

Seat No.: _____

Enrolment No. _____

GUJARAT TECHNOLOGICAL UNIVERSITY

MBA – SEMESTER (2) – EXAMINATION – WINTER 2016

Subject Code: 2820003

Date: 22/10/2016

Subject Name: Financial Management (FM)

Time: 10.30 am to 01.30 pm

Total Marks: 70

Instructions:

1. Attempt all questions.
2. Make suitable assumptions wherever necessary.
3. Figures to the right indicate full marks.

Q.1(a)	Answer the following MCQ type of questions:		06
	Which of the following models on dividend policy stresses on the investor's preference for the current dividends?		
1.	A. Traditional Model	B. Walter Model	
	C. Gordon Model	D. MM Model	
2.	Investment decision is also known as.....		
	A. Cost of Capital	B. Capital Structure	
	C. Project Planning	D. Leverage	
3.	Leverage + Cost of Capital + Value of Firm =		
	A. NI	B. Pie Model	
	C. NOI	D. EBIT	
4.	Which of the following is not a measure for monitoring receivables?		
	A. Collection Matrix	B. ABC Analysis	
	C. Days Sales Outstanding	D. Ageing Schedule	
5.	If NPV for a project is positive than.....		
	A. IRR > cost of capital	B. IRR = cost of capital	
	C. IRR < cost of capital	D. IRR = 0	
6.	The composition of long term sources of funds is known as.....		
	A. Cost of Capital	B. Capital Structure	
	C. Leverage	D. Dividend Policy	
Q.1	(b)	Explain the following terms: (i) Venture Capital. (ii) Hire Purchase.	04
Q.1	(c)	You plan to go abroad for higher studies after working for the next five years and understand that an amount of Rs. 20, 00, 000 will be needed for this purpose at that time. You have decided to accumulate this amount by investing a fixed amount at the end of each year in a safe scheme offering a rate of interest at 10 %. What amount should you invest every year to achieve the target amount?	04
Q.2	(a)	Critically examines the assumptions underlying the irrelevance hypothesis of Modigliani – Miller (MM) approach regarding cost of capital.	07
	(b)	A machine costs Rs. 5, 00,000 and its effective life is estimated to be 6 years. A sinking fund is created for replacing the machine at the end of the effective life time when its scrap will realize a sum of Rs. 20,000 only. Calculate the amount which should be provided every year for the sinking if it accumulates at 8 % per annum compounded annually.	07

		OR																										
	(b)	Explain the Net Income Approach and Net Operating Income Approach of capital structure in brief.		07																								
Q.3	(a)	Define 'Leasing' and explain in brief about 'Operating Leasing' and 'Financial Leasing'.		07																								
	(b)	Expected EBIT of the firm is Rs. 2, 00,000. The equity capitalization rate is 10 %. Find out the value of the firm and overall cost of capital on the basis of NOI approach if degree of leverage is: (i) Rs. 2, 00,000; (ii) Rs. 5, 00,000; and (iii)Rs. 7, 00,000. The Debenture interest rate is 6 % per annum.		07																								
		OR																										
Q.3	(a)	What do you mean by Working Capital Management? Explain the factors which determine the amount of working capital in a business.		07																								
	(b)	Beta Limited and Theta Limited operate in the same line of business of manufacture of rubber components. However their cost structures and financing structures differ substantially. An analysis of their financial performance has revealed the following data: <table border="1"><thead><tr><th>Particulars</th><th>Beta Ltd. (in Rs.)</th><th>Theta Ltd. (in Rs.)</th></tr></thead><tbody><tr><td>Sales</td><td>5,00,00,000</td><td>10,00,00,000</td></tr><tr><td>Less: Variable Cost</td><td>2,00,00,000</td><td>3,00,00,000</td></tr><tr><td>Contribution</td><td>3,00,00,000</td><td>7,00,00,000</td></tr><tr><td>Less: Fixed Cost</td><td>1,50,00,000</td><td>4,00,00,000</td></tr><tr><td>Operating Profit, EBIT</td><td>1,50,00,000</td><td>3,00,00,000</td></tr><tr><td>Less: Interest</td><td>50,00,000</td><td>1,00,00,000</td></tr><tr><td>Earnings Before Tax (EBT)</td><td>1,00,00,000</td><td>2,00,00,000</td></tr></tbody></table> Find out the following: a) Degree of Operating Leverage; b) Degree of Financial Leverage; and c) Degree of Combined Leverage. What is the interpretation of DOL, DFL and DCL?	Particulars	Beta Ltd. (in Rs.)	Theta Ltd. (in Rs.)	Sales	5,00,00,000	10,00,00,000	Less: Variable Cost	2,00,00,000	3,00,00,000	Contribution	3,00,00,000	7,00,00,000	Less: Fixed Cost	1,50,00,000	4,00,00,000	Operating Profit, EBIT	1,50,00,000	3,00,00,000	Less: Interest	50,00,000	1,00,00,000	Earnings Before Tax (EBT)	1,00,00,000	2,00,00,000		07
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Earnings Before Tax (EBT)	1,00,00,000	2,00,00,000																										
Q.4	(a)	What do you understand by Economic Order Quantity (EOQ)? On the basis of following information, you are required to calculate: (i) Economic Order Quantity; and (ii) Number of Orders per Annum. The annual demand for the product is 6,400 units. The unit cost is Rs. 6 and inventory carrying cost per unit per annum is 25 % of the average inventory cost. If the cost of procurement is Rs. 75.		07																								
	(b)	From the following capital structure of Anand Limited, calculate Weighted Average Cost of Capital, using (i) Book value weights; and (ii) Market value weights. <table border="1"><thead><tr><th>Particulars</th><th>Book value (in Rs.)</th><th>Market value (in Rs.)</th></tr></thead><tbody><tr><td>Equity Shares of Rs. 10 each</td><td>90,000</td><td>1,80,000</td></tr><tr><td>Retained Earnings</td><td>30,000</td><td>Nil</td></tr></tbody></table>	Particulars	Book value (in Rs.)	Market value (in Rs.)	Equity Shares of Rs. 10 each	90,000	1,80,000	Retained Earnings	30,000	Nil		07															
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Preference Share Capital	20,000	20,000													
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		The after-tax cost of capital for specific sources is as follows: Equity Share Capital: 14 %, Retained Earnings: 13 %, Preference Share Capital: 10 % and Debentures: 5 %.													
		OR													
Q.4	(a)	Under what circumstances do the Net Present Value and the Internal Rate of Return (IRR) methods differ? Which method would you prefer and why?	07												
	(b)	The project investment is Rs. 5, 00,000. Cash inflows of a project is as given below: <table><tr><td>Year = N</td><td>Cash Inflows</td></tr><tr><td>1</td><td>1,00,000</td></tr><tr><td>2</td><td>2,00,000</td></tr><tr><td>3</td><td>1,50,000</td></tr><tr><td>4</td><td>2,00,000</td></tr><tr><td>Total</td><td>6,50,000</td></tr></table> You are required to evaluate Net Present Value Method whether the project is feasible. Ascertain discounted cash flow assuming rate of interest is 15 % p.a.	Year = N	Cash Inflows	1	1,00,000	2	2,00,000	3	1,50,000	4	2,00,000	Total	6,50,000	07
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1	1,00,000														
2	2,00,000														
3	1,50,000														
4	2,00,000														
Total	6,50,000														
Q.5	(a)	You are appointed as Financial Manager of a company, the company provides the following data: <table><tr><td>Raw Materials</td><td>Rs. 52 per unit</td></tr><tr><td>Direct Labour</td><td>Rs. 19.5 per unit</td></tr><tr><td>Overheads</td><td>Rs. 39 per unit</td></tr><tr><td>Selling Price</td><td>Rs. 130 per unit</td></tr></table> The following additional information are available: Average raw material in stock: 1 Month, Average Material in process: 0.5 Month, Average Finished Goods: 1 Month, Credit allowed by suppliers: 1 Month, Credit allowed by debtors: 2 Months, Time lag in payment of wages: 1.5 weeks, Overheads: 1 Month. 25 % of sales are on cash basis. Cash balance is expected to be 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 carried on evenly, throughout the year and wages and overhead accrue similarly.	Raw Materials	Rs. 52 per unit	Direct Labour	Rs. 19.5 per unit	Overheads	Rs. 39 per unit	Selling Price	Rs. 130 per unit	07				
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	(b)	The following information is available for Avanti Corporation: Earning Per Share Rs. 4 Rate of Return on Investments 18 % Rate of Return required by Shareholders 15 % What will be the price per share as per the Walter Model if the Dividend Pay Out Ratio is 40 %, 50 % and 60 %?	07												
		OR													
Q.5	(a)	Following is the data of M/S Ambika Industries Ltd.: 10 % Debentures Rs. 50, 00,000 Equity Share Capital Rs. 10, 00,000 Retained Earnings Rs. 5, 00,000 The corporate tax rate is 40 %.	07												

		Market Price of Share is Rs. 20. The company is expected to declare dividend of Rs. 4 per share in the next year. You are required to calculate Weighted Average Cost of Capital.	
	(b)	What is the present value of an income stream which provides Rs. 2,500 at the end of year one, Rs. 3,000 at the end of year two and Rs. 5,000 during each of the years three through 10, if the discount rate is 12 %?	07
