



UNIVERSITY OF CAMBRIDGE INTERNATIONAL EXAMINATIONS
Cambridge International Diploma in Business
Standard Level

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BUSINESS FINANCE

5163/01

Optional Module

May 2011

2 hours plus 15 minutes' reading time

Additional Materials: Answer Booklet/Paper

READ THESE INSTRUCTIONS FIRST

Write your Centre number, candidate number and name on all the work you hand in.

Write in dark blue or black pen.

You may use a soft pencil for any diagrams, graphs or rough working.

Do not use staples, paper clips, highlighters, glue or correction fluid.

Attempt **all** tasks.

Start each task on a new piece of paper.

Please leave a margin on the right and left hand side of each new page.

At the end of the examination, fasten all your work securely together, in the correct order.

The number of marks is given in brackets [] at the end of each question or part question.

This document consists of **5** printed pages and **3** blank pages.



You must read the case study below and attempt ALL of the tasks that follow.

(This case study is fictitious.)

M & S Medical Supplies Ltd.

M & S Medical Supplies Ltd has been in business for five years and it is widely regarded as one of the more reputable firms in the industry. The business had been formed by two friends, Mohammad and Sunil, who were both qualified doctors. Originally they had set up in business as a limited partnership, but after two years of trading they decided to establish a limited company. They had both contributed the same amount of initial capital and currently they still have \$50 000¹ of authorised but unissued capital. 5

The company supplies hospitals and clinics with a full range of medical products ranging from bed linen to medical instruments and medicines. All of these products are bought from other suppliers and then sold on with a fixed percentage mark up of 25%. Mohammad has always insisted that this policy was the key to the firm's success, whilst Sunil believes that the firm should be more flexible and that they should adopt a policy of having variable gross profit margins on their products. He considers that such a policy will ensure that they are able to compete more effectively with competitors. 10

A recent report, produced by a firm of management accountants, appears to support Sunil's argument, but as yet there has been no decision to change the pricing policy. Mohammad has pointed out that both the company's financial accountant and the external auditor are pleased with the financial stability of the company and do not see any benefits in changing the pricing policy at this moment in time. In addition to selling goods to customers the company also provides some products for hire but this is not a major source of profit for the firm. 15

Mohammad and Sunil have agreed that there is a need to diversify by moving into the manufacture of some of the products that they supply. They intend to do this by buying a factory from one of their suppliers. This will necessitate raising a considerable amount of additional capital and they have been gathering information about the possible sources of capital. They have also collected information regarding the likely costs of production and the possible revenues that could be expected from sales. As neither of them have any practical experience of manufacturing or any formal accounting qualifications, they have commissioned a firm of management accountants to produce a business plan for this proposal. 20 25

The company's bank manager has been very supportive of the company and has increased the credit facility of the business on a number of occasions. He is however, very concerned that the movement into manufacturing could have a profound effect on the level of working capital. He has suggested that the company should adopt a much tighter approach to monitoring the level of working capital, in order to avoid any problems. He has also suggested that the company should adopt a cost-centred approach when the manufacturing takes place and this will involve monitoring both contribution and profit levels for each product. 30

Recent announcements by the government appear to indicate that the economy is beginning to recover from the economic downturn and it is expected that there will be a growth rate of 3% in the economy over the next year. However, the foreign exchange market is likely to remain uncertain during the next six months and domestic interest rates may have to be increased to bring about some stability in the financial markets. 35

¹ Quoted in US dollars

Financial Information

Item A

Information extracted from the balance sheet of M&S Medical Supplies Ltd for the year ending 30th April 2011.

	\$
Cash in hand	2 500
Work in progress	4 000
Debtors	11 000
Raw materials	6 500
Provision for taxation	4 000
Finished goods	3 500
Creditors	7 300
Overdraft	8 000

Item B

Cost and Revenue information for hire of bed linen and medical instruments is given below.

Bed linen

The company currently has 8 clients. Assume each client hires one bundle of bed linen per week.

Revenue per bundle per week \$80

Costs per week - Washing \$10 per bundle

Delivery and collection \$12 per bundle

Medical instruments

The company currently has 6 clients. Assume each client hires one set of medical instruments per week.

Revenue per set per week \$100

Costs per week - Sterilising and sharpening \$12 per set

Delivery and collection \$10 per set

The company has estimated that the fixed costs associated with the hire services will be \$44 200 per year.

You must attempt ALL of the following tasks.

Where appropriate use information from the case study to support your answer.

- 1 (a) (i) Explain what is meant by a limited partnership. [3]
 (ii) Explain **one** advantage and **one** disadvantage of operating as a limited partnership. [2 x 2 = 4]
- (b) (i) Explain what is meant by a percentage mark up and what is meant by a gross profit margin. [2 x 2 = 4]
 (ii) The company bought some medical instruments for \$400 each. It applied the normal 25% mark up to obtain the selling price. Using this selling price, calculate the gross profit percentage that would be achieved on the sale of the instruments. [3]
- (c) Explain the role of an external auditor of the company. [3]
- (d) Explain how **one** of the external factors mentioned in the final paragraph of the case study could affect the profitability of the company in the near future. [3]
 [Total: 20]
- 2 (a) Identify **four** sources of finance that the company could use to fund the manufacturing proposal. [4 x 1 = 4]
 (b) Explain **one** advantage and **one** disadvantage of using **each** of the sources identified in 2 (a). [4 x 4 = 16]
 [Total: 20]
- 3 (a) (i) Describe **three** tasks undertaken by a financial accountant. [3 x 2 = 6]
 (ii) Describe **three** tasks undertaken by a management accountant. [3 x 2 = 6]
 (b) Identify **two** internal and **two** external users of the accounts of M & S Medical Supplies Ltd. [4 x 1 = 4]
 (c) Explain how **each** of the users identified in 3 (b) above would use the accounts. [4]
 [Total: 20]
- 4 (a) Explain what is meant by the term working capital. [3]
 (b) Using the information in **Item A**, calculate the current working capital of M & S Medical Supplies Ltd. [3]
 (c) Explain **three reasons** why it is important for a business to monitor the level of working capital. [3 x 2 = 6]
 (d) List and explain **four** ways by which M & S Medical Supplies Ltd could increase the level of working capital. [4 x 2 = 8]
 [Total: 20]

- 5 (a) Explain what is meant by contribution and profit. [4]
- (b) Using the information available in **Item B**, calculate the weekly contribution for **both** of the hire contracts. [2 x 6 = 12]
- (c) Calculate the overall weekly profit for the hire services of the business. [4]
- [Total: 20]

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