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**Phase-II, Hayatabad, Peshawar**

**Khyber Pukhtunkhwa**

**Paper : Business Finance**

**Subject : Business Administration**

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**Problem: 1**

**Solution:**

1. Acid Test Ratio = Current Assets **–** Inventories

 Current Liability

 = $840,000 –$ 300,000

 $620,000

 = $540,000

 $620,000

 = 0.8709

 = 0.871 (By Rounding-Off)

1. Inventory Turnover Ratio = Cost of Goods Sold

 Inventory

 = $4,000,000

 $300,000

 = 13.333

1. Debt to Net Worth Ratio = Total Debt

 Shareholder’s Equity

 = $1,020,000

 $800,000

 = 1.275

1. Net Profit Margin = Net Profit after Taxes

 Net Sales

 = $400,000

 $5,000,000

 = 0.08

1. Total Asset Turnover Ratio = Net Sales

 Total Assets

 = $5,000,000

 $1,140,000

 = 3.478

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**Problem: 2**

**Solution:**

**Part: A**

K= 15%

N= 5yrs

I= $1000 X 10%= $100

MV = $1000

Putting values,

V= I ( $PVIFA\_{Kd,n}$) + MV ($PVIF\_{Kd,n}$)

= $100 ($PVIFA\_{15\%,5}$) + $1000 ($PVIF\_{15\%,5}$)

= $100(3.3522) + $1000(0.4972)

= $335.22 + $497.2

= $832.42

**Part: B**

K= 12%

N= 5yrs

I= $1000 X 8%= $80

MV = $1000

Putting values,

V= I ( $PVIFA\_{Kd,n}$) + MV ($PVIF\_{Kd,n}$)

= $80 ($PVIFA\_{12\%,5}$) + $1000 ($PVIF\_{12\%,5}$)

= $80(3.6048) + $1000(0.5674)

= $288.384 + $567.4

= $855.784

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**Problem: 3**

**Solution:**

**Liquidation Value versus Going-Concern Value:**

**Liquidation Value:**

Liquidation value is the amount of money that could be realized if an asset or a group of assets (E.G a firm) is sold separately from its operating organization.

**Going-Concern Value:**

Going – Concern Value is the amount a firm could be sold for as a continuing operation business

These two values are rarely equal, and sometimes a company is actually worth more dead than alive.

The security valuation model generally deals with going concern values – operating firms able to generate positive cash flows to security investors. Instances where this assumption is not appropriate (E.G Impending Bankruptcy), the firm liquidation value will have a major role in determining the value of the firm’s financial securities.

**Market Value versus Intrinsic Value:**

**Market Value:**

Market value is simply the market price at which the asset trades in an open market place. For a firm, market value is often viewed as being the higher of the firm’s liquidation or going – concern value.

**Intrinsic Value:**

The price a security “ought to have” based on all factors bearing on valuation (Assets, Earnings, Future Prospects, Management etc.). This is the present value of the cash flow stream provided to the investor discounted at a required rate of return appropriate for the risk involved.

In short, the intrinsic value of a security is its economic value. If the markets are reasonably efficient and informed, the current market price of a security would fluctuate closely around its intrinsic value.

**Bonds with Finite Maturity versus Infinite Maturity:**

**Bond:**

A bond is a security that pays a stated amount of interest to the investor, period after period, until it is finally retired by the company.

There are two types of bond on the basis of maturity

 One is called short term and the other is called long term.

**Bonds with Finite Maturity:**

Short term or finite bonds have maturity of 2 to 3 years having not fixed interest rate.

Some bonds with finite maturity:

**Non-Zero Coupon Bonds:** In this bond, we consider not only the interest stream but also the maturity value in valuing the bond.

**Zero Coupon Bond:** In this bond, there is no periodic interest payment but instead is sold at a deep discount rate from its face value.

**Semi-Annual Compounding of Interest:** Although, some bonds make interest payment once a year while most of the bonds issued pay it twice a year which is semi-annual compounding of interest.

**Bonds with Infinite Maturity:**

While infinite or long term or perpetual bond are bonds having maturity of 10 to 20 years

Infinite bonds are not consider as a debt it is consider as an equity like stocks

Infinite bonds have fixed interest rate and cannot be redeemed.

Infinite bonds are like investment.

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**Problem: 4**

**Solution:**

**Part: A**

Current Ratio = Current Assets

 Current Liability

 = $1,000,000

 $700,000

 = 1.428

For (i):

Current Ratio = Current Assets

 Current Liability

 = $800,000

 $700,000

 = 1.1428

 = 1.143 (By Rounding-Off)

Cash decreased due to purchase of inventory (i.e. purchase of trucks of $200,000) so current assets decreases by $200,000 and liabilities remain unchanged.

For (ii):

Current Ratio = Current Assets

 Current Liability

 = $1,050,000

 $750,000

 = 1.4

The company has borrowed short term loan due to which there comes an increase in both the assets (Receivables) and liabilities. (i.e. Both increases by $50,000)

**Part: B**

K= 12% = 0.12

D= 10% of 100 = $10

V= Dp

 Kp

 = $10

 0.12

 = $83.33

For 14%,

K= 14% = 0.14

D= 10% of 100 = $10

V= Dp

 Kp

 = $10

 0.14

 = $71.428

 = $71.43 (By Rounding-Off)

So market price per share decreases by $11.9.

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