

Roll No.....

Time allowed : 3 hours

Maximum marks : 100

Total number of questions : 7

Total number of printed pages : 7

- NOTE :** 1. Answer FIVE questions including Question No.1 which is compulsory. All working notes should be shown distinctly.
2. Tables showing the present value of Re.1 and the present value of an annuity of Re.1 for 15 years are annexed.

1. Comment on **any four** of the following :

- (i) Financial sector acts as conduit for the transfer of financial resources from net savers to net borrowers.
- (ii) Under capital rationing, the standard net present value (NPV) decision rule no longer holds true.
- (iii) Most businesses need cash funds to meet contingencies.
- (iv) Apart from the retention of profits and capitalising the accumulated earnings, the bonus shares serve several other objectives.
- (v) Foreign exchange risk can be managed both internally and externally.

(5 marks each)

2. (a) Mona Machines Ltd. has provided you the following information for the year 2008 :

Production for the year	...	69,000 units
Finished goods in store	...	Average 3 months
Raw materials in store	...	Average 2 months' consumption
Work-in-progress (assume 50% completion stage with full material consumption)	...	Average 1 month
Credit allowed by creditors	...	Average 2 months
Credit given to debtors (assume at selling price)	...	Average 3 months
Selling price per unit	...	Rs.50
Raw material cost	...	50% of selling price
Direct wages	...	10% of selling price
Overheads	...	20% of selling price

Company keeps Rs.1,00,000 in cash. There is regular production and sale cycle, and wages and overheads accrue evenly. Wages are paid in the next month of accrual. Material is introduced in the beginning of production cycle.

You are required to calculate working capital requirement of Mona Machines Ltd.

(10 marks)

- (b) Silver Oak Ltd., an Indian company, is mainly engaged in international trade with US and UK. It is currently 1st January. It will have to make a payment of \$7,29,794 in the coming six months time. The company is presently considering the various alternatives in order to hedge its transactional exposure through its London office. The following information is available :

Exchange Rates :

\$/£ Spot rate	:	1.5617 - 1.5773
6-month \$ forward rate	:	1.5455 - 1.5609

<i>Money Market Rates</i>	<i>Borrow</i>	<i>Deposit</i>
	(%)	(%)
US Dollar	6	4.5
Sterling	7	5.5

Foreign currency option prices (Cents per £ for contract size £12,500) :

<i>Exercise Price</i>	<i>Call Option (June)</i>	<i>Put Option (June)</i>
\$1.70/£	3.7	9.6

Suggest which of the following hedging option is the most suitable for Silver Oak Ltd. :

- (i) Forward exchange contract
- (ii) Money market
- (iii) Currency option.

(6 marks)

- (c) Monark Ltd. is considering two alternative financial plans to start a new project. In Plan-I, it is likely to issue equity shares of Rs.16 lakh and 13% preference capital of Rs.4 lakh. In Plan-II, the company will issue equity shares of Rs.8 lakh, 13% preference capital of Rs.4 lakh, and 15% debentures of Rs.8 lakh. The face value of equity shares in both plans is Rs.10. Tax rate is 30%.

You are required to determine level of EBIT at which the EPS would be same under both the plans.

(4 marks)

3. (a) Vaibhav Ltd. is engaged in manufacturing of machines used in construction. It is considering the possibility of purchasing from a supplier a component it now makes. A supplier has agreed to supply the component in the required quantities at a unit price of Rs.18. The transportation and insurance charges are Re.1 per unit.

Presently, the company produces the component from a single raw material in economic lots of 3,000 units at a cost of Rs.4 per unit. The average annual demand is 40,000 units. The annual holding cost for company is Re.0.50 per unit and it has set a minimum stock level of 800 units. The direct labour costs of the component are Rs.12 per unit. The company also hires a machine at a rate of Rs.400 per month on which the components are produced. Suggest whether the company should produce or procure the component.

(14 marks)

- (b) Two companies Rita Ltd. and Gita Ltd. are considering to enter into a swap agreement with each other. Their corresponding borrowing rates are as follows :

<i>Name of Company</i>	<i>Floating Rate</i>	<i>Fixed Rate</i>
Rita Ltd.	LIBOR	11%
Gita Ltd.	LIBOR + 0.3%	12.5%

Rita Ltd. requires a floating rate loan of £8 million while Gita Ltd. requires a fixed rate loan of £8 million.

- (i) Show which company had advantage in floating rate loans and which company has a comparative advantage in fixed loans.
- (ii) If Rita Ltd. and Gita Ltd. engage in a swap agreement and the benefits of the swap are equally split, at what rate will Rita Ltd. be able to obtain floating finance and Gita Ltd. be able to obtain fixed rate finance ?

Ignore bank charges.

(6 marks)

4. Distinguish between **any four** of the following :

- (i) 'Factoring' and 'bill discounting'.
- (ii) 'Operating lease' and 'finance lease'.
- (iii) 'Business risk' and 'financial risk'.
- (iv) 'Efficient portfolio' and 'optimal portfolio'.
- (v) 'Translation risk' and 'transaction risk'.

(5 marks each)

5. Alfa Ltd. is in the business of manufacturing bearings. Some more product lines are being planned to be added to the existing system. To manufacture the planned product lines, the firm needs a machine which if purchased outright will cost Rs.10,00,000. Modern Hire-Purchase and Leasing Co. has offered two proposals as below :

Proposal - I (Hire-Purchase)

Rs.2,50,000 will be payable on signing of the agreement. Three annual installments of Rs.4,00,000 will be payable at the end of each year starting from year first. The ownership of the machine will be transferred automatically at the end of third year. The company will be able to claim depreciation on straight line basis with zero salvage value.

Proposal - II (Lease)

Rs.20,000 will be payable towards initial service fee upon signing of the agreement which is tax-deductible expense. Annual lease rental of Rs.4,32,000 is payable at the end of each year starting from the first year for a period of three years.

Evaluate the above two proposals and advise the company as to which proposal implies lesser cost given that tax-rate is 35% and discount rate is 20%. (Calculations may be rounded off to Rupee.)

(20 marks)

6. (a) The following data is related to Raman Ltd. :

Year	Raman Ltd.		Nifty Average Index	Nifty Dividend Yield	Return on Government Stock
	Average Share Price	Dividend Per Share			
3	278	14	2,600	4 %	8 %
2	294	17	2,990	6 %	10 %
1	326	18	3,040	6.5%	9 %
Current	370	20	3,280	6.5%	9 %

Calculate --

- (i) Expected return on shares of Raman Ltd.; and
(ii) Beta (β) value using Capital Asset Pricing Model (CAPM).

(14 marks)

- (b) Following facts are available for Astro Ltd. :

- (i) Cash turnover rate is 5;
(ii) Annual cash outflow is Rs.1,75,000; and
(iii) Accounts payable can be stretched by 12 days.

What would be the effect of stretching accounts payable on the minimum operating cash requirements ? If the firm can earn 10% on its investments, what would be the savings on cost ? (Assume 360 days in a year.)

(6 marks)
Contd...

7. Write notes on **any four** of the following :
- (i) Financial instruments used for venture financing
 - (ii) Factors affecting dividend policy of a firm
 - (iii) Optimal capital structure
 - (iv) Financing cost escalation
 - (v) Domestic resource cost.

(5 marks each)

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TABLE - I : PRESENT VALUE OF RUPEE ONE

RATE	YEAR 1	YEAR 2	YEAR 3	YEAR 4	YEAR 5	YEAR 6	YEAR 7	YEAR 8	YEAR 9	YEAR 10	YEAR 11	YEAR 12	YEAR 13	YEAR 14	YEAR 15
5%	0.9524	0.9070	0.8638	0.8227	0.7835	0.7462	0.7107	0.6768	0.6446	0.6139	0.5847	0.5568	0.5303	0.5051	0.4810
6%	0.9434	0.8900	0.8396	0.7921	0.7473	0.7050	0.6651	0.6274	0.5919	0.5584	0.5268	0.4970	0.4688	0.4423	0.4173
7%	0.9346	0.8734	0.8163	0.7629	0.7130	0.6663	0.6227	0.5820	0.5439	0.5083	0.4751	0.4440	0.4150	0.3878	0.3624
8%	0.9259	0.8573	0.7938	0.7350	0.6806	0.6302	0.5835	0.5403	0.5002	0.4632	0.4289	0.3971	0.3677	0.3405	0.3152
9%	0.9174	0.8417	0.7722	0.7084	0.6499	0.5963	0.5470	0.5019	0.4604	0.4224	0.3875	0.3555	0.3262	0.2992	0.2745
10%	0.9091	0.8264	0.7513	0.6830	0.6209	0.5645	0.5132	0.4665	0.4241	0.3855	0.3505	0.3186	0.2897	0.2633	0.2394
11%	0.9009	0.8116	0.7312	0.6587	0.5935	0.5346	0.4817	0.4339	0.3909	0.3522	0.3173	0.2858	0.2575	0.2320	0.2090
12%	0.8929	0.7972	0.7118	0.6355	0.5674	0.5066	0.4523	0.4039	0.3606	0.3220	0.2875	0.2567	0.2292	0.2046	0.1827
13%	0.8850	0.7831	0.6931	0.6133	0.5428	0.4803	0.4251	0.3762	0.3329	0.2946	0.2607	0.2307	0.2042	0.1807	0.1599
14%	0.8772	0.7695	0.6750	0.5921	0.5194	0.4556	0.3996	0.3506	0.3075	0.2697	0.2366	0.2076	0.1821	0.1597	0.1401
15%	0.8696	0.7561	0.6575	0.5718	0.4972	0.4323	0.3759	0.3269	0.2843	0.2472	0.2149	0.1869	0.1625	0.1413	0.1229
16%	0.8621	0.7432	0.6407	0.5523	0.4761	0.4104	0.3538	0.3050	0.2630	0.2267	0.1954	0.1685	0.1452	0.1252	0.1079
17%	0.8547	0.7305	0.6244	0.5337	0.4561	0.3898	0.3332	0.2848	0.2434	0.2080	0.1778	0.1520	0.1299	0.1110	0.0949
18%	0.8475	0.7182	0.6086	0.5158	0.4371	0.3704	0.3139	0.2660	0.2255	0.1911	0.1619	0.1372	0.1163	0.0985	0.0835
19%	0.8403	0.7062	0.5934	0.4987	0.4190	0.3521	0.2959	0.2487	0.2090	0.1756	0.1476	0.1240	0.1042	0.0876	0.0736
20%	0.8333	0.6944	0.5787	0.4823	0.4019	0.3349	0.2791	0.2326	0.1938	0.1615	0.1346	0.1122	0.0935	0.0779	0.0649
21%	0.8264	0.6830	0.5645	0.4665	0.3855	0.3186	0.2633	0.2176	0.1799	0.1486	0.1228	0.1015	0.0839	0.0693	0.0573
22%	0.8197	0.6719	0.5507	0.4514	0.3700	0.3033	0.2486	0.2038	0.1670	0.1369	0.1122	0.0920	0.0754	0.0618	0.0507
23%	0.8130	0.6610	0.5374	0.4369	0.3552	0.2888	0.2348	0.1909	0.1552	0.1262	0.1026	0.0834	0.0678	0.0551	0.0448
24%	0.8065	0.6504	0.5245	0.4230	0.3411	0.2751	0.2218	0.1789	0.1443	0.1164	0.0938	0.0757	0.0610	0.0492	0.0397
25%	0.8000	0.6400	0.5120	0.4096	0.3277	0.2621	0.2097	0.1678	0.1342	0.1074	0.0859	0.0687	0.0550	0.0440	0.0352

TABLE - 2 : PRESENT VALUE OF AN ANNUITY OF RUPEE ONE

RATE	YEAR 1	YEAR 2	YEAR 3	YEAR 4	YEAR 5	YEAR 6	YEAR 7	YEAR 8	YEAR 9	YEAR 10	YEAR 11	YEAR 12	YEAR 13	YEAR 14	YEAR 15
5%	0.9524	1.8594	2.7232	3.5460	4.3295	5.0757	5.7864	6.4632	7.1078	7.7217	8.3064	8.8633	9.3936	9.8986	10.3797
6%	0.9434	1.8334	2.6730	3.4651	4.2124	4.9173	5.5824	6.2098	6.8017	7.3601	7.8869	8.3838	8.8527	9.2950	9.7122
7%	0.9346	1.8080	2.6243	3.3872	4.1002	4.7665	5.3893	5.9713	6.5152	7.0236	7.4987	7.9427	8.3577	8.7455	9.1079
8%	0.9259	1.7833	2.5771	3.3121	3.9927	4.6229	5.2064	5.7466	6.2469	6.7101	7.1390	7.5361	7.9038	8.2442	8.5595
9%	0.9174	1.7591	2.5313	3.2397	3.8897	4.4859	5.0330	5.5348	5.9952	6.4177	6.8052	7.1607	7.4869	7.7862	8.0607
10%	0.9091	1.7355	2.4869	3.1699	3.7908	4.3553	4.8684	5.3349	5.7590	6.1446	6.4951	6.8137	7.1034	7.3667	7.6061
11%	0.9009	1.7125	2.4437	3.1024	3.6959	4.2305	4.7122	5.1461	5.5370	5.8892	6.2065	6.4924	6.7499	6.9819	7.1909
12%	0.8929	1.6901	2.4018	3.0373	3.6048	4.1114	4.5638	4.9676	5.3282	5.6502	5.9377	6.1944	6.4235	6.6282	6.8109
13%	0.8850	1.6681	2.3612	2.9745	3.5172	3.9975	4.4226	4.7988	5.1317	5.4262	5.6869	5.9176	6.1218	6.3025	6.4624
14%	0.8772	1.6467	2.3216	2.9137	3.4331	3.8887	4.2883	4.6389	4.9464	5.2161	5.4527	5.6603	5.8424	6.0021	6.1422
15%	0.8696	1.6257	2.2832	2.8550	3.3522	3.7845	4.1604	4.4873	4.7716	5.0188	5.2337	5.4206	5.5831	5.7245	5.8474
16%	0.8621	1.6052	2.2459	2.7982	3.2743	3.6847	4.0386	4.3436	4.6065	4.8332	5.0286	5.1971	5.3423	5.4675	5.5755
17%	0.8547	1.5852	2.2096	2.7432	3.1993	3.5892	3.9224	4.2072	4.4506	4.6586	4.8364	4.9884	5.1183	5.2293	5.3242
18%	0.8475	1.5656	2.1743	2.6901	3.1272	3.4976	3.8115	4.0776	4.3030	4.4941	4.6560	4.7932	4.9095	5.0081	5.0916
19%	0.8403	1.5465	2.1399	2.6386	3.0576	3.4098	3.7057	3.9544	4.1633	4.3389	4.4865	4.6105	4.7147	4.8023	4.8759
20%	0.8333	1.5278	2.1065	2.5887	2.9906	3.3255	3.6046	3.8372	4.0310	4.1925	4.3271	4.4392	4.5327	4.6106	4.6755
21%	0.8264	1.5095	2.0739	2.5404	2.9260	3.2446	3.5079	3.7256	3.9054	4.0541	4.1769	4.2784	4.3624	4.4317	4.4890
22%	0.8197	1.4915	2.0422	2.4936	2.8636	3.1669	3.4155	3.6193	3.7863	3.9232	4.0354	4.1274	4.2028	4.2646	4.3152
23%	0.8130	1.4740	2.0114	2.4483	2.8035	3.0923	3.3270	3.5179	3.6731	3.7993	3.9018	3.9852	4.0530	4.1082	4.1530
24%	0.8065	1.4568	1.9813	2.4043	2.7454	3.0205	3.2423	3.4212	3.5655	3.6819	3.7757	3.8514	3.9124	3.9616	4.0013
25%	0.8000	1.4400	1.9520	2.3616	2.6893	2.9514	3.1611	3.3289	3.4631	3.5705	3.6564	3.7251	3.7801	3.8241	3.8593