

1. Calculate the Average Receivable Turnover (ART) and Average Collection Period (ACP) of all firms
2. Based upon the calculation, which firm is the most efficient in receivables utilization and why?
3. Which company will face a high variance in the future regarding turnover ratio and collection period?

Answer:

1)

Receivable turnover = Annual credit sale / average a/c receivable

Average collection period = No of days in year / Receivable turnover

A)

$$\begin{aligned} \text{Receivable Turnover for Company A} &= \frac{2,400,000}{(1,200,000 + 100,000) / 2} \\ &= 1800,000 / 1100000 = 1.64 \text{ times} \end{aligned}$$

$$\begin{aligned} \text{Receivable Turnover for Company B} &= \frac{1700,000}{(1,300,000 + 700,000) / 2} \\ &= 1700,000 / 1000,000 = 1.7 \text{ times} \end{aligned}$$

$$\begin{aligned} \text{Receivable Turnover for Company C} &= \frac{1,500,000}{(1,200,000 + 1400,000) / 2} \\ &= 1500000 / 1300000 = 1.15 \text{ times} \end{aligned}$$

B)

$$\text{Average Collection Period for Company A} = 360 / 1.64 = 219.51 \text{ days}$$

$$\text{Average Collection Period for Company B} = 360 / 1.7 = 211.76 \text{ days}$$

$$\text{Average Collection Period for Company C} = 360 / 1.15 = 313.04$$

Part B

Firm B is most efficient because its collection of receivables is 1.7 times during the year.

Part C

Firm C will face a highly variance in terms of turnover ratio and collection period.