Name : ....

Roll No. : ....

Invigilator's Signature : ....

CS/MBA (OLD)/SEM-(2FT & 4PT)/MB-208/2010

2010

FINANCIAL MANAGEMENT

Time Allotted : 3 Hours Full Marks : 70

The figures in the margin indicate full marks.

Candidates are required to give their answers in their own words as far as practicable.

GROUP – A

(Multiple Choice Type Questions)

1. Choose the correct alternatives for any *ten* of the following : $10 \times 1 = 10$

i) Basic objective of financial management is

a) Profit maximization b) Wealth maximization

c) both of these d) none of these.

ii) IRR is the discount rate, at which

a) NPV > 0 b) NPV < 0

c) NPV = 0 d) none of these.

iii) Financial leverage affects

a) Firm's operating profit (EBIT)

b) Earnings per share

c) both of these

d) none of these.

iv) Which of the following is not correct ?

a) Cost of equity capital is the rate of return expected by equity shareholder

b) Cost of reserve is free of cost

c) Cost of debt is the rate of return expected by lender

d) Cost of preference share is the rate of return expected by preference shareholder.

v) In Walter's model, value per share is inversely related to payout ratio in

a) Growth firm

b) Normal firm

c) Declining firm

d) Bankrupt firm.

vi) For a normal business organization

a) $K_d > K_e$ b) $K_d < K_e$

c) $K_d = K_e$ d) None of these.

vii) Current yield of a 10 year, 12% coupon bond with a par value of Rs. 1,000 and selling for Rs. 950 is

a) 13·62%

b) 12·63%

c) 12%

d) 13%.

e) none of these.

viii) CAPM analysis comprises the portfolio risk factor. The expression describing this is called

a) Alpha factor

b) Beta factor

c) Standard deviation

d) Rubric factor.

ix) The risk of default from a potential client is considered as

a) Credit Risk
b) Operational Risk

c) Hedging Risk
d) Currency Risk.

x) The following information is related to the operation of a firm :

Raw material storage period	70 days
Average conversion period	8 days
Finished goods storage period	18 days
Average collection period	39 days
Average payment period	45 days

The net operating cycle of the firm is

a) 180 days
b) 135 days

c) 90 days
d) none of these.

xi) A project is financially viable if its

a) IIR > K_o b) IIR < K_o

c) NPV < 0 d) PI < 1.

xii) When coupon interest rate is less than required yield, it is called

a) Premium bond b) Discount bond

c) Par value bond d) none of these.

GROUP – B
(Short Answer Type Questions)

Answer any *three* of the following. 3 × 5 = 15

2. Briefly state three factors affecting cost of equity of a firm.

3. Write a short note on Gordon's model on dividend.

4. Write in brief about the following :

   i) Yield to Maturity

   ii) Capital Rationing.

5. State the advantages and disadvantages of having less debt in the capital structure.

6. State the importance of adding back of depreciation in capital budgeting decisions.

GROUP – C

(Long Answer Type Questions)

Answer any *three* of the following. 3 × 15 = 45

7. A company has to select one of the two alternative projects whose particulars are given below :

		Project E (Rs.)	***Project F (Rs.)***
Initial outlay		11, 872	10,067
Net cash flow :			
End of year :	1	10,000	1,000
	2	2,000	1,000
	3	1,000	2,000
	4	1,000	10,000

The company can arrange necessary fund at 8%. Compute the net present value and internal rate of return of each project and comment on the results. Is there any contradiction in the above results ? If so, state the reason for such contradicion. The P.V. of Re. 1 to be received at the end of each year at different costs of capital is given :

Year	**8%**	**10%**	**12%**	**14%**
1	0·926	0·909	0·893	0·877
2	0·857	0·826	0·797	0·770
3	0·794	0·751	0·712	0·675
4	0·735	0·683	0·636	0·592

8. a) State Walter's model of Dividend decision.

b) From the following information supplied to you, determine the theoretical market value of equity share of a company as per Walter's model :

Earnings of the company :	Rs. 5,00,000/-
Dividend paid :	Rs. 3,00,000/-
No. of shares outstandings :	1,00,000
Price earning ratio :	8
Rate of Return on investment	15%

5 + 10

9. Critically evaluate Walter's model of dividend decision. Compare with that of Modigliani-Miller's model. 7 + 8

10. A trader whose current sales is Rs. 6,00,000 per annum and average collection period is 30 days wants to pursue a more liberal policy to improve sales. A study made by a management consultant rebuilds the following information :

Credit Policy	Increase in collection period	Increase in sales	Anticipated default
A	10 days	Rs. 30,000/-	1·5%
B	20 days	Rs. 48,000/-	2%
C	30 days	Rs. 75,000/-	3%
D	45 days	Rs. 90,000/-	4%

Selling price is Rs. 3/-per unit, average cost per unit is Rs. 2·25, variable cost Rs. 2/-, current bed debt loss 1%, required return on additional investment is 20%. Assume 360 days in a year. Which policy would you recommend ?

11. Write short notes on any *three* of the following : 3×5

a) Factors influencing capital structure

b) Capital Rationing

c) Motives of Holding Cash

d) Capital Budgeting under risk and uncertainties.