ST MARY’S UNIVERSITY

TWICKENHAM, LONDON

BA/BSc/BA(ITT) Degree Examination students registered for

Level **FIVE**

Title: **Corporate Finance**

Code: **MGT5015**

Semester: **Re-sit**

Date: **05 July 2019**

Time: **09:30-11:30am**

TIME ALLOWED: **TWO** HOURS

Section A - Please answer **all** questions (30 marks)

Section B - Please answer **two** questions only (70 marks)

Section A (30 marks)

1. Generally, a corporation is owned by its:

A. managers

B. shareholders

C. debtholders

D. managers, board of directors and shareholders

1. Which of the following is an important function of financial markets? (choose the best answer)

A. Providing financing and reducing risk

B. Providing financing and liquidity

C. Providing information and reducing risk

D. Providing financing, providing liquidity, reducing risk, and providing information

1. Costs associated with the conflicts of interest between the bondholders and the shareholders of a corporation are called

A. litigation costs.

B. agency costs.

C. deferral costs.

D. stakeholder costs.

1. The present value of $100 expected two years from today at a discount rate of 6 percent is

A. $106.00

B. $100.00

C. $89.00

D. $87.00

1. An initial investment of $380,000 is expected to produce an end-of-year cash flow of $480,000. What is the NPV of the project at a discount rate of 20 percent?

A. $20,000

B. $64,000

C. $80,000

D. $176,000

1. Which of the following statements regarding the NPV rule and the rate of return rule is false?

A. Accept a project if its NPV > 0

B. Reject a project if its NPV < 0

C. Reject a project if its rate of return > NPV

D. Reject a project if its rate of return < opportunity cost of capital

1. What is the present value of $10,000 per year in perpetuity at an annual interest rate of 5 percent? Assume the perpetuity starts in one year.

A. $1,000

B. $10,000

C. $100,000

D. $200,000

1. Which of the following is generally considered an example of a perpetuity?

A. Interest payments on a 5-year government bond

B. Interest payments on a 10-year government bond

C. Interest payments on a 30-year government bond

D. Interest payments on a consol

1. A government bond issued in Germany has a coupon rate of 5 percent, a face value of 100 euros, and matures in five years. The bond pays annual interest payments. Calculate the price of the bond (in euros) if the yield to maturity is 4 percent.

A. 110.01

B. 107.16

C. 104.45

D. 103.00

1. Generally, a bond can be valued as a package of

A. annuity and perpetuity only

B. perpetuity and single payment only

C. annuity, perpetuity, and single payment

D. annuity and single payment only

1. If the nominal interest rate per year is 10 percent and the inflation rate is 4 percent, what is the real rate of interest?

A. 4.1 percent

B. 5.8 percent

C. 6.0 percent

D. 14.0 percent

1. Assume General Electric (GE) has about 10.3 billion shares outstanding and the stock price is $29.10. Also, assume the P/E ratio is about 18.3. Calculate the approximate market capitalization for GE.

A. $379 billion

B. $367 billion

C. $351 billion

D. $300 billion

1. Wonderful Computer Company's stock is selling for $100 per share today. It is expected that, at the end of one year, it will pay a dividend of $6 per share and then be sold for $124 per share. Calculate the expected rate of return for the shareholders.

A. 10 percent

B. 20 percent

C. 20 percent

D. 30 percent

1. One can estimate the dividend growth rate for a stable firm as:

A. plow-back rate / the return on equity (ROE)

B. plow-back rate × the return on equity (ROE)

C. plow-back rate - the return on equity (ROE)

D. plow-back rate + the return on equity (ROE)

1. Happy Co. is expected to pay a dividend of $2 per share at the end of year 1, and the dividends are expected to grow at a constant rate of 4 percent forever. If the current price of the stock is $20 per share, calculate the expected return or the cost of equity capital for the firm.

A. 10 percent

B. 4 percent

C. 14 percent

D. 20 percent

Section B (70 marks)

Please answer **two** questions.

1. Describe the CAPM model, paying particular attention to the definition of beta. What features of the model explain its widespread use in corporate finance?
2. Describe the theoretical proposition known as Modigliani-Miller Proposition 2. To what extent does this proposition agree with the conventional view that market analysts have of the weighted average cost of capital?
3. Explain how a company’s mission and identity affect its choice of goals and means to attain those goals. Does the empirical evidence suggest that financial performance and corporate social responsibility are inversely correlated? What are the implications of this evidence for corporate social responsibility and its attractiveness?
4. Describe any two forms of market efficiency, and draw the implications of these forms for the movement of stock prices. Which of these two forms, if any, do you believe to be more realistic, and why?
5. Describe the concept of volatility and explain why a call option is always riskier than a simple investment in the underlying stock. Does a higher volatility result in a higher or lower call option price, and why?

6. What are the various takeover defences which a company’s management can utilise? Who are takeover defences designed to protect, and who are the real beneficiaries?

**END OF EXAMINATION**