Q.P. Code :05391

[Time: 2 Hrs 30 Mins] **[Marks:75]**

Please check whether you have got the right question paper.

N.B:
1. **All** questions are **compulsory.**
2. **Working** notes form part of your answer.
3. **Use** of simple calculator is permitted.

Q.1 A. Rewrite the Following statements and fill in the blank **(Any 8)** **08**

1) The risk arising out of the use of debt financing is called______________.
2) ________________ Risk is the uncertainty about the future EBIT.
3) If a firm has no debt, ___________ is one.
4) Modigliani and Miller (MM) approach supports the ___________ approach.
5) Low Dividend Payout Ratio leads to __________ investment.
6) In _________________ Company, EPS is very high.
7) Cash Management always attempts at _______________ the cash balance.
8) ____________ Schedule of receivables is one way of monitoring the receivables.
9) _______________ suggests that total expected return of a security is the sum of risk free return and its risk premium
10) Receivables management deals with _______________.

Q.1 B. Rewrite the Following statements and state whether True or False: **(Any 7)** **07**

1) Use of Preference Share Capital in capital structure increases Operating Leverage.
2) The objective of a credit policy is to curtail the credit period allowed by the suppliers to the firm.
3) Systematic risk reduces with diversification of investment.
4) Reduced payment of divided improves liquidity.
5) With a rise in prices a reduction in the purchasing power of the rupee is known as inflation risk.
6) Variance as a measure of risk is the square root of standard deviation.
7) Weighted average cost of capital can be calculated based on market values of securities.
8) Excessive inventory creates surplus of cash.
9) Risk-Return trade off implies optimization of risk.
10) High dividend payout ratio leads to lower retained earnings.

Q.2 A. You are given the following particulars of Vinayak Ltd. **08**

Earnings per Share	Rs. 12
No. of Equity Shares	50,000
Equity	Rs.5,00,000
Debt / Equity Mix	4:1
Debt Carries interest at	10% p.a.
Rate of Income tax	40%
Fixed Cost	Rs.3,00,000

You are required to calculate degree of Operating, Financial and Combined Leverage.

Q.2 B. If a security has a beta of 0.75 and expected rate of return on market portfolio is 17% calculate expected rate of return of the security and interpret the same. If another security has an expected rate of return of 20% what would be its beta? Risk free rate of return = 7% **07**

OR

Q.2 A. As an investment manager from the following information you are require to calculate: **08**

a. Expected rate of return
b. Risk

State of Economy	Possibility	RATE OF Return
Low Growth	0.20	25%
High Growth	0.25	40%
Stagnation	0.30	20%
Recession	0.25	12%

Q.2 B. A Company is considering raising of funds of about Rs. 1000 lakhs by one of two alternative methods, viz. 14% institutional term loan and 13% non – convertible debentures. The term loan option would attract no major incidental cost. The debentures would have to be issued at a discount of 25% and would involve cost of issue of Rs. 1 lakh. **07**

Advice the company as to the better option based on the effective cost of capital in each case. Assume a tax rate of 50%.

Q.3 From the following information prepare cash budget for Elite Ltd for a period of 3 Months ending 30th June. **15**

Months	Sales (Rs)	Material (Rs)	Wages (Rs)	Overheads (Rs)
February	1,40,000	96,000	30,000	17,000
March	1,50,000	90,000	30,000	19,000
April	1,60,000	92,000	32,000	20,000
May	1,70,000	1,00,000	36,000	22,000
June	1,80,000	1,04,000	40,000	23,000

1. 10% of the sales are on cash and balance on credit.
2. 50% of the credit sales are collected in next month and balance in the following month.
3. Creditors – Material 2 months
   Wages ¼ month
   Overheads ½ month
4. Cash and bank balance on 1st April is expected to be Rs 60,000/-.
5. Plant and machinery will be installed in February at a cost of Rs 9, 60,000/-. The monthly installments of Rs 12,000/- are payable from April onwards
6. Dividend @ 5% on preference share capital of Rs 12,00,000/- will be paid on 1st June.
7. Advanced to be received for sale of vehicles Rs 90,000 in June.
8. Dividends from investments amounting to Rs10,000 are expected to be received in June.
9. Income Tax (advance) to be paid in June is Rs 20,000.

OR

Q.3 A. From the following prepare Income Statement of Company R and T. **08**

Company	R	T
Financial Leverage	3:1	4:1
Interest	Rs 200	Rs 300
Operating Leverage	4:1	5:1
Variable cost as % to sales	$66\frac{2}{3}\%$	75%
Income tax Rate	45%	45%

Q.3 B. Calculate the level of EBIT at which the indifference point between the following financing alternatives will occur: **07**

Equity share capital of Rs. 8,00,000 and 13% Preferences share capital of Rs.2,00,000 or Equity share capital of Rs. 4,00,000, 13 % preferences share capital of Rs.2,00,000 and 15% Debentures of Rs. 4,00,000. Assume that the corporate tax rate is 50% and the price of the equity share is Rs.10.

Q.4 Jack & jones Ltd manufactures apparels and sells them on credit basis through its authorized dealers. The present sale is Rs 50 Lakhs per annum with 45 days credit period. The company is contemplating an increase in sales. Present variable costs are 50% of sales and the total fixed cost is Rs 10 Lakhs per annum. The company expects pre tax return on investment at 20%. Some other details are given as under: **15**

Proposed Credit Policy	Increase in Average Collection Period (Days)	Expected Annual Sales (Rs in Lakhs)
I	15	80
II	45	100
III	75	150

Required: Which credit policy should the company adopt? Assume 360 Days a year.

OR

Q.4 The Sun Chemicals Ltd requires Rs. 25 lakhs for a new plant. This plant is expected to yield earnings before interest and taxes of Rs. 5 lakhs. While deciding about the financial plan, the company considers the objective of maximizing earnings per share. It has three alternatives to finance the project by raising debt of Rs. 2.5 lakhs or Rs. 10 lakhs or Rs.15 lakhs and the balance in each case by issuing equity shares. The Company's share is currently selling at Rs. 150, but is expected to decline to Rs.125 in case the funds are borrowed in excess of Rs.10 lakhs. The funds can be borrowed at the rate of 10% up to Rs. 2.5 lakhs, at 15% over Rs.2.5 lakhs and up to Rs. 10 lakhs and at 20% over Rs.10 lakhs. The tax rate applicable to the company is 50%. Which form of financing should the company choose? **15**

Q.5 A. Explain factors governing capital structure. **08**

B. Discuss various technique of controlling accounts receivable. **07**

OR

Q.5 Write short notes **(any 3)** **15**

1) M M Hypothesis on dividend policy.
2) Capital asset pricing model.
3) Types of Return
4) Business risk V/s Financial Risk.
5) Net operating Approach
