

5 Ajay is a retailer. He has provided the following information.

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At 1 April 2023

Inventory	5 200
Trade receivables	6 875
Cash at bank	1 946
Trade payables	5 115

For the year ended 31 March 2024

Revenue – credit sales	86 400
– cash sales	10 600
Purchases	51 300
Expenses	23 750

At 31 March 2024

Inventory	6 500
Trade receivables	9 550
Cash at bank	1 200
Trade payables	6 000

REQUIRED

(a) Complete the following table.

ratio	working	answer
Gross margin (to 2 decimal places)		
Profit margin (to 2 decimal places)		
Rate of inventory turnover (times) (to 2 decimal places)		
Trade receivables turnover days (round up to next whole day)		
Liquid (acid test) ratio (to 2 decimal places)		

[11]

Ajay has been trading for 3 years and he has established a good reputation. He has never changed his selling price. His gross margin for the year ended 31 March 2024 is higher than for the previous years.

REQUIRED

(b) (i) Suggest **one** reason why Ajay’s gross margin has increased.

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 [1]

(ii) State **one** reason why Ajay’s customers might be interested in his financial statements.

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 [1]

Ajay is concerned about the levels of his inventory and trade receivables. He is considering reducing his selling price.

REQUIRED

(c) Advise Ajay whether or not he should reduce his selling price. Justify your answer by providing advantages and disadvantages of reducing his selling price.

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..... [5]

Although Ajay’s gross margin has increased, his profit margin has fallen for each of the last two years. Sales revenue is Ajay’s only income.

REQUIRED

(d) State **two** reasons why Ajay should be concerned about his falling profit margin.

1
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2
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..... [2]

[Total: 20]

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Question	Answer	Marks
5(a)	<p>Gross margin:</p> <p>Cost of sales $5\,200 + 51\,300 - 6\,500 = 50\,000$ Gross profit $97\,000 - 50\,000 = 47\,000$</p> <p>Gross margin = $\frac{47\,000 \text{ (1)}}{97\,000} \times \frac{100}{1} = 48.45\% \text{ (1)}$</p> <p>Profit margin:</p> <p>Profit $47\,000 \text{ OF} - 23\,750 = 23\,250$</p> <p>Profit margin = $\frac{23\,250 \text{ (1) OF}}{97\,000 \text{ CF}} \times \frac{100}{1} = 23.97\% \text{ (1) OF}$</p> <p>Inventory turnover:</p> <p>$\frac{50\,000 \text{ (1) OF}}{(5\,200 + 6\,500) / 2 = 5850 \text{ (1)}} = 8.55 \text{ times (1) OF}$</p> <p>Trade receivables turnover</p> <p>$\frac{9\,550}{86\,400} \times \frac{365 \text{ (1)}}{1} \text{ whole formula} = 41 \text{ days (1) OF}$</p> <p>Liquid (acid test) ratio</p> <p>$(9\,550 + 1\,200) : 6\,000 \text{ (1) whole formula} = 1.79:1 \text{ (1) OF}$</p>	11
Question	Answer	Marks
5(b)(i)	<p>His purchase price has fallen / he has been allowed trade discount (1) His sales mix has changed (1) Max (1)</p>	1
5(b)(ii)	<p>Whether Ajay will be able to continue in business/continue being able to supply them (1)</p>	1

Question	Answer	Marks
5(c)	<p>Advantages Should increase sales / attract new customers (1) May increase profit for the year (1) Should increase rate of inventory turnover (1) Reduces risk of inventory deteriorating / becoming damaged / obsolete (1) Reduces cost of holding inventory (storage, insurance) (1) May improve his reputation (1) Accept other valid points Max (3)</p> <p>Disadvantages Would reduce gross margin / gross profit / profit for the year / profit margins / may make a loss (1) Less money coming in from each unit sold / liquidity reduced (1) Customers may question the quality of the goods / it may damage his reputation (1) Customers may be unwilling to pay the full price in future (1) It may be better to offer cash discount to reduce trade receivables (1) Accept other valid points Max (3)</p> <p>Max (4)</p> <p>Recommendation (1)</p>	5

Question	Answer	Marks
5(d)	<p>May result in loss if expenses continue to increase (1) He may not be able to pay expenses / suppliers / wages if they continue to increase (1) The business cannot continue indefinitely if this trend continues (1) Accept other valid points Max (2)</p>	2