

UNIVERSITY OF ESWATINI
DEPARTMENT OF ACCOUNTING AND FINANCE
SUPPLEMENTARY EXAMINATION PAPER NOVEMBER 2019
ACADEMIC YEAR 2019/2020

PROGRAMME OF STUDY	:	Bachelor of Commerce
YEAR OF STUDY	:	Year 4 (Full Time/Part Time)
TITLE OF THE PAPER	:	Corporate Finance II
COURSE CODE	:	ACF 417/AC 426/ AC 514
TOTAL MARKS	:	100 Marks
TIME ALLOWED	:	Three (3) Hours

INSTRUCTIONS

1. There are **FIVE (5)** questions of 25 marks each, **ANSWER ANY FOUR (4) QUESTIONS.**
2. This paper consists of seven (7) numbered pages, including this page and Appendix 1 which contains useful formulae.
3. Begin the solution to each question on a new page.
4. The marks awarded for a question are indicated at the end of each question.
5. Show your necessary workings.
6. Round off all prices to the nearest cent, values to the nearest lilangeni, interest factors and decimalized interest rates to four decimal places, and decimalized weightings to four decimals.

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

(25 Marks)

- 1.1 You are given the following information about Epson Power Limited by their Group Financial Analyst, Mr F. Zulu.

Risk free rate of return	10%
Required rate of return on the market	15%
Beta Coefficient	1.5
Expected Dividend for the coming year (D1)	E2.50
'g' – growth rate (constant)	5%

Required:

- 1.1.1 Compute the required rate of return on the equity according to the Capital Asset Pricing Model (CAPM). (5 Marks)
- 1.1.2 Calculate the present market price of the equity share. (5 Marks)
- 1.2 Briefly discuss **ANY FIVE (5)** uses of Capital Asset Pricing Model. (5 Marks)
- 1.3 Discuss fully **ANY FIVE (5)** limitations of the Capital Asset Pricing Model. (10 Marks)

QUESTION TWO

(25 Marks)

The directors of Thiang Limited have appointed you as their financial consultant. They are considering new investment projects and need you to calculate the cost of capital for the company.

The present capital structure is as follows:

2 000 000 ordinary shares with a par value of 75 cents per share. These shares are currently trading at E4.50 per share and the latest dividend paid is 30 cents. An average dividend growth of 13% is maintained.

500 000 14% E3.00 preference shares, with a market value of E5.00 per share

R1 200 000 8% debentures with a face value of E100.00 and current quote of E120.00, due in 6 years' time. The current yield to maturity is 6%.

Additional Information:

- The company has a beta of 1.7, risk free rate of 5% and the market risk premium is 8%.
- The company's tax rate is 30%.

Required:

- 2.1 Calculate the weighted average cost of capital, using the Gordon Growth Model to calculate the cost of equity. (12 Marks)
- 2.2 Calculate the cost of equity using the Capital Asset Pricing Model (CAPM). (5 Marks)
- 2.3 Discuss **ANY FIVE (5)** risks associated with investing in bonds. (10 Marks)
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QUESTION THREE

(25 Marks)

The Board of Directors of Triple H is comparing two different capital structures: an all-equity plan and a levered plan. Under the all-equity plan, Triple H would have 10 000 000 shares in issue. Under the levered plan, there would be 5 000 000 shares and 10% perpetual debt worth R200 million. The tax rate is 25%.

- 3.1 Calculate the break-even profit before interest and tax (PBIT) and the earnings per share (EPS) for Triple H. (10 Marks)
- 3.2 Discuss **ANY FIVE (5)** assumptions of the Modigliani and Miller theories of capital structure and also compare and contrast Modigliani and Miller (M & M) Proposition II with and without taxes with the aid of fully labelled diagrams. (15 Marks)
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QUESTION FOUR

(25 Marks)

- 4.1 Zhing Park Explosives Limited has been growing at a phenomenal rate of 15% because of its rapid expansion and explosive sales. You believe this growth rate will last for two more years and then drop to 5% per year. If the growth rate then remains at 5% indefinitely, what is the value per share? Total dividends just paid for the past year were E2,500,000.00, and the required return is 10%. There are 10,000,000 shares in issue. (10 Marks)
- 4.2 A bond was issued 15 years ago with a par value of E100 and offering a coupon of 11% annually. The bond will be redeemed in three years' time and is currently trading at E109.50. What rate of return is this bond offering investors in the secondary market? (5 Marks)
- 4.3 Suppose Rosebank Ltd, a company based in the Kingdom of Eswatini, has just issued a dividend of E1.22 per share on its common stock. The company paid dividends of E0.78, E0.91, E0.93, and E1.00 per share in the last four years. If the stock currently sells for E52, what is the best estimate of the company's cost of equity capital using: