CBCS Scheme

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Third Semester MBA Degree Examination, Dec.2017/Jan.2018
Advanced Financial Management

Time: 3 hrs. Max. Marks:80

Note: 1. *Answer any Four questions from Q.No. 1 to Q.No. 7.*
2. *Question No. 8 is compulsory.*

1 a. What are the assumptions of Walter Model? **(02 Marks)**
b. Explain the importance of trade credit and accruals as sources of working capital. **(06 Marks)**
c. G Ltd produces a product which has a monthly demand of 4,000 units. The product requires a component X which is purchased at Rs 20. For every finished product, one unit of component is required. The Ordering cost is Rs 120 per order and the holding cost is 10% per annum. You are required to calculate :
i) Economic order quantity.
ii) If the minimum lot size to be supplied is 4000 units, what is the extra cost? **(08 Marks)**

2 a. What is meant by Capital cost? **(02 Marks)**
b. From the following information supplied to you, determine the theoretical market value of equity shares of a company as per Walter's model.
Earnings of the company = Rs 5,00,000 ; Dividend paid = Rs 3,00,000
No. of shares outstanding = Rs 1,00,000 ; Price earning ratio = 8
Rate of return on investment = 15%.
Are you satisfied with the current dividend policy of the firm? If not, what should be the optimal dividend payout ratio in this case? **(06 Marks)**
c. Explain in detail different sources for financing working capital. **(08 Marks)**

3 a. Differentiate between Postal float and Lethargy processing float. **(02 Marks)**
b. What are the principal motives for holding cash? **(06 Marks)**
c. Dharma Ltd has current sales of Rs 6,00,000 per annum. To push up sales, Dharma is considering a more liberal credit policy as one of the strategies. The current average collection period of the company is 30 days. Proposed increases in collection period and their impact on sales and default rate (on total sales) are given below : **(08 Marks)**

Credit Policy	Increase in collection period	Increase in sales	Default rate
I	15 days	Rs 25,000	0.5 %
II	30 days	Rs 60,000	1.0 %
III	40 days	Rs 70,000	2.0 %

Dharma is selling its product at Rs 10 each. Average cost per unit at the current level is Rs 8 and variable cost per unit is Rs 6. If Dharma requires a rate of return of 20% on its investment, which credit policy do you recommend and why? Assume 360 days a year.

4 a. What are the reasons for splitting of a firm's ordinary shares? **(02 Marks)**
b. Sky Company has a policy of maintaining a minimum cash balance of Rs 5,00,000. The standard deviation of the company's daily cash flows is Rs 2,00,000. The annual interest rate is 14%. The transaction cost of buying and selling securities is Rs 150 per transaction. Determine Sky Company's upper control limit and the return point as per the miller – Orr model. **(06 Marks)**

c. Describe and explain the EBIT – EPS and ROI – ROE analysis of capital structure. **(08 Marks)**

5 a. What do you mean by Cash Budget? **(02 Marks)**

b. What is meant by Credit Analysis? Explain in brief different steps involved in the credit investigation process. **(06 Marks)**

c. The following is the data regarding two companies 'X' and 'Y' belonging to the same risk class.

Particulars	X	Y
No. of ordinary shares	90,000	1,50,000
Market price per share	Rs 1.20	Rs 1.00
6% Debentures	Rs 60,000	NIL
Profit before interest	Rs 18,000	Rs 18,000

All profits after debentures interest are distributed as dividends. How under Modigliani and Miller approach an investor holding 10% of shares in Company X will be better off in switching his holdings to Company Y. **(08 Marks)**

6 a. What are Ordering and Carrying Costs? **(02 Marks)**

b. The Rajat Company belongs to a risk class of which the capitalization rate is 10%. It has currently 1,00,000 shares selling at Rs 100 each. The firm is contemplating the declaration of Rs 6 dividend at the end of the current fiscal year, which has just begun. Answer the following questions based on Modigliani and Miller model. **(06 Marks)**

i) What will be the price of the shares at the end of the year, if a dividend is not declared? What will it be if it is declared?

ii) Assuming that the firm pays dividend has a net income of Rs. 10,00,000 and makes new investments of Rs. 20,00,000 during the period, how many new shares must be issued?

c. The annual cash requirement of A Ltd is Rs 10,00,000. The company has marketable securities in lot sizes of Rs. 50,000 , Rs 1,00,000 , Rs. 2,00,000 and Rs. 2,50,000. The cost of conversion of marketable securities per lot is Rs. 1,000. The company can earn 5% yield on its securities. You are required to prepare a table indicating which lot size will have to be sold by the company and also show that economic lot size can be obtained by the Baumol Model. **(08 Marks)**

7 a. What is the Clientele Effect? **(02 Marks)**

b. From the following you are required to calculate i) Re – order level ii) Minimum level iii) Maximum level.

Normal usage : 100 units per day ; Maximum usage : 130 units per day

Minimum usage : 70 units per day ; EOQ : 5,000 units **(06 Marks)**

Re-order period : 25 to 30 days.

c. What are the different forms of Stable dividend? List out the merits of stability of dividends. **(08 Marks)**

8 Prepare Cash Budget for January – June from the following information :

i) The estimated sales and expenses are as following :

Particulars	Nov	Dec	Jan	Feb	Mar	April	May	June
Sales (Rs in thousands)	200	220	120	100	150	240	200	200
Wages (Rs in thousands)	30	30	24	24	24	30	27	27
Miscellaneous Exp (Rs in thousands)	27	27	21	30	24	27	27	27

ii) 20% of the sales are on cash and balance on credit.

iii) The firm has a gross margin of 25% on sales.

iv) 50% of the credit sales are collected in the month following the sales, 30% in the second month and 20% in the third month.
v) Material for the sale of each month is purchased one month in advance on a credit for two months.
vi) The time – lag in the payment of wages is 1/3rd of a month and miscellaneous expenses one month.
vii) Debentures worth Rs 40,000 were sold in Jan month.
viii) The firm maintains a minimum cash balance of Rs 40,000. Fund can be borrowed @ 12% per annum interest rate in the multiples of Rs 1000, the interest being payable on monthly basis.
ix) Cash balance at the end of December is Rs 60,000. **(16 Marks)**

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