MODEL PAPER

PRACTICAL INDUSTRY KNOWLEDGE (PIK) EXAMINATION

[COMPUTER BASED EXAMINATIONS]

[S5] Strategic Financial Management [Strategic Level-2]

TIME ALLOWED: 03 HOURS | MAXIMUM MARKS: 100

Effective from October 2025 Examinations

EXAMINATION DEPARTMENT

MULTIPLE CHOICE QUESTIONS (MCQs)

Question No.1

Abbas Limited requires an investment of Rs.360 million and needs to increase its working capital by Rs.40 million. Earnings before taxes are Rs.3,600 million, and it sets off Rs.240 million of depreciation. The tax rate is 29%. The amount of free cash flow is: **[04 Marks]**

A	Rs.2,554 million
B	Rs.2,360 million
C	Rs.2,396 million
D	Rs.2,634 million

Question No.2

Following information relates to Sameer Limited:

Cost of debt	8%	
Cost of equity	18%	
No of equity shares	3,200,000	
Market price of equity shares	Rs.35	per share
Market price of bond	Rs.35,000,000	
Tax rate	29%	

What is the weighted average cost of capital? **[04 Marks]**

A	15.73%
B	14.87%
C	16.23%
D	15.07%

Question No.3

Abbas Limited requires an investment of Rs.360 million and needs to increase its working capital by Rs.40 million. Earnings before taxes are Rs.3,600 million and it sets off against Rs.240 million of depreciation. Tax rate is29%.

What is the free cash flow?

	Rs. in million
Investment required	755
Increase in working capital required	92
Earnings before tax	7,400
Depreciation for the year	499
Tax rate	29%

[04 Marks]

A	Rs.4,906 million
B	Rs.4,521 million
C	Rs.4,272 million
D	Rs.4,025 million

[Note: The questions made available through this Model Paper reflects the pattern of questions to be tested in exams.]

Question No.4

Net cash flows relating to a project are as follow:

	YEAR			
	1	**2**	**3**	**4**
Cash flows (Rs. in million)	200	450	700	850

Other information:

	Rs. in million
• Initial investment in asset	1,650
• Residual value after 4 years	150

For depreciation use straight-line method

Return on capital employed using initial investment will be: **[04 Marks]**

A	12.55%
B	10.61%
C	13.32%
D	9.19%

Question No.5

A company with cost of capital of Rs.10% has undertaken a project with the following cash flows:

		Rs. in million	
Year	**Purchase of plant**	**Running costs**	**Savings**
0	(13,723)		
1		(3,950)	13,650
2		(4,580)	11,120

In order to break even, the cost of plant is required to be increased/ decreased by Rs.__________. **[04 Marks]**

A	Rs.500 million
B	Rs.600 million
C	Rs.700 million
D	Rs.800 million

Question No.6

Sahil Limited is an ungeared company having a cost of equity of 18%. It has an opportunity to take out a loan which is available at the rate of 10% per annum. If the company takes out the loan, the debt-to-equity ratio will be 2:3. Assume that the tax rate is 29%. The WACC after the loan has been taken out will be _________. **[04 Marks]**

A	16.74%
B	13.82%
C	10.32%
D	15.91%

Question No.7

Zayan Limited (ZL) is foreseeing a growth rate of 12% per annum in the next 2 years. The growth rate is likely to fall to 10% for the third year and fourth year. After that the growth rate is expected to stabilize at 8% per annum.

If the last dividend paid was Rs.1.5 per share and the investors' required rate of return is 16%, the intrinsic value per share of ZL as of date would be ___________.

(Note: use discounting factor to 2 decimal places) **[04 Marks]**

A	Rs.22.33
B	Rs.30.75
C	Rs.16.91
D	Rs.32.25

Question No.8

Wilfred Limited (WL) pays no taxes and is entirely financed by equity shares. The equity share has a beta of 0.60 and a P/E ratio of 5 and is priced to offer an expected return of 20%.

WL has now decided to buy back half of its equity shares by borrowing an equal amount. The debt yields a risk-free rate of return of 9%.

The beta of the equity shares and the risk premium after the buy-back will be: **[04 Marks]**

A	0.83; 35.51%
B	1.2; 18.33%
C	1.2; 27.33%
D	0.83; 31.00%

Question No.9

Pelbus Limited currently has a debt/equity ratio of 0.15 and a return on equity equal to 18.2%. However, the optimal debt ratio is much lower than the optimal level, since it can raise the debt/equity ratio up to 0.40 without increasing the risk of bankruptcy. The firm plans to borrow and repurchase stock to get to this optimal ratio. The interest rate is expected to increase from 8% to 9%. The tax rate is 29% and the retention rate is 55%. The impact of the increase in debt on the growth rate will be by ___________. **[04 Marks]**

A	0.50%
B	0.74%
C	0.85%
D	1.52%

Question No.10

Yale Limited has 10 million ordinary share issued and fully paid, and these are currently quoted on the PSX at Rs.24. Earnings are relatively stable and as reported in the more recent accounts, were equivalent to Rs.6 per share.

The company wishes to redeem Rs.45 million 10% loan stock by making rights issue of ordinary shares, but does not want to dilute the earnings per share by more than 10%. The rights issue is to be priced approximately 20% below the market price at the time of issue. The applicable tax rate is 29%.

What is the lowest market price at which Yale would consider making the issue? **[04 Marks]**

A	Rs.3.84 rights price
B	Rs.4.80 rights price
C	Rs.45.29 rights price
D	Rs.29.45 rights price

[Note: The questions made available through this Model Paper reflects the pattern of questions to be tested in exams.]

CASE STUDY

Phantom Automobile Group (PAG) is a leading player in the automotive industry comprising Phantom Automobile Limited (PAL) and its two subsidiaries. The group is competing with more than fifteen competitors in a highly competitive environment. PAL was established in 2017 through a management buy-out (MBO) from a listed company Albert Engineering Limited (AEL) and is managed by four key MBO Team Members.

PAL is situated at a large, relatively under-utilized site. The site was purchased from AEL at the time of MBO. A part of the under-utilized site was sold to a Telecommunication Corporation during the year 2025 which has resulted in a substantial capital gain on sale.

Mr. Sajid Zafar is the Chairman of the group. He and his family own 65% of the 1,000,000 ordinary shares of Rs.10 each in PAL.

Since MBO, the group has witnessed a drastic increase in the annual revenue.

You, are an Audit Manager of Spencer Consultancy Firm (SCF) and have recently conducted the audit of PAL for the year ended June 30, 2024.

You have received the following memorandum from the Audit Partner of SCF.

MEMORANDUM:

As you may be aware that Mr. Sajid Zafar is proactive to realize his investment from the group so he may opt for another investment opportunity. He also desires that the realization of his investment does not undermine the ability of the company to grow. But at the moment it appears that he is reluctant whether to retain control of the business or may deviate to the prospective opportunity.

There a number of issues that Mr. Sajid is confronting:

- He is keen to know the worth of his holding in the group and the suitable method for realizing his investment
- As the staff has grown substantially since 2017 to 2020 and there are now some very highly motivated managers in the business. Mr. Sajid is concerned about the following, if he does relinquish control:
  - The impact that a change of ownership may have on staff.
  - The problems that might develop if new owner(s) acquire the majority shareholdings.

In order to keep his management personnel contented, Mr. Sajid is willing to introduce a share option scheme as part of remuneration package for the managers to incentivize them, and for that purpose he would like us to provide a feasibility report. He is concerned as to how the issue of such options may impact the financial accounts of the business and the audit procedures.

Apart from Mr. Sajid's decision to realize his investment, he is anxious about the issue of sustainability that needs to be prioritized at Phantom Automobile Limited, and has saved extracts from several newspaper articles related to this area (**Annexure 2**). He believes that the other three shareholders are rather dismissive of it and think that the success of PAL should only be judged on financial aspects. He has asked us for any comment we have to offer on the importance of sustainability for businesses.

Requirement:

Prepare a report for the audit partner, addressing all the areas of concern of Mr Sajid and deliberating the following:

(a) A discussion of the possible options available to Mr. Sajid for realizing his investment. **[15 Marks]**

(b) Using the information in the as appended in (**Annexure 1**), estimate the value of Mr. Sajid's holding, using the following valuation methods:

- **(i)** Dividend growth **[15 Marks]**
- **(ii)** Free cash flows **[15 Marks]**

Note: You may ignore the tax issues that might arise if Mr Sajid realizes his investment.

(c) Identify the problems which might arise if new owners acquire a majority shareholdings in the group and using the information from the newspaper articles (**Annexure 2**) as appropriate, explain the importance of sustainability to Phantom Automobile Limited. **[15 Marks]**

ANNEXURE-1

Phantom Automobile Group
Information Pack – for the year ended June 30, 2025

1) History

The group was the subject of a management buy-out from Albert Engineering Limited (AEL), in 2017 and continues to be owned and managed by a buy-out team. The shareholding ownership structure is as follows:

Name	Shareholding
• Mr. Sajid Zafar and Family	65%
• Mr. Ghazanfar Khan	12%
• Mr. Luqman Baig	12%
• Mr. Azeez Kamal	11%

2) Possible flotation

The possibility of PAL for floating shares is presently under review. The share flotation will enable the shareholder directors to realize some of their investment in PAL and provide access to capital markets.

3) Competitors

The group is diverse in activity; the companies that most closely resemble PAL are Faisal Engineering Limited (FEL) and Crest Allied Limited (CAL).

4) Management

The subsidiaries of PAL are managed at an operational level by three of the shareholder directors.
The fourth, and majority, shareholder director is the group's Chairman who provides strategic direction to the group.

5) Capital expenditure

PAL recognizes the need to replace existing plants over the next few years due to normal wear and tear and also the need to maintain its competitive advantage by applying the latest technology.

6) Summary trading results

The impact of investment and the benefit of productivity improvements have resulted in a reduction in employee numbers while continuing to increase output. Sales, profit and staff number growth have been as follows:

Rs. in million

Years	2020	2021	2022	2023	2024	2025
Sales	68,400	70,376	75,810	79,068	83,482	83,594
Cost of sales	48,358	50,248	53,370	53,054	53,516	53,542
Gross profit	20,042	20,128	22,440	26,014	29,966	30,052
Operating costs	13,092	12,942	14,738	17,098	21,378	21,442
Operating profit	6,950	7,186	7,702	8,916	8,588	8,610
Profit on disposal of property	–	–	–	–	–	26,768
Profit before interest	6,950	7,186	7,702	8,916	8,588	8,610
Interest	(1,700)	(1,300)	(1,920)	(1,960)	(1,240)	1,198
Profit before tax	5,250	5,886	5,782	6,956	7,348	9,808
Tax	(1,523)	(1,707)	(1,677)	(2,017)	(2,131)	(2,844)
Profit after tax	3,728	4,179	4,105	4,939	5,217	6,964
Dividends	1,640	1,700	1,776	1,844	1,920	2,000
Staff numbers	522	515	511	502	494	490
Gross profit margin	29.3%	28.6%	29.6%	32.9%	35.9%	35.9%

The following the property disposal in this most recent year, PAL has Rs.35,200 million of cash on its statement of financial position.

[Note: The questions made available through this Model Paper reflects the pattern of questions to be tested in exams.]

7) Forecast figures 2026 – 2030

- Sales and gross profits to rise by 10% each year.
- Other operating costs excluding depreciation to rise by 3% per annum.
- Depreciation for the year 2026 to remain at the 2025 figure of Rs. 4,000 Million; the only change in the period 2026-2030 is a rise to Rs. 5,200 million from the year 2029 due to the acquisition of new assets.
- Significant expenditure of Rs. 12,000 million on non-current assets in the year 2029. Other non-current asset acquisitions and disposals to cancel out each year.
- The interest for 2026-2030 will remain at 2025 level.
- Working capital levels to increase at the start of each year to be 10% of that year's predicted sales.
- Tax to be charged at 29% of taxable profits over 2026-2030. Depreciation is fully tax allowable against profits.

8) Sector and company information

The current risk-free interest rate is 11%. The following company and sector information is provided.

	Company	Sector
P/E ratio	12.3	9.625
Beta	1.00	0.65
Expected return	18.00%	N/A

Annexure: 2

Extracts from press articles about sustainable automobile production

'The increased awareness and sheer interest in economic and environmental concerns of stakeholders at this point of time has led manufacturers to develop consistently environmental friendly automobiles and related products that contribute to a better environment.'

'Building a more environmentally friendly business for the future'.

Crest Allied Limited (CAL) has recently launched new design and battery concepts which includes, fuel cells that will have a clear advantage over these older technologies in having lower carbon dioxide (a greenhouse gas) emissions. The company is keen to make a contribution to ensure sustainable development in reducing its environmental footprint. Another key player in the engineering company, Faisal Engineering Limited (FEL) that has introduced a new design hydrogen powered vehicles. It will significantly reduce the company's carbon footprint, as well as saving costs on raw materials.'

'Consumers are demanding more renewable materials and environmental labelling on the products they buy. Many rate hydrogen automobiles as the most eco-friendly type and 38% of consumers said they regularly search for environmental labels and logos on vehicles manufacturing.'

'According to CAL's CEO, 'the findings [of a survey] reinforce the importance of putting environmental issues at the heart of the company's agenda… We have no illusions about the challenges we face, but by finding new ways to eco-friendly vehicles, we will make a difference for the future'.'

THE END

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