LOYOLA COLLEGE (AUTONOMOUS), CHENNAI – 600 034

M.Com. DEGREE EXAMINATION - **COMMERCE**

FIRST SEMESTER – **NOVEMBER 2013**

CO 1807/4800 - FINANCIAL MANAGEMENT

Date : 05/11/2013 Dept. No. Max. : 100 Marks
Time : 1:00 - 4:00

Part – A

Answer ALL Questions **10 x 2 = 20**

1. Define Financial Management
2. How do you interpret Financial Leverage?
3. Write a note on Net Income approach for Capital Structure.
4. Write the formula for Redeemable Debt.
5. Explain the term ‘ Indifferent point ‘
6. Illustrate ARR?
7. How for is Lock Box system useful to Cash Management.
8. What is present value of cash inflow of Rs.1, 000 receivable after 10 years at 6% interest rate?
9. A Company has 15% perpetual debt of Rs. 1, 00,000 (face value Rs.1, 000 each). The tax rate is 35% determine the cost of debt (Kd) assuming a) debt is issued at par, b) issued at 10% discount.
10. What will be the future value of Rs. 1,000 deposits every year at 10% interest, at the end of 5 years?

PART – B

Answer any Five Questions: **5 x 8 = 40**

11. Discuss all factors affecting Dividend Policy?
12. Critically analyze the Profit maximization and Wealth maximization.
13. Classify the types of Lease Agreements?
14. From the following details calculate all leverages and interpret the results.

Particulars	**A**	**B**	**C**
Output(units)	60,000	15,000	1,00,000
Selling Price(Rs.)	1	3	0.5
Fixed Cost	7,000	14,000	15,000
Variable Cost	0.20	1.50	0.02
Interest	4,000	8,000	10,000
Preference dividend	-	-	5,000
Tax rate	50%	50%	50%

15. A Ltd. is considering in purchasing of a machine for which two models X and Y are available. The estimated cash inflow and certainty equivalent are as follows :-

	Machine X		Machine Y	
Year	Cash inflow	Certainty equivalent	Cash inflow	Certainty equivalent
0	-30,000	1	-40,000	1
1	15,000	.95	25,000	.9
2	15,000	.85	20,000	.8
3	10,000	.70	15,000	.7
4	10,000	.65	10,000	.6

Risk – free discount rate is 5%.Which machine will you choose? Give reasons.

16.From the following data calculate the Operating Cycle in days:

	Rs.
Average Debtors	4, 80,000
Raw Materials Consumed	44, 00,000
Total Production Cost	100, 00,000
Total Cost of Sales	105, 00,000
Sales	160, 00,000
Average stock of RM	3, 20,000
Average Stock of WIP	3, 50,000
Average Stock of Finished Goods	2, 60,000
Creditors Payment Period	16 days

17. The present credit terms of A Ltd are 1/10 net 30. Its sales are 1.2 crores and its average collection period is 24 days. The purchase value ratio is 20% and cost of capital is 15%. The proportion of sales on which the customer currently allowed sales discount is 30%.
A Ltd wants to revise discount rates to 2/10 net 30. This will increase sales by 12,00,000,and to reduce average collection period to 16 days and increas the proportion of discount sale to 70%.Advice the company.

18. ABC LTD is considering the following credit policy alternatives.

	OPTIONS		
	I	II	III
Credit Period (days)	30	40	60
Sales (Rs. In Lakhs)	10	11	12
Bad Debts (% of sales)	5%	3%	6%
Cost of credit administration (Rs,in lakhs)i.e Admin.Exp	0.2	0.22	0.25
Average collection period (days)	45	50	70

The PV Ratio is 40%. The firm requires 20% of return on investment.

Suggest a suitable credit policy for the Firm.

PART – C

Answer any Two Questions **2 x 20 = 40**

19. AB ltd gives you the following figures

EBIT	3,00,000
Less: 12 % Debenture Interest	60,000

	2,40,000
Less: Income tax @ 50%	1,20,000
EAT	1,20,000

No. of Equity shares = 40000

$$EPS = \frac{120000}{40000} = \text{Rs } 3 \text{ per share.}$$

Market price per share = Rs.30

$$\text{Price Earning Ratio (PE)} = \frac{\text{Market Price Per share}}{\text{EPS}} = \frac{30}{3} = 10$$

The company has undistributed reserves of Rs.600000 It requires Rs.200000 for expansion. This amount will earn the same rate of return on funds employed as it is earned now.You are informed that the Debt-Equity ratio = (Debt/ Debt + Equity) higher than 35% will reduce the PE ratio to 8 and raise the interest rate on additional funds burrowed to 14%.The company would prefer to raise the entire funds required through equity or through debt. Which would you recommend?

20. S Ltd. has the following book value of capital structure.

	Rs.
Equity capital (Rs.10 each)	100 lakhs
11% pref. share capital (Rs.100 each)	10 "
Retained earnings	120 "
13.5% Debentures (Rs.100 each)	50 "
12% Term loans	80 "
Total	360 "

(1) The next expected_dividend per share is Rs.1.5. The Dividend per share expected to grow at 7%. The market price per share is Rs.20.
(2) Preference shares are redeemed at par after 10 years currently selling at Rs.75/-
(3) Debentures are redeemable at par after 6 years is currently selling at Rs.80.
(4) The tax rate is 50%

Calculate weighted average COC using book value and market value as weights.

21. A project requires investment of Rs.1,00,000 are the working capital of Rs. 20,000 at the end of the first year. The project has a life of 5 years and the scrap value of Rs.20,000.

The projects yields the following profits before tax :

Year	Profit before Tax (PBT) Rs.
1	20,000
2	40,000
3	60,000
4	50,000
5	30,000

Calculate

(i) Pay back period (PBP)

(ii) Average Rate of Return (ARR).
(iii) Net Present Value (NPV) and
(iv) Profitability Index PI.
(v) Discounted pay back period.
Assume cost of capital is 10% and tax @ 50%

22. A ltd. Produces 120000 units p.a. Its percentage of cost to selling price: Raw materials 60%, Wages 10%, and OHS 20%. Selling price Rs. 5 per unit.
Raw materials in stock for 2 months.
WIP in stock for 1 month.
Finished Goods in stock for 3 months.
Creditors allow 2 months credit and debtors get 3 months credit.
Wages and OHS are paid on the first of each month for the previous month.
Cash in hand Rs. 40000.
Calculate the amount of Working capital.