



Guildhall College, London

GCL FEA - Corporate Finance and Governance

Assignment 1: Individual Report:

Module Tutor:

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Submission Deadline

Friday, 13 August 2010 (at 11am),
At Programme Admin Room, Ground Floor, Building 1, Nelson Street

Background

Mineral plc is a large, international mining company operating several mines throughout the world, its operating activities spans gold mining, diamond, copper, crude oil exploration. It has several refinery plants all over the world employing over 150,000 staff across the world.

Mineral plc is a UK listed company and was formed in 1940. The company's principal base is central London, where the company's head office is located.

In the year ended 31 March 2008 the group had total revenue of £7 billion and total profit for the year of £800 million. Mineral plc is going through a restructuring period where it is attempting to increase its profitability by diversifying its operations and exploring the possibilities of expanding its activities in Africa where it has little presence especially in Medco Republic (MR).

The country is endowed with vast potential wealth and rich in mineral resources, but due to political instability as a result of conflict that began in August 1998, its economy has really declined and has dramatically reduced national output and government revenue, increased external debt, and resulted in the deaths of more than 5 million people from violence, famine, and disease. Its interest rate is very high and its currency is volatile, depreciating constantly against all major currencies.

Previously, foreign companies have been subject to unfavourable treatment by the government, assets of foreign companies have been ceased and confiscated by the state, with some of such companies been nationalised by the state, giving various reasons for such actions.

From the 1990's to present foreign businesses curtailed their operations due to uncertainty about the outcome of the conflict, political instability, rebel activities, lack of infrastructure, and the difficult operating environment.

Medco Republic (MR) has up to now had a volatile political environment, and there are currently no western mining companies operating in the country at the moment. However, the country had its first democratic election in 2005, after more than fifteen years.

In late 2006 the transitional government reopened relations with international financial institutions and international donors, the new government has began to implement reforms, although progress has been slow, with much of the economic activity still occurring in the informal sector.

Renewed activity in the mining sector, the source of most export income, boosted fiscal position and GDP growth from 2006-2008, the reform by the new government and assurance to foreign firms of new era of business and development in the country, with government promising foreign multinational

companies transparent business policies and tax incentives to encourage businesses to return to the country, this they hope will boost the national economy and increase employment.

Companies operating in Medco Republic (MR) have poor record on corporate social responsibility and seem not to care about it. In a recent report commissioned by a global body on the activities of companies in Medco Republic (MR), the report stated that government has done very little to promote corporate social responsibility among companies in the country and that they need to have a voluntary policy on corporate social responsibility for companies wanting to do business in the country.

Board meeting

In a recent board meeting, the operations director commented that “the company should review its initial position of not undertaking new investments in conflict or war torn countries, where there are political instability, since in the case of Medco Republic (MR), even though it seems that the conflict is not over, the country seems to be moving in the right direction after the election in 2005 and currently has reduced rebel activities”

The marketing director supported the view of the operations director and added that for the company to increase its profitability and increase return to shareholders, they should take advantage of the new government incentives to promote business in Medco Republic (MR) and the initial assertion the company championing corporate social responsibility is not relevant in this case, after all Mineral plc will not be the only company doing business with the new government, there are many non western companies already doing business with the new government and why not Mineral plc”, after all shareholders do not care about corporate social responsibility, so long as they receive increasing return on their investment, in the form of increasing dividend and share prices, they should be fine,

The senior independent non-executive director disagreed with the marketing director and commented that the way forward for the company is to champion corporate social responsibility, and sustainable development, since the benefits to the company in the long-run is more than the perceived cost.

Investment data:

The following information relates to the proposed investment by Mineral plc in Medco Republic (MR):

The board is unsure how long the investment in Medco Republic (MR) may last, since they are unsure of the stability of the country and the conflicts, hence they have asked you to prepare an investment appraisal for the first five years using the information provided below.

- (1) Fees for the service of consultant who undertook the initial research into the viability of the project is estimated to be £2 million, £1.2 million of which will be paid upfront for their services, the remainder to be paid on 1 January 2010.

- (2) The site to be used by Mineral plc is estimated to cost £3 million, payment expected to be made at the beginning of the year on 1 January 2009.
- (3) To prepare the site for construction work to begin, the clearing of land, tunnelling and laying pipes, is estimated to be £10 million, the cost is expected to be evenly spread over two years period, at the beginning of 1 January 2009 and 1 January 2010.
- (4) Mineral plc is expected to invest £40 million on buying new machines for the processing of copper, the supplier has agreed to take payment in instalment over three (3) years period, in the proportion of 40%:30%:30%, payment at the beginning of each year, starting 1 January 2009.
- (5) The machine is expected to have a useful life of five years, after which it is expected to have a residual value of £1 million.
- (6) Tax allowable depreciation for such machine is given as 25% reducing balance
- (7) Annual clearing of the land and preparing the site is estimated to be £250,000 per annum current prices, with cost estimated to increase by 3% per annum over the next five years. Clearing of land is expected to begin from 2010.
- (8) Working capital is forecast to be 10% of sales revenue for the period.
- (9) Assume the year 2009 is used to prepare the land, site and acquisition of machines and that the actual production and sales of copper begins from 2010. Assume that all cash flows arise at the end of the year, unless otherwise stated.
- (10) The following data is also relevant:

	2010	2011	2012	2013	2014
Production and sales volume	10 million kg	11 million kg	12 million kg	13 million kg	10.5 million kg
Current market price is estimates to be £1,500 per 1,000 kg and prices expected to increase at 5% per year.					
Chemical reagent cost for processing copper is estimated to be £200 per 1,000 kg, with estimated annual increase in current market price of 2% per year.					
Furnace cost is expected to be fixed over the five years at £500,000 per year from 1 January 2010					
Labour wages is estimated to be £1 million per year and expected to rise by 10% per year over next five years, starting from 1 January 2010.					

Additional information

Mineral plc uses weighted average cost of capital of 15% to discount investment of such nature

Tax rate is the same in both countries at 20% per annum, payable one year in arrears.

The currency is £1 = DM\$1, and is expected to remain the same over the investment life

A tax treaty exists between the two countries and foreign tax paid is allowable against any UK tax liability.

REQUIREMENTS

Requirement

Capital Investment proposal from the financial director has been forwarded to you for consideration and to prepare a report for consideration in the next board meeting. The report should consider the following issue:

The viability of the proposed investment in Medco Republic (MR), using net present value (NPV) and internal rate of return (IRR) methods (40 marks)

What corporate social responsibility and sustainable development issues should the company consider with regards to its proposed investment in Medco Republic (MR)? (15 marks)

The CEO pointed out that it is important for the report to consider the effect of foreign currency risk on the company's investment in Medco Republic (MR) and measures that can put in place to reduce such currency risk. (15 marks)

Your report should include the following headings:

Introduction	Briefly describe context and identify	10%
	Identify general subject	
	Describe the problem or issue to be reported on	
	Define the specific objectives (based on requirements) for this report	
	Signpost the report structure	
	Comment on any limitations	
Discussion	The main body of the report (approx. 2/3 – ¾ of the word length), is divided into logical sections and subsections to answer the requirements.	70%
Conclusion	<p>This section summarises the key findings of the report, as outlined in the Discussion.</p> <p>The Conclusions should:</p> <ul style="list-style-type: none"> ➤ Relate specifically to the requirements/objectives ➤ Identify the major issues ➤ Be specific, and succinct 	10%
References	Use Harvard Referencing Systems (HRS) for both in-text and reference list.	10%

Marks: 50

Deadline: 13 August 2010

Group submission: Individual

Length: 2,000 words

Referencing: Harvard Referencing

HARVARD REFERENCING METHODS

Harvard Referencing System

We expect students to use the alphabetical or name-date method known as the HARVARD system. There are two parts in this system:

1. Citation within text or body of the report:

In this the author's surname and year of publication are cited in the text, e.g. (Bond, 2004).

2. Reference List:

A reference list (of these citations) is included at the end of the assignment, in alphabetical order by author. The reference list also includes additional details such as the title and publisher.

A **bibliography** lists relevant items that you have used in the preparation of the assignment but not cited in your text. A bibliography should also be in the Harvard style and the inclusion of such a list shows that you have read widely beyond the items you have cited.

Examples of citations within text or body of the report:

1. Cormack (1994, p.32-33) states that.....
2. This view has been supported in the work of Cormack (1994, p.32-33).
3. Jones (1946) and Smith (1948) have both shown.....
4. Corporate Author: 1st citation: Royal College of Nursing (RCN), 2007
2nd citation: RCN, 2007

Examples of listings in reference list:

1. Books with one author:

Redman, P., 2006. *Good essay writing: a social sciences guide*. 3rd ed. London: Open University in assoc. with Sage.

2. Books with two, three or four authors

The required elements for a reference are: Authors, Initials., Year. *Title of book*. Edition. Place: Publisher

Kirk, J. & Munday, R.J., 1988. *Narrative analysis*. 3rd ed. Bloomington: Indiana University Press.

3. Books with more than four authors

For books where there are more than four authors, use the first author only with surname and initials followed by "et al".

The required elements for a reference are:

Author, Initials., Year. *Title of book*. Edition. (only include this if not the first edition) Place: Publisher

- Grace, B. et al., 1988. *A history of the world*. Princeton, NJ: Princeton University Press.

4. E-books

For e-books the required elements for a reference are :

Author, Year, *title of book*. [type of medium] Place of publication: Publisher

- Fishman, R., 2005. *The rise and fall of suburbia*. [e-book]. Chester: Castle Press.

If available at website:

- Fishman, R., 2005. *The rise and fall of suburbia*. [e-book]. Chester: Castle Press. Available at: [libweb.anglia.ac.uk / E-books](http://libweb.anglia.ac.uk/E-books) [accessed 5 June 2005]

5 Journal articles

Author, Initials., Year. Title of article. *Full Title of Journal*, Volume number (Issue/Part number), Page numbers.

Perry, C., 2001. What health care assistants know about clean hands. *Nursing Times*, 97(22), p.63-64.

6 Newspaper articles

Author, Initials., Year. Title of article. *Full Title of Newspaper* Day and month before page numbers of article.

Slapper, G., 2005. Corporate manslaughter: new issues for lawyers. *The Times*, 3 Sep. p.4-5.

7 Journal articles from an electronic source

Boughton, J.M., 2002. The Bretton Woods proposal: an indepth look. *Political Science Quarterly*, [online]. 42 (6), Available at: <http://www.pol.upenn/articles> (Blackwell Science Synergy) [accessed 12 June 2005]

8 Internet

National electronic Library for Health. 2003. *Can walking make you slimmer and healthier?* (Hitting the headlines article) [Online]. (Updated 16 Jan 2005) Available at: <http://www.nhs.uk.hth.walking> [accessed 10 April 2005]

The title of a web page is normally the main heading on the page.

9 E-version of annual reports

Marks & Spencer, 2004. *Annual report 2003-2004*. [Online]. Available at: <http://www-marks-and-spencer.co.uk/corporate/annual2003/> [accessed 4 June 2005]