



AUM

American University Of The Middle East

Summer 2020 – Final Assessment – (20%)

FIN300 – Managerial Finance

Name	ID

SECTION [1] Problem Solving [60 marks]

Problem 1 (12 marks)

Consider the following two potential investments Nexit and Rexit. You plan to invest 8,000 KD in investment Nexit and 12,000 KD in investment Rexit.

Date	Return Nexit	Return Rexit
2016	0.03	-0.04
2017	-0.05	0.08
2018	0.08	0.07
2019	0.12	0.13

- a. Build a portfolio consisting of Nexit and Rexit based on the information above.
- b. Calculate the average return of the portfolio.
- c. Calculate the risk of the portfolio.

Problem 2 (12 marks)

SAGE Enterprises just paid a dividend of \$2 per share. The current market price is \$50 per share. Dividends are expected to grow at a constant rate “g”. The risk-free rate is equal to 3% and the share risk premium is equal to 5%.

- a. Calculate the growth rate of dividends “g”.
- b. Estimate the price of the share 5 years from today.

Problem 3 (12 marks)

CAPITAL Partners has a beta of 1.1. The 3-month Treasury bill rate is 3%. The market risk premium is equal to 6%. The company wishes to fund a project through shares and bonds. 35% of funding came from bonds and the rest from shares. The marginal tax rate is equal to 15%. The yield to maturity on the bonds is equal to 7%.

- a. Calculate the required rate of return on shares.
- b. Calculate the Weighted Average Cost of Capital (WACC) of the firm.

Problem 4 (12 marks)

Consider the following two projects and their respective cash flows. The WACC is equal to 10%.

Time	0	1	2	3	4
Project A	-10,000	3,000	5,000	4,000	-3,000
Project B	-11,000	5,000	4,000	-3,000	3,000

- a. Calculate the NPV of each project.
- b. Which project would you choose if A and B are mutually exclusive?

Problem 5 (12 marks)

Consider a company that just paid a dividend a \$3 per share. The dividends are expected to grow at the rate of 8% per year for the next 3 years and then at 4% thereafter.

- a. Draw the timeline for the first 6 years.
- b. Calculate the expected dividends for the next five years.



AUM

American University Of The Middle East

SECTION [2] Short-answer questions [40 marks]

Question 1 (5 marks)

What is a non-diversifiable risk?

Question 2 (5 marks)

What is the type of risk that can be eliminated by diversification?

Question 3 (5 marks)

Briefly describe the concept of a tracking share.

Question 4 (5 marks)

Why is it assumed that dividends could grow in the future?

Question 5 (5 marks)

What are the major sources of funds for large corporations?

Question 6 (5 marks)

Why does a lower cost of capital serve as an incentive to invest more?

Question 7 (5 marks)

What is the decision rule of the IRR method?

Question 8 (5 marks)

What are the limitations of the payback period?