Seat No.: ________ Enrolment No.______________

GUJARAT TECHNOLOGICAL UNIVERSITY

MBA - SEMESTER–II • EXAMINATION – WINTER • 2014

Subject Code: 820003 **Date: 29-12-2014**

Subject Name: Financial Management (FM)

Time: 02:30 pm - 05:30 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)** "The concept of wealth maximization is better in modern times while comparing it with profit maximization." – Explain with suitable example. **07**

(b)1 What is the minimum amount which a person should be ready to accept today from a debtor who otherwise has to pay a sum of Rs.5000 today and Rs.6000, 8000, 9000 and 10000 at the end of the year 1,2,3 and 4 respectively from today. Rate of interest may be taken at 14% **04**

(b)2 Rajasthan Royals borrows Rs.7,50,000 loan to purchase house. The rate of interest is 11% & repayment period is 20 yrs. Calculate monthly equal installment if the interest is calculated on yearly basis. **03**

Q.2 **(a)** Royal Challengers 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?

(b) The cost sheet of Kolkata Night Riders Ltd. provides the following data: **07**

Particulars	Cost per unit
Raw material	50
Direct labour	20
Overheads (including depreciation of Rs. 10)	40
Total cost	110
Profits	20
Selling price	130

Average raw material in stock is for one month. Average work-in-progress is for half month (with full material consumption). Credit allowed by suppliers: one month; credit allowed to debtors: one month. Average time lag in payment of wages: 10 days; average time lag in payment of overheads 30 days. 25% of the sales are on cash basis. Cash balance expected to be Rs.100000. Finished goods remains in the warehouse for one month.

You are required to prepare a statement of the working capital needed to finance a level of the activity of 54000 units of output. Production is carried on evenly throughout the year and wages and overheads accrue similarly. State you assumptions, if any, clearly.

OR

(b) What is working capital? What are the different factors affecting working capital requirement of the firm? **07**

Q.3 **(a)** Under what circumstances NPV and IRR differ? Which method do you prefer and why? **07**

(b) Chennai Super Kings Ltd. is a firm whose cost of capital is 10% is considering two mutually exclusive projects X and Y, the details of which are: **07**

Year	**Project X (Rs)**	**Project Y (Rs)**
0	70,000	70,000
1	10,000	50,000
2	20,000	40,000
3	30,000	20,000
4	45,000	10,000
5	60,000	10,000

Compute the Net present Value at 10%, Profitability Index at 10% and Internal Rate of Return for the two projects and suggest which project should be selected & Why?

OR

Q.3 **(a)** Pune Warriors company is considering an investment proposal to install a new machine. This project will cost Rs.1,00,000 and will have 5 years life with no salvage value. Tax rate is 50 percent; the company follows straight line method of depreciation. The earnings before depreciation and tax as follows. **07**

Years	1	2	3	4	5
EBDT (Rs.)	20000	22000	28000	30000	50000

Evaluate the project using

(1) Pay Back Period

(2) Profitability Index at 10%

(3) Net Present Value at 12%

(b) The particulars about the existing capital structure of Deccan Chargers 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.

Q.4 **(a)** Explain in detail the NI and NOI concepts of Capital Structure with appropriate graphs. **07**

(b) The following data relates to the two companies A and B belonging to the same risk class. **07**

Particulars	**Company A**	**Company B**
No. of ordinary shares	100000	150000
8% debentures	50000	-
Market Price per share	Rs. 1.3	Re. 1
Profit Before Interest and Tax	Rs. 20000	Rs. 20000

You are required to explain how under MM 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)**	Following information is taken from the records of hypothetical company:	**07**

Installed capacity	1000 units
Operating capacity	800 units
Selling price p.u.	Rs. 10
V.C. p.u.	Rs. 7

Calculate operating leverages if fixed costs are 1.Rs.800, 2.Rs.1200, 3.Rs.1500.

(b) "Overall costs of capital and total value of the firm are relevant to the capital structure. But, beyond a certain degree of leverage overall cost increases, leading to a decrease in total value of the firm." – Explain **07**

Q.5 **(a)** The following information relates to XYZ Ltd.: **07**

Paid up capital	2000000
Earnings	200000
Dividend paid	160000
No. of shares outstanding	20000
Ke (Required Rate of Return)	0.08
R (Internal Rate of Return)	0.10

You are required to find out whether the company's dividend payout ratio is optimal, using Walter's Model and Gordon's Model.

(b) What is Bonus Issue? How is it different from Stock Split? Explain by citing proper examples. **07**

OR

Q.5 **(a)** Explain Dividend Theory of Modigliani and Miller with its practical shortcomings. **07**

(b) ABC Ltd has capital of Rs.1000000 in equity shares of Rs.100 each. The shares are currently quoted at par. The company proposes to declare a dividend or Rs.10 per share at the end of the current financial year. The capitalization rate for the risk class to which the company belongs is 12%. What will be the market price of the share under the following conditions: **07**

1. If dividends are not declared
2. If dividends are declared

Assuming that the company pays the dividend and has net profits of Rs.500000 and makes new investment of Rs.1000000 during the period, how many new shares must be issued? Use the MM model.

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