

Tutorial Letter 102/3/2014

APPLICATION OF FINANCIAL MANAGEMENT TECHNIQUES

MAC3702

Semesters 1 and 2

Department of Management Accounting

Dear Student

This tutorial letter contains important information regarding errata in the study material.

With kind regards

	Telephone number	Room number	E-mail
Mr N Masela	012 429 4415	AJH 1 – 37	MAC3702-14-S1@unisa.ac.za (for semester 1)
Mrs S Büchner	012 429 2266	AJH 1 – 57	and MAC3702-14-S2@unisa.ac.za (for semester 2)
Mrs S Klopper	012 429 8526	AJH 1 – 40	

LECTURERS: MAC3702

Bar code

1. Study guide errata

Please make the following corrections in your tutorial letter 501:

PAGE NUMBER

17 The unusual item relates to Broad-Based Black Economic Empowerment
1.8 Scheme ~~costs~~ income

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Ratio	JJ Ltd	Average for the industry	Comment
Current ratio	0,93:1	0,27:1	The current ratio for JJ Ltd is worse better than the average for the industry. The current ratio indicates the ability of the company to pay current liabilities from current assets.

33 K = $-0,01662a + 0,0111b + 0,0529c + 0,086d + 0,0174e + 0,01071f - 0,06881$
 = $-0,01662(38,95\%) + 0,0111(20,18\%) + 0,0529(1,04) + 0,086(14,39\%) +$
 $0,0174(16,37\%) + 0,01071(2,70\%) - 0,06881$
 = ~~1,25177~~ 1,1140

69 The company expects the annual growth in ordinary dividends to be as follows:

Year 1	15%
Year 2	10%
Year 3	8%
Year 4 and onwards	6%

$$79 \quad r = F + b (M - F)$$

$$K_e = R_f + \text{Beta} (R_m - R_f)$$

$$80 \quad K_e = R_f + \text{Beta} (R_m - R_f)$$

$$= [14\% + 1,1(25\% - 14\%)] + 2\%$$

$$= [14\% + 1,1 (11)] + 2\%$$

$$= 26,1\% + 2\%$$

$$= 28,1\%$$

A fair rate of return for Jacks & Jacks (Pty) Ltd, after **increasing** the required return with 2% for lack of tradability, would be **28,1%**.

$$P_0 = D_1 / (r - g)$$

$$P_4 = D_5 / (r - g)$$

$$= 24\,667\,500 / (0,281 - 0,10)$$

$$= 24\,667\,500 / (0,181)$$

$$= 136\,284\,530$$

81	Year-end	Dividend Rand	Factor @ 28,1% ②	Present value Rand
	1	13 000 000	0,781	10 147 800
	2	16 250 000	0,609	9 902 750
	3	19 500 000	0,476	9 276 150
	4	22 425 000	0,371	8 328 645
	4 ①	136 284 530	0,371	50 616 074
			PV	88 271 419

② Calculate the factor at **28,1%** with the aid of a financial calculator or the formulas

given in chapter 3 of Skae et al. The above factor was calculated by dividing 1 continuously by **1,281** using the formula $P = (1 + i)^{-n} = 1/(1 + i)^n$.

The value of a 100% interest in Jacks & Jacks Holdings Ltd equals **R88 271 419**

Because we are calculating a minority shareholding, we should factor in a discount. You may regard 10% as a reasonable minority discount.

$$(\mathbf{R88\ 271\ 419} \times 5\% \times 90\% = \mathbf{R3\ 972\ 214})$$

Therefore, the value of a 5% interest in Jacks & Jacks Holdings Ltd equals **R3 972 214**, or approximately **R3 972 000**.

142 (v) **Number of shares issued to other shareholders in each company**

$$\text{Indaka Ltd} \left[1\ 021,285 - \left(\frac{1}{10} \times 1\ 021,285 \right) \right] \div 2 = 459,578 \text{ million}$$

$$\text{Global Ltd} \left[598,678 - \left(\frac{1}{5} \times 598,678 \right) \right] \div 2 = 239,471 \text{ million}$$

Check:

Total shares issued by Zenzele Ltd = 459,578 + 239,471 = 699,049 million.

Value of total issue = 699,049 x R2 = R1 398,098 million.

Total value of assets and goodwill taken over into Zenzele Ltd = 901,550 + 496,550 = R1 398,1 million (small rounding).

158 Increase in cash = increase in **total** sales x net profit % ① x Profit retained ②

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	Calc	Current credit sales & credit terms	New credit terms	
			Current credit sales	Additional credit sales
Contributions	1	R8 240 000	R8 240 000	R800 000
Discount	2	(R154 500)	(R708 125)	(R75 000)
Bad debt	3	(R2 300 000)	(R2 300 000)	(R45 000)
Contribution before holding cost		<u>R5 785 500</u>	<u>R5 231 875</u>	<u>R680 000</u>
Tax on contribution before holding cost	7	(R1 619 940)	(R1 464 925)	(R190 400)
After tax cost		<u>R4 165 560</u>	<u>R3 766 950</u>	<u>R489 600</u>
Holding cost (after tax cost)		(R536 164)	(R395 068)	(R123 836)
Debtor holding cost	4	(R536 164)	(R395 068)	(R43 836)
Inventory holding cost	5	-	-	(R250 000)
Creditors – saving in holding cost	6	-	-	R170 000
		<u><u>R3 629 396</u></u>	<u><u>R3 371 882</u></u>	<u><u>R365 764</u></u>
		<u><u>R3 629 396</u></u>		<u><u>= R3 737 646</u></u>

**Increase /(Decrease) in annual cash flow after tax
(new total less current total)**

R108 250

Note 7: Tax on contribution before holding cost

Contribution before holding cost	R5 785 500	R5 231 875	R680 000
x 28% tax	x 0.28	x 0.28	x 0.28
Tax on contribution before holding cost	<u><u>(R1 619 940)</u></u>	<u><u>(R1 464 925)</u></u>	<u><u>(R190 400)</u></u>

Additional notes on the impact of holding costs (opportunity cost) on credit terms

Due to the fact that more sales are made on credit with the new credit terms it takes longer for the cash to be available to make payments. As this is the case the company

can consider the effect of the holding (opportunity) cost on the cash flow.

Remember that the holding cost is calculated by making use of the company's WACC and WACC is considered as an after tax cost, therefore the impact of direct tax is not calculated on the holding cost.

Companies do not always take the holding cost into consideration as it is not always significant enough to impact the decision. You do however need to calculate it for MAC3702 purposes and if you do decide not to include it based on the fact that it is insignificant, you do need to state your reasoning and show your calculation.

171 Include the following:

- Credit sales and credit purchases are VAT inclusive.