College Name: ____

Seat No: ______________________ Student's Name: ______________________________________

Copy No: ______________________

KARACHI UNIVERSITY BUSINESS SCHOOL
UNIVERSITY OF KARACHI
FINAL EXAMINATION DECEMBER 2017; AFFILIATED COLLEGES
CORPORATE FINANCE; BA(BS)–622
BBA – VIII

Date: January 13, 2018 **Max Time: 3 Hrs**
Max Marks: 60

INSTRUCTIONS:

1. **Attempt any 5 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 Abbot's Fried Chicken is a fast food chain. Although its expenses depend primarily on sales, these expenses are not necessarily paid in cash in the month of the sale. For example, wage expense amounts to 25% of the month's sales but is paid on the first day of the next month. Chicken is purchased for the current month (its cost represent 20% of the sales volume) and is paid for in cash. Frozen French fries, oil and other supplies cost 30% of a given month's sales. They are purchased with cash one month prior to the sales. Finally, Abbot has rent expenses totaling $ 220,000 per month; their expected sales are as follows;

Month	August	September	October	November	December	January
Expected Sales	1,000,000	1,200,000	1,100,000	850,000	700,000	950,000

a) Find Abbot operating expenses for September, October, November and December.
b) Abbot's is currently experiencing cash flow problem in the month of September and is considering an offer by the chicken supplier to take 60 days credit with a credit charge of 2.5% for this two month. Find Abbot's expected outflows for September, October, November and December.

Q2 a) Benson Brother Inc is considering investing in a machine to produce computer keyboards. The price of the machine will be $ 400,000 and its economic life is five years. The machine will be fully depreciated by the straight line method. The machine will produce 10,000 keyboards each year. The price of each keyboard will be $40 in the first year and will increase by 5%per year. The production cost per keyboard will be $20 in the first year and will increase by 10% per year. The corporate tax rate for the company is 34%. If the discount rate is 15%, what should they do?

b) Define the following Terms
1. Capital budgeting 2. Pay Back Period 3. Net Present Value 4. Internal rate of return.

03 a) Define the following.
i. Market return ii. Capital Asset Pricing Model iii. Risk Premium

b) Stock X has a beta of 0.75, stock Y has a beta of 1.2 and stock Z has a beta of 1.5. The risk free rate is 11% and the expected market return is 19%.
a. Find the expected return on stock X.
b. Find the expected return on stock Y.
c. Find the expected return on stock Z.
d. Suppose that you construct a portfolio consisting of 40% X, 30% Y and 30% Z. Using your answer to part a, b and c find the expected return of this portfolio.
e. What is the beta of the portfolio specified in part d
f. Using the information in the body of the problem and your answer to part e, find the expected return on your portfolio.

Q4 a) What are benefits and cost of Credit Extension Policy?

b) Abbot Company plans to liberalize its credit policy by extending its current 30 day credit period to 60 days. The company expects that this will increase its current sales of $ 348,000 by 30%. Unfortunately, however bad debt are also expected to rise to 5% up from their current level of 2% of the total sales. The company operating cost of 35% of the sales and its credit collection cost of $ 4,500 are expected to remain the same. The company is in the 30% tax bracket and it requires all investments to return 10%. Would you advise the company to go ahead by the liberalization plan? Why? Exactly how much richer or poorer will the company be if it relaxes its credit policy?

Q5 a) Define the following terms

i. Stop Loss ii. Limit Order iii. Short sell iv. Blue chip stock v. Margin Financing

b) Thomas brother is expected to pay a $0.50 per share dividend at the end of the year. The dividend is expected to grow at a constant rate of 7 percent a year. The required rate of return on the stock is 15 percent. What is the stock value per share?

Q6 a) The Allied Company's current EPS is $ 6.50 It was $ 4.42, 5 years ago. The company pays out 40 percent of its earnings as dividends and the stock sells for $ 36.

i) Calculate the past growth rate in earnings.
ii) Calculate the next expected dividend per share
iii) What is the cost of equity?

b) Johnson Iron works raised $ 1 Billion of new capital from the following sources. Calculate the WACC for this increment of funding.

$ 500 Million from bonds with after tax cost of capital of 7%.
$ 200 Million from an issue of preferred stock with cost15%
$ 200 Million from retained earning which costs 20%
$ 100 Million from new common stock which cost 21%

END OF EXAM PAPER