Final Term Papers

Fall 2009 (Session 03c)

MGT201

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Question No: 1 (Marks: 1) - Please choose one

Which of the following would **NOT** improve the current ratio?

- **Borrow short term to finance additional fixed assets**
- Issue long-term debt to buy inventory
- Sell common stock to reduce current liabilities
- Sell fixed assets to reduce accounts payable

Question No: 2 (Marks: 1) - Please choose one

Which group of ratios measures how effectively the firm is using its assets?

- Liquidity ratios
- Debt ratios
- **Coverage ratios**
- Activity ratios

Question No: 3 (Marks: 1) - Please choose one

The RBS pays 5.60%, compounded daily (based on 360 days), on a 9-month certificate of deposit, if you deposit Rs. 20, 000 you would expect to earn around _____ in interest.

- Rs.840
- **Rs.858**
- Rs.1,032
- Rs.1,121

Question No: 4 (Marks: 1) - Please choose one

Assume that the interest rate is greater than zero. Which of the following cash-inflow streams totaling Rs.1, 500 would you prefer? The cash flows are listed in order for Year 1, Year 2, and Year 3 respectively.

- **Rs.700 Rs.500 Rs.300**
- Rs.300 Rs.500 Rs.700
- Rs.500 Rs.500 Rs.500
- Any of the above, since they each sum to Rs.1,500

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Question No: 5 (Marks: 1) - Please choose one

Which of the following would be considered a cash-flow item from an "operating activity"?

- **Cash outflow to the government for taxes**
- Cash outflow to shareholders as dividends
- Cash inflow to the firm from selling new common equity shares
- Cash outflow to purchase bonds issued by another company

Question No: 6 (Marks: 1) - Please choose one

Which of the following will **NOT** equate the future value of cash inflows to the present value of cash outflows?

- Discount rate
- **Profitability index**
- Internal rate of return
- Multiple Internal rate of return

Question No: 7 (Marks: 1) - Please choose one

Which of the following is a legal agreement between the corporation issuing bonds and the bondholders that establish the terms of the bond issue?

- **Indenture**
- Debenture
- Bond
- Bond trustee

Question No: 8 (Marks: 1) - Please choose one

_____ is a high-risk, high-yield bond.

- Zero coupon bond
- Mortgage bond
- **Junk bond**
- Income bond

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Question No: 9 (Marks: 1) - Please choose one

A coupon bond pays annual interest, has a par value of Rs.1,000, matures in 4 years, has a coupon rate of 10%, and has a yield to maturity of 12%. What is the current yield on this bond?

- **► 10.65%**
- ► 10.45%
- ► 10.95%
- ► 10.52%

Question No: 10 (Marks: 1) - Please choose one

When a bond will sell at a discount?

► The coupon rate is greater than the current yield and the current yield is greater than yield to maturity

► The coupon rate is greater than yield to maturity

► The coupon rate is less than the current yield and the current yield is greater than the yield to maturity

► The coupon rate is less than the current yield and the current yield is less than yield to maturity

Question No: 11 (Marks: 1) - Please choose one

What is the price of a stock?

► The future value of all expected future dividends, discounted at the dividend growth rate

► The present value of all expected future dividends, discounted at the dividend growth rate

► The future value of all expected future dividends, discounted at the investor's required return

► The present value of all expected future dividends, discounted at the investor's required return

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Question No: 12 (Marks: 1) - Please choose one

Which of the following combinations will produce the highest growth rate? Assume that the firm's projects offer a higher expected return than the market capitalization rate.

- ► **A high plowback ratio and a high P/E ratio**
- ► A high plowback ratio and a low P/E ratio
- ► A low plowback ratio and a low P/E ratio
- ► A low plowback ratio and a high P/E ratio

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Question No: 13 (Marks: 1) - Please choose one

Diversification can reduce risk by spreading your money across many different _____.

- ► Investments
- ► Markets
- ► Industries
- ► **All of the given options**

It states that don't put all your eggs in one basket. Diversification can reduce risk. By spreading your money across many different Investments, Markets, Industries, Countries you can avoid the weakness of each.

Question No: 14 (Marks: 1) - Please choose one

The square of the standard deviation is known as the _____.

- ► Beta
- ► Expected return
- ► Coefficient of variation
- ► **Variance**

Question No: 15 (Marks: 1) - Please choose one

Which of the following is **NOT** a major cause of systematic risk.

- ► A worldwide recession
- ► A world war

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- ► World energy supply
- ► **Company management change**

Question No: 16 (Marks: 1) - Please choose one

_____ means expanding the number of investments which cover different kinds of stocks.

- ► **Diversification**
- ► Standard deviation
- ► Variance
- ► Covariance

Question No: 17 (Marks: 1) - Please choose one

Which of the following would **NOT** be the part of the risk if the stock is a single stock investment?

- ► Company specific risk
- ► Un-diversifiable risk
- ► **Diversifiable risk**
- ► Random risk

In case of portfolio risk we can further made distinction between Diversifiable Risk and Market risk

Question No: 18 (Marks: 1) - Please choose one

To limit volatility what should be the appropriate action?

- ► **To diversify**
- ► To check the stocks prices daily
- ► To own just a few securities
- ► Not to invest in risky securities

Question No: 19 (Marks: 1) - Please choose one

In efficient market the stock price depends upon the required return which depends upon _____.

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- **Market risk**
- Total risk
- Diversified risk
- Non- Systematic risk

In Perfect Markets and Efficient Markets where Rational Investors have Diversified Away ALL Company Specific Risk, Value (and Stock Price) depends on Required Return which depends on Market Risk (and not Total Risk).

Question No: 20 (Marks: 1) - Please choose one

Why markets and market returns fluctuate?

- Because of political factors
- Because of social factors
- Because of socio-political factors
- **Because of macro systematic factors**

Question No: 21 (Marks: 1) - Please choose one

The overall (weighted average) cost of capital is composed of weighted averages of which of the following?

- The cost of common equity and the cost of debt
- The cost of common equity and the cost of preferred stock
- The cost of preferred stock and the cost of debt
- **The cost of common equity, the cost of preferred stock, and the cost of debt**

Question No: 22 (Marks: 1) - Please choose one

Which of the following costs would be considered a fixed cost?

- Raw materials
- **Depreciation**
- Bad-debt losses
- Production labor

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Question No: 23 (Marks: 1) - Please choose one

Assume the nominal interest rates (annual) in the country of Fredonia and the United States are 6% and 12% respectively. What is the implied 90-day forward rate if the current spot rate is 5 Fredonia marks (FM) per U.S. dollar?

- ► 4.732
- ► **4.927**
- ► 5.074
- ► 5.283

1+(.12/4) = 1.03; 1+(.06/4) = 1.015; FM / 5 = (1.015 / 1/03); FM = 4.927.

Question No: 24 (Marks: 1) - Please choose one

A firm that acquires another firm as part of its strategy to sell off assets, cut costs, and operates the remaining assets more efficiently is engaging in _____.

- ► A strategic acquisition
- ► **A financial acquisition**
- ► Two-tier tender offer
- ► Shark repellent

Question No: 25 (Marks: 1) - Please choose one

When a firm can acquire another firm?

- ► Only by purchasing the assets of the target firm
- ► Only by purchasing the common stock of the target firm
- ► **By either purchasing the assets or the common equity of the target firm**
- ► None of the given options

Question No: 26 (Marks: 1) - Please choose one

Which of the following is **NOT** a type of financial lease arrangement?

- ► Sale and leaseback
- ► **Indirect leasing**
- ► Leveraged leasing
- ► All of the given options

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Question No: 27 (Marks: 1) - Please choose one

The Board of Directors announces the amount and date of the next dividend on the _____ date; while the _____ date is the first date on which the purchaser of a stock is no longer entitled to the recently declared dividend.

- ► Declaration; record
- ► Ex-dividend; record
- ► **Declaration; ex-dividend**
- ► Payment; record

Question No: 28 (Marks: 1) - Please choose one

What would you expect to happen to the price of a share of stock on the day it goes ex-dividend?

- ► **The price should increase by the amount of the dividend**
- ► The price should decrease by the amount of the dividend
- ► The price should decrease by one-half the amount of the dividend
- ► The price should remain constant

Question No: 29 (Marks: 1) - Please choose one

What is the amount of the annual interest tax shield for a firm with Rs. 3 million in debt that pays 12% interest if the firm is in the 35% tax bracket?

- ► **Rs.126, 000**
- ► Rs.234, 000
- ► Rs.360, 000
- ► Rs.1, 050,000

Tax Shield =(income-(debt*interest rate))*tax rate
=(3000000)*12%*35%

Question No: 30 (Marks: 1) - Please choose one

While calculating the Stock Portfolio Risk using 3x3 Matrix Approach, non-diagonal terms shown in Boxes are called:

- ► Variance
- ► Coefficient

- **Covariance**
- Correlation

Terms in all other (or NON-DIAGONAL) Boxes are called "COVARIANCE" terms which account for affect of one stock's movement on another stock's movement

Question No: 31 (Marks: 1) - Please choose one

While calculating the stock beta graphically, the formula to calculate the beta coefficient for stock B is:

- $(r_M^* - r_{RF}) / (r_B^* - r_{RF})$
- **$(r_B^* - r_{RF}) / (r_M^* - r_{RF})$**
- $(r_B^* - r_{RF}) / r_{RF}$
- $(r_B^* - r_{RF}) / r_M^*$

Slope = Beta = Δ Y / Δ X = % Δ rA* / % Δ rM*
= A =Risk Relative to Market = (rA* - rRF) / (rM* - rRF)

Question No: 32 (Marks: 1) - Please choose one

While analyzing any portfolio the value of "r" represents which of the following?

- Internal rate of return
- Expected rate of return
- **Required rate of return**
- Assumed rate of return

Question No: 33 (Marks: 1) - Please choose one

If a stock is part of totally diversified portfolio then which of the following is TRUE for that stock?

- Stock's total Risk = Company Risk
- Stock's total Risk = Market Risk
- **Stock's total Risk = Market Risk + Company Risk**
- All of the given options

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Question No: 34 (Marks: 1) - Please choose one

High uncertainty is associated with which of the following?

- ► Preferred stock
- ► **Common stock**
- ► Bonds
- ► T –Bills

Question No: 35 (Marks: 1) - Please choose one

The date on which the names of stockholders in the Stock Transfer Register of firm are documented is referred as:

- ► Declaration Date
- ► **Holder-of-record Date**
- ► Ex-Dividend Date
- ► Payment Date

Firm records names of shareholders in the Stock Transfer Register i.e. Feb 28th 2003. About 1 month after Declaration Date

Question No: 36 (Marks: 1) - Please choose one

Operating revenue can be calculated from which of the following formulas?

- ► Operating Revenue = Fixed cost * Quantity + Variable cost
- ► Operating Revenue = Price / Quantity +Variable cost
- ► Operating Revenue = Sale price * Quantity
- ► Operating Revenue = Variable cost * Quantity / Fixed cost

Question No: 37 (Marks: 1) - Please choose one

Which of the following statements is **TRUE** about an aggressive approach to finance working capital?

► Financing seasonal requirements of current assets with short-term debt and permanent requirement of current assets with long term debt

► Financing permanent requirements of current assets with short-term debt and seasonal requirement of current assets with long term debt

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► **Financing seasonal as well as permanent requirements of current assets with short-term debt**

► Financing seasonal as well as permanent requirements of current assets with long term debt

Financing some long-term needs with short-term funds. This is a maturity matching approach and is neither aggressive nor conservative in nature Rather, it is a moderate approach.

Question No: 38 (Marks: 1) - Please choose one

Capital structure theory is presented by which of the following?

► Robert Alan Hill
► **Modigliani & Miller**
► Brigham & Houston
► Van Horne & Gittman

Question No: 39 (Marks: 1) - Please choose one

All of the following are the examples of permanent financing **EXCEPT:**

► Common Equity
► **Current Liabilities**
► Long-term Loans
► Bonds

Question No: 40 (Marks: 1) - Please choose one

Which of the followings proposes that the value of the firm is independent of its capital structure?

► The Capital Asset Pricing Model
► **M&M capital structure theory**
► The law of variable proportion
► The Law of One Price

What Rubinstein generalized, was the most basic of the M&M propositions: The proposition on the irrelevance of capital structure.

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Proposition I: "The market value of any firm is independent of its capital structure and is given by capitalizing its expected return at the rate ρ appropriate to its class", Modigliani and Miller [1958, page 268]. In modern terms, capital structure is irrelevant, and firm value is equal to the present value of the free cash flow discounted at the relevant cost of capital.

Question No: 41 (Marks: 1) - Please choose one

Value of the firm can be calculated with the help of which of the following formulas?

- ► Price of a share x No. of shares outstanding
- ► Price of a share x debt / equity
- ► Price of a share / No. of shares outstanding
- ► Price of a share x earnings after tax / equity

Question No: 42 (Marks: 1) - Please choose one

If the sales are expected to be poor in future than management wants to raise capital through which of the following:

- ► Debt financing
- ► Equity financing (common & preferred stock)
- ► Term finance certificates
- ► National saving certificates

Question No: 43 (Marks: 1) - Please choose one

Company A has to purchase another company. How do Company A pay for buying the other company?

- ► In Cash
- ► In Shares
- ► Bank Borrowing
- ► All of the given options

Question No: 44 (Marks: 1) - Please choose one

Which of the following mathematical expressions depicts divestiture?

- ► 5-1=4

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- 5-1=6
- 5+1=6
- **None of the given options**

"Divestiture" = Reverse Merger. Benefit of Efficient Reallocation of Resources: 5 - 1 = 5! It means by selling an inefficient or unproductive unit of the company you can have more value as it saves costs

Question No: 45 (Marks: 1) - Please choose one

Under efficient market, the effect of debt on WACC can be represented with the help of which of the following?

- **Straight line**
- U shaped curve
- Concave
- Time to time fluctuation

Effect under Pure MM View (Ideal Efficient Markets): Its assumptions are No Taxes and No Bankruptcy Costs so Debt increases Risk BUT is also cheaper than Equity. Change in Debt has no effect on WACC and Value of the firm. WACC curve is flat.

Question No: 46 (Marks: 1) - Please choose one

Under traditional view, the effect of debt on WACC can be represented with the help of which of the following?

- Straight line
- **U shaped curve**
- Concave
- Time to time fluctuation

Effect under Traditionalist View (Tradeoff Theorists, Real Markets): Combined Effects of Taxes and Financial Distress / Bankruptcy Costs are a Flat U-Shaped WACC Curve with a Minimum Point which represents the Optimal Capital Structure (i.e. Best Debt Ratio for the Firm).

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Question No: 47 (Marks: 1) - Please choose one

According to the trade off theory, value of the firm rises as a result of _____.

- ► **Tax saving**
- ► Increase in EPS
- ► Increase in EBIT
- ► Saving in cost of debt

This is the case of pure MM theory where there are no taxes and bankruptcy costs. But in case of trade off theory in reality initially value of the firm rises as there is interest tax saving but with excessive leverage, value of the firm starts declining as interest cost goes very high due to bankruptcy risk.

Question No: 48 (Marks: 1) - Please choose one

Which of the following statements is true about business risk?

- ► The financial risk of a firm decreases when it takes on a risky project
- ► The financial risk of a firm increases when it takes on more equity
- ► **The business risk of a firm increases when it takes on a risky project**
- ► The business risk of a firm increases when it takes on more debt

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Question No: 49 (Marks: 1) - Please choose one

Under Net income approach, which of the following is a correct sequence of calculating cost of capital?

- ► Net income – Total firm's market value – WACC
- ► Net income – WACC – total firm's market value
- ► WACC – Net income – market value of equity
- ► Market value of firm – WACC – Net income

Question No: 50 (Marks: 1) - Please choose one

From which of the following equations, net income can be calculated?

- ► **NI = (EBIT - x_D r_D) (1 - Tc)**
- ► NI = (EAT - x_D r_D) (1 - Tc)

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- ► NI = (EBIT + x_D r_D) (1 - Tc)
- ► NI = (EBIT - x_D r_D) / (1 - Tc)

E = Net Income (NI)/ Cost of Equity for levered firm (rE,L)

Note that NI = EBIT - Interest - Tax = EBT – Tax

NI = (EBIT - xD rD) (1 - Tc)

Question No: 51 (Marks: 1) - Please choose one

Which of the following refers to a unique type of Japanese corporate organization based on a close partnership between government and businesses?

- ► **Keiretsu**
- ► Chaebols
- ► Lean and mean
- ► Options

www.qualitysolutions.ca/key-quality-terms.htm

Question No: 52 (Marks: 1) - Please choose one

Which of the following is a South Korea type business in that is a conglomerate with Monopoly power?

- ► Keiretsu
- ► **Chaebols**
- ► Lean and mean
- ► Options

Chaebol (alternatively Jaebol, Jaebeol;) refers to a South Korean form of business conglomerate. (form definition of chaebols)

Question No: 53 (Marks: 1) - Please choose one

What is bid rate for currency?

- ► **Buying rate for currency**
- ► Selling rate of currency
- ► Forward rate of currency
- ► Ask rate of currency\

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BID Rate = Buying Price for Currency. Example: Bid Rs.60 / US$1 Means Bank or Money Changer will Buy (or Bid) one US$ from you for Rs.60. This also means that you (the Customer) are Selling Dollar to the Bank. Bid Rs.60 / US$1 means Bid Rs60 /Ask US$1

Question No: 54 (Marks: 1) - Please choose one

What is the primary principle for money changers?

- ► Ask rate should be less than bid rate
- ► **Ask rate should be greater than bid rate**
- ► Ask rate should be equal to bid rate
- ► Bid rate should be greater than ask rate

Fundamental Principle for F/x Traders and "Money Changers": Buy Low and Sell High. So, ASK > BID Rate

Question No: 55 (Marks: 3)

Calculate tax shield from the given information.

Corporate tax rate is 35% and amount of debt is Rs. 20, 000 and rate of return is 8%.

Tax Shield =(income-(debt*interest rate))*tax rate

Tax shield = (20,000 * 8%)* 35%

= 560 Rs

Question No: 56 (Marks: 5)

How can a manager calculate the opportunity cost of capital for a project? Give answer in bulleted form only.

Question No: 57 (Marks: 5)

Suppose you are a financial manager of XYZ Corporation and you have been assigned the task to calculate the numerical value of your firm's WACC (Weighted Average Cost of Capital), what procedure would you follow keeping in mind that the firm is using NOI (Net Operating Income) approach?

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Question No: 58 (Marks: 10)

Suppose that the risk free rate is 12% and the expected market return is 20%. The FM Corporation has a beta of 0.75 and the Gord Corporation has a beta of 1.25.

a. **Find the expected return on the FM Corporation.**

b. **Find the expected return on the Gord Corporation.**

c. **Suppose that because of a suddenly unanticipated increase in inflation, the risk free rate raises to 16% and the market risk premium remains at 8%. Find the expected return on of FM and Gord.**

Question No: 59 (Marks: 10)

Ammar Watch Company is the renowned ladies watch manufacturers. They are offering watch in the market at a price of Rs. 30. They have estimated that they will manufacture and sale almost 30, 000 watches. Fixed cost for the preparation of these watches is Rs.150, 000. Variable cost associated with the preparation of these watches is Rs. 20 per watch.

From the above information you are required to calculate the followings:

- **What is the profit or loss for the units of 8, 000 or 18, 000?**
- **Calculate the break even point? (in units and sales)**

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