4/H–65 (xi) (Syllabus–2015)

2 0 1 8

(April)

BUSINESS ADMINISTRATION

(Honours)

(Financial Management)

(BBAH–402)

Marks : 75

Time : 3 hours

The figures in the margin indicate full marks for the questions

PART—A

(*Marks* : 15)

UNIT—I

1. Define financial management. 3

Or

Mr. *X* deposited ₹ 10,000 today in a financial institute at 6% compound interest for a period of 5 years. What will be the compound value after 5 years? 3

(*Turn Over*)

UNIT—II

2. State any three limitations of capital budgeting. 3

Or

Define risk with reference to capital budgeting. 3

UNIT—III

3. What is the importance of cost of capital? 3

Or

A firm is currently earning ₹ 1,00,000 and its share is selling at a market price of ₹ 90 per share. The firm has 10000 shares and no debt. Compute cost of equity. 3

UNIT—IV

4. Distinguish between operating and financial leverage. 3

Or

What is arbitrage process? 3

UNIT—V

5. What is working capital? 3

Or

What are the objectives of cash management? 3

PART—B

(*Marks* : 50)

6. *(a)* From the following information, calculate present value at 10% interest rate : 5

Year	:	0	1	2	3	4	5
Cash (₹)	:	2000	3000	4000	5000	4500	5500
PV factor at 10%	:	1	0·909	0·826	0·751	0·683	0·621

(b) How much should a person save annually to accumulate ₹ 1,00,000 for his daughter's marriage by the end of 10 years at an interest rate of 8% per annum? (FVIFA for 10 years = 14·487) 5

Or

(a) Briefly explain portfolio theory. 5

(b) An investor developed an efficient portfolio with four companies' stocks. The expected return on stocks are as follows :

1. Infosys—16%
2. Mahindra—20%
3. Maruti—17%
4. SBI—10%

The investor has decided to allocate the available amount equally on all companies' stock. Determine the expected return on portfolio. 5

7. 'WINGS' Ltd. is considering to purchase a machine in replacement of an old machine. Two models viz, BOLERO and SCORPIO are offered at a price of ₹ 22·50 lakhs and ₹ 30 lakhs respectively. The following particulars are given below :

Particulars		*BOLERO* (₹)	*SCORPIO* (₹)
Economic Life		5 years	6 years
Scrap value		2,00,000	2,50,000
After tax annual cash inflow :	Year–1	5,00,000	6,00,000
	Year–2	7,50,000	8,00,000
	Year–3	10,00,000	10,00,000
	Year–4	9,00,000	12,00,000
	Year–5	8,50,000	10,50,000
	Year–6	—	9,50,000

Present value factor at 12% are as follows :

Year :	1	2	3	4	5	6
PV factor :	0·893	0·797	0·712	0·636	0·567	0·507

Evaluate the two proposals under :

(a) Payback period

(b) NPV method

Which model would you recommend and why? 10

(Continued)

Or

(a) Define risk and state the various sources of risk. 5

(b) FLY company, manufacturing golf equipment want to choose a better of two investments namely *X* and *Y*. Each requires an initial outlay of ₹ 1,00,000 and each has a most likely annual rate of return of 14%. Management has made pessimistic and optimistic estimates of the returns associated with each and are as follows :

	X	*Y*
Pessimistic	15%	8%
Optimistic	20%	25%

Determine the range and suggest FLY company the better project. 5

8. *(a)* The equity of *X* Ltd. are traded in the market at ₹ 90 each. The expected current year dividend per share is ₹ 18. The subsequent growth in dividends is expected at the rate of 6%. Calculate the cost of equity capital. 5

(b) HP Ltd. has ₹ 100 preference shares redeemable at a premium of 10% with 15 years maturity. The coupon rate is 12%, floatation cost –5% and sale price is ₹ 95. Calculate the cost of preference share. 5

(Turn Over)

Or

Star Cement Ltd. has the following capital structure :

Particulars	*Market value*	*Book value*	*Cost %*
Equity share capital	80	120	18
Preference share capital	30	20	15
Debentures	40	40	14

Calculate the company's weighted average cost of capital based on both market values and book values. 5+5

9. Companies X and Y are identical in all respect including risk factors except for debt/equity. Company X having issued 10% debentures of ₹ 18 lakhs while company Y has issued only equity. Both the companies earn 20% before interest and taxes on their total assets of ₹ 30 lakhs. Assuming a tax rate of 50% and capitalisation of 15% for an all equity company, compute the value of company X and Y using Net Income Approach. 10

Or

A company has a total investment of ₹ 5,00,000 in assets and 50000 outstanding ordinary shares at ₹ 10 per share. It earns a rate of 15% on its investment and has a policy of retaining 50% of the earnings.

(*Continued*)

If the appropriate discount rate of the firm is 10%, determine the price of its assets using Gordon's model.

What shall happen to the price of the share, if the company has a pay out ratio of *(a)* 80% and *(b)* 20% ? 10

10. Discuss the various costs and benefits of receivables attached with a credit policy. 10

Or

Product cost sheet of X company :

	₹
Raw materials	45
Direct labour	20
Overhead	40
Total	105
Profit	15
Selling price	120

Additional Information :

(i) Raw materials are in stock on an average for 2 months

(ii) The materials are in process on an average for 1 month. The degree of completion is 50% in respect of all elements of cost

(iii) Finish goods stock on an average is for 1 month

(*Turn Over*)

(iv) Time lag in payment of wages and overhead is one and half weeks

(v) Time lag in receipt of proceeds from debtors is 2 months

(vi) Credit allowed by supplier is 1 month

(vii) 20% of output is sold against cash

(viii) The company expects to keep a cash balance of ₹ 1,00,000

(ix) The company is to manufacture 1,44,000 units in next year

You are required to prepare a statement showing the working capital requirement of the company. 10

PART—C

(Case Study)

(*Marks* : 10)

11. A firm is expecting an EBIT of 10% on its total assets of ₹ 20,00,000. The firm's cost of capital is 13·5%. Calculate the *(a)* value of the firm and *(b)* cost of equity capital. 10

Comment on the following situation :

(a) When firm uses ₹ 6,00,000 debts at 8%

(b) When firm uses ₹ 8,00,000 debts at 8%

(c) When firm uses ₹ 10,00,000 debts at 8%

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