



Exam FFM
Foundations in Financial Management

Pocket Notes



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Preface

These Pocket Notes contain everything you need to know for the exam, presented in a unique visual way that makes revision easy and effective.

Written by experienced lecturers and authors, these Pocket Notes break down content into manageable chunks to maximise your concentration.

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Introduction

In this chapter

- Overview of the assessment.
- Keys to success.

Overview of the assessment

| | No. of marks |
|--|--------------|
| Section A: 10 MCQs | 20 |
| Section B: 6 WTQs (10, 15 or 20 marks each) | 80 |
| | <hr/> |
| | 100 |
| | <hr/> |

The exam is a two hour paper.

Keys to success

- Ensure you are familiar with the entire syllabus, as this will be examined.
- Practise lots of past examination questions.
- Set out your answers clearly – and don't jump between questions in the examination itself as this may confuse the examiner.

chapter

1

Cash and cash flows

In this chapter

- Cash and cash flows.
- Sources and applications of finance.
- Cash flow and profit.
- Cash and accruals accounting.

Cash and cash flows

Definition

Cash: Paper money and money in bank accounts.

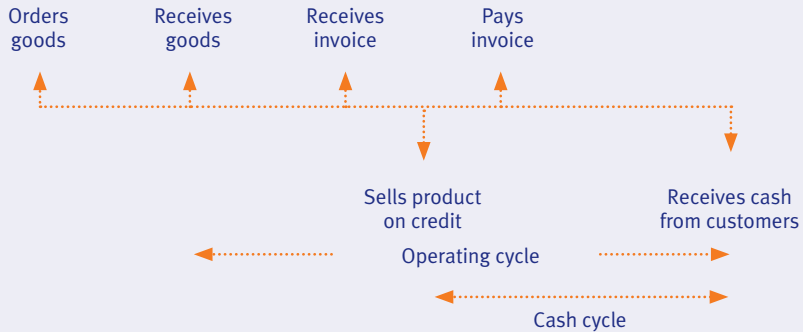
Cash flow: Receipts and payments of cash.

Net cash flow: Difference between cash received and cash paid.

Cash inflows vary depending on business type e.g.:

| | |
|-------------|------------------------------------|
| Supermarket | Regular cash inflow |
| Hats | Seasonal – spring and summer |
| Ice cream | Seasonal – summer |
| College | Irregular – whenever courses start |

Cash cycle and operating cycle



Sources and applications of finance

| Sources of cash | Uses of cash |
|--|---|
| Obtaining finance: <ul style="list-style-type: none"> • Increase in long-term debt • Increase in equity • Increase in current liabilities Selling assets <ul style="list-style-type: none"> • Decrease in current assets • Decrease in non-current assets | Paying payables or stockholders: <ul style="list-style-type: none"> • Decrease in long-term debt • Decrease in equity • Decrease in current liabilities Buying assets <ul style="list-style-type: none"> • Increase in current assets • Increase in non-current assets |

| Receipts | Payments |
|--|---|
| Revenue | |
| <ul style="list-style-type: none"> • Cash sales • Payments by receivables | <ul style="list-style-type: none"> • Trade payables (goods and services purchased) • Employees (salaries) • Sundry expenses (petty cash) |
| Capital | |
| <ul style="list-style-type: none"> • Money from shareholders/capital from owners • Non-current asset sales | <ul style="list-style-type: none"> • Non-current asset purchases |
| Drawings / dividends | |
| | <ul style="list-style-type: none"> • Drawings (sole trader / partnership) • Dividends (limited company) |
| Exceptional (unplanned) | |
| <ul style="list-style-type: none"> • Items not mentioned above | <ul style="list-style-type: none"> • Items not mentioned above |

Cash flow and profit



Key Point

- Profit = excess of income over expenditure in statement of profit or loss.
- For business to survive, cash inflows must exceed cash outflows.
- Cash flow and profits are different.
- Business can make a profit, but still have negative cash flows.

Reasons for differences in cash flows and profits

| Business activity | Effect on cash and profit |
|---|-------------------------------------|
| Purchase of non-current asset | Cash outflow, no effect on profit |
| Depreciation charge on statement of profit or loss | No effect on cash, profit decreased |
| Increase in working capital (e.g. inventory purchase) | Cash outflow, no effect on profit |
| Normal trading | See below |

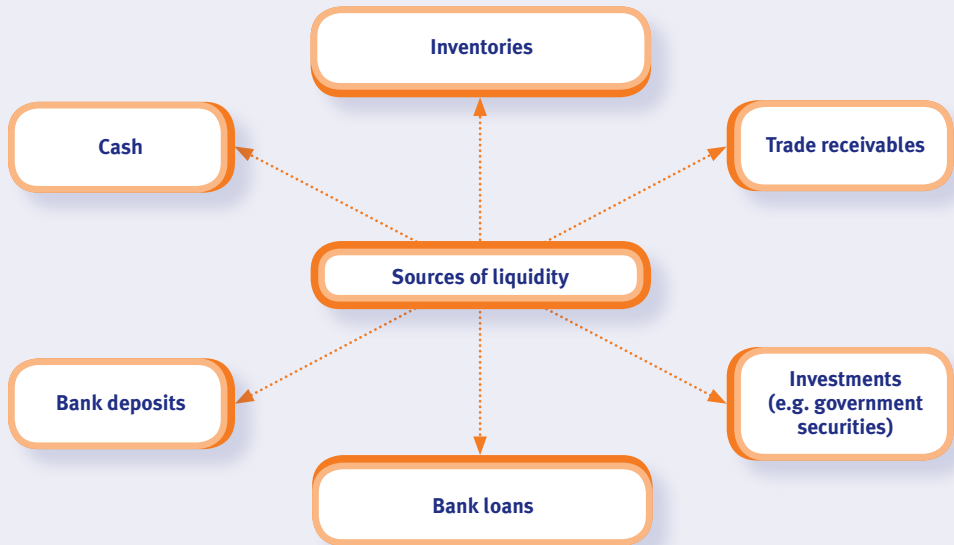
| Statement of profit or loss | | Cash effect | | |
|-----------------------------|----------------------|-------------|----------|-------|
| | January | January | February | March |
| | \$ | \$ | \$ | \$ |
| Sale | 1,000 | | 1,000 | |
| Purchase | (600) | | | (600) |
| Gross profit | 400 | | | |
| Wages | (200) | (200) | | |
| Light and heat | (100) | | (100) | |
| Net profit | 100 | | | |
| | Cumulative cash flow | (200) | 700 | 100 |

From January sales only:

- Sales made in January give profit in January.
- Cash flow in January is negative because employees must be paid; no cash received.
- Cash flow in February is positive because receivables have now been paid.
- Only in March does cash flow = profit when payables finally paid.

Definition

Liquidity: Cash or items that can be converted into cash quickly.



Cash and accruals accounting

Definition

Cash management: Systems and procedures for controlling cash flows and the use of cash in a business.

Cash accounting: Recording income when received and expenditure when it is incurred.

Accruals accounting: Recording income and expenditure when earned.

Different accounting methods give different results.

In previous cash flow example. In January:

- Cash accounting = cash outflow of \$200
- Accruals accounting = profit of \$100.



Exam focus

Ensure you understand the difference between profit and cash flows and the difference between accruals and cash accounting.