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University of Kelaniya - Sri Lanka

Centre for Distance and Continuing Education

Faculty of Commerce & Management Studies

Bachelor of Business Management (General) Degree Third Examination (External) – 2014/ 2015

July - 2019

BMGT E 3065 – Business Finance

Time: 03 hours

Instructions

- i. This paper consists of Part A and Part B.
- ii. No of Questions:
Part A – 10
Part B – 04
- iii. Answer all the questions.
- iv. Attach Part A of the question paper with your answer script.
- iv. You are strictly advised **NOT** to take Part A of the question paper out of the examination hall.

Part A

Answer question 1-10 by clearly underlining the correct answer.

- (01) Which one of the following is not normally a responsibility of the treasurer of a modern corporation but rather the financial controller?
- a) Budgets and forecasts
 - b) Risk management
 - c) Investment management
 - d) Financing management

(02) Consider the following two statements.

- (1) Preference shares normally offer investors a lower level of risk than loan capital
- (2) Companies can gain tax savings on paid preference dividend.

Which one of the following combinations relating to the above statements is correct?

	Statement	
	1	2
A	True	True
B	True	False
C	False	True
D	False	False

- a) A
- b) B
- c) C
- d) D

(03) You have just assessed a project, involving an immediate cash outflow followed by a series of cash inflows over the next seven years, by calculating the Net Present Value (NPV) and the Internal Rate of Return (IRR). You have now discovered that you have underestimated the discounting rate.

What will be the effect on NPV and IRR after correcting the under estimation?

	NPV	IRR
A	Reduce	No change
B	Increase	No change
C	No change	Reduce
D	Increase	Increase

- a) A
- b) B
- c) C
- d) D

- (04) Graygreen Company is considering the following project. The standard payback period of the company is 4 years. Would this project be acceptable?

Year	Cash flow in Rs.
0	(120,000)
1	35,000
2	35,000
3	35,000
4	35,000
5	20,000

- a) Payback is over 4 years; therefore, reject the project.
- b) The project has cash flows for 4 years; therefore, accept the project.
- c) Payback is between 3 and 4 years; accept the project.
- d) Payback is between 4-5 years; do not accept the project
- (05) A company's gearing ratio would rise if
- a) A decrease in long term loans is less than a decrease in shareholder's funds
- b) A decrease in long term loans is more than a decrease in shareholder's funds
- c) Interest rate rise
- d) Interest rate fall
- (06) JHC company has the following working capital ratios:

	2019	2018
Current ratio	1.2:1	1.6:1
Receivables days	69 days	45 days
Payables days	32 days	45 days
Inventory turnover	45 days	32 days

Which of the following statement is correct?

- a) JHC is suffering from a worsening liquidity position in 2019
- b) JHC's receiving cash from customers more quickly in 2019 than in 2018
- c) JHC's liquidity and working capital has improved in 2019
- d) JHC is taking longer to pay suppliers in 2019 than in 2018

(07) Sarani wishes to obtain a housing loan of Rs. 2,500,000 at an annual interest rate of 12.24%. The loan is to be repaid in 120 monthly instalments which will be paid at the end of each month. What is the loan capital outstanding at the end of 2nd month?

- a) Rs. 2,427,569.12
- b) Rs. 2,478,459.82
- c) Rs. 2,438,999.82
- d) Rs. 2,463,624.12

(08) Tissara plans to make 30 quarterly deposits of LKR 2,000 into a savings account. The first deposit will be made immediately. The savings account pays interest at an annual rate of 8%, compounded quarterly. Find the amount in his account at the end of the seven and a half year period ?

- a) Rs. 44,793
- b) Rs. 81,140
- c) Rs. 82,760
- d) Rs. 46,790

(09) Wilky is considering an investment that is expected to pay Rs.45,000 per year for the next five years and will be worth Rs.500,000 at the end of the fifth year. If his discount rate is 13 percent, what is the maximum amount he should be willing to pay for this investment?

- a) Rs.725,000.00
- b) Rs.658,275.41
- c) Rs.429,655.37
- d) Rs.398,434.67

(10) Suppose a company's net earnings and equity capital are Rs. 1,000,000.00 and Rs. 5,000,000.00 respectively. The dividend payout ratio is 20%. What is the growth rate of the company?

- a) 04%
- b) 08%
- c) 20%
- d) 16%

(02 X 10 = Total 20 Marks)

Part B

(01)

- a) Describe the evolution of financial management by explaining the salient features of traditional and modern approach to financial management.

(04 Marks)

- b) Explain the difference between the wealth maximization objective and profit maximization objective of a firm.

(04 Marks)

- c) "Finance manager stands in between financial markets and firm's operations." Comment on this statement highlighting the role of financial manager in an organization.

(07 Marks)

(Total 15 Marks)

(02)

- a) Methmini PLC is considering two possible investment projects named as Project A and Project B. Project A's initial cost is LKR 450 Million where Project B's initial cost is LKR 350 Million. The expected total revenue and expense for each year of the project life of the above two projects are shown below.

LKR (in Millions)

Year	Project A		Project B	
	Total Revenue	Total Expenses	Total Revenue	Total Expenses
Year 1	292	172	260	180
Year 2	301	178	273	186
Year 3	313	185	293	197
Year 4	322	192	308	204
Year 5	332	198	317	209
Year 6	344	206	329	214

Assume :

no residual values at the end of the sixth year

the firm's cost of capital is 13%.

I) You are required to calculate

i. Discounted pay back period of the two projects

ii. Net Present Value (NPV) for each project

iii. Internal Rate of Return (IRR) for each project

(If needed, use only 13 % and 18 % discounting rates for your calculations)

II) Which project should be selected based on the NPV approach? Advise the company. (15 Marks)

b) You have been provided the drafted financial statements of LBG Growintec Ltd prepared for the year ended 31st March 2018 and 31st March 2019.

Comprehensive Income Statement for the year ended 31.03.2019 and 31.03.2018

	2019 (LKR.'000')	2018 (LKR.'000')
Turnover	3,850	1,854
Less: Cost of Sales	2,460	1,150
Gross Profit for the Year	1,390	704
Less: Operating Expenses	575	410
Operating Profit	815	294
Less: Interest Expense	45	60
Add: Dividend Income	140	-
Profit before Tax	910	234
Less: Income Tax	364	94
Profit after Tax	546	140
Retained Profit	150	50
	696	190
Less: Dividend	130	40
Retained Profit Carried Forward	566	150

Statement of Financial Position as at 31.03.2019 and 31.03.2018

	2019 (LKR.'000')	2018 (LKR.'000')
Fixed Assets		
Property Plant and Equipment	2,680	2,060
Investments	450	350
	3,130	2,410
Current Assets		
Inventory	420	340
Accounts Receivable	530	440
Cash & Bank	30	55
	980	835
	4,110	3,245
Finance by		
Share Capital and Reserves		
Ordinary Share Capital (at LKR 10 each)	2,580	2,050
Retained Earnings	566	150
Non-Current Liabilities		
12 % Debentures	300	400
	3,446	2,600
Current Liabilities		
Accounts Payable	409	375
Accrual Expenses	155	145
Tax Payable	100	125
	664	645
	4,110	3,245

Market price of an ordinary share and the number of ordinary shares of LBG Growingtec Ltd as at the end of year 2018 and 2019 are given below.

	2019	2018
Market Price of an Ordinary Share (LKR.)	20	15
Number of Ordinary Shares	258,000	205,000

You are required to:

Calculate following ratios for LBG Growingtec Ltd for year 2018 and 2019.

- i) Net Profit Ratio
- ii) Return on Capital Employed (ROCE)
- iii) Quick Ratio
- iv) Interest Cover
- v) Price Earnings Ratio

(10 Marks)

(Total 25 Marks)

- (03) a) Greentera Ltd wishes to calculate its weighted average cost of capital. The capital structure of Greentera Ltd. is as follows.

	LKR
Ordinary share capital (LKR 10 each)	60,000,000
Retained Earnings	17,400,000
10% Preference shares of LKR 10 each	18,000,000
11% Debentures of LKR 100 each	40,000,000
09% Debentures of LKR 100 each	45,000,000
14% Long term loan	10,000,000
	190,400,000

The market price of a ordinary share is LKR 23.50. Company currently pays an annual ordinary dividend of LKR 2.50 per share. The company's dividend has grown steadily over the past 8 years (from 01st of April 2011 to 31st of March 2019) from LKR 0.80 to its current level and this growth trend is expected to continue. The preference shares are currently selling at LKR 17 per share. 11% debentures are redeemable at par in 11 years' time.

11% debentures and the 9% debentures are currently selling at LKR 117 and LKR 113 respectively per debenture.

The preference share dividend and 9 % debenture interest are due to be paid in near future. Ordinary share dividend and 11% debenture interest has just been paid.

Assume that the corporate tax rate is 30%.

You are required to,

calculate the Weighted Average Cost of Capital (WACC) for Greentera Ltd based on market values. (if required, **only use 05% and 13% discounting rates** for your calculations)

(14 Marks)

b) Briefly explain the three (03) levels of informational market efficiencies.

(06 Marks)

(Total 20 Marks)

(04) Write short notes on following:

- a) Working Capital Management
- b) EBIT-EPS Analysis
- c) Degree of Operating Leverage and Financial Leverage
- d) Types of Dividend Policies.

(05 Marks x 4 = Total 20 Marks)

1%	2%	3%	4%	5%	6%	7%	8%	9%	10%	11%	12%	13%	14%	15%	16%	20%	24%	26%	30%
0.9901	0.9804	0.9709	0.9616	0.9524	0.9434	0.9346	0.9259	0.9174	0.9091	0.9009	0.8929	0.8850	0.8772	0.8696	0.8621	0.8333	0.8065	0.8009	0.7692
0.9803	0.9612	0.9428	0.9246	0.9070	0.8900	0.8734	0.8573	0.8417	0.8264	0.8116	0.7972	0.7831	0.7693	0.7559	0.7428	0.6845	0.6504	0.6400	0.5917
0.9706	0.9423	0.9151	0.8890	0.8639	0.8398	0.8163	0.7936	0.7722	0.7513	0.7312	0.7110	0.6919	0.6730	0.6554	0.6391	0.5707	0.5245	0.5120	0.4562
0.9610	0.9238	0.8885	0.8548	0.8227	0.7921	0.7629	0.7350	0.7084	0.6830	0.6587	0.6355	0.6133	0.5921	0.5718	0.5523	0.4823	0.4230	0.4098	0.3509
0.9515	0.9057	0.8626	0.8210	0.7805	0.7413	0.7030	0.6666	0.6319	0.6000	0.5695	0.5402	0.5120	0.4848	0.4586	0.4332	0.3619	0.3000	0.2877	0.2283
0.9420	0.8880	0.8375	0.7893	0.7432	0.7000	0.6583	0.6180	0.5790	0.5414	0.5050	0.4698	0.4357	0.4026	0.3704	0.3391	0.2669	0.2040	0.1917	0.1323
0.9327	0.8708	0.8131	0.7599	0.7107	0.6651	0.6227	0.5825	0.5437	0.5062	0.4700	0.4350	0.4010	0.3680	0.3359	0.3047	0.2325	0.1696	0.1573	0.0979
0.9235	0.8535	0.7894	0.7307	0.6768	0.6274	0.5820	0.5403	0.5009	0.4636	0.4284	0.3943	0.3612	0.3290	0.2977	0.2673	0.1951	0.1322	0.1199	0.0605
0.9143	0.8368	0.7664	0.7026	0.6446	0.5919	0.5439	0.5002	0.4604	0.4241	0.3909	0.3586	0.3272	0.2967	0.2670	0.2380	0.1658	0.1029	0.0906	0.0312
0.9053	0.8203	0.7441	0.6756	0.6139	0.5584	0.5083	0.4632	0.4224	0.3855	0.3522	0.3200	0.2886	0.2580	0.2291	0.2000	0.1278	0.0649	0.0526	0.0032
0.8963	0.8043	0.7224	0.6496	0.5847	0.5268	0.4751	0.4289	0.3875	0.3505	0.3173	0.2856	0.2546	0.2243	0.1947	0.1659	0.0937	0.0308	0.0185	0.0091
0.8874	0.7885	0.7014	0.6246	0.5568	0.4970	0.4440	0.3971	0.3555	0.3186	0.2856	0.2537	0.2224	0.1917	0.1616	0.1322	0.0600	0.0271	0.0148	0.0054
0.8787	0.7730	0.6810	0.6006	0.5303	0.4688	0.4150	0.3677	0.3262	0.2897	0.2575	0.2262	0.1950	0.1641	0.1338	0.1043	0.0321	0.0092	0.0069	0.0025
0.8700	0.7579	0.6611	0.5775	0.5051	0.4423	0.3878	0.3405	0.2992	0.2633	0.2320	0.2006	0.1693	0.1381	0.1070	0.0767	0.0200	0.0071	0.0048	0.0014
0.8613	0.7430	0.6419	0.5553	0.4810	0.4173	0.3624	0.3152	0.2745	0.2394	0.2090	0.1787	0.1484	0.1181	0.0878	0.0585	0.0100	0.0071	0.0048	0.0014
0.8528	0.7284	0.6232	0.5339	0.4581	0.3938	0.3387	0.2919	0.2519	0.2178	0.1883	0.1581	0.1280	0.0978	0.0685	0.0392	0.0000	0.0071	0.0048	0.0014
0.8444	0.7142	0.6050	0.5124	0.4363	0.3714	0.3166	0.2703	0.2311	0.1978	0.1686	0.1386	0.1086	0.0786	0.0486	0.0186	0.0000	0.0071	0.0048	0.0014
0.8360	0.7002	0.5874	0.4936	0.4155	0.3503	0.2959	0.2502	0.2120	0.1799	0.1528	0.1250	0.0972	0.0694	0.0416	0.0138	0.0000	0.0071	0.0048	0.0014
0.8277	0.6864	0.5703	0.4746	0.3957	0.3305	0.2765	0.2317	0.1945	0.1635	0.1377	0.1119	0.0861	0.0603	0.0345	0.0087	0.0000	0.0071	0.0048	0.0014
0.8195	0.6730	0.5537	0.4564	0.3769	0.3116	0.2584	0.2145	0.1784	0.1486	0.1240	0.1007	0.0774	0.0541	0.0308	0.0075	0.0000	0.0071	0.0048	0.0014
0.8114	0.6598	0.5375	0.4388	0.3589	0.2942	0.2415	0.1987	0.1637	0.1351	0.1117	0.0892	0.0676	0.0460	0.0244	0.0028	0.0000	0.0071	0.0048	0.0014
0.8034	0.6480	0.5219	0.4220	0.3418	0.2775	0.2257	0.1839	0.1502	0.1228	0.1007	0.0792	0.0586	0.0380	0.0174	0.0058	0.0000	0.0071	0.0048	0.0014
0.7954	0.6342	0.5067	0.4067	0.3256	0.2616	0.2105	0.1703	0.1378	0.1117	0.0907	0.0706	0.0510	0.0314	0.0118	0.0002	0.0000	0.0071	0.0048	0.0014
0.7876	0.6217	0.4919	0.3901	0.3101	0.2470	0.1973	0.1577	0.1264	0.1015	0.0817	0.0629	0.0442	0.0256	0.0070	0.0000	0.0000	0.0071	0.0048	0.0014
0.7799	0.6090	0.4776	0.3751	0.2953	0.2330	0.1842	0.1460	0.1180	0.0923	0.0735	0.0558	0.0381	0.0204	0.0028	0.0000	0.0000	0.0071	0.0048	0.0014
0.7719	0.5921	0.4610	0.3583	0.2784	0.2171	0.1694	0.1314	0.0994	0.0764	0.0573	0.0407	0.0240	0.0074	0.0000	0.0000	0.0000	0.0071	0.0048	0.0014
0.7639	0.5800	0.4554	0.3524	0.2724	0.2111	0.1634	0.1254	0.0934	0.0704	0.0513	0.0347	0.0180	0.0014	0.0000	0.0000	0.0000	0.0071	0.0048	0.0014
0.7559	0.5690	0.4460	0.3428	0.2628	0.2015	0.1538	0.1158	0.0838	0.0608	0.0417	0.0251	0.0084	0.0000	0.0000	0.0000	0.0000	0.0071	0.0048	0.0014
0.7479	0.5580	0.4360	0.3326	0.2526	0.1913	0.1436	0.1056	0.0736	0.0506	0.0315	0.0149	0.0000	0.0000	0.0000	0.0000	0.0000	0.0071	0.0048	0.0014
0.7399	0.5470	0.4260	0.3224	0.2424	0.1811	0.1334	0.0954	0.0634	0.0404	0.0213	0.0047	0.0000	0.0000	0.0000	0.0000	0.0000	0.0071	0.0048	0.0014
0.7319	0.5360	0.4160	0.3122	0.2322	0.1709	0.1232	0.0852	0.0532	0.0302	0.0111	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0071	0.0048	0.0014
0.7239	0.5250	0.4060	0.3020	0.2220	0.1607	0.1130	0.0748	0.0428	0.0198	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0071	0.0048	0.0014
0.7159	0.5140	0.3960	0.2920	0.2120	0.1507	0.1030	0.0648	0.0328	0.0098	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0071	0.0048	0.0014
0.7079	0.5030	0.3860	0.2820	0.2020	0.1407	0.0930	0.0548	0.0228	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0071	0.0048	0.0014
0.6999	0.4920	0.3760	0.2720	0.1920	0.1307	0.0830	0.0448	0.0128	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0071	0.0048	0.0014
0.6919	0.4810	0.3660	0.2620	0.1820	0.1207	0.0730	0.0348	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0071	0.0048	0.0014
0.6839	0.4700	0.3560	0.2520	0.1720	0.1107	0.0630	0.0248	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0071	0.0048	0.0014
0.6759	0.4590	0.3460	0.2420	0.1620	0.1007	0.0530	0.0148	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0071	0.0048	0.0014
0.6679	0.4480	0.3360	0.2320	0.1520	0.0907	0.0430	0.0048	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0071	0.0048	0.0014
0.6599	0.4370	0.3260	0.2220	0.1420	0.0807	0.0330	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0071	0.0048	0.0014
0.6519	0.4260	0.3160	0.2120	0.1320	0.0707	0.0230	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0071	0.0048	0.0014
0.6439	0.4150	0.3060	0.2020	0.1220	0.0607	0.0130	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0071	0.0048	0.0014
0.6359	0.4040	0.2960	0.1920	0.1120	0.0507	0.0030	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0071	0.0048	0.0014
0.6279	0.3930	0.2860	0.1820	0.1020	0.0407	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0071	0.0048	0.0014
0.6199	0.3820	0.2760	0.1720	0.0920	0.0307	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0071	0.0048	0.0014
0.6119	0.3710	0.2660	0.1620	0.0820	0.0207	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0071	0.0048	0.0014
0.6039	0.3600	0.2560	0.1520	0.0720	0.0107	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0071	0.0048	0.0014
0.5959	0.3490	0.2460	0.1420	0.0620	0.0007	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0071	0.0048	0.0014
0.5879	0.3380	0.2360	0.1320	0.0520	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0071	0.0048	0.0014
0.5799	0.3270	0.2260	0.1220	0.0420	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0071	0.0048	0.0014
0.5719	0.3160	0.2160	0.1120	0.0320	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0071	0.0048	0.0014
0.5639	0.3050	0.2060	0.1020	0.0220	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0071	0.0048	0.0014
0.5559	0.2940	0.1960	0.0920	0.0120	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0071	0.0048	0.0014
0.5479	0.2830	0.1860	0.0820	0.0020	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000	0.0071	0.0048	0.0014
0.5399	0.2720	0.1760	0.0720	0.															

