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TEST-3 EXAMINATION- MAY- JUNE -2016

B.Tech (IV) Semester – All Branches

COURSE CODE: 10B11PD411 MAX. MARKS: 35

COURSE NAME: FINANCIAL MANAGEMENT

COURSE CREDITS: 03 MAX. TIME: 2 HRS

Note: All questions are compulsory. Carrying of mobile phone during examinations will be treated as case of unfair means. Assume suitable data, if necessary.

1. Briefly answer the following questions (max 100 words) **(2+3+2+3=10)**

a) "Agency problem may affect the profitability of a firm". Comment.
b) Discuss the conditions under which a preference shareholder may get voting rights in a firm.
c) "Cost of retained earnings may be treated as equivalent to cost of equity". Explain.
d) A deposit carries an interest rate of 10% per annum with quarterly compounding. The effective rate of interest would be 40% because you would receive 10% every quarter, four times a year. What is wrong with the statement? What would be the correct effective rate of interest? Explain with the help of suitable calculations.

2. Discuss in detail about the Gordon Model of dividend. How is it better than the Walter's Model of dividend? **(2)**

3. Briefly explain the concept of leverages. Discuss different types of leverages along with their significance? **(2)**

4. Ravi Enterprises needs Rs 50,00,000 for the installation of a new factory. The new factory is expected to yield an annual EBIT of Rs 10,00,000. In choosing a financial plan, the firm has an objective of maximizing earnings per share. It is considering the possibility of issuing equity shares and remaining amount by raising debt of Rs 5,00,000 or Rs 20,00,000 or Rs 30,00,000. The current market price per share is Rs 300/- and is expected to drop to Rs 250/- if the funds are borrowed in excess of Rs 20,00,000. Funds can be raised at the following rates:
Upto Rs 5,00,000 @ 10% **(5)**
Over Rs 5,00,000 to Rs 20,00,000 @ 15%
Over Rs 20,00,000 @ 20%.

Assuming a tax rate of 50%, advise which financial plan should the company adopt?

P.T.O.

5. Calculate the level of EBIT at which the indifference point between the following financing alternatives will occur:

   a) Ordinary share capital of Rs 30,00,000 OR ordinary shares capital of Rs 15,00,000, 13% preference share capital of Rs 6,00,000 and 15% debentures of Rs 9,00,000.
   b) Ordinary share capital of Rs 18,00,000 and 15% debentures of Rs 12,00,000 OR ordinary shares capital of Rs 12,00,000, 13% preference share capital of Rs 6,00,000 and 15% debentures of Rs 12,00,000.
   c) Ordinary share capital of Rs 24,00,000 and 13% preference share capital of Rs 6,00,000 OR ordinary shares capital of Rs 12,00,000, 13% preference share capital of Rs 6,00,000 and 15% debentures of Rs 12,00,000.

(1+2+2=5)

Assume face value of equity share is Rs 100/- and tax rate is 25%.

6. Prepare a working capital forecast of Neelaksh Limited with the given information: total capacity of production is 8,00,000 units while capacity utilization is 70%. Selling price per unit is Rs 50/- and profit per unit is 20%. Raw materials and overheads constitute of 50% and 20% of total production costs. Holding period for raw materials, WIP and finished goods are 2 months, 3 months and 1.5 months respectively. It is assumed that WIP consumes 50% of production cost. Credit availed by the company is 3 months while credit given by the company is 2 months. Lag in payment of wages and overhead is 1 month and half month respectively. The company wants to maintain a cash balance of Rs 1,00,000/- and a contingency of 15%.
Prepare a schedule of working capital forecast along with the relevant calculations. **(5)**

7. Prakhar Enterprises is planning a major investment to expand its business into different markets. It has prepared a projected cash flow for next eight years as follows:

(in Rs lakhs)

Year	0	1	2	3	4	5	6	7	8
CFAT	-250	58	165	385	-250	125	100	175	150

Calculate: **(2+3+1=6)**

   a) NPV of the project
   b) MIRR.

Should the project be accepted using NPV or MIRR or both the approaches? (Assume cost of capital is 10%).