جامعة السلطان الشريف علي الإسلامية
UNIVERSITI ISLAM SULTAN SHARIF ALI
SULTAN SHARIF ALI ISLAMIC UNIVERSITY

Faculty of Islamic Economics and Finance
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Final Examination Question Paper

Course Code : BF3311
Course Name : Corporate Finance
Course Level : Bachelor of Science in Islamic Finance
Time : 3 hours

Reference allowed:

Calculator allowed.

Notes:

1. Answer all **sixty** of the following questions.
2. Select **ONE best answer** for each question.
3. Each question carries one (1) mark. This paper carries 60 marks.
4. Write your answer in the booklet provided.
5. Candidates are **not allowed** to take the Question Paper and Answer Booklet out of the exam venue.

بسم الله الرحمن الرحيم

QUESTION 1
You are trying to decide how much to save for retirement. Assume you plan to save $9500 per year with the first investment made 1 year from now. You think you can earn 2.5% per year on your investments and you plan to retire in 40 years. How much will you have in your retirement account on the day you retire?

A. $13,425.32
B. $640,324.26
C. $5,125

Answer: ______________________

QUESTION 2
With continuous compounding at 10% for 30 years, the future value of an initial investment of $1,000 is

A. $1,100.00
B. $15,863.09
C. $17,449.40

Answer: ______________________

QUESTION 3
You are considering investing in an investment product that sells for $250. At maturity in 16 years it will be redeemed for $1,000. What approximate annual rate of return does this represent?

A. 9.1%
B. 5%
C. 4.3%

Answer: ______________________

QUESTION 4
If a bond sells at a high premium, then which of the following relationships hold true?

A. Price < par
B. Price > par
C. Price = par

Answer: ______________________

QUESTION 5

A 5 year bond with \$2000 face-value and a 4% coupon rate paid annually has a YTM of 5%. What is the value of each coupon payment made annually?

A. \$80
B. \$8
C. \$4

Answer: ____________________

QUESTION 6

When the market's required rate of return for a particular bond is much less than its coupon rate, the bond is selling at:

A. A premium
B. A discount
C. Face Value

Answer: ____________________

QUESTION 7

You plan to invest \$1000 in an investment product with a stated return of 4% per year with semi-annual compounding. What is the effective annual rate of return?

A. 4%
B. 1.04%
C. 4.04%

Answer: ____________________

QUESTION 8

What is the present value of the following set of cash flows set to be received in the corresponding years:

Year 1: \$1000; Year 2: \$800; Year 3: \$500.
Assume a rate of return of 2%.

A. \$2,000.49
B. \$2,220.49
C. \$2,000.00

Answer: ____________________

QUESTION 9
Company LBR Sdn. Bhd. is considering a capital investment of BND 50 million that will return cash flows of BND 10 million per year for the first 5 years and BND 5 million in the sixth year. If the company's required rate of return is 5%, what is the Net Present Value (NPV) of this investment?

A. BND-$2.97 million
B. BND5 million
C. BND55 million

Answer: ____________________

QUESTION 10
Permanent working capital is represented by which of the following?

A. The difference between the firm's actual level of investment in short-term working capital needs and its permanent working capital requirements
B. The amount that a firm must keep invested in its short-term assets to support its continuing operations.
C. Circumstances in which cash flows are temporarily negative for an unexpected reason.

Answer: ____________________

QUESTION 11
The price of sukuk is calculated by which of the following?

A.
$$P_B = \sum_{t=1}^{T} \frac{C_t}{(1+\frac{YTM}{n})^t} + \frac{C + Par\,Value}{(1+\frac{YTM}{n})^T}$$

B.
$$Par\,Value = \sum_{i=1}^{T} \frac{C_t}{(1+\frac{YTM}{n})^t} + \frac{C + P_B}{(1+\frac{YTM}{n})^T}$$

C.
$$P_B = \sum_{i=1}^{T} \frac{C_t}{(1+YTM)^t} + \frac{C + Par\,Value}{(1+YTM)^T}$$

Answer: ____________________

QUESTION 12

Consider a 2-year sukuk with par value of $100 that pays a coupon of 5% semi-annually with a YTM of 6%. The price of the sukuk is

A. Trading at a discount
B. Trading at a premium
C. Trading at par

Answer: ____________________

QUESTION 13

Consider a risk-free sukuk with a YTM of 3.5%. The YTM of a corporate Sukuk is 4.2%. Calculate the credit risk premium of the corporates Sukuk.

A. 70 basis points
B. 7 basis points
C. 0.7 basis points

Answer: ____________________

QUESTION 14

Private Department of Skh Mohamed Bin Khalid Al Nahyan – LLC ("PD"), rated BB- (stable outlook) by S&P. A Benchmark 3-year USD RegS senior unsecured Sukuk offering, expected to be rated B+ by S&P.

Which of the following contains the most correct information about the above issuance:

A. The issuer is Private Department of Skh Mohamed Bin Khalid Al Nahyan – LLC, with credit rating BB-, is looking to issue a 3 year sukuk
B. The issuer is PD, with credit rating BB-, is looking to issue a 3 year sukuk
C. The issuer is PD, with credit rating B+, is looking to issue a 3 year sukuk

Answer: ____________________

The following information relates to question 15 to 16:

	Company A	Company B	Industry Average
Earnings before interest and taxes	2,550,000	5,250,000	1,400,000
Funds from operations	500,000	650,000	600,000
Interest expense	90,000	260,000	100,000
Total debt	1,900,000	1,700,000	2,600,000
Total capital	3,000,000	9,500,000	6,000,000

QUESTION 15

Which of the following statements is true about the capital structure of Companies A and B?

A. Company A has a lower debt to capital ratio compared to Company B but is lower than the industry average
B. Company A has a higher debt to capital ratio compared to Company B and the industry average
C. Company A has a lower debt to capital ratio compared to Company B but is higher than the industry average

Answer: ____________________

QUESTION 16

Which of the following statements is true about the debt interest coverage of Companies A and B?

A. Both Companies A and B have higher EBIT to interest expense ratio compared to the industry average
B. Company A has a lower EBIT to interest expense ratio compared to company B
C. Company B has a lower EBIT to interest expense ratio compared to Company B and the industry average

Answer: ____________________

QUESTION 17
Which of the following is a type of public debt?

A. Stocks and shares
B. Venture capital
C. Bond

Answer: ______________________

QUESTION 18
Which of the following are elements to consider when analysing companies' credit risks?

A. Profitability, coverage ratios, leverage ratios, retention policies, dividend payout policies
B. Profitability, coverage ratios, leverage ratios, other information such as credit ratings and reports
C. Reputation, stance on political issues, treatment of employees

Answer: ______________________

QUESTION 19
Retained earnings are

A. An indication of a company's liquidity
B. The same as cash in the bank
C. The cumulative earnings of the company after dividends

Answer: ______________________

QUESTION 20
Investments 1 and 2 have the following outlays and patterns of future cash flows are different. The cash flows, as well as the NPV and IRR, for the two investments are shown below. For both investments, the required rate of return is 10%. Which of the following is true based on the general rule between NPV and IRR?

	Cash Flows						
Year	**0**	**1**	**2**	**3**	**4**	**NPV**	**IRR (%)**
Investment 1	−100	30	30	30	30	46.97	33%
Investment 2	−50	0	0	0	150	47.68	32%

A. Invest in Investment 2 as it has a higher NPV
B. Invest in Investment 1 as it has a higher IRR
C. Do not invest in either

Answer: ______________________

QUESTION 21
Which of the following is the correct formula for Weighted Average Cost of Capital (WACC)?

A. $\text{WACC} = w_d r_d (1 - t) + w_e r_e$
B. $\text{WACC} = w_d r_d (t) + w_e r_e$
C. $\text{WACC} = w_d r_d + w_e r_e$

Answer: ______________________

QUESTION 22
Which of the following statements holds true about Working Capital Management?

A. Working capital is a measure of a company's financial debt and obligations.
B. Working capital is a measure of a company's profitability and ability to invest in short term investment projects,
C. Working capital is a measure of a company's financial health and operational efficiency, as it reflects its ability to meet its short-term obligations.

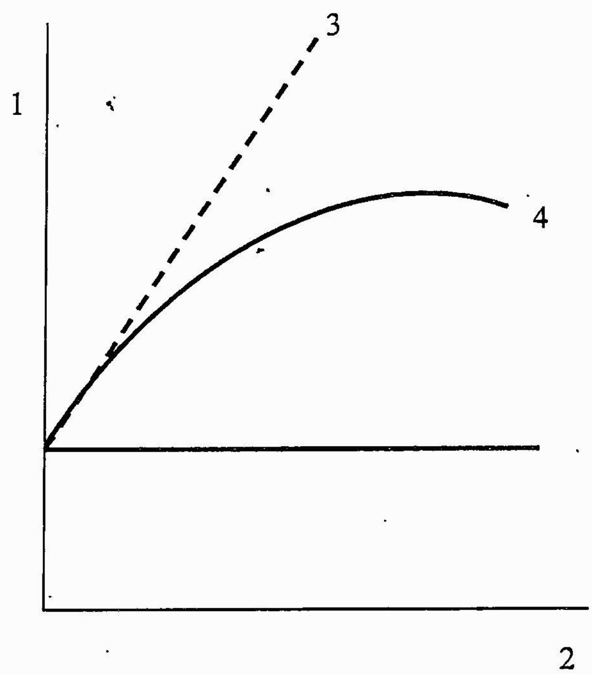
Answer: ______________________

QUESTION 23
The formula for Cash Conversion Cycle (CCC) is

A. CCC = Funds from Operations + Inventory Days – Days Payable Outstanding
B. CCC = Days Sales Outstanding + Inventory Days – Days Payable Outstanding
C. CCC = Days Sales Outstanding + Sales Days – Days Payable Outstanding

Answer: ______________________

QUESTION 24
Which of the following labelling correctly labels the chart elements which corresponds to the trade off theory in deciding the level of debt and value of a firm?



A. 1: Level of debt; 2: Value of firm; 3: Value of levered firm with no financial distress from leverage; 4: Value of levered firm with financial distress from leverage
B. 1: Value of firm; 2: Debt level; 3: Value of unlevered firm; 4: Value of levered firm without financial distress from leverage
C. 1: Value of firm; 2: Debt level; 3: Value of levered firm with no financial distress from leverage; 4: Value of levered firm with financial distress from leverage

Answer: ______________________

QUESTION 25

Which of the following holds true about the relationship between the value of a firm, its free cash flows and weighted average cost of capital?

A. Value increases as free cash flows decreases / weighted average cost of capital decreases
B. Value increases as free cash flows increases / weighted average cost of capital decreases
C. Value decreases as free cash flows increases / weighted average cost of capital decreases

Answer: ______________________

QUESTION 26

Which of the following correctly describes the "matching principle" in short term financial planning?

A. A firm's short-term cash needs should be financed with short-term debt and long-term cash needs should be financed with long-term sources of funds.
B. A firm's short-term cash needs should be financed with long-term debt and long-term cash needs should be financed with long-term sources of funds.
C. Occasionally, a company will encounter circumstances in which cash flows are temporarily negative for an unexpected reason. These situations, which we refer to as negative cashflow shock, can create short-term financing needs.

Answer: ______________________

QUESTION 27

Consider a 5-year sukuk that pays a coupon of 4% annually with a YTM of 5%. If the YTM increases to 6%, the price of the sukuk should

A. Decrease
B. Increase
C. Remain unchanged

Answer: ______________________

QUESTION 28

Assume a firm's interest expense for the year 2017 was USD50 million and the corporate tax rate was 35%. What is the interest tax shield for the firm in year 2017?

A. USD50 million
B. USD17.5 million
C. USD32.5 million

Answer: ______________________

QUESTION 29

Which of the following statements holds true about the general rules on Net Present Value and Internal Rate of Return?

A. Invest if NPV < 0; Invest if IRR < required rate of return
B. Invest if NPV < 0; Invest if IRR > required rate of return
C. Invest if NPV > 0; Invest if IRR > required rate of return

Answer: ____________________

QUESTION 30

The Principal-Agent Problem arises:

A. because managers have little incentive to work in the interest of shareholders when this means working against their own self-interest.
B. because of the separation of ownership and control in a corporation.
C. Both A and B

Answer: ____________________

QUESTION 31

Which group of company stakeholders would be least affected if the firm's financial position weakens?

A. Suppliers
B. Customers
C. Managers and employees

Answer: ____________________

QUESTION 32

______ investing is the umbrella term used to describe investment strategies that incorporate environmental, social, and governance (ESG) factors into their approaches.

A. ESG
B. Sustainable
C. Responsible

Answer: ____________________

QUESTION 33
Which statement correctly describes corporate governance?

A. Corporate governance complies with a set of global standards.
B. Corporate governance is independent of both shareholder theory and stakeholder theory.
C. Corporate governance seeks to minimize and manage conflicting interests between insiders and external shareholders.

Answer: ______________________

QUESTION 34
Which of the following statements is FALSE?

A. If the corporation fails to satisfy debt holders' claims, debt holders may lose control of the firm.
B. Because a corporation is a separate legal entity, when it fails to repay its debts, the people who lent to the firm, the debt holders are entitled to seize the assets of the corporation in compensation for the default.
C. As long as the corporation can satisfy the claims of the debt holders, ownership remains in the hands of the equity holders.

Answer: ______________________

QUESTION 35
A company's profitability for a period would best be evaluated using the:

A. balance sheet.
B. income statement.
C. statement of cash flows.

Answer: ______________________

QUESTION 36
The financial statement that presents a shareholder's residual claim on assets is the:

A. balance sheet.
B. income statement.
C. cash flow statement.

Answer: ______________________

QUESTION 37

For 2020, Flamingo Products had net income of $1,000,000. At 1 January 2020, there were 1,000,000 shares outstanding. On 1 July 2020, the company issued 100,000 new shares for $20 per share. What is Flamingo's basic earnings per share for 2009?

A. $0.80.
B. $0.91.
C. $0.95.

Answer: ______________________

QUESTION 38

For its fiscal year-end, Sublyme Corporation reported net income of $200 million and a weighted average of 50,000,000 common shares outstanding. There are 2,000,000 convertible preferred shares outstanding that paid an annual dividend of $5. Each preferred share is convertible into two shares of the common stock. The diluted EPS is closest to:

A. $3.52.
B. $3.65.
C. $3.70.

Answer: ______________________

QUESTION 39

Which statement is most accurate? A common size income statement:

A. restates each line item of the income statement as a percentage of net income.
B. allows an analyst to conduct cross-sectional analysis by removing the effect of company size.
C. standardizes each line item of the income statement but fails to help an analyst identify differences in companies' strategies.

Answer: ______________________

QUESTION 40

Denali Limited, a manufacturing company, had the following income statement information:

Revenue	$4,000,000
Cost of goods sold	$3,000,000
Other operating expenses	$500,000
Interest expense	$100,000
Tax expense	$120,000

Denali's gross profit is equal to:

A. $280,000.
B. $500,000.
C. $1,000,000.

Answer: ______________________

QUESTION 41

At the beginning of 2022, Glass Manufacturing purchased a new machine for its assembly line at a cost of $600,000. The machine has an estimated useful life of 10. Under the straight-line method, how much depreciation would Glass record in 2023 for financial reporting purposes?

A. $55,000.
B. $60,000.
C. $65,000.

Answer: ______________________

QUESTION 42

Shareholders' equity reported on the balance sheet is most likely to differ from the market value of shareholders' equity because:

A. historical cost basis is used for all assets and liabilities.
B. the balance sheet omits important aspects of a company's ability to generate future cash flows, such as its reputation, management skills and future expansion plans.
C. shareholders' equity reported on the balance sheet is updated continuously.

Answer: ______________________

QUESTION 43

Money received from customers for products to be delivered in the future is recorded as:

A. revenue and an asset.
B. an asset and a liability.
C. revenue and a liability.

Answer: ______________________

QUESTION 44

The item "retained earnings" is a component of:

A. assets.
B. liabilities.
C. shareholder's equity.

Answer: ______________________

QUESTION 45

Which of the following would an analyst most likely be able to determine from a common-size analysis of a company's balance sheet over several periods?

A. An increase or decrease in sales.
B. An increase or decrease in financial leverage.
C. How profitable a company is over time.

Answer: ______________________

QUESTION 46

An investor concerned whether a company can meet its near-term obligations is most likely to calculate the:

A. current ratio.
B. payables turnover
C. gross profit margin.

Answer: ______________________

QUESTION 47
An investor worried about a company's long-term solvency would most likely examine its:

A. quick ratio.
B. return on total assets.
C. debt to equity ratio.

Answer: ______________________

QUESTION 48
An analyst compiles the following data for a company:

	FY19	FY20	FY21
ROE	19.8%	20.0%	22.0%
Return on total assets	8.1%	8.0%	7.9%
Total asset turnover	2.0	2.0	2.1

Based only on the information above, the most appropriate conclusion is that, over the period FY19 to FY21, the company's:

A. net profit margin and financial leverage have decreased.
B. net profit margin and financial leverage have increased.
C. net profit margin has decreased but its financial leverage has increased

Answer: ______________________

The following information relates to questions 49 to 51:

Exhibit 1: Common-Size Balance Sheets for Company A, Company B, and Sector Average

	Company A	**Company B**	**Sector Average**
ASSETS			
Current assets	5	5	7
Cash and cash equivalents	5	0	2
Marketable securities	5	15	12
Accounts receivable, net	15	20	16
Inventories	5	15	11
Prepaid expenses	35	55	48
Total current assets	40	35	37
Property, plant, equipment	25	0	8
Goodwill	0	10	7
Other assets	100	100	100
Total assets	5	5	7
LIABILITIES AND SHAREHOLDERS' EQUITY			
Current liabilities			
Accounts payable	10	10	10
Short-term debt	25	10	15
Accrued expenses	0	5	3
Total current liabilities	35	25	28
Long-term debt	45	20	28
Other non-current liabilities	0	10	7
Total liabilities	80	55	63
Total shareholders' equity	20	45	37
Total liabilities and shareholders' equity	100	100	100

<u>QUESTION 49</u>

The quick ratio for Company A is closest to:

A. 0.43.
B. 0.57.
C. 1.00.

Answer: ______________________

QUESTION 50
Based on Exhibit 1, the financial leverage ratio for Company B is closest to:

A. 0.55.
B. 1.22.
C. 2.22.

Answer: ______________________

QUESTION 51
Based on Exhibit 1, which ratio indicates lower liquidity risk for Company A compared with Company B?

A. Cash ratio
B. Quick ratio
C. Current ratio

Answer: ______________________

QUESTION 52
The three major classifications of activities in a cash flow statement are:

A. inflows, outflows, and net flows.
B. operating, investing, and financing.
C. revenues, expenses, and net income.

Answer: ______________________

QUESTION 53
Based on the following information for Star Inc., what are the total net adjustments that the company would make to net income in order to derive operating cash flow?

Income Statement Item		12/31/2018	
Net income		$20 million	
Depreciation		$2 million	
Balance Sheet Item	**12/31/2017**	**12/31/2018**	**Change**
Accounts receivable	$25 million	$22 million	($3 million)
Inventory	$10 million	$14 million	$4 million
Accounts payable	$8 million	$13 million	$5 million

A. Add $2 million.
B. Add $6 million.
C. Subtract $6 million.

Answer: ____________________

QUESTION 54
An analyst is conducting a valuation analysis of Frontier Corporation and has gathered the following information on Frontier Corporation:

	Current Year ($)	Forecasted for Next Year ($)
Book value of debt	50	50
Market value of debt	62	63
Book value of equity	55	58
Market value equity	210	220

The weights that the analyst should apply in estimating Frontier's cost of capital for debt and equity are, respectively:

A. $w_d = 0.200$ and $w_e = 0.800$.
B. $w_d = 0.185$ and $w_e = 0.815$.
C. $w_d = 0.223$ and $w_e = 0.777$.

Answer: ____________________

QUESTION 55

An analyst assembles the following facts concerning a company's component costs of capital and capital structure.

	%
Cost of equity based on the CAPM	15.60
Pretax cost of debt	8.28
Corporate tax rate	30.00
Capital structure weight	Equity 80%, Debt 20%

Based on the information given, the company's WACC is closest to:

A. 12.64%.
B. 13.64%.
C. 13.10%.

Answer: ____________________

QUESTION 56

An analyst's data source shows that Newmont Mining (NEM) has an estimated beta of –0.2. The risk-free rate of return is 2.5%, and the equity risk premium is estimated to be 4.5%. Using the CAPM, the required rate of return for investors in NEM is closest to:

A. 1.6%.
B. 3.4%
C. 1.2%

Answer: ____________________

QUESTION 57

An analyst estimates the intrinsic value of a stock to be in the range of €17.85 to €21.45. The current market price of the stock is €24.35. This stock is most likely:

A. overvalued.
B. undervalued.
C. fairly valued.

Answer: ____________________

QUESTION 58

Babu's Corporation has just paid a dividend of $1.75 per share. If the required rate of return is 12:3% per year and dividends are expected to grow indefinitely at a constant rate of 9.2% per year, the intrinsic value of Babu's Corporation is closest to:

A. $15.54.
B. $56.45.
C. $61.65.

Answer: ______________________

QUESTION 59

An analyst gathers the following information about similar companies in the banking sector:

	First Bank	Prime Bank	Pioneer Trust
P/B	1.10	0.60	0.60
P/E	8.40	11.10	8.30

Which of the companies is most likely to be undervalued?

A. First Bank.
B. Prime Bank.
C. Pioneer Trust.

Answer: ______________________

QUESTION 60

An analyst has determined that the appropriate EV/EBITDA for Rainbow Company is 10.2. The analyst has also collected the following forecasted information for Rainbow Company:

EBITDA = $22,000,000
Market value of debt = $56,000,000
Cash = $1,500,000

The value of equity for Rainbow Company is closest to:

A. $169 million.
B. $224 million.
C. $281 million.

Answer: ______________________

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