Name: Roll No.

Indian Institute of Management Kozhikode

eMEP 07

Repeat Examination in

Course code – 132 FINANCIAL MANAGEMENT - I

Maximum marks: 45 Maximum time: 90 minutes

1. Answer all the questions on this question paper only. No additional sheets will be provided. You can make use of the space on this question paper for rough work and submit the full paper for evaluation.
2. This question paper contains 5 pages.
3. For all the objective type questions mark your answers on the question paper itself by encircling the choice no other way of answering is permitted.
4. Don't mark more than one answer in case you want to change an earlier answer cancel it completely and then mark only one answer
5. If more than one answer is marked you will not get any credit
6. Q. Nos 3, 4, 5, 12, 17, 25, 32, 33 carry different marks indicated in the parenthesis. All other questions carry 1 mark each.
7. Don't carry with you any laptops, textbooks or mobile phones.

1. The limitations of the profit maximization goal include:
   a. It lacks a time dimension (i.e., it is static)
   b. It fails to consider risk
   c. The definition of profit is ambiguous
   d. All the above are limitations

2._ ______ markets deal in long-term securities having maturities greater than one year.
   a. Credit
   b. Money
   c. Commodity futures
   d. Capital

3. When you purchased a car, you borrowed $20,000 from the bank at 9.20% and agreed to make monthly payments for 3 years. What is your monthly payment? (2 marks)
   a. $153.33
   b. $662.08
   c. $584.12
   d. $559.78
   e.

4. Keith Stone has a 10-year-old daughter, Kate, who will be entering college in 8 years. Keith estimates college costs to be $16,000, $17,000, $18,000 and $19,000 payable at the beginning of each of Kate's four years in college. How much must Keith save each year (assume end of year payments) for each of the next 8 years to have enough savings to pay for Kate's education? Assume Keith can earn 9% on his savings. (3 marks)
   a. $5.569
   b. $7.720
   c. $5.108
   d. $7.677

5. You just purchased a new $25,000 car and agreed to pay for the car in 50 monthly payments. If the *monthly* interest rate is 1 percent, what is your total financing cost? (2 marks)
   a. $637.82

b. $12,500
c. $574.25
d. $6,891

6. Which of the following is *not* an example of a source of systematic risk?
   a. interest rate changes
   b. foreign competition with an industry's products
   c. changes in the overall economic outlook
   d. changes in the inflation rate

7. Beta is defined as:
   a. a measure of volatility of a security's returns relative to the returns of a broad-based market portfolio of securities.
   b. the ratio of the variance of market returns to the covariance of returns on a security with the market
   c. the inverse of the slope of the security regression line
   d. all of the above

8. All of the following are primary sources of systematic risk *except*
   a. changes in the amount of foreign competition facing an industry
   b. changes in investor expectations about the economy
   c. interest rate changes
   d. a and b

9. Fast Wheels, Inc. expects to pay an annual dividend of $0.72 next year. Dividends have been growing at a compound annual rate of 6 percent and are expected to continue growing at that rate. What is the value of a share of stock of Fast Wheels to an investor who requires a 14 percent rate of return?
   a. $9.00
   b. $5.14
   c. $9.54
   d. None of the above

10. There is a(n) _______ relationship between the value of a bond and its required rate of return.
    a. direct
    b. distant
    c. inverse
    d. turgid

11. The _______ represents the debtholders in dealings with the issuing company.
    a. trustee
    b. stakeholders
    c. broker
    d. investment banker

12. What is the value of an Orion bond that has a 10 percent coupon, pays interest semiannually, and has 10 years to maturity, if the required rate of return is 12 percent? (2 marks)
    a. $1,200
    b. $885.50
    c. $895.27
    d. None of the above

13. Which of the following is *not* a characteristic of common stock:
a. has no maturity date
b. considered a permanent form of long-term financing
c. has claims on assets prior to those of preferred stock
d. is a residual form of ownership

14. In the constant-growth dividend valuation model, the required rate of return must be _______ the dividend growth rate in order for the formula price to be meaningful.
a. less than
b. equal to
c. greater than
d. proportional to

15. The returns investors receive from holding common stocks may be in two forms. They are
a. cash dividend payments and capital gains
b. future earnings and treasury stock
c. stock splits and stock dividends
d. cash dividends and stock dividends

16. Rank in ascending order (lowest to highest) the relative risk associated with holding the preferred stock, common stock and bonds of a firm.
a. preferred stock, bonds, common stock
b. bonds, common stock, preferred stock
c. common stock, preferred stock, bonds
d. bonds, preferred stock, common stock

17. What is the value of a share of stock of HOV Inc. to an investor who requires a 12 percent rate of return if HOV's current dividend is $1.20? Assume earnings and dividends are expected to grow at a compound annual rate of 7 percent. (2 marks)
a. $24.00
b. $18.34
c. $25.68
d. None of the above

18. The value of resources used in an investment project should be measured in terms of their
a. acquisition cost
b. historical cost
c. opportunity cost
d. depreciated cost

19. Which of the following would not be classified as a capital expenditure for decision-making purposes?
a. purchase of a building
b. investment in a management training program
c. purchase of 90-day Treasury Bills
d. development of a major advertising campaign

20. Which of the following is a basic principle when estimating a project's cash flows?
a. cash flows should be measured on a pretax basis
b. cash flows should ignore depreciation because it is a non-cash charge
c. only direct effects of a project should be included in cash flow calculations

d. cash flows should be measured on an incremental basis

21. The effect of a one rupee increase in depreciation expenses is to _______ the typical firm's net cash flows by _______ one rupee.
    a. increase, less than
    b. increase, exactly
    c. decrease, more than
    d. increase, more than

22. In estimating the net investment, an outlay that has already been made is known as a (n)
    a. sunk cost
    b. cash outflow
    c. opportunity cost
    d. expansion cost

23. In terms of the capital budgeting process, net cash flows are
    a. the net cash outlays required to place a project in service
    b. the funds invested in additional assets
    c. incremental changes in a firm's cash flow
    d. the outlays that have already been made

24. The capital budgeting process is very important to the firm because it:
    a. highlights the impacts of a project on net income
    b. essentially plots the company's future direction
    c. is used in working capital analysis
    d. indicates the net cash flows available for employee education

25. Basin Manufacturing (40% marginal tax rate) is considering a plant expansion project. The equipment will cost $100,000 and will require an additional $10,000 for delivery and installation. The expansion also will require Basin to increase immediately its net working capital by $25,000. The expansion is expected to generate revenues of $150,000 per year. Calculate the project's net investment. (2 marks)
    a. $ 81,000
    b. $125,000
    c. $131,000
    d. None of the above

26. Multiple internal rates of return can occur when there is (are):
    a. large abandonment costs at the end of a project's life
    b. a major shutdown and rebuilding of a facility sometime during its life
    c. more than one sign change in the pattern of cash flows over a project's life.
    d. all of the above are correct

27. The payback method is at best a crude measure of the risk of a project because it fails to consider the _______ of a project's returns.
    a. liquidity
    b. variability
    c. timing
    d. magnitude

28. The payback period of an investment is defined as:

a. the number of years required for cumulative profits from a project to equal the initial outlay.
b. the number of years required for the cumulative cash flows from a project to equal the initial outlay.
c. the number of years required for the cumulative cash flows from a project to equal the average investment in the project, when depreciation is considered.
d. a period of time sufficient to earn a rate of return equal to the firm's cost of capital.

29. The relationship between NPV and IRR is such that:
   a. both approaches always provide the same ranking of alternative investment projects.
   b. the IRR of a project is equal to the firm's cost of capital if the NPV of a project is $0.
   c. if the NPV of a project is negative, the IRR must be greater than the cost of capital.
   d. none of the above

30. The profitability index (PI) approach:
   a. fails to directly consider the timing of a project's cash flows
   b. considers only a project's contributions to net income and does not consider cash flow effects
   c. always gives the same accept-reject decisions for independent projects as does NPV and IRR
   d. always gives the same accept-reject decisions for mutually exclusive projects as does NPV and IRR

31. If a net present value analysis for a normal project gives an NPV greater than zero, an internal rate of return calculation on the same project would yield an internal rate of return ___________ the required rate of return for the firm.
   a. greater than
   b. less than
   c. equal to
   ✓ d. cannot be determined from the information given

32. The Atlantic Company plans to open a new branch office in a suburban area. The building will cost $200,000 and will be depreciated (on a straight-line basis) over a 20-year life to a $0 estimated salvage value. Equipment for the building will cost an additional $100,000. This equipment has a 20-year life and will be depreciated on a straight-line basis to a $0 estimated salvage value. The branch office is expected to generate additional before tax net income of $30,000 per year. The tax rate is 40 percent and the cost of capital is 12 percent. Compute the net present value for the project. (4 marks)
   a. $-63,523
   b. $+246,477
   c. $+53,523
   d. $-53,523

33. What is the internal rate of return for a project that has a net investment of $14,600 and a single net cash flow of $25,750 in 5 years? (3 marks)
   a. 10%
   b. 12%
   c. 15.3%
   d. 13.1%