Victoria university of Bangladesh
Final Assessment
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Introduction to Finance - FIN 322

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Answer to the question no-2

sales	Firm A	Firm B
A: 40/100 × 20,00,000	20,00,000	30,00,000
B: 30/100 × 30,00,000	8,00,000	9,00000
Contribution	12,00,000	21,00,000
Less: Fixed Cost: A	5,00,000	
Firm B		7,00,000
Operation Profit	7,00,000	14,00,000
Less: Interest: Firm A	1,00,000	
" B		1,25,000
	6,00,000	12,75,000

(a) Financial Leverage $= \frac{\text{EBIT (operating Profit)}}{\text{EBT (Earnings before Tax)}}$

Firm A $= \frac{7,00,000}{6,00,000}$; Firm B $= \frac{14,00,000}{12,75,000}$

Firm A = 1.16 times ; Firm B = 1.09 times

(b) operating Leverage $= \frac{\text{EBIT (operating Profit)}}{\text{EBT (Earnings befor tax)}}$

Firm A $= \frac{12,00,000}{7,00,000}$; Firm B $= \frac{21,00,000}{14,00,000}$

Firm A = 1.71 times Firm B = 1.5 times

Firm A has greather business and financial risk than Firm B.

Answer to the question no-4

Midterm financing differs from short term financing in that its maturity is at least one year and may be up to 5 or 10 years. It is sometimes defined collateral based installment loan made by a bank running for a period up to as much as 10 years.

Scholars view:-

(i) Term loan is a loan made by a bank/financial institution to a business having an initial to maturity of more than 1 year - Khan and Jain.

(ii) Term loan is a debt originally scheduled for repayment in more than 1 year but generally in less than 10 years - Van Horne.

(iii) Term finance represents a source of debt finance which is generally repayable in less than 10 years. Prasanna Chandra.

We regard mid term financing an involving final maturities of one to ten years. In only a few cases. term finance exceed 10 years and most typical term is 5 to 7 years. Mid-term finance is known as term loan, medium term finance, intermediate finance, Project finance, term finance ect.

Different features and sources of mid-term financing there are given below :-

Features :-

(i) maturity :- Maturity of term finance typically range from 1 to 10 years, with the maturity of loans drawn for less then 5 years.

(ii) Repayment :- The repayment schedule for the loan usually can be made to fit the needs of each borrower, Most common arrangment calls for amortization the loan with equal annual semiannual, quarterly or monthly installment payments.

(iii) Interest Rate :- The interest rate on most term loans is variable and tied to the payment lending rate.

(iv) Collateral :- Many term loans are secured by assets, specially borrowing is used to acquire to specific high value items equipment, building, land and machinery.

(v) use of Funds :- Term loans primarily provide working capital and secondary plan and equipment financing.

(vi) size of loan :- The term loan is a small loan in term of its amount. Banks usally make the smaller and shorter term loans.

(vii) Flexibility :- Mid-term financing is very flexible, so, the borrower can change and term and the condition of the contract for his benefit with the consent of lender.

(viii) Renewal :- The agreement of the financing is renewable.

Sources :-

(i) Commercial Bank :- The majority of term loans are made by commercial banks. The banks prefer to make term loans of less than five years maturity.

(ii) Insurance Company :- insurance companies have a highly predictable flow of funds. They prefer loan term arrangement unto 10 years or more.

(iii) Finance Company :- term finance is made from finance company which is specialized financial institution.

(iv) Development Bank :- Development bank is generally specialized bank which provides term loan for special sector in the economy.

(v) Development Agencies :- Government and nongovernmental agencies provide term loans for the establishing, expanding, and modernizing in small and medium industries.

(vi) NGO :- NGO is another source of term loan. They provide loans for poor people rural area like Grameen bank.

(vii) Equipment financing :- The borrower may find fund to finance machinery and equipment from several sources. The major sources of this financing are bank, direct vendor or leasting company.

(viii) Donor Agency :- Different types of foreign doner agencies are providing the mid term financing

Answer to the question no-5

Dividend refers to a reward cash or otherwise that a company gives to its shareholders. Dividends can be issued in various forms, such as cash payment, stocks or any other form. A company's dividend is decided by its board of director and it requires the shareholder's approval.

Leverage is an investment strategy of using borrowed money-specifically, the use of various financial instruments or borrowed capital to increase the potential return of an investment. Leverage can also refer to the amount of debt a firm uses to finance assets.

The ~~factors~~ factors influencing dividend policy there are given below :-

(i) Stability of earnings :- stability of earning is one of the important factors influencing the dividend policy. if earnings are relatively stable a firm is in a better position to predict what its future earnings will be and such companies are more likely to pay out a higher percentage

(ii) Financing Policy of the company :- Dividend policy may be affected and influenced by financing the dividend policy of the company. it will have to pay less dividend to shareholders.

(iii) Liquidity of funds :- The liquidity of funds is an important consideration in dividend to decisions. According to dividends out of Profits a cash dividend only be paid from money in the bank.

(iv) Dividend Policy of competitive concerns :- Another factor which influences is the dividend Policy of other competitive concerns in the market.

(v) Past Dividend Rates :- if the firm is already existing the dividend rate may be decided one the basis of dividends declared in the previous years.

(vi) Debt obligations :- A firm which has incurred heavy indebtedness, is not in a position to pay higher dividends to shareholders.

(vii) Ability to Borrow :- Every company requires finance both for expansion programmes as well as for meeting unanticipated expenses. Hence, the companies have to borrow from the market, .

(viii) Growth needs of the company :- Another factor which influences the rate of dividend is the growth needs of the company.

(ix) Profit Rate :- Another important consideration for deciding the dividend is the Profit rate of the firm. The internal Profitability rate of the firm provides a basis for company.

(x) Legal requirements :- while declaring dividend, the board of director will have to consider the legal restriction. The indian companies Act 1956 prescribes to certain guidelines in respect of declaration and payment of dividends and they are to be strictly observed by the company for declaring dividends.

(xi) Policy of control :- Policy of control is another important factor which influences dividend policy. if the company feels that no new shareholders should be added, then it'll have to pay less dividends.

(xii) Corporate taxation Policy :- corporate taxes affect the rate of dividends of the work. High rates of taxation reduce the profits available for distribution to shareholder.

(xiii) Tax Position of shareholders :- The tax position of shareholders is another financing factor on dividend decisions.

(xiv) Effect of trade cycle :- trade cycle also influences the dividend policy of the concern. For example, during the period of inflation, funds generated from depreciation not be adequate to replace the assets.

(xv) Attitude of the interested group :- A concern may have certain group of interested and powerful shareholders. Those people have certain attitude towards payment of dividend and have a definite say in policy formulation regarding dividend.

Answer to the question no-6

Risk is defined in financial terms as the chance that an outcome or investment's actual gains will differ from an expected outcome or return. Risk includes the possibility of losing some or all of an original investment

A return also known as a financial return in its simplest terms, is the money made or lost on an investment over some period of time. A return can be expressed nominally as the change in dollar value of an investment over time.

Different types of risks there are given below:-

(i) economic risk :- economic risk refers to the amount of risk your organization is at due to shifts in macroeconomic forces. This includes everything from inflation or policy change to interest rates or even employment levels.

(ii) Legal or compliance risk :- Legal or the compliance risk ~~fe~~ refers to any situation where an organizations actions might violate state, local, or federal laws or regulations such violations might be due to data security breaches, product liability, or illegal action taken by employees.

(iii) Security and fraud risk :- Fraud or security risk relates to any event where persons internal or external to the organization cause harm through deliberate deception. This might include embezzlement, theft, or other loss of material or reputation.

(iv) financial risk :- Also sometimes known as downside risk, financial risk is any potential loss of money or other assets. A common type of financial risk is market risk, which occurs when the value of an asset drops because investors expectations about future returns differ. Another type that might occur involves currency fluctuation.

(v) Reputation risk :- Reputation risk is the risk that people will lose confidence in your brand or product. If customers believe that your company has acted dishonest or irresponsibly, it can cause irreparable harm to your organizations brand in the market. Reputation risk could be the result of deliberate action by an organization but one of the more common causes, especially lately, is from data breaches.

(vi) Operational risk :- Operational risk involves anything that could put a halt to business as-usual. This can include everything from a natural disaster, like a hurricane taking a huge swath of your operations offline to many key employees being out sick and unable to contribute their expertise. The best way to manage operational risk is to have a business continuity plan in place for all of the most likely events that could strike your organization maybe even a few that are less likely but still possible. This way, you'll already have a plan in place should something devastating occur.

(vii) Competitive risk :- Competitive risk refers to the potential loss of customers due to competition. it's also known as market share risk because it's related to how much of the market you control. No matter how popular your product or service, technology and consumer expectations change over time and in order to reduce competitive risk you must be always looking to maintain your competitive edge.