

Session 25: Post Class tests

1. Westerly Inc. is a publicly traded company that generated \$1000 million in operating income in the most recent year, after taking a depreciation charge of \$200 million. The company had capital expenditures of \$500 million during the year and its working capital increased by \$120 million. If the effective tax rate for the company was 30% for the year, what is the FCFF (Free Cash flow to the Firm) for the most recent year?
 - a. \$80 million
 - b. \$280 million
 - c. \$580 million
 - d. \$780 million
 - e. None of the above
2. Now assume that Westerly reported a book value of equity of \$2.5 billion and book value of debt of \$1.5 billion at the start of the most recent year; the cash balance at the start of the year was \$0.5 billion. Assuming that Westerly maintains its existing return on capital and reinvestment rate, what is the expected growth rate in operating income for Westerly?
 - a. 8.4%
 - b. 10.5%
 - c. 12%
 - d. 16.8%
 - e. None of the above
3. You expect Westerly to become a mature company at the end of year 5, growing 3% a year in perpetuity. Assuming that you expect Westerly's return on capital to drop by half from current levels after year 5, what would your reinvestment rate be in year 6 (the first year for your stable growth)?
 - a. 0%
 - b. 25%
 - c. 30%
 - d. 60%
 - e. None of the above

Bonus: Estimate the terminal value at the end of year 5, if your cost of capital is 9% in perpetuity.

4. You are valuing Neruda Telecom, a growing telecom company. You have estimate the free cash flows to equity and cost of equity for the company for the next three years below (in millions):

	1	2	3
FCFE	-\$25.00	\$50.00	\$150.00
Cost of equity	14%	12%	10%

You expect the cash flows to grow 3% a year in perpetuity after year 3 and the cost of equity to stay at year 3 levels in perpetuity (after year 3). What is the value of equity in the firm?

- a. \$1,553 million
 - b. \$1,650 million
 - c. \$1,696 million
 - d. \$1,789 million
 - e. \$2,331 million
5. You are valuing Uggle Inc., discounting free cash flows to the firm at the cost of capital and have arrived at a present value of \$2.5 billion. The company has \$300 million in cash, \$600 million in debt (market and book value) and a minority holding in other company (10% of that company) that is valued at \$150 million. If there are 100 million shares outstanding, what is the value of equity per share?
- a. \$14.50
 - b. \$17.50
 - c. \$20.50
 - d. \$23.50
 - e. \$35.50