2021

FINANCIAL MANAGEMENT — HONOURS

Paper : DSE-6.2A

Full Marks : 80

The figures in the margin indicate full marks.

Candidates are required to give their answers in their own words as far as practicable.

Group-A

Answer ***any four*** questions.

1. Discuss the important functions of financial management. 10

2. What do you mean by wealth maximization objective of a firm? How can it be achieved by the firm? Why is it considered superior to the profit maximization objective of the firm? 2+3+5

3. (a) What do you mean by time value of money? What are its reasons? 5

(b) X decides to invest ₹ 6,000 at the end of each year at the compound rate of interest of 12% p.a. for 8 years. What total amount he will get at the end of 8th year? [FVAF at 12% for 8 years 12·30] 5

4. (a) Calculate payback period from the following information:

Cost of machine: ₹ 1,00,000; Depreciation 10% p.a. under reducing balance method. Corporate tax rate 40%

Year	1	2	3	4	5
Expected PBT (₹ '000)	NIL	54	88	104	125

(b) What are the distinguishing features of capital budgeting decisions? 6+4

5. A firm is considering the proposal of buying a machine with installation cost of ₹ 5,00,000. The machine will have a useful life of 4 years after which it can be sold for ₹ 70,000. Depreciation is to be charged under straight line method. Additional working capital of ₹ 50,000 will be introduced. Profits before depreciation and tax are expected to be ₹ 1,72,000, ₹ 1,98,000. ₹ 2,18,000 and ₹ 1,80,000 in those four years. If applicable tax rate is 30%, calculate ARR of the project. 10

6. Discuss the various sources of finance to meet working capital requirement. 10

7. A firm has sales of ₹ 10,00,000, variable cost of ₹ 7,00,000 and fixed cost of ₹ 2,00,000. The company has debt capital of ₹ 3,00,000 at 10% rate of interest. Compute operating, financial and combined leverages. If the firm wants to double its earnings before interest and tax (EBIT), how much rise in sales would be required? 10

8. You are given the following information in respect of ABC Ltd.

Earning	₹ 1,00,000
Equity capital	5,000 shares of ₹ 10 each
Cost of capital	10%
Expected rates of return	(i) 9%, (ii) 10% and (iii)12%

Assuming that dividend pay-out ratios are 0%, 50% and 100% respectively, determine the effects of the different dividend policies on the share price of ABC Ltd. for the above mentioned three alternative levels of rate of return using Gordons's model. 10

Group-B

Answer ***any two*** questions.

9. (a) Discuss the relevance of cost of capital. What do you mean by implicit and explicit cost of capital? 5+5

(b) A company's share is currently quoted in the market at ₹ 30. The company paid a dividend of ₹ 5 per share last year and the investors expect a growth rate of 5% per year.

You are required to calculate (i) cost of equity share capital of the company and (ii) the market price per share, if the anticipated growth rate of dividend is 10%. 10

10. (a) What do you mean by EBIT-EPS Analysis? Discuss its importance in financing decision. 10

(b) Discuss the significance of operating leverage and financial leverage. 10

11. Following details are available from the management of BAS Ltd:

Particulars	**Amount per unit (₹)**
Raw materials	120
Direct labour	45
Overhead	90

The company wants to make 15% profit on sales price.

The following further particulars are available:

Raw materials are kept in stock, on average, for one month. Processing time can be taken as, on average, half a month; Finished goods in stock, on average, for 30 days. Credit enjoyed by BAS Ltd. in one month; Credit allowed is for two months; Average time-lag in payment of wages and overhead is one month. Cash in hand and at bank is desired to be maintained at ₹ 30,000. BAS Ltd. prefers to value debtors at sales value.

Compute the working capital required for BAS Ltd. with necessary assumptions to finance a level of activity of 24,000 units of production in the next year. 20

12. (a) SMB Ltd. has considered two projects with economic life of 6 years having following cash inflows after tax:

End of year	**1**	**2**	**3**	**4**	**5**	**6**	**Total (₹)**
Project 1	1,00,000	80,000	75,000	70,000	68,000	62,000	4,55,000
Project 2	62,000	68,000	70,000	75,000	80,000	1,00,000	4,55,000

As the total cash inflows are identical and investment amount is ₹ 3,30,000 for both the projects, the management of SMB Ltd. has decided to go for any one of the given projects. Do you support their decision? Justify your answer.

The post-tax cost of capital of SMB Ltd. is calculated as 10%, and the required discounting factors are given below:

Year	**1**	**2**	**3**	**4**	**5**	**6**
DF @ 10%	0·909	0·826	0·751	0·683	0·621	0·564

(b) Project A and Project B are the two mutually exclusive projects under consideration. While Project A has a higher NPV, Project B has a higher IRR. Which project should be selected and why? 12+8

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