Seat No.: _____ Enrolment No.______

GUJARAT TECHNOLOGICAL UNIVERSITY

MBA. Second Semester (Regular / Evening) Examination May 2010

Subject code: 820003

Subject Name: Financial Management

Date: 24 / 05 / 2010 **Time : 11.00 am – 01.30 pm**

Total Marks: 70

Instructions:

1. **Attempt all questions.**
2. **Make suitable assumptions wherever necessary.**
3. **Figures to the right indicate full marks.**

Q.1 **(a)** "Financial Management is that managerial activity which is concerned with the planning and controlling of the firm's financial resources". **07**
In view of the above statement, discuss in detail the major finance functions and the role played by the finance manager.

(b) An investor has invested his savings in a company from whom dividends are expected to grow @20% for 15 years and thereafter @7% forever. Find out the value of the equity share given that the current dividend per share is Re. 1 and the required rate of return of the investor is 9%. **07**

Q.2 **(a)** Explain the concept of Working Capital and discuss in brief the major factors which generally influence the working capital requirements of firms. **07**

(b) From the following information, you are required to estimate the net working capital. **07**

	Cost per unit (Rs.)
Raw Materials	300
Direct Labour	100
Overheads (excluding Depreciation)	200
Total Cost	600

Additional Information :

Selling Price	Rs. 800 per unit
Output	50,000 units per annum
Raw Materials in Stock	average 4 weeks
Work-in-process : (assume 50% completion stage with full material consumption)	average 2 weeks
Finished Goods in Stock	average 5 weeks
Credit allowed to Debtors	average 5 weeks
Credit allowed by Creditors	average 10 weeks
Cash at Bank is expected to be	Rs. 60,000

Assume that production is sustained at an even pace during the 52 weeks of the year. All sales are on credit basis.

OR

(b) 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% p.a. **07**
You are required to calculate :
(i) Economic order quantity.
(ii) If the minimum lot size to be supplied is 4,000 units, what is the extra cost, the company has to incur ?

Q.3 **(a)** Discuss in detail the advantages and disadvantages of the various discounted cash flow methods of capital budgeting. **07**

(b) The particulars about the existing capital structure of A Ltd. are given : **07**

	Amount Rs.	Before-tax Cost (%)
Equity Share Capital	8,00,000	12%
Preference Share Capital	1,00,000	7%
Long-term Debt	6,00,000	8%

The company wants to undertake an expansion project costing Rs. 5,00,000 which can be taken from a bank at 10%. The minimum acceptable rate of return from the new project is based on the company's cost of capital. What is the minimum acceptable rate of return to the company in the case of the proposed expansion project? You may assume a 50% tax rate.

OR

Q.3 **(a)** Explain the concept of cost of capital, giving its significance. Distinguish between Weighted Average Cost of Capital and Weighted Marginal Cost of Capital. **07**

(b) Machine A costs Rs. 1,00,000 payable immediately. Machine B costs Rs. 1,20,000 half payable immediately and half payable in one year's time. The cash receipts expected are as follows : **07**

Year (at the end)	A	B
1	20,000	--
2	60,000	60,000
3	40,000	60,000
4	30,000	80,000
5	20,000	--

With 7% interest which machine should be selected ?

Q.4 **(a)** Describe the traditional view on the optimum capital structure. Compare and contrast this view with the NOI approach and the NI approach. **07**

(b) The following is the data regarding two companies A and B belonging to the same risk class : **07**

	Company A	Company B
Number of ordinary shares	90,000	1,50,000
Market price per share (Rs.)	1.20	1.00
6% Debentures (Rs.)	60,000	---
Profit before interest (Rs.)	18,000	18,000

All profits after debenture interest are distributed as dividends.
Explain how under Modigliani & Miller approach, an investor holding 10% of shares in company A will be better off in switching his holding to Company B.

OR

Q.4 **(a)** Give in brief the major sources of long term finance. **07**

(b) A firm has sales of Rs. 10,00,000 variable cost of Rs. 7,00,000 and fixed costs of Rs. 2,00,000 and debt of Rs. 5,00,000 at 10% rate of interest. What are the operating, financial and combined leverages ? If the firm wants to double its Earning Before Interest and tax (EBIT), how much of a rise in sales would be needed on a percentage basis ? **07**

Q.5 **(a)** Explain the Walter's dividend model giving its assumptions and shortcomings. **07**

(b) What is a bonus issue ? What are its advantages and disadvantages ? **07**

OR

Q.5 **(a)** Explain the factors that generally influence the dividend policy of the firm. **07**

(b) M Ltd. belongs to a risk class of which the appropriate capitalization rate is 12%. It currently has 90,000 shares selling at Rs. 100 each. The company is contemplating declaration of a dividend of Rs. 5 per share at the end of the current fiscal year which has just begun. Answer the following questions based on Modigliani and Miller Model and assumption of no taxes. **07**

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

(ii) What will be the price if dividend is declared ?

(iii) Assuming that the company pays dividend, has net income of Rs. 12 lakhs and makes a new investment of Rs. 25 lakhs during the period, how many new shares should be issued ?

****