



STAMFORD COLLEGE

SCHOOL OF BUSINESS, MARKETING AND ACCOUNTING

DIPLOMA IN BUSINESS ADMINISTRATION (SEMESTER 5)

DBA 208: FINANCIAL MANAGEMENT

Date : 30 August 2007
Time : 9.30am-12.30pm

Duration: 3 hours

Instructions to Candidates

This paper consists of FIVE questions. Candidates are required to answer FOUR questions.

Please ensure that this examination paper contains FIVE questions on FOUR printed pages before you start the examination.

Books, papers and other written materials are not allowed to be brought into the examination hall. A candidate who violates the examination rules of Stamford College or commits a malpractice will be disqualified from the examination.

Write your Examination Index Number on each page of your answer booklet.

Note: This examination paper is attached with the formula sheet and mathematical tables.

Answer any FOUR out of FIVE questions.

Question 1

Alwayslate Corporation

Income Statement for the year ended December 31, 2006

	[\$ 000]
Sales	3 756
Cost of goods sold	2 453
Depreciation	490
EBIT	813
Interest paid	613
Taxable income	200
Taxes [34%]	68
Net Income	132

Dividends	46
Additions to retained earnings	86

Alwayslate Corporation

Balance Sheet as of December 31, 2006

	[\$ 000]
Current assets	
Cash	88
Account receivables	192
Inventory	368
Total	648
Fixed assets	
Net equipment	5 354
Total assets	6 002
Current liabilities	
Account payables	144
Notes payables	1 039
Total	1 183
Long-term debt	2 077
Owner's equity	
Common stock	300
Retained earnings	2 442
Total liabilities and owner's equity	6 002

- a.) From the income statement and the balance sheet of Alwayslate Corporation above, compute the following:
- i. Current ratio.
 - ii. Cash ratio.
 - iii. Inventory turnover.
 - iv. Receivables turnover.
 - v. Day's sale in inventory.
 - vi. Day's sale in receivables.
 - vii. Total debt ratio.
 - viii. Times interest earned.
 - ix. Cash coverage.
 - x. Return on equity. (12.5 marks)
- b.) Briefly explain four limitations in ratio analysis. (12.5 marks)
- (Total = 25 marks)

Question 2

You are considering three investments. The first is a bond that is selling in the market at \$1 200. The bond has a \$1 000 par value, pays interest at 14 per cent, and is scheduled to mature in 12 years. For the bonds of this risk class, you believe that a 12 per cent rate of return should be required.

The second investment that you are analysing is a preferred stock that has \$100 par value and sells for \$80. The preferred stock pays an annual dividend of \$12. Your required rate of return for this stock is 14 per cent.

The last investment is a common stock with \$35 par value that recently paid a \$3 dividend. The firm's earnings per share have increased from \$4 to \$8 in the last 10 years, which also reflects the expected growth in the dividends per share for the indefinite future. The stock is selling for \$25, and you think the reasonable required rate of return for the stock is 20 per cent.

Required:

- a) Calculate the value of each of the securities based on your required rate of return. (15 marks)
- b) Which investment or investments should you accept and why? (5 marks)
- c) If your required rates of return changed to 14 per cent for the bond, 16 per cent for the preferred stock, and 18 per cent for the common stock, how would your answers to parts (a) and (b) change? (5 marks)

(Total = 25 marks)

Question 3

Below is the information of Slowpay Company:

<u>Item</u>	<u>Beginning [\$]</u>	<u>Ending [\$]</u>
Inventory	5 000	7 000
Account receivables	1 600	2 400
Account payables	2 700	4 800

In addition, the credit sales for the year just ended was \$50 000, and the cost of goods sold was \$30 000.

Required:

- Calculate the inventory period. (5 marks)
- Calculate the receivables period. (5 marks)
- Calculate the payables period. (5 marks)
- Calculate the cash cycle. (5 marks)
- Explain the flexible short-term financial policies in terms of a firm's investment in current assets, and its financing of the current assets. (5 marks)

(Total = 25 marks)

Question 4

A proposed investment has the following cash flows:

<u>Year</u>	<u>Cash Flow [\$]</u>
0	-100
1	50
2	40
3	40
4	15

The required rate of return for the investment is 15 per cent.

Required:

- Calculate the payback period. (5 marks)
- Calculate the net present value [NPV]. (5 marks)
- Briefly explain two advantages and three disadvantages of the average accounting return [AAR]. (5 marks)
- Assume a three-year project with a projected net income of \$1 000 in Year 1, \$2 000 in Year 2, and \$4 000 in Year 3. The cost is \$9 000, which will be depreciated using the straight-line method with zero residual value at the end of Year 3. Determine the AAR of the project. (10 marks)

(Total = 25 marks)

Question 5

The following forecasts have been made for the six months of 1 July to 31 December 2007 for Chucky Ltd.

- (a) Cash and Bank balance at 1 July 2007 is \$4 500.
- (b) Sales in units:

May	June	July	Aug.	Sept.	Oct.	Nov.	Dec.
300	350	400	450	470	330	220	200

- (c) Selling price is \$30 per unit.
- (d) Debtors will pay two months after the receipt of goods.
- (e) Production in units:

May	June	July	Aug.	Sept.	Oct.	Nov.	Dec.
420	460	500	430	290	250	270	230

- (f) Raw material costs \$7 per unit, which is paid for two months after the material is used in production.
- (g) Direct labour costs \$8 per unit is payable in the same month as production.
- (h) Variable expenses are \$2 per unit and will be paid for in the month after production.
- (i) Fixed expenses of \$2 500 per month are paid in the same month.
- (j) A machine is to be bought and paid for in September for \$15 000.
- (k) Debenture amounting to \$8 000 will be issued in December.
- (l) An interim dividend of \$4 000 will be paid in August.

Required:

Prepare a Cash Budget from July to December 2007.

(Total = 25 marks)

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