

END TERM EXAMINATION

SIXTH SEMESTER [B.COM] MAY-JUNE 2017

Paper Code: BCOM-302

Subject: Financial Management

Time: 3 Hours

Maximum Marks: 75

Note: Attempt any five questions. All questions carry equal marks.
Calculator is allowed.

- Q1 "The prominent areas of financial decision-making today are considerably different from what they were few decades ago." Discuss.
- Q2 The balance sheets of X Ltd. as on 31-12-2010 and 31-12-2011 were as under:

	31-12-2010	31-12-2011
Liabilities:		
Share Capital	5,00,000	6,50,000
Securities Premium	50,000	—
Profit & Loss A/c	—	25,000
8% Debenture	2,00,000	1,10,000
Bank Overdraft	80,000	1,00,000
Creditors	80,000	75,000
Proposed Dividend	10,000	15,000
Provision for Tax	20,000	25,000
Total	<u>9,40,000</u>	<u>10,00,000</u>
Assets:		
Goodwill	1,00,000	75,000
Investment	1,50,000	2,00,000
Fixed Assets	5,50,000	5,50,000
Debtors	60,000	90,000
Stock	60,000	80,000
Cash	12,000	5,000
Prepaid Expenses	8,000	—
Total	<u>9,40,000</u>	<u>10,00,000</u>

Additional Information:

- (a) Net profit for the year 2011 before tax and dividend was Rs. 63,000.
- (b) Provision for tax made during the year 2011 was Rs. 23,000.
- (c) Depreciation charged for 2011 was Rs. 80,000.
- (d) Bonus shares of Rs. 50,000 were issued out of securities premium.
- (e) Debentures amounting to Rs. 90,000 were redeemed on 1st April, 2011. Interest on debentures was paid regularly in cash.
- Prepare Cash Flow statement.

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Q3 Sonu Ltd. has the following capital structure:

Equity shares (2,00,000)	Rs. 40,00,000
10% Preference Shares	10,00,000
9% Debenture	30,00,000
	<u>80,00,000</u>

The share of the company sells for Rs. 20. It is expected that the company will pay next year a dividend of Rs. 2 per share which will grow at 7% for ever. Assume a 35% tax rate.

- (a) Compute the weighted average cost of capital based on the existing capital structure.
- (b) Compute the new weighted average cost of capital if the company raises an additional Rs. 30,00,000 debt by issuing 10% debentures. This would increase the expected dividend to Rs. 3 and leave the growth rate unchanged, but the price of share will fall to Rs. 15 per share.

Q4 (a) Two firms 'U' and 'V' are identical in every respect, except that 'U' is unlevered and 'V' is levered. 'U' has Rs. 20 lakh of 8% debt outstanding. The net operating income of both firms is identical, i.e. Rs. 6 Lakh. The corporate tax rate is 35% and equity capitalisation rate for 'U' is 10%. Find out the value of each firm according to the MM approach.

(c) What do you understand by Leverage? Discuss the benefits and risks of financial leverage with the help of an example.

Q5 A firm whose cost of capital is 10%, is considering two mutually exclusive projects X and Y, the details of which are:

	Project 'X' Rs.	Project 'Y' Rs.
Investment	43,500	36,000
Cash inflow year 1	10,000	15,000
Cash inflow year 2	12,000	13,000
Cash inflow year 3	13,000	12,000
Cash inflow year 4	14,000	10,000
Cash inflow year 5	16,000	10,000

- Compute for both the projects:
- (a) The Net Present Value at 10% discount rate.
- (b) Profitability index at 10% discount rate.
- (c) Internal rate of return

Following tables may be used to solve the question:

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$$N \times \frac{1}{(1+r)^n} = \frac{600 \times 10}{35}$$

Discount Factor Table

Year	10%	15%	20%	25%	30%
1	.909	.870	.833	.800	.769
2	.826	.756	.694	.640	.592
3	.751	.658	.579	.512	.455
4	.683	.572	.482	.410	.350
5	.621	.497	.402	.328	.269

Annuity Table

Year	10%	15%	20%	25%	30%
5	3.791	3.352	2.991	2.689	2.436

Q6 Write short notes on the following (attempt any three):

- (a) Risk adjusted discounting rate
- (b) Decision Tree
- (c) Sensitivity Analysis
- (d) Replacement decisions

Q7 (a) MM Foam Company currently has 50,000 outstanding shares selling at Rs. 100 each. The firm expected to have a net earning of Rs. 4,00,000 and contemplating dividend of Rs. 5 per share at the end of the current financial year. There is a proposal for making new investments of Rs. 12,00,000. Assuming 10% cost of capital show that under the MM hypothesis, the payment of dividend does not affect the value of the firm.

(b) What do you understand by dividend? Discuss the various factors influencing the corporate dividend policy.

Q8 Calculate the working capital requirement from the following particulars:

	Per annum (Rs.)
Raw Material Cost	6,24,000
Wages	3,12,000
Overheads (including depreciation of Rs. 20,000)	1,44,800
Total:	10,80,800
Add: Profit	1,19,200
Sales	12,00,000

Additional Information:

- (a) Inventory norms:
 - Raw Material 6 weeks
 - Work in progress 2 weeks
 - Finished goods 4 weeks
- (b) 60% of the sales is for cash, for the remaining one month credit is allowed.
- (c) Creditors allow 1.5 months credit on 1/3rd of the purchase
- (d) Lag in payment of overhead is half month.
- (e) Wages are paid on the first day of the next month.
- (f) Cash is to be held to the extent of 50% of current liabilities.

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