening Trade Receivables} + \text{Closing Trade Receivables}}{2}$

= $\frac{1{,}20{,}000 + 2{,}00{,}000}{2}$

Closing trade receivables- opening trade receivables = 80,000

Closing trade receivables = 2,00,000

Opening trade receivables = 2,00,000 - 80,000 = 1,20,000

NOTE: Trade receivables include Debtors and Bills receivable.

ii.Interest Coverage Ratio $= \frac{\text{Net Profit before Interest and Tax}}{\text{Interest on Long-term Borrowings}} = \frac{7{,}82{,}000}{72{,}000}$ = 10.86 times

Net profit after interest and tax	= 4,97,000
(+) Tax (4,97,000 $\times$ 30 / 70)	= 2,13,000
(+) Interest on debentures (6,00,000 $\times$ 12%)	= 72,000
Net profit before interest and tax	Rs. 17,82,000

Profit before Interest and Tax = Profit after tax + Tax + Interest This ratio shows how many times the interest charges are covered by the profits available to pay interest.

13.
1. **Decrease:** Current assets will decrease because of outflow of cash but current liabilities will remain unchanged therefore current ratio will decrease.
2. **No change:** Both debtors and cash/bank are current assets, so increase and decrease in current assets by the same amount leaves current ratio unaffected.
3. **No change:** Since non- current assets and non-current liabilities are increased by the same amount and have no effect on current assets and current liabilities, therefore the current ratio remains the same.
4. **No change:** Here, only one current liability is converting to another current liability(i.e creditors into bills payable). Thus, the current ratio remains unaffected.

14. **Construction of Balance Sheet:**

Liability	Rs.	Assets	Rs.
Capital	800000	Fixed Asset	7,20,000
Reserve & Surplus	160000	Stock	160000
Bank Overdraft	40000	Other Current Asset	240000
Sundry Creditors	120000		
	11,20,000		11,20,000

Working Note : Proprietary Ratio = $\frac{FA}{Propreitary\ Fund}$ = 0.75 Fixed Asset = 0.75

$\times$Proprietary Fund

Net working Capital = 0.25$\times$Proprietary Fund

Proprietary Fund = 240000/0.25= 960000

Fixed Asset = 0.75$\times$960000 = **720000**

Capital = 960000-160000 = **800000**

Creditors = 160000-40000= **120000**

Current Asset and current liability computation

$$\frac{Current Asset}{Current Liability} = \frac{2.5}{1}$$

Current Asset = 2.5$\times$Current liability

Working capital = C.A. - C.L.

240000 = 2.5$\times$C.L. - C.L.

240000 = 1.5$\times$C.L.

Curret liability = 240000/1.5 = **160000**

Current Asset = 160000$\times$2.5 = **400000**

Computation of Stock

Liquid Ratio = $\frac{LA}{CL}$

1.5$\times$160000 = 400000- Stock

Stock = **160000**