The Institute of
Bankers Pakistan

IBP Superior Qualification
Summer 2023

Time Allowed: 3 Hours | **Maximum Marks: 100**

Financial Planning and Budgeting

Date: June 22, 2022 | **AIBP (Core Subject)** | **Roll No:**

Instructions:

i. Attempt ALL questions;
ii. Answers must be neat, relevant and brief;
iii. In checking the answers, the examiner takes into account clarity of exposition, logic of arguments, presentation and language;
iv. Read the instructions printed inside the top cover of answer script CAREFULLY before attempting the paper;
v. DO NOT write your Name, Access No. or Roll No. etc. anywhere inside the answer script(s);
vi. Candidates are advised not to mark any of the objective answer on the Question Paper, otherwise their paper will be cancelled;
vii. Question Paper must be returned to invigilator before leaving the examination hall;
viii. Ensure that you shade your choice on the Optical Mark Reader sheet correctly. Only **ONE** circle must be shaded as shown below:

Correct way A ● C D **(Choice B is selected)**

Incorrect ways A B C D

SECTION B: SUBJECTIVE

Attempt ALL Questions. **(40 Marks)**

Q2.

A. A company has a high inventory turnover ratio but a low gross profit margin ratio. How can this be possible, and what does it indicate about the company's financial performance? **(04 marks)**

B. A company has a debt-to-equity ratio of 1.5 and an interest coverage ratio of 3. The company decides to take on additional debt at the same interest rate as of previous debt, which increases its debt-to-equity ratio to 2.5. Calculate the new interest coverage ratio assuming there is no change in the profitability of the company other than the debt and its interest and analyze what the result indicates about the company's financial risk. **(05 marks)**

Q3. Extracts from the recent financial statements of Blue Ltd are given below.

	Rs. In '000
Revenue	21,300
Cost of sales	16,400
Gross profit	4,900

	Rs. In '000		Rs. In '000
		Equity	
Non-Current Assets	3,000	Ordinary shares	1,000
		Reserves	1,000
Current Assets		Non-current liabilities - bonds	3,000
Inventory	4,500	Current liabilities	
Trade Receivables	3,500	Trade payable	3,000
		Over drafts	3,000
Total assets	11,000	Total equity and liabilities	11,000

A factor has offered to manage the trade receivables of Blue Ltd. in a servicing and factor-financing agreement. The factor expects to reduce the average trade receivables period of Blue Ltd from its current level to 35 days; to reduce bad debts from 0.9% of revenue to 0.6% of revenue; and to save Blue Ltd. Rs. 40,000 per year in administration costs.
The factor would also make an advance to Blue Ltd of 80% of the revised book value of trade receivables. The interest rate on the advance would be 2% higher than the 7% that Blue Ltd. currently pays on its overdraft. The factor would charge a fee of 0.75% of revenue on a with-recourse basis, or a fee of 1.25% of revenue on a non-recourse basis. Assume that there are 365 working days in each year and that all sales and supplies are on credit.

Required:

A. Calculate the current cash operating cycle of Blue Ltd. **(4 marks)**

B. Calculate the value of the factor's offer on a with-recourse basis **(4 marks)**

Q4. The equity beta of Fortune Ltd. is 0.9 and the company has issued 10 million ordinary shares. The market value of each ordinary share is Rs 7.50. The company is also financed by 7% bonds with a nominal value of Rs. 100 per bond, which will be redeemed in seven years' time at nominal value. The bonds have a total nominal value of Rs. 14 million. Interest on the bonds has just been paid and the current market value of each bond is Rs. 107.14. The risk-free rate of return is 4% per year and the average return on the stock market is 11% per year. Fortune Ltd pay corporation tax at the rate of 20% per year.

Required:

Calculate the current weighted average cost of capital of Fortune Ltd. **(06 marks)**

Q5. Discuss any **seven** factors which influence the decision on how much of a company's profit should be retained, and how much paid out to shareholders. **(07 marks)**

Q6. State the **five** sources of interest rate risk. Discuss any **four** of them and provide one example for each in your explanation. **(10 marks)**

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