2022

(May/June)

COMMERCE

(Honours)

(Financial Management)

(BC–402)

Marks : 75

Time : 3 hours

The figures in the margin indicate full marks for the questions

1. *(a)* "Investment, financing and dividend decisions are all inter-related." Comment. 12

   (b) Distinguish between Discounting and Compounding. 3

Or

   (a) John deposited ₹ 1,00,000 in a savings bank account today, at 5% simple interest for a period of 5 years. What is his accumulated interest? 3

(b) A borrower offers 16% rate of interest will quarterly compounding. Determine the effective rate of income. 3

(c) State with examples how poor financial management of a company affects its marketing functions. 9

2. (a) What is capital budgeting? State its need and importance. 2+3=5

(b) A company is evaluating a project that costs ₹ 2,00,000 and it requires as all additional net working capital of ₹ 1,00,000. It is expected to generate a net cash flow of ₹ 1,05,000 for 5 years. What is the NPV and IRR of the project assuming 50% tax rate and 10% cash of capital? 10

Or

A company is considering the following proposals. Assuming a required rate of return of 10% per annum, evaluate the investment proposals as per *(i)* PBP, *(ii)* ARR and *(iii)* PI : 15

	Project—A	*Project—B*
Cost of project	₹ 24,000	₹ 35,000
Life	4 years	5 years
Scrap value	₹ 2,000	₹ 4,000

Inflows after depreciation and tax :

Year	*1*	*2*	*3*	*4*	*5*
Project A	1000	2500	4000	3000	—
Project B	—	4200	4200	4200	4200

Each project will require an additional working capital of ₹ 2,000, which will be received back in full after expiry of the project life. Depreciation is provided under straight line method.

3. (a) What do you understand by cost of capital? 3

(b) The capital structure of *H* Ltd. as on 31st March, 2022 is as follows :

Equity share capital—₹ 100 lakhs
(10 lakhs shares of ₹ 10 each)

Reserves and surplus—₹ 20 lakhs

14% debentures of ₹ 100 each—
₹ 30 lakhs

For the year ended 31st March, 2022, the company paid equity dividend at 20% and dividends are expected to grow by 3% every year. The current market price per share is ₹ 75 and the tax rate applicable for the company is 25%.

Find out the WACC for *H* Ltd. 12

Or

(a) State the assumptions of Net Income (NI) approach and using imaginary figures, show how to determine the value of firm under Net Income (NI) approach. 2+6=8

(b) A company requires ₹ 5,00,000 for construction of a new plant. It has identified the following three finance options :

(i) Issue of 50000 shares @ ₹ 10 each

(ii) Issue of 25000 equity shares @ ₹ 10 each and 2500, 8% debentures of ₹ 100 each

(iii) Issue of 25000 equity shares @ ₹ 10 each and 2500, 10% preference shares of ₹ 100 each

Assuming EBIT after construction would be ₹ 1,00,000, which financing option would you recommend assuming tax rate of 35%? 7

4. *(a)* Explain the various factors which influence the dividend decision of a firm. 6

(b) The following information is available for Dipu Ltd. :

Earnings per share—₹ 4

Rate of return on investments—18%

Rate of return required by shareholders—15%

Using Walter's model, what will be the price per share, if the dividend payout rate is 30%, 50% and 60%? 9

Or

(a) If the firm's cost of capital is 11% and earnings per share is ₹ 15, calculate the price per share of Raphael Ltd. for return on investments are 12%, 11% and 10% for the following levels of dividend payout ratios : 10

(i) 10%

(ii) 30%

(iii) 50%

(b) Describe the 'birds-in-hand' argument of dividend. 5

5. *(a)* Briefly explain the importance of working capital. 5

(b) A proforma cost sheet of Ari Ltd., provides the following information. You are required to estimate the working capital needed to finance a level of activity of 52000 units of production :

	Amount (per unit)
Raw Materials	40
Direct Labour	15
Overheads (excluding depreciation)	30
Total Cost	85
Profit	30
Selling Price	115

Additional Information :

(i) Average raw materials in stock—1 month

(ii) Average materials-in-process (50% completion stage)—Half a month

(iii) Average finished goods in stock—1 month

(iv) Credit allowed by suppliers—1 month

(v) Credit allowed to customers—2 months

(vi) Time lag in payment of wages—1½ weeks

(vii) Time lag in payment of overhead expenses—1 month

(viii) Half of the sales is on cash basis—Cash balance is expected to be ₹ 12,500

You may assume that production is carried on evenly throughout the year, and wages and overhead expenses accrue similarly. 10

Or

(a) Briefly describe the credit policy variables. 5

(b) Ailad Ltd. uses quarterly 50000 units of raw materials. Cost of raw materials is ₹ 100 per unit, cost of placing an order is ₹ 120 and carrying cost is 9% per year. Calculate EOQ. 5

(c) A financial manager projects that the firm needs an estimated net cash flow of ₹ 5,00,000 for the next month. The cost of raising funds in the market is 18% and that of transaction involve a cost of ₹ 500 per transaction. The firm is planning to sell 8% marketable securities.

You are required to determine the optimal amount of securities to be converted into cash. 5

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