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10MBA23

Second Semester MBA Degree Examination, Dec.2014/Jan.2015
Financial Management

Time: 3 hrs.

Max. Marks:100

Note: 1. Answer any FOUR questions from Q.No. 1 to Q.No. 7.

2. Question No. 8 is compulsory.

3. Students are permitted to use present values and future value tables.

- 1 a. What is i) Profit maximization? ii) Wealth maximization? (03 Marks)
 b. The market price of a Rs 1000 par value bond carrying a coupon rate of 14% and maturing after 5 years is Rs 1050. What is the yield to maturity on this bond? What will be the realized yield to maturity if the re – investment rate is 12%. (07 Marks)
 c. From the following capital structure of a company, calculate the overall cost of capital using
 i) Book value weights ii) Market value – weights.

Source	Book value	Market value
Equity share capital (Rs 10 shares)	Rs 45,000	Rs 90,000
Retained earnings	Rs 15,000	- Nil -
Preference share capital	Rs 10,000	Rs 10,000
Debentures	Rs 30,000	Rs 30,000

The after Tax cost at different sources of finance is as follows : Equity Share capital 14%. Retained earnings 13%, Preference capital 10%, Debentures 5%. (10 Marks)

- 2 a. What are Sweat Equity Shares? (03 Marks)
 b. Calculate the combined leverage and operating leverage from the following data :
 Sales 5,00,000 units at Rs 10/- per unit ; Variable cost per unit at Rs 3-50 per unit ;
 Fixed charges Rs 5,00,000 ; Interest charges Rs 20,000. (07 Marks)
 c. What is Working Capital? What are the factors influencing working capital? (10 Marks)
- 3 a. What is "Time-value of money? (03 Marks)
 b. What are the objectives of Financial Management? (07 Marks)
 c. The following figures relate to 2 companies :

	P Ltd (Rs in lakhs)	Q Ltd (Rs in lakhs)
Sales	500	1000
Variable cost	200	300
Contribution	300	700
Fixed Assets	150	400
EBIT	150	300
Interest	50	100
Profit before Tax	100	200

You are required to :

1. Calculate the Operating, Financial and Combined leverage for the two companies.
 2. Comment on the relative risk position of them. (10 Marks)

- 4 a. What is CAPM? (03 Marks)
 b. Mention any four merits and demerits of Discounted cash flow method. (07 Marks)

Important Note : 1. On completing your answers, compulsorily draw diagonal cross lines on the remaining blank pages.
 2. Any revealing of identification, appeal to evaluator and /or equations written eg, 42+8 = 50, will be treated as malpractice.

- c. The selected financial data of A, B and C companies for the year ended 31-12-2010 are as follows :

	A	B	C
Variable expenses as % of sales	66.66	75	50
Interest Expenses	Rs 200	Rs 300	Rs 1000
Degree of operating leverage	5.1	6.1	2.1
Degree of financial leverage	3.1	4.1	2.1
Income Tax rate	0.50	0.50	0.50

Prepare Income statement for A, B and C companies.

(10 Marks)

- 5 a. Define Capital Market. (03 Marks)
- b. The following data for Kishan Ltd for the year ended 2010 is given below :
Profit and Loss A/c data (Rs. In millions)
 Sales ---- Rs 80.
 Cost of goods sold ---- Rs 56.

(07 Marks)

Balance sheet data (Rs. in millions)

	1-1-2010	31-12-2010
Inventory	9	12
Accounts receivables	12	16
Accounts payable	7	10

What is the length of the operating cycle and the cash cycle? Assume 365 days in a year.

- c. Briefly explain the factors effecting dividend policy.

(10 Marks)

- 6 a. State the differences between shares and debentures. (03 Marks)
- b. Kishan ltd and Kishore Ltd are in the same type of business and hence are having similar operating risks. The capital structure of each of them is as follows :

	Kishan Ltd	Kishore Ltd
Equity share capital (Shares of Rs 10 each)	4,00,000	5,00,000
Market value per share	15.00	12.00
Dividend per share	2.70	2.88
Debentures (100 each)	Nil	2,50,000
Market value per Debenture	Nil	80.00
Interest rate	Nil	8%

Assuming that level of dividends are generally expected to continue indefinitely and the Income tax rate is 50%. You are required to compute the weighted average cost of capital of each company.

(07 Marks)

- c. Explain the capital budgeting process.

(10 Marks)

- 7 a. What is Capital Structure? What are the major determinants of capital structure? (03 Marks)
- b. Kishan Company is contemplating conversion of 500, 14% convertible bonds of Rs 1000 each. Market price of the bond is Rs 1080. Bond indenture provides that one Bond will be exchanged for 10 shares. Price earnings ratio before redemption is 20:1 and anticipated price earnings ratio after redemption is 25:1. Number of shares outstanding prior to redemption are 10,000. EBIT amounts to Rs 2,00,000. The Company is in the 35% tax bracket. Should the company convert bonds to shares? Give reasons. (07 Marks)

- c. As a Financial Manager of Karishma Ltd., Bangalore, you have to advise the Board of Directors on choosing between two competing project proposals, which require an equal investment of Rs 1,00,000 and expected to generate cash flows as under :

Year	PV factor at 10%	Project – I (Rs)	Project – II (Rs)
2001	0.909	48,000	20,000
2002	0.825	32,000	24,000
2003	0.751	20,000	36,000
2004	0.683	Nil	48,000
2005	0.621	24,000	16,000
2006	0.564	12,000	8,000

Which project proposal should be recommended and why? Assume cost of capital to be 10% P.A are given in the above table. Evaluate the projects by NPV. (10 Marks)

8 CASE STUDY : (compulsory)

A Ltd company wishes to expand its operations. Details of the project are given below :
Investment Rs 1,00,000

Cash Flows	Rs
I Year	1,00,000
II Year	2,60,000
III Year	2,50,000
IV Year	3,00,000
V Year	3,00,000

The cost of capital for the company is 11% using NPV method, find if the above project is feasible.

Three financing plans are available to the company.

Financing plan I – 100 % equity.

Financing plan – II a) 50% equity
b) 50% debt

Financing plan – III a) 70% debt
b) 30% equity.

The cost of equity is 11% and the debt capitalization rate is 14%.

- Which financing plan would the company adopt?
- What are the other considerations in adopting a new project?

(20 Marks)
