CA

THE INSTITUTE OF CHARTERED ACCOUNTANTS OF SRI LANKA

SUGGESTED SOLUTIONS

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21404 – Strategic Financial Management

CA Professional (Strategic Level II) Examination
December 2012

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Answer No. 01

(a) Explain the relevance of each of the items of economic data listed above to Autosmile.

(9 marks)

(i) **Increase in CBSL base rate**

- **This will directly affect the cost of capital;** both the cost of borrowing and the cost of equity (expected rate of return by shareholders) will go up due to increasing base interest rate.

  It will have a negative impact on the expected expansion projects/investments of the company. As the cost of capital (WACC) will go up, future cash flows of the project will be discounted by a higher discount rate. This will result in lower NPV or even negative NPV.

- The interest rate increase will have an impact on the level of overall demand in the economy. This will have a heavy impact on supermarket customers. Credit available through credit cards will also be expensive with the increase in the base rate. The Autosmile's turnover might not grow as expected when the level of interest rates goes up. (It may even come down)
  The increase in interest rate will also reduce the general economic confidence. This will also have a negative impact on the business.

(ii) **Effects of present and forecast rates of inflation**

- A parallel increase in inflation will further influence the level of interest rates to go up as higher levels of inflation will reduce the real rate of interest for savings.
- The increase in inflation will also result in reducing the purchasing power. But the business can be temporarily better off with inflation as they can buy cheaper and eventually sell higher. However, this principle would not be applicable for price marked items. Furthermore, there will not be a much inflation gain as most of the items sold in supermarkets are price marked.
  There will be a negative impact on trade volume especially for non-essential items for which supermarkets will get better margins.
- The required amount of capital for the expansion will go up. The capital cost of planned expansion/investments will also go up.

(iii) **Effects of Tax Rates**

As no change is expected in tax rates in the near future, it is easier to plan with confidence for the next 12 months .

(iv) **Effects of Increasing VAT**

We can expect a drop in sales as well as a drop in profit margins and the overall profits. This will have a negative impact on the supermarket.

(v) **The government investigation on processed foods**

This will have a special impact on the supermarket(as supermarkets are concentrated more on processed foods) leading to drop in profit margins

(vi) **Increase in tax on alcohol products**:

The increase in alcohol tax has been a very common strategy adopted by successive governments in Sri Lanka with an increase in tax. There will be an initial drop in sales volume but it will reverse soon as alcohol is an addictive product. However, the long term growth of alcohol business not be affected in the case of milk powder a similar behaviour would be expected.

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(b) ***Explain whether Autosmile should continue with its expansion plan and other investment proposals. Clearly justify your arguments for or against the expansion.***

(9 marks)

Currently, there are two major threats faced by Autosmile.

1. Unfavorable macro environment
2. Stiff competition coming from the growing number of supermarket chains in the country and the numbers of stores under each chain

How to achieve a sustainable growth for the company under the current environment seems to be a major issue.

Candidates are required to make an attempt to develop their arguments within the backdrop of these current issues.

Arguments in favor of Expansion:

i. Need for growth

The company has started and continued as a family business. now desiring an expansion. As the macroeconomic factors are cyclical, the identified investment proposals business should not be completely abandoned due the changing macro environment. The challenge is meeting the threats of the changing environment effectively.

ii. The need to increase sales

The Company's gross margins would be lower as discussed above. Therefore, the company has to adopt some strategies to increase the volume of sales. The innovative ideas, .e.g. expansion of the product range, introduction of gift vouchers which the company has already implemented seem to be successful. With this positive trend, introducing more outlets would help to expand its customer base. Also, the two new proposals; viz. starting a food processing factory and a processing factory for dairy products, would help to expand the business through supply chain and enhance the value addition by the company, and its profit margins. However, before embarking on new projects, the proposals should be properly evaluated.

iii. Increase in cost of capital

Further increase in the interest rate levels in the near future is expected. In the current Sri Lankan context, interest rates will go up further due to the day by day worsening of public finance situation. and it is expected that this trend will continue in the medium term. Therefore, it can be argued that it is better to raise the capital now for the expansion and other investment projects before the level of interest rates goes up further. (However, the Central Bank has decreased the policy rates by 25 basis points in December. This can be construed as a measure taken against the trend. Medium to long run rates will tend to go up further, unless the macro-economic factors improve.

Access to capital:

From the provided information, it seems that Autosmile has not yet tapped the all possible sources of finance. Hopefully they may raise further equity capital by way of a right issue. Further, the company may consider the use of debt as well.. This is slightly higher but , the after tax cost of debt (Debt is tax deductible) would not be that high. The company has to carefully decide on the options for raising the required funds for any expansion.

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v. Bulk order discounts

With the expansion, the company would be able to change its convenient but expensive purchasing policy. Operating more stores definitely can induce purchases with direct imports yielding higher trade discounts.

Advantage over supply chain and bulk order discount

The proposed expansion will help to overcome some weaknesses of its current business model of the company. If the company has its own processing and packaging factory (both dairy and other products), maintaining the quality of products and reducing the dependency of outside suppliers could be expected.

iv. Economy of scale

Business expansion could lead to various forms of economy of scale. Most of the supermarkets today go for their own brands, especially for processed food and dairy products. Further it enables the company to have a more effective management system etc.; improvements in supply chain etc.

v. Wider geographical coverage

When the company reaches a wider customer base with expansion, its operational risk will go down.

Growing per capita income and changing lifestyle

With the growing per capita income, lifestyle of the people is changing. More and more people are getting used to the supermarket concept and this is an opportunity to Autosmile.

Argument against expansion:

i. Weak Capital market:

Due to the current negative sentiments in the CSE, the company may not be able to get the right price for new issue of shares to raise the required capital.

Worsening macro environment

Most of these factors have been discussed in the previous section of the answer.

ii. Absence of a proper business strategy

The company does not seem to have a proper business strategy. Mere expansion will not be a proper strategy at this moment of severe competition. Any decision needs prudent approach.

Absence of proper project appraisal

Before, taking a concrete decision on the proposal, it is necessary for the company should carry out a comprehensive project appraisal. It is important for the company to understand the incremental cost and incremental revenues from the projects and determine the NPV of the projects. The company may also have to consider the "real options" available for each of these projects. One of the major real options that the company could consider is the timing of the project, whether to start now or to start later. Probably a gradual expansion would be ideal.

iii. Competitive pressure

The company will also have to pay attention on the growing number of supermarket chains in the country and declining sales. However, this does not mean the overall customer base of supermarkets is declining. It seems that the investment in the industry is growing faster than the growth of the customer base. This emphasizes the need for a well focused strategy in terms of target market, business locations, promotion plan, product range etc.

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Overall Conclusion:
As a company, it has to consider growth opportunities and develop strategies to face the challenges of the environment. However, the company should carry out proper planning and evaluation of projects before implementing them.

(c) How do you propose for the company to raise the required capital Justify your answer with valid reasons?

As already discussed in the previous sections with the present macro economic development in the country, the cost of capital for any business would increase .(Recently presented 2013 budget has also proposed to raise more local funding to bridge the budget deficit. when in Sri Lankan government is already indebted heavily locally and to the outside world). With the increase in government borrowing interest rates will go up further. Therefore, an immediate long term borrowing would be beneficial to the company.

(i) The company should consider of issuing debentures with longer term maturity. This will cause a net gain over years for the company (with the increase in interest rates in the economy). It may be attractive to the public if the coupon rate is fixed around 75 to 125 basis points above the long-term bank deposits. The Company's goodwill in the supermarket business will help to raise required capital through debentures subject to other underlying factors.

Other advantages associated with the debentures to the company:

i. Features of the debenture to be issued can be decided by the company to match its cash flows and financial market condition. (e.g. with other underlying factors maturity, call provisions, collateral, convertibility etc.)

ii. Tax deductibility.

(ii) **Rights Issue :**If the debentures do not fit the existing capital structure of the firm raising a part of the required capital by way of right issue could be considered, i.e. initially the company may raise further equity through a right issue and then go for a debenture issue. This will help the company to keep its capital structure at its target and also to keep the rate of debt at a relatively low level.

(iii) **Term Loan :** Term Loan from bankers: If the company wishes to raise a large amount by way of loans for a long period, it would not be cheaper due to the prevailing market conditions. Bankers will be reluctant to lend over a long period. If bankers are agreeable, a term loan is not a bad idea account for the tax shield.

With the limited data it is difficult to conclude what exactly the company should do in this regard. The company should take a decision by analyzing various factors such as the current capital structure, the impact on the cash flow and the profitability, the cost of issue, collateral requirements placement & other schemes such as sale of surplus assets, if any etc.

(d) ***Candidates should be able to link the issue to the current financial markets.***

The company intends to embark on a number of new projects and it is said that "in planning its future the Autosmile was advised to look carefully at a number of factors which may affect the business …….".

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The identified projects require a substantial amount of funds which the company may or may not be able to raise easily. If the company cannot raise the required capital it will be subject to external capital rationing .i.e. hard rationing Even if the company could raise the required capital at a high cost, the company may not be able to realize the important overall business objective of "maximizing shareholder wealth". In such a situation the company should consider soft capital rationing" at least in the short run.

In the context of high uncertainty and limitations of capital discussed above it is important to identify the projects that have the potential of realizing the best outcome within a planning period and in this regard, among other matters Scenario Analysis, Linear Programming and Real Options will be useful.

Scenario Analysis recognises possible outcomes under alternative scenarios based on "what if" criterion. It is a useful tool for identifying the critical factors in project evaluation.

Linear Programming can identify projects which will maximize benefits e.g. NPV, under a capital rationing situation due to budget constraints.

Real options offer the management a flexibility in decision making in response to changes in the environment by postponing, abandoning etc. of projects and thereby enabling the company decision making under uncertainty and limiting downside risk.

(Total 25 marks)

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Answer No. 02

(a) (i) Growth companies are those which generate significant positive cash flows or earnings, increasing at significantly faster rates than the overall economy. The ideal example of a growth company is Google. A growth company tends to have very profitable reinvestment opportunities for its own retained earnings. Thus, it typically pays little or no dividends to stockholders, opting instead to ploughing most or all of its profits back into expanding business.

Growth companies are capable of generating substantial earnings giving attractive re-investment opportunities subject to available liquidity. Thus these companies, as a policy, must plough some profits for reinvestment rather than paying dividends, especially due to the fact that the such companies would be subject to serious pressures and threats from the external factors.

There is no definite optimal factor for an optimal D/E ratio to a growth company viz. it could vary according to the industry or line of business stage of development etc. The debt-equity relationship could vary according to industries involved, a company's line of business and its stage of development. However, because investors are better off putting their money into companies with strong balance sheets, common sense tells us that these companies should have, generally speaking, lower debt and higher equity levels.

Growth rate positively affects the capital structure of a company. The growth opportunity will require more capital to finance the growth. However, companies will tend to take the course of least resistance, obtaining financing from sources that are readily available and then steadily moving on to sources that may be more difficult to utilize. (Pecking Order Theory)

Note: The question specifically refers to optional mix for a **'growth company'**. The candidates required to answer accordingly.

(ii) MV (g) = MV (u) + DT
Market value of a geared company is greater than an ungeared company, and the difference is due to the debt tax shield . (DT)

(b) Market value of Eveready Paint = Rs. 8 million shares x Rs. 100
= Rs. 800 million.

since Natures Chemi's earnings are 4 times greater, the market value of Natures –Chemi is Rs. 800 x 4 = Rs. 3,200 million

∴	MV (g)	=	MV (u) + DT
		=	800 x 4 + 3,000 x 15%
		=	Rs. 3,650 million
	MV (d)	=	Rs. 3,000
∴	MV (e)	=	3,650 - 3,000 = Rs. 650 million
∴	MV of share	=	Rs. $\frac{650 \text{ million}}{10 \text{ mn shares}}$ = Rs. 65

since Natures Chemi's current share price is Rs. 75 and is currently trading at an overvalued price (difference of Rs. 10)

Note – There are other alternative approaches to determine the answers.

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(c) (i) Rights issue = 8,000,000 x 50 = Rs. 400 million

Capital Structure after right issue		Rs. Mn
Equity	⟶ 18mn shares @ Rs. 65	1,170
Debt	⟶ (3,000 - 400)	2,600
		3,770

(ii)

	Rs.
Operating profit	1,500
Less: Redundancy (35,000 x 6 x 1,000)	(210)
Finance cost (Rs. 2,600 @ 12%)	(312)
Profit before tax	978
Tax @ 15%	(146.7)
Profit after tax	831.3

Dividend (60%) = 831.3 x 60% = 498.78

High networth individual dividend = Rs. 498.78 x 51%
= Rs. 254.37

High networth individual investment = (51% x 10 x Rs. 75) + (400 x 51%)
= 382.5 + 204= Rs. 586.5 million

$$\text{Dividend yield} = \frac{254.37}{586.5} = 43\%$$

(iii)

$$\text{Dividend per share} = \frac{\text{Rs. } 498.78 \text{ million}}{18,000,000} = \text{Rs. } 27.71$$

$$\therefore \quad P = \frac{Do\,(I + g)}{Ke - g}$$

$$= \frac{27.71\,(1.05)}{0.2 - 0.05}$$

share price = Rs. 193.97

(Total 15 marks)

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Answer No. 03

(a) "Business in Distress", simply means a business that is in danger or trouble due to various factors, internal or external.
These companies, in order to sustain, may require " reconstruction" and turning around and the financing required for the turnaround process is called turnaround financing.

Turnaround financing could provide an injection of funds e.g. fresh equity), debt structuring of writing off debts conversion of debts to equity or conversion of interest rates, conversion of currency (SWAPS), enabling to resuscitate a sick business.

(b) higher the Z score ⟶ financially strong (Z > 2.99)
lower the Z score ⟶ likelihood of bankruptcy (generally score below 1.81)

$Z = 0.012\ x_1 + 0.014\ x_2 + 0.033\ x_3 + 0.006 x_4 + 0.010 \times x_5$

$= 0.012 \times \frac{150}{1000} + 0.014 \times \frac{300}{1000} + 0.033 \times \frac{225}{1000}(175+50) + 0.006 \times \frac{1,000}{500}(100\times10) + 0.010 \times \frac{800}{1000}$

$= (0.0018 + 0.0042 + 0.007425 + 0.012 + 0.008) \times 100$

$= 3.34$

===

The company is in a financially healthy position.

(c) (i) Share buyback(required cash) = 10 million shares x 15% x 1/10 x 100
= Rs. 15 million

(ii) Share buyback: the cash payment is used to buy back shares to reduce the stated capital. In future, there would not be cash outflows. Furthermore, share buy back would change the capital structure of the firm by way of dividend on the shares cancelled.

By way of dividend. In a dividend payment a periodic cash outflow is expected affecting fund availability. When a dividend is paid dividend tax on behalf of shareholders will have to be made by the company.

(iii)

Capital structure		Rs. mn
Equity = (10,000,000 - 150,000) x 90	=	886.5
Debt	=	500.0
Capital employed	=	1,386.5
		======

(d)

Property at cost	180
Revaluation adjustment	310
Property Revaluation	490
	===

Value attributable to ordinary shareholders = 250 + 310 =Rs. 560 million
= 560/5.6mn share
= Rs. 100 per share

Price to Book value = 560 x 1.5 = Rs. 840 million
= 840/5.6
= Rs. 150 per share

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Price to Earnings	= 30 x 11.5 P/E	=	Rs. 345 million
		=	345/5.6 million
		=	Rs. 61 per share
Replacement	= Rs. 33 x 12 million	=	Rs. 396 million
		=	396/5.6 million
		=	Rs. 70 per share

The intrinsic value of the shares Rs. 61 - Rs. 150

∴ it is not prudent to sell at the maximum price of Rs. 84 /(70 x 1.2)

(e)

US $ 100 x 40 x 85% x 365 x 132	=	Rs. 163,812,000
Net profit margin	=	0.20
Net profit	=	Rs. 32.76 million

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Answer No. 04

(a) **Note:** Rates expressed are" annualized rates". Therefore before solving the problems it is important to express the given rates as rates for a period of three months.

3 months annualized rates converted for a period of three month rates

	Borrowing	***Deposit***
3 Months SKW	2.4%	1.8%
3 Months JPY	3.075%	2.25%
3 Months PHP	1.75%	1.625%

The balance to be settled = CNY 4,000,000/2 = CNY 2,000,000

Spot rate (CNY to SKW) = 2.1610 +/- 0.0050
As Juad buying CNY, they have to buy at the bank's selling rate which is = 2.1610 + 0.0050 = 2.166
Cost at the spot rate = CNY 2,000,000 x 2.166 = **SKW 4,332,000**

Three month forward rate (CNY to SKW) = 2.2145 + 0.0075
Under forward rate Juad has to buy at the rate of = 2.2145 + 0.0075 = 2.2220 (bank forward selling rate)
Cost at the forward rate = CNY 2,000,000 x 2.222
= **SKW = 4,444,000**

Approximately
At a glance it seems the cost is more if the company goes for a forward contract.

The advantage in terms of SKW = 4,444,000 – 4,332,000 = 112,000

Advantages of using forward agreement:
A firm can fix the exchange rate today (at the current rate) for a transaction which will take place at a future date. Then the firm is sure of exactly how much it is going to receive or pay in terms of local currency. Therefore, it does not face a risk in terms of future exchange rate changes. Finally a large fluctuation of firms cost/revenue and profits due to exchange rate changes can be controlled.

Disadvantages of using forward contracts:
The exchange rate could change favorably. There is a possibility that the value of the paying foreign currency to go down against the local currency. and to pay less in terms of the local currency. Such favorable changes cannot be expect when the rate is fixed in advance under a forward agreement.

There may be occasions where you may have to cancel the transaction due to various reasons.

(b) Juad has to borrow SKW and buy JPY in advance and invest in JPY for three months till the payment date.

The amount of JPY needed at the end of three months = JPY 1,400,000

The amount ,Juad has to invest now to get JPY 1,400,000 in 3 months $= \frac{JPY1,400,000}{1+R} = \frac{JPY1,400,000}{1.0225}$
= **JPY 1,369,193**

**Note that the JPY deposit Rate is 2.25% or 0. 0225 for a period of three months*
Amount of SKW needed to buy JPY 1,369,193 = JPY 1,369,193x7.56045 =**SKW 10,351,715**
**** Recognize that Juad has to buy at Bankers selling rate (7.5585 +0.00195 = 7.56045)***

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As Juad is going to borrow SKW 10,351,715**,** it has to pay in 3 months with interest

= SKW 10,351,715* (1+R)

= SKW 10,351,715* (1.024)

= **SKW 10,600,156**

<u>SKW 10,600,156 is the real cost South Korean Won.</u>

Recognize that they have to borrow at the rate of 2.4% = .024

The effective forward rate of the firm:

At the end of three months Juad settles JPY 1,400,000 to the Japanese party with the money available in JPY deposit. For the borrowed money they will have to pay to the bank SKW 10,600,156

So effective forward rate is = approximately

$$JPY = \frac{10,600,156}{1,400,000} = 7.571$$

(c) Juad borrows Philippine Peso (PHP) in 3 months advance and invest in SKW.

Amount Juad has to collect from Philippine in three months' time = PHP 2,500,000

Juad has to borrow PHP against the amount receivable in 3 months =

$$\frac{PHP2,500,000}{1+R} = \frac{PHP2,500,000}{1.0175}$$ **= PHP 2,457,002**

(That is the present value of future receivables)

*Note that PHP borrowing rate is 1.75% = 0.0175

Convert PHP 2,457,002 to SKW = PHP 2,457,002 x 2.2444 = SKW 5,514,495

(***Note that they have to sell at the bank buying rate*** = 2.2504 - 0.0060 = 2.2444)

The company then will invest SKW 5514495 for three months at the rate of 1.8%

=SKW 5,514,495 * (1+R)

= SKW 5,514,495 * (1.0180)

Amount with the interest = SKW 5,613,755

Therefore, the receipt in South Korean Won (SKW) with a money market hedge is = SKW 5,613,755

The company will settle the PHP borrowing with PHP 2.5m receipt.

The effective forward exchange rate in this case is = 2.245 approximately

$$\frac{SKW5,613,755}{PHP2,500,000}$$

Note: Exchange rates given in the question do not necessarily reflect the real parity rates.

(c) Relevant matters to be considered.

- Location
- Availability of infrastructure//manpower
- Cost considerations
- Comparative/Competitive advantage
- Industrial relations/Trade union behaviour
- Government Policies e. g. Duties/duty concession/taxation
- Financial Market
- Risks

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Answer No. 05

(a) Financial flexibility refers to a firm's ability to take advantage of unforeseen circumstances depending on the firm's financial policies and financial structure.

Key factors driving dividend policy include:

- the amount of profit to be distributed/liquidity
- Leverage
- Future growth opportunities/reinvestment opportunities and plans
- Investor/shareholder psychology
- Taxation
- Economic uncertainty
- Cost of funds
- Macro-economic considerations
- Peer benchmarking
- Company Policy
- Legal & Contractual Restrictions –(e.g. solvency test)
- Effect on share Price Volatility, etc

(b) **To : Finance Director**
Re : Proposal for simplifying the capital structure.

This refers to our discussion on 28th December 2012 on the above.

(I) Principles to be considered in preparing an equitable scheme for the proposed revision of the capital structure.

(a) The rights attaching to each class of share are contained in the Articles of Association (AA) of the company and the rights could only be altered in accordance with the procedure laid down in the Articles of Association with the specific approval of the requisite majority of the holders of the particular class of share.

(b) As far as possible, the rights and priorities attached to each class of share should be maintained and if rights and privileges of a particular class of shares are affected, it is important to consider provision of adequate compensation for such class of shares, as discussed below.

(i) 6% cumulative preference shares

Currently they have a priority over others in income distribution. This right is preserved under the proposed scheme. Furthermore; they will be entitled to a higher percentage of dividend. However the adequacy of the compensation is questionable.

(ii)` 8% cumulative participating preference shares

When 8% cumulative participating preference shares are converted to 6.5% cumulative preference shares some of their privileges will be lost viz. 8% is to lowered to 6.5% and they lose the right to participate in further distribution of 'surplus' of ¼ currently available. However the attributable loss to them will be compensated by the issue of 6,00,000ordinary shares. The adequacy of the compensation should be considered.

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(c) Ordinary shareholders

The capitalization of revenue reserves will be a disadvantage to the existing ordinary shareholders as part of the revenue reserves after capitalization will be distributed to the cumulative participating preference shareholders.

Sucha scheme will also dilute the controlling interest of the current ordinary shareholders. However, the suggested scheme will benefit the existing ordinary shareholders by lowering the prior charges of the cumulative preference shares against the profits.

(II) The capital structure of the company after the proposed revision

	Rs. '000'
9,500,000 6.5% cumulative preference shares	95,000
Stated capital (30,000 + 330,000)	360,000
	455,000
Revenue reserves (Rs. 375 m - Rs. 330 m)	45,000
	500,000

Workings

	Current ('000)	Proposed ('000')
(i) No. of Cumulative Preference Shares	1,500	1,500
(ii) No. of Cumulative Participating Preference shares No. of ordinary shares (a)	8,000	8,000 (in the form of cumulative preference shares) 6,000
(iii) Ordinary Shares (b)	3,000	27,000

(III) The company currently earns 10% of the net assets (Rs. 500m) after tax i.e. Rs. 50 million

	Current											
	Stated Cap Rs.	**Div%**	**Div Distribution**		**Furthrt DD**	**Total Div**		**Share Distr after CR (Value) (Rs.)**	**No of Ord Shares**	**DivDist After CR**		
										0.6	0.8	1
OrdSh	30,000,000	1	3,000,000	2/30 f E2	2,000,000	5,000,000	Ord. Shares	30,000,000	3,000,000			
(No)								270,000,000	27,000,000			
								300,000,000	30,000,000	18,000,000	24,000,000	30,000,000
CPS	15,000,000	0.06	900000		0	900,000	6.5% CPS	15,000,000		975000	975,000	975,000
						0		15,000,000				
CPPS	80,000,000	0.08	6400000		1600000	8,000,000	6.5% CPS	80,000,000		5,200,000	5,200,000	5,200,000
						0	Ord. Shares	60,000,000	6,000,000	3,600,000	4,800,000	6,000,000
						0						
	125,000,000		10,300,000		3,600,000	13,900,000		455,000,000		27,775,000	34,975,000	42,175,000
RR	375,000,000		39,700,000		36,100,000	36,100,000		450,000,000		22,225,000	15,025,000	7,825,000
	500,000,000		50,000,000		50,000,000			500,000,000	3,600,000	50,000,000	50,000,000	50,000,000

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(IV) Under the proposed scheme the existing 6% cumulative preference shareholders would gain marginally, (only 75,000) whereas the 8% cumulative participating preference shareholders may gain but the extent of which depends on the rate of ordinary dividend declared. The expected gain dividend of ordinary shareholders will be high. The proposed scheme will increase the number of ordinary shares, leading to a reduction of EPS and the annual transfers to revenue reserves.

Any other matters

- The proposal will improve the current seems unsound effect of high gearing, but at the same time sufficiency of distributable profits should be considered.
- Convening a meeting of shareholders under the provisions of Article of Association.
- Obtain approval of shareholders for by way of an EGM to consider the resolution.
- The effect on EPS/leverage.
- Higher dividend payout ratio will reduce the revenue reserve and affect the company's growth/reinvestment prospects/profit potential.
- The company has resorted to external borrowing at a marginal cost of capital at 18%, the potential undesirable impact on profitability will be higher.
- Possibility of further simplification of the capital structure
- Currently the interest rates are higher (compared to a few years ago) recognizing the market interest rates it is important to consider whether the 6.5% to cumulative preferences shares is adequate.

(20 marks)

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