

UNIVERSITY OF BOLTON
INSTITUTE OF MANAGEMENT
MSC INTERNATIONAL MANAGEMENT/MBA
BUSINESS ADMINISTRATION

SEMESTER 1 EXAMINATION 2019/2020

FINANCIAL MANAGEMENT AND DECISION
MAKING

MODULE NO: MBA7011

Date: Monday 13 January 2020 Time: 2.00 – 5.00

INSTRUCTIONS TO CANDIDATES:

There are Five questions on this paper.

Answer all questions.

All questions carry equal marks

This examination is 3 hours.

This is a closed book examination.

You must hand in this exam paper with your answer booklet.

(Discount tables are attached at the back of this question paper)

Institute of Management
 MSc International Management/MBA Business Administration
 Semester 1 Examination 2019-2020
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 Module No. MBA 7011

Question 1

Roberts Limited is a medium size electronic company.
 It is considering investment in new plant to enable a brand new
 Component to be manufactured.

The cash flows that have been estimated are as follows:

Year 0	Initial Investment	(£500,000)
Year 1	Net after tax cash flow	£200,000
Year 2	Net after tax cash flow	£220,000
Year 3	Net after tax cash flow	£100,000
Year 4	Net after tax cash flow	£ 80,000
Year 5	Net after tax cash flow	£105,000

It is expected that the new plant will have zero value at the end of the five year project life.

The capital structure of Roberts Limited is as follows:

Ordinary Share Capital of 1,000,000 (Par Value £1)

10 % irredeemable Debentures of £100,000.

The ordinary shares are currently trading at 50 pence per share.

The debentures are currently trading at a price of £80.00 per £100 block.

The company has just paid an ordinary share dividend of 10 pence per share and future dividends are expected to remain the same.

The company pays corporation tax at a rate of 25%.

Required :

(a) Calculate the Weighted Average Cost of Capital for Roberts Limited. (8 marks)

b) Using the Weighted Average Cost as the investment hurdle rate calculate the net present value for the proposed project. (8marks)

c) Advise the management of Roberts Limited as to whether to proceed with the project, highlighting any assumption's that you have made. (4 marks)

(Total 20 Marks)

Institute of Management
MSc International Management/MBA Business Administration
Semester 1 Examination 2019-2020
Financial Management and Decision Making
Module No. MBA 7011

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Question 2

(a) Critically appraise the advantages and disadvantages of the traditional absorption costing techniques in modern management accounting product costing and those of Activity Based Costing (ABC) techniques.

(10 Marks)

(b) Outline the method used to compute the break-even of a company's products and the use of such a technique when considering a company's pricing strategy.

(10 Marks)

(Total 20 Marks)

Question 3

(a) Analyse the benefits of a good budgetary control identifying measures that organisations can take to ensure that the budget plan is achieved.

(10 marks)

(b) Critically analyse the effect on behaviour of employees of a budgetary control system.

(10 marks)

(Total 20 Marks)

Question 4

A challenge to companies is identifying the most appropriate method of raising finance. Evaluate the strengths and weaknesses of the following options for sourcing finance:

- (i) Initial Public Offering
- (ii) Rights Issue
- (iii) Debenture / Bank Loan
- (iv) Internal Funds

(Total Marks 20)

Question 5

Evaluate the benefits to a company in embracing increased corporate governance together with a focus on social and ethical issues.

(Total Marks 20)

Institute of Management
MSc International Management/MBA Business Administration
Semester 1 Examination 2019-2020
Financial Management and Decision Making
Module No. MBA 7011

END OF QUESTION PAPER

Present Value Table

Present value of 1 i.e. $(1 + r)^{-n}$

Where r = discount rate and n = number of periods until payment

Periods (n)	Discount rate (r)									
	1%	2%	3%	4%	5%	6%	7%	8%	9%	10%
1	0.990	0.980	0.971	0.962	0.952	0.943	0.935	0.926	0.917	0.909
2	0.980	0.961	0.943	0.925	0.907	0.890	0.873	0.857	0.842	0.826
3	0.971	0.942	0.915	0.889	0.864	0.840	0.816	0.794	0.772	0.751
4	0.961	0.924	0.888	0.855	0.823	0.792	0.763	0.735	0.708	0.683
5	0.951	0.906	0.863	0.822	0.784	0.747	0.713	0.681	0.650	0.621
6	0.942	0.888	0.837	0.790	0.746	0.705	0.666	0.630	0.596	0.564
7	0.933	0.871	0.813	0.760	0.711	0.665	0.623	0.583	0.547	0.513
8	0.923	0.853	0.789	0.731	0.677	0.627	0.582	0.540	0.502	0.467
9	0.914	0.837	0.766	0.703	0.645	0.592	0.544	0.500	0.460	0.424
10	0.905	0.820	0.744	0.676	0.614	0.558	0.508	0.463	0.422	0.386
11	0.896	0.804	0.722	0.650	0.585	0.527	0.475	0.429	0.388	0.350
12	0.887	0.788	0.701	0.625	0.557	0.497	0.444	0.397	0.356	0.319
13	0.879	0.773	0.681	0.601	0.530	0.469	0.415	0.368	0.326	0.290
14	0.870	0.758	0.661	0.577	0.505	0.442	0.388	0.340	0.299	0.263
15	0.861	0.743	0.642	0.555	0.481	0.417	0.362	0.315	0.275	0.239

(n)	11%	12%	13%	14%	15%	16%	17%	18%	19%	20%
1	0.901	0.893	0.885	0.877	0.870	0.862	0.855	0.847	0.840	0.833
2	0.812	0.797	0.783	0.769	0.756	0.743	0.731	0.718	0.706	0.694
3	0.731	0.712	0.693	0.675	0.658	0.641	0.624	0.609	0.593	0.579
4	0.659	0.636	0.613	0.592	0.572	0.552	0.534	0.516	0.499	0.482
5	0.594	0.567	0.543	0.519	0.497	0.476	0.456	0.437	0.419	0.402
6	0.535	0.507	0.480	0.456	0.432	0.410	0.390	0.370	0.352	0.335
7	0.482	0.452	0.425	0.400	0.376	0.354	0.333	0.314	0.296	0.279
8	0.434	0.404	0.376	0.351	0.327	0.305	0.285	0.266	0.249	0.233
9	0.391	0.361	0.333	0.308	0.284	0.263	0.243	0.225	0.209	0.194
10	0.352	0.322	0.295	0.270	0.247	0.227	0.208	0.191	0.176	0.162
11	0.317	0.287	0.261	0.237	0.215	0.195	0.178	0.162	0.148	0.135
12	0.286	0.257	0.231	0.208	0.187	0.168	0.152	0.137	0.124	0.112
13	0.258	0.229	0.204	0.182	0.163	0.145	0.130	0.116	0.104	0.093
14	0.232	0.205	0.181	0.160	0.141	0.125	0.111	0.099	0.088	0.078
15	0.209	0.183	0.160	0.140	0.123	0.108	0.095	0.084	0.074	0.065

Institute of Management
MSc International Management/MBA Business Administration
Semester 1 Examination 2019-2020
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Formulae

Cost of Equity

$$k_e = \frac{d_1}{P_0} + g$$

Ke = Cost of Equity

d1 = Dividend expected in 1 years time

P0 = Current ex dividend share price

g = Constant growth rate in dividends

Gordon growth model

$$P = D / (k - g)$$

P = market value of the share

D = firm's next expected dividend pay out

k = required rate of return

g = constant growth rate.

CAPM

$$K_e = R_f + \text{Beta} \times (K_m - R_f)$$

Ke is the Cost of Equity;

R_f is the rate of a "risk-free" investment

Beta measures the volatility of the security

K_m is the systematic risk or medium risk rate

Cost of debt

$$\text{Cost of debt} = \text{interest paid} \times (1 - \text{tax rate})$$

Cost of irredeemable debentures

$$\text{Cost of debt (Kd)} = \frac{\text{Interest rate}}{\text{Market Value (Ex int)}}$$

Cost of redeemable preference shares

Internal Rate of Return (IRR)

WACC

Institute of Management
MSc International Management/MBA Business Administration
Semester 1 Examination 2019-2020
Financial Management and Decision Making
Module No. MBA 7011

Weighted Average Cost of Capital

$$\text{WACC} = \frac{\text{Market Value of Equity}}{\text{Total Value of Financing}} \times \text{Cost of Equity} + \frac{\text{Market Value of Debt}}{\text{Total Value of Financing}} \times \text{Cost of Debt} \times (1 - \text{Tax Rate})$$

Past Examination Paper