Closed book

1. Character, capacity, capital, collateral, and conditions
2. It categorizes inventory into 3 groups-A, B, or C-on the basis of critical needs. The most important things go into category A and the least into category C
3. A
4. clearly stated objectives, assumptions, strategies, contingency plans, budgets, a financial program, and pro forma financial statements.
5. C
6. A
7. B
8. D
9. A
10. B
11. A
12. B
13. D
14. A
15. D
16. E
17. B

Open book

1. (15 points) Your company has $0 in its checking account. Your company needs to borrow money for one year, such that it has a $125,000 remaining balance at the end of one year. You are offered the following loans, all with a quoted 8% annual interest rate. Two question for each loan. 1) What amount must you borrow today in order to have $125,000 at the end of one year? What is the effective annual interest rate for each loan?

   Interest in Arrears
   Initial Loan Amount = ___125000____ Effective Interest Rate = ____8%___

   Discount Loan
   Initial Loan Amount = ____135875____ Effective Interest Rate = ___8.7%___

   Interest in Arrears with a 15% Compensating Balance
   Initial Loan Amount = ___147058____ Effective Interest Rate = ___9.41____

   Discount Interest with a 15% compensating balance
   Initial Loan Amount = ____159846____ Effective Interest Rate = ___10.39%___

2. (12 points) For the following trade credit terms, what are the effective and nominal rates.

   3/10, net 30 Nominal Rate  56.44%  Effective Rate  74.35%
   1/20, net 45 Nominal Rate  14.75%  Effective Rate  15.8%
   2/10, net 15 Nominal Rate  149%  Effective Rate  337%
   1/30, net 60 Nominal Rate  12.29%  Effective Rate  13.01%
3. (12 points) Pemini Beverage has the following historical balance sheet:

- Cash $220
- Accounts payable $204
- Accounts receivable $60
- Notes payable $130
- Inventory $312
- Accruals $36
- Total current assets $592
- Current liabilities $370
- Net plant & equipment $420
- Long-term bonds $260
- Common stock $270
- Retained earnings $112
- Total assets $1,012
- Total liabilities & equity $1,012

Next year Gemini's sales are forecast to increase from 1200 to 1440. Several balance sheet items vary directly with sales as follows: Accounts Receivable= 5%, Inventory=26%, Net Plant and Equipment=35%, Accounts payable =17%, Accruals = 3%. Cash will remain at $220. The firm has no plans to issue long-term securities. The firm's net profit margin is 10%. The firm pays out 50% of net income as dividends. Write out the new balance sheet, use the Notes Payable account as a plug account to make your balance sheet balance. It is OK if the Notes Payable is negative on your pro forma statement.

<table>
<thead>
<tr>
<th>Item</th>
<th>Historical</th>
<th>New</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cash</td>
<td>$220</td>
<td>$220</td>
</tr>
<tr>
<td>Accounts receivable</td>
<td>$60</td>
<td>$72</td>
</tr>
<tr>
<td>Inventory</td>
<td>$312</td>
<td>$374.4</td>
</tr>
<tr>
<td>Total current assets</td>
<td>$592</td>
<td>$666.4</td>
</tr>
<tr>
<td>Net plant &amp; equipment</td>
<td>$420</td>
<td>$504</td>
</tr>
<tr>
<td>Total assets</td>
<td>$1,012</td>
<td>$1,170.4</td>
</tr>
</tbody>
</table>

- Accounts payable $204 x 1.2 = $244.8
- Notes payable $130 x 1.2 = $168.4
- Accruals $36 x 1.2 = $43.2
- Current liabilities $370 x 1.2 = $456.4
- Long-term bonds $260
- Common stock $270
- Retained earnings $112 x 1.2 = $184

Total liabilities & equity $1,012 x 1.2 = $1,170.4

Cash     Accounts payable    Notes payable
$220     $244.8              $168.4
Accounts receivable Notes payable Accruals
$72      $168.4              $43.2
Inventory Current liabilities
$374.4   $456.4
Net plant & equipment Long-term bonds Common stock Retained earnings
$504     $260     $270     $184
Total assets Total liabilities & equity
$1,170.4 $1,170.4