

[Time: 2 ½ Hours]

[Marks: 75]

N.B. 1) Q. 1 is compulsory.

2) Q.2 to Q.5 are compulsory with internal choice.

3) Figures to the right indicate full marks.

4) Workings should form part of your answer.

5) Use of simple calculator is allowed.

Q.1 (A) Choose correct alternative and rewrite the statement: (Any 8) (8)

1. Under Walter dividend policy if $r < k_e$, the firm should have _____ payout ratio
 - a) Zero dividend
 - b) 100% dividend
 - c) Any dividend
 - d) 50% dividend
2. _____ is a situation where a constraint or budget is placed on the total size of capital expenditures during a particular period.
 - a) Capital budgeting
 - b) Capital rationing
 - c) Cost of capital
 - d) Leverage
3. The relationship between dividend per share and earning per share is _____.
 - a) Dividend yield ratio
 - b) Dividend payout ratio
 - c) Book value per share
 - d) Price Earnings ratio
4. PI of a project is the ratio of present value of inflows to _____.
 - a) Initial cost
 - b) PV of outflows
 - c) Total cash inflows
 - d) Total outflows
5. _____ represents those funds which are required to manage day-to-day business operations.
 - a) Long term capital
 - b) Short term capital
 - c) Working capital
 - d) None of above
6. _____ is a schematic representation of several decisions followed by different chances of the occurrence.
 - a) Sensitivity analysis
 - b) Probability techniques
 - c) Risk Adjusted Discounting Rate
 - d) Decision Tree
7. Net Profit for calculation of EVA is _____.
 - a) NPAT
 - b) NPBT
 - c) NOPAT
 - d) NOP

8. If a profit-making company is absorbed into a loss-making company, then this is a case of _____
 - a) Hostile takeover bid
 - b) Horizontal merger
 - c) Reverse Merger
 - d) Takeover
9. In case of Sub-Standard Asset (unsecured), provision for NPA should be made at _____
 - a) 15%
 - b) 25%
 - c) 40%
 - d) 100%
10. Which among the following is short term sources of working capital financing?
 - a) Bill discounting
 - b) Letter of credit
 - c) Commercial paper
 - d) All of the above

Q.1 (B) State whether given statements are True or False: (Any 7) (7)

1. MM model deals with irrelevance of dividend decision.
2. Under Walter dividend policy, if $r = k_e$, the firm is indifferent between dividends and investments.
3. Capital budgeting deals with long term decisions.
4. An estimation of the present value of cash for high-risk investments is known as Risk adjusted discounting rate.
5. Corporate governance is the system of rules, practices and processes by which a firm is directed and controlled.
6. In order to protect the earnings available to shareholders, the swap ratio should be based on EPS.
7. Trade credit is a spontaneous source of finance.
8. In hostile takeover bid, the price of the merger depends upon the mutual consent.
9. Vertical merger involves a merger between two firms operating and competing in the same kind of business.
10. Working capital represent those funds which are required to manage long term business operations

Q.2 (A) Butter Ltd provided you with the following information: (7)

Earnings Per Share is Rs. 18

Rate of return expected by investors is 12%

Internal rate of return is 15%

Calculate the price per share by 'Gordon Approach', if dividend payout ratio is 25% and 75%.

Q.2 (B) Akshay Ltd. is considering new projects for investments. The two alternative investment proposal are Project 'Red' and Project 'Blue'. The cost of each project is estimated to be Rs. 75,00,000. The cash inflows from the projects are expected as follows: (8)

| Year | Red | Blue |
|------|-----------|-----------|
| 1 | 30,00,000 | 42,50,000 |
| 2 | 22,50,000 | 27,50,000 |
| 3 | 17,50,000 | 20,00,000 |
| 4 | 15,00,000 | 16,00,000 |

The current yield on government securities is 8% and the risk premium for Project Red is 5% and Project Blue is 7%. Which investment should be preferred by Akshay Ltd.?

| Discounting Rate | Year 1 | Year 2 | Year 3 | Year 4 |
|------------------|--------|--------|--------|--------|
| 13% | 0.885 | 0.783 | 0.693 | 0.613 |
| 15% | 0.870 | 0.756 | 0.658 | 0.572 |

OR

Q.2 (A) Porel Ltd. has an earning per share of Rs. 15 and an equity capitalisation rate of 10%. The company has an option of adopting either 40% or 60% dividend payout ratio. Compute the market price of the company's quoted shares as per Walter's Model if it can earn a return of 15% on its retained earnings. (7)

Q.2 (B) Sandeep Ltd is considering one of two mutually exclusive proposals. Project 'MI' and project 'CSK', which require cash outlay of Rs 76,50,000 and Rs. 86,25,000 respectively. The certainty equivalent (C.E.) approach is used in incorporating risk in capital budgeting decisions. The current yield on government bonds is 8% and this considered as the risk-free rate of return. The expected net cash flow and their certainty equivalents are as follows: (8)

| Year | Project MI | | Project CSK | |
|------|-----------------|------|-----------------|------|
| | Cash Flow (Rs.) | C.E. | Cash Flow (Rs.) | C.E. |
| 1 | 40,50,000 | 0.9 | 50,50,000 | 0.8 |
| 2 | 45,00,000 | 0.7 | 40,50,000 | 0.7 |
| 3 | 50,00,000 | 0.6 | 45,00,000 | 0.9 |

Present value factors of Rs. 1 discounted at 8% at the end of year 1,2 and 3 are 0.926, 0.857 and 0.794 respectively. You are required to suggest the company as to which project should be accepted.

Q.3 (A) Saloni Ltd has Rs. 70,00,000 allocated for capital budgeting purposes. The proposals and associated profitability indexes have been determined. (7)

| Projects | Initial Investment (Rs.) | Profitability Index |
|----------|--------------------------|---------------------|
| A | 21,00,000 | 1.22 |
| B | 10,50,000 | 0.95 |
| C | 24,50,000 | 1.20 |
| D | 31,50,000 | 1.18 |
| E | 14,00,000 | 1.20 |
| F | 28,00,000 | 1.05 |

- Calculate the Net Present Value for each of the projects
- Which of the above investments should be undertaken? Assume that projects are indivisible and there is no alternative use of the money allocated for capital budgeting.

Q.3 (B) Calculate Economic Value Added (EVA) with the help of the following information of Hypothetical Ltd. (8)

| Particulars | |
|--------------------|---------------|
| Financial leverage | 1.4 times |
| Equity Capital | Rs. 170 lakhs |
| Reserves & Surplus | Rs. 130 lakhs |
| 10% Debentures | Rs. 400 lakhs |
| Tax Rate | 30% |
| Cost of Equity | 17.5% |

OR

Q.3 (A) Whale Ltd is studying the possible acquisition of Shark Ltd. by way of merger. The following data are available. (7)

| Company | After tax earnings | No. of equity shares | Market price per share |
|---------|--------------------|----------------------|------------------------|
| Whale | Rs. 1,25,00,000 | 10,00,000 | Rs. 187.50 |
| Shark | Rs. 37,50,000 | 2,50,000 | Rs. 150 |

- If the merger goes through by exchange of equity shares and exchange ratio is set according to the current market price, what is the new earnings per share of Whale Ltd. after merger.
- Shark Ltd wants to be sure that their earnings per share is not diminished by the merger, what exchange ratio is relevant to achieve the objective?

Q.3 (B) From the following information, compute the amount of provision to be made in the Profit & Loss Account of Bharosa Bank: (8)

| Assets | Rs. (in Lakhs) |
|---|----------------|
| • Standard assets | 50,000 |
| • Sub-Standard assets (fully secured) | 32,500 |
| • Doubtful assets: | |
| ➤ Doubtful for less than one year (Realisable value of security Rs. 3,500) | 15,750 |
| ➤ Doubtful for more than one year but less than three years (Realisable value of security Rs. 1,500) | 5,250 |
| ➤ Doubtful for more than three years (Unsecured) | 2,500 |
| • Loss Assets | 1,750 |

Q.4 A company is considering taking up of one of two projects 'Alpha' and 'Beta'. Both the projects have the same life, require equal investment of Rs. 80 lakhs each and both are estimated to have almost the same yield. As the company is new to this type of business, the cashflows arising from the projects cannot be estimated with certainty. An attempt was, therefore, made to use probability to analyse the pattern of cashflow from either project during the first year of operation. The pattern is likely to continue during the life of these projects. The results of the analysis are as follows (15)

| Project Alpha | | Project Beta | |
|--------------------------|-------------|--------------------------|-------------|
| Cash Flow (Rs. in lakhs) | Probability | Cash Flow (Rs. in lakhs) | Probability |
| 12 | 0.10 | 8 | 0.10 |
| 14 | 0.20 | 12 | 0.25 |
| 16 | 0.40 | 16 | 0.30 |
| 18 | 0.20 | 20 | 0.25 |
| 20 | 0.10 | 24 | 0.10 |

Which of the two projects would be riskier based on the criteria of coefficient of variation.

OR

- Q.4** Natsya Ltd. requests you to prepare a statement showing the working capital requirements forecast for a level of activity of 1,09,200 units of production. The following information is available for your calculation. **(15)**

| Cost sheet | Rs. (per unit) |
|---------------|----------------|
| Raw material | 63.00 |
| Wages | 28.00 |
| Overheads | 52.50 |
| | 143.50 |
| Profit | 42.00 |
| Selling price | 185.50 |

Additional Information:

- Raw materials are in stock on average one month.
- Materials are in process, on average 2 weeks.
- Finished goods are in stock, on average one month.
- Credit allowed by the suppliers - one month.
- Credit allowed to debtors - 2 months.
- Lag in payment of wages – 1 ½ weeks.
- Lag in payment of Overheads - one month.

20% of the output is sold against cash. Cash in hand and at bank is expected to be Rs. 42,000. It is to be assumed that production is carried on evenly throughout the year.

Wages and overheads accrue similarly and a time period of 4 weeks is equivalent to one month.

Also Calculate Maximum Permissible Bank Finance as per Tandon committee assuming that core current assets are 25% of total asset.

- Q.5 (A)** What is sensitivity analysis? What are its merits? **(8)**
(B) Define working capital? Explain various strategies of working capital financing. **(7)**

OR

- Q.5** Write Short Notes on: (Any three) **(15)**

- Corporate Governance
- Decision Tree Analysis
- Advantages of XBRL
- Types of Mergers
- Commercial Paper
