

**International Islamic University Chittagong**

**Department of Business Administration**

BBA Final Examination, Spring-2022

Course Title: Financial Management

Course Code: FIN-2402

Time: 2.5 hours

Marks: 50

No.	Category	Key Terms	Marks	COs
1.a.	Understand	Define leverage and capital structure. Explain the different factors that influence the capital structure	3	CLO <sub>2</sub>
1.b.	Analyze	A company currently has assets of Tk. 10 million. The firm is all equity financed. The company currently has net income of Tk. 1.6 million and it pays out 40% of its income as dividend and its growth rate in dividend is 5%. There are 350,000 shares outstanding and the cost of capital is 12.5%.  The company is considering a recapitalization where it will issue Tk. 1.8 million in debt and use the proceeds to repurchase the stock. Its cost of debt will be 10% and cost of equity will rise to 13.5%. What is the current share price? What will be the share price after recapitalization, assuming the same payout ratio and 30% tax rate?	7	CLO <sub>3</sub>
2.a.	Remember	What do investors prefer? Dividends or capital gains?	3	CLO <sub>2</sub>
2.b.	Evaluate	Pacific Jean made a net income of \$3,000,000, and it had 1,000,000 shares of common stock outstanding. The stock of company trades at \$32 a share. A pacific jean is considering a plan in which it will use available cash to repurchase 20% of its stock in the open market. The repurchase of stock is expected to have no effect on the net income or the company's P/E ratio. What will be the stock price of pacific jean after the stock repurchase?	3	CLO <sub>3</sub>
2.c.	Analyze	Welch Company is considering two mutually exclusive projects, each of which requires a 10 million investment. The estimated internal rate of return(IRR) and cost of capital for these projects are given below: Project A: Cost of capital = 13% , IRR=18% Project B: Cost of capital =13%' IRR=20% The optimal capital structure of the company consists of 40% debt and 60% equity, and expects to have a net income of \$ 8 million. Calculate the dividend payout ratio using residual dividend model.	4	CLO <sub>3</sub>
3.a.	Analyze	McDowell Industries sells on terms of 2/12, net 40. Total sales for the year are \$912,500; the customers pay on average 50 days after their purchases. i. What is the nominal cost of trade credit? ii. What is the effective cost of trade credit? iii. What would happen to its accounts receivable if McDowell toughened up on its collection policy with the result that all non-discount customers paid on the 30th day?	5	CLO <sub>3</sub>
3.b.	Analyze	The Zocco Corporation has an inventory turnover of 5 times, an average collection period of 35 days, and a payables deferral period of 45 days. i. What is the length of the cash conversion cycle? ii. If Zocco's annual sales are \$346,750 and all sales are on credit, what is the investment in accounts receivable? iii. if the company holds negligible amount of cash and marketable securities and its current liabilities are of \$65,000, what is its current ratio?	5	CLO <sub>3</sub>
4.a.	Evaluate	Mr. Chowdhury is negotiating a loan with Delta Bank for Tk. 300, 000 1-year loans. Delta Bank has offered the following alternatives. Calculate effective annual cost for each of the alternatives. Which alternative should be selected?	6	CLO <sub>3</sub>

A 10% annual rate on a simple interest loan, with 20% compensating balance required and the interest is payable at the end of the year.

- i. A 9.5 percent annual rate on a discounted loan with 12 percent compensating balance required.
- ii. Interest is figured as 8 percent of Tk. 300,000 payable at the end of the year but the Tk. 300,000 is payable in monthly installment.

4.b. Remember How can you define working capital? Explain the different alternatives of current asset policies. 4 CLO<sub>2</sub>

5.a. Evaluate ACI is thinking of modifying its working capital policy. Fixed assets are \$600,000, sales are projected at \$3 million, and the EBIT/sales ratio is projected at 15%. The interest rate is 10% on all debt, the federal-plus-state tax rate is 40% and ACI plans to maintain a 50% debt-to-asset ratio. Three alternative current asset policies are under consideration: 40% 50%, and 60% of projected sales. What is the expected return on equity under each alternative? 5 CLO<sub>3</sub>

5.b. Analyze ACI and SQUARE had the following balance sheets as of December 31, 2020 (Thousands of dollars): 5 CLO<sub>3</sub>

Assets/Liabilities and Equity	ACI	SQUARE
Current Assets	\$100,000	\$80,000
Fixed assets	100,000	120,000
Total assets	\$200,000	200,000
Current liabilities	\$20,000	\$80,000
Long-term debt	80,000	20,000
Common stock	100,000	100,000
Total liabilities and equity	\$200,000	\$200,000

Earnings before interest and taxes for both firms are \$30 million, and corporate tax is 40%.

- a. What is the return on equity for each firm if the interest rate on current liabilities is 10% and the rate on loan-term debt is 13%?
- b. Assume the interest on current debt rises to 20%, while the rate on existing loan remains unchanged. What would be the return on equity for both companies?
- c. Which company is in a riskier position? Why?

6.a The GPH is trying to determine the effect of its inventory turnover ratio and days sales outstanding (DSO) on its cash flow cycle. The sales of GPH in 2020 were \$150,000, and it earned a net profit of 6% or \$9,000. It turned over its inventory 6 times during the year, and its DSO was 36.5 days. The firm had fixed assets totaling \$35,000. GPH's payable deferral period is 40 days. 7 CLO<sub>3</sub>

- a. Calculate the cash conversion cycle of GPH
- b. Assuming GPH holds negotiable amount of cash and marketable securities, calculate its total assets turnover and ROA.
- c. Suppose GPH believes that the inventory turnover can be raised to 7.3 times. What would GPH's cash conversion cycle, total assets turnover, and ROA have been if the inventory turnover had been 7.3 times for 2020.

6.b. Remember Define cash conversion cycle (CCC), and explain why, holding other things constant, a firm's profitability would increase if it lowered its CCC. 3 CLO<sub>1</sub>

7.a. Understand Why some trade credit is called free while other credit is called costly? Justify your answer with example. 2 CLO<sub>1</sub>

7.b. Creativity Robi has recently acquired Airtel. Argue in favor of this acquisition. 2 CLO<sub>1</sub>

7.c. Understand Compare different types of mergers. 3 CLO<sub>1</sub>