

1. Swim Suits Unlimited is in a highly seasonal business, and the following summary balance sheet data show its assets and liabilities at peak and off-peak seasons (in thousands of dollars):

Peak Off-Peak

Cash \$ 50 \$ 30

Marketable securities 0 20

Accounts receivable 40 20

Inventories 100 50

Net fixed assets 500 500

Total assets \$690 \$620

Payables and accruals \$ 30 \$ 10

Short-term bank debt 50 0

Long-term debt 300 300

Common equity 310 310

Total claims \$690 \$620

From this data we may conclude that

- a. Swim Suits' current asset financing policy calls for exactly matching asset and liability maturities.
- b. Swim Suits' current asset financing policy is relatively aggressive; that is, the company finances some of its permanent assets with short-term discretionary debt.
- c. Swim Suits follows a relatively conservative approach to current asset financing; that is, some of its short-term needs are met by permanent capital.**
- d. Without income statement data, we cannot determine the aggressiveness or conservatism of the company's current asset financing policy.
- e. Without cash flow data, we cannot determine the aggressiveness or conservatism of the company's current asset financing policy.

2. Which of the following statements is CORRECT?

- a. A firm that makes 90% of its sales on credit and 10% for cash is growing at a constant rate of 10% annually. Such a firm will be able to keep its accounts receivable at the current level, since the 10% cash sales can be used to finance the 10% growth rate.
- b. In managing a firm's accounts receivable, it is possible to increase credit sales per day yet still keep accounts receivable fairly steady, provided the firm can shorten the length of its collection period (its DSO) sufficiently.**
- c. Because of the costs of granting credit, it is not possible for credit sales to be more profitable than cash sales.
- d. Since receivables and payables both result from sales transactions, a firm with a high receivables-to-sales ratio must also have a high payables-to-sales ratio.
- e. Other things held constant, if a firm can shorten its DSO, this will lead to a higher current ratio.

3. Halka Company is a no-growth firm. Its sales fluctuate seasonally, causing total assets to vary from \$320,000 to \$410,000, but fixed assets remain constant at \$260,000. If the firm follows a maturity matching (or moderate) working capital financing policy, what is the most likely total of long-term debt plus equity capital?

- a. \$260,642
- b. \$274,360
- c. \$288,800
- d. \$304,000
- e.) \$320,000

Lower total asset range \$320,000

Upper total asset range \$410,000

Minimum total assets = FA + Min. CA = \$320,000 = LT Debt + Equity

A maturity matching policy implies that fixed assets and permanent current assets are financed with long-term sources. This is its most likely level of long-term financing.

4. Your consulting firm was recently hired to improve the performance of Shin-Soenen Inc, which is highly profitable but has been experiencing cash shortages due to its high growth rate. As one part of your analysis, you want to determine the firm's cash conversion cycle. Using the following information and a 365-day year, what is the firm's present cash conversion cycle?

Average inventory = \$75,000

Annual sales = \$600,000

Annual cost of goods sold = \$360,000

Average accounts receivable = \$160,000

Average accounts payable = \$25,000

- a. 120.6 days
- b. 126.9 days
- c. 133.6 days
- d. 140.6 days
- e. 148.0 days

Avg. inventory =	\$75,000	Annual sales =
\$600,000		
Avg. receivables =	\$160,000	Annual COGS =
\$360,000		
Avg. payables =	\$25,000	Days in year
=	365	

Inv. conv. period = Inv./(COGS/365)	76.0
+ DSO = Receivables/(Sales/365)	97.3
- Payables deferral = Payables/(COGS/365)	-25.3
Cash conversion cycle (CCC)	148.0

5. Affleck Inc.'s business is booming, and it needs to raise more capital. The company purchases supplies on terms of 1/10 net 20, and it currently takes the discount. One way of getting the needed funds would be to forgo the discount, and the firm's owner believes she could delay payment to 40 days without adverse effects. What would be the effective annual percentage cost of funds raised by this action? (Assume a 365-day year.)

- a. 10.59%
- b. 11.15%
- c. 11.74%
- d. 12.36%
- e. 13.01%**

Discount %	1%	Net days	20
Discount days	10	Actual days to payment	40

$$\text{EAR} = [1 + \text{Disc. \%}/(100 - \text{Disc. \%})][365/(\text{Actual days} - \text{Disc. Period})] - 1 = 13.01\%$$