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Business Finance - Assigment 1

Unit 3 & 4

Q1 D
Q2 A
Q3 B
Q4 D

Q5 i) Cashflow = 2500 - 1500
= +1000

ii) NPV = Net cashflow × Discounting factor

$= 1000 \times \left(\frac{1}{1.20}\right)^1$

$= \frac{1000}{1.2}$

= 833.3

iii) $NPV_2 = \frac{2500}{1.20} + \frac{(-1500)}{(1.20)^2}$

= 2083 - 1041.7
= 1041.3
∴ NPV increases

Q6 The ratios which can be used to measure the efficiency of business are as follows:

- Inventory Turnover Ratio - Inventory turnover is the rate that inventory stock is sold, or used and replaced

$$= \frac{\text{Cost of good Sold}}{\text{Average Inventory}}$$

- Trade Payable Turnover period:- This ratio is used to measure the number of times the business is paying off its creditors or suppliers in an accounting period

$$= \frac{\text{Supplier Purchases}}{\text{Average Accounts Payables}}$$

- Trade recievable turnover Ratio - The receivables turnover ratio measures the efficiency with which a company is able to collect on its receivables of the credit it extends to customers

Q7 • Ration analysis informatis is historic- it is not current.

• Ratio analysis does not take into account external factors such as World wide recession.

• Ratio analysis doesn't not measure human element of a firm

• Ratio analysis can only be used for comparison with other firms of same size & type.

Q8 i) Beta is a concept that measures the expected move in a stock ~~marke~~ relative to overall movements in the market. A stock's beta will change over time because it compares the stocks return with the returns of the overall market.

ii) $\beta_{geared} - \beta_{ungeared}\left[1 + \frac{D}{E}(1-t)\right]$

$\beta_{ungeare}\left[1 + \frac{1}{2}(1-30\%)\right]$

$\beta_{Ungeared} = 0.81481$

β geared = β ungeared $\times \left[1 + \frac{\cancel{D}}{E}(1 - 30\%)\right]$

$= 0.8148 \times 1.70$

$= 1.4$

Q9 D

Q10 i) There can be a conflict of interests between the management.

ii) Share price = 70

DPS = 10

Growth = 8%

Risk-free = 6%

Market risk = 5%

$= \frac{10}{76} + 8\%$

$= 22.3\%$ Cost of Equity

$22.3\% + 80\%$ of 22.3%

$22.3\% + 17.84\%$

$= 40.14\%$

Q11 i) Beta is a concept that measures the expected move in a stock relative to movement in the overall market.

$$\beta_i = \frac{Cov(r_i, r_m)}{Var(r_m)}$$

ii) ~~Beta could be calculated by first dividing the security's standard deviation of returns by the benchmark's standard deviation of returns. The resulting value is multiplied~~

ii) Beta can be calculated by covariance and variance and then dividing them. Covariance measures how two stock move together. Variance refers to how far a stock move's relative to its mean.

iii) Shareholder should invest in the stock with Beta 1 as the price of stock will tend to move with the market

iv) Government Bonds

Q12 i) WACC = Net cost of Debt $\times \frac{Debt}{Debt + Equity}$ + Net cost of Equity $\times \frac{Equity}{Debt + Equity}$

~~= 6.8 × 14.5 × 0.5 × 0.5~~

$= (6.8 \times 0.5) + (14.5 \times 0.5)$

$= 10.65$

$= 10.7\%$

ii) As debt is repaid which states that debt is 0 only equity is remaining

Q13 NPV =

Q14 i) a) Current ratio - is a liquidity ratio that is used to measure whether a firm has enough resources to meet its short term obligation.

b) Debtor's turnover period - this ratio is used to measure how many times a company's receivables are converted to cash in a certain period of time

ii) The super quick ratio can be used as this ratio calculates and estimated by dividing super quick assets by current liabilities of any busines