PG – 993

II Semester M.B.A. Degree Examination, June/July 2015
(CBCS Scheme)
2.5 : FINANCIAL MANAGEMENT

Time : 3 Hours Max. Marks : 70

SECTION – A

Answer **any five** questions. **Each** question carries **five** marks. The answer must not exceed **250** words. **(5x5=25)**

1. Comment on the emerging role of finance manager in India.
2. Explain the determinants of working capital.
3. Discuss the various methods of calculating cost of equity.
4. Explain briefly the long term sources of finance available to business.
5. A company has 20,00,000, 6% debentures outstanding today. The company has to redeem the debentures after 5 years and establishes a sinking fund to provide funds for redemption. Sinking fund investments can earn @ 10% p.a. The investments are made at the end of each year. What annual payments must the firm make to ensure that the needed 20,00,000 is available on the designated date ?
6. From the following extracts of financial data prepare income statement for Radiant Ltd. and comment on its financial performance :

Variable cost (% of sales)	–	65
Interest burden	–	200
Degree of operating leverage	–	4%
Degree of financial leverage	–	3%

Tax rate @ 35%.

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7. The management of Royal industries has called for a statement showing the working capital needs to finance a level of activity of 1,80,000 units of output for the year. The cost structure for the company's product line the above mentioned activity level is detailed below :

	Cost per Unit (Rs.)
Raw materials	20
Direct labour	5
Overheads	15
	40
Profit	10
Selling price	50

Additional Information :

a) Minimum desired cash balance is Rs. 20,000.

b) Raw materials are held in stock, on an average, for 2 months.

c) Work-in-progress (assume 50% completion stage) will approximate to half month's production.

d) Finished goods remain in warehouse, on an average, for a month.

e) Suppliers of materials extend a month's credit and debtors are provided two month's credit; cash sales are 25% of total sales.

f) There is a time lag in payment of wages of a month and half-a-month in case of overheads.

From the above data, you are required to

1) Prepare a statement showing working capital needs;

SECTION – B

Answer **any three** questions. **Each** question carries **ten** marks. The answer must not exceed **500** words. **(3x10=30)**

8. Discuss the Walter's model of dividend policy. What are its implications ?

9. What is capital structure ? Explain the factors that influence capital structure.

10. Three financing plans are available for Texas Manufacturing which needs Rs. 10,00,000 for construction of a new plant. Texas wants to maximize EPS. Currently the equity share is selling for Rs. 30 per share. The EBIT resulting from the plant operation is Rs. 1,50,000 p.a. The marginal tax rate is 30%. Money can be borrowed at the rates indicated below :

Upto Rs. 1,00,000 @ 10%

Over Rs. 1,00,000 to Rs. 5,00,000 @ 14%

Over Rs. 5,00,000 @ 18%.

The three financing plans are :

Plan A – Use 1,00,000 debt; expected EBIT Rs. 2,50,000

Plan B – Use 3,00,000 debt ; expected EBIT Rs. 3,50,000

Plan C – Use 6,00,000 debt ; expected EBIT Rs. 5,00,000.

Determine EPS for these three plans and indicate the plan which results in highest EPS.

11. Alpha Ltd. has the following capital structure as per its B/S as at 31-3-2015 :

	in lakhs
Equity share capital (fully paid share of Rs. 10 each)	8
18% Preference share capital	
(fully paid share of Rs. 100 each)	6
Reserves and surplus	2
12.5% debentures (fully paid debenture of Rs. 100 each)	16
12% term loans	8
	40

Additional Information :

a) The current market price of the company's share is Rs. 64.25. The prevailing default risk free interest rate on 10 year GOI treasury bonds is 5.5%. The average market risk premium is 8%. The beta of the company is 1.1875.

b) The Preference shares of the company which are redeemable after 10 years are currently selling at 90 per preference share.

c) The debentures of the company which are redeemable after 5 years are currently quoted at 95 per debenture.

d) The corporate tax rate is 30%.

Required :

Calculate weighted average cost of capital using

a) book value weights

b) market value weights.

SECTION – C

Case Study (Compulsory) : **(1×15=15)**

12. Karnataka Diagnostics a mid sized medical service company wished to invest in new medical diagnostic technology. The management is considering the following two projects which it is considered will meet Karnataka requirement :

	(Million)	
	Project 1	**Project 2**
Initial cash outlay	160	100
Net cash inflows :		
Year 1	30	30
Year 2	40	30
Year 3	50	30
Year 4	60	30
Year 5	70	30

Assume cost of capital as 10%.

a) Determine payback period, NPV, PI and IRP.

b) Indicate which project would you recommend ?

c) Discuss briefly any non-financial factors which Karnataka Diagnostics should consider ?