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SCHOOL OF ACCOUNTING AND BUSINESS
BSc. (APPLIED ACCOUNTING) GENERAL / SPECIAL DEGREE
PROGRAMME

YEAR II SEMESTER I
END SEMESTER EXAMINATION – NOVEMBER 2014

AFM 20530 Business Finance

Date : 10th November 2014
Time : 9.00 a.m. - 12.00 p.m.
Duration : Three (03) hours

Instructions to Candidates:

- Answer ALL the questions
- The total marks for the paper is 100.
- The marks for each question are shown in brackets.
- Present Value and Future Value Tables are provided
- Use of scientific calculator is allowed.
- Answers should be written neatly and legibly.

Question No. 01

“Business concerns need finance to meet their requirements in the economic world. Any kind of business activity depends on the finance. Hence, it is called as lifeblood of business organizations”

- a. Explain briefly the term “Finance”.

(03 Marks)

- b. State major decisions involved in finance as a business function and explain them briefly.

(08 Marks)

- c. Discuss the objective of financial management and its role in a contemporary business organization.

(09 Marks)

(Total 20 Marks)

Question No. 02

- a. Explain the relationship between the price of a bond and its yield to maturity (YTM).

(05 Marks)

- b. Explain why some bonds sell at a premium over par value while other bonds sell at a discount.

(05 Marks)

- c. On 1st January 2013, ABC Plc issued Rs 100/-, 8 percent coupon unsecured debentures that have a maturity period of 10 years. The coupon is paid semi-annually.

- i. If the yield to maturity on these debentures is 10 percent per annum, determine the price of a debenture on 1st November, 2014.

(06 Marks)

- ii. If the current market price of a debenture is Rs 106/-, calculate the yield to maturity on ABC Plc's debentures.

(04 Marks)

(Total 20 Marks)

Question No. 03

a. What is meant by cost of capital of a business organization?

(03 Marks)

b. Explain briefly the importance of cost of capital in financial decision making.

(04 Marks)

c. Dividends paid by CSR Plc over the last five years were as follows.

| Year ended 31st March; | Dividend per share (Rs) |
|--|------------------------------------|
| 2010 | 2.00 |
| 2011 | 2.16 |
| 2012 | 2.32 |
| 2013 | 2.45 |
| 2014 | 2.65 |

The following information has been extracted from the Statement of Financial Position of the company as at 31st March, 2014.

| | Rs in Mn |
|---|-----------------|
| Stated capital – Ordinary Shares (10,000,000 shares) | 400 |
| Retained earnings | 100 |
| 12% Debentures of Rs 100/- each | 300 |
| Total | 800 |

The ordinary shares and the debentures of the company are currently traded at the prices of Rs 50/- and Rs 105/- each respectively. The debentures have a remaining maturity period of 4 years. The company has recently paid the dividend for the year ended 31st March, 2014. The corporate tax rate is 28%.

You are required to determine the following;

- i. Average dividend growth rate from year 2010 to 2014.
- ii. The expected dividend for the year ended 31st March, 2015 if this average growth rate is expected to be continued.
- iii. Cost of equity capital
- iv. Cost of debentures
- v. Weighted average cost of capital of CSR Plc

(13 Marks)

(Total 20 Marks)

Question No. 04

- a. State four (04) characteristics of equity shares.

(04 Marks)

- b. Critically examine advantages and disadvantages of equity shares as a source of finance.

(06 Marks)

- c. XY (Pvt) Ltd has recorded the following results for the year ended 31st March, 2014.

| | (Rs '000) |
|-------------------------------|-----------|
| Sales | 12,930 |
| Gross profit | 5,350 |
| Profit after tax | 1,260 |
| Preference dividend | 180 |
| Property, plant and equipment | 8,750 |
| Current assets | 450 |
| Current liabilities | 300 |
| Non-current liabilities | 900 |

The company has an issued share capital of 500,000 shares as of 31st March, 2014. The Price-earnings (P/E) ratio of the industry in which the company operates is 10 times. 75% of the industry P/E ratio is an approximation for the P/E Ratio for an unquoted company. The company plans to go public to raise funds for its new projects.

You are required to determine the intrinsic value of an equity share of XY (Pvt) Ltd on the basis of the following approaches;

- i. Earnings based valuation
- ii. Assets based valuation

(10 Marks)

(Total 20 Marks)

Question No. 05

- a. Discuss briefly the concepts of Operating Cycle and Cash Conversion Cycle.

(04 Marks)

- b. The following information has been extracted from the financial statements of Black Plc and Brown Plc for the year ended 31st March 2013. Both companies operate in the same industry.

| | Black Plc (Rs'000) | Brown Plc (Rs'000) |
|--|-----------------------------------|-----------------------------------|
| Current liabilities | 125,380 | 85,600 |
| Sales | 2,329,500 | 2,100,570 |
| Gross profit margin | 20% | 20% |
| Inventory as at 1 st April, 2012 | 239,710 | 194,200 |
| Balances as at 31 st March, 2013; | | |
| - Inventory | 257,530 | 231,700 |
| - Trade debtors | 160,610 | 100,520 |
| - Trade creditors | 85,300 | 32,210 |
| - Cash in hand and at bank | 11,300 | 5,305 |

- i. Calculate gross working capital and net working capital of Black Plc and Brown Plc as at 31st March, 2013.

(02 Marks)

- ii. Compute the operating cycle and cash conversion cycle for Black Plc and Brown Plc.

(06 Marks)

- c. Discuss the importance of inventory management and two (02) techniques used in managing inventory of a manufacturing company.

(08 Marks)

(Total 20 Marks)