

Seat No.: _____

Enrolment No. _____

GUJARAT TECHNOLOGICAL UNIVERSITY

MBA – SEMESTER 02– • EXAMINATION – WINTER 2015

Subject Code: 2820003

Date: 19/12/2015

Subject Name: FINANCIAL MANAGEMENT (FM)

Time: 02.30 PM TO 05.30 PM

Total Marks: 70

Instructions:

1. Attempt all questions.
2. Make suitable assumptions wherever necessary.
3. Figures to the right indicate full marks.
4. Use of Compound value and Discount value Tables is permitted.

Q.1 (a) From the four alternative answers given against each of the following cases, indicate the correct answer (Just state a,b,c or d) **06**

1. Which of the following evaluation criteria does not consider time value of money ?
 - (a) NPV
 - (b) ARR
 - (c) PI
 - (d) IRR
2. Which of the following actions would not result in increase or decrease in total requirement of working capital.
 - (a) Decrease in credit period allowed to customers.
 - (b) Decision to pay immediate cash to suppliers to enjoy cash discount.
 - (c) Changing the method of depreciation.
 - (d) Implementing a scheme which cuts down the production period.
3. The Debt Equity ratio of a company.
 - (a) Affects its financial leverage
 - (b) Affects the dividend decision of the company.
 - (c) Does not affect the earnings per share
 - (d) Both (a) & (b)
4. According to Gordon's model the optimal dividend payout ratio for a firm whose cost of capital is 15% and return on investment is 12% is
 - (a) 0%
 - (b) 50%
 - (c) 100%
 - (d) None of the above.
5. Which of the following is not an assumption to EOQ model ?
 - (a) Cost per order is proportional to the size of the order.
 - (b) The demand is even throughout the year.
 - (c) The usage of one year can be anticipated.
 - (d) Cost of carrying is a fixed proportion of the average value of inventory.
6. The method of raising equity capital from existing members by offering securities on pro-rata basis is referred to as :
 - (a) Public issue
 - (b) Private placement
 - (c) Bonus issue
 - (d) Rights issue

Q.1 (b) Answer the following: **04**

- 1 Define the term net working capital
- 2 What is meant by share split ?
- 3 What is financial leverage ?

4 What do you mean by payback period

Q.1 (c) A house owner has rented out his house for 3 years at a rent of Rs. 40,000/- with an agreement that rent will increase by 5% every year. If the owners required rate of return is 8%, what is the present value of expected (annuity) rent ? **04**

Q.2 (a) Discuss briefly the various sources of long term finance of Indian Companies **07**

Q.2 (b) An investor has invested in a company which is growing at an above average rate, translated to an annual increase in dividend of 20% for 10 years. Thereafter, dividend growth returns to an average rate of 7%. The capitalization rate of the company is 10% and current dividend per share is Re.1.00. Determine the present value of the share.

OR

Q.2 (b) The following is the balance sheet of W Ltd. as on 31/03/2011. **07**

Liabilities	Amt.	Assets	Amt.
Equity Share Capital (Rs. 10 F.V/Share)	1,80,000	Fixed Assets	4,50,000
10% Debentures	2,40,000	Current Assets	1,50,000
Retained Earnings	60,000		
Current Liabilities	1,20,000		
	6,00,000		6,00,000

The Company's total asset turnover ratio is 2.5 times. The fixed operating cost are Rs. 2,00,000. Variable operating cost ratio is 40%. Income Tax rate is 50%.

You are required to

- (1) Calculate leverages.
- (2) Determine the likely level of EBIT if EPS is Rs. 6.

Q.3 (a) Critically examine the assumptions underlying the irrelevance hypothesis of MM regarding dividend distribution. **07**

Q.3 (b) A company has an average cost of capital of 18% and hence its required rate of return is 18%. The company has an investment opportunity in a project, the details of which are as under : **07**

Year	Cash Flow (Rs.)
0	-5,00,000
1	50,000
2	1,50,000
3	3,00,000
4	2,00,000
5	1,00,000

Using the IRR method, you are required to help the company decide whether it should invest in the project or not ?

OR

Q.3 (a) What is a bonus issue ? Give the advantages and disadvantages of a bonus issue. **07**

Q.3 (b) XYZ company buys and uses a component for production at Rs. 100 per unit. The annual requirement is 2000 units. Carrying cost of inventory is 10% p.a. and ordering cost is Rs. 400 per order. The purchase manager argues that the ordering cost is high, it is advantageous to place a single order for the entire annual requirement. He also says that if the order is 2000 units at a time, there is a 3% discount from the supplier. Evaluate this proposal and give your recommendation. **07**

Q.4 (a) "Traditional approach is neutral to NOI and NI approaches". Discuss **07**

- Q.4 (b)** There are two options available to an investor. Scheme A promises to pay Rs. 1,50,000 at the end of 10 years if an investment of Rs. 10,000 is made annually. Scheme B promises to pay Rs. 1,50,000 at the end of 8 years if Rs. 15,000 is invested annually. Suggest which of the two schemes is better for the investor. **07**

OR

- Q.4 (a)** Explain the concept of leasing giving its advantages. **07**

- Q.4 (b)** A company is providing 25% returns to its shareholders. The current market price of its share is Rs.80 with 1.25 crore shares outstanding. The firm is expected to earn Rs. 4 crore in the year, while its investment requirement of the period is Rs. 6 crores. It has been distributing dividend at 75% of the earnings. In view of its expansion requirements, it is exploring the proposition of skipping the dividend altogether for the year while mobilizing the remaining funds by issue of fresh shares.

Examine the value of the firm when the firm (a) continued with the current dividend policy of 75% payout and (b) decides to skip the dividend for the year.

- Q.5** Super Ltd. has appointed you as a consultant and you are required to prepare monthly cash forecast for the company for the months of January to June and indicate the cash deficit / Surplus for the months. **14**

The past data reveals that the firm's cash sales have been 30% on an average. 50% of the sales are realized in the next month, while 19% are realized in the second month. Sales for the previous two months (Nov & Dec) were Rs. 175 lacs and Rs. 176.5 lacs respectively. The sales department has submitted the following forecasts for the sales in the coming months :

Month →	Jan	Feb	Mar	Apr	May	June
Sales (in lac) →	178	178.5	177	195	215	256

The projected expenditure details given by the production department are as under :

Direct Material : 42% of sales.

Direct Labour : 25% of sales for Jan, Feb & Mar but expected to rise to 26.5% for the period thereafter. As per the past trends, the direct labour is generally paid for in the month it is incurred. The suppliers grant the terms of sales of net 60 days, which are fully utilized. Monthly fixed expenses like rent are estimated to be Rs. 45 lacs. Capital expenditure worth Rs. 215 lacs is due in June. The company has a policy of maintaining a cash balance at a level of 5% of monthly sales. Surplus cash, if any is invested in marketable securities and deficit is to be borrowed.

OR

- Q.5** R. Ltd. is considering a project to produce rubber rollers with an initial investment of Rs. 400 lacs. The project would last for 8 years after which 10% of the initial investment may be realized as salvage value. The company has a policy of charging depreciation on SLM basis. **14**

After taking costing of the product a profit before tax of Rs. 52 lacs is expected for the next 8 years. Though the normal rate of tax is 40%, the company would pay only 28% taxes due to tax incentives available. Assume that no tax is payable on the salvage value realized.

If the cost of capital of the company is 12% what is the NPV of the project and what shall be the decision with respect to its acceptance ?
