

QUESTION 2015

GROUP – A

(Multiple Choice Type Questions)

1. Choose the correct alternatives for any ten of the following:
 - i) The CAPM Model calculates the cost of equity shares by taking into consideration
 - a) Risk free rate of return
 - b) Beta coefficient for measuring market risk
 - c) Expected returns on market as a whole
 - ✓d) all of these

- ii) In deciding the appropriate level of current assets for the firm, Management is considered with
- a) A trade-off between profitability and risk
 - b) A trade-off between liquidity and marketability
 - c) A trade-off between equity and debt
 - ✓d) A trade-off between short terms versus long-term borrowing
- iii) The Dividend Irrelevance Model was propounded by
- a) Walter
 - b) Gordon
 - c) Graham and Dodd
 - ✓d) Modigliani and Miller
- iv) Which of the following is not a motive of holding cash?
- a) Transaction Motive
 - b) Precautionary Motive
 - ✓c) Revenue Motive
 - d) Speculative Motive
- v) Which of the following is not a Capital Budgeting Technique?
- ✓a) Cost Comparison Method
 - b) Pay-back period Method
 - c) Internal rate of return Method
 - d) Profitability index Method
- vi) The overall cost of Capital is also known as
- a) Marginal Cost of Capital
 - b) Variable Cost of Capital
 - ✓c) Weighted Average Cost of Capital
 - d) Specific Cost of Capital
- vii) To increase a given present value, the discount rate should be adjusted
- a) Upward
 - ✓b) Downward
 - c) None of these
 - d) Cannot be determined
- viii) Time value of money explains that
- ✓a) A unit of money received today is worth more than a unit received in future
 - b) A unit of money received today is worth less than a unit received in future
 - c) A unit of money received today and at some other time in future is equal
 - d) None of these
- ix) A student takes a loan of Rs. 50,000/- from SBI. The rate of interest being charged by SBI is 10% per annum. What should be the amount of equal annual installment if he wishes to pay it back in 5 installments & 1's installment he will pay at the end of year 5?
- a) Rs. 11,000/-
 - b) Rs. 19,310/-
 - c) Rs. 15,000/-
 - ✓d) None of these
- x) Issue of 12% preference shares will _____ debt-equity ratio of a corporate enterprise.
- ✓a) decrease
 - b) increase
 - c) remain constant
 - d) none of these
- xi) Acid Test ratio can be expressed as –
- a) Current Assets/Liquid Liabilities
 - b) Stock/Debtors
 - c) Fixed Assets/Capital
 - ✓d) Current assets-stock/current Liabilities-Bank overdraft.

xii) According to the traditional approach of capital structure, what is the effect increase in degree of leverage on the valuation of the firm?

a) Increases

b) Decreases

c) Remains unaffected

✓d) Increases first then decreases

GROUP – B

(Short Answer Type Questions)

2. Why do financial managers take financing and investment decisions?

See Topic: FINANCIAL MANGEMENT, Short Answer Type Question No. 5.

3. State the indifference point in EBIT-EPS analysis. How is it measured?

See Topic: CAPITAL STRUCTURE, Short Answer Type Question No. 6.

4. State the rationale behind the use of weighted average cost of capital over specific cost of capital in evaluating a project?

See Topic: COST OF CAPITAL, Short Answer Type Question No. 10.

5. Narrate the situations when a company needs to have capital budgeting decisions.

See Topic: CAPITAL BUDGETING, Short Answer Type Question No. 8.

6. Sun Ltd. issued 10,000, 11% Debenture of Rs. 100 each. The flotation cost was @2% on issue price. The debentures will be redeemed at a premium of 5% after 5 years. The tax rate applicable to the company is 30%. Compute the cost of debentures.

See Topic: COST OF CAPITAL, Short Answer Type Question No. 11.

GROUP – C

(Long Answer Type Questions)

7. X Ltd. has a share capital of Rs. 2,00,000 divided into shares of Rs. 10 each. The present EBIT stands at Rs. 80,000 per annum. It has a major expansion programmed requiring an investment of another Rs. 1,00,000. The management is considering the following alternatives for raising the amount.

i) Issue of 10,000 equity shares of Rs. 10 each

ii) Issue of 10,000, 12% preference shares of Rs. 10 each

iii) Issue of 10% Debentures for Rs. 1,00,000.

You are required to calculate the effect of the above method of financing on EPS if EBIT increases by Rs. 20,000.

See Topic: CAPITAL STRUCTURE, Long Answer Type Question No. 6.

8. SDF Ball bearing is an SME firm which supplies light ball bearing to large industries.

From the following information prepare a statement showing the estimated working Capital requirement.

(i) Projected annual sales 36,000 units

(ii) Analysis of sales:

Raw material	Rs. 6 p.u
Labour	Rs. 4 p.u
Overhead	Rs. 3 p.u
Profit	Rs. 2 p.u
Selling Price	Rs. 15 p.u

iii) Additional Information:

- Raw materials in stock 1 month
- Production process 2 months
- Finished goods in store 3 months
- Credit allowed to debtors 4 months
- Credit allowed by suppliers 2 months
- Monthly wages and expenses are paid twice on 1st and 16th of each month.
- Production is carried on evenly during the year and expenses and wages accrue similarly.

See Topic: MANAGEMENT OF WORKING CAPITAL, Long Answer Type Question No. 12.

9. Sum Traven Ltd. has the following capital structure.

Type of Capital	Amount
Equity capital (1 lakh shares @ Rs. 10 each)	Rs. 10 lakhs
11% preference capital (1000 shares @Rs. 100 each)	Rs. 1 lakhs
Retained earning	Rs. 12 lakhs
13.5% debentures (5000 debentures @ Rs 100 each)	Rs. 5 lakhs
12% term loan	Rs. 8 lakhs
Total	Rs. 36 lakhs

- The expected dividend on equity share is Rs. 1.50 which is expected to grow @ 7%. The market price of the share is Rs. 20.
- The preference share, redeemable after 10 years is currently selling at Rs. 75 per share.
- The debentures redeemable after 6 years are selling at Rs. 80 per debenture.
- The tax rate applicable for the company is 50%.

Compute the WACC of the company.

See Topic: COST OF CAPITAL, Long Answer Type Question No. 4.

10. a) A Machine has an initial cost of Rs. 2,00,000. Following are the details of each inflow

Year	Cash Inflows (Rs.)
1	80000
2	70000
3	95000
4	65000
5	50000

If discount rate is 10% find out the Net Present Value of the project and comment.

b) Distinguish between "Net Present Value" and "Internal Rate of Return".

See Topic: CAPITAL BUDGETING, Long Answer Type Question No. 8.

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11. Write short notes on any three of the following:

(a) Agency problem

(b) Bonus share

(c) Cost of preference share capital

(d) EBIT-EPS analysis

(e) ABC system of inventory management.

a) See Topic: FINANCIAL MANGEMENT, Long Answer Type Question No. 2.(e).

b) See Topic: DIVIDEND POLICY, Long Answer Type Question No. 6.(b).

c) See Topic: COST OF CAPITAL, Long Answer Type Question No. 5.(d).

d) See Topic: CAPITAL STRUCTURE, Long Answer Type Question No. 8.(d).

e) See Topic: MANAGEMENT OF WORKING CAPITAL, Long Answer Type Question No. 14.(d).