

**M.B.A DEGREE EXAMINATIONS: JULY 2010**

Third Trimester

**MBA517: FINANCIAL MANAGEMENT**

**Time: Three Hours**

**Maximum Marks: 100**

**Answer all the Questions:**

**PART A (1 x 20 = 20 Marks)**

**1. Case Study:**

B Ltd., needs Rs. 10, 00, 000 for expansion. The expansion is expected to yield annual EBIT of Rs. 160000. In choosing a financial plan, AB Ltd has an objective of maximizing EPS. It is considering the possibility of issuing equity shares and raising debt of Rs. 1, 00, 000 or Rs. 4, 00, 000 or 6,00,000. The current market price per share is Rs.25 and is expected to drop to Rs. 20 if the funds are borrowed in excess of Rs. 5, 00, 000. Funds can be borrowed at the rates indicated below:

- (a) Upto Rs. 1,00,000 @ 8%
- (b) Over Rs. 1,00,000 upto Rs. 5,00,000 @ 12%
- (c) Over Rs. 5,00,000 @ 18%

Advise the management in selecting a best alternative. Assume tax rate @ 50%.

**PART B (10 x 2 = 20 Marks)**

2. Comment on the emerging role of the Finance Manager in India.
3. What is time value of money?
4. State any two limitations of pay back period method of capital budgeting.
5. How is the cost of a specific source of finance calculated?
6. Brief the relationship between EBIT & EPS.
7. Give the formula of Watler's Dividend Model.
8. Define operating cycle.
9. What is a Commercial Paper?
10. What are the various sources of long term finance?
11. Define lease.

**PART C (4 x 15 = 60 Marks)**

12. (a) (i) What are the basic financial decisions? How do they involve risk- return trade off? (8)

- (ii) Briefly describe the reasons why profit / EPS maximization fail to be consistent with wealth maximization. (7)

**(OR)**

- (b) (i) Under what circumstances do the NPV and IRR methods differ? Which method would you prefer and why? (8)

- (ii) Two projects have been suggested to H Co. Ltd., The after-tax cash flows for each are tabulated below. If the firm's cost of capital is 12%, rank them in order of profitability by using PI method. The present value of Re. 1 @ 12% for the first four years are .893., .797 .712 and .636 respectively. (7)

After Tax Cash Flows

Period	0	1	2	3	4
Project A	- Rs. 18,000	+6,500	+6,500	+6,500	+6,500
Project B	- Rs. 30,000	+6,000	+10,000	+12,000	+16,000

13. (a) Explain the different methods of computing cost of capital with suitable examples.

**(OR)**

- (b) (i) Explain Gordon's dividend growth model with an example (8)

- (ii) ABC has a total investment of Rs. 5, 00,000 in assets and 50,000 outstanding ordinary shares at Rs. 10 per share (par value). It earns a rate of 15% on its investment and has a policy of retaining 50% of the earnings. If the appropriate discount rate of the firm is 10%, determine the price of its share using Gordon's model. What shall happen to the price of the share if the company has a payout of 80% or 20% (7)

14. (a) What are the stages of operating cycle? How would you calculate them? Illustrate with a suitable example.

**(OR)**

- (b) (i) Explain credit policy variables. (5)

- (ii) The proforma cost sheet of a company provides the following data:

Cost per unit	
Raw material	: Rs. 52.00
Direct labour	: Rs. 19.50
Overheads	: <u>Rs. 39.00</u>
Total Cost per Unit	: Rs. 110.50
Profit	: <u>Rs. 19.50</u>
Selling price	: <u>Rs. 130.00</u>

The following is the additional information available:

Average raw material in stock: one month, average material in process; half a month. Credit allowed by suppliers: one month; credit allowed to debtors: two months. Time lag in payment of wages: one and a half weeks and overheads one month. Stock of finished goods one month. One-fourth of sales are on cash basis. Cash balance is expected to be Rs. 1, 20,000. You are required to prepare a statement showing the working capital needed to finance a level of activity of 70,000 units of output. You may assume that production is carried on evenly throughout the year and wages and overheads accrue similarly. (10)

15. (a) (i) What is an ordinary share? How does it differ from a preference share and a debenture? Explain its most important features. (8)

(ii) Explain the advantages and disadvantages of preference share to the company.(7)

**(OR)**

(b) (i) Explain the different types of leasing? (8)

(ii) What is the hire purchase financing? How does its differ from the lease financing? (7)

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