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UNIVERSITY OF SWAZILAND

DEPARTMENT OF ACCOUNTING AND FINANCE

EXAMINATION PAPER MAY 2019 ACADEMIC YEAR 2018/2019

PROGRAMME OF STUDY	**Bachelor of Commerce**
YEAR OF STUDY	**Year 4 (Full/Part Time)**
TITLE OF THE PAPER	**Advanced Business Finance**
COURSE CODE	**ACF418/AC 428 /AC 513**
TIME ALLOWED	**Three (3) Hours**

INSTRUCTIONS

1. There are Four (4) questions, ANSWER ALL.
2. Begin the solution to each question on a new page.
3. The marks awarded for a question are indicated at the end of each question.
4. Show your necessary workings.

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 layout and presentation of your answer.

THIS PAPER IS NOT TO BE OPENED UNTIL PERMISSION HAS BEEN GRANTED BY THE INVIGILATOR / SUPERVISOR.

QUESTION ONE

A. A Swazi importer buys merchandise amounting to $ 100 000 from an American supplier. The supplier grants the buyer three months' credit from delivery date, which is 15 September. The spot rate on 15 September is $1 = R 11.20. The forward 3 Monthly dollar premium is 7% (annualized). The importer does not want to speculate in foreign exchange, and therefore wishes to fix the future liability in terms of Rands. Given this information;

i. What instrument could the buyer use to hedge their position. **(1 mark)**

ii. How much will this instrument guarantee the buyer to pay in Rands three months later. **(3 Marks)**

iii. If the importer decided not to utilize the instrument above, and the rand traded at R11.8 to the dollar when payment is due, What would be the cost of this choice in rand terms. **(3 marks)**

B. SMI, a Swazi company exports meat products to the USA. The company has delivered an order for $500 000. Payment is due on 10 March 2019. The current exchange rate on 10 December 2018 is R11.1640/$ and the rand is expected to trade at a 5% 3-month forward premium to the US dollar. The local and foreign interest rates are as follows:

- New York interest rate: 6.0% per annum
- Swazi interest rate: 10% per annum

The Finance manager over hears you talking about a money market hedge and becomes interested. She shares with you the information above and asks you to explain how she can execute this money market hedge. In your explanation;

i. Illustrate to her how much she should borrow, where and for how long. **(4 marks)**

ii. What should she do with the borrowed amount and how much in rands will that strategy yield for SMI on 19 March 2019. **(4 Marks)**

iii. If interest rate parity holds, how much is the gain/loss expected in rand terms. **(5 Marks)**

iv. What is the Gain/Loss on export sale proceeds in the absence of the hedge if parity holds. **(3 Marks)**

v. What is the Net Gain/Loss from taking the hedge if parity holds. **(2 Marks)**

(Total Marks 25)

QUESTION TWO

A. Manqoba Magagula Corporation is an American firm manufacturing natural fertilizer used for growing organic vegetables. Its export business has risen to the point that it is considering establishing a manufacturing operation in Swaziland.

Suppose Manqoba's Swaziland facility is expected to generate the following cash flows in Swazi Emalangeni (E):

Year:	0	1	2	3	4	5
Cash flow (millions of emalangeni)	-22.8	6.0	7.5	9.0	10.5	12.0

The interest rate in the United States is 3 percent. Manqoba's financial manager estimates that the company requires an additional expected return of 8 percent to compensate for the risk of the project.

The financial manager looks in the newspaper and finds that the current exchange rate is 9.49 lilangeni to the dollar ($s_{L/D}$ = 9.49), while the interest rate is 3 percent in the United States (r_D = 0.03) and 9 percent in Swaziland (r_L= 0.09).

Required

a. Calculate the NPV of Manqoba Corporation's project. **(21 marks)**

b. Should they pursue the project? **(2 marks)**

c. Would you be able to buy more or less emalangeni in the forward market than in the spot market? **(2 marks)**

Total marks: 25)

QUESTION THREE

Company A is considering merging with X. The following data has been collected:

	A	X
Earnings after interest and taxes	1,500,000	600,000
Earnings before interest and taxes	2,000,000	1,000,000
Number of shares	3,000,000	2,000,000
Dividends Paid	750,000	300,000
Shares are currently trading at	250cents	150cents

Company A and X have similar growth rate of five percent. After the merger the growth rate is expected to be 10 percent. The payout ratio will is 50%.

Required:

Calculate the

(a) Value of A **7 Marks**

(b) Value of X **3 Marks**

(c) The total value of the two firms. **3 Marks**

(d) The value of the merged firm, assuming that company A made a cash payment **7 Marks**

(e) Should company A merge with company X? why or why not? **5 Marks**

(Total Marks 25)

QUESTION FOUR

a) Briefly discuss three key characteristics each of an Operating lease and a Financial lease **(6 Marks)**

b) List and briefly explain six advantages of leasing **(12 Marks)**

c) Briefly explain how a sale and lease-back works and when it can be used **(7 marks)**

(Total Marks 25)

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