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12MBAFM321

Third Semester MBA Degree Examination, June/July.2015
Advanced Financial Management

Time: 3 hrs. Max. Marks:100

Note: 1. ***Answer any THREE full questions from Q.No.1 to Q.No.6.***
2. ***Question No. 7 & 8 are compulsory.***

1 a. With the formulae, explain what working capital leverage is. **(03 Marks)**
b. Explain the various sources of working capital. **(07 Marks)**
c. Define Merger, Explain the various types of mergers of motives behind merger. **(10 Marks)**

2 a. What is concentration banking? **(03 Marks)**
b. The annual cash requirement of A Ltd is ₹ 10 lakh. The company has marketable securities in lot sizes of ₹ 50,000, ₹ 100,000, ₹ 2,00,000, ₹ 2,50,000 and ₹ 5,00,000. Cost of conversion of marketable security per lot is ₹ 1,000. The company caw earn 5% yield on securities, you are required to prepare a table indicating which lot size will have to be sold by the company. Also show the economic lot size to be obtained by Baumol model. **(07 Marks)**
c. The following results are expected by xyz Ltd by quaters next year in thousand of rupees.

Particulars	1	2	3	4
Sales Cash payments :	7500	10,500	18,000	10,500
Production cost :	7,000	10,000	8,000	8,500
Selling, administrative and other costs	1,000	2,000	2,900	1,600
Purchase of plants and other fixed assets	100	1,100	2,100	2,100

The debtors at the end of the quarter are ⅓rd of sales for the quarter. The opening balance of debtors is ₹ 30,00,000. Cash on hand at the beginning of the year is ₹ 5,00,000. Borrowings are made at the beginning of quarters in which multiplies of ₹ 10,000 and are repaid at the end of quarters interest charges may be ignored. You are required to prepare i) Cash Budget by quarters for the year. ii) State loan outstanding at the end of the year. **(10 Marks)**

3 a. Define EVA and explain its components. **(03 Marks)**
b. What are stock dividends and stock splits. Explain their rationale. **(07 Marks)**
c. Define industrial sickness. Explain the causes and symptoms of sickness. **(10 Marks)**

4 a. What is an ageing schedule. **(03 Marks)**
b. The financial manager of firm is wondering whether credit should be granted to a new customer who expected to make repeat purchase on the basis of credit evaluation. The financial manager feels that the probability that the customer will pay 0.70 and probability that customer will default is 0.30. Once the customer pays for the first purchase, the probability that he will pay for the repeat purchase will be 0.90. The revenue from the sales will be ₹ 2,00,000 of the cost of sale will be 160,000 – these figures apply to both initial and repeat purchases. What is the expected pay off if the credit is granted? **(07 Marks)**

c. Rakesh enterprise is currently providing 30 days credit to its customers. Its present sales are ₹ 200 million. Its cost of capital is 12% of the ratio of variable cost to sales is 0.80. Rakesh enterprise is considering extending its credit period to 45 days which is likely to push sales up by ₹ 60 million. The bad debt proportion on additional sales would be 15%. The tax rate is 33%. What will be effect of lengthening the credit period as residual income of the firm. **(10 Marks)**

5 a. What is ROI – ROE analysis? **(03 Marks)**

b. Precision Engg factory consumer 50,000 units of component per year. The ordering, receiving and handling costs are ₹ 3 per order while tracking cost are ₹ 12 per order. Further details are as follows : deterioration and obsolescence cost ₹ 0.004 per unit per year ; interest cost ₹ 0.06 per unit per year ; storage cost ₹ 1000 per year for 50,000 units. Calculate EOQ. **(07 Marks)**

c. From the details given below, calculate ;
i) Reordering level ii) Minimum level iii) Maximum level iv) Danger level. Reorder quantity is to be calculated on the basis on the following :-
cost of placing a purchase orders is ₹ 20 No. of units to be purchased during the year is 5,000 purchased price per unit inclusive of transportation cost is ₹ 50. Annural cost of storage per unit is ₹ 5 Details of lead time: Average 10 days ; maximum 15 days minimum – 6 days. For emergency purchase 4 days. Rae of consumption : Average : 15 units per day maximum : 20 units per day. **(10 Marks)**

6 a. How is EFR computed? **(03 Marks)**

b. In engineering company has a cost of equity capital of 10%. It earns 18% return an investment. The companys earning is ₹ 10 per share. According to Walters model what should be the price of shares at 25% dividend payout ratio? Is it optimal ratio. If not what is the market price at optimal ratio? **(07 Marks)**

c. R company belongs to a risk class whose capitalization rate is 10%. It currently has 1,00,000 shares selling at ₹ 100. The firm is contemplating the declaration of ₹ 6 dividend at the end of the year. Answer the following questions based on MM model on the assumption that taxes does not exist. Assuming that the firm has net income of ₹ 10,00,000 and also pay dividends. It makes investments of ₹ 20 lakhs during the period. How many new shares must be issued. **(10 Marks)**

7 a. Define agency cost/problem and explain why firms incur them. How can it be reduced? **(05 Marks)**

b. What is the cost of trade for credit terms " $^{2}/_{15}$ net 45". **(05 Marks)**

c. In considering the most desirable capital structure of a company, the following estimates of the cost of debt and equity capital (after tax) have been made at various levels of debt – equity mix:

Debt as % of Total Capital employed	Cost of debt (%)	Cost of equity (%)
0	5.1	12.0
10	5.0	12.0
20	5.0	12.5
30	5.5	13.0
40	6.0	14.0
50	6.5	16.0
60	7.0	20.0

You are required to calculate/determine optimal debt equity minimum by calculating composite cost of capital. **(10 Marks)**

8 Compulsory

a. A company currents operating income is ₹ 4 lakhs. The firm has ₹ 10 lakhs of 10% debt outstanding. Its cost of equity capital is estimated to be 15%.
i) Determine the current value of the firm using traditional approach.
ii) Calculate overall capitalisation rate as well as leverage ratio
1) B/S 2) B/V 3) The firm is considering increasing its leverage by raising an additional ₹ 500,000 debt and using the proceeds to retire that amount of equity. As a result of increased financial risk Ki is likely to go up to 12% and Ke is 18% would you recommend the plan. **(15 Marks)**

b. Give a critical approaisal of Modigliani – Muller approach to capital structure theory. **(05 Marks)**

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