

Mid-West University
Examinations Management Office
Surkhet, Nepal
End-Semester Examination-2081
Bachelor of Business Studies (BBS)
Semester - IV

Subject: Introduction to Finance-II
Full Marks: 60 Pass Marks: 30

Course Code: MGMT 441/341
Time: 3: 00 Hours

You are required to answer in your own words as far as applicable. Figures in the margins indicate full marks.

SECTION A: VERY SHORT ANSWER QUESTIONS (10 X 1 = 10 MARKS)

Answer **ALL** the questions.

1. What is trade credit?
2. How is factoring of receivable different than pledging of receivable?
3. Write the meaning of capital gain yield.
4. What is sinking fund?
5. Write the meaning of return.
6. Assume that the risk-free rate is 12% and the expected return on the market is 17%. What is the required rate of return on a stock that has a beta of 1.25?
7. Define financial leverage.
8. The sales of Siddharth Communication Inc. are Rs 800,000. The variable cost is Rs 300,000 and fixed cost is Rs 250,000. Find the degree of operating leverage.
9. Write the meaning of static tradeoff theory of capital structure.
10. Deuti Electrical Products Company has Rs 5 million in debt outstanding. The corporate income tax rate is 25 percent. What is the tax advantage of Deuti Electrical Products Company for the use of debt under the assumption of corporate income taxes?

SECTION B: SHORT ANSWER QUESTIONS (3 X 8 = 24 MARKS)

Answer any **THREE** questions.

11. Write the meaning of short-term financing. Mention the various types short-term financing and explain any two of them. [2+2+4]
12. What do you mean by common stock? Explain the features of common stock? [3+5]
13. a) Annapurna Watch Company purchases under the term of 4/18 net 50. Compute the percentage cost under each of the following conditions.
 - i. If the company does not take discount and pays on due date. [1.5]
 - ii. If the company does not take discount and pays on 40th day. [1.5]
 - iii. If the company stretches the credit period by 20 days. [1]b) Rara Sports Club Pvt. Ltd. wishes to borrow Rs 1200,000 for one year. It has the following alternatives available to it.
 - i. An 8 percent loan on a discount basis with 25 percent compensating balances required. [1.5]
 - ii. A 10.5 percent loan on a collect basis with no compensating balance requirement. [1.5]Which alternative should the Rara Sports Club Pvt. Ltd. choose if it is concerned with the effective interest rate? [1]
14. Gangamala Bakery Industry's bond has a 12 percent coupon rate and Rs 1,000 face value. Interest is paid semi-annually, and the bond has 8 years to maturity. Currently the bond is selling at Rs 1,130. What is the bond's semi-annual YTM? What is the bond's annual YTM? What is the effective YTM? [6+1+1]

15. Surkhet Garment Company has net operating earnings of Rs 20,000 and Rs 40,000 of debt with 10 percent interest charge. Assume the absence of taxes
- Using the net income approach and an equity capitalization rate of 16 percent, compute the total market value and the implied overall capitalization rate. [2]
 - Assume that the firm issues an additional Rs 40,000 in debt and uses the proceeds to retire the stock, the interest rate and equity capitalization rate remains the same. Compute the new total value of the firm and overall capitalization rate. [2]
 - Using the net operating income approach and overall capitalization rate of 10 percent, compute the total market value, the market value of stock, and the implied equity capitalization rate for the Surkhet Garment Company before and after the sale of additional debt. [4]

SECTION C: LONG ANSWER QUESTIONS (2 X 12 = 24 MARKS)

Answer any **TWO** questions.

16. Define Net Income Approach of capital structure. Mention its assumptions and differentiate between Net Income Approach and Net Operating Income Approach of capital structure. [4+4+5]
17. Panchakanya Steel Company presently has Rs 4.5 million in debt outstanding bearing an interest rate of 8 percent. It wishes to finance Rs 5 million expansion program and is considering three alternatives: additional debt at 10 percent interest, preferred stock with 11 percent dividend, and the sale of common stock at Rs 10 per share. The company presently has 800,000 share of common stock outstanding and is in a 40 percent tax bracket.
- If earnings before interest and taxes are presently Rs 2 million, what would be earnings per share for the three alternatives, assuming no immediate increase in profitability? [6]
 - Determine the indifference point between debt and common stock alternative [7]
18. Following are the probability distribution and rates of return associated with stock X and Y.

Probability	Stock X's Returns, R_x	Stock Y's Return, R_y
0.10	22	(5)
0.30	18	18
0.25	(7)	20
0.35	22	15

- Calculate the expected rate of return and standard deviation of return of stock X and Y. [6]
- What is the covariance and correlation coefficient between return of stock X and Y. [2]
- Calculate portfolio expected return and standard deviation consisting 30 percent fund in stock X and 70 percent fund in stock Y. [5]

THE END