SAMPLE QUESTIONS - PART 3

Section A. Strategic Planning

1. A company is undertaking a growth strategy of acquiring other companies which supply the inputs to its original line of business. This strategy is called

   a. horizontal growth.
   b. vertical growth.
   c. conglomerate diversification.
   d. concentric diversification.

2. Samsec Inc. has four major divisions, each doing business in a different market. Market growth rates and relative competitive positions for each of these four divisions are shown below. A relative competitive position is defined as the division's market share relative to the market share of the next largest competitor in the industry.

	Business growth rate	Relative competitive position
Division A	13%	4%
Division B	12%	110%
Division C	5%	12%
Division D	4%	170%

   Which division is **most** likely to have the strategic potential to generate a significant level of cash?

   a. Division A.
   b. Division B.
   c. Division C.
   d. Division D.

3. Just-in-time inventory systems have been increasingly popular over the last twenty years. Which one of the following is the **most** critical component of just-in-time systems?

   a. The parts delivered by vendors must be received on time and meet quality specifications.
   b. Actual sales to end users must be consistently close to forecasted sales.
   c. The production facility must completely fill the space available.
   d. Management must disclose major corporate decisions to workers.

4. Which one of the following areas of SWOT analysis is **most** likely to be considered a positive, external factor?

   a. the company's strengths
   b. the company's weaknesses
   c. the company's opportunities
   d. the company's threats.

Section B. Strategic Marketing

5. Which one of the following is the **best** advantage of marketing a product to a specific market segment?

   a. Each consumer's needs and wants are different.
   b. Mass marketing can provide the low costs of long production runs.
   c. The company can better design, price and deliver the product to a market segment.
   d. Each segment can be reached by a different mix of marketing channels.

6. In marketing hair brushes as its single product, Hollow Company uses one marketing mix, believing all hair brush users have similar needs. Such an approach to target marketing is called

   a. mass marketing.
   b. market segmentation.
   c. micromarketing.
   d. concentrated marketing.

7. Many retail stores have found that it is more profitable to sell a product carrying the store's private brand name as opposed to the more well-known national brands. Which one of the following is the **best** explanation of this?

   a. The private brand costs more to manufacturer.
   b. The marketers of the national brand spend a lot for advertising.
   c. The retailer can charge more for the private brand.
   d. The national brand generally has a better reputation for quality.

8. Many new products, especially electronics, are often priced very high when the product is introduced, but the price will come down over time. Which one of the following is the **best** explanation of this pricing practice?

   a. The first manufacturer of the product wants to quickly recover its R&D costs.
   b. The first manufacturer knows that early adapters will pay the high price for the new product.
   c. The first manufacturer wants to expand the market quickly, to maintain its lead over competitors.
   d. The first manufacturer wants to ensure profits before competitors copy the product.

Section C. Corporate Finance

9. A firm has daily receipts averaging $100,000. A bank has offered to reduce the collection time on the firm's deposits by one day for a monthly fee of $400. If money market rates are expected to average 6% during the year, the net annual benefit from using this service is

   a. $0.
   b. $1,200.
   c. $6,000.
   d. $12,000.

10. Cleveland Masks and Costumes Inc. (CMC) has a majority of its customers located in the states of California and Nevada. Keystone National Bank, a major west coast bank, has agreed to provide a lock-box system to CMC at a fixed fee of $50,000 per year and a variable fee of $0.50 for each payment processed by the bank. On average, CMC receives 100 payments per day, each averaging $10,000. With the lock-box system, the company's collection float will decrease by 2 days. The annual interest rate on money market securities is 4%. If CMC makes use of the lock-box system, what would be the net benefit to the company? Use 365 days per year.

    a. $11,750.
    b. $68,250.
    c. $18,250.
    d. $80,000.

11. On January 1, Scott Corporation received a $300,000 line of credit at an interest rate of 8% from Main Street Bank and drew down the entire amount on February 1. The line of credit agreement requires that an amount equal to 10% of the loan be deposited into a compensating balance account. What is the effective annual cost of credit for this loan arrangement?

    a. 7.27%
    b. 8.00%.
    c. 8.89%.
    d. 10.00%.

12. Keller Industries currently has a capital structure consisting of 40% debt and 60% equity, which it believes is the optimal structure. The common stock produced a 7% capital gain in the recent 12-month period and the dividend yielded 5%. Keller's effective income tax rate is 30%. Its debt is rated AA and the issues outstanding are currently yielding 8%.

Keller's marginal cost of capital is approximately

a. 7.0%.
b. 8.0%.
c. 9.4%.
d. 10.4%.

13. Three years ago, an investor required a 15% return for an investment in a high tech stock. But now, the same investor requires a 25% return in the same stock. Which one of the following **best** describes a change that may explain why the required return increased?

a. The Federal Reserve increased the Fed Funds rate.
b. This investor is expecting a large increase in the market risk premium.
c. The beta for this stock has decreased significantly.
d. The company's profits have increased and become less volatile.

14. A casual restaurant chain is considering a major change to their menu. Which one of the following issues should the chain consider **first**?

a. Determine the strategic issues
b. Identify the alternative actions
c. Select on of the choices
d. Evaluate the performance

15. In a make-versus-buy decision, which one of the following is **not** considered a relevant cost?

a. Factory management costs.
b. Variable manufacturing costs.
c. Avoidable fixed costs.
d. Costs of materials.

16. Many companies use cost/volume/profit analysis to assist in their operating decisions. Which one of the following conditions may make CVP analysis difficult to use?

    a. The product is in the early stages of its life cycle.
    b. The company must increase sales to reach the break-even point.
    c. Fixed costs are a majority of the total costs of the product.
    d. Variable costs increase much more quickly than unit sales.

17. Smithtown Corporation expects to sell 5,000 units of its product at a target price of $100 per unit. The current full cost of the product is $75 per unit. If Smithtown wants to earn an operating profit margin of 20%, the target cost per unit is

    a. $20.
    b. $75.
    c. $80.
    d. $100.

18. Polaris Company sells refrigeration components both in the U.S. and to a subsidiary located in France. One of the components, Part No. 567, has a variable manufacturing cost of $35. The part can be sold domestically or shipped to the French subsidiary for use in the manufacture of a residential subassembly. Relevant data with regard to Part No. 567 are shown below.

	Part No. 567
Domestic selling price	$ 70
Shipping charges to France	15
Cost of acquiring Part No. 567 in France	80
French residential subassembly:	
Sales price	180
Other additional manufacturing costs	60
Units shipped to France	200,000[1]

[1]If deemed preferable, these units could be sold in the U.S.

Polaris' applicable income tax rates are 40% in the U.S. and 70% in France.

Polaris will transfer Part No. 567 to the French subsidiary at either variable manufacturing cost or the domestic selling price. On the basis of this information, which one of the following strategies should be recommended to Polaris' management? (assume no fluctuations in Euro/ US$ exchange rate)

a. Transfer 200,000 units at $35 and the French subsidiary pays the shipping costs.
b. Transfer 200,000 units at $70 and the French subsidiary pays the shipping costs.
c. Sell 200,000 units in the U.S. and the French subsidiary obtains Part No. 567 in France.
d. Transfer 200,000 units at $70 and have the U.S. company absorb the shipping costs.

Section E. Investment Decisions

19. Adams Corporation uses net present value techniques in evaluating its capital investment projects. The company is considering a new equipment acquisition that will cost $100,000, fully installed, and have a zero salvage value at the end of its five-year productive life. Adams will depreciate the equipment on a straight-line basis for both financial and tax purposes. Adams estimates $80,000 in annual recurring operating cash income and $25,000 in annual recurring operating cash expenses. Adams' cost of capital is 10% and its effective income tax rate is 35%. What is the net present value of this investment on an after-tax basis?

a. $26,537.
b. $35,528.
c. $35,750.
d. $62,065.

20. Omega Inc., a large conglomerate with operating divisions in many industries, uses risk-adjusted discount rates in evaluating capital investment decisions. Consider the following statements concerning Omega's use of risk-adjusted discount rates.

    I. Omega may accept projects only with internal rates of return greater than Omega's overall average cost of capital.
    II. Discount rates vary depending on the type of project.
    III. Omega may reject some projects with internal rates of return greater than the cost of capital.
    IV. Discount rates may vary depending on the division.

    Which of the above statements are correct?

    a. I and III, only.
    b. II and IV, only.
    c. II, III and IV, only.
    d. I, II, III and IV.

21. Tectronics Inc. has a project that requires a $35,000,000 initial investment, and is expected to generate incremental after-tax cash flows of $6,000,000 for each of the next 10 years. Tectronics's weighted average cost of capital is 14%. This project's net present value (NPV) is

	NPV
a.	-$35,000,000
b.	-$25,000,000
c.	-$3,704,000
d.	+$31,296,000

22. Bedrock Corporation is considering buying and developing a silver mine. If the price of silver declines below the variable costs of mining it, Bedrock has the ability to close the mine at minimum cost. This ability to close the mine

    a. reduces the likelihood Bedrock will develop the mine.
    b. adds value to the mine, in addition to discounted cash flow.
    c. guarantees that Bedrock will not lose money on the mine project.
    d. can be traded on one or more public option exchanges.

23. On rare occasions, a capital budget analyst will find a project that has an internal rate of return below the weighted average cost of capital, but a positive NPV. Which one of the following is the **best** explanation for these conflicting results?

    a. The analyst made a calculation error.
    b. The proposed project requires additional cash-out payments in later periods.
    c. The NPV method is not theoretically sound.
    d. The IRR is based on more conservative assumptions than the NPV.

24. QLP Corporation is planning to build a new plant but wishes to complete a capital budgeting analysis before deciding to proceed with construction. The following cost data has been collected. The land on which the plant will be built was purchased eight years ago for $1,300,000, but a recent appraisal indicates that the current value of the land is $2.2 million. The plant will cost $8.7 million to construct. Last year, QLP paid a consulting company $650,000 for an environmental impact study on the new plant. What total cost figure should QLP Corporation use in a capital budgeting analysis of the new plant?

a. $1,310,000.
b. $1,960,000.
c. $10,900,000.
d. $11,550,000.

Sample Questions Part 3 - Answers

Question#	Key
1	B
2	B
3	A
4	C
5	C
6	A
7	B
8	B
9	B
10	A
11	C
12	C
13	B
14	A
15	A
16	D
17	C
18	C
19	D
20	C
21	C
22	B
23	B
24	C