

2. Study the information below and then answer the questions that follow.

Casey's Ltd.

John Casey runs a family-owned DIY company, employing two staff, both of whom have been with him since he and his sister inherited the business 10 years ago. Since a branch of B&Q opened up some eight miles away, business has dipped alarmingly. For this reason John is keen to finalise negotiations to supply a local building company with all its paint requirements for the next three years. This will require him to hold extra stock, but will also enable him to take advantage of a cash discount of 10% from his own paint suppliers, as long as he maintains regular monthly payments. In order to meet the contract requirements he will need to install new storage equipment which he estimates will cost approximately £5 000 – money which he hopes to borrow from the bank.

John regards the investment as worthwhile because he estimates that the contract will increase his annual turnover by £20 000. The building firm will undertake to purchase all its paint from him, at a fixed price, over the next three years. It will also settle its account every six months, at the end of June and December.

John has requested that his sister construct a cash flow forecast based on his plans for the next six months, so that he can use it in the loan negotiations with his bank manager. Currently Casey's has a £2 500 overdraft limit with the bank.

Cash Flow Forecast for Casey's Ltd: January to June 2006.

£s	JAN	FEB	MARCH	APRIL	MAY	JUNE
Receipts						
Cash sales	6 500	6 500	7 500	8 500	9 500	8 500
Contract sales						10 000
Bank loan	5 000					
Total receipts	11 500	6 500	7 500	8 500	9 500	18 500
Payments						
Install new storage equipment	5 000					
Stock purchases	3 500	3 500	4 000	4 500	5 000	4 500
Wages	2 000	2 000	2 000	2 400	2 400	2 400
Insurance		450				
Electricity	150			150		
Telephone			270			270
Advertising	30	30	30	30	30	30
Loan repayments	200	200	200	200	200	200
Drawings	2 300	2 300	2 300	2 500	2 500	2 500
Total payments	13 180	8 480	8 800	9 780	10 130	9 900
Net Cash Flow	(1 680)	(1 980)	(1 300)	(1 280)	(630)	8 600
Opening Balance	2 700	1 020	(i)	(2 260)	(3 540)	(4 170)
Closing Balance	1 020	(960)	(2 260)	(3 540)	(ii)	4 430

- (a) Identify **two** external parties who will want to examine the accounts of a company and explain why they may wish to do so. [6]
- (b) Calculate the following values in the cash flow forecast:
- (i) opening balance for March; [1]
 - (ii) closing balance for May. [1]
- (Write your answers in the answer book.)*
- (c) On the basis of the cash flow forecast **alone**, comment on the view that the bank would be unlikely to grant the loan of £5 000 to Casey's Ltd. [4]
- (d) Suggest ways in which Casey's Ltd could improve its cash flow situation and assess any adverse consequences your suggestions might have. [8]