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CIMA F3 Financial Strategy Sample Questions (Q44-Q49):

NEW QUESTION #44
A company's Board of Directors is assessing the likely cost of financing future new projects using either equity or debt. The directors are uncertain of the effects on key variables. Which THREE of the following statements are true?

- A. Retained earnings have no risk, and is therefore the lowest form of equity finance
- B. Equity finance will reduce the overall financial risk
- C. Debt finance has a higher cost than equity finance
- D. Equity finance will increase returns to a higher total future dividends
- E. Debt finance is always preferable to equity finance
- F. The choice between using either equity or debt will have no impact on the amount of corporate income tax payable

Answer: B,C,D

NEW QUESTION #45
An oil equity finance company plans an issue of new ordinary shares to the general public to raise £10 million in total proceeds. The following data applies:
• 10 million ordinary shares are currently in issue with a market value of £5 each share
• The current share price is £5.20 million and is expected to give a positive NPV of £5 million
• The issue will be priced at a 10% discount to the current share price
What gain or loss per share will accrue to the existing shareholders?

- A. Gain of £0.08
- B. Loss of £0.08
- C. Gain of £1.18
- D. Loss of £0.92

Answer: A

NEW QUESTION #46
A company has 1% convertible bonds in issue. The bonds are convertible in 5 years time at a value of 20 ordinary shares per £100 nominal value bond.
Each share

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CIMA F3 Financial Strategy Sample Questions (Q68-Q73):

NEW QUESTION # 68

Company A plans to acquire Company B, an unlisted company which has been in business for 3 years.

It has incurred losses in its first 3 years but is expected to become highly profitable in the near future.

No listed companies in the country operate the same business field as Company B, a unique new high- risk business process.

The future success of the process and hence the future growth rate in earnings and dividends is difficult to determine.

Company A is assessing the validity of using the dividend growth method to value Company B.

Which THREE of the following are weaknesses of using the dividend growth model to value an unlisted company such as Company B?

- A. The cost of capital will be difficult to estimate.
- B. The future projected dividend stream is used as the basis for the valuation.
- C. The company has been unprofitable to date and hence, there is no established dividend payment pattern.
- D. The future growth rate in earnings and dividends will be difficult to accurately determine.
- E. The dividend growth model does not take the time value of money into consideration.

Answer: A,C,D

NEW QUESTION # 69

At the last financial year end, 31 December 20X1, a company reported:

□ The corporate income tax rate is 30% and the bank borrowings are subject to an interest cover covenant of 4 times.

The results are presently comfortably within the interest cover covenant as they show interest cover of 8.3 times. The company plans to invest in a new product line which is not expected to affect profit in the first year but will require additional borrowings of \$20 million at an annual interest rate of 10%.

What is the likely impact on the existing interest cover covenant?

- A. Interest cover would reduce to 3 times and the covenant would NOT be breached.
- B. Interest cover would reduce to 5 times and the covenant would be breached.
- C. Interest cover would reduce to 3 times and the covenant would be breached.
- D. Interest cover would reduce to 5 times and the covenant would NOT be breached.

Answer: D

NEW QUESTION # 70

Company BBB has prepared a valuation of a competitor company, Company BBD. Company BBB is intending to acquire a controlling interest in the equity of Company BBD and therefore wants to value only the equity of Company BBD.

□ The directors of Company BBB have prepared the following valuation of Company BBD:

Value of Equity = $4.63 + 5.14 + 5.56 = \$15.33$ million

Additional information on Company BBD:

□ Which THREE of the following are weaknesses of the above valuation?

- A. The valuation is overstated as the directors have failed to deduct tax from the free cash flows.

- B. The valuation is understated as forecast future growth has been ignored beyond year 3.
- C. The valuation is understated as the directors have failed to include a perpetuity factor in the calculations.
- D. The approach used calculates the value of the total entity not the value of equity.
- E. Free cash flows to all investors should be discounted at the cost of equity of 10% rather than WACC of 8%.

Answer: A,C,D

NEW QUESTION # 71

Company U has made a bid for the entire share capital of Company B.

Company U is offering the shareholders in Company B the option of either a share exchange or a cash alternative.

Advise the shareholders in Company B which THREE of the following would be considered disadvantages of accepting the cash consideration?

- A. Cash consideration is certain whereas Company U's future share price performance is uncertain.
- B. There will be no opportunity to participate in the future economic success of Company U.
- C. Company U is not expected to change its dividend policy post-acquisition.
- D. Taxation is payable on realised capital gains.
- E. Interest rates on deposit accounts are currently at a historic low and are expected to remain low.

Answer: B,D,E

Explanation:

B). Low deposit interest rates - cash received will likely earn poor returns compared with equity.

D). Taxation on realised capital gains - cash offer crystallises a disposal now, potentially triggering CGT.

E). No opportunity to participate in Company U's future success - once they take cash, they no longer share in upside from post-acquisition performance.

Option A is actually an advantage of cash (certainty), and C relates to the dividend policy if they take shares, not a disadvantage of cash itself.

NEW QUESTION # 72

Company A is based in country A with the AS as its functional currency. It expects to receive BS20 million from Company B in settlement of an export invoice.

The current exchange rate is A\$1 =B\$2 and the daily standard deviation of this exchange rate = 0 5%

What is the one-day 95% VaR in AS?

- A. A\$50,000
- B. A\$82,250
- C. A\$822,500
- D. A\$164,500

Answer: B

NEW QUESTION # 73

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