C 82133 (Pages : 4) Name..............................

Reg. No..............................

# SECOND SEMESTER M.B.A. DEGREE EXAMINATION, JUNE 2020

(CUCSS)

MBA

BUS 2C 11—FINANCIAL MANAGEMENT

(2016 Admission onwards)

Time : Three Hours Maximum : 36 Weightage

## Part A

*Answer the following.*
*Each question carries 1 weightage.*

1. What are the objectives of financial management ?
2. State the significance of capital budgeting.
3. At the end of six years, how much is an initial Rs. 5,000 deposit followed by five year-end, annual Rs. 100 payments worth, assuming a compound annual interest rate of (i) 10 percent ? ; (ii) 5 percent ?
4. How does market value of share differ from its book value ?
5. What are the various sources of working capital ?
6. List the factors influencing dividend policy of firm.

($6 \times 1 = 6$ weightage)

## Part B

*Answer any* **four** *questions.*
*Each question carries 3 weightage.*

7. Explain briefly the reasons for conflicting ranking by NPV and IRR in mutually exclusive projects.
8. Equipment A has a cost of Rs. 75,000 and net cash flow of Rs. 20,000 per year, for six years. A substitute equipment B would cost Rs. 50,000 and generate net cash flow of Rs. 14,000 per year for six years. The required rate of return of both equipments is 11 per cent. Calculate the IRR and NPV for the equipments. Which equipment should be accepted and why ?

Turn over

9. Silicon Company currently pays a dividend of Rs. 1 per share and has a share price of Rs. 20.

   (a) If this dividend was expected to grow at a 12 percent rate forever, what is the firm's expected, or required, return on equity using a dividend discount model approach ?

   (b) Instead of the situation in Part (a), suppose that the dividend was expected to grow at a 20 percent rate for five years and at 10 percent per year thereafter. Now what is the firm's expected, or required, return on equity ?

10. Mica Ltd. spends Rs. 2,20,000 per annum on its collection department. The company has Rs. 12 million in credit sales, its average collection period is 2.5 months, and the percentage of bad-debt losses is 4 percent. The company believes that, if it were to double its collection personnel, it could bring down the average collection period to 2 months and bad-debt losses to 3 percent. The added cost is Rs. 1,80,000, bringing total collection expenditures to Rs. 4,00,000 annually. Is the increased effort worthwhile if the before-tax opportunity cost of funds is 20 percent ?

11. Emkay Company was recently formed to manufacture a new product. It has the following capital structure in market value terms :

| | | |
|---|---|---|
| Debentures | ... | Rs. 60,00,000 |
| Preferred stock | ... | Rs. 20,00,000 |
| Common stock (3,20,000 shares) | ... | Rs. 80,00,000 |
| | | Rs. 1,60,00,000 |

The company has a marginal tax rate of 40 percent and the required return on equity is about 17 percent. The Company's debt is currently yielding 13 percent, and its preferred stock is yielding 12 percent. Compute the firm's present weighted average cost of capital.

12. Outline the approaches available for computing cost of capital.

($4 \times 3 = 12$ weightage)

## Part C

*Answer any* **three** *questions.*
*Each question carries 4 weightage.*

13. Greaves Ltd. is considering the finalization of the capital structure. Accordingly, the firm expects the EBIT of Rs. 1,50,000 per annum on an investment Rs. 5,00,000,. The company has access to raise funds of varying amounts by issuing equity share capital, 12% preference share and 10% debenture or any combination thereof. Suppose, it analyzes the following four options to raise the required funds of Rs. 5,00,000.

   (a) By issuing equity share capital at par.

   (b) 50 % funds by equity share capital and 50 % funds by preference shares.

(c) 5 % funds by equity share capital, 25 % by preference shares and 25 % by issue of 10 % debentures.

(d) 25 % funds by equity share capital, 25 % as preference share and 50 % by the issue of 10 % debentures.

Assuming that Assuming Ltd. belongs to 35% tax bracket, Compute the EPS under the above four options.

14. Signiti Corporation has earnings before interest and taxes of Rs. 3 million and a 40 percent tax rate. It is able to borrow at an interest rate of 14 percent, whereas its equity capitalization rate in the absence of borrowing is 18 percent. The earnings of the company are not expected to grow, and all earnings are paid out to shareholders in the form of dividends. In the presence of corporate but no personal taxes, what is the value of the company in an M & M world with no financial leverage ? With Rs. 4 million in debt ? With Rs. 7 million in debt ?

15. Explain briefly the capital budgeting techniques.

16. Amber Company is considering a new product line to supplement its range line. It is anticipated that the new product line will involve cash investment of Rs. 7,00,000 at time 0 and Rs. 10,00,000 in year 1. After-tax cash inflows of Rs. 2,50,000 are expected in year 2, Rs. 3,00,000 in year 3, Rs. 3,50,000 in year 4, and Rs. 4,00,000 each year thereafter through year 10. Though the product line might be viable after year 10, the company prefers to be conservative and end all calculations at that time.

(a) If the required rate of return is 15 percent, what is the net present value of the project ? Is it acceptable ?

(b) What is its internal rate of return ?

(c) What would be the case if the required rate of return was 10 percent ?

(d) What is the project's payback period ?

17. Should companies in the same industry have approximately the same required rates of return on investment projects ? Why or why not ?

($3 \times 4 = 12$ weightage)

## Part D

*Compulsory question.*
*6 weightage.*

18. The pro forma cost sheet of Alpha limited provides following data :

| Costs (per unit) | | (In Rs.) |
|---|---|---|
| Raw materials | ... | 52.0 |
| Direct labour | ... | 19.5 |
| Overheads | ... | 39.0 |
| Total cost (per unit) | ... | 110.5 |
| Profit | ... | 19.5 |
| Selling price | ... | 130.0 |

The following is the additional information available :

(a) Average raw material in stock: one month; average materials in process: half a month.

(b) Credit allowed by suppliers: one month:

(c) Credit allowed to debtors: two months.

(d) Time lag in payment of wages: one and a half weeks.

(e) Overheads: one month.

(f) One-fourth of sales are on cash basis.

(g) Cash balance is expected to Rs. 1,20,000.

You are required to prepare a statement showing the working capital needed to finance a level of activity of 70,000 units of output. You may assume that production is carried on evenly throughout the year and wages and overheads accrue similarly.

(1 × 6 = 6 weightage)