



UNIVERSITY  
OF  
JOHANNESBURG

Department of Finance and Investment Management

# INTERMEDIATE FINANCE B

S3PFMQ5 / PFM0005 / ADFM007

LAST ASSESSMENT OPPORTUNITY

9 November 2015

Time: 2.25 hours & 15 minutes reading time

Marks: 75

**Assessors:** Ms Bianca Göbel  
Ms Chantelle Viljoen

**Internal Moderator:** Ms Melissa McGill

**External Moderator:** Mr Matthew Keevy

## INSTRUCTIONS:

- This paper consists of 11 pages.
- Answer ALL questions.
- Start each question (2 and 3) on a new page.
- **Question 1 should be answered on the answer sheet at the back of this question paper.**
- Silent, non-programmable calculators may be used, unless otherwise instructed.
- Show all calculations clearly. Round all calculations to two decimal places.
- Answers with Tippex and in pencil will **not** be marked and the script will also **not** be considered for a remark.
- **Scratch out open spaces and empty pages otherwise your paper will not be considered for a remark.**

Question	Topic	Marks	Time
	Reading time		15 minutes
1	Objective Test Questions	25	45 minutes
2	Various Topics	50	90 minutes
		<b>75</b>	<b>150 minutes</b>

**This page is blank**

## QUESTION 1

**[25 Marks]**

### Instructions for answering Objective Test (OT) Questions

The answers to the OT questions should be recorded in your answer script. Number each question appropriately from 1 to 20, and write only the correct answer or letter you select next to each question number.

Questions consist of the following types:

- 1) Multiple choice – select only the most appropriate answer from multiple statements;
- 2) Multiple response – select as many statements as is true from the options provided;
- 3) Number/text entry – filling in the missing text (words, symbols or numbers) in a statement;
- 4) True/false – assessing a statement as either correct, or incorrect; and/or
- 5) Matching – matching statements from one column, with the appropriate one/s in another column.

Clear instructions will be provided when more than one statement is correct (multiple response), or where statements to be matched (matching), may be used more than once.

**Please pay close attention to each questions' mark allocation.**

1. Indicate whether the following statement is true or false:

*'The International Accounting Standard IAS17 defines a finance lease as a lease that transfers substantially all the risks and rewards associated with ownership of an asset from the lessor to the lessee.'*

**(1)**

The following information relates to questions 2 – 10.

Round all answers, where necessary, to two decimals.

Star Ltd is a listed company which has produced the following summarised Statement of comprehensive Income for the year ended and Statement of Financial Position as at 30 June 20X5:

<b>Statement of Comprehensive Income for the year ended 30 June 20X5 in R' 000</b>	
Sales	30 000
Operating costs	(18 000)
Depreciation	(4 000)
EBIT	8 000
Interest	(3 000)
Earnings before tax	5 000
Taxation	(1 500)
Net income	<u>3 500</u>

**Statement of Financial Position as at 30 June 20X5**

Net working capital	35 000
Net fixed assets	<u>28 000</u>
Invested capital	<u>63 000</u>
Equity	35 000
Long term debt	<u>28 000</u>
Equity and long-term debt	<u>63 000</u>

2. Calculate the company's debt-equity ratio. (1)
3. What is the interest cover (times interest earned)? (1)
4. Calculate the company's total asset cover? (1)
5. Calculate the company's fixed asset cover? (1)
6. Calculate the company's net profit margin? (1)
7. Calculate the company's return on equity. (1)
8. If the company's cost of capital is 11%, calculate the company's EVA? (2)
9. Assume that the company's market capitalisation is R52.2 million and the company has 7 million shares in issue. Determine the company's earnings per share (EPS)? (1)
10. Calculate the company's price-earnings (P/E) ratio? (1)
11. Indicate whether the following statement is true or false:  
*'The use of financial leverage does not cause a given return on assets to be levered up to a higher return on equity.'* (1)
12. Panda Ltd is a stuffed teddy manufacturer. The company's share price is currently trading at R15 and the earnings per share is R1.25. The company's P/E ratio is 12 and the sector average is 17.  
 Calculate the value of Panda Ltd based on the industry sector average P/E ratio. (1)

13. Smiley Ltd wishes to issue 12% preference shares at an issue price of R1 each. If the current market rate for preference shares in the same class has risen to 14%.

Determine the value of a preference share.

Round your answer to two decimals.

(1)

14. Complete the following sentence by filling in the missing words that are provided in the table below:

'Leverage is intended to (a) \_\_\_\_\_ the return on shareholders' funds in exchange for (b) \_\_\_\_\_ financial risk.'

increase	maximise	greater
minimise	less	decrease

(2)

15. Eagle Ltd's capital structure is as follows:

Debt	60%
Preference shares	5%
Ordinary share equity	35%

The after-tax cost of debt is 8.8%; the cost of preference shares is 11%; and the cost of equity is 15.6%.

Calculate the weighted average cost of capital.

Round your answer to two decimals.

\_\_\_\_\_ %

(1)

16. Closets, Closets, Closets, a company with R100 million in assets and 50% debt in its capital structure, is considering a series of projects in the same risk category as the overall business, based on a capital budget of R25 million. The company's after-tax weighted average cost of capital is 10.4%, the marginal cost of debt is 8% and the marginal tax rate is 28%.

If the project is financed exclusively with new equity, calculate the rate of return it must earn to be acceptable.

Ignore flotation costs.

\_\_\_\_\_ %

(2)

17. Which of the following are NOT fundamental building blocks of a valuation?

- A. The amount of each future cash flow
- B. The cost of capital
- C. The period within which the cash flows occur
- D. The riskiness of future cash flows

(2)

## QUESTION 2

[27 Marks]

### PART A

The following are extracts from the Annual Financial Statements of Sea Ltd and Land Ltd.

Year	Sea Ltd			Land Ltd		
	EPS(c)	DPS(c)	Price Range (R)	EPS(c)	DPS(c)	Price Range (R)
2001	1782	637	100.00-64.00	1500	570	90.00-66.50
2002	1653	673	110.00-75.00	1549	687	120.00-79.00
2003	1823	700	152.00-130.00	1154	623	130.00-75.00
2004	1994	812	182.00-130.00	890	575	133.00-80.00
2005	1684	845	260.00-170.00	947	515	91.00-74.75

#### REQUIRED:

- 2.1 Calculate the dividend pay-out ratios for **both** Sea Ltd and Land Ltd. (5)
- 2.2 Calculate the growth in dividends and earnings for **both** Sea Ltd and Land Ltd. (12)
- 2.3 Are the dividend policies different? Motivate your answer (2)

### PART B

Air Ltd supplies various adventure travel companies with hang gliders. The company's net income after-tax is R25 million. The company is investing in new, durable materials at a cost of R10 million in the coming year which will give the gliders more stability in the air.

Air Ltd's target capital structure is represented by a debt equity ratio of 70%. The Company follows the residual approach to dividends.

#### REQUIRED:

- 2.4 What is the Company's dividend pay-out ratio? (6)
- 2.5 Identify what type of decision a leasing decision will be classified as **and** identify the appropriate discount rate of a leasing decision. (2)

[Total Question 2 = 27 Marks]

**QUESTION 3**  
**PART C**

**[23 Marks]**

Assume that the following indirect exchange rates were quoted against the Rand (ZAR):

Japanese Yen (JPY)	0.1673
Swiss Franc (CHF)	0.7983

The previous closing rates were:

Japanese Yen (JPY)	0.1728
Swiss Franc (CHF)	0.7811

**REQUIRED:**

- 3.1 Indicate whether the above currencies have depreciated or appreciated against the rand. (4)

**Part D**

A South African importer purchases glassware from the Czech Republic. The cost is €301 200. Payment is due in three-month's time in euros.

Czech Republic (euros)

Spot	€0.81034
Three-month forward	€0.82259

South Africa

Spot	R11.3810
Three-month forward	R11.5690

Interest rates (three-monthly, annualised)

United States	4.1%
Czech Republic	5.5%
South Africa	11.4%

**REQUIRED:**

- 3.2 **Calculate** is the forward premium or discount on the rand/dollar leg of the above transaction? (2)
- 3.3 **Calculate** is the forward premium or discount on the rand/euro leg of the above transaction? (2)
- 3.4 Assume that the importer wants to cover the transaction against foreign exchange risk. **Calculate** the cost of a forward contract transaction **and** a money market hedge.  
• Assume no capital controls. (10)
- 3.5 If the importer expects the rand to depreciate against the dollar but expects the dollar to appreciate against the euro, which hedging policy should the importer follow? (2)
- 3.6 List the **THREE** types of foreign exchange exposure. (3)

**[Total Question 3 = 23 Marks]**

**(TOTAL 75 MARKS)**

**- END -**



**This page is blank**

**ANSWER SHEET FOR QUESTION 1**

**Name and surname:** \_\_\_\_\_

**Student number:** \_\_\_\_\_

1. \_\_\_\_\_
2. \_\_\_\_\_
3. \_\_\_\_\_
4. \_\_\_\_\_
5. \_\_\_\_\_
6. \_\_\_\_\_
7. \_\_\_\_\_
8. \_\_\_\_\_
9. \_\_\_\_\_
10. \_\_\_\_\_
11. \_\_\_\_\_
12. \_\_\_\_\_
13. \_\_\_\_\_
14. (a) \_\_\_\_\_
- (b) \_\_\_\_\_
15. \_\_\_\_\_
16. \_\_\_\_\_
17. \_\_\_\_\_
- \_\_\_\_\_
18. \_\_\_\_\_
19. \_\_\_\_\_
20. \_\_\_\_\_