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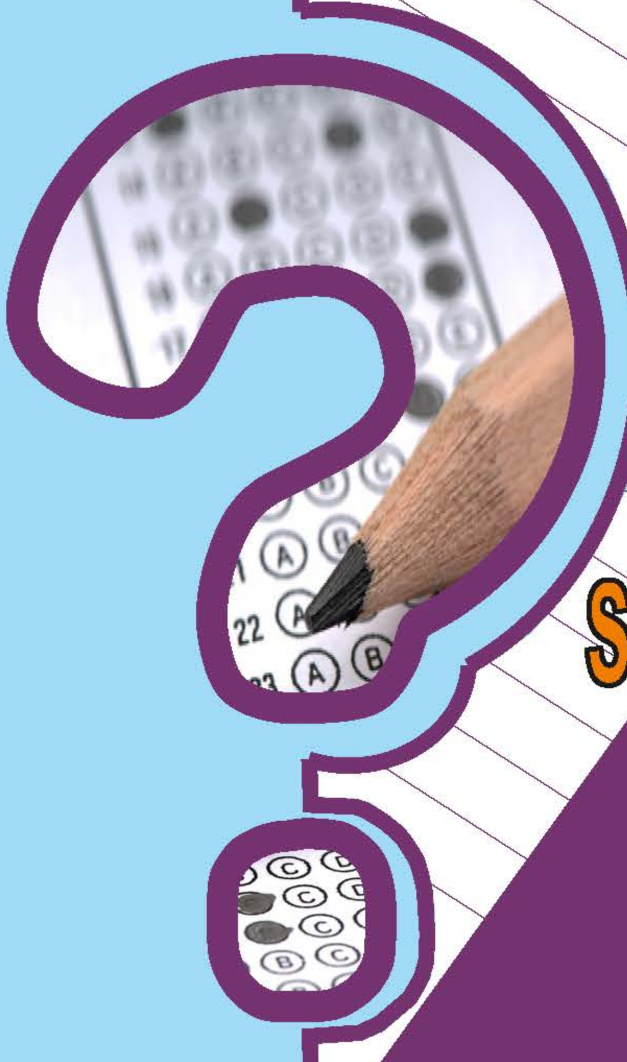

PAPER - 20

MCQs

BIT QUESTIONS

Strategic Performance Management and Business Valuation

DIRECTORATE OF STUDIES

THE INSTITUTE OF COST ACCOUNTANTS OF INDIA

Statutory Body under an Act of Parliament

Behind every successful business decision, there is always a CMA

MISSION STATEMENT

"The CMA Professionals would ethically drive enterprises globally by creating value to stakeholders in the socio-economic context through competencies drawn from the integration of strategy, management and accounting."

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Behind every successful business decision, there is always a CMA

PAPER -20
Strategic Performance Management and Business Valuation
Bit Questions

STRAGETIC PERFORMANCE MANAGEMENT

Choose the most appropriate answer giving justification.

1. Risk Management Strategies are
(A) Avoid Risk, Reduce Risk, Retain Risk, Combine Risk
(B) Transfer Risk, Share Risk and Hedge Risk
(C) Both (A) and (B)
(D) None of the above

2. The necessary condition for equilibrium position of a firm is
(A) MC>MR
(B) MC> Price
(C) MC = MR
(D) MC = AC

3. The Cost function of a firm is given by C = x3 - 4x2 + 7x. Find at what level of output the average cost is minimum and what would be the minimum average cost.
(A) 2,3
(B) 4,5
(C) 1,4
(D) None of the above

4. Which one of the following is not a measure related to Balanced Score Card?
(A) Financial
(B) Customer Satisfaction
(C) Internal Processes
(D) Gap Analysis

5. Performance will be a product of
(A) Efficiency and Utilization
(B) Utilization and Productivity
(C) Efficiency and Productivity
(D) Efficiency, Utilization and Productivity

6. _______is the uncertainty of the purchasing power of the monies to be received, in the future?
(A) Market risk
(B) Physical risk
(C) Purchasing power risk
(D) Interest rate risk

7. Unsystematic risk relates to
(A) Market risk
(B) Inherent risk
(C) Beta
(D) Interest rate risk

8. In which discipline supply chain concept was originated?
(A) Production
(B) Operation

(C) Marketing
(D) Logistics

9. Under perfect competition and at the point of equilibrium of firm
(A) MC curve must be falling
(B) MC curve must be rising
(C) MR curve must be falling
(D) None of the above

10. Financial risk arises out of ___________
(A) Increased competition
(B) Conduct of business and investment
(C) The nature of financial transaction
(D) Both (B) and (C)

11. An Index number is a statistical measure of __________ in a variable arranged in the form of a series and using a base for making comparison.
(A) productivity
(B) inputs
(C) efficiency
(D) fluctuations

12. Benchmarking focuses on
(A) Production
(B) Profit
(C) Best Practices
(D) Best performance

13. Project risk does not include
(A) Institutional risk
(B) Turbulence
(C) Completion risk
(D) Uncertainty

14. Physical risk arising out of Social, Political, Economic and Legal Environments are often identified through
(A) the performance of lead indicators
(B) the performance of lag indicators
(C) the performance of lead and lag indicators
(D) None of the above

15. Which out of the following financial ratios is not in the Altman Model: Z-Score?
(A) Market Value to Book Value of equity shares
(B) Working Capital to Total Assets
(C) Retained Earnings to Total Assets
(D) EBIT to Total Assets

16. The purpose of supply chain management is
(A) provide customer satisfaction
(B) improve quality of a product
(C) integrating supply and demand management
(D) increase production

17. The major decision areas in supply chain management are

(A) location, production, distribution, inventory
(B) planning, production, distribution, inventory
(C) location, production, scheduling, inventory
(D) location, production, distribution, marketing

18. Which of the following is not one of the Customer Relationship Management (CRM) business drivers?
(A) Inventory control
(B) Increase revenues
(C) Define information needs and flows
(D) Automation/productivity/efficiency

19. Customer Relationship Management is about:
(A) Acquiring the right customer
(B) Instituting the best processes
(C) Motivating employees
(D) All of the above

20. Process of managing information about customers to maximize loyalty is said to be
(A) company relationship management
(B) supplier management
(C) retailers management
(D) customer relationship management

21. A supply chain is made up of a series of processes that involve an input, a _______, and an output.
(A) shipment
(B) supplier
(C) customer
(D) transformation

22. Which of the following is not an accounting technique to analyse financial performance?
(A) Trend analysis
(B) Common-size financial analysis
(C) Ratio analysis
(D) Time series analysis

23. Supply Chain Management encompasses the planning and management of all activities involved in —
(A) sourcing and procurement,
(B) conversion
(C) logistics management
(D) All of the above

24. Which of the following is not a component of supply chain management?
(A) Plan
(B) Deliver
(C) Organising
(D) Return

25. Consultants who contributed to the concept of TQM (Total Quality Management):
(A) W. Edwards Deming
(B) Joseph Juran
(C) (A) V. Feigenbaum
(D) All of the above

26. Which of the following does not form part of Benchmarking process?
(A) Redesign
(B) Planning
(C) Analysis
(D) Integration

27. Benchmarking is:
(A) The analytical tool to identify high cost activities based on the 'Pareto Analysis'
(B) The search for industries best practices that lead to superior performance
(C) The simulation of cost reduction schemes that help to build commitment and improvement of actions
(D) The process of marketing and redesigning the way a typical company works

28. Total Quality Management emphasises:
(A) the responsibility of the Quality Control staff to identify and solve all quality-related problems
(B) a commitment to quality that goes beyond internal company issues to suppliers and customers
(C) a system where strong managers are the only decision makers
(D) a process where mostly statisticians get involved

29. A successful TQM program incorporates all of the following except :
(A) continuous improvement
(B) employment involvement
(C) benchmarking
(D) centralized decision making authority

30. The six sigma DMAIC process consist of:
(A) define, measure, analyze, improve, control
(B) define, manage, analyze, improve, control
(C) define, measure, analyze, improve, co-ordination
(D) deliver, measure, analyze, improve, control

31. The components of Stewart Cycle or PDCA are:
(A) Plan-Do-Check-Act
(B) Plan-Define-Check-Act
(C) Plan-Do-Control-Act
(D) Program-Do-Check-Act

32. Which of the following statements is true?
(A) Elasticity of demand is constant throughout the demand curve
(B) Elasticity of demand increases as one goes down the demand curve
(C) Elasticity of demand decreases as one goes down the demand curve
(D) The slope of the demand curve equals its elasticity

33. If the total expenditure of the consumer increases as a result of an increase in the price of the commodity, the elasticity of demand for the commodity is
(A) Infinity
(B) Greater than one
(C) Less than one
(D) Equal to one

34. If the supply of a commodity is perfectly elastic, an increase in demand will result in
(A) Decrease in both price and quantity at equilibrium
(B) Increase in both price and quantity at equilibrium

(C) Increase in equilibrium quantity, equilibrium price remaining constant
(D) Increase in equilibrium price, equilibrium quantity remaining constant

35. If proportion of income spent on a good is significant, price elasticity of demand for the good tends to be
(A) Perfectly elastic
(B) Elastic
(C) Inelastic
(D) Perfectly inelastic

36. Which of the following is/are true?
(A) Income elasticity is the ratio of percentage change in the price of a good to the percentage change in the income.
(B) Goods are independent if a price change for one has no effect on the demand for the other.
(C) The reciprocal of income elasticity is the percentage change in the income to the percentage change in the quantity demanded of a good
(D) Both (B) and (C) above

37. A demand curve shows
(A) The quantity demanded of a good at various levels of income of the consumer
(B) The quantity demanded of a good at various levels of price of the good
(C) The amount of money spent by a consumer on the good at various levels of price
(D) The quantity supplied of a good at various levels of price of the good

38. Which of the following is not true?
(A) The law of demand says, *ceteris paribus*, the lower the price of a good, the greater the quantity demanded
(B) The law of supply says, *ceteris paribus*, the higher the price of a good, the greater the quantity supplied
(C) The supply curve for a highly perishable good is horizontal
(D) The demand curve for a life saving drug is almost vertical

39. For complementary products, the cross elasticity of demand will be
(A) Zero
(B) Infinity
(C) Positive, but less than infinity
(D) Negative

40. When the income elasticity of demand for a good is negative, the good is
(A) Normal good
(B) Luxury good
(C) Inferior good
(D) Giffen good

41. The price elasticity of demand for a product is infinity. If the firm increases price of the product by 10%, total revenue of the firm will
(A) Increase to infinity
(B) Fall to zero
(C) Decrease by more than 10%
(D) Decrease by less than 10%.

42. When consumption of a product remains unaffected by the change in price of the product, demand for the product is
(A) Perfectly inelastic
(B) Kinked

(C) Perfectly elastic
(D) Unitary elastic

43. Total revenue will increase -
(A) When demand is elastic and price rises
(B) When demand is elastic and price decreases
(C) When demand is inelastic and price decreases
(D) When demand is perfectly elastic and price decreases

44. In perfect competition, a firm maximizing its profits will set its output at that level where
(A) Average variable cost = price
(B) Marginal cost = price
(C) Fixed cost = price
(D) Average fixed cost = price

45. Average fixed cost
(A) Always declines as the output increases
(B) Is U-shaped, if there are increasing returns to scale
(C) Is U-shaped, if there are decreasing returns to scale
(D) Is intersected by marginal cost at its minimum point

46. In the short run which of the following is not true of a profit-maximizing firm operating under perfect competition?
(A) P – MC
(B) MR – MC
(C) AR = MR = MC
(D) P=AR = AC

47. Which of the following curves is called envelope curve?
(A) Long run total cost curve
(B) Long run average total cost curve
(C) Long run marginal cost curve
(D) Long run average variable cost curve

48. The supply curve under perfect competition in the short run resembles
(A) Average cost curve above break-even point
(B) Marginal cost curve above shut down point
(C) Marginal utility curve
(D) Average utility curve

49. Which of the following is not a feature of perfect competition?
(A) Large number of sellers and buyers
(B) No one is large enough to influence the market price
(C) A horizontal demand curve
(D) Low price

50. The horizontal demand curve for a firm is one of the characteristic features of
(A) Oligopoly
(B) Monopoly
(C) Monopolistic competition
(D) Perfect competition

51. In India which of the following best describes a perfectly competitive market?
(A) Wheat cultivation
(B) Indian railways

(C) Soft drinks industry
(D) Toilet soap industry

52. In a monopoly, price is
(A) Lesser than the marginal revenue
(B) Greater than the average revenue
(C) Greater than the marginal revenue
(D) Equal to the total revenue

53. The demand for which of the following goods best illustrates derived demand?
(A) Rice
(B) Motor car
(C) Machinery
(D) Book

54. A perfectly competitive firm earns abnormal profits when its
(A) Average revenue curve is tangent to average cost curve
(B) Demand curve lies above the average cost curve
(C) Marginal revenue curve lies above the average cost curve
(D) Both (B) and (C) above

55. Which of the following is true with reference to marginal revenue (MR) in a monopoly?
(A) When MR is negative, AR will be negative
(B) When MR is negative, price will be negative
(C) When demand slopes downward price will be less than MR
(D) MR curve lies below the AR curve

56. The equilibrium condition for a monopoly firm is
(A) Total cost should be minimum
(B) Total revenue should be maximum
(C) Marginal revenue = Marginal cost
(D) Quantity should be maximum

57. Which of the following is false in a monopolistic competition?
(A) Many buyers and sellers
(B) Identical products
(C) Easy entry and exit
(D) Price of the competitor is the benchmark price

58. Which of the following is not a feature of monopolistic competition?
(A) Large number of sellers
(B) No single seller has control over the market
(C) Horizontal demand curve for the firm
(D) Differentiated products

59. When the demand for most products varies directly with the change in consumer income, such products are known as
(A) Normal goods
(B) Prestigious goods
(C) Complementary goods
(D) Inferior goods

60. In case of monopolistic competition, the long run equilibrium price will be equal to
(A) Marginal revenue
(B) Average cost
(C) Marginal cost

(D) Minimum average cost

61. The cross price elasticity of demand for the products X and Y is 10, It implies that X and Y are
(A) Substitutes
(B) Complements
(C) Independent
(D) Inferior goods

62. Which of the following does not cause a shift in the demand curve?
(A) Change in the price of the good
(B) Change in the income of the buyers
(C) Change in the price of the related goods
(D) Change in the consumer taste and preferences

63. In a long run period
(A) All costs are fixed costs
(B) All costs are variable costs
(C) Fixed costs tend to be greater than variable costs
(D) Fixed costs tend to be less than variable costs
(E) None of the above

64. Which of the following best describes monopoly?
(A) An indisputable market leader in an industry
(B) Only a single buyer in the market
(C) A single seller with large control over me price in the industry.
(D) Only a single seller with complete control over the industry

65. For a perfectly competitive firm the shut down point in the short run is where the price of the product falls below the
(A) Total cost
(B) Fixed cost
(C) Average variable cost
(D) Semi-fixed cost

66. Which of the following is not a legal barrier to entry?
(A) Patents
(B) Economies of scale
(C) Franchise
(D) Copy rights

67. Unsystematic risk relates to
(A) Market Risk
(B) Inherent Risk
(C) Beta
(D) Interest rate risk

68. Which of the following is not a risk management technique
(A) Risk avoidance
(B) Risk maximization
(C) Risk Sharing
(D) Risk bearing

69. Financial risk is associated with__________
(A) Production strategies
(B) Financing strategies

(C) Marketing strategies
(D) Purchasing strategies

70. Systematic risk is measured by __________
(A) Alpha
(B) Beta
(C) Gamma
(D) Delta

71. Portfolio diversification reduces ____________
(A) Only systematic risk
(B) Only unsystematic risk
(C) Both systematic and unsystematic risk
(D) None of systematic and unsystematic risk

72. Increase in the interest and corresponding decrease in the intrinsic value of debt instruments indicates__________
(A) Interest rate risk
(B) Liquidity risk
(C) Default risk
(D) Purchasing power risk

73. Which of the following is not an actuarial concept used in risk pooling?
(A) Statistical variation
(B) The law of averages
(C) The law of large numbers
(D) The law of subjective judgment

74. The financial performance analysis which is undertaken by the outsiders of the business, namely investors, credit agencies, government agencies, and other creditors who have no access to the internal records of the company, is called:
(A) Internal analysis
(B) External analysis
(C) Horizontal Analysis
(D) Vertical Analysis

75. Which of the following is a cause for corporate distress?
(A) Fraud by Management
(B) Working Capital Problems
(C) Mismanagement
(D) All of the above

76. Six Sigma has two key methodologies. These are:
(A) DMAIC and DMADV
(B) DMADC and DMADV
(C) DMAIC and DMADC
(D) DMAII and DMADV

77. Who has prompted the phrases, ―Zero Defects‖?
(A) Walter A Shewhart
(B) Philip Crosby
(C) Peter Drucker
(D) F. W. Taylor

78. One of the exceptions of Law of Demand is described by Sir Robert Giffen. He said that even though the price, for necessary goods rise, the demand for them will not decrease. These goods are called:
(A) Prestigious goods
(B) Speculative goods
(C) Giffen goods
(D) None of the above

79. If the proportionate change in the price is more than the proportionate change in the demand, it is called:
(A) Relatively inelastic demand
(B) Relatively elastic demand
(C) Perfectly Inelastic demand
(D) Perfectly Elastic Demand

80. A French economist Cournot analyzed a special case of competitive business behaviour with only two firms in an Industry. It is called:
(A) Oligopoly
(B) Monopoly
(C) Duopoly
(D) None of the above

81. The risk which is primarily influenced by the level of financial gearing, interest cover, operating leverage, and cash flow adequacy, is called:
(A) Financial risk
(B) Business risk
(C) External risk
(D) Exchange risk

82. Which of the following are not the element/ parameter of NCAER model of corporate distress prediction?
(A) Net worth position
(B) Outstanding liability position
(C) Net working capital position
(D) Cash profit position

83. The type of benchmarking, which is concerned with the development of core competencies that will help sustained competitive advantage, is called:
(A) Global Benchmarking
(B) Strategic Benchmarking
(C) Internal Benchmarking
(D) Competitive Benchmarking

84. ________measures overall productivity and efficiency by considering all inputs and all outputs in the production process.
(A) Total Factor Productivity
(B) Partial Factor Productivity
(C) Parametric Index Number Approach
(D) Non-parametric Index Number Approach

85. A firm has total cost function: C =1/9 X3-l/2 X2-18 X +30; C is total cost and X is quantity produced. One is wondering whether MC (marginal cost) can ever be zero. If you believe that the firm's MC can be zero, then it will be when X is equal to
(A) 2
(B) 5
(C) 9
(D) None of the above is true

86. Which one the following is NOT a type of Benchmarking?
(A) Product Benchmarking
(B) Competitive Benchmarking
(C) Process Benchmarking
(D) Brand Benchmarking

87. If the average cost function of a firm is given by $AC = x^2 – 4x + 7$, in terms of output x, what will be its marginal cost?
(A) $2x^3 - 4x^2 + 7x$
(B) $3x^2 -8x + 7$
(C) $x^3 - 8x^2 + 7x$
(D) None of the above

88. Which one of the following strategies is not for managing risk?
(A) Risk-Avoidance Strategy
(B) Risk-Transferring Strategy
(C) Risk-Measurement Strategy
(D) Risk-Acceptance Strategy

89. For a monopolist firm, the profit will be maximum when
(A) AR = AC
(B) AR > AC
(C) MR = MC
(D) MR > MC

90. Which one of the following is NOT true about On-Line Analytical Processing (OLAP)?
(A) OLAP functionality includes trend analysis over sequential time periods
(B) It provides slicing subsets for on-screen viewing
(C) It is a category of hardware technology
(D) It helps the end user to drill-down to deeper levels of consolidation data

91. Performance management creates a direct link between
(A) employee performance and employee's goal
(B) organizational performance and employee's goal
(C) employee performance and organizational goals
(D) organizational goals and employee's goals

92. If productivity growth of an organization is _________ that of its competitors, that firm performs better and is considered to be more efficient.
(A) higher than
(B) lower than
(C) stable
(D) fluctuating in both higher and lower sides

93. The program which encompasses the planning and management of all activities involved in sourcing procurement, conversion and logistics management activities is called

(A) Supply Chain Management
(B) Customer Relationship Management
(C) Total Quality Management
(D) None of the above

Answer:

(1) (C) Both (A) and (B)
Since Risk Management strategies covers all points under both (A) and (B)
(2) (C) MC=MR
(3) (A) 2,3
Total Cost = x^3-4x^2+7x
Average Cost = x^2-4x+7
In order that average cost is minimum, dy/dx =0 and the value of d^2y/dx^2 should be positive.
dy/dx = 2x-4=0 or x-2 =0 or x=2.
d^2y/dx^2 =2, which is positive, so that the function will have minimum values.
Minimum: Average Cost = x^2-4x+7= 4-(4x2) +7 =4-8+7 =3
(4) (D) Gap Analysis
Gap Analysis, since Balance Scorecard is not concerned with Gap Analysis
(5) (D) Efficiency, Utilization and Productivity
Efficiency, Utilization & Productivity, since this option fully covers all aspects of Performance
(6) (C) Purchasing power risk
(7) (B) Inherent risk
(8) (C) Marketing
(9) (B) MC curve must be rising
(10) (D) Both (B) and (C)
(11) (D) fluctuations
(12) (C) Best Practices
(13) (D) Uncertainty
(14) (A) the performance of lead indicators
(15) (A) Market Value to Book Value of equity shares
(16) (C) integrating supply and demand management
(17) (A) location, production, distribution, inventory
(18) (C) Define information needs and flows
(19) (D) All of the above
(20) (D) customer relationship management
(21) (D) transformation
(22) (D) Time series analysis
(23) (D) All of the above
(24) (C) Organising
(25) (D) All of the above
(26) (A) Redesign
(27) (B) The search for industries best practices that lead to superior performance
(28) (B) a commitment to quality that goes beyond internal company issues to suppliers and customers
(29) (D) centralized decision making authority
(30) (A) define, measure, analyze, improve, control
(31) (A) Plan-Do-Check-Act
(32) (C) Elasticity of demand decreases as one goes down the demand curve
(33) (C) Less than one
(34) (C) Increase in equilibrium quantity, equilibrium price remaining constant

(35) (B) Elastic
(36) (D) Both (B) and (C) above
(37) (B) The quantity demanded of a good at various levels of price of the good
(38) (C) The supply curve for a highly perishable good is horizontal
(39) (D) Negative
(40) (C) Inferior good
(41) (B) Fall to zero
(42) (A) Perfectly inelastic
(43) (B) When demand is elastic and price decreases
(44) (B) Marginal cost = price
(45) (A) Always declines as the output increases
(46) (D) P=AR = AC
(47) (B) Long run average total cost curve
(48) (B) Marginal cost curve above shut down point
(49) (D) Low price
(50) (D) Perfect competition
(51) (A) Wheat cultivation
(52) (C) Greater than the marginal revenue
(53) (C) Machinery
(54) (D) Both (B) and (C) above
(55) (D) MR curve lies below the AR curve
(56) (C) Marginal revenue = Marginal cost
(57) (B) Identical products
(58) (C) Horizontal demand curve for the firm
(59) (A) Normal goods
(60) (B) Average cost
(61) (A) Substitutes
(62) (A) Change in the price of the good
(63) (B) All costs are variable costs
(64) (D) Only a single seller with complete control over the industry
(65) (C) Average variable cost
(66) (B) Economies of scale
(67) (B) Inherent Risk
(68) (B) Risk maximization
(69) (B) Financing strategies
(70) (B) Beta
(71) (B) Only unsystematic risk
(72) (A) Interest rate risk
(73) (D) The law of subjective judgment
(74) (B) External analysis

The financial performance analysis which is undertaken by the outsiders of the business, namely investors, credit agencies, government agencies, and other creditors, who have no access to the internal records of the company, is called External analysis

(75) (D) All of the above

The causes for corporate distress can be — Technological Causes, Working Capital Problems, Economic Distress, Mismanagement, Fraud by Management etc

(76) (A) DMAIC and DMADV

DMAIC (Define, Measure, Analyze, Improve, Control) is used to improve an existing business process and DMADV (Define, Measure, Analyze, Design, Verify) is used to create new product or process designs for predictable, defect-free performance

(77) (B) Philip Crosby

Philip Crosby prompted the phrases, ―Zero Defects‖. It does not mean mistakes never happen, rather than there is no allowable number of errors built into a product or process and that it is to be got right first time

(78) (C) Giffen goods

According to the Law of demand, when the price rises, demand decreases and vice-versa But, according to Sir Robert Giffen, even though the price for necessary goods rise, the demand for them will not decrease. These goods are called Giffen goods

(79) (A) Relatively inelastic demand

If the proportionate change in the price is more than the proportionate change in the demand, it is called relatively inelastic demand The demand is less elastic This is one type of price elasticity of demand

(80) (C) Duopoly

A special case of competitive business behaviour with only two firms in an industry is called duopoly. It is assumed that each member in this two – firm industry produces a homogeneous product, treats the rivals output as given and maximizes profit

(81) (A) Financial risk

Financial risk is primarily influenced by the level of financial gearing, interest cover, operating leverage, and cash flow adequacy. The financial risk depends on the capital structure and method of financing adopted by the company

(82) (B) Outstanding liability position

The NCAER Study on Corporate Distress Prediction prescribed three elements/ parameters for predicting the stages of corporate sickness, such as: (i) Cash profit position (a profitability measure) (ii) Net working capital position (a liquidity measure) and (iii) Net worth position (a solvency measure)

(83) (B) Strategic Benchmarking

Strategic Benchmarking helps to develop a vision of the changed organizations. It will develop core competencies that will help sustained competitive advantage

(84) (A) Total Factor Productivity

(85) (C) 9

We know that C = 1/9 x ^3-1/2 x ^2-18 x+30; Then, MC = dC/dx = 1/3 x^2-x-18;

When MC = 0, we get 1/3 x^2-x-18=0↔x^2-3x-54=0↔(x-9)(x+6)=0. Since x can never be negative, x = 9, to get MC = 0

(86) (D) Brand Benchmarking

(87) (B) $3x^2$ -8x + 7

Total cost (c) = $x(x^2 – 4x + 7) = x^3 – 4x^2 + 7x$

Marginal cost $= d/dx\ (x^3 – 4x^2 + 7x)$

$= 3x^2 – 8x + 7$

(88) (C) Risk-Measurement Strategy

Risk-Measurement Strategy as it is not a strategy of managing risk but a strategy to quantify risk

(89) (C) MR = MC

MC = MR, as this is the condition for Profit Maximization

(90) (C) It is a category of hardware technology

On-Line Analytical Processing (OLAP) is a category of software technology and not hardware technology.

(91) (C) employee performance and organizational goals

Performance management creates a direct link between employee performance and organizational goals

(92) (A) higher than

If productivity growth of an organization is higher than that of its competitors, that firm performs better and is considered to be more efficient

(93) (A) Supply Chain Management

Supply Chain Management encompasses the planning and management of all activities involved in sourcing, procurement, conversion and logistics management activities

BUSINESS VALUATION

Choose the most appropriate answer giving justification.

1. **It is assumed that M. Ltd, would realize ₹40 million from the liquidation of its assets. It pays ₹20 millions to its creditors and Preference Shareholders in full and final settlement of their claims. If the number of Equity Shares of M. Ltd is 2 million, the Liquidation per Share would be:**
   (A) ₹1 per Share
   (B) ₹10 per Share
   (C) ₹12 per Share
   (D) ₹15 per Share

2. **Assume that the following details are given for a company: Sales - ₹1,00,000; Costs - ₹75,000; Depreciation - ₹20,000; Tax- 35%; Change in Net Working Capital - ₹1,000; Change in Capital Spending - ₹10,000. The Free Cash Flow to Firm (FCFF) for the given data would be:**
   (A) ₹10,000
   (B) ₹12,250
   (C) ₹13,500
   (D) ₹15,000

3. **Shyam Ltd has announced issue of warrants on 1: 1 basis for its equity share holders. The Exchange ratio is 1.00. The current market price of the stock is ₹10 and warrants are convertible at an exercise price of ₹11.71 per share. Warrants are detachable and are trading at ₹3. What is the minimum price of this warrant?**
   (A) ₹3.00
   (B) Zero
   (C) ₹1.71
   (D) ₹2.00

4. **Given: The growth rate in the dividends is expected to be 8%. The Beta of the stock is 1.60 and the return on the market index is 13%. The required rate of return would be:**
   (A) 14%
   (B) 16%
   (C) 18%
   (D) 20%

5. **Given: The risk-free rate is 5.5%; the market price of risk=7% and the company's Beta=1.2. The Cost of Equity would be**
   (A) 11%
   (B) 13.9%
   (C) 15.2%
   (D) 16.3%

6. **If a company has a P/E ratio of 20 and a ROE (Return on Equity) of 15%, then the Market to Book Value Ratio is**
   (A) 3 times
   (B) 3%
   (C) cannot be calculated from the given information
   (D) None of the above

7. Assume that in a stock market the CAPM is working. A company has presently beta of 0.84 and its going to finance its new project through debt. This would increase its debt/equity ratio to 1.56 from the existing 1.26. Due to increased debt/equity ratio, the company's beta would
(A) increase
(B) decrease
(C) remain unchanged
(D) nothing can be concluded

8. Identify which of the following is not a financial liability?
(A) X Ltd has 1 lakh ₹10 ordinary shares issued
(B) X Ltd has 1 lakh 8% ₹10 redeemable preference shares issued
(C) X Ltd has ₹2,00,000 of 6% bond issued
(D) Both (A) and (B)

9. X Ltd's share beta factor is 1.40. The risk free rate of interest on government securities is 9%. The expected rate of return on the company equity shares is 16%. The cost of equity capital based on CAPM is
(A) 15.8%
(B) 16%
(C) 18.8%
(D) 9%

10. A firm current assets and current liabilities are ₹1,600 and ₹1,000 respectively. How much can it borrow on a short-term basis without reducing the current ratio below 1.25?
(A) ₹1,000
(B) ₹1,200
(C) ₹1,400
(D) ₹1,600

11. If a company has a P/E ratio of 12 and a Market to Book Value Ratio 2.10, then its Return on Equity will be
(A) 14.10%
(B) 17.50%
(C) 25.20%
(D) None of the above

12. A firm has PAT of ₹33.6 lakh with extraordinary income of ₹6 lakh. Cost of capital is 20% and the applicable tax rate is 40%. The value of the firm is
(A) ₹250 lakh
(B) ₹150 lakh
(C) ₹180 lakh
(D) ₹168 lakh

13. Firms that intend to buy only a small percentage of the outstanding stock can buy them in the market, in a process called
(A) Repurchase tender offer
(B) Open market purchase
(C) Privately negotiated repurchase
(D) None of the above

14. ______________ is a measure of value of which tells whether a company is able to generate returns that exceed the costs of capital employed

(A) Cost of capital
(B) Economic Value Added
(C) Market value added
(D) Financial profit

15. If the divestiture value is greater than the present value of the expected cash flows, the value of the divesting firm will
(A) increase on the divestiture
(B) decrease on the divestiture
(C) remains same on the divestiture
(D) None of the above

16. Relative valuation approach is also known as
(A) Market approach
(B) Income approach
(C) Asset approach
(D) Liability approach

17. Efficient Market is one in which security prices fully reflect
(A) the available information
(B) no information
(C) good information
(D) bad information

18. Key to income based approach of valuation is
(A) internal rate of return
(B) capitalization rate
(C) inflation rate
(D) None of the above

19. The value of an asset must equal the ---------------------- of its future cash flows.
(A) Future value
(B) Real value
(C) Present value
(D) expected value

20. A valuation is an objective search for------------------value.
(A) Fair
(B) True
(C) Real
(D) Objective

21. ---------------------- measures the variation of distribution for the expected returns.
(A) Regression
(B) Correlation
(C) Mean
(D) Standard deviation

22. The value of an asset by looking at the pricing of Comparable assets relative to a common variable like earnings, cash flows, book value or sale, is……..
(A) Discounted cash flow valuation
(B) Relative valuation
(C) Contingent claim valuation
(D) Free cash flow valuation

23. Which of the one is not the principles of Valuation

(A) Principles of Substitution
(B) Principle of Time Value of Money
(C) Principle of Risk & Return
(D) Discounted cash flow Valuation

24. ……….. is the Typical price a product fetches in an unregulated market
(A) Value
(B) Price
(C) Valuer
(D) Mutual fund

25. According to basic valuation model, the value of a financial asset is
(A) future value of its expected future cash flows
(B) Contingent value of its expected future cash flows
(C) value of its expected future cash flows
(D) present value of its expected future cash flows

26. Relative valuation is much more likely to reflect
(A) market perceptions and mood than DCF valuation
(B) market perceptions and mood than contingent valuation
(C) contingent and bad information
(D) None of the above

27. The CAPM assumes
(A) efficient capital market
(B) perfect market competition
(C) stock market
(D) None of the above

28. As per Capital Asset Pricing Model (CAPM), the only relevant risk to price a security is
(A) Unsystematic Risk
(B) Systematic Risk
(C) Total risk
(D) Political risk

29. Under Asset based valuation approach individual assets are valued and aggregated in the process of finding
(A) Enterprise value
(B) True value
(C) Real value
(D) Objective value

30. In DCF valuation, the value of an asset is present value of ————cash flows on the asset.
(A) actual
(B) expected
(C) calculated
(D) real

31. A ratio that presents willingness of the stock market to pay for one rupee of earning per share is called __________.
(A) price to Net Profit Ratio
(B) Earnings to Price Ratio
(C) Price to Earnings Ratio
(D) Earnings Ratio

32. If capitalization rate is reduced by growth rate, the Cash Flows should also be reduced by ____________.
(A) capital expenditure
(B) dividend payment
(C) cost of capital
(D) Discounted cash flow

33. The required rate of return may also be called _____________of capital.
(A) cost
(B) opportunity cost
(C) expenditure
(D) none of the above

34. Under DCF valuation technique, higher rates of discount will be used for ....project.
(A) good
(B) risky
(C) Bad
(D) safe

35. In condition of rising prices for change from LIFO to FIFO method,
(A) earnings should fall
(B) earnings should be same
(C) earnings should rise
(D) earnings should be zero

36. Whenever the yield on a bond is more than coupon rate,
(A) The bond will be trading at par
(B) the bond will be trading at a discount
(C) the bond will be trading at a premium
(D) None of the above

37. Increasing the company's future Economic Value Added is key to
(A) Create shareholders' value
(B) Destroy shareholders' value
(C) stock market efficiency
(D) None of the above

38. ………………….. would be applied to the cash flows of a government bond compared to a corporate debenture
(A) A higher discount
(B) A lower discount rate
(C) A discount rate
(D) None of the above

39. Divestitures represent the …………..of a part of a total undertaking.
(A) sale
(B) purchase
(C) holding
(D) leasing

40. Super profit is the excess of future maintainable profits over ____________ expected profits.
(A) normally
(B) abnormally
(C) estimated

(D) computed

41. The stronger a brand of a company is, -------------its risk,
    (A) Higher is
    (B) Lower is
    (C) Nothing can be said regarding
    (D) None of the above

42. A firm having positive PAT but negative EVA is actually ___________ Value.
    (A) destroying
    (B) creating
    (C) changing
    (D) none of the above

43. Which is not a, human capital related intangible asset?
    (A) Trained workforce
    (B) Employment agreements
    (C) Union contracts
    (D) Design patent

44. In a reverse merger a smaller company acquires a
    (A) Smaller company
    (B) Larger company
    (C) FMCG company
    (D) Banking company

45. In a synergistic merger, the post-merger value exceeds
    (A) the sum of the separate companies pre-merger values
    (B) the separate companies pre-merger values
    (C) the separate companies post-merger values
    (D) Enterprise value

46. —————involves splitting up of a large company such as a conglomerate comprising of different divisions, into separate companies.
    (A) Amalgamation
    (B) Demerger
    (C) Share buyback
    (D) Stock split

47. Recent acquisition shows that the price paid for an acquired company is almost invariably higher than its book value and the difference is incorporated under conventional accounting practice as ——.
    (A) Revenue reserve
    (B) Capital reserve
    (C) goodwill
    (D) brand value

48. A theory of Mergers and Acquisitions that explains the result of the winner‘s curse, causing a bidder to overpay is called _____________.
    (A) Synergy
    (B) Agency
    (C) Hubris
    (D) Real value

49. In the ————Approach, the key relationships are computed for a group of similar companies or transactions as a basis for valuation of companies involved in a merger or takeover.
(A) Real Option
(B) Industry
(C) Option
(D) Comparable companies

50. Premium paid by target company to buy-back its shares from a potential acquirer is called ____
(A) Green Shoe Option
(B) Green Bid
(C) Greenmail
(D) Green option

51. Post merger control and the ______ are two of the most important issues in agreeing on the terms of merger.
(A) negotiated price
(B) calculated price
(C) market price
(D) Share price

52. A type of merger ...., takes place when two companies in unrelated lines of business with nothing in common join hands.
(A) Vertical Integration
(B) Horizontal Integration
(C) Conglomerate
(D) Mutual fund

53. Which one of the following is not a measure taken by a target firm to avoid acquisition?
(A) Poison Puts
(B) Poison Calls
(C) Golden Parachute
(D) Flip Over Pill

54. The annual coupon bond with duration of 9 years, coupon of 14% and YTM of 15% will have a modified duration of
(A) 6.9 years
(B) 8.18 years
(C) 7.83 years
(D) 9.78 years

55. A major advantage of Price/Sales ratio is that
(A) It can be used to value firms with negative earnings
(B) It can be used to value firms with negative net worth
(C) Both (A) and (B) above
(D) It can be used effectively in cyclical industries

56. Under _________ method, increasing shareholders wealth is given maximum importance.
(A) Economic Value Added
(B) Constant growth FCFE model
(C) Dynamic true growth model
(D) Variable growth FCFE model

57. A company with PAT of ₹40 lacs, tax rate 50%, RONW of 100%, Reserves of ₹30 lac and a par value of ₹5 will have pre-tax EPS of
(A) ₹4.00
(B) ₹80.00
(C) ₹40.00
(D) Insufficient information

58. P/E rises when:
(A) Growth rises, discount rate falls, reinvestment rate is flat
(B) Growth falls, discount rate falls, reinvestment rate rises
(C) Growth exceeds, discount rate and reinvestment rate falls short of growth
(D) Discount rate falls and reinvestment rate rises

59. An investment is risk free when actual returns are always _______ the expected returns.
(A) equal to
(B) less than
(C) more than
(D) depends upon circumstances

60. In valuing a firm, the _________ tax rate should be applied to earnings of every period
(A) marginal
(B) effective
(C) average
(D) maximum

61. In the context of an acquisition of a firm, which one of the following concepts of value is least relevant?
(A) Market Value
(B) Opportunity Cost
(C) Synergy Value
(D) Value Gap

62. Shareholders of target companies are typically paid in
(A) Government bonds held by the target company
(B) Government bonds held by the acquiring company
(C) Cash and / or shares of the acquiring company
(D) None of the above

63. If the expected rate of return on a stock exceeds the required rate,
(A) the stock is experiencing super normal growth
(B) the stock should be sold
(C) the company is not probably trying to maximize price per share
(D) the stock is a good buy

64. Which of the following items would not be included in a WACC calculation?
(A) Proportion or weight of debt
(B) Proportion or weight of equity
(C) Personal tax rate on interest payments
(D) Cost of equity

65. In calculating Market Value added of the company ________ is/are considered.
(A) Market value of equity
(B) Market value of debt
(C) Both (A) and (B)
(D) Only economic value added

66. An investment is risk free when actual returns are always __________ the expected returns.
(A) Equal to
(B) Less than
(C) More than
(D) Depends upon circumstances

67. Duration of a bond will __________ when the yield-to-maturity on the bond increases.
(A) Decrease
(B) Increase
(C) not change
(D) all three above are possible

68. A bond of a company is trading at a premium at present. It is expected that in future its price will _________ with the passage of time keeping other factors constant.
(A) decrease
(B) increase
(C) not change
(D) All three above are possible

69. Which of the following is a financial liability for a company?
(A) X Ltd. has issued 10 crores of ₹10 each equity shares
(B) X Ltd. has issued 10 crores of ₹10 each cumulative redeemable preference shares
(C) X Ltd. has issued 10 crores of ₹10 each non-cumulative compulsorily convertible preference shares
(D) Both (B) and (C)

70. A Company based on up-to-date financial statements has determined that the current Free Cash Flows to Equity (FCFE) per share is ₹1.00. It has outstanding number of shares 100 crores with a face value of ₹10 each. Its interest expenses are ₹30 crores and tax rate is 30%. Given this information, The Free Cash Flow to the Firm (FCFF) will be
(A) ₹109 crores
(B) ₹112 crores
(C) ₹121 crores
(D) ₹130 crores

71. Estimated fair value of an asset is based on the ________ value of operating cash flows.
(A) current
(B) future
(C) discounted
(D) None of the above

72. SBT Ltd. has an issued and paid up Capital of 100000 shares of ₹100 each. The company declared a dividend of ₹25 lakh during the last five years and expects to maintain the same of level of dividends in the future. If the average dividend yield for

the listed companies in the same line of business is 16%, then value per share of SBT Ltd. is
(A) ₹150.50
(B) ₹156.25
(C) ₹160.50
(D) Insufficient information

73. ANINY LTD. earned free cash flow to Equity shareholders during the financial year ended-2019 at ₹5 lakh. If its cost of equity is 12% and free cash flow to Equity (FCFE) is expected to grow forever at 10%, what will be value of ANINY LTD. (using FCFE valuation approach)?
(A) ₹450 lakh
(B) ₹300 lakh
(C) ₹275 lakh
(D) None of the above

74. Smith Ltd. has announced issue of warrants on 1:1 basis for its equity shareholders. The warrants are convertible at an exercise price of ₹15. Warrants are detachable and trading at ₹7. What is the minimum price of the warrant if the current price of the stock is ₹20?
(A) ₹4
(B) ₹5
(C) ₹7
(D) ₹15

75. The value of Alpha Ltd. and Beta Ltd. are ₹50 lakh and ₹25 lakh respectively. On merger their combined value ₹94 lakh. If Beta Ltd. receives premium on merger ₹15 lakh, what will be the synergy gain for merger?
(A) ₹19 lakh
(B) ₹24 lakh
(C) ₹34 lakh
(D) None of the above

76. A company with PAT of ₹60 Crores, Tax Rate 30% plus a cess of 3%, Return on Equity is 20%, Other Equity ₹225 Crores, PAT of the Company is growing by 8% per year and equity share with a par value of ₹10 will have EPS of
(A) ₹2
(B) ₹8
(C) ₹10
(D) Insufficient information

77. A Limited is considering to acquire B Limited through all shares deal. Relevant information about these companies are given below

Particulars	A Limited	B Limited
Present Earnings - (₹in crores)	₹7.50	₹2.50
No. of Equity Shares (in crores)	4	2
Price/Earnings Ratio	10	9

Given the above information, the exchange ratio based on the market price will be
(A) 0.60
(B) 0.67
(C) 0.93
(D) 1.67

Answer:

(1) (B) ₹10 per Share
Liquidation/share= (₹40 million - ₹20 million)/2 million = ₹10 per share

(2) (B) ₹12,250

Sales – Costs – Depreciation	5,000
Less : Tax	1,750
PAT	3,250
Add: Depreciation	20,000
Less: Change in Net Working Capital	1,000
Less: Change in Capital Spending	10,000
Free Cash Flow to Firm (FCFF)	12,250

(3) (B) Zero
Minimum Price = (Market Price of Common Stock-Exercise Price) × Exchange Ratio
= (₹10.00 - 11.71) × 1.0 = ₹1.71.
Thus, the minimum price of this warrant is considered to be zero, because things simply do not sell for negative prices

(4) (B) 16%
Required rate of Return = $R_f+\beta(R_m-R_f)$ = 8% + 1.60 (13% - 8%)
= 8+1.6 × 5 = 8 + 8 = 16%

(5) (B) 13.9%
Cost of Equity=5.5% + 7% (1.2) =13.9%

(6) (A) 3 times
(Since P/E x ROE = 20 x 0.15)

(7) (C) remain unchanged
(Because as per CAPM the company specific risk has no impact on the systematic risk)

(8) (A) X Ltd has 1 lakh ₹10 ordinary shares issued
A share is an indivisible unit of capital, expressing the proprietary relationship between the company and the shareholder

(9) (C) 18.8%
9% + 1.40 (16% - 9%)] = 9% + 9.8% = 18.8%

(10) (B) ₹1,200
Amount of borrowing be x [current asset will increase because borrowing will increase the cash amount]
1600 + X divided by 1000 + X = current ratio 1.25 X = 1400

(11) (B) 17.50%
Return on Equity will be 17.5% (= 2.10/12)

(12) (B) ₹150 lakh
PAT = 33.6 lacs
PBT = (33.6/0.6) lacs = 56 lacs
Less: extraordinary income = <u>6 lacs</u>
= 50 lacs
Less: Tax @ 40% = <u>20 lacs</u>
= 30 lacs
Value = 30 lacs / 0.20 = 150 lacs

(13) (B) Open market purchase

(14) (B) Economic Value Added

(15) (A) increase on the divestiture
How does a divestiture affect a firm's value?
To answer this question, need to compare the price received on the divestiture to the present value of the expected cash flows that the firm would have from the divested assets.
If the divestiture value is greater than the present value of expected cash flows, the value of the firm will increase on divestiture

(16) (A) Market approach
(17) (A) the available information
(18) (B) capitalization rate
(19) (C) Present value
(20) (B) True
(21) (D) Standard deviation
(22) (B) Relative valuation
(23) (D) Discounted cash flow Valuation
(24) (A) Value
(25) (D) present value of its expected future cash flows
(26) (A) market perceptions and mood than DCF valuation
(27) (B) perfect market competition
(28) (B) Systematic Risk
(29) (A) enterprise value
(30) (B) expected
(31) (C) Price to Earnings Ratio
(32) (A) capital expenditure
(33) (B) opportunity cost
(34) (B) risky
(35) (C) earnings should rise
(36) (B) the bond will be trading at a discount
(37) (A) Create shareholders' value
(38) (B) A lower discount rate
(39) (A) sale
(40) (A) normally
(41) (B) Lower is
(42) (B) creating
(43) (D) Design patent
(44) (B) Larger company
(45) (A) the sum of the separate companies pre-merger values
(46) (B) Demerger
(47) (C) goodwill
(48) (C) Hubris
(49) (D) Comparable companies
(50) (C) Greenmail
(51) (A) negotiated price
(52) (C) Conglomerate
(53) (B) Poison Calls
(54) (C) 7.83 years

Modified duration = {9 / (1 + 0.15)}

(55) (C) Both (A) and (B) above

Price/Sales ratio is the multiplication of P/E ratio to profit margin. It can be used to value firms with negative earnings and negative net worth

(56) (A) Economic Value Added

The theory of Economic Valued Added has traditionally suggested that every company's primary goal is to maximize the wealth of shareholders

(57) (C) ₹40.00

PBT = 80 lac, i.e. 40/5,
RONW = PAT/NW = 40/NW = 100%,
So NW = 40lac,
Value of equity shares = 40-30 = 10 lac,
No. of Shares = 10/5 = 2 lac, so Pre tax EPS = 80/2 = 40Lac

(58) (D) Discount rate falls and reinvestment rate rises

The P/E ratio (price-to-earnings ratio) of a stock also called its P/E, or simply ―multiple‖ is a measure of the price paid for a share relative to the annual Earnings per share.

Price of stock will rise if discount rate falls and reinvestment rate increases which in turn will increase the P/E ratio

(59) (A) equal to

(60) (A) marginal

(61) (B) Opportunity Cost

(62) (C) Cash and / or shares of the acquiring company

(63) (D) the stock is a good buy

The stock is a good buy, as the investor will earn higher than required rate

(64) (C) Personal tax rate on interest payments

Personal tax rate on interest payments is not relevant, it is the corporate tax rate applicable to the company that may be relevant

(65) (C) Both (A) and (B)

As both market value of equity as well as market value of debt are required to be considered

(66) (A) Equal to

As risk free investments give an assured fixed rate of return like government securities, where interest and principal repayment is guaranteed by the Central /State Government

(67) (A) Decrease

Duration of a bond has a negative or inverse relation with YTM (Yield-to-Maturity). Higher the YTM, lower will be the duration of a bond hence duration of a bond will "Decease"

(68) (A) decrease

The bond is presently trading at a premium and when it approaches to its maturity, its price will converge to par value. Hence, its price in future will decrease

(69) (B) X Ltd. has issued 10 crores of ₹10 each cumulative redeemable preference shares

The reason is that the cumulative redeemable preference shares are financial liability of the company because the company is under obligation to pay dividend and redeem at the maturity

(70) (C) ₹121 crores

Particulars	Amount
FCFE (Per Share)	1.00
No. of Shares (in crores)	100.00
Total FCFE (in crores)	100.00
Plus [Interest × (1 – tax rate)] (in crores)	21.00
Therefore, Free Cash Flows to the Firm (in crores) will be	121.00

(71) (C) discounted

In Discounted Cash Flow (DCF) Valuation, the value of an asset is the present value of the expected cash flows on the asset

(72) (B) ₹156.25

Dividend per share = 25,00,000 / 1,00,000 = ₹25

Dividend yield = 16%

Value per share = 25 / 0.16 = ₹156.25

(73) (C) ₹275 lakh

According to FCFE Valuation Approach:

V_0 = ($FCFE_i$) / (K_e-g)

= (5 x 1.10) / (0.12 - 0.10) = 5.5 / 0.02 = ₹275 lakh

(74) (B) ₹5

Minimum Price Warrant of Smith Ltd : (Current Stock Price - Exercise price of Warrant) x (Exercise Ratio):

= (20 -15) x 1 = ₹5

(75) (A) ₹19 lakh

Synergy gain for Merger: Combined Value-Value of Merging Companies = ₹ [(94) - (50 + 25)] = ₹19 lakh (Premium on merger is irrelevant)

(76) (B) ₹ 8

PAT	60
ROE	20%
Total Equity (PAT/ROE)	300
Other Equity	225
Share Capital (Total Equity - Other Equity)	75
No. of Shares (Share Capital / Par Value of the share) (crore)	7.5
EPS = PAT ÷ No. of share = 60 / 7.5 = EPS	8

(77) (A) 0.60

Particulars	**A Limited**	**B Limited**
Present Earnings (₹in crores)	7.50	2.50
No. of Equity Shares (in crores)	4	2
Price/Earnings Ratio	10	9
EPS	1.875	1.250
Market Price	18.75	11.25
Exchange Ratio (11.25 / 18.75)	**0.60**	

Notes

Behind every successful business decision, there is always a CMA

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