

SESSION 5: BALANCE SHEET & CASH FLOW STATEMENT

KEY CONCEPTS:

- Focus on transactions involving shares and how these effect the balance sheet and cash flow statement.

X-PLANATION

FORMAT OF THE STATEMENT OF FINANCIAL POSITION(BALANCE)

Note 7.	Ordinary share capital	
	Authorised	
	Number of authorised ordinary shares: 500 000 shares	
	Issued	R
	300 000 shares in issue at beginning of year	1 500 000
	200 000 shares issued during year at R7,00 per share	1 400 000
	80 000 shares repurchased during year (average issue price R5.80 per share)	(464 000)
	420 000 shares in issue at end of year ***	<u>2 436 000</u>

*****Note:**

After the repurchase of 80 000 shares, average issue price of 420 000 shares remains R5.80.

Note 8.	Retained income	
		R
	Retained income at beginning of the year	620 000
	Net profit after tax for the year	840 000
	Retained income on 80 000 shares repurchased	(160 000)
	Dividends	(351 000)
	Interim (300 000 shares x R0.40)	<u>(120 000)</u>
	Final (420 000 shares x R0.55)	<u>(231 000)</u>
	Retained income at end of the year	<u>949 000</u>

XYZ LIMITED

Extract from the Balance Sheet on 30 June 2013

	Note	R
SHAREHOLDERS' EQUITY		3 385 000
Ordinary share capital	7	2 436 000
Retained income	8	949 000

XYZ LIMITED

Extract from the Cash Flow Statement for the year ended 30 June 2013

	R
Cash effects of financing activities	1 276 000
Proceeds of shares issued	1 400 000
Repurchase of shares (160 000 + 464 000)	(624 000)
Proceeds of loan received	500 000

X-AMPLE QUESTIONS:

QUESTION 1:

REPURCHASE OF SHARES & INTERPRETATION (50 marks; 30 minutes)

You are provided with information relating to Prospect Limited for the year ended 31 March 2013. The CEO Ronnie Phosa, together with his children, owns 150 000 shares in the company.

Where explanations or comments are required, you are required to quote figures or financial indicators to support your explanations.

REQUIRED:

- 1.1 Shareholders' equity section of the Balance Sheet on 31 March 2013. (6)
- 1.2 Notes for:
 - Ordinary share capital (13)
 - Retained income. (15)
- 1.3 Calculate the Net Asset Value per share on 31 March 2013 after the repurchase of the shares from the Gaptu family. (4)
- 1.4 The Gaptu family were keen to sell their shares because they were unhappy with the low pay-out policy that the directors were using in deciding on dividends. In your opinion, are their complaints valid or not? Explain. (4)
- 1.5 Have the Gaptu family been offered a fair value for their shares? Explain. (3)
- 1.6 In your opinion, will the repurchase of the shares from the Gaptu family benefit the remaining shareholders or not? Explain. (5)

INFORMATION:

1. The ordinary share capital on 1 April 2012 consisted of:
 - 250 000 ordinary shares issued in the 2010 financial year at R5,00 per share
 - 150 000 ordinary shares issued in the 2011 financial year at R7,00 per share.

2. Retained income on 1 April 2012 amounted to R1 960 000.

3. The following changes occurred to share capital during the 2013 financial year:
 - On 1 October 2012, 100 000 new ordinary shares were issued at R9,00 per share. These shareholders are not entitled to interim dividends.
 - On 31 March 2013, the directors decided to repurchase 220 000 ordinary shares from members of the Gaptu family who were no longer interested in being shareholders. These shareholders had originally bought most of their shares on the JSE at different prices and at different times. The repurchase price was R10,70 per share. These shareholders are entitled to all dividends for the 2013 financial year.

4. Additional information for the past two financial years:

	Financial year ended:	
	31 March 2013	31 March 2012
Net income after tax	R1 600 000	R2 200 000
Ordinary shareholders' equity at year-end	?	R4 260 000
Number of shares in issue at year-end	?	400 000 shares
Market price per share on the JSE	1 040 cents	1 040 cents
Net asset value per share	?	1 065 cents
Earnings per share	356,6 cents	488,9 cents
Interim dividends	70 cents	90 cents
Final dividends	102 cents	140 cents

ANSWER BOOK

QUESTION 1:

**1.1 PROSPECT LIMITED
EXTRACT FROM THE BALANCE SHEET ON 31 MARCH 2013**

Note

1.2 NOTES TO THE FINANCIAL STATEMENTS

Note 7. SHARE CAPITAL

Note 8. RETAINED INCOME

Balance at beginning of year	
Balance at end of year	

MEMO

QUESTION 1

1.1 PROSPECT LIMITED

EXTRACT FROM THE BALANCE SHEET ON 31 MARCH 2013

Note See notes 7 & 8

Shareholders' equity ✓		☑ 3 616 000	
Ordinary share capital ✓	7.	☑ 1 792 000	
Retained income ✓	8.	☑ 1 824 000	6

1.2 NOTES TO THE FINANCIAL STATEMENTS

Note 7. SHARE CAPITAL

✓ 400 000 ordinary shares in issue at beginning of year (1 250 000 ✓ + 1 050 000 ✓)		✓ 2 300 000	
✓ 100 000 ordinary shares issued during year at R9,00 ✓ each		✓ 900 000	
✓ 220 000 shares repurchased (R6,40 ✓✓ average price) <i>One part correct</i>		☑ (1 408 000)	
✓ 280 000 ordinary shares in issue at end of year		☑ 1 792 000	13

Check operation

Note 8. RETAINED INCOME

Balance at beginning of year		✓ 1 960 000	
✓ Net profit after tax		✓ 1 600 000	
✓ Repurchase of 220 000 shares <i>part correct</i> (at R4,30 above average price)	<i>One</i>	☑✓✓ (946 000)	
✓ Dividends for year		(790 000)	
Interim (400 000 ✓ x 70c ✓)		✓ 280 000	
Final (500 000 ✓ x 102c ✓)		✓ 510 000	
Balance at end of year <i>Check operation</i>		☑ 1 824 000	15

1.3 Net asset value on 31 March 2013 after the repurchase of shares

correct **See 4.1** **See 4.2** **Operation, one part**

R3 616 000 ÷ 280 000 shares = 1291,4 cents or R12,91

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1.4 In your opinion, are the complaints by the Gaptu family about the dividends valid or not? Explain, quoting figures or financial indicators to support your opinion.

Excellent answer = 4 marks; Good = 3; Satisfactory = 2; Poor = 1; Incorrect = 0

No. The company has been paying out just less than 50% of earnings over the past two years (e.g. 172 cents out of earnings of 356,6 cents / 240 cents out of earnings of 488,9 cents). They are retaining income for future development. The Gaptu family are obviously looking for high dividends which would not have been responsible management.

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1.5 Have the Gaptu family been offered a fair value for their shares? Explain.

Excellent answer = 3 marks; Good = 2; Satisfactory/Poor = 1; Incorrect = 0

Yes. The price offered of R10.70 is 30 cents more than the price on the JSE and it is R4,30 above the average issue price.

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1.6 In your opinion, will the repurchase of the shares from the Gaptu family benefit the remaining shareholders or not? Explain.

Excellent answer = 5 marks; Good = 3/4; Satisfactory = 2/3; Poor = 1; Incorrect = 0

Yes: **Maximum 5 marks**

- After the repurchase of the shares the NAV has increased to R12,91 per share because there are now only 280 000 shares in the company. This is likely to have a positive effect on price on the JSE.
- If the repurchase had not taken place, the NAV would have been only R11,94.
- Assuming profit remains the same at R1,6m next year, EPS would

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be 571,4 cents (because of fewer shares) compared to 356,6 cents in 2013. This will also have a positive effect on share price and dividends per share.

OR

No: **Maximum 2 marks**

- Equity is reduced by R2 354 000 as a result of the repurchase. This will severely affect the operating activities of the company.

Workings:

If the repurchase of 220 000 had not taken place:

OSHE would = R3 200 000 + R2 770 000
= R5 970 000

NAV would = R5 970 000 ÷ 500 000
shares = R11,94

Assuming profit remains the same next year at R1 600 000:

EPS would = R1 600 000 ÷ 280 000 =
571,4 cents

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