

CPA

Exam FIN

Finance

Version: 6.0

[Total Questions: 80]

Question No : 1

It has been claimed that the weighted average cost of capital (WACC) should only be used to evaluate investment decisions, involving discounted cash flow calculations, where:

1. The proposed project does not alter the business risk profile of the business.
2. The WACC reflects the long-term capital structure of the business.

Which ONE of the following combinations (true/false) is correct?

- A. Statement 1 = True, Statement 2 = True
- B. Statement 1 = True, Statement 2 = False
- C. Statement 1 = False, Statement 2 = True
- D. Statement 1 = False, Statement 2 = False

Answer: A

Question No : 2

Consider the following two statements concerning convertible loan notes:

1. A business will aim to issue convertible loan notes with the lowest possible conversion premium.
2. Convertible loan notes normally have a higher coupon rate of interest than non-convertible loan notes.

Which ONE of the following combinations (true/false) is correct?

- A. Statement 1 = True, Statement 2 = True
- B. Statement 1 = True, Statement 2 = False
- C. Statement 1 = False, Statement 2 = True
- D. Statement 1 = False, Statement 2 = False

Answer: D

Question No : 3

Consider the following statements concerning the efficient market hypothesis:

1. When markets demonstrate semi-strong form efficiency, share prices will react to publicly-available information about the future prospects of a business.
2. When markets demonstrate weak form efficiency, there is no connection between past share price movements and future share price movements.

Which of the following combinations (true/false) is correct?

- A. Statement 1 = True, Statement 2 = True
- B. Statement 1 = True, Statement 2 = False
- C. Statement 1 = False, Statement 2 = True
- D. Statement 1 = False, Statement 2 = False

Answer: A

Question No : 4

Com Ltd has multiple operations around the world. Com Ltd consider following hedging methods in its operation:

1. International diversification of operations
2. Matching assets and liabilities
3. Leading and lagging
4. Money market hedge

Which TWO of the hedging methods are suitable for minimizing economic exposure of Com Ltd?

- A. 1 and 2
- B. 1 and 4
- C. 2 and 3
- D. 3 and 4

Answer: A

Question No : 5

Which of the following statements are correct regarding the Modigliani and Miller (no taxes) proposition?

As the level of capital gearing increases from zero:

1. The cost of equity capital will increase
2. The cost of debt capital will remain unchanged
3. The value of the business will decrease
4. The weighted average cost of capital will increase

- A. 1 and 2
- B. 1 and 3
- C. 2 and 4
- D. 3 and 4

Answer: A

Question No : 6

Company X pays an annual cash return to shareholders of 40 cents per share and this is expected to continue in perpetuity. The risk-free rate of return is 6% and the current average market rate of return is 10%. Company X's coefficient is 1.1.

What is the expected return from Company X, and what would be the predicted market value of company's shares?

- A. Expected return 14.4%, Predicted value 278 cents
- B. Expected return 10.4%, Predicted value 385 cents
- C. Expected return 10.6%, Predicted value 377 cents
- D. Expected return 61%, Predicted value 66 cents

Answer: B

Question No : 7

A business is considering various investment projects, with each expected to have an initial cash outflow followed by positive cash inflows over the rest of its life. The operations

director has stated that the net present value and internal rate of return methods will, if correctly applied to each individual project, always give projects with the same characteristics:

1. Accept or reject decision for individual projects
2. Priority ranking for those projects that are acceptable

Which of the following combinations (true/false) is correct?

- A. Statement 1 = True, Statement 2 = True
- B. Statement 1 = True, Statement 2 = False
- C. Statement 1 = False, Statement 2 = True
- D. Statement 1 = False, Statement 2 = False

Answer: A

Question No : 8

Consider the following statements concerning financial options:

1. The time value of an option is the value assigned to the possibility that the price of the underlying item will move infavorof the option writer.
2. The time value of an option less its intrinsic value is equal to the option premium.

Which ONE of the following combinations (true/false) concerning the above statements is correct?

- A. Statement 1 = True, Statement 2 = True
- B. Statement 1 = True, Statement 2 = False
- C. Statement 1 = False, Statement 2 = True
- D. Statement 1 = False, Statement 2 = False

Answer: D

Question No : 9

Where there is capital rationing, the profitability index (PI) may be used to rank investment projects with a positive net present value. It has been claimed that using the PI is

appropriate only when:

- 1) Capital rationing is for a single period.
- 2) The investment projects are indivisible.

Which ONE of the following combinations (true/false) is correct?

- A. Statement 1 = True, Statement 2 = True
- B. Statement 1 = True, Statement 2 = False
- C. Statement 1 = False, Statement 2 = True
- D. Statement 1 = False, Statement 2 = False

Answer: B

Question No : 10

Aralia Co and Corylus Co both pay a constant dividend of \$0.30 per share. Aralia Co has a beta of 1.2 and Corylus Co has a beta of 0.9. The market share price of Aralia Co is \$3.70 and the market share price of Corylus Co is \$3.80.

The market rate of return is 8% and the risk free rate is 5%.

Based on the Capital Asset Pricing Model (CAPM) analysis, which ONE of the following combinations (underpriced/overpriced) concerning the market price of the shares of Aralia Co and Corylus Co is correct?

- A. Aralia Co = Overpriced, Corylus Co = Overpriced
- B. Aralia Co = Overpriced, Corylus Co = Underpriced
- C. Aralia Co = Underpriced, Corylus Co = Overpriced
- D. Aralia Co = Underpriced, Corylus Co = Underpriced

Answer: B

Question No : 11

The shares of Derwent Co and Plym Co have beta values of 0.5 and 1.2 respectively. The expected rate of return for Derwent Co investors is 9% and the expected return to the market is 12%. Using the Capital Asset Pricing Model, what is the expected rate of return

for investors in Plym Co?

- A. 7.2%
- B. 10.8%
- C. 13.2%
- D. 21.6%

Answer: C

Question No : 12

Which ONE of the following statements concerning the issue of shares is correct?

- A. A placing of shares involves an offer of shares to selected investors rather than to the general public
- B. An offer for sale is an invitation to the general public to subscribe for shares not yet in issue
- C. An offer for subscription is an invitation to the general public to subscribe for shares already in issue
- D. A bonus issue raises finance through an offer of shares to existing shareholders

Answer: A

Question No : 13

Aludra Co has \$450 million loan notes in issue that pay an annual fixed rate of interest of 6.3%. The directors of the company have recently decided to change this fixed rate for a floating rate of interest. A bank has offered a swap agreement whereby the bank pays a fixed rate of interest of 5.8% and receives LIBOR in return.

Assuming LIBOR is 5.4% for the first year of the swap agreement, what will be the percentage borrowing cost for Aludra Co?

- A. 6.7%
- B. 5.9%
- C. 5.8%
- D. 5.4%

Answer: B