ALLAMA IQBAL OPEN UNIVERSITY, ISLAMABAD

Level: MBA
Paper: Financial Management (5535)
Time Allowed: 3 hrs

Semester: Spring 2006
Maximum Marks: 100
Pass Marks: 40

Note: - ATTEMPT ANY FIVE QUESTIONS. ALL CARRY EQUAL MARKS.

Q.No.1 (20)

Given the information that follows, prepare a cash budget for the Sitara Group of Industries for the first six months of 19X2.

a. All prices and costs remain constant.
b. Sales are 75% for credit and 25% for cash.
c. With respect to credit sales, 60% are collected in the month after the sale, 30% in the second month, and 10% in the third. Bad-debt losses are insignificant.
d. Sales, actual and estimated are

October 19X1	$300,000	March 19X2	$200,000
November 19X1	350,000	April 19X2	300,000
December 19X1	400,000	May 19X2	250,000
January 19X2	150,000	June 19X2	200,000
February 19X2	200,000	July 19X2	300,000

e. Payments for purchases of merchandise are 80% of the following month's anticipated sales.
f. Wages and salaries are.

January	$30,000	February	$40,000
March	50,000	April	50,000
May	40,000	June	35,000

g. Rent is $2,000 a month.
h. Interest of $7,500 is due on the last day of each calendar quarter, and no quarterly cash dividends are planned.
i. A tax prepayment of $50,000 for 19X2 incomes is due in April.
j. A capital investment of $30,000 is planned in June to be paid for then.
k. The company has a cash balance of $100,000 at December 31, 19X1, which is the minimum desired level for cash. Funds can be borrowed in multiples of $5,000. (Ignore interest on such borrowings.)

Q.No.2 (20)

The Kari Kid Corporation manufactures only product: planks. The single raw material used in making planks is the dint. For each plank manufactured 12 dints are required. Assume that the company manufactures 150,000 planks per year, that demand for planks is perfectly steady throughout the year, that it costs $200 each time dints are ordered and that carrying costs are $8 per dint per year.

Required:

(a) Determine the economic order quantity of dints.
(b) What are total inventory costs for Kari Kid
(c) How many times per year would inventory be ordered?

Q.No.3 (20)

The Dud Company has been factoring its accounts receivable for the past five years. The factor charges a fee of 2% and will lend up to 80 percent of the volume of receivables purchased for an additional 1.5 percent per month. The firm typically has sales of $500,000 per month, 70 percent of which are on credit. By using the factor, two savings would be affected.

a. $2,000 per month that would be required to support a credit department.
b. A bad-debt expense of 1 percent on credit sales.

The firm's bank has recently offered to lend the firm up to 80 percent of the face value of the receivables shown on the schedule of accounts. The bank would charge 15 percent per annum interest plus a 2 percent monthly processing charge per dollar of receivables lending. The firm extends terms of net 30 and all customers who pay their bills do so by the 30th day. Should the firm discontinues its factoring arrangement in favor of the bank's offer if the firm borrows, on the average, $100,000 per month on its receivables?

Q.No.4 (20)

North Great Timber Company will pay a dividend of $1.50 a share next year. After this earnings and dividends are expected to grow at a 9 percent annual rate. Indefinitely. Investors presently require a rate of return of 13 percent. The company is considering several business strategies and wishes to determine the effect of these strategies on the market price per share of its stock.

a. Continuing the present strategy will result in the expected growth rate and required rate of return stated above.
b. Expanding timber holdings and sales will increase the expected dividend growth rate to 11 percent bull will increase the risk of the company. As a result the rate of return required by investors will increase to 16 percent.
c. Integrating into retail stores will increase the dividend growth rate to 10 percent and increase the required rate of return to 14 percent.

From the standpoint of market price per share, which strategy is best?

Q.No.5 (20)

Discuss the adjustments in the capital budgeting process that should be made to compensate for expected inflation.

Q.No.6 (20)

(A) What are the three major functions of the financial manager? How are they related?
(B) Why are dividends the basis for the valuation of common stock?

Q.N0.7 (20)

(A) Who is able to issue commercial paper and for what purpose?
(B) Compare and contrast a line of credit and a revolving credit agreement.

Q.No.8 (20)

(A) What is the purpose of a balance sheet? An income statement?
(B) Explain why a long term creditor should be interested in liquidity ratios.

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