UNIVERSITY OF BRADFORD

STRATEGIC FINANCIAL MANAGEMENT (MSc)

MAN4152M

07 May 2013 **16:00 – 17:30 hours**

Main

This is a **CLOSED BOOK** examination

Answer **ONE** question from Section A
All questions carry equal weighting

Answer **ONE** question from Section B
All questions carry equal weighting

Section A

Answer ONE question from Section A. All questions carry equal weighting

Question 1

Discuss carefully market efficiency and evaluate the extent to which market efficiency hypothesis is supported empirically.

(Total 100% weighting)

Question 2

(a) Explain why, in certain circumstances, the IRR technique can be criticised and how these criticisms are addressed by the Modified Internal Rate of Return.

(40% weighting)

(b). Discuss the different problems associated with the use of profit maximisation as the objective of the firm. Explain how shareholder value maximisation can overcome these problems.

(60% weighting)

(Total 100% weighting)

Section B

Answer ONE question from Section B. All questions carry equal weighting

Question 3

(a) You plan to construct a portfolio consisting of two equity investment in ordinary shares of two companies – Glacier Ltd and Express Ltd. From your research, you find out that these two investments have a correlation coefficient of ρ_{ab} = +0.57

The following information was also collected:

	Glacier Ltd	Express Ltd
Standard Deviation	20%	15%
Expected Return	16%	13%

Find the portfolio returns and portfolio risk if the portfolio weights are:

(i) 25% Glacier 75% Express. Show your workings.

(15% weighting)

(ii) Calculate the covariance of the two stocks. Show your workings.

(15% weighting)

(b) “The market will pay an investor for taking on non-diversifiable risk, but will not pay an investor for taking on diversifiable risk.” Discuss.

(40% weighting)

(c) You are looking at a Luzern Ltd’s ordinary share that has recently paid a $0.55 dividend. The firm’s earning has been increasing at a rate of 4.7% per annum and is expected to maintain the same growth rate in the future. You believe that a reasonable required rate of return for the ordinary share is 12% per annum. Calculate the fair value for the ordinary share. Show your workings

(30% weighting)

Question 4

The riskless return is currently 6%, and Chicago Gear has estimated the following contingent returns:

		REALISED RETURN	
State of the Market	Probability that State Occurs	Stock Market	Chicago Gear
Stagnant	0.20	(10%)	(15%)
Slow growth	0.35	10	15
Average growth	0.30	15	25
Rapid growth	0.15	25	35

Required

(a) Calculate the expected return on the stock market and on Chicago Gear stock.

(20% weighting)

(b) Calculate Chicago Gear's beta.

(30% weighting)

(c) Calculate Chicago Gear's required return according to the capital asset pricing model (CAPM).

(20% weighting)

(d) The Capital Asset Pricing Model (CAPM) can be used as a basis for calculating the cost of equity of a firm. Explain the CAPM and within your answer distinguish between systematic and unsystematic risk.

(30% weighting)

(Total 100% weighting)