College Name: ____________________________________________________________

Student Name: _______________________ Father's Name: _________________________

Copy No: _________________________

**KARACHI UNIVERSITY BUSINESS SCHOOL**
**UNIVERSITY OF KARACHI**
**FINAL EXAMINATION JUNE 2017; AFFILIATED COLLEGES**
**INTRODUCTION TO BUSINESS FINANCE; BA (H)–412 (PART B)**
**BBA – IV**

**Date: June 14, 2017** **Max. Time: 1.5 Hrs**
**Max. Marks: 40**

**INSTRUCTIONS:**

1. **Attempt any 4 questions. Do not write anything on the question paper, EXCEPT the initials mentioned above.**
2. **Mobile phones or any other communicating device will not be allowed in the examination room. Students will have to remove the batteries of these devices before entering the examination hall.**

Q1 Given the following data, find the expected rate of inflation during the next year.

r* = real risk-free rate = 3%.
Maturity risk premium on 10-year T-bonds = 2%. It is zero on 1-year bonds, and a linear relationship exists.
Default risk premium on 10-year, A-rated bonds = 1.5%.
Liquidity premium = 0%.
Going interest rate on 1-year T-bonds = 8.5

Q2 Tariq is 30 years old and is saving for her retirement. She is planning on making 36 contributions to her retirement account at the beginning of each of the next 36 years. The first contribution will be made today (t = 0) and the final contribution will be made 35 years from today (t = 35). The retirement account will earn a return of 10 percent a year. If each contribution she makes is $3,000, how much will be in the retirement account 35 years from now (t = 35)?

Q3 A company has just been taken over by new management which believes that it can raise earnings before taxes (EBT) from $600 to $1,000, merely by cutting overtime pay and thus reducing the cost of goods sold. Prior to the change, the following data applied:

| | | | |
|---|---|---|---|
| Total assets: | $8,000 | Debt ratio: | 45% |
| Tax rate: | 35% | BEP ratio: | 13.3125% |
| EBT: | $600 | Sales: | $15,000 |

These data have been constant for several years, and all income is paid out as dividends. Sales, the tax rate, and the balance sheet will remain constant. What is the company's cost of debt? (Hint: Work only with old data.)

Q4 You are given the following cash flows. What is the present value (t = 0) if the discount rate is 8 percent, rounded to a whole dollar?

| | | | | |
|---|---|---|---|---|
| 0 | 1 | 2 | 3 | 4 |
| 0 | 1,000 | 2,000 | 3,000 | 4,000 |

Q5 Hamid Grocers is deciding among two mutually exclusive projects. The two projects have the following cash flows:

| Year | Project A Cash Flow | Project B Cash Flow |
|---|---|---|
| 0 | −$50,000 | −$30,000 |
| 1 | 10,000 | 6,000 |
| 2 | 15,000 | 12,000 |
| 3 | 40,000 | 18,000 |
| 4 | 20,000 | 12,000 |

The company's cost of capital is 10 percent (WACC = 10%). Which project with the highest internal rate of return (IRR) and minimum PBP?

Q6 Jarrett Enterprises is considering whether to pursue a restricted or relaxed current asset investment policy. The firm's annual sales are $400,000; its fixed assets are $100,000; debt and equity are each 50 percent of total assets. EBIT is $36,000, the interest rate on the firm's debt is 10 percent, and the firm's tax rate is 40 percent. With a restricted policy, current assets will be 15 percent of sales. Under a relaxed policy, current assets will be 25 percent of sales. What is the difference in the projected ROEs between the restricted and relaxed policies?

**END OF SUBJECTIVE PAPER**