Project Financing

The sample questions are related to the AIBP Specialization course "***Project Financing***". The students are advised to thoroughly read the exam guidelines and the course syllabus for this course before start studying for the paper. The questions are shared to give an idea to the student about the paper format and types of questions. For further information visit the IBP website www.ibp.org.pk

Multiple Choice Questions

Each MCQ carry one mark.

Q1. If a scooter manufacturing unit adds motor cycles to its product line, it is called as

A. Vertical Integration

B. Concentric Integration (Answer)

C. Conglomerate Integration

D. Horizontal Integration

Q2. An investment by Polka Motors to replace old machinery to improve productivity represents a:

A. Tactical investment (Answer)

B. Strategic investment

C. Expansion investment

D. Mandatory investment

Q3. Which of the following is a capital budgeting technique that is NOT considered as discounted cash flow method?

A. Payback period (Answer)

B. Internal rate of return

C. Net present value

D. Profitability index

Constructed Response Question

Each CRQ carry five marks.

Question:

A). List strengths and weaknesses of any THREE investment decision rules. **(3 Marks)**

B). Suggest why it is necessary to use two or more investment decision rules? **(2 Mark)**

Answer:

Part-A:

Payback
No accounting for cash flows received subsequent to the cutoff date,
No explicit adjustment for either the timing or the uncertainty of future cash flows,
No an objective standard, Useful for "small routine" expenditure decisions.
Internal Rate of Return
Subject to pitfalls associated with sequencing, timing, and scale problems,
Existence of multiple internal rates of return, misleading impression that the internal rate of return is a multipored rate of return, implicit adjustment for both the timing or the uncertainty of future cash flows, when used properly, the IRR provides an objective standard for capital investment decisions
Net Present Value (Discounted Cash Flow)

- Explicit adjustment for both the timing or the uncertainty of future cash flows,
- Objective standard of measurement,
- Clear economic interpretation.

Considering payback Considering payback and internal rate of return:
The payback rule fails to consider cash flows occurring subsequent to the cutoff date, a company that relies solely on the payback rule would consider the two projects to be equally desirable. While most companies do in fact supplement the payback rule with evaluations based either on the average accounting rate of return or some kind of internal rate of return criteria.

Part-B
In case of abnormal cash flow IRR cannot be calculated whereas NPV can be used. Thus, it may be suitable to use two decision rules to reach a firm decision.

Please note: Candidate may provide a comparison of any other decision rule thus the reasoning may be changed.

Extended Response Question

Each ERQ carry ten marks.

Question:

The ABC company applied for a project finance loan amounting Rs. 00,000/- for a period of 5 years. The data for ABC Company is:

Debt Equity Ratio	**1:1**
Profit margin	**6%**
Return on Total Asset	**9%**
Return on Equity	**30%**
Total asset turnover	**1.5 times**

- Equity = 75,000/-
- Liabilities = 175,000/-
- Assets = 250,000/-

Show your analysis and state your decision whether to finance the company or not? Give at least FOUR reasons for rejection / approval. **(10 Marks)**

Answer:
Loan approved. (Define)

Reasons for approval: (Explain)

1. Future cash flows positive
2. Moderate Leverage
3. Profit margin is positive
4. Loan amount is lower than threshold of 125,000/-