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(July)

COMMERCE

(Honours)

(Financial Management)

(BC–402)

Marks : 75

Time : 3 hours

The figures in the margin indicate full marks for the questions

1. *(a)* What is financial management? Explain the scope of financial management. 2+6=8

   (b) "Financial management is indispensable in any organization." Elucidate. 7

   Or

   (a) Explain compounding and discounting concepts of time value of money. 4

   (b) Miss Phieladshisha receives ₹ 50,000 per year for 3 years and desires to invest the amount at the end of each year @ 7% compound interest. How much will she receive at the end of 3 years? 3

(c) Miss Sabu is thinking of purchasing a flat in Shillong for ₹ 36,00,000. She applies for a loan of this amount from SBI @ 12% p.a. to be repaid over 15 years. Compute the annual instalments for repayment starting from the end of 1st year. 4

(d) Exactly 6 years ago, Mr. Sujay borrowed ₹ 3,00,000 at 6% p.a. on a 25 years mortgage with monthly payment of ₹ 1,933. What is the balance on Sujay's mortgage today? 4

2. *(a)* Establish the relationship between NPV and IRR. When do they differ? 3+3=6

   (b) A project costing ₹ 1,00,00,000 has an estimated effective life of 10 years at the end of which its scrap value is likely to be ₹ 10,00,000. The firm's cut-off rate is 12%. The project is expected to yield an annual profit (after tax) of ₹ 10,00,000. Depreciation being charged on straight-line basis.

   At 12% p.a., the present value of ₹ 1 received annually for 10 years is ₹ 5·650 and the present value of ₹ 1 received at the end of 10th year is ₹ 0·322.

   Ascertain the NPV of the project and state whether we should accept the project. 8+1=9

(3)

Or

(a) Why should a project having positive net present value be accepted? 3

(b) Kanu Ltd. wishes to invest in either of the two investments at the beginning of the next year. The required rate of return is 10% p.a. Evaluate the investment proposals and advise under—

(i) discounted payback period method;

(ii) NPV method;

(iii) profitability index method : 3+6+3=12

	Proposal—A	Proposal—B
Cost of investment (in ₹)	1,50,000	2,50,000
Effective life (in years)	4	5
Scrap value	Nil	Nil
Estimated earnings after taxes :		
	₹	₹
Year 1	15,000	Nil
2	30,000	54,000
3	45,000	54,000
4	35,000	54,000
5	Nil	54,000
Additional working capital required (in ₹)	20,000	20,000
Method of depreciation	Straight line	Straight line

(4)

3. (a) Why is 'cost of capital' important? 3

(b) Haru Ltd. issues ₹ 10,000, 10% debentures to be redeemed after 10 years. The company is in the 25% tax bracket. Floatation cost is 2% on issue price. Compute the cost of debentures in each of the following cases : 3+3=6

(i) Issued at par and redeemable at par

(ii) Issued at a premium of 10% and redeemable at par

(c) Dilip Co. issues 10000 equity shares of ₹ 100 each at a premium of 10%. The company has been paying 20% dividend to equity shareholders for the past five years and expects to maintain the same in the future also. Compute the cost of equity capital. Will it make any difference if the market price of equity share is ₹ 150? 3+3=6

(5)

Or

(a) What is optimum capital structure?   3

(b) The capital structure and specific cost of capital (after tax) of a company are given below :

Sources	Book value (₹)	After tax cost (%)
Equity share capital (shares of ₹ 10 each)	2,00,000	18
Retained earnings	1,00,000	18
Long-term debt	2,00,000	6
	5,00,000	

The present market value of equity is ₹ 90 per share. Corporate tax rate is 25%.

Calculate weighted average cost of capital using—

  (i) book values as weights;

  (ii) market values as weights.   6+6=12

4. (a) Critically evaluate the assumptions of Modigliani and Miller's model of dividend policies.   6

(6)

(b) Sonakshi Ltd. has an investment of ₹ 5,00,000 in assets and 50000 shares outstanding at ₹ 10 each. It earns a rate of 15% on its investment and has a policy of retaining 50% of the earnings. If the appropriate discount rate is 10%, determine the price of company's share using Gordon's model. What will be the share price if the company has a payout of 80% or retention ratio of 80%?

    3+3+3=9

Or

(a) State the factors which influence the dividend policy of a firm.   5

(b) The following figures are collected from the annual report of Sudina Ltd. :

Net profit—₹ 30 lakhs

Outstanding 12% preference shares—₹ 100 lakhs

Number of equity shares—3 lakhs

Return on investment—20%

Cost of capital—16%

What should be the appropriate dividend payout ratio so as to keep the share price at ₹ 42 by using Walter's model?   10

5. *(a)* What is fixed working capital? 3

(b) From the following information, calculate reorder quantity : 12

Average usage—100 units per week

Minimum reorder period—4 weeks

Maximum usage—150 units per week

Average reorder period—5 weeks

Average stock level—750 units

Or

The Sumedha Ltd. proposes to raise its turnover from ₹ 6,00,000 to ₹ 8,40,000 next year and to ₹ 9,60,000 in the succeeding year. It is expected that the purchases will go up from ₹ 1,80,000 to ₹ 2,40,000 and then to ₹ 2,70,000 in the next two years. A steady profit of 10% on turnover is estimated over the years; and the materials, labour and factory overheads are expected uniformly to be 30%, 20% and 30% respectively of the total cost of goods sold. At the end of each year, the raw materials stock would amount to two months' consumption, work-in-progress to one month's factory cost and finished goods to half a month's total cost. There is a two months' credit period allowed to customers and received from suppliers. The company has a policy of

carrying cash equivalent to one month's requirement for payment of labour and other overhead cost. Ignoring prepayments and accrued charges as they normally offset each other, work out an estimate of working capital requirement for all the three years separately. State assumptions, if any. 15

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