



UNIVERSITY OF ESWATINI

SECOND SEMESTER MAIN EXAMINATION PAPER, AUGUST 2020

FACULTY OF SOCIAL SCIENCES

DEPARTMENT OF ECONOMICS

COURSE CODE: ECO428

CORPORATE FINANCE II

TIME ALLOWED: 2 HOURS

Instructions

1. This paper consists of Section (A) and (B);
2. Section A is compulsory and carries 40 marks;
3. Answer any two (2) questions from Section B.
4. All questions in Section B carry equal marks of 30 each

Special Requirements

1. Scientific Calculator

Additional Material (s)

None

Candidates may complete the front cover of their answer book when instructed by the Chief Invigilator and sign their examination attendance cards but must NOT write anything else until the start of the examination period is announced.

No electronic devices capable of storing and retrieving text, including electronic dictionaries and any form of foreign material may be used while in the examination room.

DO NOT turn examination paper over until instructed to do so

SECTION A

Question 1 [Compulsory and Carries 40 Marks]

a) Write short notes on the following:

[3 Marks each]

- i. Capital Asset Pricing Model
- ii. Real Options
- iii. Capital Budgeting
- iv. Treasury Bill

b) Define what beta (β) is in finance and interpret its different coefficients [12]

c) Earlier today, Stuart sold 200 shares of stock he owned. He purchased the stock three years ago for E28 per share. Following is a table that shows the market value of the stock at the end of each year and the amount of the dividend that Stuart received during the year:

Year	Market Value (per share)	Dividend (per share)
1	E26	E0.60
2	E28	E0.60
3	E32	E0.60

- i) What total return (yield) did Stuart earn during the three –year period he held the stock? [4]
- ii) What return did Stuart earn each year he held the stock? [9]
- iii) Stock A has an expected rate of return of 15%. Today's expected return on the market portfolio is 10%. The current risk free interest rate is 7.5%. What is the beta of stock A? [3]

SECTION B (ANSWER ANY TWO QUESTIONS)

QUESTION 2

[30 Marks]

- a) Consider the following information about two stocks where the probability of an economic boom is 40%.

Economic State	Return A (R_A)	Return B (R_B)
Boom	38%	6%
Recession	-4%	12%

- i. Calculate the expected return for stock A and stock B. [4]
 - ii. Calculate the standard deviation of stock A and stock B. [6]
 - iii. Calculate the correlation between stock A and stock B. [4]
 - iv. Calculate the expected return on a portfolio with equal proportions in the risky assets, and 30% in a risk-free asset. [4]
- b) The overall performance of your portfolio is the ultimate measure of success for your portfolio manager. Discuss any four metrics that can be used to rate your portfolio manager. [12]

QUESTION 3

[30 Marks]

- a) Express Surgery Canter's (ESC) preferred stock, which has a par value equal to E110 per share, pays an annual dividend equal to 9% of the par value. If investors require a 15 % return to purchase ESC's preferred stock, what is the stock's market value? [5]
- b) Construct an NPV profile for a capital budgeting project that costs E64, 000 and is expected to generate E18, 200 per year for five years. Using the NPV profile, determine the project's internal rate of return (IRR) and its net present value (NPV) at required rates of return equal to 10%, 13%, and 15%. [10]
- c) Giving examples, discuss the three main categories of mergers. [15]

QUESTION 4

[30 Marks]

- a) Your broker offers to sell you shares of Wingler & Company common stock, which paid a dividend of \$2 yesterday. You expect the dividend to grow at a rate of 5% per year into perpetuity. If the appropriate rate of return for the stock is 12%, what is the market value of Wingler's stock? [5]
- b) What is the expected return of the following portfolio of investment? [7]

Investment	\hat{r}	Amount Invested
DEF	4%	E30,000
JKL	24	25,000
TUV	14	45,000

- c) Define and discuss four factors that lead to financial distress for a company. [18]