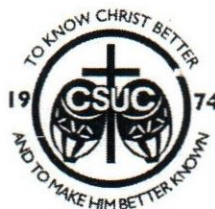


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**CHRISTIAN SERVICE UNIVERSITY COLLEGE
KUMASI, GHANA
CSUC SCHOOL OF BUSINESS
DEPARTMENT OF ACCOUNTING AND FINANCE**

END OF SECOND SEMESTER EXAMINATIONS – 2018/19 ACADEMIC YEAR

LEVEL 200

COURSE CODE&TITLE: CSBG 268 BANKING AND CORPORATE FINANCE

MAY, 2019

70 MARKS

TIME ALLOWED: 2 ½ HOURS.

GENERAL INSTRUCTIONS TO CANDIDATES:

- The paper is divided into four sections A, B, C and D
- **QUESTION ONE OF SECTION B IS COMPULSORY**
- Answer all the questions in Section A, TWO from Section B
- Answer all questions in Section C and only one from section D
- Circle the correct answers on the objective paper
- Write your index number on top of the question paper and every page of the answer booklet used.
- Submit both question paper and answer sheet.

Examiner: Osei-Anim Reindolph

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SECTION A: MULTIPLE CHOICE (50 MARKS)

ANSWER ALL QUESTIONS IN THIS SECTION

1. All the following are components of five C's in Credit analysis except?
 - A. Character
 - B. Capacity
 - C. Component
 - D. Condition
2. Letters of Credit are contingent liabilities. This means that they.....
 - A. are under compulsion to occur
 - B. occur on the left hand side of the balance sheet
 - C. bear no resemblance with current liabilities
 - D. may or may not occur
3. Miss Shetty wants to retire with GH¢100,000 after 5 years. If the bank offers a return of 12% p.a, what should be a onetime deposit she is required to do today.
 - A. GH¢56,742.686
 - B. GH¢55,684.283
 - C. GH¢70,312.123
 - D. GH¢54,298.134
4. What is the stakeholder view of the firm?
 - A. Shareholders should eventually be return their stake in the firm
 - B. The firm must honor its wider social obligations as well as making money
 - C. The only obligation of the firm is to maximize profit
 - D. The firm exists to maximize return
5. Which of the following is a legitimate reason why firm value maximization is preferred to profit maximization as the ideal goal for the firm?
 - A. Value takes into account both profit and cashflow
 - B. Value or discounted cashflow is less ambiguous than profit
 - C. Value takes account of depreciation
 - D. Profit is too much concerned with the longer term.
6. Maximization of corporate wealth is the value maximization for.....
 - A. Stakeholders
 - B. Employees
 - C. Debt holders
 - D. Stockholders
7. What is the future value of an annuity due of ¢15,000 for a period of 6years at a rate of 9% per annum
 - A. \$25,157
 - B. \$25,359
 - C. \$24,693
 - D. \$15,734

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8. At 12% per annum 3 year discount factor is
 - A. 0.826
 - B. 0.712
 - C. 0.909
 - D. 0.829
9. All the following are qualities of marketable securities except
 - A. Affordability
 - B. Liquidity
 - C. Yield
 - D. Safety
10. Which of the following is **not** one of the qualities which make debt attractive to firms?
 - A. The cost of debt is generally less than the cost of share capital and hence can lower the overall cost of capital for a firm.
 - B. Debt interest only gets paid when the company is making a profit.
 - C. It reduces the amount of corporate tax payable by firms by reducing the amount of taxable profit
 - D. The required return on debt is lower because, from the lender's point of view, debt is less risky than equity.
11. Which of the following is **not** a defining quality of a bond?
 - A. Face Value
 - B. Coupon payment
 - C. Maturity
 - D. Dividend yield
12. What is the value of a 6%, five year bond with annual coupons and face value equal to £1,000, if the current yield to maturity is 6%?
 - A. £1,089
 - B. £ 920
 - C. £ 1200
 - D. £ 1000
13. Which of the following is **not** a money market instrument?
 - A. Bond
 - B. Certificate of Deposit
 - C. Commercial Paper
 - D. Treasury Bills
14. If corporation bankrupts, who is first for a corporation's assets?
 - A. President of corporation
 - B. Preferred stockholder
 - C. Loans from banks, bondholders, and taxes from government
 - D. Common stock holders

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15. Which financial statement would you find revenue?
 - A. Income Statement
 - B. Balance Sheet
 - C. Changes in Owner's Equity
 - D. Statement of Cash Flow
16. When a bank grants a 30-year loan for a property and the property is the collateral, what kind of loan is this?
 - A. Mortgage
 - B. Commercial bank loan
 - C. A bond
 - D. Corporate stock
17. Why should financial managers strive to maximize the current value per share of the existing stock?
 - A. Doing so guarantees the company will in size at maximum possible rate
 - B. Doing so increases employee salaries
 - C. Because they have been hired to represent the interests of the current interests of the current shareholders
 - D. Because this will increase the current dividends per share
18. If 20% is the interest rate on a monthly compounded security, calculate the periodic interest rate.
 - A. 20%
 - B. 1.67%
 - C. 1.5%
 - D. 32%
19. Which bond allows the investor to change bond into stock?
 - A. Coupon bond
 - B. Discount bond
 - C. Convertible bond
 - D. Registered bond
20. Asymmetric information occurs because
 - A. One party to a financial transaction has more information than the other
 - B. Not all investors understand company accounts and balance sheets
 - C. Stock market prices on the internet lag real time prices by up to fifteen minutes
 - D. Not all shareholders are able to attend company annual general meetings
21. Which of the following is not a fundamental concept in corporate finance?
 - A. Net Present Value
 - B. Double-entry book keeping
 - C. Business cycle
 - D. Relationship between Risk and Return

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22. Which bond does not have an interest rate stated on it?
- A. Coupon bond
 - B. Discount bond
 - C. Stock
 - D. Perpetuity (or consol) bond
23. In the area of investment banking, what is a syndicate?
- A. Several investment banks work together to sell new stocks and bonds
 - B. The mafia work together to increase crime and profits
 - C. An investment bank works with government to create new corporations
 - D. The syndicate helps the government regulate the financial markets
24. What kind of contract gives an investor the right to *sell* an asset in the future?
- A. Call option
 - B. Put option
 - C. Option premium
 - D. Hedging
25. All the following ratios indicate profitability except
- A. Return on capital employed (ROCE)
 - B. Net Profit Margin
 - C. Gross Profit Margin
 - D. Quick ratio
26. All the following are categories of inventory except
- A. Work in progress
 - B. Raw materials
 - C. Finished goods
 - D. Stock overloads
27. The delay between ordering of goods and the delivery is called
- A. Stock out time
 - B. Inventory hold period
 - C. Lead time
 - D. Holding period
28. The creditors of company are usually interested in observing the --
- A. Liquidity Ratio
 - B. Solvency Ratio
 - C. Profitability Ratio
 - D. Turnover Ratio
29. From the following, which is not considered as the financial asset?
- A. Common Stock
 - B. Patents
 - C. Bonds
 - D. Preferred Stock

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30. A business raises a share capital of \$50,000 and a bank loan of \$20,000. If stockholders require 11.5% on the investment and the bank charges 8.45% on the loan. Calculate the WACC of the business if the tax rate is 17.5%
- A. 10%
 - B. 10.21%
 - C. 10.8%
 - D. 10.6%
31. Some projects that a firm accepts will undoubtedly result in zero or negative returns. In the light of this fact, it is best if the firm
- A. Adjusts its hurdle rate upwards to compensate for this fact
 - B. Adjusts its hurdle rate downwards to compensate for this fact
 - C. Does not adjust its hurdle rate up or down regardless of this fact
 - D. Raises its price to compensate for this fact
32. Which of the following statements is incorrect regarding a normal project?
- A. If the NPV of a project is greater than 0, then its PI will exceed 1
 - B. If the IRR of a project is 8% its NPV using a discount rate K, greater than 8% will be less than 0
 - C. If the PI of a project equals 0, then the projects initial cash out flow equals the PV of its cashflows
 - D. If the IRR of a project is greater than the discount rate K, then its PI will be greater than 1
33. The existence of leasing is primarily because
- A. Intermediate-term loans are difficult to obtain
 - B. This type of financing is unaffected by changes in tax laws
 - C. Companies, financial institutions and individuals derive different benefits from owning
 - D. Leasing is a renewable source of intermediate-term loan funds

A bond is represented by the following information

Use this information to answer questions 34 to 38

\$1000	
(A)	
5yrs	12%
(B)	(C)

34. What does A, B and C represent?

A	B	C
A. Face Value	coupon	maturity
B. Coupon	maturity	par value
C. Par value	maturity	yield to maturity
D. Face value	maturity	coupon

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35. What is the coupon payment of this bond?
- A. \$1200
 - B. \$1120
 - C. \$1020
 - D. \$120
36. How much will a holder of this bond receive in the 3rd year?
- A. \$1200
 - B. \$1120
 - C. \$1020
 - D. \$120
37. How much will the holder receive in the 5th year
- A. \$1200
 - B. \$1120
 - C. \$1020
 - D. \$120
38. If the prevailing market interest rate is 12% then it can be concluded that the bond truly is sold at
- A. Premium
 - B. Par
 - C. Discount
 - D. Maximum
39. Businesses maintain cash balances in order to take advantage of unanticipated business opportunities that may come long from time to time. This motive is
- A. Precautionary
 - B. Transactionary
 - C. Speculative
 - D. Aggressive
40. Present value is defined as
- A. Inverse of future cashflows
 - B. Future cash flows discounted to the present at an appropriate discount rate
 - C. Discounting of compounded future cash flows
 - D. Present cashflows compounded in the future
41. By applying rule 72, cedi will double in nine (9) years if the rate of interest is
- A. 18%
 - B. 9%
 - C. 8%
 - D. 6%
42. The risk that occurs if bond issuers don't pay coupon or principal or both is called
- A. Interest rate risk
 - B. Reinvestment rate risk
 - C. Default risk
 - D. Volatility risk
43. All the following are categories of inventory except
- A. Work in process
 - B. Raw materials
 - C. Finished goods
 - D. Stock overloads

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44. The delay between ordering of goods and the delivery is called
- A. Stock out time
 - B. Inventory hold period
 - C. Lead time
 - D. Holding period
45. In finance, there is a positive trade-off between risk and
- A. Workers capital
 - B. Total cost
 - C. Return
 - D. Fixed assets
46. The minimum amount a bank keeps in a non-interest checking account equal to the specific percentage of an amount borrowed is called
- A. Minimum balance
 - B. Compensating balance
 - C. Cash balance
 - D. Bank overdraft
47. If an asset has a beta of one. Which of the following can be true about the asset
- A. It is very risky
 - B. It is risk free
 - C. It is riskier than the market portfolio
 - D. It has the same risk as the market portfolio
48. Which bond allows the investor to change bond into stock?
- A. Coupon bond
 - B. Discount bond
 - C. Convertible bond
 - D. Registered bond
49. Asymmetric information occurs because
- A. One party to a financial transaction has more information than the other
 - B. Not all investors understand company accounts and balance sheets
 - C. Stock market prices on the internet lag real time prices by up to fifteen minutes
 - D. Not all shareholders are able to attend company annual general meetings
50. Banks have recently introduced the service in what is called RTGs. This stands for
- a. Reliable trade guarantee system
 - b. Real time guarantee system
 - c. Real time gross statement system
 - d. Real trade gross settlement system

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SECTION B

ANSWER QUESTION ONE AND ANY OTHER QUESTION

QUESTION ONE

- a. The data below is the financial statement of Benso Oil Palm plantation for the year 2017.

Benso Oil Palm Plantation Limited

Statement of comprehensive income for the year ended 31 December, 2017

(All amounts are expressed in thousands of Ghana cedis)

	2017	2016
Revenue	89,974	74,278
Cost of sales	(70,108)	(57,732)
Net gains from changes in fair value of biological assets	1,084	300
Gross profit	20,950	16,846
Administrative expenses	(8,121)	(7,051)
Other income	1,247	382
Operating profit	14,076	10,177
Finance income	377	529
Net profit before tax	14,453	10,706
Current tax expense	(1,882)	(2,616)
Total comprehensive income	12,571	8,090
Basic and diluted earnings per share (GH¢)	0.3612	0.2325
Income surplus account		
At 1 January	45,717	39,258
Net profit for the period	12,571	8,090
Dividend declared	(1,618)	(1,631)
At 31 December	56,670	45,717

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Benso Oil Palm Plantation Limited

Statement of financial position as at 31 December, 2017

(All amounts are expressed in thousands of Ghana cedis)

	2017	2016
Non-current assets	51,434	46,617
Property, plant and equipment	47,473	43,740
Biological assets	3,961	2,877
Current assets	224,326	19,709
Inventories	7,282	4,985
Trade and other receivables	8,744	5,957
Amounts due from related companies	5,652	5,110
Current tax asset	97	-
Cash and bank balances	2,551	3,657
Total assets	75,760	66,326
Current liabilities	9,461	10,980
Trade and other payables	6,340	5,132
Amounts due to related companies	406	3,778
Deferred tax liability	1,986	1,366
Dividends payable	729	675
Current tax liability	-	29
Equity	66,299	55,346
Stated capital	2,000	2,000
Capital surplus account	7,629	7,629
Income surplus account	56,670	45,717
Total liabilities and equity	75,760	66,326

The financial statements do not contain untrue statements, misleading or omit material facts to the best of our knowledge.

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Statement of cashflows for the year ended 31 December, 2017

(All amounts are expressed in thousands of Ghana cedis)

Cash flows from operating activities	2017	2016
Cash generated from operations	8,084	14,825
Interest received	377	529
Tax paid	(1,388)	(1,433)
Net cash/ generated from operating activities	7,073	13,921
Cash flows from investing activities		
Purchase of property, plant and equipment	(6,616)	(14,060)
Proceeds from sale of property, plant and equipment	16	49
Net cash used in investing activities	(6,616)	(14,011)
Cash flows from financing activities		
Dividends paid to the company shareholders	(1,564)	(1,490)
Net cash used in investing activities	(1,564)	(1,490)
Increase in cash and cash equivalents	(1,107)	(1,580)
Cash and cash equivalents at beginning of the year	3,658	5,238
Cash and cash equivalent at end of the period	2,551	3,658

Based on the data above calculate the following ratios

- i. Return on Investment
- ii. Net profit margin
- iii. Return on equity
- iv. Total asset turnover
- v. Inventory Turnover in days
- vi. Creditors days
- vii. Receivable Turnover
- viii. Current Ratio
- ix. Acid Test Ratio

(10MARKS)

- b. Mega obtained a loan of GHC 150,000 from Orchestra Bank. The bank charges 16% interest on the loan. The bank also charges 10% as compensating balance. Calculate the following

- i. The loan amount available to Mega
- ii. The periodic monthly interest rate
- iii. Effective monthly interest rate
- iv. The Annual percentage rate
- v. Briefly explain the effect of the compensating balance on the effective interest rate

(5MARKS)

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- c. In the spring of 2010, Templeton was considering the acquisition of a chain of extended care facilities and wanted to estimate its own WACC as a guide to the cost of capital for the acquisition. Templeton's capital structure consists of the following:

<i>SOURCE OF FUND</i>	<i>MARKET VALUE</i>
Debt	250 million
Preferred stock	50 million
Common stock	100 million
Total	400million

Templeton contacted the firm's investment banker to get estimates of the firm's current cost of financing and was told that if the firm were to borrow the same amount of money today, it would have to pay lenders 8%; however, given the firm's 25% tax rate. Preferred stockholders currently demand a 10% rate of return, and common stockholders demand 15%. Templeton's CFO knew that the WACC would be somewhere between 6% and 15% since the firm's capital structure is a blend of the three sources of capital whose costs are bounded by this range. Calculate the accurate WACC of the company. (5marks)

QUESTION TWO

20marks

A. Orchestra Company is analyzing two mutually exclusive projects A and B with each cashflows shown below

year	0	1	2	3	4	5
Project A	(10,000)	1050	2300	4300	2300	1500
Project B	(10,000)	3000	3000	3000	3000	3000

Orchestra Company's cost of capital is 12 percent and it can obtain an unlimited capital at that cost. Calculate the regular **IRR** of the better project that is the project the company should choose if it wants to maximize shareholder wealth. (10marks)

B. It costs Okukuseku Company £20 in labor, £10 in electricity and £15 is printing materials to produce a text book which sells for £90 each. Straight line depreciation is used to apportion the cost of the fixed tangible asset over its 5 year useful economic life. The original cost of the asset £20,000 and has a scrap value of £5000. Other fixed costs that go into

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producing a text book amount to £1500. The total revenue for the accounting period is £13,400. Calculate

- a) The total fixed cost for the account period **(2marks)**
- b) The product breakeven level **(2marks)**
- c) Break even sales level **(2marks)**
- d) The margin of safety as a percentage of sale **(2marks)**
- e) If the selling price is decreased by 15% calculate the new product breakdown level. **(2marks)**

QUESTION THREE

20marks

A. Orchestra incorporated has issued a bond with a face value of \$1000 and a coupon interest rate of 15%. If the yield to maturity is 12% and the bond has a maturity of 10years. Deduce the following.

- I. The price of the bond. **(6marks)**
- II. The duration of the bond. **(2marks)**
- III. Is the bond selling at discount, premium or at par? Explain the basis for your answer **(2marks)**

B. An investment company XYZ is selling an investment package for \$25,000. The package offers an annual cashflow of \$5120 every year for the next **five (5)** years at an interest rate of **650 basis points**. As an investment analyst you have been hired by an investor who wants to buy such an investment package. Advice the investor on whether the package is financially prudent or not. Explain the basis for your answer. **(5marks)**

C. Will your decision above still hold if the annual cashflow and interest rate for the investment are increased to \$5790 and 690 basis points respectively? Explain the basis for the change or otherwise. **(5marks)**

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QUESTION 4

20marks

- A. The material DX is issued uniformly throughout the year. The data below shows the annual requirement, ordering cost and the holding cost of this material

Annual cost: 2400 units

Ordering cost: \$10 per order

Holding cost: \$0.30 per unit.

Determine the following using the above data

- i. the economic order quantity (EOQ) of material DX **(2marks)**
 - ii. the number of orders per year **(2marks)**
 - iii. the total ordering cost for the year **(2marks)**
 - iv. the total holding cost for the year. **(2marks)**
- B. If a firm needs \$100 million to finance its new project and the flotation cost is expected to be 5.5%
- i. How much should the firm raise by selling price securities? **(5marks)**
 - ii. How much is the flotation costs? **(1mark)**

C. An investor invests \$100 and receives the following returns from the portfolio

Year	Returns (%)
1	3
2	5
3	8
4	-1
5	10

- i. Calculate the arithmetic and geometric mean return of the portfolio **(3marks)**
- ii. Which of these two average methods is better in estimating average return of investment? Why? **(3marks)**

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QUESTION 5

- a. An organization wants to embark on a project out of which they expect some returns in a years' time. The organization therefore wishes to finance the project through debt. They have approached a bank which has agreed to advance a loan to finance the project. The bank wishes to use the cashflows from the project as collateral. The organization has therefore prepared a project proposal specifying the proposed cashflows from the project for a period of five years. The initial requirement for the project is GHC500, 000.

YEAR	0	1	2	3	4	5
Cashflow GHC (000)	(500)	100	120	250	350	550

The bank is convinced with the proposal and has agreed to give the said amount at an interest of 10% per annum subject to an expert advice. The bank has therefore hired you as a project financial consultant to advice the management of the bank on the financial viability or otherwise of the project. Your findings will help the bank take a decision in the loan advance. Your presentation must be centered on the following financial appraisal techniques stating your reasons in each case

- i. Simple payback method (2MARKS)
- ii. Net present Value (NPV) (5MARKS)
- iii. Profitability index (PI) (1MARK)
- iv. Internal rate of return (IRR) (2MARKS)

- b. Using the following information below to answer the following questions

Long term debt to equity	0.5 to 1
Total asset turnover	2.5 times
Average collection period	18 days
Inventory turnover	9 times
Gross profit margin	10%
Acid test ratio	1 to 1

Assume a 360 day year and all sales are on credit

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Cash		Notes and payables	GHC 100,000
Account receivables		Long term debt	
Inventory		Common stock	GHC100,000
		Retained earnings	GHC100,000
Plant and equipment			
Total asset		Total liabilities and shareholders' equity	

-
- ```

graph LR
 A[A] -- "Savings/Deposits" --> B[B]
 B -- "E" --> A
 B -- "Loans" --> C[C]
 C -- "D" --> B

```

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Use the process of financial intermediation to identify the parts labeled A, B, C and D  
(2marks)

9. What is economic order quantity? (1mark)

10. State three factors which affect the choice of source of business finance. (1.5marks)

#### SECTION D

Answer only ONE question from this section

##### QUESTION ONE (20marks)

- a. With the aid of a diagram explain the difference between direct financing and indirect financing. (12marks)
- b. What is a financial intermediation? (2marks)
- c. With the aid of a diagram explain how the process of financial intermediation leads to economic development (6marks)

##### QUESTION 2

(20marks)

- a. Explain working capital management (5marks)
- b. What is the difference between gross *working capital* and net *working capital*? (5marks)
- c. Explain how excessive levels of current assets affect the profitability of a business entity (10marks)

##### QUESTION 3 (20marks)

- a. State three internal sources of business finance (6marks)
- b. Give two advantages and one disadvantage each of the above named sources (9marks)
- c. Explain briefly how the risk profile of a business affects its choice of business finance. (5marks)



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**QUESTION 4 (20marks)**

- a. Letters of Credit and Bank guarantee are two banking products which banks offer their customers as a sign of credit worthiness. With the aid of illustration, explain the mechanism of Letter of Credit (LC) and bank guarantee and explain how different and similar they are in respect of their operations **(16MARKS)**.
- b. State four differences between pledge and hypothecation **(4marks)**