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Third Semester MBA Degree Examination, June 2012
Advanced Finance Management

Time: 3 hrs.

Max. Marks:100

Note: 1. Answer any FOUR full questions from Q.No.1 to 7.
2. Q.No. 8 is compulsory.

- 1 a. What do you mean by industrial sickness? (03 Marks)
 b. What are the different types of factoring? Explain any three, in detail. (07 Marks)
 c. The present annual sales of m/s Info Way Ltd. are ₹ 30 lakhs. The company classify its customers into three categories viz : 1, 2 and 3. At present, it is providing unlimited credit to category 1, limited credit to category 2 customers and extends no credit business to those in category 3. Due to the present credit policy, the company is foregoing sales of ₹ 5 lakhs in customers in category 2 and ₹ 8 lakhs to the category 3 customers. Now the company is considering the adoption of more liberal credit, in which the customers in category 2 would be provided unlimited credit facility and customers in category 3 would be provided limited credit facility. Such relaxation would increase the sales by ₹ 9 lakhs on which bad debts would be 5%. The variable cost to sales ratio is 70%, the average collection period is expected to be 50 days and cost of capital is 15%. The company is in a tax bracket of 40%. Determine the change in act profits and suggest whether the proposed change is desirable. (10 Marks)

- 2 a. What is the annual percentage interest cost associated in the credit term 3/10, act 45? (03 Marks)
 b. Following is the information relating to M/S ABC Ltd. and M/S XYZ Ltd :

Description	₹ in million	
	ABC Ltd.	XYZ Ltd.
Current assets (CA)	₹ 200	₹ 80
Net fixed assets (FA)	₹ 80	₹ 200
Total assets	₹ 280	₹ 280
Earnings before interest and tax (EBIT)	₹ 700	₹ 700
ROI	25%	25%

You are required to compute the working capital leverage (WCL) :

- i) For 20% increase in current assets of M/S XYZ company Ltd. and
 ii) 20% decrease in the level of current assets of M/S ABC Ltd. (07 Marks)
 c. M/S Max Matrix Company Ltd. belongs to a risk class of which the appropriate capitalization rate is 10%. IT currently has 100000 shares selling at ₹ 100 each. The firm is contemplating the declaration of a ₹6 dividend at the end of the current fiscal year, which has just begun. Given the above piece of information and that there are no taxes, comment on the following based on Modigliani-Miller approach :
 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 in come of ₹ 10 lakhs and makes new investment of ₹ 20 lakhs during the period, how many new shares must be issued? (10 Marks)
- 3 a. What do you mean by working capital leverage? (03 Marks)
 b. What are the various causes for industrial sickness? (07 Marks)
 c. Explain the concept of economic value added (EVA). What are the merits? How can EVA be improved? (10 Marks)

- 4 a. List the costs associated with inventory management. (03 Marks)
 b. Using Baumol model of cash, student has arrived at the economic lot size (ELS) as ₹ 200000. If the estimated cash needs is ₹ 20 lakhs per year, cost of conversion of marketable securities is ₹ 2000 per lot, what is the rate of interest associated with this problem? (07 Marks)
 c. M/S fortune company Ltd. would like to adopt selective inventory control. If the following information is available, show how would you classify the materials in to A, B and C items :

Material code	A-36	B-48	C-12	P-14	L-10	Q-07	M-05	G-03
Units	7000	8000	10000	6000	8000	2000	5000	4000
Unit cost (₹)	₹ 10	9.00	2.00	8.00	1.00	60.0	0.40	40.0

(10 Marks)

- 5 a. Mention the four capital structure theories. (03 Marks)
 b. From the following information of M/S Best company Ltd. compute :
 i) Re-order level
 ii) Minimum level
 iii) Maximum level
 iv) Average stock level.

The company uses two components x and y for its manufacturing a product.

- Normal usage - 100 units per week,
 Maximum usage - 150 units per week,
 Minimum usage - 50 units per week,
 Re-order period - component x – 4 to 10 weeks,
 component y – 2 to 8 weeks
 Re-order quantity - component x – 600 units
 component y – 900 units

(07 Marks)

- c. M/S mega insulator Ltd. has investigated the profitability of its assets and cost of its funds. The result indicates as below :
 i) Current assets earn 6%,
 ii) Fixed assets earn 13%,
 iii) Current liabilities costs 3% and
 iv) Average cost of long term funds cost 10%.

The latest balance sheet of M/S mega insulators Ltd. is as follows :

Liabilities	₹	Assets	₹
Current liabilities	10000	Current assets	20000
Long term funds	70000	Fixed assets	60000
	80000		80000

You are required to compute :

- i) Net profitability
 ii) The company wishes to lower its net working capital to ₹ 7000 by either-shifting ₹3000 of current assets to fixed assets or shifting ₹ 3000 of its long term funds into current liabilities. Work out the profitability for each of these options. Which do you prefer? Why? (10 Marks)
- 6 a. What do you mean by “dividend”? (03 Marks)
 b. The following is the data regarding two companies X Ltd. and Y Ltd. belonging to the same risk class :

Particulars	X Ltd.	Y Ltd.
Number of ordinary shares	90000	150000
Market price per share	₹ 1.20	₹ 1.00
6% debentures	₹ 60000	NIL
Profits before interest and taxes	₹ 18000	₹ 18000

All profits after debenture interest are distributed as dividends. Explain how under Modigliani and miller approach an investor holding 10% of the shares in company X will be better off in switching his holding to Y Ltd. (07 Marks)

- c. M/S Mae-Million ventures Ltd's earnings per share is ₹ 10. It has an internal rate of return of 15% and the capitalization rate of risk class is 12.5%. If Watter model of dividend is used :
- What should be the optimum payout ratio of the firm?
 - What should be the price of the share at this point that is i) above?
 - How shall the price of the share be affected if a different payout were employed?
- (10 Marks)

- 7 a. What are the three broad approaches to valuing an intangible asset? Briefly explain. (08 Marks)
- b. From the following particulars, prepare a monthly cash budget for the quarter ended 31st March 2011 :

Month	Sales	Purchases	Wages	₹ in lakhs
				Expenses
November 10	5.0	1.0	2.0	0.40
December 10	6.0	2.0	2.0	0.40
January 2011	4.0	3.0	2.20	0.50
February 2011	5.0	2.0	2.20	0.50
March 2011	6.0	1.0	2.40	0.50

Additional information :

- 10% sales and purchases are on cash.
- Credit to debtors : one month on an average, 50% of debtors will make payment on the due date while the rest will make payment one month there after.
- Credit from creditors : 2 months.
- Wages to be paid twice in a month-on the 1st and 16th respectively.
- Expenses are generally paid within the month.
- Plant costing ₹ 100000 will be installed in February on payment of 25% of the cost in addition to the installation cost of ₹ 5000/-, balance to be paid in three equal installments from the following month.
- Opening balance of cash : ₹ 200000. (12 Marks)

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CASE STUDY

M/S Simon steel mills Ltd. has a share capital of ₹ 2 lakhs divided into shares of ₹ 10 each. It has a major expansion program that requires an additional investment of ₹ 100000. The management is considering the following options :

Option I : Issue of 10% debentures for ₹ 100000

Option II : Issues of 10000, 15% preference shares of ₹ 10 each

Option III : Issue of 10000 equity shares of ₹ 10 each.

The company's present EBIT is ₹ 60000 per year. Calculate the EPS for the above three options presuming :

- EBIT continuous to be the same
 - EBIT increases by ₹ 20000
- Tax rate is 50%. (20 Marks)

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