

Course No:
Course Title: Advanced Financial
Management
Date: 16/11/2011
No. of Questions: (4)
Time: 1 hour
Using Calculator (Yes)

University of Palestine



Midterm Exam.
First Semester 2011
Total Grade: 20

Instructor Name: Yousef El-Mudallal
Student No.: _____
Student Name: _____
College Name: _____
Dep. / Specialist: _____
Using Dictionary (No)

Answer the following five questions:

Q.1 : True or False

3 marks

- 1- Under a relaxed working capital policy, a firm would hold relatively small amounts of each type of current asset ()
- 2- A security's beta measures its nondiversifiable (or market) risk relative to that of most other securities ()
- 3- Net working capital is defined as current assets divided by current liabilities ()
- 4- Capital can be defined as the funds supplied by investors ()
- 5- The cost of common stock is the rate of return stockholders require on the firm's common stock. ()
- 6- Portfolio diversification reduces the variability of the returns on each security held in the portfolio()

Q.2 : Choose the correct answer

4 marks

- 1- Inflation, recession, and high interest rates are economic events which are characterized as
 - a. Company-specific risk that can be diversified away.
 - b. Market risk.
 - c. Systematic risk that can be diversified away.
 - d. Diversifiable risk.
 - 2- The common stock of Anthony Steel has a beta of 1.20. The risk-free rate is 5 percent and the market risk premium ($r_M - r_{RF}$) is 6 percent. What is the company's cost of common stock, r_s ?
 - a. 7.0%
 - b. 7.2%
 - c. 11.0%
 - d. 12.2%
 - 3- Bouchard Company's stock sells for \$20 per share, its last dividend (D_0) was \$1.00, and its growth rate is a constant 6 percent. What is its cost of common stock, r_s ?
 - a. 5.0%
 - b. 5.3%
 - c. 11.0%
 - d. 11.3%
1. Helena Furnishings wants to sharply reduce its cash conversion cycle. Which of the following steps would reduce its cash conversion cycle?
 - a. The company increases its average inventory without increasing its sales.
 - b. The company reduces its DSO.

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- c. The company starts paying its bills sooner, which reduces its average accounts payable without reducing its sales.
- d. Statements a and b are correct.

Q.3: Essay questions: Answer the following questions

6 marks

1. Define the following terms :
 - a. Security Market Line (SML); SML equation
 - b. Risk aversion
 - c. Working capital policy
2. Speak briefly about working capital Investment policies (Explain with drawing).
3. Spartan Sporting Goods has \$5 million in inventory and \$2 million in accounts receivable. Its average daily sales are \$100,000. The company's payables deferral period (accounts payable divided by daily purchases) is 30 days. What is the length of the company's cash conversion cycle?

Q.4: Mini cases: Answer the following questions

8 marks

1. Suppose you are the money manager of \$4 million investment fund. The fund consist of 4 stocks with the following investments and betas

| Stock | Investment | Beta |
|-------|------------|------|
| A | \$400,000 | 1.5 |
| B | 600,000 | 0.50 |
| C | 1,000,000 | 1.25 |
| D | 2,000,000 | 0.75 |

If the market required rate of return is 14% and the risk-free rate is 6%, what is the Funds required rate of return?

2. The Christie Corporation is trying to determine the effect of its inventory turnover ratio and days sales outstanding (DSO) on its cash flow cycle. Christie's 2002 sales (all on credit) were \$150,000. It turned over its inventory 5 times during the year, and its DSO was 36.5 days. Christie's payables deferral period is 40 days.
 - a. Calculate Christie's cash conversion cycle.
 - b. Suppose Christie's managers believe that the inventory turnover can be raised to 7.3 times. What would Christie's cash conversion cycle have been if the inventory turnover had been 7.3 for 2002?

Good Luck