THE OPEN UNIVERSITY OF SRI LANKA
MASTER OF BUSINESS ADMINISTRATION /PUBLIC ADMINISRTATION
FINAL EXAMINATION - 2017
MCP 2610 - CORPORATE FINANCE
DURATION – THREE HOURS

Date : 26. 07. 2017 Time : 9.30 am to 12.30 pm

Instructions: Answer ALL four (04) questions.

Numbering of the answers in your answer script should follow the numbers assigned to the questions in the paper. Illegible hand writing is liable to loose marks.

Non programmable calculator is allowed to use

Question No. 01

Whether business concerns are big or small, they need finance to fulfill their business activities. In the modern world, all activities are concerned with economic activities and very particular to earning profit.

(a) Explain briefly the term "Finance" as business function and how it relates to increasing business value.

(07 Marks)

(b) "Wealth maximization is superior to the profit maximization" Critically evaluate this statement.

(08 Marks)

(c) "A company may have important non-financial objectives which must be satisfied in order to ensure the continuing participation of all stakeholders. Without their participation, financial objectives such as maximizing shareholder wealth may be compromised in the future."
Discuss this statement providing two (02) examples in relation to non-financial objectives.

(10 Marks)
(Total Marks 25)

Question No. 02

(a) Explain briefly the term "Financial Markets".

(02 Marks)

(b) Discuss the role of money market and capital market with different types of financial instruments traded in those markets in Sri Lanka.

(08 Marks)

(c) What is meant by Hybrids Security? Explain with examples.

(06 Marks)

(d) Agiya PLC has in issue 10 million ordinary shares with a market value of Rs 23/- per share. A dividend of Rs 2.50 per share for the year 2016 has just been paid. The recent dividend paid by the company is given below. The dividend is expected to grow at a constant rate of 6% per annum. The required return on the company's ordinary shares is 16% per annum.

Year	2013	2014	2015	2016
Dividend per share (Rs.)	2.00	2.05	2.30	2.50

Agiya PLC has also in issue 9% debentures redeemable in five years' time with a total nominal value of Rs 6 million. The market value of each Rs 100 debenture is Rs 107. Redemption will be at the nominal value. The yield-to-maturity on these debentures is 8% per annum.

The company is planning to invest significant amount of money in a new business area. The project has business risk similar to that of the company and is expected to be financed 80% by equity and 20% by debt, on market value basis.

You are considering Agiya PLC to invest and therefore, required to;

(i) Calculate intrinsic value of an Ordinary Share and a Debenture of Agiya PLC.

(ii) Discuss the use of the intrinsic values calculated in (i) above in your investment decision making.

(09 Marks)
(Total Marks 25)

Question No. 03

You have been hired as an analyst for Lanka Plantation PLC and your team is working on an independent assessment of Ceylon Foods PLC., a firm that specializes in the production of freshly imported farm products. Your assistant has provided you with the following data for Ceylon Foods PLC and its industry.

Ratio	2016	2015	2014	Industry Average 2016
Long-term debt-to-total assets	0.45	0.40	0.35	0.35
Inventory Turnover (times)	62.65	42.42	32.25	53.25
Depreciation/Total Assets	0.25	0.014	0.018	0.015
Debtors' Collection Period (Days)	113	98	94	130.25
Debt to Equity	0.75	0.85	0.90	0.88
Profit Margin (%)	8.2	7	6	7.5
Total Asset Turnover (times)	0.54	0.65	0.70	0.40
Quick Ratio	1.028	1.03	1.029	1.031
Current Ratio	1.33	1.21	1.15	1.25
Times Interest Earned	0.9	4.375	4.45	4.65
Total Assets to Equity	1.75	1.85	1.90	1.88

In the annual report to the shareholders, the CEO of Ceylon Foods PLC wrote, "2016 was a good year for the firm with respect to our ability to meet our short-term obligations. We had higher liquidity largely due to an increase in highly liquid current assets (cash, account receivables and short-term marketable securities)."

You are required to;

(a) Critically analyze the validity of the statement given by the CEO of Ceylon Foods PLC in the annual report. Is the CEO correct? Explain and use only relevant information in your analysis.

(10 Marks)

(b) Comment on Ceylon Foods PLC's asset management. **(08 marks)**

(c) Provide the shareholders with a complete analysis of Ceylon Foods PLC's solvency and leverage.

(07 Marks)
(Total Marks 25)

Question No. 04

(a) Distinguish between systematic risk and unsystematic risk in relation to the investment in equity shares.

(04 Marks)

(b) The following are the rates of return expected from a company's equity shares under different economic conditions.

State of Economy	Probability of State of Economy	Expected Rate of Return
Boom	0.3	0.28
Normal	0.5	0.16
Recession	0.2	-0.03

Based on the above information, calculate the expected return and risk of the equity shares.

(05 Marks)

(c) The following information relates to the investment in the equity shares of ABC PLC. The shares were bought on 1st January, 2013 at Rs 25/- each.

Year	Dividend Received (Rs.)	Share Price at the end (Rs.)
2013	1.20	30.50
2014	1.40	32.75
2015	1.50	38.20
2016	1.50	45.10

Using the above information, calculate the holding period return on this investment.

(03 Marks)

(d) What are the types of correlation of security returns? Explain their importance in forming investment portfolios.

(05 Marks)

(e) "Derivatives are used by organizations to help manage their risk". Discuss this statement providing appropriate examples.

(08 Marks)

(Total Marks 25)

-All Rights Reserved-