Business Studies

(a) Distinguish between debt and equity financing for a young company. [5 marks]

(b) You have won a contract to write and supply some software and set up a company to do so. The contract is worth £100,000, with 30% payable at start, 20% at a milestone expected to be completed in month 3 after starting, 40% on delivery expected in month 6 and 10% 1 month after delivery. You will need to employ two contract programmers at a rate of £2,500 each per month (plus overheads) for the duration of the contract.

(i) Draw up an outline cash flow budget. What is the working capital requirement? [5 marks]

(ii) You raise investment of £15,000 in the company and arrange a bank loan facility up to another £15,000 (ignore bank charges and loan interest for this question). You purchase £10,000 of capital equipment initially (computers etc). Draw up the balance sheet at the end of month 6. [5 marks]

(iii) The project unfortunately takes an additional two months before passing the milestone. Draw up a revised cash-flow budget including the funds raised and purchases made as specified in part (b)(ii). What effect does this have on the working capital requirement? What options do the Directors have if the bank refuses to extend the loan? [5 marks]