Course No: **Course Title: Advanced Financial Management** **Date: 18 /08/2011** **No. of Questions: (5)** **Time: 2 hours** **Using Calculator (Yes)**	**University of Palestine** **End Exam.** **Summer Semester 2011** **Total Grade: 60**	**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 **10 marks**

1- The credit period is the amount of time it takes to do a credit search on a potential customer ( )
2- If a company increases its safety stock, then its average inventory will go up( )
3- Portfolio diversification reduces the variability of the returns on each security held in the portfolio ( )
4- If a company increases its safety stock, then its EOQ will go up ( )
5- The opportunity cost of the capital tied up in the inventory is part of the carrying cost ( ) .
6- According to *Bird-in-the-Hand* Theory Investors think dividends are less risky than potential future capital gains, hence they like dividends ( )
7- The cash conversion cycle can be shortened by reducing the inventory conversion period by processing and selling goods more quickly ( )
8- The primary objective of the firm should be shareholder wealth maximization, which translates to maximizing stock price ( )
9- Market risk is that part of a security's stand-alone risk that can be eliminated by diversification ( )
10- According to Tax preference Theory, Investors prefer a high payout( )

Q.2 : Choose the correct answer **10 marks**

1- The economic ordering quantity will rise due to an increase in which of the following variable(s)?
   a. Product demand (sales).
   b. Carrying costs.
   c. Ordering costs.
   d. Both a and c

The Norris Company is trying to determine its optimal average cash balance. The firm has determined that it will need $5,000,000 net new cash during the coming year. The fixed transaction cost of converting securities to cash is $50, and the firm earns 10 percent on its marketable securities investments.

2- According to the Baumol model, what is the optimal transaction size for transfers from marketable securities to cash?
   a. $ 7,071
   b. $ 38,357
   c. $ 70,711
   d. $102,956

3- According to the Baumol model, what should be Norris' average cash balance?
   a. $35,356
   b. $ 3,536
   c. $22,157
   d. $70,711

4- What will be the total cost to Norris of maintaining the optimal average cash balance, as determined by the Baumol model?
   a. $35,356
   b. $ 7,071
   c. $18,493
   d. $70,711

5- If receivables are $657,534 and sales are $10 million, the receivables collection period is:-
   a. 28 Days
   b. 65 Days
   c. 24 Days
   d. 15 Days

Q.3: Answer the following questions **15 marks**

1. Define the following terms :
   a. Dividend Irrelevance Theory
   b. Risk aversion
   c. Capital Asset Pricing Model
2. What's the "*residual distribution model*"?
3. What are the reasons for holding cash
4. What are the four elements of a firm's credit policy? To what extent can firms set their own credit policies as opposed to accepting policies that are dictated by its competitors?

Q.4: Answer the following question **20 marks**

1- Berkeley Prints expects to have sales this year of $15 million under its current credit policy. The present terms are net 30; the days dales outstanding (DSO) is 60 days; and the bad debt loss percentage is 5 percent. Also, Berkeley's cost of capital is 15 percent, and its variable costs total 60 percent of sales. Since Berkeley wants to improve its profitability, a proposal has been made to offer a 2 percent discount for payment within 10 days; that is, change the credit terms to 2/10, net 30. The consultants predict that sales would increase by $500,000, and that 50 percent of all customers would take the discount. The new DSO would be 30 days, and the bad debt loss percentage on all sales would fall to 4 percent.

Should the company change the credit policy?

2- First National Bank of Micanopy has offered you the following loan alternatives in response to your request for a $75,000, 1-year loan.

Alternative 1: 7 percent simple interest, with interest paid monthly.

Alternative 2 7 percent simple interest, with interest paid monthly.

Alternative 3: 7 percent discount interest, with a 10 percent compensating balance.

What is the effective annual rate on each alternative?

Good Luck