

# Skills Exercises

## AO2 Analysis

Cambridge IGCSE™ / IGCSE (9–1)  
Accounting 0452 / 0985

Cambridge O Level  
Accounting 7707

For examination from 2023



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## Introduction

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Cambridge IGCSE / O Level Accounting attracts a variety of learners from many different backgrounds. For some learners Accounting is a new subject and an opportunity to explore an area of study that interests them, while developing a set of transferable skills. Other learners have previously studied Accounting and are looking to continue developing their knowledge of the subject. Either way, the study of Accounting allows learners to experience the diverse and dynamic world within which organisations exist and gain the knowledge needed to understand how organisations operate within real contexts, analyse alternative courses of action and develop the ability to make justified recommendations.

### Skills and why they are important?

Skills are the key to success. The performance of candidates in Cambridge IGCSE/ O Level Accounting examinations have shown a range of areas where improvement would be helpful. These areas of improvement tend to centre around the assessment objectives (AOs) of the course and we have addressed these AOs in three Skills Exercise booklets.

- Skills Exercises – AO1 Knowledge and understanding
- Skills Exercises – AO2 Analysis
- Skills Exercises – AO3 Evaluation

Skills Exercises make use of examination questions and data and include activities and worksheets to help skills development and incorporate suggested teaching approaches, such as group work, discussion, structured support and writing in sequence. They do not attempt to cover all possible aspects of the examinations, only those problem areas which have presented consistently over time.

### How will these skills be developed?

The Skills Exercise booklets aim to help learners develop skills in:

- applying knowledge and understanding of facts, terms, concepts, policies, procedures and techniques relating to financial and management accounting in a variety of accounting situations and present outcomes in the most appropriate manner
- developing skills of analysis by selecting, calculating and interpreting financial and management accounting information to communicate outcomes in the most appropriate manner
- building evaluation skills, including making judgements and drawing conclusions based on financial and non-financial data to make recommendations and decisions.

Skills Exercises provide suggestions so you can have confidence that the materials you prepare and use in the classroom are building skills and resilience in your learners. This document should be used alongside the other teaching and learning resources provided on the [School Support Hub](#)

## AO2 Analysis

Analysis is usually considered to be a high-level assessment objective. At its heart, analysis is about answering the question. Learners are required to:

- analyse financial accounting information
- select, calculate and interpret relevant data and information
- communicate outcomes in the most appropriate form.

The following table contains some command words that might indicate to learners that they need to demonstrate and apply knowledge and understanding.

| Command word    | What it means   |
|-----------------|---|
| <b>Identify</b> | name / select / recognise elements and the relationship between them                    |
| <b>Analyse</b>  | examine in detail to show meaning, identify elements and the relationship between them  |
| <b>Compare</b>  | identify/comment on similarities and/or differences from different sets of calculations |
| <b>Discuss</b>  | write about issue(s) or topic(s) in depth in a structured way                           |
| <b>Prepare</b>  | present information in a suitable format  |
| <b>Contrast</b> | identify/comment on differences in results  |

### Exercise 1: Answering the question

When a learner reads an examination question for analysis, they should know what is required.

Knowing what is required helps learners structure their answer as it helps them to select, calculate, interpret the data and information and present the outcomes in the most appropriate form.

#### Activity 1: How to answer the question

Provide learners with a series of analytical questions from either past examination or specimen papers. The questions on **Worksheet 1: How to answer the question** can be used along with any other analytical questions.

For each question, learners decide what is required. This provides a starting point to answer the question. Go through the worksheet with learners to check they understand what is required of the task. For this activity learners may work individually, in pairs or groups.

Use **Worksheet 1: How to answer the question answers** and ask learners to peer assess each other's work. Lead a class discussion to develop learners' analysis. Ensure any misconceptions are addressed.

## Worksheet 1: How to answer the question

For each of the following questions, decide what you are required to analyse.

1. Calculate to the nearest whole day the trade receivables turnover.

**What are you analysing?**

2. Calculate to the nearest whole day the trade payables turnover.

**What are you analysing?**

3. Calculate the current ratio.

**What are you analysing?**

4. Calculate, to two decimal places the gross margin.

**What are you analysing?**

5. Calculate the inventory turnover.

**What are you analysing?**

6. Prepare the bank reconciliation statement.

**What are you analysing?**

7. Discuss two advantages and two disadvantages of the straight-line method of depreciation.

**What are you analysing?**

**Worksheet 1: How to answer the question answers**

1. Calculate to the nearest whole day the trade receivables turnover.

**What are you analysing?**

*Selecting the correct figures to enable the calculation of trade receivables turnover enables decisions to be made regarding the credit control policy of the business.*

2. Calculate to the nearest whole day the trade payables turnover.

**What are you analysing?**

*This allows analysis of the relationships the business has with its credit suppliers and the opportunity cost.*

3. Calculate the current ratio.

**What are you analysing?**

*This looks at the current assets the business has in relation to the liabilities it needs to meet in the short term. Alternate strategies may need to be introduced if there will be insufficient funds to meet debts when they fall due.*

4. Calculate, to two decimal places the gross margin.

**What are you analysing?**

*The relationship between the sales price and cost price enabling decisions to be made regarding increasing or reducing selling price to increase gross profit or looking for alternate suppliers to increase gross profit.*

5. Calculate the inventory turnover.

**What are you analysing?**

*The number of times a business replaces its inventory in a specific period. Trends may be analysed, and decisions taken regarding stockholding.*

6. Prepare the bank reconciliation statement.

**What are you analysing?**

*The reasons for the difference between the balances in the cash book and on the bank statement.*

7. Discuss two advantages and two disadvantages of the straight-line method of depreciation.

**What are you analysing?**

*Using the example of motor vehicles state the positive and the negative aspects of using the straight-line method of depreciation.*

## Exercise 2: Spotting analysis

Analysis is the skill that unlocks higher marks and top grades. Learners who can effectively analyse in their answers will be able to build arguments and come to conclusions.

Analysis is about:

- effects
- consequences
- or reactions.

Many learners think that analysis is about description or explanation and often spend too much time explaining and describing elements of an answer without getting to the all-important analysis. Analysis is about effects, consequences or reactions.

### Activity 1: Analysis or not

Provide learners with a series of sentences where one sentence involves analysis and the other does not. The sentences in **Worksheet 2: Analysis or not** can be used or replaced with other sentences. Go through the worksheet with learners to check they understand what is required of the task. For this activity learners may work individually or in pairs. For each sentence, learners decide which is the analytical one.

Use **Worksheet 2: Analysis or not answers** and ask learners to peer assess each other's work. Lead a group discussion, ensuring any misconceptions are addressed.



## Worksheet 2: Analysis or not

For each of the following pairs of sentences, decide which one is analytical. Remember that analysis is about effects, consequences or reactions.

1.

| Sentence 1   | Sentence 2  |
|--|---|
| The gross profit increased due to higher selling prices. | Revenue is calculated by multiplying the number of units sold by the selling price. |

2.

| Sentence 1                      | Sentence 2  |
|---------------------------------|---|
| Profit is lower than last year. | The expenses were not controlled so profit reduced. |

3.

| Sentence 1                           | Sentence 2                              |
|--------------------------------------|---|
| Working capital increased this year. | Inventory was sold at a higher mark up. |

4.

| Sentence 1   | Sentence 2                              |
|--|---|
| The average inventory value reduced and cost of sales remained the same. | Inventory turnover increased this year. |

5.

| Sentence 1  | Sentence 2  |
|---|---|
| Trade payables were \$12 000 for the years ended 2021 and 2022 but cost of sales reduced. | The trade payables turnover increased in the year ended 2022. |

6.

| Sentence 1  | Sentence 2  |
|---|---|
| Trade receivables turnover reduced this year end. | The business was more successful at collecting debts. |

7.

| Sentence 1  | Sentence 2                          |
|---|-------------------------------------|
| Unpaid rent was included in the income statement. | The matching principle was applied. |

8.

| Sentence 1   | Sentence 2   |
|--|--|
| A lower quality of raw material was used to make the finished product. | The lower quality of raw materials led to lower quality of finished goods. |

**Worksheet 2: Analysis or not answers**

|    |  |
|----|--|
| 1. | <i>Sentence 1 – increasing selling prices is just one strategy to increase gross profit.</i>   |
| 2. | <i>Sentence 2 – This gives a more detailed reason why profit is lower than last year.</i>  |
| 3. | <i>Sentence 2 – The effect of increasing mark up resulted in higher working capital.</i>   |
| 4. | <i>Sentence 1 – This shows understanding of the components used to calculate inventory turnover.</i>                                   |
| 5. | <i>Sentence 2 – This shows detailed knowledge and application of the formulae for trade payables turnover.</i>                         |
| 6. | <i>Sentence 2 – A possible strategy to improving trade receivables turnover.</i>   |
| 7. | <i>Sentence 1 – This is the detail of applying the matching principle.</i>   |
| 8. | <i>Sentence 2 – The lower quality of raw materials was a cause for lower quality of finished good. Sentence 1 is just descriptive.</i> |

## Activity 2: Identifying analysis in simple sentences

Show learners one or two sentences containing analysis, that are explanations of causal connections. These can be everyday examples or accounting related. Choose examples suitable for the topic being studied. For example:

- The shop was shut therefore I wasn't able to buy what I needed.
- Workers are happy to work overtime because they can earn more money.

Learners identify the decisions made and the reasons given for those decisions in each statement. Introduce the idea of connecting words including, 'because', 'this means', 'so', 'therefore'.

In groups, learners consider other possible connecting words. Remind them that not all connecting words, such as 'and', are relevant for developing analysis.

Learners make notes on their discussion before sharing ideas with the class. These could be used later as part of a display about connecting words.

Use **Worksheet 3: Identifying analysis in simple sentences** to encourage learners to practice spotting analysis and adding development. Go through the worksheet with learners to check they understand what is required of the task. For this activity learners may work individually or in pairs.

Use **Worksheet 3: Identifying analysis in simple sentences answers** and ask learners to peer assess each other's work. Lead a group discussion to go through the answers ensuring any misconceptions are addressed.

**Extension activity:** ask learners questions such as, 'Why does this develop the statement?' or 'How will this help explain the point being made?'

### Worksheet 3: Identifying analysis in simple sentences

Complete the following sentences by choosing a suitable connecting word to develop each point in this exercise. Note connecting words can be used more than once.

**Because                      therefore                      as a result                      so                      lead to**

1. The introduction of a cash discount may \_\_\_\_\_ more customers paying early.
2. The directors should agree with the shareholders \_\_\_\_\_ although the loan interest has to be paid there is no requirement to pay a dividend.
3. Loan interest must be paid despite lower profits. \_\_\_\_\_ shareholders may receive a lower or no dividend.
4. Cost of sales reduces \_\_\_\_\_ of suppliers increased trade discount.
5. Profit for the year improved \_\_\_\_\_ of controlling expenses.
6. Employees are interested in the financial statements of the business \_\_\_\_\_ they may have an impact on their wages.
7. The advantage of setting up the business as a sole trader is that you are your own boss. \_\_\_\_\_ you don't have to waste time consulting anyone else so can make decisions straightaway.
8. Inventory should be valued at the lower of cost or net realisable value. \_\_\_\_\_ the principle of prudence must be applied.

**Worksheet 3: Identifying analysis in simple sentences answers**

1. The introduction of a cash discount may lead to more customers paying early.
2. The directors should agree with the shareholders because although the loan interest has to be paid there is no requirement to pay a dividend.
3. Loan interest must be paid despite lower profits. Therefore shareholders may receive a lower or no dividend.
4. Cost of sales reduces as a result of suppliers increased trade discount.
5. Profit for the year improved as a result of controlling expenses.
6. Employees are interested in the financial statements of the business because they may have an impact on their wages.
7. The advantage of setting up the business as a sole trader is that you are your own boss. Therefor/as a result you don't have to waste time consulting anyone else so can make decisions straightaway.
8. Inventory should be valued at the lower of cost or net realisable value because the principle of prudence must be applied.

### Activity 3: Identifying analysis in paragraphs

Give learners a copy of **Worksheet 4: Identifying analysis in paragraphs**. Go through the worksheet with learners to check they understand what is required of the task. For this activity learners may work individually or in pairs. Using a highlighter pen or a pencil, learners identify the analytical components of each paragraph.

Use **Worksheet 4: Identifying analysis in paragraphs answers** and ask learners to peer assess each other's work. Lead a class discussion around whether the analysis could be extended further to make a better analytical point. Ensure any misconceptions are addressed.

## Worksheet 4: Identifying analysis in paragraphs

For each of the following paragraphs, identify the analysis by either highlighting or underlining the focus of the analysis.

1. The loan from the bank will cost Arlo more interest than borrowing from his friend Frank. With the loan from the bank Arlo has more pressure to earn profits as the interest will be paid irrespective of profits. The loan from the bank needs security and Arlo could lose his business if he fails to repay the loan as the bank will take his assets.
2. Albert is considering accepting the offer of higher trade discount from his main supplier if he places larger orders each month. He is concerned that he will incur additional cost of warehouse space and that he will hold too much inventory for too long that may be difficult to sell.
3. Marex Limited have now eliminated a rival partnership business and have gained their list of customers to widen their customer base. They hope that by doing so this may lead to greater sales revenue and therefore profit. Marex Limited anticipate that through increased sales greater purchases will be needed to support this strategy and they will be able to benefit from both an increased trade discount and cash discount for early payment of debts which should also increase profit.
4. Jane is considering allowing her customers a longer period of credit. She believes it may encourage new customers leading to increased sales and, hopefully, profits. She also hopes that by increasing her credit period this will lead to better relationships with customers possibly also increasing sales.
5. The directors of Caldu, Limited who are the principal shareholders wish to enlarge the company by purchasing a small factory. The options to finance the purchase is by the issue of a debenture or the issue of further ordinary shares. They are concerned that the fixed interest payment on the debenture may lead to reduced or no dividend for the shareholders.

**Worksheet 4: Identifying analysis in paragraphs answers**

1. The loan from the bank will cost Arlo more interest than borrowing from his friend Frank. With the loan from the bank Arlo has more pressure to earn profits as the interest will be paid irrespective of profits. The loan from the bank needs security and Arlo could lose his business if he fails to repay the loan as the bank will take his assets.
2. Albert is considering accepting the offer of higher trade discount from his main supplier if he places larger orders each month. He is concerned that he will incur additional cost of warehouse space and that he will hold too much inventory for too long that may be difficult to sell.
3. Marex Limited have now eliminated a rival partnership business and have gained their list of customers to widen their customer base. They hope that by doing so this may lead to greater sales revenue and therefore profit. Marex Limited anticipate that through increased sales greater purchases will be needed to support this strategy and they will be able to benefit from both increased trade discount and cash discount for early payment of debts which should also increase profit.
4. Jane is considering allowing her customers a longer period of credit. She believes it may encourage new customers leading to increased sales and, hopefully, profits. She also hopes that by increasing her credit period this will lead to better relationships with customers possibly also increasing sales.
5. The directors of Caldu, Limited who are the principal shareholders wish to enlarge the company by purchasing a small factory. The options to finance the purchase is by the issue of a debenture or the issue of further ordinary shares. They are concerned that the fixed interest payment on the debenture may lead to reduced or no dividend for the shareholders.



### Exercise 3: Focus on developing analysis

Analysis must be focussed on a business or a stakeholder group. It is essential that learners focus their analysis in the right way. An examination question will always have a clear focus for the analysis.

Analysis can be limited or developed.

Limited analysis does not go far enough. For example, it may identify an impact, effect or reaction, but it does not continue and demonstrate how it will really affect the business or stakeholder.

Developed analysis is about creating a chain of analysis. This means that there is a clear link between the initial impact, effect or reaction and how this might develop to really affect the business or stakeholder.

#### Activity 1: Who is the focus?

Provide learners with a series of possible or past examination questions. The questions on **Worksheet 5: Who is the focus?** can be used or changed with other analytical or evaluative questions. Go through the worksheet with learners to check they understand what is required of the task. For this activity learners may work individually or in pairs. For each sentence, learners highlight or underline the focus of the analysis.

Use **Worksheet 5: Who is the focus answers** and ask learners to peer assess each other's work. Lead a discussion on how the focus of each question could be misinterpreted. Ensure any misconceptions are addressed.

## Worksheet 5: Who is the focus?

For each of the following questions, identify and underline the focus of the analysis.

1. Analyse two advantages to the owners of a business of operating as a partnership to forming a limited company.
2. Analyse two advantages to the business of maintaining a debtors control account.
3. Analyse two factors to the business of maintaining a provision for depreciation account for non-current assets.
4. Analyse two likely considerations of a reduction in return on capital employed to the managers of a business.
5. Analyse two factors which Alice should consider when increasing the selling price.
6. Analyse two reasons for the decision for maintaining a provision for irrecoverable debts for the owners.
7. Explain two reasons why shareholders will be interested in the financial statements of a company.
8. Analyse two factors which the owners of a business should consider when offering cash discount to credit customers.

**Worksheet 5: Who is the focus answers – suggestions of what learners might do:**

1. Analyse two advantages to the owners of a business of operating as a partnership to forming a limited company.

*Learners may be tempted to analyse the differences between operating as a limited company and a partnership rather than the advantages of operating as a partnership.*

2. Analyse two advantages to the business of maintaining a debtors control account.

*The emphasis is on the benefits to the business, e.g., the preparation of the statement of financial position is quicker when a debtors control account is maintained. Learners may just give a list of what is entered in the debtors control account.*

3. Analyse two factors to the business of maintaining a provision for depreciation account for non-current assets.

*Learners may make the emphasis on the definition of depreciation rather than the reasons for maintaining a provision for depreciation on non-current assets.*

4. Analyse two likely considerations of a reduction in return on capital employed to the managers of a business.

*Learners must demonstrate here that they know the components needed to calculate ROCE. They will then be confident in demonstrating what may have happened to those components that resulted in a reduction in ROCE.*

5. Analyse two factors which Alice, the owner, should consider when increasing the selling price.

*This is from Alice's point of view. Learners may be tempted to look at this from the customers point of view.*

6. Analyse two reasons for the decision for maintaining a provision for irrecoverable debts for the owners.

*Learners must be confident in using the relevant information in order to calculate an increase/decrease in the provision for irrecoverable debts. They will then be able to analyse why the business maintains a provision for irrecoverable debts.*

7. Explain two reasons why shareholders will be interested in the financial statements of a company.

*Many learners may be tempted to look at this from the general point of view of stakeholders rather than directing their analysis from the shareholders angle.*

8. Analyse two factors which the owners of a business should consider when offering cash discount to credit customers.

*Learners must be look at how the owners will be affected by the introduction of cash discount and not how customers will react.*

### Activity 2: Who might be affected?

Sometimes a question asks learners to analyse the effects or impacts of a business's actions on different stakeholders. Learners need to be able to identify all the potential stakeholders who might be affected by a business action and how they might be affected.

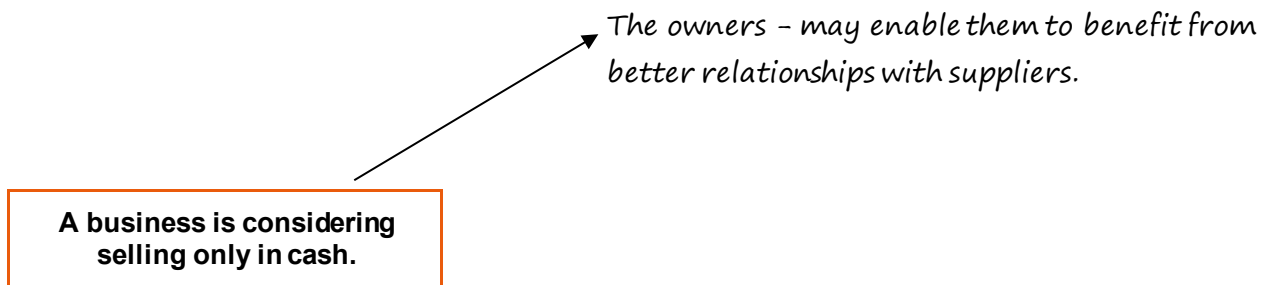
Provide learners with a series of business actions. The actions on **Worksheet 6: Who might be affected?** can be used or changed with other business actions. For each business action, learners identify as many stakeholders as they can that might be affected. Go through the worksheet with learners to check they understand what is required of the task. For this activity learners may work individually or in pairs.

Use **Worksheet 6: Who might be affected answers** and ask learners to peer assess each other's work. For each of these stakeholders, lead a discussion on how they might be affected. Ensure any misconceptions are addressed.

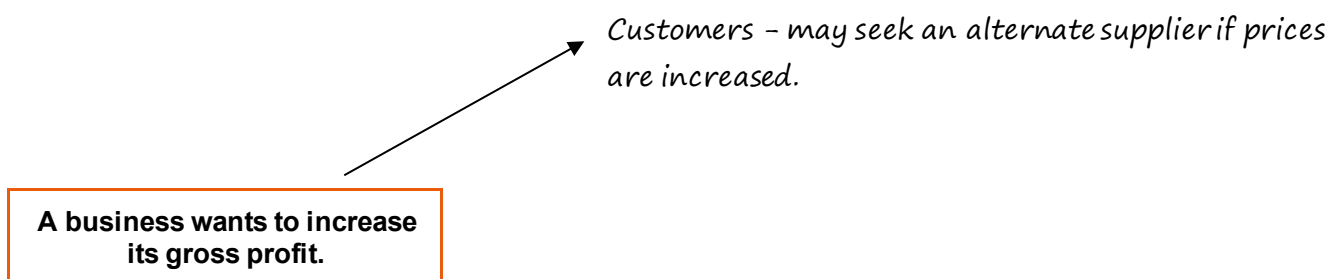
## Worksheet 6: Who might be affected?

For each of the following business actions, identify which interested parties might be affected by adding a spoke to the mind-map. The first interested party has been added for you.

1.



2.



3.

**The owners of a business consider the inventory level is too high.**

*The bank – overdraft may reduce if a sale takes place.*

4.

**A business has decided to install a high-speed packing machine.**

*The employees – may be concerned for the continuity of their jobs.*

**Worksheet 6: Who might be affected answers**

1. A business is considering selling only in cash.

Accept any reasonable answers including:

- *The owners – may enable them to benefit from better relationships with suppliers.*
- *The employees/managers – may lose their jobs as no need for credit control department.*
- *Customers – may go to another supplier who does offer credit terms.*
- *Bank – improved relationship as increased cash deposits.*

2. A business wants to increase its gross profit.

Accept any reasonable answers including:

- *Customers – may seek an alternate supplier if prices are increased.*
- *Suppliers – may be asked to supply cheaper/lower quality products.*
- *Manager – may have to process higher returns if lower quality products sold.*
- *The employees – may seek higher wages if increased gross profit leads to higher profit.*

3. The owners of a business consider the inventory level is too high.

Accept any reasonable answers including:

- *The bank – overdraft may reduce if a sale takes place.*
- *The employees – may lead to staff reduction if less warehouse staff are required.*
- *The owners – may lead to opportunity to rent out warehouse space.*
- *Suppliers – may reduce favourable terms if less inventory purchased or inventory purchased less frequently.*

4. A business has decided to install a high-speed packing machine.

Accept any reasonable answers including:

- *The employees – may be concerned for the continuity of their jobs.*
- *The owners – anticipate increased production leading to higher profits.*
- *The customers – may benefit from lower prices if new machine leads to lower costs.*
- *The suppliers – may lead to larger orders with suppliers if production increases.*

### Activity 3: Chains of analysis

Developed analysis can be seen as a chain of effects. This activity helps learners think about the links in the chain that go from the initial effect through to the end effect.

Give learners a starting effect and how this might end. The chains on **Worksheet 7: Chains of analysis** can be used or changed with other effects.

For each sentence, learners complete the missing links in the chain that match up to the initial effect to the end effect. Go through the worksheet with learners to check they understand what is required of the task. For this activity learners may work individually or in pairs.

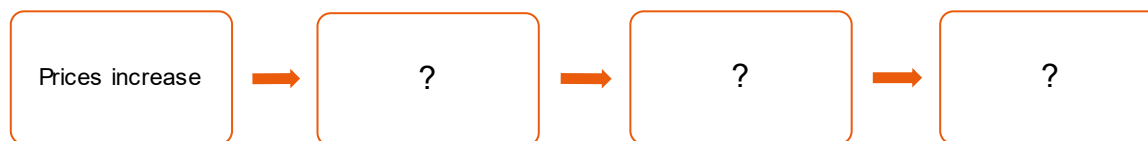
Use **Worksheet 7: Chains of analysis answers** and ask learners to peer assess each other's work. There may be many ways to get from the first effect to the last, so discuss the different routes learners have taken and whether any of the links are more realistic than others. Ensure any misconceptions are addressed.



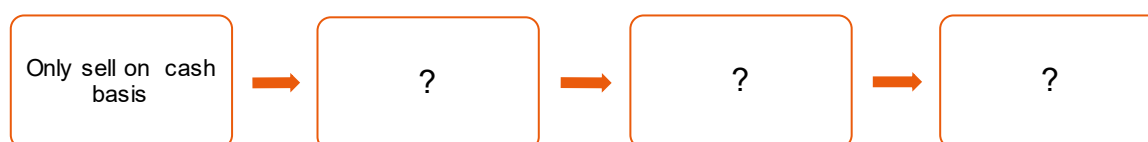
## Worksheet 7: Chains of analysis

For each of the following questions, identify the focus of the analysis.

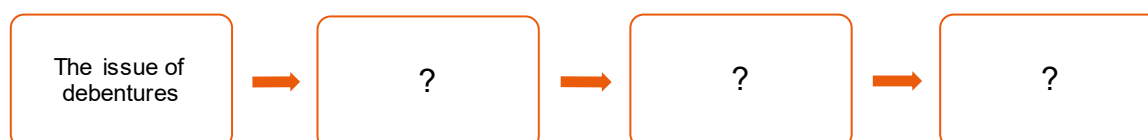
1. A business increases its prices. Develop a chain of analysis that shows how this might affect the business.



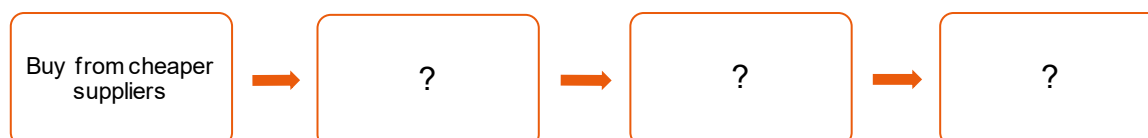
2. A business decides to stop selling on credit terms and to only sell to customers on a cash basis. Develop a chain of analysis of how this might affect the business.



3. A limited company needs to raise additional long-term capital. The company has decided to issue debentures rather than increase share capital. Develop a chain of analysis to show how this might affect the ordinary shareholders.

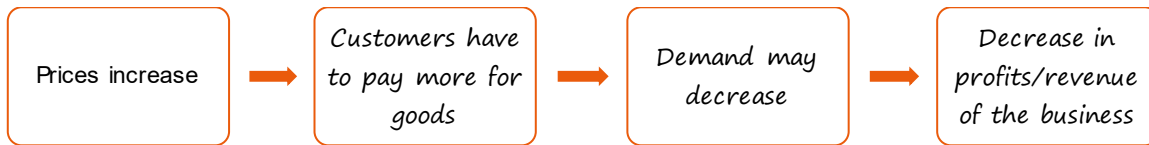


4. A business has decided to buy products for resale from a cheaper supplier. Develop a chain of analysis of how this might affect the business.

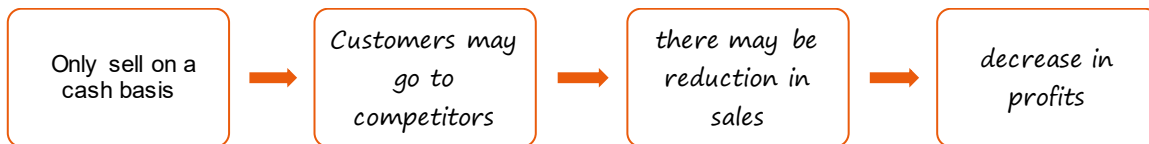


### Worksheet 7: Chains of analysis answers

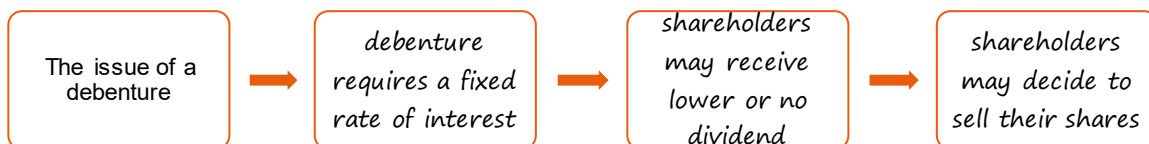
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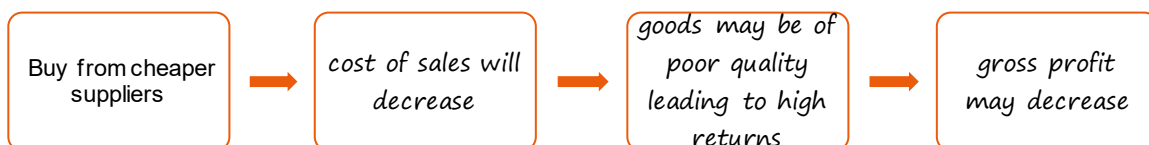
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3. A limited company needs to raise additional long-term capital. The company has decided to issue debentures rather than increase share capital. Develop a chain of analysis to show how this might affect the ordinary shareholders.



4. A business has decided to buy products for resale from a cheaper supplier. Develop a chain of analysis of how this might affect the business.



### Activity 4: Developing advantages and disadvantages

Analysis questions often ask for advantages and/or disadvantages. Being able to analyse the advantages and disadvantages is an essential part of analysis and needs to be in context as well as developed.

Provide learners with a business scenario that may have advantages and disadvantages for a business or a stakeholder. The scenarios in **Worksheet 8: Developing advantages and disadvantages** may be used or replaced with other scenarios.

For each scenario, learners think of two advantages and two disadvantages and explain the impact on the business or stakeholder. Go through the worksheet with learners to check they understand what is required of the task. For this activity learners may work individually or in pairs.

Use **Worksheet 8: Developing advantages and disadvantages answers** and ask learners to peer assess each other's work. Learners are likely to find a range of answers, so different responses should be discussed. Ensure any misconceptions are addressed.

**Extension activity:** discuss with learners whether any of the advantages or disadvantages are more realistic than others?

## Worksheet 8: Developing advantages and disadvantages

Complete the following tables for the given business scenario. Use the scenario to make sure the development is in context.

1. Jason is in business and uses the straight-line method of depreciation to depreciate his motor vehicles. His sister is also in business and uses the reducing balance method.

Analyse one advantage and one disadvantage to Jason for changing to the reducing balance method.

| Advantage | Disadvantage |
|-----------|--------------|
|           |              |

2. Hamid is a wholesaler. His credit suppliers are prepared to double the rate of trade discount provided he increases his current monthly purchases by 20%.

Analyse two advantages and two disadvantages to accepting this offer from his suppliers.

| Advantage | Disadvantage |
|-----------|--------------|
|           |              |

3. Anjula has been in business for many years. All receipts are paid into the bank and payments are made from the bank. She is now considering whether she should sell some of her goods on credit.

Analyse two advantages/benefits and two disadvantages/drawbacks to her selling on credit.

| Advantage | Disadvantage |
|-----------|--------------|
|           |              |

4. A limited company wishes to expand by purchasing additional premises. It is considering either issuing further ordinary shares or by taking a debenture.

Analyse one advantage/benefit and one disadvantage/drawback to the company for each of these strategies.

| Advantage | Disadvantage |
|-----------|--------------|
|           |              |

**Worksheet 8: Developing advantages and disadvantages answers**

1. Jason is in business and uses the straight-line method of depreciation to depreciate his motor vehicles. His sister is also in business and uses the reducing balance method.

Analyse one advantage and one disadvantage to Jason for changing to the reducing balance method.

| Advantage  | Disadvantage  |
|--|---|
| <i>The reducing balance method of depreciation is a suitable method for depreciating motor vehicles as more depreciation is charged in the earlier years of the asset's life when the benefits from the asset are greater.</i> | <i>The reducing balance method of depreciation is more difficult to calculate than the straight-line method. The reducing balance must be calculated each year whereas the straight-line method only needs to be calculated once.</i> |

2. Hamid is a wholesaler. His credit suppliers are prepared to double the rate of trade discount provided he increases his current monthly purchases by 20%.

Analyse two advantages and two disadvantages to accepting this offer from his suppliers.

| Advantage   | Disadvantage   |
|---|--|
| <i>An increased trade credit will reduce Hamid's cost of sales.</i>   | <i>Hamid may have to organise larger storage for the increased inventory which will increase costs.</i>  |
| <i>Hamid will be able to reduce his selling prices which will make him more competitive and may increase revenue.</i> | <i>Hamid will need to make larger payments to his suppliers which may lead to problems in cash flow.</i> |

3. Anjula has been in business for many years. All receipts are paid into the bank and payments are made from the bank. She is now considering whether she should sell some of her goods on credit.

Analyse two advantages/benefits and two disadvantages/drawbacks to her selling on credit.

| Advantage   | Disadvantage   |
|---|--|
| <i>More customers may be attracted by the opportunity to buy on credit so revenue may increase.</i> | <i>Administration costs may increase with the introduction of a credit control department.</i> |
| <i>There may be an increase in profit if revenue increases.</i>                                     | <i>There will be the risk of irrecoverable debts from customers.</i>                           |

4. A limited company wishes to expand by purchasing additional premises. It is considering either issuing further ordinary shares or by taking a debenture.

Analyse one advantage/benefit and one disadvantage/drawback to the company for each of these strategies.

| Advantage   | Disadvantage   |
|---|--|
| <p><u>Issuing shares</u></p> <p>If the expansion proves successful there is increased chance the shareholders will benefit from increased dividends.</p> <p><u>Debenture</u></p> <p>Debenture holders are not members of the company and therefore have no influence on the company operations.</p> | <p><u>Issuing shares</u></p> <p>There may be the possibility of low or no dividend if the payment of interest on the debenture is onerous on the company.</p> <p><u>Debenture</u></p> <p>A debenture carries a fixed rate of interest and has to be paid to the debenture holders whether or not the company makes a profit.</p> |

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