3.11 Cash Versus Profit and the Importance of Working Capital: 30-minute Pack

AQA 8132 · Calculators not allowed · about 30 minutes

Total Marks

Name: _____ Date: ____ / ____ / _____

Answer ALL questions. Write in full sentences for questions worth 3 marks or more. Show your working for any calculation. All businesses named in prompts are fictional.

1 Which one of the following would appear as a cash inflow in a business's cash-flow forecast for June?

- ☐ A) The depreciation charged on a delivery van
- ☐ B) Stock bought in June on 30 days' credit, not yet paid for
- ☐ C) An invoice sent to a customer in June that is payable in August
- ☐ D) Payment received in June from a customer for an invoice sent in May

(Total for Question 1 is 1 mark)

---

2 Which one of the following is a current liability?

- ☐ A) A five-year bank loan
- ☐ B) A delivery van
- ☐ C) Money owed to a supplier and due in 30 days
- ☐ D) Money invested by the owner at the start of the business

(Total for Question 2 is 1 mark)

---

3 Which one of the following best describes working capital for a business such as a small online retailer in the UK?

- ☐ A) Current assets minus current liabilities
- ☐ B) Total assets minus total liabilities
- ☐ C) Net profit plus depreciation
- ☐ D) Cash in the bank only

(Total for Question 3 is 1 mark)

© Revision Library | revisionlibrary.co.uk

4 State two examples of current assets a florist like Amelia's Blooms would list when calculating working capital.

(Total for Question 4 is 2 marks)

---

5 Which one of the following scenarios describes a liquidity problem, rather than a profit problem, for a small UK business named Stellar Shoes?

- ☐ A) Stellar Shoes made an accounting profit last year but cannot pay this month's supplier invoices because customers pay on 60-day credit terms
- ☐ B) Stellar Shoes consistently sells below cost leading to accounting losses
- ☐ C) Stellar Shoes has high depreciation charges reducing reported profit
- ☐ D) Stellar Shoes pays its owners large dividends, reducing retained profit

(Total for Question 5 is 1 mark)

---

6 A business starts a month with a bank balance of £3,200. Its net cash flow for the month is -£4,700. What is its closing balance?

- ☐ A) £7,900
- ☐ B) -£1,500
- ☐ C) £1,500
- ☐ D) £3,200

(Total for Question 6 is 1 mark)

---

7 A small business expects to be short of cash for about two weeks while it waits for customers to pay. Which one of the following is the most suitable short-term source of cash?

- ☐ A) Issuing new shares to investors
- ☐ B) Taking out a ten-year bank loan
- ☐ C) A bank overdraft
- ☐ D) Selling the freehold of its premises

(Total for Question 7 is 1 mark)

© Revision Library | revisionlibrary.co.uk

8 Which one of the following would improve a business's cash position in the short term?

- ☐ A) Giving customers 90 days to pay instead of 30 days
- ☐ B) Buying extra stock that will not be sold for six months
- ☐ C) Paying all suppliers a month earlier than needed
- ☐ D) Agreeing 60 days to pay suppliers instead of 30 days

(Total for Question 8 is 1 mark)

---

9 A business sells goods worth £5,000 on 20 June and agrees that the customer can pay in 30 days. Which one of the following is true at 30 June?

- ☐ A) Revenue and cash have both increased by £5,000
- ☐ B) Revenue has increased by £5,000 but the cash has not yet been received
- ☐ C) Cash has increased by £5,000 but revenue has not
- ☐ D) Neither revenue nor cash has increased

(Total for Question 9 is 1 mark)

---

10 Calculate the working capital for Noor's Noodle Bar in Bristol. Current assets £6,400; current liabilities £9,100. Show your working and state whether it is positive or negative.

(Total for Question 10 is 2 marks)

---

11 State two reasons why a business might deliberately accept a short-term negative working capital position, naming an example UK business.

.....

.....

(Total for Question 11 is 2 marks)

---

12 Maya owns a small print shop. In March she recorded sales of £4,200, of which £3,500 were credit sales to a local business to be paid in April. Her cash in the bank at 1 March was £1,000. She paid £2,400 to suppliers in March and £600 in wages during March. Calculate Maya's cash in bank at 31 March. Show your working.

(Total for Question 12 is 2 marks)

© Revision Library | revisionlibrary.co.uk

13 Explain one problem that a persistent shortage of cash could cause for a business.

(Total for Question 13 is 3 marks)

---

14 Analyse whether Tamsin's Tailors, a small tailoring firm in York, is facing a profit problem or a liquidity problem. Tamsin's accounts show a profit of £12,000 for the year. However, Tamsin currently has only £500 in the bank. Most of her sales are to local wedding customers who pay 90 days after the order is delivered. She also holds a large amount of bespoke fabric in stock bought in advance for seasonal orders.
Write a short analysis and conclude whether this is mainly a profit problem or a liquidity problem, giving reasons based on the facts given.

(Total for Question 14 is 6 marks)

© Revision Library | revisionlibrary.co.uk

Mark scheme · 3.11 Cash Versus Profit and the Importance of Working Capital: 30-minute Pack

Question 1

D cao **B1**

Answer: D

Question 2

C cao **B1**

Answer: C

Question 3

A cao **B1**

Answer: A

Question 4

cash or bank balance **B1**

inventory, such as cut flowers or gift stock, or trade receivables from credit customers **B1**

Answer: Any two current assets, e.g. cash/bank balance; inventory such as flowers or gift stock; trade receivables from credit customers.

Question 5

A cao **B1**

Answer: A

Question 6

B cao **B1**

Answer: B

Question 7

C cao **B1**

Answer: C

Question 8

D cao **B1**

Answer: D

Question 9

B cao **B1**

Answer: B

Question 10

6,400 - 9,100 seen **M1**

-£2,700 cao and states negative **A1**

Answer: -£2,700, negative working capital.

Question 11

to grow quickly by buying more stock or investing in marketing, e.g. a fashion start-up taking risks **B1**

because suppliers offer long trade credit allowing the business to use cash for other strategic investment, e.g. an electronics retailer using supplier credit **B1**

Answer: Any two, e.g. a fashion start-up may accept negative working capital to grow quickly; an electronics retailer may use supplier credit to free cash for investment.

Question 12

start cash 1,000 + cash sales 700 - payments (2,400 + 600) seen, where cash sales = 4,200 - 3,500 = 700 **M1**

-£1,300 cao **A1**

Answer: -£1,300 (overdrawn).

Question 13

identifies a problem, e.g. the business cannot pay its suppliers on time **B1**

develops the point, e.g. suppliers may refuse to deliver more goods or demand cash on delivery, so the business cannot restock **B1**

links to an outcome, e.g. without stock the business loses sales and may become insolvent (accept unable to pay wages, so staff leave) **B1**

Answer: It may be unable to pay suppliers, who then stop supplying it, so it loses sales and may fail.

Question 14

Level 1 Provides a basic analysis that identifies timing or stock as an issue, or simply repeats the facts, with little linkage to profit versus liquidity and no clear conclusion. **1-3**

Level 2 Provides a clear analysis that links the 90-day credit terms and high stock levels to cash being tied up, contrasts this with the reported profit, and concludes that the firm has a liquidity problem, supported by evidence from the prompt. **4-6**

Indicative content:

- The firm reports a profit of £12,000, so on accounting measures it is profitable rather than loss-making.
- Having only £500 in the bank while owing day-to-day costs suggests an inability to meet immediate payments, which is a liquidity issue.
- Long customer credit terms of 90 days delay cash receipts, creating a timing gap between sales (which give profit) and cash collection.
- Holding large amounts of bespoke fabric ties up cash in inventory until orders are completed and paid for, worsening cash availability.
- Judgement: the evidence points to a liquidity problem rather than a profit problem, because the business is profitable on paper but lacks cash due to slow customer payments and high stock levels.

© Revision Library | revisionlibrary.co.uk