



Part C- Essay Questions

Part C contains three (03) questions.

Answer only two (02) questions

Marks allocated for part C is Fifty (50)

Show all workings. Assumptions (if any) should clearly be stated.

01)

a) State the different approaches available to assess the value a common stock.

(3 marks)

b) The following information are relevant to the investment in common stock

Dividend paid in the current year Rs.3.00 per share

Dividend growth rate 6% constant

Required rate of return 12%

i. Calculate the value of a share

(4 marks)

ii. Calculate the expected value of a share one year from today

(4 marks)

iii. Calculate the capital gain yield and dividend yield ratios

(6 marks)

c) Mr. Rodrigo, a recently retired government servant considering investment in common stocks. He is willing to invest in ABC PLC and has collected five years details regarding Market Price of a Share, Earning per Share (EPS) and Price Earnings Ratio (PE Ratio) of ABC PLC. Since he does not have much knowledge on such investments, Mr. Rodrigo is requesting your advice on this investment decision.

| Year | 2008 | 2009 | 2010 | 2011 | 2012 |
|-------------------|------|--------|------|------|------|
| Market price (Rs) | 120 | 85 | 145 | 140 | 142 |
| EPS (Rs) | 14 | 8 | 12.5 | 11.2 | 11.8 |
| PE Ratio | 8.57 | 10.625 | 11.6 | 12.5 | 12 |

Consider the historical average PE Ratio as the benchmark PE Ratio of the company for the purpose of valuing the shares.

You are required to advise Mr.Rodrigo whether to invest or not in this company.

(8 marks)

(Total 25 marks)

02)

a) Why it is required a proper appraisal by using appropriate appraisal technique before investing in a long term project?

(3 marks)

b) A company is considering on investing in a suitable project. Currently three investments options are available to the company out of which only one can be undertaken. The estimated investment costs and cash inflows of each investment option are given below.

| Year | Project A | Project B | Project C |
|---------|-----------|-----------|-----------|
| Year 0 | (120,000) | (120,000) | (120,000) |
| Year 01 | 50,000 | 30,000 | 45,000 |
| Year 02 | 55,000 | 32,000 | 45,000 |
| Year 03 | 35,000 | 47,000 | 45,000 |
| Year 04 | 20,000 | 68,000 | 45,000 |

The Company's policy is to calculate the profit after deducting depreciation on straight-line method. The Weighted Average Cost of Capital of the company is 10%.

You are required to;

i. Calculate the payback period of each project and state your recommendation on what project to be undertaken?

(3 marks)

ii. Calculate Net Present Value of each project and state whether you agree with your answer to part (i) above.

(8 marks)

iii. Calculate the Internal Rate of Return of the three projects and state your recommendation based on IRR rule?

(8 marks)



iv. Considering above all in which project you recommend to invest

(3 marks)

(Total 25 marks)

03)

a) Explain the meaning and purpose of investment portfolio management

(4 marks)

b) What is meant by investment policy statement? What specific information is available in the investment policy statement?

(6 marks)

c) Write short notes on any three topics given below

i. Margin trading and margin provider

ii. Bull market and bear market

iii. Order book and odd lot book

iv. Initial public offering and seasoned equity offering

(5 marks for each)

(5 x 3 = 15 marks)

(Total 25 marks)

