

UNIVERSITY OF SWAZILAND
DEPARTMENT OF ACCOUNTING
MAIN EXAMINATION PAPER 2011

- COURSE TITLE** : PRINCIPLES OF FINANCE AND BANKING
- COURSE CODE** : AC303/IDE- AC 303
- DEGREE/DIPLOMA** : DIPLOMA IN COMMERCE III
- TIME ALLOWED** : THREE (3) HOURS
- INSTRUCTIONS** :
1. TOTAL NUMBER OF QUESTIONS ON THE PAPER: FOUR (4)
 2. ATTEMPT ALL FOUR (4) QUESTIONS
 3. THE MARKS AWARDED FOR A QUESTION ARE INDICATED AT THE END OF EACH QUESTION
 4. WHERE APPLICABLE, ALL WORKINGS ARE TO BE SHOWN
 5. CALCULATIONS ARE TO BE MADE TO TWO DECIMAL PLACES OF ACCURACY, UNLESS OTHERWISE INSTRUCTED.
- SPECIAL REQUIREMENTS** : NONE
- NOTE** : YOU ARE REMINDED THAT IN ASSESSING YOUR WORK, ACCOUNT WILL BE TAKEN OF THE ACCURACY OF LANGUAGE, THE GENERAL QUALITY OF EXPRESSION, TOGETHER WITH THE LAYOUT AND PRESENTATION OF YOUR FINAL ANSWER

THIS QUESTION PAPER SHOULD NOT BE OPENED UNTIL PERMISSION HAS BEEN GRANTED BY THE INVIGILATOR.

QUESTION 1

(a) Achieving financial objectives of any firm or company generally involves taking decisions in three (3) key areas.

Briefly discuss these three areas. (10 marks)

(b) Within a Financial Management Context, discuss the inherent conflicts of interests which may exist between the following:

(i) Employees and shareholders (3 Marks)

(ii) Shareholders and Lending Financial Institutions and other Finance Providers (3 Marks)

(iii) Shareholders and Managers (3 Marks)

(9 Marks)

(c) Busi LTD offers standard credit terms of 60 days net. Its cost of short term borrowing is 16% p.a. You are required to determine whether a 2.5% discount should be offered for payment within 7 days to customers who would normally pay after:

(i) 60 days (2 Marks)

(ii) 80 days (2 Marks)

(iii) 105 days (2 Marks)

Total: (25 Marks)

QUESTION 2

Mbanjwa is a medium-sized company that manufactures luxury goods for several well-known chain stores. In real terms, the company has experienced only a small growth in turnover in recent years, but it has managed to maintain a constant, if low, level of reported profits by careful control of costs. It has paid a constant nominal (money terms) dividend for several years and its managing director has publicly stated that the primary objective of the company is to increase the wealth of shareholders. Mbanjwa is financed as follows:

	Em
Overdraft	12
10 year fixed interest bank loan	24
Share capital and reserves	<u>54</u>
	<u>90.0</u>

Mbanjwa has the agreement of its existing shareholders to make a new issue of shares on the stock market but has been informed by its bank that current circumstances are unsuitable. The bank has stated that if new shares were to be issued now they would be significantly under-priced by the stock market, causing Mbanjwa to issue many more shares than necessary in order to raise the amount of finance it requires. The bank recommends that the company waits for at least six months before issuing new shares, by which time it expects the stock market to have become strong-form efficient.

The financial press has reported that it expects the Central Bank to make a substantial increase in interest rate in the near future in response to rapidly increasing consumer demand and a sharp rise in inflation. The financial press has also reported that the rapid increase in consumer demand has been associated with an increase in consumer credit to record levels.

Required:

- (a) Discuss the meaning and significance of the different forms of market efficiency and comment on the recommendation of the bank that Mbanjwa waits for six months before issuing new shares on the stock market.

(10 Marks)

- (b) On the assumption that the Central Bank makes a substantial interest rate increase, discuss the possible consequences for Mbanjwa in the following areas:

- (i) Sales
- (ii) Operating costs, and
- (iii) Earnings (profit after tax)

(15 Marks)

Total (25 Marks)

QUESTION 3

The following are summary financial statements for Dladla LTD

	2006	2011
	E000	E000
Non-current Assets	115	410
Current Assets	650	1000
Current Liabilities	513	982
Non-Current Liabilities	42	158
Capital and Reserves	210	270

	2006	2011
	E000	E000
Sales	1,200	3,010
Cost of sales, expenses and interest	1,102	2,860
Profit before tax	98	150
Tax and distributions	33	133
Retained earnings	65	17

Notes

Cost of sales was E530,000 for 2006 and E 1,330.000 for 2011

Debtors are 50% of current assets and trade creditors are 25% of current liabilities for both years.

Required:

You are a consultant advising Dladla LTD. Using suitable financial ratios, and paying particular attention to growth and liquidity, write a report on the significant changes faced by the company since 2006. The report should also comment on the capacity of the company to continue trading, together with any other factors considered appropriate

An appendix to the report should be used to outline calculations

Total (25 Marks)

QUESTION 4

- (a) An exporter in UK has invoiced a customer in the USA the sum of \$300,000 receivable in one year's time..
He has under consideration two methods of hedging his exchange risk.
 - (i) He could borrow \$300,000 now for one year, convert the amount into sterling, and repay the loan out of the eventual receipts.
 - (ii) He could enter into a 12-month forward exchange contract to sell the \$300,000 and meanwhile borrow equivalent amount in sterling.

The sterling – US dollar spot rate is 1.8190 – 1.8402.

The 12 months forward rate of dollars against sterling is 1.7915.

Interest rates for 12 months are USA 6.65%, UK 9.25%.

Required

Using part (b) above, calculate the net proceeds in sterling under each alternative and to explain the result you obtain.

(8 Marks)

(b) You are given the following information about currency rates for sterling spot and forward.

	Spot	One Month Forward	Three Months Forward
US (dollar)	1,5200 – 1,5210	032 -027c pm	0.89 – 0.84pm
Canada (dollar)	1,8630 – 18640	030 -0.20c pm	0.90 – 0.80pm
Netherlands (guilder)	4.05¼ - 4.06¼	2¾ - 1 7/8c pm	6 ¾ - 6 ¼pm
Blgium (franc)	72.20 – 72.30	10 – 20c disc	45 -55 dis
Denmark (krone)	13.01 -13.02	44 – 5 5/8 ore dis	18¾ -19¾ dis
Germany (DM)	3.06½ - 3.07 ½	2 - 1½ pf pm	5½-5 pm

Calculate the cost or value in sterling to a customer who wishes to:

- (a) Buy US\$14,000 one month forward from his bank
- (b) Buy Canadian \$25,000 spot
- (c) Buy Belgian francs 75,000 three months forward
- (d) Sell guilders 28, 000 one month forward
- (e) Sell Danish kroner 20,000 three months forward
- (f) Sell DM 6,000 one month forwards.

(9 Marks)

- (c) Discuss any five factors which influence foreign exchange rates for a currency

(8 Marks)

Total (25 Marks)