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**CRAWFORD UNIVERSITY
FAITH CITY, IGBESA
DEPARTMENT OF ECONOMICS ACCOUNTING AND FINANCE
RAIN SEMESTER EXAMINATION 2010/2011 SESSION**

COURSE TITLE: BUSINESS FINANCE II COURSE CODE: FIN 302

TIME ALLOWED: 2 Hours INSTRUCTION: Attempt Any THREE Questions

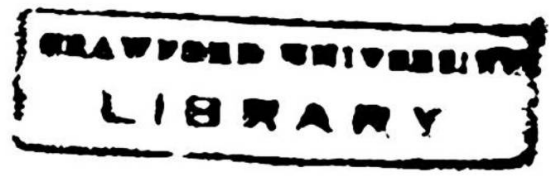
1 (a) What do you understand by financial ratios and how can they be broadly classified?

(3 marks)

(b)

**TOO GOOD NIGERIA PLC.
Balance Sheet As At 31st December 2003**

	N'000	N000	N'000
Assets			
Goodwill			35,000
Plant and Machinery		250,000	
Less Accumulated Depreciation		<u>62,500</u>	187,500
Current Assets			
Stock	37,500		
Debtors	25,000		
Prepaid Expenses	6,250		
Marketable Securities	18,750		
Cash	<u>6,250</u>	93,750	
Less Current Liabilities			
Bank Overdraft	15,000		
Bills Payable	5,000		
Accrued Expenses	5,000		
Provision for Tax	<u>16,250</u>	<u>41,250</u>	
			<u>52,500</u>
			<u>275,000</u>
Financed by			
Ordinary Share Capital (N10 per share)			87,500
8% Preference Share Capital			50,000
Reserves and Surplus			50,000
6% Long Term Loan		25,000	
7% Debentures		<u>62,500</u>	
			<u>87,500</u>
			<u>275,000</u>



TOO GOOD NIGERIA PLC

Trading, Profit and Loss Account for the Year Ended 31st December, 2003.

	N'000	N'000
Sales:		
Cash	75,000	
Credit	<u>300,000</u>	375,000
Opening Stock	43,750	
Add Purchases (Credit)	<u>268,750</u>	
	312,500	
Less Closing Stock	<u>37,500</u>	
Cost of Goods Sold		<u>275,000</u>
Gross Profit		100,000
Less Admin Expenses	8,750	
Selling Expenses	6,250	
Depreciation	<u>12,500</u>	
		<u>27,500</u>
Operating Profit		72,500
Less Interest		<u>5,750</u>
		66,750
Add Other Income		2,250
Profit Before Taxation		69,000
Income Tax		31,500
Profit After Taxation		37,500
Less Dividends: Preference Shares	4,000	
Ordinary Shares	<u>13,125</u>	
		<u>17,125</u>
Retained Profit for the Year		20,375
Add Profit from Previous Year		<u>29,625</u>
Balance Carried to Balance Sheet		<u><u>50,000</u></u>

Given that TOO GOOD NIGERIA PLC belongs to the Pharmaceutical Industry and the Industry average is as shown below

Ratio	Industry Average
Acid Test	1.0
Inventory Turnover	5 times
Gearing Ratio	60%
Return on Capital Employed	25%
Net Profit Margin	20%
Earnings Per Share	N3.00
Dividend Per Share	N1.50
Earnings Yield	25%
Dividend Yield	15%
Price Earnings Ratio	2.0



Required: Calculate the ratios above for TOO GOOD NIGERIA PLC and comment on each of your results vis-a-vis the industry average. (20marks)

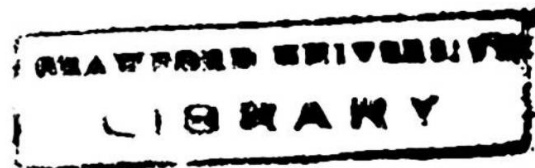
2 (a) Make a distinction between each of the following :

(i). General Inflation and Specific Inflation (2marks)

(ii). Money Cash Flow and Real Cash Flow. (2marks)

(b) A company is considering a project that has the following cash flow estimates which are expressed in constant price level terms

Year	Cash flow
0	300,000
1	250,000
2	180,000
3	150,000
4	120,000
5	80,000



If the money cost of capital is 22% and the real cost of capital is 17%, calculate the NPV of the project. (4marks)

(c) Investors in XYZ Ltd currently require a nominal return of 20% on their investment. What is the real rate of return if inflation is currently at 4% per annum? (4 marks)

(d) Apson Ltd wishes to embark on a project costing ₦1,000,000 with an estimated useful life of 4 years and residual value of ₦80,000. The annual revenue from the project is expected to be ₦70,000 in year 1, rising by 7% p.a. for inflation. Running costs are expected to be ₦300,000 in year 1 but would increase by 12% p.a. because of inflating labour costs. The company's money cost of capital is 20%. Advise whether the project should be accepted or not by the company. (11 marks)

3 (a) K K Ventures has a capital structure consisting of ₦50,000, 15% debenture and 100,000 ₦1 ordinary shares. The ordinary shares are currently valued at 83 kobo and the debenture at ₦88. Annual dividends of 15 kobo have been stable over the years and dividend has just been paid. The interest on debenture is due for payment. Calculate the cost of equity and the cost of debt for the venture. (4marks)

(b) The current capital structure of ABC Ltd is as follows:

	N'000
Ordinary Shares (6m shares of N1 each)	6,000
Reserves	9,000
15% Debenture	2,800
16% Preference Shares (N1 per value)	2,500

The current market price per share is N2.27 cum div. An annual dividend of N1.62m is due for payment shortly. The summary of dividends since the last 5 years (including proposed dividends) is as follows.

Year	N'000
1	1240
2	1300
3	1420
4	1500
5	1620

The debentures which are currently selling at N84 are redeemable in 5 years time. Annual interest has just been paid on the debentures. The preference shares are irredeemable and are currently at N1.80 per share. Preference dividends have just been paid. The current rate of corporation tax is 48%. Estimate the company's overall cost of capital?

(19marks)

4(a) Distinguish between each of the following

(i) Risk and Uncertainty

(ii) Risk Free Rate and Risk Adjusted Discount Rate

(iii) Risk Aversion and Risk Indifference

(6marks)

(b) A project costing N300,000 has an estimated cash flows and probability distributions as given below:

Year 1		Year 2		Year 3	
Cash Flow	Probability	Cash Flow	Probability	Cash Flow	Probability
N		N		N	
140,000	0.25	120,000	0.20	100,000	0.15
170,000	0.30	160,000	0.35	160,000	0.35
180,000	0.35	200,000	0.15	190,000	0.25
200,000	0.10	240,000	0.30	220,000	0.25

If the risk-free rate is 13% and the risk-adjusted rate of the company is 17%, calculate the expected NPV of the project.

(6 marks)



- (c) The following are the possible cash flows of projects A and B and their associated probabilities.

A			B		
Event	Cash Flow	Probability	Event	Cash Flow	Probability
1	80,000	0.10	1	240,000	0.10
2	100,000	0.20	2	200,000	0.15
3	120,000	0.40	3	160,000	0.50
4	140,000	0.20	4	120,000	0.15
5	160,000	0.10	5	80,000	0.10

Which of the two projects is riskier? (11 marks)

- 5 (a) A company wants to raise ₦6m for a new factory and the factory is expected to yield an annual EBIT of ₦1.2m. The Managing Director of the company is considering the following options.

- Issuing 300,000 common shares of ₦10 each with 18% preference share capital of ₦1.2million and 16% debenture of ₦1.8 million.
 - Issuing 360,000 common shares of ₦10 each and 16% debenture of ₦2.4 million.
 - Issuing 600,000 common shares of ₦10 each
- (Assume a corporation tax of 40%)

Required (i) Using both the table and the formula, calculate the earnings per share for each of the three options (12marks)

(ii) Which of the options will you recommend for the company and why? (2mark)

(ii) Calculate the degree of financial leverage for the appropriate option (4marks)

- (b) Bako Nig. Ltd has a fixed cost of ₦240,000 in producing 150,000 bottles of malt drink. Bako sells a bottle for ₦9 but incurs a variable cost of ₦5 per bottle of the drink. The company's capital structure is made up of ₦800,000 equity shares and ₦800,000 18% debenture. Calculate the company's operating, and financial leverage. (5 marks)

