Code No: MB1621/R16

MBA II Semester Regular Examinations, May-2017

Financial Management

Time: 3 Hours **Max. Marks: 60**

Answer Any **FIVE** *Questions*
All Questions Carry Equal Marks
Question No. 8 is Compulsory

1. a What is finance function? What are its objectives? 8
   b What major decisions are required to be taken in finance. 4

2. a What is the importance of Cost of capital? Discuss the problems in determining it? 6
   b The financial plans are being considered by ABC Ltd., which requires Rs.10,00,000 for construction of a new plant. It wants to maximize the EPS and the market price of the share is Rs.30. It has a tax rate of 50% and debt financing can be arranged as follows: Up to Rs. 1,00,000@ 10%. From Rs. 1,00,000 to Rs.5,00,000 @14% and over Rs.5,00,000@18%. The three financing plans and the corresponding EBIT are as follows: 6
   Plan I: Rs.1,00,000 debt ; expected EBIT Rs.2,50,000
   Plan II: Rs.3,00,000 debt ; expected EBIT Rs.3,50,000
   Plan III: Rs.6,00,000 debt ; expected EBIT Rs.5,00,000
   Find out the EPS for all the three plans and suggest which plan is better from the point of view of the company.

3. a Define Capital Structure. What should generally be the features of an appropriate Capital structure. 6
   b From the following selected data, determine the value of the firms, P and Q belonging to the homogeneous risk class under (a) the Net Income approach and (b) the Net operating Income approach. 6

	Firm P	**Firm Q**
EBIT	Rs.2,25,000	Rs.2,25,000
Interest at 15%	75,000	-

   Equity capitalization rate20%
   Corporate tax rate 50%
   Which of the two firms has an optimal capital structure under the (i) NI approach, and (ii) NOI approach.

4. a Distinguish between Operating Leverage and Financial Leverage. 4
   b Calculate operating leverage and financial leverage from the following data: 8

Sales (1,00,000 Units)	Rs.2,00,000
Variable cost per unit	Rs.0.70
Fixed cost	Rs.65,000
Interest charges	Rs.15,000

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5. a What is capital Budgeting? Examine its need and importance? 6

b XYZ Co. is considering the purchase of one of the following machines., whose relevant data are as given below: 6

		Machine X	Machine Y
Estimated life		3 years	3 years
Capital cost		Rs.90,000	RS.90,000
Earnings after tax	Year 1	40,000	20,000
	Year 2	50,000	70,000
	Year 3	40,000	50,000

The company follows the straight-line method of depreciation; the estimated salvage Value of both the types of machines is zero. Show the most profitable investment based on

(i) Pay back period
(ii) Net present value assuming a10% cost capital.

6. a Discuss the various forms of Dividends? 6

b The earnings per share of a company are Rs.16. The market rate of discount applicable to the company is 12.5%. Retained earnings can be employed to yield a return of 10%. The Company is considering a pay-out of 25%, 50% and 75%. Which of these would maximize the wealth of shareholders? 6

7. a What is the importance of working capital in a business? 6

b The following information has been submitted by a borrower. 6

Expected level of production 1,20,000 units
Raw materials to retain in stock on an average 2 months
Processing period for each unit of product(consisting of 100% of raw material, wages and overheads) 1 month
Finished goods remain in stock on an average 3 months
Credit allowed to the customers from the date of despatch 3 months
Expected ratios of cost to selling price:

i. Raw materials- 60%
ii. Direct wages- 10%
iii. Overheads- 20%
iv. Selling price per unit Rs.10
v. Expected margin on sale 10%

You are required to estimate the working capital requirements of the borrower.

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8. **Case study:**
Based on the following information prepare a cash budget for ABC Ltd. 12

	1st Quarter	2nd Quarter	3rd Quarter	4th Quarter
Opening cash balance	Rs.10,000			
Collection from customers	Rs.1,25,000	Rs.1,50,000	Rs.1,60,000	Rs.2,21,000
Payments:				
Purchase of materials	20,000	35,000	35,000	54,200
Other expenses	25,000	20,000	20,000	17,000
Salary and wages	90,000	95,000	95,000	1,09,200
Income tax	-	-	-	-
Purchase of Machinery	-	-	-	20,000

The company desires to maintain a cash balance of Rs.15,000 at the end of the each quarter. Cash can be borrowed or repaid in multiples of Rs.500 at an interest of 10% per annum. Management does not want to borrow cash more then what is necessary and wants repay as early as possible. In any event, loans cannot be extended beyond four quarters. Interest is computed and paid when repayment is made at the end of the quarter.

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