UNIVERSITY OF ESWATINI

DEPARTMENT OF ECONOMICS

MAIN EXAMINATION DECEMBER 2018

PAPER TITLE : CORPORATE FINANCE I

COURSE CODE : ECO 427

INSTRUCTIONS:

1. ANSWER THREE QUESTIONS.
2. QUESTION ONE IS COMPULSORY.
3. TIME ALLOWED: TWO (2) HOURS

REQUIREMENTS

1. SCIENTIFIC CALCULATORS

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QUESTION 1 (COMPULSORY)

a) Define finance and state why it is important for financial managers to understand economics. [4]

b) Describe the major differences among three primary forms of business organization (a proprietorship, a partnership and a corporation). [6]

c) Accounting information is required by various individuals and organizations in order to make decisions. Explain why each of the following user groups need accounting information relating to a business. [10]

   i. Customers
   ii. Government
   iii. Lenders
   iv. Employees
   v. Investment analysts

d) Pixma Limited began operations in January 2009 with E900 000 obtained from selling 450 000 ordinary shares at an issue price of E2 each. Some of the major transactions for the year included the following:

It purchased plant and equipment for E750 000 as well as land and buildings for E450 000, financing the purchase with a mortgage bond of E287 500, a long-term loan of E595 000, and cash for the balance. During the year the company used cash to reduce the mortgage bond balance by E25 000 and to repay E75 000 towards the long-term loan.

The company also invested E195 000 in short-term marketable securities. On 01 October 2009, the company issued a further 200 000 shares at E3 each. Depreciation expense for the year was E200 000. The Profit after tax for the year ended 31 December 2009 was E250 000. Dividends for the year (declared and paid) amounted to E220 000.

REQUIRED

From the information provided above, calculate the amount that should be reflected for each of the following items in the Statement of Financial Position of Pixma Limited at the financial year end 31 December 2009:

i.	Non-current assets	[3]
ii.	Retained earnings	[3]
iii.	Total Equity	[3]
iv.	Non-current liabilities	[3]

e) Name 2 control measures that you would recommend to prevent the following situations from occurring at Pixma Limited: (that is, two measures for each).

i.	Payments made without proper authorization	[4]
ii.	Theft of stock from the warehouse	[4]

QUESTION 2

Excerpts of financial data for Polar Enterprises are as follows:

Statement of Comprehensive Income	**2010 (E)**	**2009 (E)**
Sales (10% credit)	32 011 500	19 373 000
Cost of sales (10% credit purchases)	26 180 100	15 993 700
Operating profit	1 931 200	1 327 800
Profit before tax	1 831 400	1 226 420
Tax (25%)	457 850	306 600
Profit after tax	1 373 550	919 820

Statement of Financial Position	**2010**	**2009**
Non-current assets	5 200 000	4 700 000
Current assets	2 866 530	4 974 530
Inventories	1 482 200	2 038 860
Accounts receivable	261 290	155 200
Marketable securities	326 950	2 306 440
Cash	796 090	474 030
Current liabilities	1 088 860	588 310
Accounts payable	190 660	192 040
Other current liabilities	898 200	396 270

Required

a) Calculate the gross margin, operating margin and profit margin for 2010 and 2009 and comment on your findings. [9]

b) Calculate the current ratio and acid test ratio at the end of each year. How has the enterprise's liquidity changed over this period? [4]

c) Compute the following for 2010 and give interpretations of the enterprise's performance with respect to your answers (ratios for 2009 are given in brackets):

i. Inventory turnover (2009: 9.04 times) [3]

ii. Debtors collection period (2009: 29.24 days) [3]

iii. Creditors payment period (2009: 42.40 days) [3]

iv. Turnover to net assets (2009: 2.13) [3]

QUESTION 3

a) Your company has the option to invest in machinery in projects F and G but finance is only available to invest in one of them. You are given the following projected data:

	Project F (E)	Project G (E)
Initial cost	140 000	150 000
Net cash inflows:		
Year 1	30 000	40 000
Year 2	36 000	50 000
Year 3	40 000	50 000
Year 4	44 000	80 000
Year 5	26 000	0

Additional information

- All cash flows take place at the end of the year except the original investment in the project which takes place at the beginning of the project.
- Project F machinery will be disposed of at the end of year 5 with a scrap value of E20 000.
- Project G machinery will be disposed of at the end of year 4 with a nil scrap value.
- Depreciation is calculated on a straight line basis.
- The discount rate to be used by the company is 14%.

Required

i. Calculate the payback period for project F. (Answer must be expressed in years and months) [3]

ii. Calculate the accounting rate of return for project F. (Answer expressed to 2 decimal places) [10]

iii. Calculate the net present value of each project. (Round off amounts to the nearest Rand) [8]

b) A machine with a purchase price of E140 000 is estimated to eliminate manual operations by E40 000 per year. The machine will last 5 years and have no residual value at the end of its life. Calculate the internal rate of return. [4]

QUESTION 4

a) If Samantha invest E700 today in an account that pays 4% interest compounded annually, how much will she have in her account four years from today? [3]

b) Suppose that you invest E385 at the end of the each of the eight years.

  i. If your opportunity cost rate is 7 percent compounded annually, how much will your investment be worth after the last E385 payment made? [3]

  ii. What will be the ending amount if the payments are made at the beginning of each year? [3]

c) Define what an amortized loan is and why amortization schedules are important. [5]

d) Prepare an amortization schedule for a E33, 000, 6.5 percent loan that requires three equal annual payments of E12, 460 per year. [6]

e) "A director is a steward of the company. The ethics of governance requires that in this stewardship role, each director be faithful to the four basic ethical values of good corporate governance (responsibility, accountability, fairness and transparency). In performing their stewardship role directors need to exercise the following five moral duties: conscience, care, competence, commitment and courage." Explain what is meant by each of these five moral duties. [5]