University of Swaziland
Department of Accounting
Supplementary Exam Paper - Semester - I

Programme of Study	:	Bachelor of Commerce
Year of Study	:	Year Three / Four
Title of Paper	:	Intermediate Business Finance
Course Code	:	AC 322/415
Time Allowed	:	**3 Hours.**

Instructions:

1. Total number of questions on this paper is four (4).

2. Answer all the questions.

3. The marks awarded for a question / part is indicated at the end of each question / part of question.

4. Where applicable, submit all workings and calculations on the answer sheet alongside the case.

5. Calculations are to be made to two decimal places of accuracy unless otherwise instructed.

Note: You are reminded that in assessing your work, account will be taken of accuracy of the language and the general quality of expression, together with the layout and presentation of your final answer.

Special requirement : Calculator and P V tables

This paper is not to be opened until permission has been granted by the invigilator.

QUESTION 1:

a. Mr. Sipho is evaluating two possible portfolios, each of which consists of five assets held in portfolio A and portfolio B. For the purposes of evaluation, he wants to use beta co-efficient to compare the risks of the portfolios. So, he gathered the data shown in the following table.

Asset	Asset Beta	Portfolio weights	
		Portfolio A	Portfolio B
1	1.2	15	25
2	0.75	25	15
3	1.30	10	20
4	1.10	20	20
5	0.80	30	20
		100%	100%

Required:

i) Calculate the beta co-efficient for portfolios A & B **(10 marks)**

ii) Compare the risk of these portfolios to the market as well as to each other. Also, compare the riskiness of each portfolio. **(5 marks)**

b. Swazi Agribusiness has E 600,000 in invested capital, 60 percent of which is in the form of debt. With this capital structure, the company's average cost of funds is 10 percent. According to Swazi Agribusiness's latest income statement, the firm's operating income is E 150,000 and its marginal tax rate is 30 percent.

Required:
According to EVA approach, is Swazi Agribusiness a good company in which to invest? **(5 marks)**

c. You are considering the purchase of SSA Corporation's bond that was issued 2 years ago. SSA's bond has 9.5 percent annual coupon and a 30 year original maturity. Interest rates have since declined, and the bond is currently selling for E 1,265.62. Its face value is E 1,000.

Required:
i) What is the YTM of SSA Corporation now? **(7 marks)**

ii) Would you buy the bond if your required rate of return is 9 percent? **(1 marks)**

Total (28 marks)

QUESTION 2:

Write short notes on the following:

a. Commercial paper **(5 marks)**
b. The determinants of market interest rates **(10 marks)**
c. Expectations theory **(5 marks)**
d. Working capital financing strategies. **(5 marks)**

Total (25 marks)

QUESTION 3:

a. Kangroo Inc., paid a common dividend of E 1.50 per share last year. The company expects its earnings and dividends to grow at a rate of 6 percent per year for the foreseeable future.

Required:
i) If Kangroo's stock is selling at a price of E 30 what will be the current yield that you expect from this stock?
ii) What portion of this yield is dividend yield and capital gains yield?

(7 marks)

b. Assume that the real risk-free rate is 5 percent and the maturity risk premium is zero. If the nominal rate of interest on one-year bonds is 12 percent, and on comparable risk two-year bonds it is 14 percent, what is the one-year interest rate that is expected for Year 2? What inflation rate is expected during Year 2?

(7 marks)

c. You have recently been hired to improve the performance of Multiplex Corporation which has been experiencing a severe cash shortage. As part of your analysis, you want to determine the firm's cash conversion cycle. Using the following information and a 360-day year, what is your estimate of the firm's current cash conversion cycle?

Current inventory = E 120,000
Annual sales = E 600,000
Accounts receivable = E 160,000
Accounts payable = E 25,000
Total annual purchases = E 360,000
Purchases credit terms: net 30 days
Receivables credit terms: net 50 days

(8 marks)

Total (22 marks)

QUESTION 4:

Savelots Stores' current financial statements are shown below:

Inventories	E 500	Accounts payable	E 100
Other current assets	400	Short-term notes payable	370
Fixed assets	370	Common equity	800
Total assets	E1,270	Total liab. and equity	E1,270

Sales	E2,000
Operating costs	1,843
EBIT	157
Less: Interest	37
EBT	120
Less: Taxes (40%)	48
Net income	72

A recently released report indicates that Savelots' current ratio of 1.9 is in line with the industry average. However, its accounts payable, which have no interest cost and which are due entirely to purchases of inventories, amount to only 20% of inventory versus an industry average of 60%. Suppose Savelots took actions to increase its accounts payable to inventories ratio to the 60% industry average, but it (1) kept all of its assets at their present levels (that is, the asset side of the balance sheet remains constant) and (2) also held its current ratio constant at 1.9. Assume that Savelots' tax rate is 40%, that its cost of short-term debt is 10%, and that the change in payments will not affect operations. In addition, common equity would not change. With the changes, what would be Savelots' new ROE?

(25 marks)

End of Question Paper