

Exam 3 Fall 2002 FINC 4532 Answer Key

Closed Book

1. Total Current Assets – Total Current Liabilities
2. False
3. False
4. C
5. Increases in Current Assets associated with seasonality in sales.
6. True
7. False, always formal, but may also be guaranteed by payment of upfront fee.
8. False, would be true except for the comments about interest “rates.”
9. A
10. True
11. E, since increase in AR exceeds decrease in Inventory
12. D
13. E
14. True
15. A

Open Book

1.

Two points:

1. the AR of 135000 is irrelevant, as we have no idea how long that has been on the books.
2. The Net 30 actually implies everything is collected the following month, so I gave credit for the below answer as well as assuming collection the following month.

	Dec	Jan	Feb	March
Sales	95000	55000	65000	65000
Collections				
Month of	47500	27500	32500	32500
Following		47500	27500	32500
Purchases	32500	32500		
Payment for Purchases		-47500	-27500	-32500
Collections		+75000	+60000	+65000
Purchase Payments		-47500	-27500	-32500
Wages		-16500	-19500	-19500
Dividend				-100000
Taxes		-40000		
Net Cash Flows		-29000	+13000	-87000
Beginning Cash		41000	25000	25000
Available Balance		12000	38000	-62000
Minimum Cash Balance		25000	25000	25000
Borrowings		13000		87000
Repayment			13000	
Ending Cash Balance		25000	25000	25000
Cumulative Borrowing		13000	0	87000

2. (24 points) Your company has \$0 in its checking account. Your company needs to borrow money, such that it has a \$60,000 remaining balance at the end of one year. You are offered the following loans, all with a quoted 6% annual interest rate. Two question for each loan. 1) What amount must you borrow today in order to have \$60,000 at the end of one year? What is the effective annual interest rate for each loan?

Simple Interest

Initial Loan Amount = 60000 Effective Interest Rate = 6%

Discount Interest

Initial Loan Amount = 63829.79 Effective Interest Rate = 6.383

Discount Interest with a 10% compensating balance

Initial Loan Amount = 71428.57 Effective Interest Rate = 7.14

Add-on Interest

Initial Loan Amount = not graded Effective Interest Rate = 11.46

3. (5 points) Wildthing Amusement Company's total assets fluctuate between \$320,000 and \$410,000, while its fixed assets remain constant at \$260,000. If the firm follows a maturity matching or moderate working capital financing policy, what is the likely level of its long-term financing?

e. \$320,000, as you finance both long-term and permanent short term assets with long-term financing