Seat No.: _____ Enrolment No._____

GUJARAT TECHNOLOGICAL UNIVERSITY

MTM – SEMESTER – 9 • EXAMINATION – WINTER 2015

Subject Code:4290105 **Date: 23/12/2015**

Subject Name: Financial Management

Time:02.30 PM TO 05.30 PM **Total Marks: 70**

Instructions:

1. **Attempt all questions.**
2. **Make suitable assumptions wherever necessary.**
3. **Figures to the right indicate full marks.**

Q.1 (a) 'The profit maximization is not an operationally feasible criterion'. Do you agree? Illustrate your views. **07**

(b) Ms Punam is interested in a fixed annual income. She is offered two possible annuities. Her required rate of return is 8%. Which of the alternatives should she choose in each of the following case? **07**

i) Pay Rs 80,000 now in order to receive Rs 14,000 at the end of each year for the next 10 years

ii) Pay Rs 1,50,000 now in order to receive Rs 14,000 at the end of each year for the next 20 years

Q.2 (a) The expected cash flows of a project are as follows: **07**

Year	Cashflow
0	-1,00,000
1	20,000
2	30,000
3	40,000
4	50,000
5	30,000

The cost of capital is 12 percent. Calculate the following:

i) Net Present Value

ii) Benefit- cost ratio

iii) Payback Period

(b) What is the CAPM approach for calculating the cost of equity? What is the difference between this approach and the constant growth approach? Which one is better? Why? **07**

OR

(b) The Internal Rate of Return has wide applicability as a meaningful approximation of the time – adjusted rate of return. But it suffers from certain major limitations.' Explain. **07**

Q.3 (a) The following is the capital structure of X Ltd as on 31 December 2014. **07**

	(Rs in million)
Equity capital (paid up)	563.50
Reserves and surplus	485.66
10% Irredeemable Preference Shares	56.00
10% Redeemable Preference Shares	28.18
15% Term loans	377.71
Total	1,511.05

The share of the company is currently selling for Rs 36. The expected dividend next year is Rs 3.60 per share anticipated to be growing at 8 percent indefinitely. The redeemable preference shares were issued on 1 January 2008 with 12 year maturity period. A similar issue today will be at Rs 93. The market price of 10% irredeemable preference share is Rs 81.81 . The company had raised the term loan from IDBI in 1998. A similar loan will cost 10% today.

Assume an average tax rate of 35 percent. Calculate the weighted average cost of capital for the company using book value weights.

(b) Illustrate the method of valuing **07**

i) Perpetual bonds
ii) Bonds with maturity

OR

Q.3 (a) For Phoenix Limited, the following data is available : **07**

EBIT	Rs 200
Contribution	Rs 400
Interest	Rs 100

If the company's sales are expected to decline by 5 percent, determine the percentage change in EPS.

(b) Explain how nature of business, market conditions, technology and credit policy affects a firm's working capital requirement. **07**

Q.4 (a) From the information and the assumption that the cash balance in hand on January 2015 is Rs 72, 500, prepare a cash budget. **07**

Assume that 50 percent of total sales are cash sales. Assets are to be acquired in the months of February and April. Therefore, provisions should be made for the payment of Rs 8,000 and Rs 25,000 for the same in respective months. An application has been made to the bank for the grant of a loan of Rs 30,000 and the loan amount is likely be received in the month of May.

It is anticipated that a dividend of Rs 35,000 will be paid in June. Debtors are allowed one month's credit. Creditors for material purchased and overheads grant one months' credit. Sales commission at 3percent on sales is paid to the salesman each month.

Month	Sales (Rs)	Material Purchases(Rs)	Salaries & Wages(Rs)	Production Overheads(Rs)	Selling Overheads(Rs)
January	72,000	25,000	10,000	6,000	5,500
February	97,000	31,000	12,100	6,300	6,700
March	86,000	25,500	10,600	6,000	7,500
April	88,600	30,600	25,000	6,500	8,900
May	1,02,500	37,000	22,000	8,000	11,000
June	1,08,700	38,800	23,000	8,200	11,500

(b) Explain the various sources of working capital finance. **07**

OR

Q.4 **(a)** A firm's estimated demand for a material during the next year is 2,500 units. Acquisition costs are Rs 400 per order and carrying cost is Rs 50 per unit. The safety stock is set at 25 percent of the EOQ. The daily usage is 10 units and the lead time is 10 days. Determine : a) the EOQ b) the safety stock c) reorder point. **07**

(b) Explain Baumol's Model for Cash Management in detail. **07**

Q.5 **(a)** The following data relates to T Pharmaceutical Co. **07**

Earnings per share - Rs 10
Capitalization rate - 10 %
Retention ratio - 40 %

Determine the price per share under Walter's and Gordon's model if the internal rate of return is 15%.

(b) Describe the traditional view on the optimum capital structure. Compare and contrast this view with the NI approach. **07**

OR

Q.5 **(a)** Raj Ltd has a net operating income of Rs 2,00,000 on an investment of Rs 10,00,000 in assets. It can raise debt at 16 percent rate of interest. Assume that taxes do not exist. **07**

Using the NI Approach and an equity capitalization rate of 18 percent, compute the total value of the firm and the weighted average cost of capital if the firm has

i) no debt
ii) Rs 3,00,000 debt
iii) Rs 6,00,000 debt

(b) Why a preference share is called a hybrid security? Explain its features. **07**

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