



FINAL
Examination Paper

(COVER PAGE)

Session : January 2014

Programme : Diploma in Business Administration

Course : FIN2101 : FINANCIAL MANAGEMENT

Date of Examination : 11 MARCH 2014

Time : 2.00pm – 4.00pm Reading Time : Nil

Duration : 2 Hours

Special Instructions :

Section A: Answer **ALL** questions.

Section B: Answer any **ONE (1)** question in the answer booklet provided.

Materials permitted : Non-programmable Calculator

Materials provided : Mathematical Tables

Examiner(s) : _____

Moderator : _____

This paper consists of 6 printed pages, including the cover page

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DIPLOMA IN BUSINESS PROGRAMME/DIPLOMA IN BUSINESS
FIN 2101/2102 : FINANCIAL MANAGEMENT
FINAL EXAMINATION : JANUARY 2014 SESSION

Instructions: This paper consists of **TWO (2)** sections. Answer **ALL** questions from **SECTION A** and any **ONE (1)** question in **SECTION B** in the answer booklet provided.

SECTION A: Answer ALL questions.

Question 1

- (a) Explain what should be the goal of a company from a financial management's point of view.
(6 marks)
- (b) What is market efficiency? Explain the three forms of market efficiency according to the efficient market hypothesis.
(13 marks)
- (c) Name one type of business organisation and briefly discuss its advantages.
(6 marks)

Total 25 marks

Question 2

- (a) A public company had just undergone an issuing exercise of debentures. The debentures are at 10%, \$100 par, maturing in 10 years, to be redeemed at par. If the current market price for these debentures is at \$110.20 per unit, calculate the yield-to-maturity of the debentures.

(6 marks)

- (b) Bullet Tech Ltd, a public listed company in manufacturing, has the following capital structure:

	\$
Ordinary share capital, \$1.00 par	2,000,000
Preference share capital, 5%, \$2.00 par	500,000
10% debentures, \$100 par, 10 years maturity	1,000,000

Additional information

Bullet Tech Ltd is expected to experience growth at a constant rate of 7%.

The current dividend paid was \$0.80.

Its ordinary shares are currently trading at the stock market for \$9.50 per share.

The preference shares are now at \$3.50 per share

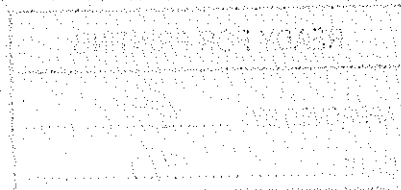
The yield to maturity of the debentures has been calculated to be 12.5%

Current tax rate is at 30%.

Required:

- (i) Calculate the cost of common stock (shares). (4 marks)
- (ii) Calculate the cost of preference shares. (4 marks)
- (iii) Calculate the after-tax cost of debentures. (4 marks)
- (iv) If the proportions of the capital structure are 60% equity, 25% debt and 15% preference shares, how much is the Weighted Average Cost of Capital? (3 marks)
- (c) Gunner Ltd's shares are currently trading at \$5.50 per share in the stock exchange. Its beta is at 2.56. Assuming the current risk-free rate is at 6%, and market return is at 15%, how much is the expected return of the share? Show your workings. (4 marks)

Total 25 marks



Question 3

The financial manager of Max Untung Ltd is considering the planned upcoming marketing campaign for one of its new products. The forecasted financial information for the campaign is as below:

Marketing campaign

Cost	\$450,000
Annual estimated Net after-tax cash inflow (not inclusive of salvage value)	\$155,000
Economic life of project	4 years
Salvage value at end of year 4	\$60,000

The financial manager for Max Untung Ltd uses a 10% rate of return for this project. He can accurately foresee that the salvage value at end of Year 4 can be recovered in full and in cash. Current tax rate is at 30%. It is assumed the cash flows will remain the same throughout the campaign except in the final year due to salvage value.

Required:

- (a) Calculate for the marketing campaign above
- (i) Net Present Value (6 marks)
 - (ii) Accounting Rate of Return (based on total cost) (6 marks)
- (b) State whether the marketing campaign is beneficial to the company and should it be continued as planned? (5 marks)
- (c) Give **TWO** criticisms each for the Accounting Rate of Return and Payback Period capital budgeting techniques. (8 marks)

Total 25 marks

SECTION B: Answer ONE (1) question**Question 4**

- (a) Mei Lin is saving to buy a new car in four years. She will save \$450 at the end of each month until the four years are over. She intends to save the money into an account that will give her 2.0% interest compounding per month. How much will she have after 4 years?

(5 marks)

- (b) John Hsu wants to start a business in 10 years. He hopes to have \$200,000 by that time to invest in the business. To reach his goal, he intends to invest a certain amount today in an investment fund that will give him 8.0% p.a., compounding semi-annually. How much will John have to invest today to achieve his target?

(5 marks)

- (c) Muthu had just obtained a car loan from a bank. The bank had agreed to lend him \$120,000, with a 5% deposit upfront for the car. Muthu will have to pay monthly installments to repay the loan, at an interest of 3.0% per annum, compounding monthly, for 9 years.

- (i) How much is his monthly installment?

(5 marks)

- (ii) How much is the total interest that Muthu will have paid if he continues the loan until the agreed settlement term (ie 9 years)?

(4 marks)

- (iii) If Muthu decides to settle the loan completely after 6 years, how much interest will he save?

(6 marks)

Total 25 marks

Question 5

- (a) Share A and Share B have the following returns under different states of the economy.

State of economy	Probability	Share A (Returns)	Share B (Returns)
Recession	0.1	(10%)	11%
Normal	0.5	13%	7%
Boom	0.4	25%	8%

Calculate the following:

- i The expected rate of returns for both shares. (6 marks)
- ii The standard deviation for both shares. (6 marks)
- iii On a stand-alone basis, which share is riskier? (3 marks)
- (b) If the beta for both shares are known, would the expected returns for both shares calculated using the Capital Asset Pricing Model (CAPM) be the same as part (a)(i)? Why or why not? (4 marks)
- (c) Explain unsystematic risk and elaborate ONE way to reduce this type of risk (diagrams are not necessary). (6 marks)

Total 25 marks

-THE END-

FIN2101/2102/(F)Jan2014/Kee Cheun Howe /12.1.2014

