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Course Advance Corporate Finance

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Exam Mid Term

Program MBA second Semester

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Advance Corporate finance

Q1

Managers should not focus on the current stock value because doing so will lead to overemphasis on short-terms profit at the expense of long-term profits.

Background

In a corporation managers are the employee of the stockholders and their job is to maximize the wealth of these owners. They are considered residual claimants in that they have claim to the funds that are left over after bills have been paid. The Creation of shareholders wealth means making investment whose value is greater than the amount of Capital used. In measuring this value the concept of time has to be considered

Explanation

Current stock value reflects risk timing and magnitude of all future cash flows both short term and long term under this assumption then the statement is false

Stock price fundamentally is based on all the expected cash flows of the firm be it in the short run medium run or long run. A share price today is nothing but present value of all the future flows the firm will generate.

p.t.o

Q2 ⓐ why might the revenue and cost figures shown on a standard income statement not represent the actual cash inflows and outflows that occured during a period

Generally accepted accounting principles require the use of accrual accounting instead of cash basis accounting so revenue and expenses on the income statement doesnot exactly line up with cash inflows and outflows for the period particularly as it relates to transactions occuring at the beginning or end of the period

Furthermore recognition and matching principles in financial accounting call for revenue and the cost associated with producing those revenues to be booked when the revenue process is essentially complete not necessarily when cash is collected or bills are paid this way is not necessarly correct its the way accountant have chosen to do it. therefore the revenue and cost figures shown on a standard income statement not represent the actual cash inflows and out flows occured during a period.

Q2(a) continued

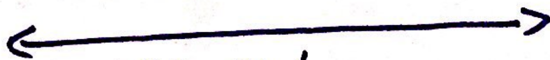
The main difference between the income statement is based on an accrual basis (due or received) while the cash flow statement is based on the actual receipt and payment of cash. The income statement is a part of the financial statement used to show revenues, gains, expenses & losses for a particular accounting period. on the other the cash flow statement is part of the financial statement used to ~~collect~~ reflect cash inflows and outflows for a particular accounting period.

In the income statement all expenses all expenses ~~are~~ and income are accounted for on an accrual basis. It means whether paid or not will have an impact on the financial statement on the other hand only paid activities and accounted for and disclosed in the cash flow statement. A cash flow statement shows exactly how much money a company has received and how much it has tradionally spent over a period of one month It record cullent operating results and balance sheet changes such as increase or decrease in accounts receivible or account payable and does not include non cash accounting such as depreciation and amortization.

Q2 (b)

The bottom line number shows the change in the Cash balance on the balance sheet As such it is not a usefuf number for analyzing a company. The bottom line number is likely to be increase / decrease in Cash and cash equalents.

the bottom line number is likely to be increase / decrease in Cash and Cash equalitents the bottom line reports that overall change in the Company Cash and its equalents. the assets that can be immediately converted into Cash



Q2 End

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Q3@ Financial Ratios

Backrounds

Financial ratios are created with the Use of numerical values taken from financial - statements to gain meaningful information about a Company. The numbers found on a company financial statements, balance sheet, incom statement and Cash flow statement are used to perform quantative analysis and assess a Company liquidity leverage, growth, margins, profitability, rates of return valuation and more.

Time Trend Analysis

Trend analysis is a technique used in technical analysis that attempts to predict the future stock price movements based on recently observed trend data Trend analysis is based on the idea that what has happened in the past gives traders an idea of what has happened in the past gives traders an idea of what will happen in the future there are three main types of trends shorts, intermediate and long term.

p.t.o

Time Trend analysis gives picture of changes in the Company financial situation over time comparing a farm itself over time allows the financial managers to evaluate whether same aspects of the firms operations finances or investment activities have changed.

It help in identifying any change and the firm undergone any changes if any. It help management in identifying whether the areas of firms operations, finances or investment have changed.

Peer group Analysis

It involves comparing the financial ratios and operating ~~program~~ performance of a particular firm to a set of peer group firms in the same industry or line of business. Comparing a firm to its peer allows the financial manager to evaluate whether some aspects of the firm operations, finances or investment activities are out of line with the norm thereby providing some.

p.t.o

thereby providing some guidence on appropriate actions to take to adjust these ratios it appropriate. Both allow an investigation into what is different about a company from a financial prospective but neither method gives an indication of whether the difference is positive or negative. For example suppose a company current ratio is increasing over time It could mean that the company had been facing liquidity problem in the past and is rectifing those problems it could mean the Company has become less effecient in managing its current accounts. Similar arguments could be made for a peer group Comparison.

A Company with a current ratio lowers than its peer could be more efficient at managing its current accounts or it could be facing liquidity problems. Neither Analysis method tell us whether a ratio is good or bad both simply show that something is different and tells us where to look.

Importance of Ratio Analysis

Analysis of financial statements

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Analysis of operation Efficiency of the firm

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Liquidity of the firms

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Help in identifying the business Risk of the firm

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Help in identifying the financial Risk of the Company

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For planing and Future Forecasting of the firm

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To Compare the performance of the firms

Diagramitical Explanation

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End of paper