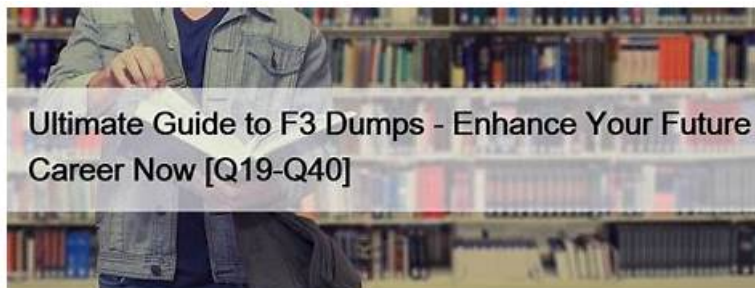


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CIMA F3 Financial Strategy Sample Questions (Q280-Q285):

NEW QUESTION # 280

Company WWW is considering making a takeover bid for Company KKA Company KKA's current share price is \$5.00
Company WWW is considering either

" A cash payment of \$5.75 for each share in Company KKA

" A 5 year corporate bond with a market value of \$90 in exchange for 15 shares in Company KKA Calculate the highest percentage premium which Company KKA shareholders will receive.

- A. Corporate bond premium = 20%
- B. Corporate bond premium = 80%
- C. Cash premium = 15%
- D. Cash premium = 10%

Answer: A

Explanation:

Current KKA share price = \$5.00

Cash offer: \$5.75 per share

Premium = $(5.75 - 5.00) / 5.00 = 0.75 / 5 = 15\%$

Bond offer: market value \$90 bond for 15 KKA shares

Value per KKA share = $90 / 15 = \$6.00$

Premium = $(6.00 - 5.00) / 5.00 = 1 / 5 = 20\%$

The highest premium is therefore 20% on the bond offer, i.e. option B.

NEW QUESTION # 281

A company has 6 million shares in issue. Each share has a market value of \$4.00.

\$9 million is to be raised using a rights issue.

Two directors disagree on the discount to be offered when the new shares are issued.

* Director A proposes a discount of 25%

* Director B proposes a discount of 30%

Which THREE of the following statements are most likely to be correct?

- A. More shares will be issued under Director B's proposal than under Director A's proposal.
- B. The terms of the rights issue will be one new share for every two existing shares under Director A's proposal.
- C. Shareholder wealth will be higher under Director A's proposal than under Director B's proposal.
- D. The theoretical ex-rights price will be higher under Director B's proposal than under Director A's proposal.
- E. The rights issue price will be \$3.00 under Director A's proposal.

Answer: A,B,E

Explanation:

Common data

Existing shares = 6 million

Current share price = \$4.00

Funds to raise = \$9 million

Director A - 25% discount

Rights issue price:

$$4.00 \times (1 - 0.25) = 4.00 \times 0.75 = \$3.00$$

So C is correct ("The rights issue price will be \$3.00 under Director A's proposal.") Number of new shares:

$$\frac{9 \text{ million}}{3.00} = 3 \text{ million shares}$$

After issue, total shares = 6m + 3m = 9m. To issue 3m against 6m existing, the terms are:

Director B - 30% discount

Rights issue price:

$$4.00 \times (1 - 0.30) = 4.00 \times 0.70 = \$2.80$$

Number of new shares:

$$\frac{9 \text{ million}}{2.80} \approx 3.214 \text{ million}$$

This is more shares than under Director A's proposal (3.214m > 3m), so B is correct. Because the total post-issue value is the same (\$24m existing + \$9m new cash), but Director B issues more shares, the TERP under B will be lower, not higher - so A is false. Total shareholder wealth is the same in theory (ignoring costs and signalling), so E is also false.

Correct statements: B, C, D.

NEW QUESTION # 282

Company R is a major food retailer. It wishes to acquire Company S, a food manufacturer.

Company S currently supplies many stores owned by Company R with food products that it manufactures.

Company S is of similar size to Company R but has a lower credit rating.

Which of the following is most likely to be a synergistic benefit to R on purchasing S?

- A. Lower cost of borrowing due to the acquisition of a company with a different credit rating.
- B. Reduced competition resulting in the ability to raise retail selling prices for food products.
- C. Cost savings due to reducing the range of products manufactured by Company S.
- D. Savings due to a reduction in purchase costs and more control over the value chain.

Answer: D

Explanation:

R is a retailer; S is its supplier (manufacturer). The classic vertical-integration synergy is lower purchase costs and better value-chain control.

NEW QUESTION # 283

Company A is based in Country A where the functional currency is the A\$. Currently all sales are to domestic customers in Country A. However, the company is planning to expand internationally by acquiring Company B, a distribution company in Country B, to enable it to sell goods worldwide. The functional currency of Country B is the B\$. Company A will invoice its international customers in their local currency.

Wage increases in Country B are forecast to be modest, due to high unemployment levels, but overall inflation in Country B is forecast to be significantly higher than in Country A. Which TWO of the following statements about the economic risk of the acquisition of Company B are true?

- A. Using purchasing power parity, AS is forecast to strengthen against B\$, so the economic risk can be ignored
- B. Financing this acquisition with block denominated in B\$ will reduce economic risk.
- C. Higher inflation will increase the project's BS returns, so the economic risk can be ignored
- D. Economic risk can be eliminated by using forward contracts to convert future cash flows into A\$
- E. Exporting into a variety of international markets will reduce economic risk.

Answer: E

NEW QUESTION # 284

Company T is a listed company in the retail sector.

Its current profit before interest and taxation is \$5 million.

This level of profit is forecast to be maintainable in future.

Company T has a 10% corporate bond in issue with a nominal value of \$10 million.

This currently trades at 90% of its nominal value.

Corporate tax is paid at 20%.

The following information is available:

Which of the following is a reasonable expectation of the equity value in the event of an attempted takeover?

- A. \$41.6 million
- B. \$32.0 million
- C. \$65.0 million
- D. \$50.2 million

Answer: A

NEW QUESTION # 285

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