# Exam Paper for Corporate Finance in BBA (With Answers)

**PAPER # 1**

**Course: BBA in Corporate Finance**

**Duration: 2 hours**

**Instructions:**

1. Answer all questions.
2. You may use a calculator.
3. Write your answers clearly and legibly.

**Section A: Multiple Choice Questions (10 marks)**

Choose the best answer for each question.

1. Which of the following represents the primary goal of financial management for a corporation?

   a. Maximizing sales

   b. Minimizing expenses

   c. Maximizing shareholder wealth

   d. Maximizing employee satisfaction



   **Answer: c**

2. What is the term for the cost of capital that represents the required return for a firm's investors?

   a. Weighted Average Cost of Capital (WACC)

   b. Return on Investment (ROI)

   c. Internal Rate of Return (IRR)

   d. Dividend Yield

Operating expenses are expenses that are incurred on a day-to-day basis in order to keep a business running.

7. The three main sources of financing for a business are debt, equity, and retained earnings.

8. The two main types of equity are common stock and preferred stock.

9. The formula for calculating the WACC is:

WACC = (Cost of equity * Weight of equity) + (Cost of debt * Weight of debt)

10. A company can use financial leverage to increase its return on equity by using debt to finance its investments. Debt has a lower cost than equity, so using debt to finance investments can increase the company's overall return on equity. However, it is important to note that financial leverage also increases the company's risk.

Part C

11. The different types of capital budgeting techniques are:

- Net present value (NPV)
- Internal rate of return (IRR)
- Payback period
- Discounted payback period



The most effective capital budgeting technique is NPV. NPV takes into account the time value of money and calculates the net present value of all future cash flows from the investment. IRR is also a good capital budgeting technique, but it is important to note that it can have multiple solutions and can be difficult to interpret. Payback period and discounted payback period are simpler capital budgeting techniques, but they do not take into account the time value of money.

12. The different types of corporate risk are:

- Business risk
- Financial risk

- **Higher Operating Leverage**: A company with high fixed operating costs will have greater potential for profit when sales increase, but it will also suffer larger losses when sales decline. This increases the operational risk.

In summary, while leverage can enhance returns, it also introduces additional risk. Companies must carefully manage their leverage to strike the right balance between risk and return.

**Section C: Calculation Questions (10 marks each)**

6. XYZ Corporation is evaluating two mutually exclusive projects, A and B. Project A has an initial investment of $50,000 and is expected to generate cash flows of $20,000 per year for five years. Project B has an initial investment of $60,000 and is expected to generate cash flows of $18,000 per year for five years. Calculate the Net Present Value (NPV) of both projects using a discount rate of 10%.

**Answer:**

NPV of Project A:

NPV(A) = ∑(Cash Flows / (1 + r)^t) = (-$50,000) + ($20,000 / (1 + 0.10)^1) + ($20,000 / (1 + 0.10)^2) + ($20,000 / (1 + 0.10)^3) + ($20,000 / (1 + 0.10)^4) + ($20,000 / (1 + 0.10)^5)



NPV(A) = -$50,000 + $18,181.82 + $16,528.93 + $15,026.30 + $13,659.37 + $12,414.8[illegible]

NPV(A) = $25,811.30

NPV of Project B:

NPV(B) = ∑(Cash Flows / (1 + r)^t) = (-$60,000) + ($18,000 / (1 + 0.10)^1) + ($18,000 / (1 + 0.10)^2) + ($18,000 / (1 + 0.10)^3) + ($18,000 / (1 + 0.10)^4) + ($18,000 / (1 + 0.10)^5)

NPV(B) = -$60,000 + $16,363.64 + $14,876.04 + $13,523.67 + $12,294.24 + $11,175.67

NPV(B) = $8,232.26

Therefore, the NPV of Project A is $25,811.30, and the NPV of Project B is $8,232.26.