M.COM [PART – II]
-: ACCOUNTS GROUP :-
ADVANCED FINANCIAL MANAGEMENT
(PAPER- III) (DEC- 2018)



**Q. P. Code : 21750**

**( 3 Hours )** **( Total Marks: 100 )**

**Please check whether you have the right question paper.**

**N.B:**
1) **Question No 1 and 2 are compulsory and carry 20 and 16 marks respectively.**
2) **Solve any four questions from question Nos.3 to 9, each carrying 16 marks.**
3) **Working notes and assumptions should form part of your answers.**
4) **Use of simple calculator is allowed.**

**Q1.** RAJ Limited has the following capital structure: **(20)**

| Particulars | Book value Rs. | Market value Rs. |
|---|---|---|
| Equity capital (25,000 shares of Rs.10 each) | 2,50,000 | 4,50,000 |
| 13% Preference capital (2,000 shares of Rs.100 each) | 2,00,000 | 1,80,000 |
| 12% Debentures (1,500 debentures of Rs.100 each) | 1,50,000 | 1,45,000 |

The expected dividend per share is Rs.1.40 and the dividend per share is expected to grow at a rate of 8% forever. Market price of each equity share is Rs.18. Preference shares are redeemable after 5 years at par whereas Debentures are redeemable after 6 years at par. The tax rate for the company is 40%.

You are required to compare the weighted average cost of capital (using book value & market value weights.)

**Q2.** (A) Fill in the blank with appropriate word and rewrite the sentence: **(08)**

1. Low gearing capital structure involves ____________.
   a) High risk
   b) Low risk
   c) Moderate risk
   d) No risk

2. An appropriate capital structure is_______.
   a) Flexible
   b) Conservative
   c) Minimum risk of loss of control
   d) All of the above

3. The project with highest NPV should be______.
   a) Accepted
   b) Rejected
   c) Ignored
   d) None of the above

4. Lower Gross Profit Ratio may be due to__________.
   a) Higher rate of profitability
   b) Higher trading efficiency
   c) Lower trading efficiency
   d) All of the above



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5. Tax saving on retrenchment compensation is treated as___________.
a) Cost of tax
b) Cash inflow
c) Cash Outflow
d) None of the above

6. Combined cost of capital of various sources of capital to____________.
a) Composite cost
b) Marginal cost
c) Specific cost
d) None of the above.

7. Financial statements can judge____________.
a) Liquidity
b) Short term solvency
c) Long term solvency
d) All the above.

8. The rate of dividend on preference shares is _____________.
a) Fixed
b) Fluctuating
c) Both (a) & (b)
d) None of the above

(B) Match the columns: **(08)**

| Column A | Column B |
|---|---|
| • Positive working capital | ❖ Excess of Current Liabilities over Current Assets |
| • Composite cost | ❖ Cash Management Model |
| • Optimum capital structure | ❖ Cost of placement of order |
| • Ordering cost | ❖ Cost of Project |
| • Equity shares | ❖ Maximizes Earnings Per Share |
| • Return on Investment | ❖ Risky securities |
| • Capital Outlay | ❖ Weighted average cost of capital |
| • Baumol's Model | ❖ Excess of Current Assets over Current Liabilities. |
| | ❖ Overall profitability |



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**Q3.** The data retailing to two companies are given below: **(16)**

| Particulars | A Ltd | B Ltd |
|---|---|---|
| Equity share capital | Rs.6,00,000 | Rs.3,50,000 |
| 12% Debentures | Rs.4,00,000 | Rs.6,50,000 |
| Output (units) per annum | 60,000 | 15,000 |
| Selling price per unit | Rs30 | Rs.250 |
| Fixed Costs per annum | Rs.7,00,000 | Rs.14,00,000 |
| Variable cost per unit | Rs.10 | Rs.75 |

You are required to calculate the Operating leverage, Financial leverage and Combined leverage of two companies.

**Q4.** Using the following data, complete the balance sheet of PK LTD given below: **(16)**

Gross profit — Rs.60,000
Gross profit ratio — 20% on sales
Shareholders' Equity — Rs.50,000
Credit Sales to Total Sales — 80%
Total Assets Turnover (Sales /Total Assets) — 3 times
Inventory Turnover (based on Cost of sales) — 8 times
Average Collection Period (360 days a year) — 18 days
Current Ratio — 1.6:1
Long term Debt to Equity — 40%

**Balance Sheet as at**

| Liabilities | Rs. | Assets | Rs. |
|---|---|---|---|
| Shareholders' Equity | 50,000 | Fixed Assets | ? |
| Long term debts | ? | Inventory | ? |
| Creditors | ? | Debtors | ? |
| | | Cash | ? |
| **Total** | **?** | **Total** | **?** |

**Q5.** MRF LTD is considering the proposal of taking up a new project which requires an investment of Rs.400 lakhs on machinery and other assets. the project is expected to yield the following earnings (before depreciation and taxes) over the next five years: **(16)**

| Year | Earnings (Rs. in lakhs) |
|---|---|
| 1 | 160 |
| 2 | 160 |
| 3 | 180 |
| 4 | 180 |
| 5 | 150 |

The cost of raising additional capital is 12% and assets have to be depreciated at 20% on Written Down Value basis. The scrap value at the end of five years' period may be taken as zero. Income tax applicable to the company is 50%.



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You are required to calculate the Net Present Value of the project and advice the management to take appropriate decision.
Note: Present Values of Rs1 at 12% rate of interest is given below:

| Year | 12% |
|---|---|
| 1 | 0.8929 |
| 2 | 0.7972 |
| 3 | 0.7118 |
| 4 | 0.6355 |
| 5 | 0.5674 |

**Q6.** JK LTD manufactures readymade garments and sells them on credit basis through a network of dealers. Its present sale Rs.60 lakhs per annum with 20 days credit period. The company is contemplating an increase in the credit period with a view to increasing sales. Present variable cost are 70% of sales and the total fixed costs Rs.8 lakhs per annum. The company expects pre-tax return on investment@ 25 %(based on total cost). Some other details are given as under: **(16)**

| Proposed Credit Policy | Average Collection Period (days) | Expected Annual Sales (Rs. lakhs) |
|---|---|---|
| I | 30 | 65 |
| II | 40 | 70 |
| III | 50 | 74 |
| IV | 60 | 75 |

Which credit policy should the company adopt? Present your answer in a tabular form. Assume 360 days a year. Calculations should be made upto two digits after decimal.

**Q7.** The sales forecast for January to May,2018 and actual sales for November and December,2017 for PEP COLA LTD are given as under: **(16)**

| Month | Sales(Rs.) |
|---|---|
| Actual | |
| November,2017 | 80,000 |
| December,2017 | 70,000 |
| Forecast | |
| Jaunary,2018 | 80,000 |
| February,2018 | 1,00,000 |
| March,2018 | 80,000 |
| April,2018 | 1,00,000 |
| May,2018 | 90,000 |

20% of sales is in cash and rest is on credit, payment of which is realized in the third month. The following other information are also available:

i) Amount of purchase is budgeted at 60% of the sales turnover of a month and paid in the third month of purchase.
ii) Variable expenses is 5% of turnover-time lag of payment one month.
iii) Commission on credit sales @ 5% is payable in the third month.
iv) Rent and other expenses amounting Rs.3,000 paid every month.
v) Payment of purchase of fixed assets Rs.50,000 in March,2018.
vi) Payment for taxes in April, 2018 Rs.20,000.
vii) There will be an opening cash balance of Rs.25,000.

You are required to prepare a cash budget for five from January to May,2018



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**Q8.** CEAT LTD earns a profit of Rs.3,00,000 per annum after meeting its interest liability of Rs.1,20,000 on 12% Debentures. The tax rate is 50%. The number of Equity Shares of Rs.10 each are 80,000 and the retained earnings amount to Rs.12,00,000. The company proposes to take up an expansion scheme for which a sum of Rs.4,00,000 is required. It is anticipated that after expansion, the company will able to achieve the same return on investment as at present. the funds required for expansion can be raised either through debt at the rate of 12% or by issuing Equity Shares at par. **(16)**

Required:

(1) Compute the Earnings per share(EPS), if:
(a) The additional funds were raised as a new debt.
(b) The additional funds were raised by issue of Equity Shares.

(2) Advise the company as to which source of finance is preferable.

**Q9.** Write short note on **(any four):-** **(16)**

1. Significance of the Ratio Analysis
2. Profit Maximization v/s Wealth Maximization
3. Financial Leverage
4. Sources of Credit Information
5. ABC Analysis for Inventory Management
6. Net Present Value

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