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Code No: 721CM

JAWAHARLAL NEHRU TECHNOLOGICAL UNIVERSITY HYDERABAD
MBA II Semester Examinations, December - 2019
FINANCIAL MANAGEMENT

Time: 3hours **Max.Marks:75**

Note: This question paper contains two parts A and B.
Part A is compulsory which carries 25 marks. Answer all questions in Part A. Part B consists of 5 Units. Answer any one full question from each unit. Each question carries 10 marks and may have a, b, c as sub questions.

PART - A **5 × 5 Marks = 25**

1.a) What are the principal activities of finance manager? [5]

b) What are the problems in determining cost of capital? What is the relevance of cost of capital to capital budgeting decisions? [5]

c) What is composite leverage? Explain briefly. [5]

d) What are the considerations to be kept in mind when company issues
i) bonus shares ii) right shares. [5]

e) What are the various costs associated with receivables? [5]

PART - B **5 × 10 Marks = 50**

2. The probability distribution of expected future returns are as follows:

Probability	Return on shares (percentages)	
	X	Y
0.1	(16)	(18)
0.2	2	12
0.4	8	18
0.2	12	32
0.1	20	40

Compute the a) standard deviation of expected returns of each share and b) coefficient variation. Which share is more risky and why? [10]

OR

3. To supplement your planned retirement after 30 years, you estimate that you need to accumulate Rs.22,00,000 by the end of 30 years from today. You plan to make equal end-of-the year deposit into an account paying 6% annual interest. Calculate the amount to be deposited each year. [10]

4. A plastic manufacturing company is considering replacing an older machine which was fully depreciated for tax purposes with a new a machine costing Rs.40,000. The new machine will be depreciated over its eight year life. It is estimated that the new machine will reduce labour costs by Rs.8000 per year. The management believes that there will be no change in other expenses and revenues of the firm due to the machine. The company requires an after tax return on investment of 10 percent. Its rate of tax is 35 percent. The company's income statement for the current year is given for other information.

Income statement for the current year

Sales		Rs. 5,00,000
Costs		
Materials	Rs. 1,50,000	
labour	2,00,000	
Factory and administrative	40,000	
Depreciation	40,000	4,30,000
Net income before taxes		70,000
Taxes (0.35)		24,500
Earnings after taxes		45,500

Should the company buy new machine? You may assume the company follows straight line method of depreciation and the same is allowed for tax purposes. [10]

OR

5. From the following information supplied to you, determine the appropriate weighted average of cost of capital, relevant for evaluating long term investment projects of the company.

Cost of equity: 12 percent
After tax cost of long term debt: 7
After tax cost of short term debt: 7

Source of capital	Book value (Rs.)	Market value (Rs.)
Equity	5,00,000	7,50,000
Long term debt	4,00,000	3,75,000
Short term debt	1,00,000	1,00,000
Total	10,00,000	12,25,000

[10]

6. AB Ltd., provides you the following information:

Profit	Rs. 3,00,000
Less: interest on debentures(0.12)	60,000
Earnings before taxes	2,40,000
Less: taxes (0.35)	84,000
Earnings after taxes	Rs.1,56,000
Number of equity shares (Rs. 10 each)	*40,000*
Earnings per share	3.9
Ruling market price	39
P/E ratio	10

The company has undistributed reserves Rs.6,00,000. It needs Rs.2,00,000 for expansion which will earn the same rate as funds already employed.
You are informed that a debt-equity ratio higher than 35 percent will push the P/E ratio down to 8 and raise the interest rate on additional amount borrowed to 14 percent.
You are required to ascertain the probable price of equity share if the additional funds are raised as debt. [10]

OR

7. Give a critical appraisal of the traditional approach and the Modigliani-Millers approach to the problem of capital structure. [10]

8. The earnings per share of a company are Rs. 10 and the rate of capitalization applicable to it is 10%. The company has before it, the options of adopting a payout of 20% or 40% or 80%. Using Walter's formula, compute the market value of the company's share if the productivity of retained earnings is a) 20% b) 10% and c) 8%. What inference can be drawn from the above exercise? [10]

OR

9.a) What is meant by preemptive right of the shareholders?
b) What are the sources of bonus issue? [5+5]

10. As a part of the strategy to increase sales and profits, the sales manager of accompany proposes to sell goods to a group of new customers with 10% risk of nonpayment. The group would require one and a half months credit and is likely to increase sales by Rs.1,00,000 p.a. Production and selling expenses amount to 80% of sales and the income tax rate is 50%.The company's minimum required rate of return after tax is 25%. Should the sales manager's proposal be accepted? Also find the degree of risk of nonpayment that the company should be willing to assume if the required rate of return after is 30%. [10]

OR

11. Mr. Krishnan wishes to commence a new trading business and gives the following information:
i) The total estimated sales in a year will be Rs.12,00,000
ii) His expenses are estimated as fixed expenses of Rs.2,000 per month plus a variable expenses equal to 5% of his turnover.
iii) He expects to fix a sales price for each product which will be 25% in excess of his cost of purchase.
iv) He expects to turnover his stock four times in a year.
v) The sales and purchases will be evenly spread throughout the year. All sales will be for cash but he expects one month's credit for purchases.
Calculate
a) His estimated profit for the year and
b) his average working capital need. [10]

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