Certificate in Investment Banking

Mock Test Questions

Q1. Please help Henry, a Nomura analyst with the right order of steps for doing "ComparableCompanies Valuation Analysis"

(a) A. Set Industry Valuation Benchmarks
B. Spread Key Statistics, Ratios, and Trading Multiples
C. Screen the Universe of Comparable Companies
D. Determine Valuation of Target
(b) A. Spread Key Statistics, Ratios, and Trading Multiples
B. Screen the Universe of Comparable Companies
C. Determine Valuation of Target
D. Set Industry Valuation Benchmarks

Q2. What would be the Enterprise Value (EV) of Blue Nile given the following details? (in million)
Common Shares outstanding: 2 million
Current Share Price: USD 10.00
Total Debt: USD 5 million
Cash and equivalents: USD 7 million
Total Revenues: USD 3 million

(a) 22.00
(b) 32.00
(c) 18.00

Q3. Best's Foods is seeking to acquire the Heinz Baking Company, whose book value is USD 34 million. A comparable bakery was recently acquired for USD 300 million, 20% more than the book value of the firm.
How much should Best's Foods expect to have to pay for the Heinz Baking Company, considering the same premium levels? (in million)

(a) 34.00
(b) 27.20
(c) 40.80

Q4. Please help Henry, a Nomura analyst with the right order of steps for doing "Precedent Transactions Valuation Analysis":

(a) A. Set Comparable Acquisition Benchmarks
B. Spread Key Statistics, Ratios, and Deal Multiples
C. Screen the Universe of Comparable Acquisitions
D. Determine Valuation of Target
(b) A. Screen the Universe of Comparable Acquisitions
B. Spread Key Statistics, Ratios, and Deal Multiples
C. Set Comparable Acquisition Benchmarks
D. Determine Valuation of Target
(c) A. Spread Key Statistics, Ratios, and Deal Multiples
B. Screen the Universe of Comparable Acquisitions
C. Determine Valuation of Target
D. Set Comparable Acquisition Benchmarks

Q5. In a friendly bid Nature Corp has shown interest to
acquire Blue Nile in a stock deal. BlueNile board has demanded an Exchange Ratio of 0.60 for each shares of Blue Nile.
The pre announcement market price of Nature Corp was USD 100.00 per share.
Considering these what is the implied Offer Price?

(a) 166.67
(b) 100.00
(c) 60.00

Q6. In a friendly bid Nature Corp has shown interest to acquire Blue Nile in a Cash and Stock deal.
Blue Nile board has demanded 0.60 shares of Nature Corp and USD 10 in cash, for each shares of Blue Nile.
Pre announcement share price of Nature Corp and Blue Nile was USD 100 and USD 50 respectively.
Considering these what is the implied Offer Price?

(a) 70.00
(b) 60.00
(c) 40.00

Q7. Joshua, a Blackrock banker intends to read about Required Return from Google material. Which of the following is another name for the required return on a stock, for his effective search?

(a) Discount Rate
(b) Dividend Payout Ratio
(c) Risk Free Rate

Q8. Which of the following is equal to the present value of all cash proceeds received by a stock investor?

(a) Value
(b) Retention Ratio
(c) Dividend Payout Ratio

Q9. Nature Corp. can reinvest net income to earn 18% per year. What will be Nature's long-term dividend growth rate if Nature constantly pays out 25% of earnings as dividends?

(a) 22.50%
(b) 13.50%
(c) 4.50%

Q10. Old Quartz Gold Mining Company is expected to pay a dividend of USD 6.00 in the coming year. Dividends are expected to decline at the rate of 2% per year.
The risk-free rate of return is 6% and the expected return on the market portfolio is 14%. The stock of Old Quartz Gold Mining Company has a beta of -0.25 (negative).

What would be the intrinsic value of this stock?

(a) 100.00
(b) 98.00
(c) 37.50

Q11. Fools Gold Mining Company's dividends are expected to decline at the rate of 2% per year. The risk-free rate of return is 6% and the expected return on the market portfolio is 14%. The stock of Fools Gold Mining Company has a beta of −0.25 (negative).

What would be the minimum return you should require to invest in this stock?

(a) 8.00%
(b) 1.00%
(c) 4.00%

Q12. Predictable Corp has increased its annual dividend each year of its life by 2% (and will continue to do
so indefinitely).
If Predictable paid its annual dividend yesterday of USD 8.00 and the cost of capital is currently 4%, then by what amount will the stock price change by, if the cost of capital increases to 5%?

(a) 136.00
(b) -136.00
(c) -133.33

Q13. Mike, an analyst is searching for an LBO candidate in Tyre Industry.
Which of the following is generally not considered as a characteristic of a strong LBO Candidate?

(a) Strong Cash Flow Generation Capacity
(b) Weak Asset Base
(c) High Growth Opportunities

Q14. Which of the followings are almost always involved in Leveraged buyouts (LBOs)?

I. A large part of the purchase price is financed mostly by debt
II. Most of the debt financing is below investment grade (junk)
III. The firm goes private and its shares are no longer traded in the open market

(a) I, II and III
(b) I and III
(c) II and III

Q15. Accenture is evaluating acquisition of Health Net.

Health Net has an existing share-holders' equity of USD 700 million, where as USD 825 million has been agreed to be paid by Accenture as purchase price of Health Net's Equity.
Accenture already has existing goodwill of USD 175 million on its balance sheet before this acquisition.

What would be the Goodwill amount on the balance sheet of
Accenture post acquisition, whichwould be tested annually for impairment? (in Millions)

(a) 50.00
(b) 300.00
(c) 175.00

Q16. Angelina, an analyst of Goldman is working on a buyer screening mandate for Dunlop Corp (Target).
To have an effective Buyer search, she spoke to few of her colleagues and came across following statements:

I. A Strategic Acquirer typically will be willing to pay more for a company than a Financial Sponsor
II. A Strategic Acquirer typically will be willing to pay less for a company than a Financial Sponsor
III. Both Strategic Acquirer and Financial Sponsor typically will be willing to pay same amount for a company

Which of these statements is correctly stated?

(a) I. A Strategic Acquirer typically will be willing to pay more for a company than a Financial Sponsor
(b) III. Both Strategic Acquirer and Financial Sponsor typically will be willing to pay same amount for a company
(c) II. A Strategic Acquirer typically will be willing to pay less for a company than a Financial Sponsor

Q17. Which of the following companies is an ideal candidate for reverse merger?

(a) An unlisted company looking to raise fresh funds through private placement
(b) A listed company with high trading volumes in the share market
(c) A listed company that has shut down all its business operations but continues to exist legally
(d) A listed company against which bankruptcy proceeding have been initiated

Q18. Which of the following accurately describes underwriting?

(a) Underwriting involves a commitment by the underwriter to offload additional stake in the event of over subscription of securities
(b) Underwriting involves a commitment by the underwriter to subscribe to the remaining shares if the entire issue is not subscribed by the public
(c) Underwriting involves a commitment by the underwriter to make good any loss to the issuer on account of difference between the issue price and pre-agreed price
(d) Underwriting involves a commitment by the underwrite to make good any loss to the investors if the listing price of the share is below the issue price

Q19. Which of the following statement about stock split is appropriate?

(a) It affects the price of the share but does not affect the face value of the share

(b) It affects the overall shareholder's value but does not affect the face value of the share
(c) It affects the price of the share as well as the wealth of the shareholders
(d) It affects the price of the share but does not affect the overall shareholder's value

Q20. Which of the following benefits of spin-off is most accurate?

(a) Spin-off enables better discovery of value of business that is being spun-off
(b) Spinning off loss making business units enable company to save taxes
(c) Spinning off business units make it easy to maintain books of accounts
(d) Spinning off business enables promoters to increase their stake in the business

Q21. Which of the following should raise a major red flag at the time of financial due diligence for mergers and acquisitions (M&A)?

(a) A foreign currency debt of 350 million fully disclosed in the balance sheet
(b) An agreement to pay 1% interest per month to suppliers on delayed payment, not disclosed earlier.
(c) Golden Parachute to the company CEO
(d) Loan covenant that requires prior approval from the lender for any M&A transactions.

Q22. The return on capital employed of a company is 7% while its cost of debt is 9%. Which of the following statement is correct about its return on equity (ROE)?

(a) ROE is likely to be 2%
(b) ROE is likely to be between 7% and 9%
(c) ROE is likely to be above 9%
(d) ROE is likely to be below 7%

Q23. Which of the following statement is most accurate about financial leverage?

(a) Financial leverage can help increase ROE if business conditions are favourable
(b) Companies with high financial leverage would be better positioned to survive tough economic conditions compared to companies with low leverage
(c) High financial leverage would always result in lower ROE as the company would have higher interest burden
(d) High financial leverage would always result in higher ROE as the company would require relatively less equity

Q24. Preleverd Co has an EBITDA of GBP 60 million. It currently has three categories of debt: (i) Senior debt of GBP 30 million at 4% interest per annum (ii) Mezzanine debt of GBP 120 Million at 8% interest per annum and (iii) Subordinate debt of GBP 60 million at 8% per annum. Which of the following is closest to Debt/EBITDA ratio relevant for the Mezzanine debt holders?

(a) 2.0
(b) 2.5
(c) 3.0
(d) 1.5

Q25. A corporate bond with coupon rate of 8% is currently trading USD 94. Which of the following is most likely to be true about yield to maturity (YTM) on the bond?

(a) YTM is equal to 8%
(b) YTM is below 8%
(c) YTM is above 8%
(d) YTM is equal to 14%

Q26. Jennifer was giving a lecture on American Depository Receipt" at an university where she made the following statement:"It is possible for a depository to issue an ADR even without getting any permission from the company whose shares underlie the ADR. These are called as unsponsored ADRs and they carry the same rights as that of a sponsored ADR"

(a) Jennifer is correct about both issuing unsponsored ADRs and the rights of such ADR holder
(b) Jennifer is correct about issuing ADR but incorrect about the rights
(c) Jennifer is correct about issuing ADR but incorrect about the rights

Q27. Which of the following is *least* accurate about the desirability of a collateral?

(a) Collateral should be liquid
(b) Collateral should have low correlation to that of the underlying loan
(c) Collateral should have a high positive correlation with the business of borrower
(d) Collateral should be marketable

Q28. Which of the following listing methods result in fresh funds being raised by the company?

(a) Initial Public Offering
(b) Offer for sale
(c) Reverse merger
(d) Listing by placement

Q29. Which of the following are the reasons for which a fixed price issue may be preferred over book-building?

(a) It reduces the chances of under subscription
(b) It enables issuer to get higher price compared to book building
(c) It is less cumbersome than book building
(d) It is easy to determine the number of shares that are likely to be subscribed

Q30. Gracious corp. is considering the acquisition of Lever corp. in an all cash deal. The two companies last reported an EPS of INR 24 and INR 9 respectively. The synergy from the acquisition is likely to result in net EPS accretion of INR 2 per share. Which of the following is closest to the maximum consideration that can be paid to shareholders of Lever corp. so that there is no dilution in the value of shareholders of Gracious Corp? Assume that the fair PE multiple for both the companies in 10x.

(a) INR 90 per share
(b) INR 100 per share
(c) INR 20 per share
(d) INR 110 per share

Q31. Gracious corp. is considering the acquisition of Lever corp.
in an all share deal. Gracious corp. last reported a net profit of USD 200 mn while Lever corp. reported a net profit of USD 60 mn. The two companies had 40 mn and 20 mn shares respectively. The companies estimate that they could have realised net synergy benefit of USD 20 million in the previous year if the business combinationhad already taken place. Calculate the maximum number of shares that Gracious corp. would be willing to issue so that there is no reduction in their EPS.

(a) 26.7 mn shares
(b) 16 mn shares
(c) 12 mn shares
(d) 44 mn shares

Q32. NAL Capital held 840 shares out of 1500 shares that were issued in a company. Another investor invested USD 200 million in a fresh round of funding against 20% stake in the company. Calculate the value of the stake held by NAL Capital.

(a) USD 560 million
(b) USD 467 billion
(c) USD 448 million
(d) USD 112 billion

Q33. Which of the following accurately explains the difference between certificate of deposits and fixed deposit?

(a) Certificate of deposit is a bearer instrument whereas fixed deposit is not a bearer instrument
(b) Fixed deposit is a bearer instrument but certificate of deposit is not a bearer instrument
(c) Fixed deposits are negotiable instrument whereas certificate of deposits are not negotiable
(d) Certificate of deposits are negotiable instrument whereas fixed deposits are not negotiable instruments

Q34. Which of the following is a bearer instrument?

(a) Commercial paper
(b) Treasury bills
(c) Certificate of deposits
(d) Repo Contracts

Q35. A company has two classes of equity shares: Class A and Class B. Class B shares are not entitled to any voting rights but are entitled to enhanced dividend of USD 0.20 over and above the dividends of Class A shares. The market estimates the voting rights to be worth USD 0.50 per share. Which of the following is closest to fair value of Class B shares, if Class A shares are valued at USD 20 per share, and the company's cost of preferred capital is 10%?

(a) USD 20.5
(b) USD 21.5
(c) USD 22.0
(d) USD 20.5

Q36. Which of the following accurately describes the impact of risk on the valuation multiple of a company.

(a) Companies with higher risk traded at relatively higher valuation multiples compared to its peers
(b) The PEG ratio of company with higher risk is likely to be higher than companies with lower risk
(c) Companies with higher risk traded at relatively lower valuation multiples compared to its peers
(d) Companies with higher risk tend to have higher EV based multiple while having lower price based multiple compared to its peers

Q37. Why measures of systematic risk such as Beta may not be appropriate in evaluating private equity investments?

(a) Measures of systematic risk assume that the investors is likely to hold a diversified investment, which may not be appropriate in private equity context.
(b) Private companies are not part of an index
(c) Higher tax rates in case of private equity transaction adds additional risk

Q38. A bank has total risk weighted assets of GBP 240 billion and Tier 1 capital of GBP 20 billion. The company intends to increase its Tier 1 capital adequacy ratio to 9% by securitizing its assets. Calculate the value of assets that need to be securitized assuming all assets carry 100% risk weightage.
Note: Tier 1 capital adequacy ratio is calculated as Tier 1 capital divided by total risk weighted assets

(a) GBP 1.8 billion
(b) GBP 40 billion
(c) GBP 20.0 billion
(d) GBP 17.8 billion

Q39. An unsecured debt of a bank with USD 350,000 outstanding has gone bad. The net realisable value of the company's assets is expected to be USD 600,000 of which USD 400,000 is expected to be paid towards servicing senior debt obligation of the company. The entire process is likely to take an year. What is the fair value at which the bank can sell it to an asset reconstruction company (ARC) if the ARCs expect an annual return of 8%.

(a) USD 200,000
(b) USD 185,185
(c) USD 350,000
(d) USD 296,610

Q40. Which of the following is an example of maintenance covenants?

(a) The company shall not pay any dividends to shareholders

(b) The company should take prior permission from the lender before raising any further debt
(c) The company's interest coverage ratio should always be above 2.0x
(d) The company should pay back the entire loan outstanding in the event of any takeover

Q41. A company has won the bid for a project that is likely to commence in 18 months. The company is worried about increase in interest rates that could make the project unviable. Which of the following position can help the company protect itself from increase in interest rates?

(a) Enter into forward rate agreement to borrow at a fixed rate in future
(b) Enter into a forward rate agreement to lend at a fixed rate in future
(c) Invest the capital required for the project in treasury bond to earn interest till the project commences

Q42. Steven and Dean were discussing Enterprise Value of two companies, Climatic Corporation and Weather Inc. Climatic Corporation has raised additional debt that is held on the balance sheet as cash and Weather Inc issues equity and uses the proceeds to repay debt. What's the effect of these transactions on Enterprise Value?

(a) Increases for Climatic Corporation and decreases for Weather Inc.
(b) Remains constant for both companies.
(c) Decreases for Climatic Corporation and Increases for Weather Inc.
(d) Increases for both companies.

Q43. Delta Corporation agreed to exchange 0.6 shares of its stock for every 3 shares of the target stock. What is the exchange ratio for this transaction?

(a) 5
(b) 0.17
(c) 0.20
(d) 0.25

Q44. Tomato Inc has Account Receivable of USD 35 million, Sales of 350 million, Inventory of USD 20 million, Cost of Goods Sold (COGS) of USD 250 million. What's Inventory Turns for Tomato Inc?

(a) 17.5
(b) 0.08
(c) 12.5
(d) 0.06

Q45. Asia Venture Partners (AVP) was established to provide equity financing to later stage to 'Mobile App' companies. For one of their funds AVP1, in 2013 capital called down is USD 25 million, Paid in capital is USD 145 million, Management fees are USD 2.7 million, DPI is 1.8, and RVPI is 2.2. What is the TVPI after 2013?

(a) 4
(b) 0.4
(c) 0.82
(d) 1.22

MOCK TEST
ANSWERS

Q1. (a)

Q2.(c) EV = Equity + Debt – Cash
(2 x 10) + 5 – 7 = USD 18 million
Total Revenues has no role to play in EV equation.

Q3. (c)

Acquisition Value
= Book Value + Premium
= 34 + 34*20%
= USD 40.80 million

Q4. (b)

A. Screen the Universe of Comparable Acquisitions
B. Spread Key Statistics, Ratios, and Deal Multiples
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Q5. (c) 60

Exchange Ratio define the number of shares of the acquirer's stock to be exchanged for each share of the target's stock.

Offer Price = 0.6*100
= USD 60.00 per share

Q6. (a)

Offer Price
= Cash + Stock consideration
= 10 + 0.6*100
= USD 70.00 per share

Q7. (a) Discount rate

Q8. (a)Value

Q9. (b)

Long-Term Growth Rate
= (1-Payout Ratio) * ROE
= (1-0.25) * 18% = 13.50%

Q10. (a)

$K_e = R_f + B(R_m - R_f)$
$= 6\% + [-0.25(14\% - 6\%)] = 4\%$

$P_0 = D1 / (R - G)$
$= 6/[4\% - (-2\%)]$
= USD 100.00

Q11. (c)

$K_e = R_f + B(R_m - R_f)$
$= 6\% + [-0.25(14\% - 6\%)] = 4\%$

Q12. (b)

$P_o = D_0 * (1+G) / (R - G)$

Before = 8*(1+2%)/(4%-2%)
= USD 408.00

After = 8*(1+2%)/(5%-2%)
= USD 272.00

Decreased by USD 136 (408-272) or negative change

Q13. (b) A strong asset base is pledged as collateral against the Leveraged Financing condition to work.

Q14. (a) All of the options are almost always involved in Leveraged buyouts (LBOs)

Q15. (b)

Goodwill is created from the excess amount paid for a target over its existing book value.

Total Goodwill
= Existing + New Creation
= 175 + (825-700)
= USD 300 million

Q16. (a)

II. A Strategic Acquirer typically will be willing to pay less for a company than a Financial Sponsor. Because the strategic acquirer can realize revenue and cost synergies that the Financial Sponsor cannot unless it combines the company with a complementary portfolio company. Those synergies boost the effective valuation for the target company

Q17. (c) A listed company that has shut down all its business operations but continues to exist legally

Q18. (b) Underwriting involves a commitment by the
underwriter to subscribe to the remainingshares if the entire issue is not subscribed by the public

Q19. (d) It affects the price of the share but does not affect the overall shareholder's value

Q20. (a) Spin-off enables better discovery of value of business that is being spun-off

Q21. (c) Golden Parachute to the company CEO

Q22. (d) ROE is likely to be below 7%

Q23. (a) Financial leverage can help increase ROE if business conditions are favourable

Q24. (b) 2.5

Q25. (c) YTM is above 8%

Q26. (b) Jennifer is correct about issuing ADR but incorrect about the rights

Q27. (c) Collateral should have a high positive correlation with the business of borrower

Q28. (a) Initial Public Offering

Q29. (c) It is less cumbersome than book building

Q30. (d) INR 110 per share

Q31. (b) 16 mn shares

Q32. (c) USD 448 million

Q33. (d) Certificate of deposits are negotiable instrument whereas fixed deposits are not negotiable instruments

Q34. (a) Commercial paper

Q35. (b) USD 21.5

Q36. (c) Companies with higher risk traded at relatively lower valuation multiples compared to its peers

Q37. (a) Measures of systematic risk assumes that the investors is likely to hold a diversified investment, which may not be appropriate in private equity context.

Q38. (d) GBP 17.8 billion

Q39. (b) USD 185,185

Q40. (c) The company's interest coverage ratio should always be above 2.0x

Q41. (a) Enter into forward rate agreement to borrow at a fixed rate in future

Q42. (b) Remains constant for both companies.

Q43. (c) 0.20

Q44. (c) 0.06

Q45. (a) 4