Seat No. : _______________

XU-121

April-2013

Five Years MBA Integrated (K.S.)

Fourth Year M.B.A.

Financial Management

Time : 3 Hours] **[Max. Marks : 70**

1. (a) Answer the following questions (any **two**) : **7**

   (1) Critically evaluate the goal of profit maximization as a goal of financial management.

   (2) "The role of Finance Manager has changed significantly." Comment.

   (3) Describe the Financial System in detail.

   (b) (i) A person is 50 years of age today. He will retire at the age of 60. In order to receive ₹ 2.50 lakhs annually for 10 years after retirement, how much amount should he save per annum from now till his retirement ? Assume the interest rate to be 10%. **5**

   (ii) An investor deposits ₹ 1000 in a bank account for 5 years at 8% interest. Find out the amount which he will receive after 5 years if interest is compounded semi annually. **2**

2. From the following information, you are required to determine the weighted average cost of capital of the company using (a) book value weights (b) market value weights. **14**

   The present capital structure is

	₹
Equity shares (₹ 10 each)	1 crore
Preference shares (₹ 100 each)	20 lakhs
Debentures (₹ 100 each)	80 lakhs

   All the above securities are traded in the capital market; their market values being debentures 10% more, preference shares 20% more and equity shares 120% more than their respective face values.

   Additional Information :

   (1) Debentures are redeemable at par, 10 years maturity, 11% coupon rate, 4% flotation cost, sale price ₹ 100.

   (2) Preference shares are redeemable at par, 10 years maturity, 12% dividend rate, 5% flotation cost, sale price ₹ 100.

(3) Equity shares : sale price ₹ 22, flotation cost ₹ 2 per share.

Dividend expected at the end of the year on the equity share is ₹ 2 per share. The growth rate in dividend is 7%. The corporate tax rate is 35%.

OR

A project involving an outlay of ₹ 1 crore has the following cash inflows associated with it over its useful life of 3 years.

Year – 1		**Year – 2**		**Year – 3**	
Cash flow	**Probability**	**Cash flow**	**Probability**	**Cash flow**	**Probability**
40	0.4	50	0.4	30	0.3
50	0.5	60	0.4	40	0.5
60	0.1	70	0.2	50	0.2

Assume that the cash flows are independent and the risk free discount rate is 10%.

Required :

(1) What is the expected NPV and its standard deviation ?

(2) If the distribution is normal, what is the probability that the NPV will be zero or less ?

(3) What is the probability that the profitability index will be greater than 1.2 ?

3. Answer any **two** from a, b and c. **14**

(a) Explain the relationship between leverage and cost of capital as per the net income approach and as per the net operating income approach.

(b) Financial details of two companies A Ltd and B Ltd., belonging to the same risk class are given below :

Particulars	**A Ltd.**	**B Ltd.**
Net operating income	₹ 6,25,000	₹ 6,25,000
Debt interest	–	₹ 2,50,000
Equity earnings	₹ 6,25,000	₹ 3,75,000
Equity capitalization rate	12%	14%
Market value of equity	₹ 52,08,333	₹ 26,78,571
Market value of debt	–	₹ 31,25,000
Total market value of the firm	₹ 52,08,333	₹ 58,03,571
Average cost of capital	12%	10.77%

If an investor owns equity share of A Ltd. worth ₹ 12,500, show what arbitrage he would resort to.

(c) A company's present capital structure contains 15 lakhs equity shares and 5 lakhs preference shares of ₹ 10 each. The rate of dividend on preference share is 12%. The current EBIT is ₹ 720 lakhs. The company is planning to raise ₹ 1 crore of external financing. Two financing alternatives are being considered :

(i) issuing equity shares of ₹ 10 each.

(ii) issuing debentures carrying 15% interest.

Compute the EPS-EBIT indifference point.

4. Answer any **two** from (a), (b) and (c) : **14**

(a) Explain various factors affecting requirement of working capital in organisation. Also show operating cycle calculation.

(b) What are the motives for holding cash ? Explain Baumol model of cash management.

(c) The Star ltd. currently provides 45 days of credit to its customers. Its present level of sales is ₹ 60 lakhs. The ratio of variable costs to sales is 0.80.

The firm is considering extending its credit period to 60 days. The sales are expected to increase by 6 lakhs. The bad debt proportion on additional sales would be 5%. The company's cost of capital is 15% and the tax rate is 40%. Advise the company about the extension of credit period.

5. (a) Write a detail note on various sources of financing of working capital requirement. **7**

OR

Discuss various reasons for merger and type of mergers.

(b) State Walter Model and Gordon Model of dividend relevance with their assumptions. **7**

OR

Explain various foreign exchange exposures with example.