Question 22 (12 marks)

Balance Sheet for Chalker Pty Ltd
as at year ending 30 June 2012

	$	$
Current Assets		
Cash	8 000	
Receivables	12 000	
Inventories	15 000	35 000
Non-Current Assets		
Property, Plant and Equipment		33 000
Total Assets		**68 000**
Current Liabilities		
Creditors		14 000
Non-Current Liabilities		
Loan		20 000
Owners Equity		
Capital	15 000	
Retained Net Profit	19 000	34 000
Total Liabilities and Owners Equity		**68 000**

(a) Calculate the current ratio (current assets ÷ current liabilities) of this business. Show all working. **2**

35000 ÷ 14000
= 2.5
= 2.5 : 1

(b) Calculate the debt to equity ratio (total liabilities ÷ total equity) of this business. Show all working. **2**

$\frac{14\,000 + 20000}{34\,000}$
= 1:1

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Question 22 (continued)

(c) Why is it important for a business to control its debt to equity ratio? **4**

The debt to equity ratio ensures that the business has enough equity to cover its total long term and short term liabilities. A business with a low debt to equity or gearing ratio, for example 0.5:1, will not have enough capital or retained profits to cover its total liabilities. If this becomes an issue, a business may have undertake a form of debt finance, such as borrowing from a bank

(d) Explain the interdependence of finance and operations in a business. Support your answer with relevant examples. **4**

All key business functions must work together, or interdependently to ensure their maximum efficiency. The Finance and Operations functions must coincide with each other to undergoe transformation processes with a businesses products and to ensure value adding occurs properly. Finance ensures that the relevant costs associated with operations, eg LOGS, roads of distribution, whareshousing, are recorded and monitored, and this ensures the business does not run into debt, and opens opportunities for cost minimisation on the balance sheet.

End of Question 22