



**PG-612**

12393

II Semester MBA (CBCS) Examination, July - 2019

**MANAGEMENT**

**Paper - 2.5 : Financial Management**

Time : 3 Hours

Max. Marks : 70

**SECTION - A**

Answer **any five** questions, each question carries **5** marks.

**5x5=25**

1. Define Financial Management. Explain its functions.
2. Define Working Capital. What are the factors determining working capital structure in an organization ?
3. What is Time Value of Money ? What is its relevance in financial decision making ?
4. The following are the details regarding the operation of a firm during a period of 12 months :

Sales	₹ 12,00,000
Selling price per unit	10
Variable cost per unit	7
Total cost per unit	9
Credit period allowed to customers	One month

The firm is considering a proposal for a more liberal credit by increasing the average collection period from one month to two months. This relaxation is expected to increase sales by 25%.

You are required to advise the firm regarding adopting of the new credit policy, presuming that the firm's required return on investment is 25 percent.

**P.T.O.**



5. A company has on its books the following amounts and specific cost of each type of capital :

Type of Capital	Book Value ₹	Market Value ₹	Specific Cost %
Debt	400000	380000	5
Preference	100000	110000	8
Equity	600000	1200000	15
Retained earnings	200000		13
<b>Total</b>	1300000	1690000	

Determine the weighted average cost of capital using (a) Book value weights, and (b) Market value weights.

6. Excel Ltd. is considering three financial plans. The key information is as follows :

- (a) Total funds to be raised ₹ 200000  
 (b) Financing Plans :

Plans	Equity %	Debt %	Preference %
A	100	----	----
B	50	50	----
C	50	----	50

- (c) Cost of debt 8%, Cost of preference shares 8%  
 (d) Tax rate 35%  
 (e) Equity shares of the face value of ₹ 10 each will be issued at a premium of ₹ 10 per share.  
 (f) Expected EBIT ₹ 80000

Determine for each plan EPS and Financial BEP.

7. Northern Chemicals Ltd., owns a machine with the following characteristics :

Book Value ₹ 110000  
 Current Market Value ₹ 80000  
 Expected salvage value at the end of 5 years remaining useful life NIL  
 Annual cash operating cost ₹ 36000

The firm's cost of capital is 15%, its tax rate is 35%. The company follows the straight line method of depreciation and the same is accepted for tax purpose. The management of the company is considering selling the machine. If it does so, total cash operating cost to perform the work now done by the machine will increase by ₹ 40000 per year to ₹ 76000 per year. Advise whether the machine should be sold.



## SECTION - B

Answer any three questions, each question carries 10 marks.

3x10=30

8. Define Venture Capital. Explain stages of venture capital. Discuss the recent trends in venture capital financing in India.

9. A firm's sales, variable cost and fixed cost amounts to ₹ 75,00,000, ₹ 42,00,000 and ₹ 6,00,000 respectively. It has borrowed ₹ 45,00,000 at 9% and its equity capital total ₹ 55,00,000.

- What is firm's ROI ?
- Does it have favourable financial leverage ?
- If the firm belongs to an industry whose asset turnover is 3, does it have a high or low asset leverage ?
- What are the operating, financial and combined leverages of the firm ?
- If the sales drops to ₹ 50,00,000, what will new EBIT be ?
- At what level will the EBT of the firm be equal to zero ?

10. ABC Ltd., wishes to raise additional finance of 100 lakhs for meeting its investment plans. It has ₹ 20,00,000 in the form of retained earnings available for investment purposes. The following are further details :

- |                                      |   |                 |
|--------------------------------------|---|-----------------|
| (a) Debt/Equity Mix                  | - | 30%/70%         |
| (b) Cost of debt :                   |   |                 |
| (i) Up to 20 lakhs                   | - | 10%             |
| (ii) Beyond 20 lakhs                 | - | 14%             |
| (c) Earnings per share               | - | ₹ 4             |
| (d) Dividend payout                  | - | 50% of earnings |
| (e) Expected growth rate in dividend | - | 10%             |
| (f) Current Market price per share   | - | ₹ 44            |
| (g) Tax rate                         | - | 50%             |

You are required :

- Determine the pattern of raising additional finance.
- To determine the post-tax average cost of additional debt.
- To determine the cost of retained earnings and equity.
- Compute the overall weighted average after tax cost of additional finance.



11. The following information is available in respect of a firm :

Capitalisation rate = 10%

Earnings per share = ₹ 50

Assumed rate of return on Investment :

(a) 12%                      (b) 8%                      (c) 10%

Show the effect of dividend policy on market price of shares applying Walter's formula when dividend payout ratio is :

(a) 20%                      (b) 40%                      (c) 80%

### SECTION - C

#### Compulsory question.

1x15=15

12. ABC Ltd., is considering investing in a project that costs ₹ 10,00,000. The estimated salvage value is zero; tax rate is 35 percent. The company uses straight line depreciation for tax purposes and the proposed project has cash Flows Before Tax (CFBT) as follows :

Year	1	2	3	4	5
CFBT (₹)	2,00,000	3,00,000	4,50,000	4,50,000	6,50,000

Determine the following :

- Pay back period
- Average rate of return
- NPV at 14% required rate of return
- IRR, and
- PI at 14% required rate of return

Suggest the company whether it should accept this or not with necessary working notes assuming standard pay back period of 3 years and minimum rate of return of 15%.

**Q.P. Code : 61315**

**Second Semester (DAY) M.B.A. Degree Examination, July 2019**

*(CBCS – 2014 Scheme)*

**Management**

**Paper 2.5 – FINANCIAL MANAGEMENT**

*Time : 3 Hours]*

*[Max. Marks : 70*

*Instruction : Answer All the Sections.*

**SECTION – A**

Answer any **FIVE** of the following. Each question carries **5** marks : **(5 × 5 = 25)**

1. Explain the “Emerging role of finance manager in India”.
2. Discuss the importance of venture capital to developing countries.
3. “Depreciation is an important source of working capital”. Do you agree? Defend your answer.
4. The following information relates to XYZ Ltd. :

	Rs.
Paid-up equity capital	20,00,000
Earnings of the company	2,00,000
Dividend paid	1,60,000
Price-earning ratio	125
Number of shares outstanding	20,000

You are required to find out whether the company’s dividend pay out ratio is optimal, using Walter’s Model.

5. The following data are available for X Ltd. :

Selling Price per unit = ₹ 120

Variable cost per unit = ₹ 70

Fixed cost = ₹ 2,00,000

- (a) What is the operating leverage when X Ltd. produces and sells 6,000 units?
- (b) What is the percentage change that will occur in the EBIT of X Ltd. if output increases by 5%?

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6. Vishnu Steels Ltd. has issued 30,000 irredeemable 14% Debentures of Rs. 150 each. The cost of floatation of Debentures is 5% of the total issued amount. The company's taxation rate is 40%. Calculate the cost of debt.
7. A firm has two alternative plans for raising additional funds of ₹ 10,00,000 :
- (a) Issue of 10,000 debentures of ₹ 100 each bearing 10% interest per annum.
- (b) Issue of 4,000 debentures of ₹ 100 each bearing 10% interest per annum and balance by the issue of 12% preference shares.

You are required to calculate the Financial Break Even Point for each plan assuming a tax rate of 50%.

### SECTION – B

Answer any **THREE** of the following. Each question carries **10** marks :

(3 × 10 = 30)

8. "Wealth Maximisation of the organisation leads to Economic growth of the country". Discuss.
9. A company proposes to install a machine involving a capital cost of ₹ 1,80,000. The life of the machine is 5 years and its salvage value at the end of the life is nil. The machine will produce the net operating income after depreciation of ₹ 34,000 per annum. The company's tax rate is 45%.

The net present value factors for 5 years are as under :

Discounting rate :	14	15	16	17	18
Cumulative factor :	3.43	3.35	3.27	3.20	3.13

You are required to calculate the internal rate of return of the proposal.

10. A company has the following capital structure :

		(Rs. lakhs)
Equity Capital	1,00,000 shares of Rs. 10 each	10
Reserves and surplus (retained earnings)		8
12% debentures	5,000 numbers of Rs. 100 each	5
		23

- (a) If the company is paying dividend at 27%, calculate the cost of equity and weighted average cost of capital, based on book values.
- (b) If the market value of equity shares is Rs. 15 each and if the debentures are quoted at Rs. 95 each, what is the weighted average cost of capital, based on market values?

Note : Tax rate in both cases is 50%.

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11. Compute the market value of the firm value of shares and the average cost of capital :

	₹
Net operating income	2,00,000
Total investment	10,00,000

Equity capitalisation rate :

- (a) If the firm uses no debt 10%
- (b) If the firm uses ₹ 4,00,000 debentures
- (c) If the firm uses ₹ 6,00,000 debentures

Assume that ₹ 4,00,000 debentures can be raised at 5% interest, whereas ₹ 6,00,000 debentures can be raised at 6% interest.

SECTION – C

12. Case Study (**Compulsory**) : **(1 × 15 = 15)**

The Board of Directors of Nanak Engineering Company Private Ltd. requests you to prepare a statement showing the Working Capital Requirements for a level of activity of 1,56,000 units of production.

The following information is available for your calculations :

	Per unit
	₹
(a) Raw materials	90
Direct labour	40
Overheads	75
	<hr/>
	205
Profit	60
	<hr/>
Selling price per unit	265

- (b) (i) Raw materials are in stock, on average one month.
- (ii) Materials are in process, on average 2 weeks.
- (iii) Finished goods are in stock, on average one month.
- (iv) Credit allowed by suppliers, one month.
- (v) Time lag in payment from debtors, 2 months.
- (vi) Lag in payment of wages, 1½ weeks.
- (vii) Lag in payment of overheads is one month.

20% of the output is sold against cash. Cash in hand and at bank is expected to be ₹ 60,000. It is to be assumed that production is carried on evenly throughout the year, wages and overheads accrue similarly and a time period of 4 weeks is equivalent to a month.