

MAC3702 APPLICATION OF FINANCIAL MANAGEMENT TECHNIQUES

FREQUENTLY ASKED QUESTIONS

1. *Can I expect to see **identical examination questions** as included in MAC3702 previous exam papers or other questions included in the assignment questions or study guide?*

No. You will not get questions that you have seen before, although the exam paper will test the **same principles** as the questions included in papers, MAC3702 mock exam paper, assignment questions and the study guide. The principles will be tested on a level that is acceptable for third year students. Please work through all the examples and questions in your text book, the study guide (tutorial letter 501 available in hard copy and on myUnisa), your assignment questions and the solutions (available on myUnisa) and the mock exam paper (tutorial letter 103 available on myUnisa).

Once working through all these different examples you will get an understanding of the different methods as to how the principles can be tested.

2. *Do I only need to focus on the information included in the MAC3702 guide or do I also need to have **knowledge of MAC2602**?*

In your study guide of MAC3702 we refer to **assumed prior knowledge** and we refer you to the study guide of MAC2602. If you have not done that specific course but the ACN203 course, please make sure that you make use of the study material available on the website relating to MAC2602.

3. *Will I receive a **formula sheet** or do I need to know my formulas?*

After numerous enquiries, a decision was taken that only **certain formulas** will be provided to you should it be tested in the exam. These formulas include the following:

1. Formulas to calculate the beta coefficient
2. Covariance and standard deviation

3. Portfolio variance based on the correlation coefficient

4. Correlation coefficient

5. Failure prediction: K-score model, Z-score model and A-score model (please refer to your study guide (study unit 1 for some examples) (Also note that you will get the definition of the formulas for the symbols (a-f) that needs to be substituted in your main formula)

Please note that you should still know and **understand these formulas and how to interpret** their meanings.

NB. You still need to know all other formulas by heart.

4. *Do we need to make adjustments to the figures in accordance with **IFRS** (as in financial accounting) that we are using in the ratio formulas or do we only use the figures included in the Annual Financial Statements?*

In terms of the SAICA's decision to base all information on the integrated reporting principles, accounting adjustments need to be incorporated in the figures that we use for the ratio analysis (refer to Activity 1.2 in your study guide).

HOWEVER

During the transition period (semester 1 and 2 of 2014) **both methods** (adjusted and non-adjusted figures) will be accepted as correct in the exams.

Should this principle be examined, bonus marks will be allocated to students that make the correct adjustments.

5. *Do I need to write out the **formula** or can I substitute my amounts directly into the formula to save time?*

Writing down the formula and substituting the components / elements will enable the marker to follow your process and may lead to conceptual / principle marks when applicable.

6. *When calculating the **debtors' collection period & creditors' payment period** should we use the average debtors & creditors or should we use the closing balance for debtors and*

creditors?

ONLY when the question specifically states calculate the **average** debtors collection period OR creditors' payment period should you use the **average** debtors and creditors.
In all other instances use the **CLOSING BALANCES**.

7. *What should be included in the debt balance of the **debt : equity ratio**?*

The debt balance should **include all the interest bearing debt balances** (this includes both the long- and short term portions of long term loans). Bank overdraft is usually not included in the debt balance as the bank overdraft is normally used to finance working capital shortfalls and not other long term investments, unless the scenario / information depicts the overdraft to be of a permanent nature

8. *There are two methods that can be used to determine the **cash flow**, can we only study one method or should we know both?*

You need to be able to know and apply both the methods to determine cash flow (one is used in your text book and the other is included in your study guide). If we do not specify which method to use and the information is sufficient enough to apply both methods you will not be penalised for any method used and correctly applied.

9. *Can I make use of my calculator when calculating the **standard deviation** and the **coefficient correlation**?*

If the question does not specify that you need to use the formula you may use your calculator.

HOWEVER:

You need to write down the amounts and steps entered into your calculator and the type of calculator (SHARP or HP) used. Marks will be allocated to these amounts and steps.

10. When calculating the **present value** should I use the factors included in the table or can I use my calculator?

No tables will be provided in the exams. However, you will be allowed to use a calculator. You need to write down the amounts and steps entered into your calculator and the type of calculator (SHARP or HP) used. Marks will be allocated to these amounts and steps.

11. Will the **valuation** methods only be tested as part of Mergers and Acquisitions or will it be tested separately?

You may be tested on both of the above. If an exam includes a valuation question, only one of the two options will be tested (that is to say either as part of a Mergers and Acquisition question **or** as a standalone valuation question).

12. When using the **free cash flow method** for valuation purposes, the non-operating assets of the entity will not form part of the free cash flow valuation and should be valued separately. What is the implication thereof?

It means that you will only include cash flow that represents the operational cash flow that is “free” for distribution to all providers of capital that is independent of the way the business is financed.

Therefore you need to **EXCLUDE:**

- Non-operational cash flow as non-operating assets should be valued separately
- Non-cash charges (depreciation and amortization)
- Finance related cash flows

Therefore you need to **INCLUDE:**

- The effect of capital expenditure and working capital investment that are necessary to sustain the projected future free cash flow
- The taxation effect of the cash flows included

Once you have determined the value by making use of the free cash flow method you will

also value the non-operating assets and the combined value is the value of the entity.

You may be tested on the free cash flow method where you need to exclude and include the relevant cash flows but we will not examine you on the principle of the combined value. This is only tested in later MAC modules.

Also refer to section 11.6.5(a) to (d) in your text book.

13. *When calculating cost of capital and **WACC**, should one use market values or book values?*

Always make use of your market values unless the question specifically states that you need to use the book values or if the only information available is the book values and there is no information with relation to the market values.

14. *How do I take tradability discounts and **minority interest** discounts into consideration when I value my company?*

Please refer to Question 2 of study unit 4 (make sure that you work on the correct version – errata as per tutorial letter 102 on the myUnisa website).

In this question it is evident that due to the lack of tradability of Jacks & Jacks (Pty) Ltd, for whatever reason, that we need to adjust the discounting rate with 2%.

You will therefore first determine your fair rate of return (discounting factor) by making use of the market information for a similar company,

After this is calculated you will adjust the calculated fair rate of return with the mentioned rate of 2%.

If the question makes reference to the fact that there are tradability issues with the shares but the additional information does not make specific reference to a rate, please adjust your answer with a % (say 3%) and state in the question that the fair rate of return has been adjusted with a rate of 3% that is considered a fair rate for shares with the marketing and tradability issue.

In the instance of the minority shareholding discount, the question did not specify or mention a discount rate relating to minority shareholding. You do however still need to display the fact to the marker that you understand that the fair rate of return and therefore the company value represents a 100% and that you cannot use that to determine the minority shareholding. Remember minority shares normally trades at a lower price than majority shares therefore you need adjust the 5% of the 100% value with a discount factor. In this instance we assumed a 10% discount to be fair. You should just state in your answer that 10% is considered a fair adjustment for minority shareholders.

If the additional information includes a discount factor for minority shareholders then use the discount factor as per the additional information.

You may also be provided with the fair rate of return that is applicable to majority shareholders or minority shareholders. Make sure that if you value majority shareholders that you use the rate applicable to them and if you have to value the minority shareholders that you use the applicable rate for them.

Remember even if the discounting rates are not provided we will still test the fact that you understand the principle.

15. Other matters to consider:

- Make sure that you understand the difference between total assets and operating assets.
- Make sure that you understand the difference between qualitative factors and quantitative factors that can impact a decision. Qualitative factors are also known as environmental factors.