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AJANAKU PLC

Statement of Profit or Loss for the year ended 31/12/2014

	₦
Revenue (all on credit)	2,000,000
Profit after charging all expenses except debenture interest	220,000
Debenture interest(gross)	20,000
Profit before taxation	200,000
Taxation Expense	88,000
Profit for the year	112,000

Statement of Financial Position as at 31/12/2014

	₦	₦
Non-current Assets (carrying values)		
Property plant and equipment		840,000
Current Assets		
Inventory	500,000	
Receivables	200,000	
Investments	60,000	760,000
		1,600,000
Equity and Liabilities		
400,000 ₦1 ordinary share		400,000
Issued and fully paid 200,000 ₦1 ordinary shares		200,000
Capital Reserves		100,000
Revenue Reserves		400,000
		700,000
Non-current Liability		
200,000 10% Debentures (secured on freehold property) 200,000		200,000
		900,000
Current Liabilities		
Trade Payables	172,800	
Bank overdraft	439,200	
Current Taxation	88,000	700,000
		1,600,000

RATIO ANALYSIS FOR 2014

PROFITABILITY RATIO

Return on (long term) Capital Employed (ROCE) ROCE=Profit before interest and tax/capital employed * 100= ([220,000/900,000]* 100%)	24.4%
Returns on Equity (ROE) ROE=Profit after taxation and preference dividend/share capital and reserves(excluding prefrence share capital) X 100=([112,000/700, 000]* 100%)	16%
Operating Profit Margin (OPM) OPM=Profit after interest and taxation/Revenue * 100=([112,000/2,000,000]* 100%)	5.6%
Gross Profit Margin(GPM) GPM=Gross profit/Revenue* 100%=([500,000/2,000 000]* 100%)	25%

LIQUIDITY RATIO

Current Ratio(CR) CR=Current Assets/Current Liabilities=760, 000/700,000	1.1:1
Quick/Acid Test Ratio(ATR) ATR=Current Asset – Inventories/Current liabilities=260,000/700,000	0.4:1

WORKING CAPITAL EFFICIENCY RATIO

	Days
Average Collection Period ACP=Trade Receivables/Credit Sales*365 days=([200,000/2,000,000]*365days)	36.5
Inventory Turnover Period ITP=Inventory/Cost of sales*365days=([500,000/1, 500,000]*365days)	121.7
Average Payble Period APP=Trade Payables/Purchases*365days=([172, 000/1,080,000]*365days)	58.4

Additional Notes:	₦
Dividends during the year end	53,600
Purchases for the year	1,080,000
Cost of Sales for the year	1,500,000
The market price of Ajanaku Plc ordinary share as 31/12/2014	4

Working Note	₦
Current asset-Inventory=760, 000-60,000	260,000
Capital Employed(share capital+reserves+long term debt)=700,000+200,000	900,000
Gross Profit(revenue-cost of sales)=2,000,000-1,500, 000	500,000

QUESTION 1B

LIQUIDITY RATIO

The Liquidity ratio of Ajanaku Plc is very low and will there not be easy to convert to cash at close to its book values to meet its present obligations. Since Ajanaku Plc cant settle its obligation at such short notice, it will therefore be difficult to sell off its liquid assets. The current ratio shows that the company has relatively low resources to settle its debts over the next twelve months.
Since both the current and acid-test ratios are below the standard of the industry average i.e. 1.1, Ajanaku Plc will be unable to meet its obligations and settle it debts. From the liquidity ratio, we can also say that Ajanaku Plc is going through poor management of its working capital which could be as a result of negotiating fast payment or cash from customers, and long terms of suppliers.

PROFITABILITY RATIO

The Profitability ratio of Ajanaku Plc is very high. From the profitability ratio, we can say that the company is efficiently generating profit from every unit of of share holder's equity and as a result of using its assets and controlling its expenses effectively and efficiently which has now led to an acceptable rear of return. The company's return on both equity and capital employed and its gross profit margin is high which indicates that the company is efficiently using its resources and is generating high income from its operations which could be due to successful marketing or even low cost base. Due to this successful management of its cost of production, the company now has enough money left for its other operations. The profitability ratio of the company has therefore proven that the company is very profitable.

WORKING CAPITAL EFFICIENCY RATIO

Apart from the Inventory turnover period which appears that inventories have been managed poorly, the working capital efficiency ratio is good by general standard. The inventory turnover period is very high meaning that the

company holds inventory for too long before selling or using it. Hence it is very very inefficient.

COMPARISON

The liquidity ratio compared to profitability ratio is very low which is due to insufficient current assets to cover up its debts. Even though they make profit, some part of this profit still has to be kept in reserves thereby, leaving them with little or no profit. Due to this problem, the company may also be burdened with debts which the company's profit may suffer while paying these debts. The liquidity ratio is also in comparison with the working capital efficiency ratio due to insufficient liquid resources thereby affecting working capital and making it impossible to settle debts. Even though the company's profit performance is very good, flaws and deficiencies can still be found its liquidity and working capital efficiency ratio.

Liquidity is critically important for any company. If a company cannot meet its financial obligations, then it is in serious danger of bankruptcy, no matter how rosy its prospects for future growth may be. However, the working capital ratio is not a truly accurate indication of the liquidity position of the company. It simply reflects the net result of total liquidation of assets to satisfy liabilities, an event that rarely occurs in the business world. Nonetheless, comparisons of working capital levels over time can at least serve as potential early warning indicators that the company may have problems in terms of timely collection of receivables that, if not addressed, could lead to a future liquidity crisis.

In conclusion, the company must seek out its areas of flaw and deficiency, solve and improve these problems if not the company will be suffering from bankruptcy and other liquidity crisis.