International Islamic University Chittagong
Department of Business Administration
Program: MBA
Final Examination, Spring-2022
Financial Restructuring and Corporate Governance (FIN5507)

Time: 3 Hours **Full Marks: 40**

Answer any four from the following Questions:

Question:01

a) How would you distinguish between LBO and MBO? Analyze the typical types of financing involved in LBOs and MBOs. 3

b) You are given the following information of a potential LBO firm: 7

Sales Revenue = Tk 12000				
	Year-1	Year-2	Year-3(n)	Year-4(n+1)
Sales Growth rate	7%	7%	9%	5%
Interest expense	400	380	300	200
NOPAT	10% on Sales Revenue for every years			
Depreciation	5% on Sales Revenue for every years			
Changes in Working Capital	1.5% on Sales Revenue for every years			
Capital expenditure	5% on Sales Revenue for every years			
Debt amount	Tk.2500			
Tax rate	40%			
Required rate of return	12.00%			
Number of shares	100			

Calculate: Intrinsic Share Price of LBO firm.

Question:02

a) Describe the major forces of cross border transaction. 3

b) Suppose we find the following data: 7

Current forward exchange rate: TK 1= $ 0.011 ; $1= taka 93
Current spot exchange rate: TK 1= $ 0.0104 ; $1= taka 96
Current domestic interest rate = 12%; domestic inflation rate = 6.9%
Foreign country WACC = 10%. Cash flows and respective probabilities are given in the following table:

	0	1	2	3	4	5
Cash flow in $		150	160	170	180	1200
Probabilities		.9	.9	.8	.8	.6

Calculate: i) Current foreign interest rate ii) foreign country inflation rate iii) real rate of interest iv) Present value of the investment in $ and in TK.

Question:03

a. What are the effects of using levered recapitalization? 2

b. Initial input values of a company are as follows: 8

Operating Income	Tk300000
Shares outstanding	100000
Management ownership	20%
Market value per share	$30
Market value of the firm	$3000000
Tax rate	40%

Requirement: If total asset is $200000, calculate the following for both alternatives i.e., 20% debt and 40% debt of market value of the firm:

i) Balance sheets for both the alternatives ii) shares repurchased with debt proceeds iii) debt to market equity ratio iv) TIE

Question:04

a) Analyze the accounting treatment of share repurchase. 2

b) **Pedrollo Motor** Incorporation, a producer of Turbine Generators, is in this situation: 8
EBIT= Tk.5 million, tax rate(T)= 37%, debt outstanding(D) = 3 million, cost of debt(Kd)= 10% and cost of stock (Ks)= 15%; shares of stock outstanding(N_0) =750000; and book value per share=Tk.10. Since Pedrollo Motor's product market is stable and the company expects no growth, all earnings are paid out as dividends. The debt consists of perpetual bonds.

i. Pedrollo is now trying to increase its debt by Tk.7 million, to a total of Tk.10 million, using the new debt to repurchase and retire some of its shares at the current price. Its interest rate on debt will be 12 percent, and its cost of equity will rise from 15% to 17%. EBIT will remain constant. Should Pedrollo go for its Shares Repurchase? Provide your suggestion comparing the Earning per Share (EPS) and Share Price (P_0) before repurchase as well as after repurchase.

ii. What is Time Interest Earn (TIE) ratio before repurchase as well as after repurchase?

Question:05

a) What are the Key Responsibilities of the Board of Directors and Management? 5

b. How do you define the corporate governance? Discuss its principles. 5

Question:06

a.) A company currently has assets of $5 million. The firm is 100% equity financed. The company currently has net income of $1 million, and it pays out 40 % of its net income as dividends. Both dividends and net income are expected to grow at a constant rate of 5% per year. There are 200000 shares outstanding and the current cost of capital is 13.40%.
The company is considering a recapitalization where it will issue $1 million in debt and use the proceeds to repurchase stock. Its cost of debt will be 11% and the cost of equity will be 14.5%. The company has a 40% tax rate. 6

i) What is the current share price?

ii) Assume that the company maintains the same payout ratio, what will be its share price following the recapitalization?

b.) Evaluate the effects of share repurchase on leverage ratios. 2

c.) Discuss the various methods of financial restructuring. 2