

Roll No.....

Time allowed : 3 hours

Maximum marks : 100

Total number of questions : 6

Total number of printed pages : 8

NOTE : 1. Answer **ALL** Questions.

2. Tables showing the present value of ₹1 and the present value of an annuity of ₹1 for 15 years are annexed.

1. Comment on the following :

- (a) Financial sector performs basic economic function of intermediation through transformation mechanisms.
- (b) Project review is a very important aspect of the entire project life.
- (c) A firm having high current ratio may not necessarily be treated as being favourably placed as regards payment of its current liabilities.
- (d) Sharpe ratio is a risk adjusted measure of return to evaluate the performance of a portfolio.

(5 marks each)

Attempt all parts of either Q.No. 2 or Q.No. 2A

2. Distinguish between the following :

- (a) 'Forfaiting' and 'export factoring'.
- (b) 'Net net net lease' and 'update lease'.
- (c) 'Interest rate parity' and 'purchasing power parity'.
- (d) 'Call premium' and 'put premium'.

(4 marks each)

OR (Alternate question to Q.No. 2)

- 2A. (i) What are the risks and uncertainties in capital budgeting decisions ?
- (ii) Explain 'pecking order hypothesis' relevant to capital structure planning.
- (iii) Describe the meaning of 'pegging of currency'. Highlight the intermediate arrangements for determining exchange values of foreign currency.
- (iv) 'Reverse stock split' is generally an indication of financial difficulty. Elucidate.

(4 marks each)

Attempt all parts of either Q.No. 3 or Q.No. 3A

3. (a) ABC Chemicals Ltd. is considering two mutually exclusive proposals. Your advice is sought for choice between the two options under consideration :

- (i) Purchase of petrol truck
(ii) Purchase of a battery powered truck

	<i>Year</i>	<i>Petrol truck</i>	<i>Battery powered truck</i>
Purchase cost (₹)	0	1,50,000	2,50,000
Operating cost (₹)	1	24,000	12,000
	2	34,000	12,000
	3	29,000	12,000
	4	31,000	12,000
	5	—	12,000

Assume an investment incentive of 100% initial depreciation allowance and a 30% incidence of corporate tax. No depreciation is allowed on subsequent years. Taxes are promptly paid. A return of 10% after tax as investment incentives is required.

You are required to find out equivalent cost for two options.

(4 marks)

- (b) Sagar Ltd. has been in IT business for six years and enjoys a favourable market reputation. Corporate tax is 30%. They anticipated that the demand for IT solutions would increase considerably since many foreign firms are setting-up their BPO centres in India. For an expansion project, they propose to invest ₹22 crore to be funded by new debt and equity on 50:50 basis. Enquiries with merchant bankers reveal that funds can be available at following rates :

	<i>Rate</i>
Debt	
First ₹5 crore	10%
Next ₹5 crore	12%
All additional funds	15.72%
Equity	12%
Risk gradation by company	2% over cost of capital

You are required to compute the appropriate risk adjusted discount rate.

(4 marks)

- (c) Describe the tool that provides insights into whether a company is creating or destroying wealth.

(4 marks)

: 3 :

- (d) A group of new customers with 10% risk of non-payment, desires to establish business connection with you. The group desires one and a half months credit and is likely to increase the sales of your concern by ₹1,20,000 per annum. Cost of sales would be 80% of sales. Tax rate is 30% and required rate of return is 40% (after tax). Should the new business connection be established ? Give your decision with supporting calculations.

(4 marks)

OR (Alternate question to Q.No. 3)

- 3A. (i) Describe various tools of treasury management.

(4 marks)

- (ii) From the following given operating data, calculate the degree of operating leverage of the two companies :

	<i>ABC Ltd.</i>	<i>XYZ Ltd.</i>
Sales (₹)	40 lakh	50 lakh
Variable expense (<i>as % of sales</i>)	40%	30%
Fixed cost (₹)	10 lakh	20 lakh

Also, state which company has the greater business risk and why ?

(4 marks)

- (iii) Madhur Ltd., an Indian company has an export exposure of 100 lakh Yen value at December end. Yen is not directly quoted against Rupee. The current spot rates are $\text{INR/USD} = ₹63.60$ and $\text{JPY/USD} = 124.75$ Yen. In December end, it is estimated that Yen will be depreciated to 144 and Rupee to 65 against a Dollar.

You are required to calculate the expected loss if hedging is not done.

(4 marks)

- (iv) Diva Ltd. has 10 lakh equity shares outstanding at the end of accounting year 2014-15. The current market price of the shares is ₹150 each. The Board of directors of the company has recommended ₹8 per share as dividend. The rate of capitalisation appropriate to the risk class to which the company belongs is 12%.

Based on Modigliani-Miller approach, calculate the market price of the share if the recommended dividend is – (a) declared; and (b) not declared.

(4 marks)

4. (a) There are various sources of permanent working capital. Comment. (4 marks)
- (b) In a portfolio of the company, ₹2,00,000 have been invested in Asset-X which has an expected return of 8.5%, ₹2,80,000 in Asset-Y, which has an expected return of 10.2% and ₹3,20,000 in Asset-Z which has an expected return of 12%. What is the expected return for the portfolio ? (4 marks)

- (c) Saraswati Engineering Company is considering its working capital investment for the next year. Estimated fixed assets and current liabilities for the next year are ₹2.60 crore and ₹2.34 crore respectively. Sales and profit before interest and taxes (PBIT) depend on investment in current assets – particularly inventories and book debts. The company is examining the following alternative working capital policies :

<i>Working capital policy</i>	<i>Investment in current assets (₹ in crore)</i>	<i>Estimated sales (₹ in crore)</i>	<i>PBIT (₹ in crore)</i>
Conservative	4.50	12.30	1.23
Moderate	3.90	11.50	1.15
Aggressive	2.60	10.00	1.00

You are required to calculate the rate of return on total assets for each policy.

(4 marks)

- (d) ABC Ltd. has 10,000 shares of ₹7 each, ₹10,000, 12% debentures and ₹20,000 as short-term loan @10%. Tax rate for the company is 30%. Assume the cost of equity capital as 20%. Calculate weighted average cost of capital at book value.

(4 marks)

5. (a) A company has two alternatives for selecting a new machine to replace its existing machine. The cash flows under the two alternatives are as follows :

	<i>Machine-A (₹ in lakh)</i>	<i>Machine-B (₹ in lakh)</i>
Year 0 cash outflow	25	40
Year 1 cash inflow	Nil	10
Year 2 cash inflow	5	14
Year 3 cash inflow	20	16
Year 4 cash inflow	14	17
Year 5 cash inflow	14	15

: 5 :

You are required to appraise the two alternatives using net present value and profitability index methods.

The cost of capital of the company is 15%.

(8 marks)

- (b) Aman Ltd. is producing a single Product-X and presently commanding a market share of 15%. The following cost details are provided :

	₹	₹
Sales price		100
Less : Material	40	
Labour	20	
Overheads	<u>10</u>	<u>70</u>
Contribution		30
Less : Fixed cost		<u>20</u>
Profit		<u><u>10</u></u>

The current volume of sale of Product-X is 15,000 units. It has now been estimated that the market share can be increased up to 25% from next year for 3 years if the following promotional expenses are incurred in the corresponding previous year :

For Year-1	₹1,00,000
For Year-2	₹75,000
For Year-3	₹50,000

There will be an increase in fixed cost by ₹30,000 when production is increased from present level. The company wants to achieve 15% return and would apply discounted cash flow technique for evaluation.

- You are required to evaluate the impact of above situation on profitability when —
- Market share is increased by 25%; and
 - Market share is increased by 20%.

(8 marks)

6. A newly formed company has applied for a short-term loan to a commercial bank for financing its working capital requirements. Projected statement of profit and loss is as follows :

	₹
Sales (20% cash)	21,00,000
Less : Cost of goods sold	<u>15,30,000</u>
Gross profit	5,70,000
Less : Administrative expenses	1,40,000
Selling expenses	<u>1,30,000</u>
Profit before tax (PBT)	<u>3,00,000</u>
Less : Tax	<u>1,00,000</u>
Profit after tax (PAT)	<u><u>2,00,000</u></u>
Cost of goods sold has been derived as follows :	
Material	8,40,000
Wages and money expenses (one month arrear)	6,25,000
Depreciation	<u>2,35,000</u>
	17,00,000
Less : Stock (10% of finished goods)	<u>1,70,000</u>
	<u><u>15,30,000</u></u>

The figures given above relate only to the goods that have been finished and not to work-in-progress; goods equal to 15% of year's production (in terms of physical units) are in progress on an average requiring full materials and only 40% of other expenses. The company believes in keeping two months consumption of material in stock. Credit allowed to customers is 2 months. Selling expenses and administrative expenses are one month in arrears. Credit allowed by supplier is 1½ months.

You are requested by the bank to prepare an estimate of requirements of working capital for the company. Add 10% to your estimated figure to cover contingencies.

(16 marks)

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TABLE - 1 : PRESENT VALUE OF RUPEE ONE

RATE	YEAR	YEAR	YEAR	YEAR	YEAR	YEAR	YEAR	YEAR	YEAR	YEAR	YEAR	YEAR	YEAR	YEAR	YEAR	YEAR	YEAR	YEAR
	1	2	3	4	5	6	7	8	9	10	11	12	13	14	15	16	17	18
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	0.4580	0.4359	0.4146
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	0.3932	0.3700	0.3477
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	0.3385	0.3154	0.2931
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	0.2917	0.2690	0.2471
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	0.2513	0.2292	0.2080
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	0.2169	0.1954	0.1748
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	0.1873	0.1666	0.1467
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	0.1619	0.1420	0.1229
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	0.1401	0.1210	0.1027
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	0.1219	0.1044	0.0876
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	0.1059	0.0900	0.0750
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	0.0920	0.0770	0.0630
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	0.0800	0.0660	0.0530
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	0.0700	0.0570	0.0450
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	0.0610	0.0490	0.0380
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	0.0530	0.0420	0.0320
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	0.0460	0.0360	0.0270
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	0.0400	0.0310	0.0230
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	0.0350	0.0270	0.0200
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	0.0310	0.0240	0.0180
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	0.0270	0.0210	0.0160

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

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