IMANET-CMA$^{Q\&As}$

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QUESTION 1

Companies that adopt just-in-time purchasing systems often experience

A. A reduction in the number of suppliers.

B. Fewer deliveries from suppliers.

C. A greater need for inspection of good as the good arrive.

D. Less need for linkage with a vendo\\'s computerized order entry system.

Correct Answer: A

The objective of jit is to reduce carrying costs by eliminating inventories and increasing the deliveries made by suppliers.Ideally,shipments of raw materials are received just in time to be incorpotated into the manufacturing process.the focus of quality control under jit is the prevention of quality problems.quality

control is shifted to the supplier.Jit companies typically do not inspect incoming goods;the assumption is that receipts are of perfect quality.suppliers are limited to those who guarantee perfect quality and prompt delivery.

QUESTION 2

For capital budgeting purposes, management would select a high hurdle rate of return for certain projects because management

A. Wants to use equity funding exclusively.

B. Believes too many proposals are being rejected.

C. Believes bank loans are riskier than capital investments.

D. Wants to factor risk into its consideration of projects.

Correct Answer: D

Risk analysis attempts to measure the likelihood of the variability of future returns from the proposed investment. Risk can be incorporated into capital budgeting decisions in a number of ways, one of which is to use a hurdle rate (desired rate of return) higher than the firm\\'s cost of capital, that is, a risk-adjusted discount rate. This technique adjusts the interest rate used for discounting upward as an investment becomes riskier. The expected flow from the investment must be relatively larger or the increased discount rate will generate a negative net present value, and the proposed acquisition will be rejected.

QUESTION 3

The payback reciprocal can be used to approximate a project\\'s

A. Profitability\\' index.

B. Net present value.

C. Accounting rate of return if the cash flow pattern is relatively stable.

D. Internal rate of return if the cash flow pattern is relatively stable.

Correct Answer: D

QUESTION 4

Kim is thinking of organizing a funraiser to support a local charity. She has planned to rent a banquet hall and provide the guests with food, entertainment , and various party favors. She has decided to charge $500 a person. After researching around town, Kim has discovered the following costs: What is Kim\\'s contribution margin?

Fixed Costs	
Rental fee of banquet hall	$150,000
Advertising	50,000
Entertainment	4,000
Variable Costs	**Per Guest**
Food	$12
Other miscellaneous costs	8

A. $400

B. $450

C. $480

D. $500

Correct Answer: C

The contribution margin in a breakeven analysis can be found by taking the revenues per person and subtracting the variable cost per person. In this case, it would be $500-- $20 = $480.

QUESTION 5

An analysis of a company\\'s planned equity financing using the capital asset pricing model (or security market line) would incorporate only the

A. Expected market earnings, the current U.S. Treasury bond yield, and the beta coefficient.

B. Expected market earnings and the price-earnings ratio,

C. Current U.S. Treasury bond yield, the price-earnings ratio, and the beta coefficient.

D. Current U.S. Treasury bond yield and the dividend payout ratio.

Correct Answer: A

The capital asset pricing model adds the risk-tree rate to the product of the market risk premium and the beta coefficient. The market risk premium is the amount above the risk- free rate (approximated by the

U.S. Treasury bond yield) that must be paid to induce investment in the market The beta coefficient of an individual stock is the correlation between the price volatility of the stock market as a whole and the price volatility of the individual stock.

QUESTION 6

The following data pertain to a 4-year project being considered by Metro Industries:

A depreciable asset that costs $1 .200.000 will be acquired on January 1. The asset, which is expected to

have a $200,000 salvage value at the end of 4 years, qualifies as 3- year property under the Modified

Accelerated Cost Recovery System (MACPS).

The new asset will replace an existing asset that has a tax basis of $150,000 and can be sold on the same

January 1 for $180,000.

The project is expected to provide added annual sales of 30,000 units at $20. Additional cash operating

costs are: variable, $12 per unit fixed, $90,000 per year.

A $50,000 working capital investment that is fully recoverable at the end of the fourth year is required.

Metro is subject to a 40% income tax rate and rounds all computations to the nearest dollar. Assume that

any gain or loss affects the taxes paid at the end of the year in which it occurred. The company uses the

net present value method to analwe investments and will employ the following factors and rates.

Period	Present Value of $1 at 12%	Present Value of $1 Annuity at 12%	MACRS
1	0.89	0.89	33%
2	0.80	1.69	45
3	0.71	2.40	15
4	0.64	3.04	7

The discounted, net-of-tax amount that relates to disposal of the existing asset is

A. $168,000

B. $169,320

C. $180,000

D. $190,680

Correct Answer: B

The cash in flow from the existing asset is $180,000, but that amount is subject to tax on the $30,000 gain ($180,000--$150,000 tax basis). The tax on the gain is $12,000 ($30,000 x 40%). Because the tax will not be paid until year-end1 the discounted value is $10,680 ($12,000 x .89 PV of $1 at 12% for one period). Thus, the net-of-tax inflow is $169,320 ($180,000--$10,680). NOTE: This as set was probably a Section 1231 asset, and any gain on sale qualifies for the special capital gain tax rates. Had the problem not stipulated a 40% tax rate, the capital gains rate would be used. An answer based on that rate is not among the options.

QUESTION 7

Sensitivity analysis, if used with capital projects,

A. Is used extensively when cash flows are known with certainty.

B. Measures the change in the discounted cash flows when using the discounted payback method rather than the net present value method.

C. Is a "what-if" technique that asks how a given outcome will change if the original estimates of the capital budgeting model are changed.

D. Is a technique used to rank capital expenditure requests.

Correct Answer: C

After a problem has been formulated into any mathematical model, it may be subjected to sensitivity analysis, which is a trial-and-error method used to determine the sensitivity of the estimates used. For example, forecasts of many calculated NPVs under various assumptions maybe compared to determine how sensitive the NPV is to changing conditions. Changing the assumptions about a certain variable or group of variables may drastically alter the NPV, suggesting that the risk of the investment may be excessive.

QUESTION 8

The accounting rate of return

A. Is synonymous with the internal rate of return.

B. Focuses on income as opposed to cash flows.

C. Is inconsistent with the divisional performance measure known as return on investment.

D. Recognizes the time value of money.

Correct Answer: B

The accounting rate of return (also called the unadjusted rate of return or book value rate of return) is calculated by dividing the increase in accounting net income by the required investment. Sometimes the denominator is the average investment rather than the initial investment. This method ignores the time value of money and focuses on income as opposed to cash flows.

QUESTION 9

A manufacturing concern sells its sole product for $10 per unit, with a unit contribution margin of $6. The fixed manufacturing cost rate per unit is $2 based on a denominator capacity of 1 million units, and fixed marketing costs are $1.5 million. If 900,000 units are produced, the absorption-costing breakeven point in units sold is

A. 425,000 units

B. 583.333 units

C. 900,000 units

D. 1,000,000 units

Correct Answer: A

QUESTION 10

Exhibit

Xerbert Co.
Budget and Actual Income Statements
For the Year Ending December 31
(000s omitted)

	Budget			Actual		
	Xenox	Xeon	Total	Xenox	Xeon	Total
Unit sales	150	100	250	130	130	260
Net dollar sales	$900	$1,000	$1,900	$780	$1,235	$2,015
Variable expenses	450	750	1,200	390	975	1,365
	$450	$ 250	$ 700	$390	$ 260	$ 650
Fixed expenses						
Manufacturing			$ 153			$ 140
Marketing			95			90
Other Fixed Expenses			200			190
Total fixed expenses			$ 448			$ 420
Income before taxes			$ 252			$ 230

The percentage difference between the actual and the budgeted breakeven point in units was that actual was

A. 500% above budget

B. 6.67% below budget.

C. 6.67% above budget

D. 5.00% below budget.

Correct Answer: A

QUESTION 11

The following data pertain to a 4-year project being considered by Metro Industries: ?A depreciable as set that costs $1, 200,000 will be acquired on January 1 . The asset, which is expected to have a $200,000 salvage value at the end of 4 years, qualifies as 3- year property\\' under the Modified Accelerated Cost Recovery System (MACPS). The new asset will replace an existing asset that has a tax basis of $150,000 and can be sold on the same January 1 for $180,000. The project is expected to provide added annual sales of 30,000 units at $20. Additional cash operating costs are: variable, $12 per unit fixed, $90,000 per year. A $50,000 working capital investment that is fully recoverable at the end of the fourth year is required. Metro is subject to a 40% income tax rate and rounds all computations to the nearest dollar. Assume that any gain or loss affects the taxes paid at the end of the year in which it occurred. The company uses the net present value method to analyze investments and will employ the following factors and rates.

Period	Present Value of $1 at 12%	Present Value of $1 Annuity at 12%	MACRS
1	0.89	0.89	33%
2	0.80	1.69	45
3	0.71	2.40	15
4	0.64	3.04	7

The discounted cash flow for the fourth year MACPS depreciation on the new asset is

A. $0

B. $17,920

C. $21,504

D. $26,880

Correct Answer: C

Tax law allows taxpayers to ignore salvage value when calculating depreciation under MACPS. Thus1 the depreciation deduction is 7% of the initial $1 .200000 cost, or $84,000. Ata4O% tax rate, the deduction will save the company $33,600 in taxes in the fourth year. The present value of this savings is $21,504 ($33,600 x 0.64 present value of $1 at 12% for four periods).

QUESTION 12

On August 15, 19XX, National Corporation announced a 1-for-10 reverse split, the event to occur on September 6, subject to shareholder approval. The stock\\'s closing price on August 14 was $1.375. If nothing changes, at what price would you expect the stock to sell after the stock split is made effective on September 6?

A. $13.75

B. $10.00

C. $2.75

D. $1.38

Correct Answer: A

A reverse stock split, like a regular stock split, should not change market capitalization. Thus, if there are 1/10 as many shares outstanding as previously, they should be worth 10 times as much. Thus, the price after the reverse split would be $13.75 (10 x $1375).

QUESTION 13

While auditing a marketing department, the internal auditor discovered that the product life cycle model was used to structure the marketing mix. The manager has asked the auditor for advice about increasing advertising of various products. During which stage of the life cycle would it be appropriate to advertise that the company\\'s products is the lowest price and best quality of all competitors?

A. Introduction stage.

B. Growth stage.

C. Maturity stage.

D. Decline stage.

Correct Answer: C

The maturity stage is the ideal time for advertising lower price and superior quality because this is the period during a product\\'s life when competition is greatest. Due to the availability of many alternatives or substitutes, a firm has reasons to set itself apart. Because price and quality are both concerns of customers during the maturity stage, it is ideal for the firm to differentiate its product by advertising low prices and higher quality.

QUESTION 14

The treasury analyst for Garth Manufacturing has estimated the cash flows for the first half of next year (ignoring any short-term borrowings) as follows: Garth has a line of creditor unto $4 million on which it pays interest monthly ate rate of 1% of the amount utilized. Garth is expected to have a cash balance of $2 million on January 1 and no amount utilized on its line of credit. Assuming all cash flows occur at the end of the month, approximately how much will Garth pay in interest during the first half of the year?

	Cash (millions)	
	Inflows	Outflows
January	$2	$1
February	2	4
March	2	5
April	2	3
May	4	2
June	5	3

A. $O

B. $61,000

C. $80,000

D. $132,000

Correct Answer: B

The sum of the beginning balance and inflows exceeds the outflows for the first 2 months. At the end of March, however1 Garth must use $2,000,000 of its line of credit ($2,000,000 beginning balance + $6,000,000 inflows--$10,000,000 outflows). Thus, interest for April is $20,000 ($2,000,000 x 1%). The net cash outflow for April (ignoring short-term borrowings) is $1,000,000 of an additional $1,000,000 of the line of credit. However, the $20,000 of interest for April must also be paid, so the amount of the line of credit used in May is $3,020,000 ($2,000,000 + $1,000,000 + $20,000). Interest for May is therefore $30,200 ($3,020,000 x 1%). Given the net cash inflow for May of $2,000,000 (again ignoring short-term borrowings) and the borrowing of $30,200 to pay the interest for May, the amount of the line of credit used in June is $1,050,200. Interest in June is $10,502 ($1,050,200 x 1%), and total interest is $60,702 ($20,000 + $30,200 + $10,502). Consequently, the closest answer is $61, 000.

QUESTION 15

A firm is planning to issue a callable bond with an 8% coupon rate and 10 years to maturity. A straight bond with a similar rate is priced at $1,000. If the value of the issuer\\'s call option is estimated to be $50, what is the value of the callable bond?

A. $1,000

B. $950

C. $1,050

D. $900

Correct Answer: B

A callable bond is not as valuable to an investor as a straight bond. Thus, the $50 call option is subtracted from the $1,000 value of a straight bond to arrive at a $950 value for the callable bond.