

CIMA Gateway Exam

Cima G1

Version Demo

Total Demo Questions: 1

Total Premium Questions: 9

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Topic Break Down

Topic	No. of Questions
Topic 1, Fundamentals of Business Economics	2
Topic 2, Fundamentals of Management Accounting	3
Topic 3, Fundamentals of Ethics, Corporate Governance and Business Law	2
Topic 4, Mix Questions	2
Total	9

QUESTION NO: 1 - (HOTSPOT)

Net present value calculation

	A	B	C	D	E	F	G
	Year	1	2	3	4	5 onwards	Total
		\$ million	\$ million	\$ million	\$ million	\$ million	\$ million
1	Franchise fees	2.6	4.8	8.1	9.3	11.4	
2	Royalties	0.7	2.7	7.9	13.8	18.7	
3	Contribution from sales of ingredients and disposables	0.6	2.4	7.1	12.4	16.8	
4	Sales of furniture and fittings	2.1	5.2	9.3	10.4	11.7	
5	Cost of furniture and fittings	(1.7)	(4.3)	(8.6)	(9.1)	(10.4)	
6	Legal fees	(2.5)	(1.5)	(3.1)	(4.2)	(6.1)	
7	Banking charges	(0.1)	(0.2)	(0.5)	(0.7)	(0.9)	
8	Advertising	(2.6)	(4.8)	(8.1)	(9.3)	(11.4)	
9	Net cash flow	(0.9)	4.3	12.1	22.6	29.8	
10	Discount factor at 10%	0.909	0.826	0.751	0.683		
11	Discount factor at 10% for perpetuity					6.831	
12	Discounted cash flow	(0.8)	3.6	9.1	15.4	203.6	230.9
13							
14							
15							
16							

Two weeks have passed since you responded to the Finance Director concerning the C-land restaurant. You have received the following email.

From: Matt Spot, Finance Director

To: Financial Manager

Subject: significant expansion in C-land

Hello

The Board has had a number of discussions since your helpful reply to my last email. We have decided to embark on an ambitious expansion plan, involving at least 50 new restaurants, in C-land. To minimise our exposure to the risks of operating in this relatively unfamiliar environment, we plan to use franchising to expand. We have projected some figures and these are shown in the attached spreadsheet.

We have projected five years into the future. We are working on the assumption that things will have settled down by year five and that year five 's results will be repeated into the indefinite future. I have attached a spreadsheet that shows that this expansion has the potential to generate a significant positive net present value for us.

I need your advice on the following matters.

Firstly, I need your thoughts on the validity of the assumptions underlying our projections. I am happy that the arithmetic is correct and that an appropriate discount rate has been applied, so please ignore those issues.

Secondly, I would appreciate your advice on the specific project management issues arising from the implementation of this project. What should we do to ensure that this aspect of the expansion is a success?

Matt

ANSWER:

	A	B	C	D	E	F	G
1	Year	1	2	3	4	5 onwards	Total
2		\$ million	\$ million	\$ million	\$ million	\$ million	\$ million
3	Franchise fees	2.6	4.8	8.1	9.3	11.4	
4	Royalties	0.7	2.7	7.9	13.8	18.7	
5	Contribution from sales of ingredients and disposables	0.6	2.4	7.1	12.4	16.8	
6	Sales of furniture and fittings	2.1	5.2	9.3	10.4	11.7	
7	Cost of furniture and fittings	(1.7)	(4.3)	(8.6)	(9.1)	(10.4)	
8	Legal fees	(2.5)	(1.5)	(3.1)	(4.2)	(6.1)	
9	Banking charges	(0.1)	(0.2)	(0.5)	(0.7)	(0.9)	
10	Advertising	(2.6)	(4.8)	(8.1)	(9.3)	(11.4)	
11	Net cash flow	(0.9)	4.3	12.1	22.6	29.8	
12	Discount factor at 10%	0.909	0.826	0.751	0.683		
13	Discount factor at 10% for perpetuity					6.831	
14	Discounted cash flow	(0.8)	3.6	9.1	15.4	203.6	230.9
15							
16							

Explanation:

The correct selection is the total of I\$230.9 million in the “Discounted cash flow” row and “Total” column. Net present value is the total present value of all relevant project cash flows after each future amount has been converted into its value at the appraisal date. In this worksheet, the annual net cash flows are first calculated for years 1 to 5. The relevant 10% discount factors are then used to convert the annual amounts into present values. The project is also assumed to continue indefinitely after year 5, so the year-5 continuing cash flow is capitalised as a perpetuity and then discounted back to the present. This produces the I\$203.6 million shown for the continuing period.

The I\$230.9 million figure is the final aggregate of the discounted cash flows: the discounted early-year values together with the present value of the post-year-5 perpetuity. Since it is already expressed in present-value terms and is the total of the full investment appraisal cash-flow stream, it is the net present value presented by the model. A positive NPV indicates that, on the stated cash-flow and discount-rate assumptions, the expansion is expected to add value above the required return. This follows the standard capital-investment appraisal principle that NPV is calculated by discounting expected incremental cash flows and summing them, as described in the [ACCA investment appraisal guidance](#).

QUESTION NO: 2 - (SIMULATION)

Comparative results for Pizzatime and Pizza2Go

	Pizzatime	Pizza2Go
Earnings growth in 2015	5%	31%
ROCE	38% (= 135m / 357m)	58% (= 80m / 139m)
Gross profit margin	74% (= 443m / 597m)	38% (= 165m / 440m)
Share capital	45 million I\$1 shares	200 million I\$0.10 shares
Share price	I\$ 60	I\$ 8
Market capitalisation	I\$ 2,700 million	I\$ 1,600 million
Earnings yield	3.3% (= 90m / 2,700m)	3.4% (= 55m / 1,600m)
Gearing (D/D+E) book values	45% (= 160m / (160m + 197m))	27% (= 37m / (37m + 102m))

You have received the following email:

From: Monica Lall, Chief Executive

To: Financial Manager

Subject: benchmarking and growth ideas

Hi,

As you will already be aware, in 2015 our annual growth in both earnings and revenue was well below the target of 10%. This has clearly been a disappointment to our shareholders and we need to take rapid action to rebuild market confidence and avoid a fall in our share price. I would value your input on this one.

You will also see, from the financial data in the attachment, that our competitor, Pizza2Go, has reported higher growth and also a higher ROCE and I need to be able to explain these figures to our analysts. It would be really helpful to understand what they mean in terms of shareholder returns. The earnings growth figures are particularly disappointing, especially as Pizza2Go has shown such strong growth.

I need a response to this email as soon as possible that:

- Analyses the financial data in the attachment and explains what the ROCE and earnings growth figures mean in terms of the relative success of the two companies and returns to shareholders. I notice that we have a much higher gross profit margin and approximately the same earnings yield. Is it possible that the ROCE and earnings growth figures are misleading and that we are actually performing better than Pizza2Go?
- Suggests ways in which we could improve profitability. Use Porter 's value chain model as your base.

Regards

Monica Lall

ANSWER: Old Answer:

Answer:

New Answer:

No valid hotspot selection exists in the supplied question. The exhibit contains only a financial table and email text, with no hotspot instruction or selectable target. Provide the missing hotspot prompt and its interactive image/targets before an exact marker location can be specified. Reasoning:

The supplied material contains a comparative financial-results table and an email requesting an analysis, but it does not contain a hotspot prompt, an instruction to select a particular item, or any defined clickable regions. The table is an attachment only; its rows are not presented as answer targets. Therefore, no exact UI area can be selected as a valid hotspot answer from the information provided. The financial analysis requested in the email would conclude that Pizza2Go has the stronger reported return performance: it has ROCE of 58% and earnings growth of 31%, compared with Pizzatime's 38% and 5%. Pizzatime's 74% gross profit margin is a product-level margin measure and does not overturn the lower overall return on capital. The two earnings yields, 3.3% and 3.4%, are broadly similar, indicating that the market is not currently attributing a markedly different earnings return relative to share price. However, this does not create a selectable hotspot. The correct remediation is to provide the missing hotspot question and/or image with its selectable targets.

Explanation:

The information shown supports a clear financial interpretation, even though it does not supply a selectable hotspot. Pizza2Go is reporting the stronger operating return because its return on capital employed is 58%, compared with Pizzatime's 38%. Return on capital employed relates operating profit to the capital committed to the business, so the comparison indicates that Pizza2Go is generating more operating profit for each unit of long-term capital it uses. Its earnings growth of 31%, against Pizzatime's 5%, also shows substantially stronger growth in profit attributable to shareholders.

Pizzatime's gross profit margin of 74% is strong, but gross margin measures the surplus after direct production or purchase costs only. It does not measure the effect of operating overheads, asset intensity, financing structure, or the efficiency with which capital is employed. Accordingly, it cannot by itself demonstrate superior overall shareholder performance. The very similar earnings yields—3.3% and 3.4%—show that current earnings relative to market value are broadly comparable, rather than establishing that Pizzatime has outperformed.

To improve profitability, Pizzatime should review the full value chain: improve purchasing terms and ingredient availability; reduce preparation waste and delivery inefficiencies; use demand data to optimise store capacity; strengthen customer ordering and retention processes; and support staff with effective systems and training. Porter's value-chain framework is designed to identify where activities can add customer value or reduce cost; see [Cambridge Institute for Manufacturing's value-chain analysis guidance](#). A valid hotspot answer cannot be produced until the missing selection instruction and selectable target are provided.