

MIDTERM EXAMINATION
Spring 2009

MGT201- Financial Management (Session - 4)

Time: 60 min

Marks: 50

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

What are the earnings per share (EPS) for a company that earned Rs.100, 000 last year in after-tax profits, has 200,000 common shares outstanding and Rs.1.2 million in retained earning at the year end?

- ▶ **Rs.1.00**
- ▶ Rs. 6.00
- ▶ Rs. 0.50
- ▶ Rs. 6.50

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

Among the pairs given below select a(n) example of a principal and a(n) example of an agent respectively.

- ▶ Shareholder; manager
- ▶ Manager; owner
- ▶ Accountant; bondholder
- ▶ **Shareholder; bondholder**

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

Which of the following is equal to the average tax rate?

- ▶ **Total tax liability divided by taxable income**
- ▶ Rate that will be paid on the next dollar of taxable income
- ▶ Median marginal tax rate
- ▶ Percentage increase in taxable income from the previous period

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

Which of the following would be deductible as an expense on the corporation's income statement?

- ▶ **Interest paid on outstanding bonds**
- ▶ Cash dividends paid on outstanding common stock
- ▶ Cash dividends paid on outstanding preferred stock
- ▶ All of the given options

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

In conducting an index analysis every balance sheet item is divided by _____ and every income statement is divided by _____ respectively.

- ▶ Its corresponding base year balance sheet item; its corresponding base year income statement item
- ▶ Its corresponding base year income statement item; its corresponding base year balance sheet item
- ▶ Net sales or revenues; total assets
- ▶ **Total assets; net sales or revenues**

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

Which group of ratios measures a firm's ability to meet short-term obligations?

- ▶ **Liquidity ratios**
- ▶ Debt ratios
- ▶ Coverage ratios
- ▶ Profitability ratios

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

Which group of ratios relates profits to sales and investment?

- ▶ Liquidity ratios
- ▶ Debt ratios
- ▶ Coverage ratios
- ▶ **Profitability ratios**

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

Interest paid on the original principal borrowed is often referred to as _____.

- ▶ Compound interest
- ▶ Present value
- ▶ **Simple interest**
- ▶ Future value

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

If the following are the balance sheet changes, which one of them would represent use of funds by a company?

- ▶ Rs. 8,950 decrease in net fixed assets
- ▶ Rs. 5,005 decrease in accounts receivable
- ▶ **Rs. 10,001 increase in accounts payable**
- ▶ Rs. 12,012 decrease in notes payable

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

In preparing a forecast balance sheet, it is likely that either cash or _____ will serve as a "plug figure" or balancing factor to ensure that assets equal liabilities plus shareholders' equity.

- ▶ Retained earnings
- ▶ Accounts receivable
- ▶ Shareholders' equity
- ▶ **Notes payable (short-term borrowings)**

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

What is the present value of Rs.8,000 to be paid at the end of three years if the interest rate is 11%?

- ▶ **Rs.5,850**
- ▶ Rs.4,872
- ▶ Rs.6,725
- ▶ Rs.1,842

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

What is the present value of Rs.1,000 to be paid at the end of 5 years if the interest rate is 8%.

- ▶ **Rs.680.58**
- ▶ Rs.1,462.23
- ▶ Rs.322.69
- ▶ Rs.401.98

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

As interest rates go up, the present value of a stream of fixed cash flows _____.

- ▶ **Goes down**
- ▶ Goes up
- ▶ Stays the same
- ▶ Can not be found

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

The benefit we expect from a project is expressed in terms of:

- ▶ **Cash in flows**
- ▶ Cash out flows
- ▶ Cash flows
- ▶ None of the given options

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

A proposal is accepted if payback period falls within the time period of 3 years.
According to the given criteria which of the following project will be accepted?

	Payback period
Project A	1.66
Project B	2.66
Project C	3.66

- ▶ Project A
- ▶ Project B
- ▶ Project C
- ▶ **Project A & B**

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

If a project's initial cash outflow of Rs. 100,000 is followed by four annual receipts of 36,000 we can get the nearest discount factor by:

- ▶ Interpolation
- ▶ Dividing 100,000 by 36,000
- ▶ **Dividing 36,000 by 100,000**
- ▶ Insufficient information

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

In which of the following situations you can expect multiple answers of IRR?

- ▶ **More than one sign change taking place in cash flow diagram**
- ▶ There are two adjacent arrows one of them is downward pointing & the other one is upward pointing
- ▶ During the life of project if you have any net cash outflow
- ▶ All of the given options

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

Which of the following technique would be used for a project that has non-normal cash flows?

- ▶ Internal rate of return
- ▶ **Multiple internal rate of return**
- ▶ Modified internal rate of return
- ▶ Net present value

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

What is the advantage of a longer life of the asset?

- ▶ Cash flows from the asset becomes non-predictable
- ▶ **Cash flows from the asset becomes more predictable**
- ▶ Cash inflows from the asset becomes more predictable
- ▶ Cash outflows from the asset becomes more predictable

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

Which one of the following is **NOT** the disadvantage of the asset with very short life?

- ▶ Money has to be reinvested in some other project with uncertain NPV
- ▶ Money has to be reinvested in some other project with certain NPV
- ▶ Money has to be reinvested in some other project with return so risky
- ▶ **None of the given options**

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

You are selecting a project from a mix of projects, what would be your first selection in descending order to give yourself the best chance to add most to the firm value, when operating under a single-period capital-rationing constraint?

- ▶ Profitability index (PI)
- ▶ Net present value (NPV)
- ▶ Internal rate of return (IRR)
- ▶ **Payback period (PBP)**

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

Which one of the following is the right of the issuer to call back or retire the bond by paying off the bondholders before the maturity date?

- ▶ Call in
- ▶ Call option
- ▶ **Call provision**
- ▶ Put option

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

Which of the following is a characteristic of a coupon bond?

- ▶ Pays interest on a regular basis (typically every six months)
 - ▶ **Does not pay interest on a regular basis but pays a lump sum at maturity**
- ▶ Can always be converted into a specific number of shares of common stock in the issuing company
- ▶ Always sells at par

Question No: 24 (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: 25 (Marks: 1) - Please choose one

An investment opportunity set formed with two securities that are perfectly negatively correlated. What will be standard deviation in the global minimum variance portfolio?

- ▶ **Equal to zero**
- ▶ Greater than zero
- ▶ Equal to the sum of the securities' standard deviations
- ▶ Equal to -1

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

How efficient portfolios of "N" risky securities are formed?

- ▶ These are formed with the securities that have the highest rates of return regardless of their standard deviations
- ▶ They have the highest risk and rates of return and the highest standard deviations
- ▶ They are selected from those securities with the lowest standard deviations regardless of their returns
- ▶ **They have the highest rates of return for a given level of risk**

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

Which of the following is **NOT** an example of hybrid equity?

- ▶ Convertible bonds

- ▶ **Convertible debenture**
- ▶ Common shares
- ▶ Preferred shares

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

The value of dividend is derived from which of the following?

- ▶ Cash flow streams
- ▶ Capital gain /loss
- ▶ Difference between buying & selling price
- ▶ **All of the given options**

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

How dividend yield on a stock is similar to the current yield on a bond?

- ▶ Both represent how much each security's price will increase in a year
- ▶ Both represent the security's annual income divided by its price
- ▶ Both are an accurate representation of the total annual return an investor can expect to earn by owning the security
- ▶ **Both incorporate the par value in their calculation**

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

The market capitalization rate on the stock of Fast Growing Company is 20%. The expected ROE is 22% and the expected EPS is Rs. 6.10. If the firm's plowback ratio is 90%, the P/E ratio will be _____.

- ▶ **8.33**
- ▶ 50.0
- ▶ 9.09
- ▶ 7.69

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

In the dividend discount model, which of the following is (are) **NOT** incorporated into the discount rate?

- ▶ Real risk-free rate
- ▶ Risk premium for stocks
- ▶ **Return on assets**
- ▶ Expected inflation rate

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

A company whose stock is selling at a P/E ratio greater than the P/E ratio of a market index, most likely has _____.

- ▶ An anticipated earnings growth rate which is less than that of the average firm
- ▶ **A dividend yield which is less than that of the average firm**
- ▶ Less predictable earnings growth than that of the average firm
- ▶ Greater cyclicality of earnings growth than that of the average firm

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

Which of the following is the variability of return on stocks or portfolios not explained by general market movements. It is avoidable through diversification?

- ▶ **Systematic risk**
- ▶ Standard deviation
- ▶ Unsystematic risk
- ▶ Financial risk

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

When Return is being estimated in % terms, the units of Standard Deviation will be mention in _____.

- ▶ **%**
- ▶ Times
- ▶ Number of days
- ▶ All of the given options

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

A well-diversified portfolio is defined as:

▶ **One that is diversified over a large enough number of securities that the nonsystematic variance is essentially zero**

- ▶ One that contains securities from at least three different industry sectors
- ▶ A portfolio whose factor beta equals 1.0
- ▶ A portfolio that is equally weighted

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

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

- ▶ New competitors
- ▶ New product management
- ▶ **Worldwide inflation**
- ▶ Strikes

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

You are considering two investment proposals, project A and project B. B's expected net present value is Rs. 1,000 greater than that for A and A's dispersion of net present value is less than that for B. On the basis of risk and return, what would be your conclusion?

- ▶ Project A dominates project B

- ▶ Project B dominates project A
- ▶ Neither project dominates the other in terms of risk and return
- ▶ **Incomplete information**

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

Which of the following is a drawback of percentage of sales method?

- ▶ It is a rough approximation
- ▶ There is change in fixed asset during the forecasted period
- ▶ Lumpy assets are not taken into account
- ▶ **All of the given options**

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

Which of the following need to be excluded while we calculate the incremental cash flows?

- ▶ Depreciation
- ▶ **Sunk cost**
- ▶ Opportunity cost
- ▶ Non-cash item

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

Why companies invest in projects with negative NPV?

- ▶ **Because there is hidden value in each project**
- ▶ Because they have chance of rapid growth
- ▶ Because they have invested a lot
- ▶ All of the given options

Question No: 41 (Marks: 10)

ICO Company must decide between two mutually exclusive projects. The following information describes the cash flows of each project.

Year	Project "A"	Project "B"
0	Rs. (20,000)	Rs. 24,000
1	10,000	10,000
2	8,000	10,000
3	6,000	10,000

- Assume that 15% is the appropriate required rate of return. What decision should the firm make about these two projects?
- If the firm reevaluated these projects at 10%, what decision should the firm make about these two projects?

A) We have 2 project A , B

Project A, $I_0 = -Rs20000$, $Yr 1 = +Rs10000$, $Yr2 = Rs8000$, $Yr3 = Rs6000$

Project B, $I_0 = -Rs24000$, $Yr1 = +Rs10000$, $Yr2 = Rs10000$, $Yr3 = Rs10000$

In simple NPV=

$$\text{Project A} = -20000 + 10000 + 8000 + 6000 / (1.15)^3$$

Rs= 2630.19

$$\text{Project B} = -24000 + 10000 + 10000 + 10000 / (1.15)^3$$

Rs= 3945.29

The firm will decide to take the 2nd project B. becuz its NPV is greater tha project A.

B)

$$\text{Project A} = -20000 + 10000 + 8000 + 6000 / (1.10)^3$$

Rs= 3005.25

$$\text{Project B} = -24000 + 10000 + 10000 + 10000 / (1.10)^3$$

Rs= 4507.88

Again on 10%, project B is better tha project A.