Session 24: Post class test solutions

1. **e. $70 million.** FCFE = 100 + 50 – 75 - 20 + 15 = 70 million
2. **d. $80 million.** FCFE = 100 + 50- 75+20-15 = 80 million
3. **c. $35 million.** FCFE = 80 + 30-60 = 50 million. Since the cash balance increased by $15 million, the company must have paid out $15 million less than the FCFE = $50 -15 = $35 million.
4. **c. Maybe (probably no)**. First, I have to check the FCFE. While the earnings are positive, it is possible that the company, being a growth company, has other reinvestments that make the FCFE negative. Second, I have to check future reinvestment needs to see if the company may need the cash in future years. It is likely that the company will not be able to pay dividends yet.
5. **b. $214 million**. First, compute the FCFE
   FCFE = 150(1.1) + 60(1.1) -100(1.1) - .08 (1100-1000) = 113
   Note that working capital is currently 8% of revenues and will continue at that same percent next year.
   The dividends paid are 60% of net income = .60 (165) = 99
   Change in cash balance = 113- 99= +14
   New cash balance = 200 + 14 = $214 million
6. **f. Company F: ROC = 5%, Actual debt ratio = 10%**. An under levered company that takes bad projects has no business holding on to cash. It cannot claim that it needs the cash for great projects or as a buffer against a downturn (default).