



UNIVERSITY OF COLOMBO, SRI LANKA

FACULTY OF MANAGEMENT AND FINANCE **Postgraduate & Mid-career Development Unit**

Master of Business Administration/Master of Business Administration in Finance/Master of Business Administration in Marketing/Master of Business Administration in HRM (Semester III, First -half) Examination – April 2016

MBAFI 600 – Strategic Finance

Three (03) Hours (Additional 15 minutes for reading)

Answer All Questions
Open-Book

Use of Calculators is allowed

Part I

1. WAC Trading PLC

Mr. Florence Fernando who was educated in England and returned to Sri Lanka just after the general election in 1977 as a qualified Electrical and Electronic engineer wanted to start his own business in Sri Lanka. He invested Rs.100, 000/- initially for the stated capital of the company and WAC Trading(Pvt) Limited was registered as a private limited liability company in the year 1979 as an importer of electrical and electronic goods. At the start the company acted as a distributor of those goods by opening three showrooms two in Colombo and one in Kandy

city. His good friend, Mr. Palitha Silva and two other friends joined him as directors of the company in order to provide their expert knowledge in retail business. Mr. Fernando used his overseas contact and successfully obtained the local agency for several world class brands for electrical and electronic equipment and components. In 1996 Mr. Fernando decided to expand his business opening 10 more Showrooms island wide and expand the repairs and service units attached to each showroom in order to provide after sale services for their customers. In the year 1996, the company offered to the public via initial public offer to raise required funds as equity capital of Rs.122,750,000/-. Mr. Fernando and his team (three friends) held the majority of the stated capital (58% of stated capital) while offering 42% to the public. Subsequently in the year 2015, WAC Trading PLC borrowed Rs.63,958,000/- as a term loan from Bank of Ceylon at 8% interest rate p.a while having short term borrowings of Rs.995,578,000/- as at 31.03.2015 in order to fund the expansion of the company and to meet the demand of WAC branded electronic and electrical goods. The company has funded the capital expenditure of the other companies in the group via the current accounts which are shown as dues from the related parties amounting Rs.774.3 Million as at 31st March 2016 (no interest has been charged from the related parties). The β (beta) of WAC PLC is 0.9 and risk premium is 4% while the current Treasury bill rate is 7%. The company has utilized short terms borrowing facility which was offered only to WAC Trading PLC by Bank of Ceylon at average interest rate of 12% per annum in order to fund the requirement of related parties. The principal activities of the Company are manufacturing and assembling of household electric and electronic appliances and providing repair and maintenance services for the same under two departments.

(a) Manufacturing Department: This Department was set up primarily for the manufacturing and assembling of household electric and electronic appliances in collaboration with internationally recognized brand names. It engages in the assembling and manufacturing of LG Washing Machines, LG Refrigerators, Water Geezers, Air Conditioners, Cookers & Solar PV systems Installation. There is a 10% sales growth per annum in this section

(b) Service Department: This Department handles the installation, repair, maintenance and all after sale services of electrical and household appliances sold by the company. The cost structure of the service centers is increasing and currently earned only 9.8% on invested capital.

The company is liable to pay 28% corporate tax on its taxable profit.

The group finance controller, Mr Manoharan had a long discussion with the managing director Mr. Palitha Silva about the related party balances appeared in the balance sheet and advised him that this is building up balances unnecessarily and that the company needs to find a solution. He also informed that the recent enactment in tax about transfer pricing too would query on the transactions and that it needs management urgent attention (The related party information are submitted in the note 03).

Mr Manoharan pointed out that the land (60 perches) belonging to WAC Trading PLC situated in Kurunagala bought 5 years ago at Rs.500,000 per perch is now value at 1.2 million per perch and that the land was not utilized for any income generating project but still showing in the balance sheet under property and plant and equipment at the historical cost. He said this should be revalued and the current market value should be brought to the balance sheet. Also that there is another land situated in Kandy which is shown in the books at the historical cost of Rs.15 Million but the current market value is Rs13.5million and this can be immediately disposed at that price. However Mr Manoharan suggested to revalue this immediately and bring the current market price to the books thinking that in the long term the value of the land would appreciate .

During the financial year 2015/16, the company has performed a capitalization of reserves for a proportion of 1 each for every 5 share hold at that time. The board of directors decided at the recent board meeting, the company should declared 26 %(dividend per share is Rs.3.44/) of the current year profit as dividend to the shareholders for 2015/16, even though the company had the consistent corporate dividend policy in previous years.

At the recent board meeting the managing director brought these issues to the notice of other directors and also mentioned that as per the draft accounts submitted by the finance controller for the year ended 31st March 2016 the company has earned a net profit after tax of Rs.67.585 million. Also he said That they should celebrate this achievement which was achieved under tough market conditions. However the board was not happy about the performance and approached you as a consultant to advise the board about the above issues and requested to answer the following specifically your opinion and appropriate strategies to be present at the next board meeting. You are required to

- a. Critically examine the existing financial strategies of the company and if any strategy is not acceptable, suggest your remedial strategy to rectify the situation and create value to the shareholder. (Marks 12)
- b. Advise the board about the importance of the risk management and identify the existing risk and possible source of risk to the company while suggesting the appropriate risk management policy statement (Marks 12)
- c. Critically examine the performance of the company during the financial year ending 31st March 2016 while considering all existing issues and facts and suggest your strategies to improve the shareholder value calculating the following performance measurements currently and after implementation of your proposed strategies.
 - i. Profitability ratio and ROCE ratio (Marks 04)
 - ii. Economic Value Addition of the company (Marks 05)
 - iii. Sustainable growth rate (marks 04)
 - iv. Whether company create value to shareholders or destroy the shareholder value (Marks 06)

- v. Suggest your financial strategy to improve the above situation which is discussed under part (iv) (Marks 08)
 - vi. Consider the financial strategic matrix and advise about the related party companies position in the financial strategic matrix and give your suggestions to use it to create value of the shareholders (WAC Trading PLC) (Marks 10)
- d. Advise about the existing supply chain of the company and discuss the importance of managing supply chain while calculating the existing C2C of the company and suggest realistic sustainable financial strategy to improve C2C if needed. (Marks 06)
- e. Provide the value of the company as at 31.03.2016 using an appropriate valuation model which would consider the sustainable growth(you should consider your suggestions) (Marks 08)

(Total Marks 75)

WAC Trading PLC
Statement of Income for the Year Ended 31st March

	2016	2015
	Rs	Rs
	000	000
Revenue		
Manufacturing	2,492,777	2,210,295
Services	713,035	682,043
Total Income	3,205,812	2,892,338
Cost of Sales	(2,756,672)	(2,451,384)
Gross Profit	449,140	440,954
Other Income		
Scrap & sundry parts sales	6,622	7,150
Interest income	10,353	2,814
Transport and warehouse	17,402	12,000
Insurance claim	1,836	1,206
Exchange gain	12,946	9,869
Profit on disposal of motor vehicle	1,585	4,510
Total Other Income	50,744	37,549
Less Expenses		
Distribution cost	89,803	64,690
Administration expenses	215,377	168,947
Finance and other expenses	116,473	117,469
Total Expenses	421,653	351,106
Net operating Profit before taxation	78,231	127,397
Income tax expenses	(4,593)	(34,731)
Profit For the Year	73,638	92,666
Other Comprehensive Income /(expenses)		

Actuarial gain or loss on defined benefit plan	(6,053)	1,304
Total comprehensive income. expenses net of tax	67,585	93,970
Dividend per share Rs .	3.44	2.00

WAC Trading PLC

Statement of Financial Position

as at 31st March

Non Current Assets

2016
Rs '000

2015
Rs '000

Property , plant and equipment

412,388

378,586

Investment in Subsidiaries

11,454

11,454

Investment in Fixed Deposits

131,530

51,383

Total Non Current Assets

555,372

441,423

Current Assets

Inventories

360,769

573,135

Trade and Other Debtors

162,351

59,588

Amount due from related parties

774,292

868,335

Deposits ,advances and pre payments

22,492

15,512

Cash and cash equivalent

119,895

30,465

Total Current Assets

1,439,799

1,547,035

Total Assets

1,995,171

1,988,458

Capital and Reserve

Stated Capital

186,732

122,850

Capital Reserve

2,100

2,100

Retained Earning

429,808

426,105

Total Equity

618,640

551,055

Non Current Borrowings

Borrowing

64,968

1,010

Retirement benefit obligation

66,897

50,023

Deferred Tax Liability	19,662	30,625
Non Current Liabilities	151,527	81,658
Current Liabilities		
Trade and Other Receivable	250,202	324,494
Income tax Payable	887	26,663
Deferred Service Income	7,863	
Amount Due to Related parties	11,487	9,010
Borrowings	954,565	995,578
Current Liabilities	1,225,004	1,355,745
Total Liabilities	1,376,531	1,437,403
Total Equity and Liabilities	1,995,171	1,988,458

Note 01

Finance and other expenses

	2016	2015
Interest on long term loan	344	407
Bank charges, stamp duty	1,543	1,033
Terms Loan Interest(Short term & OD)	114,537	115,980
Lease Interest	49	49
Total Finance and Other Expenses	116,473	117,469

Note 02

Segment Information

Rs 000'	Manufacturing 2016	Services 2016	Total 2016
Revenue	2,492,777	713,035	3,205,812
Gross Profit	270,882	178,258	449,140
Net Profit after tax and interest	24,548	53,683	73,638
Invested Capital	572,253	548,626	1,120,879

Note 03

Amount due from & Amount due to) Related parties	2016				
	Rs '000	ROE	WACC	Dividend payout %	Sales Growth %
		%			
WAC PLC	542,567	13	11.5	50	5
WAC Environmental (Pvt) Limited	112,521	16	12	40	7
WAC Restaurants (Pvt) Limited	119,204	11	12	50	10
	774,292				
WAC City Developer (pvt) limited	(3,250)				
WAC retailer pvt limited	(8,237)				
	(11,487)				

Note 04**Weighted average number pf shares as at 31.03.2016**

Number of shares prior to capitalization of reserve	4,258,800
Shares from the capitalization of reserve	851,760
Weighted average number of shares	5,110,560

