Max Marks: 60 **Financial Management** **Max. Time: 2 Hours**

Ques.1 A Company is considering whether it should spend `40 lacs on a machine to manufacture and sell a new product. The unit variable cost of the product is ` 60. It is expected that the new product can be sold at `110 per unit. The fixed costs (only cash) will be ` 2,00,000 p.a. in year 1 and expected to increase by 20,000 annually. The project will have a life of six years with a scrap value of ` 2,50,000. Machine is to be depreciated as per WDV method. A private bank offers an interest rate of 15% p.a. on 3 month deposits. To start with the company expects to sell at least 40,000 units during the first year.
You are required to find out Net Present Value of the project based on the sales expected during the first year and on the assumption that it will continue at the same level during the remaining years. [6]

Ques.2 ABC firm is considering to make certain relaxation in its credit policy. The ABC management has evaluated two new policies. From the following details advice the ABC management which policy has to be adopted.
(i) Annual Sales at present `90 lakhs
(ii) Proposed Sales:

Under alternative – I `115 lakhs
Under alternative – II `128 lakhs

(iii) Accounts receivable turnover ratio and bad debts losses:

EXISTING	I	II
7 Times 3%	5.25 times 5%	4 times 7%

(iv) The ABC is required to give a pre tax return of 21% on the investment.
(v) Incremental Investment in Stock Alt. **I:** 5 Lacs; **Alt. II:** 8 Lacs.
(vi) 20% of Sales is on cash basis.
(vii) Its Profit Volume Ratio is 25%.
(viii) Applicable Tax Rate is 30%. [6]

Ques.3 A Ltd. has a total sale of `6.5 crores and its average collection period is 90 days. The past experience indicates that bad-debts losses are1.5% on sales. The expenditure incurred by the firm in administering its receivables collection efforts are `7,00,000. A factor will pay advance on receivables to the firm at an interest rate of 18% p.a. after withholding 15% as reserve. Commission is charged @ 2%.
Calculate the effective cost of factoring to the Firm. [6]

Ques.4 ICICI, in its issue of Flexi bonds 3. offered Growing Interest Bond. The interest will be paid to the investors every year at the rates given below and the minimum deposit is `25,000.

	Interest (p.a.)
Year 1	9.50%
Year 2	11.00%
Year 3	12.50%
Year 4	15.00%
Year 5	18.00%

Calculate the yield to maturity (YTM). [5]

Ques.5 D Ltd. is foreseeing a growth rate of 13% per annum in the next two years. The growth rate is likely to be 10% for the third and fourth year. After that the growth rate is expected to stabilize at 8% per annum. If the last dividend was `1.50 per share and the investor's required rate of return is 15%, determine the current value of equity share of the company. [4]

Ques.6 Balance Sheet of Beta Ltd
on 31/3/14 and 31/3/15

	31/3/14	31/3/15		31/3/10	31/3/15
Equity share Cap.	15,00,000	23,00,000	**F. Assets**		
12% pref. sh. Cap.	5,00,000	3,00,000	Cost	25,00,000	38,00,000
Res. & Surplus			(-) Prov. for dep.	7,40,000	8,90,000
P & L a/c	2,50,000	4,10,000	Net Block	17,60,000	29,10,000
Sec. premium	1,50,000	1,66,000	**Investments**	5,30,000	6,70,000
General Reserve	1,80,000	2,50,000	**C. Assets**		
10 % Debentures	5,00,000	8,00,000	Stock	3,50,000	4,00,000
Creditors	1,70,000	3,04,000	Debtors	4,80,000	4,10,000
Prop Dividend	1,00,000	1,40,000	Cash & Bank	2,30,000	2,80,000
	33,50,000	46,70,000		33,50,000	46,70,000

i) Pref. shares redeemed on 31/3/15 at 10% premium.
ii) `5,00,000 eq. shares issued to brothers against acquisition of fixed assets of `2,50,000, stock `2,20,000 and creditors of `40,000.
iii) Balance Eq. shares issued at premium of 12%.
iv) Investment of `80,000 w/o through General Reserve.
v) Machine costing of `3,00,000 with book value of `1,70,000 sold for `1,45,000.
vi) Dividend of `80,000 declared for 13 - 14 and discharged simultaneously with CDT @17%.
vii) Income Tax paid during the year of `1,20,000.

Prepare Cash Flow Statement [12]

Ques.7 SSP is contemplating a change in inventory policy. Currently, the firm has an inventory turnover of 24 times a year. Sales have been holding steady at $3,00,000 per year. Variable costs are 60% of the total sales dollar. Productive fixed costs of $40,000 and will increase to $60,000 if sales exceeds 25% of current sales. The company feels that if it were to increase inventories, it could also increase return before taxes which is 25%. The company estimates the following relationship between inventory turnover and sales:

Inventory Turnover	24	12	10	6	4
Sales	$3,00,000	$3,52,000	$3,75,000	$3,90,000	$4,00,000

Using the marginal analysis technique, ***determine*** the optimal inventory policy. [6]

Ques.8 The following figures of GS Ltd. are presented to you:

	Details	**Amount**
Earnings before interest and tax		` 25,00,000
Less: Debenture interest @ 8%	80,000	
Long term loan interest @ 11%	2,20,000	` 3,00,000
= PBT		22,00,000
Less: Income tax		11,00,000
Earnings after tax		11,00,000
No. of equity shares of ` 10 each		5,00,000
EPS		` 2.2
Market price per share		` 22
P/E ratio		10

The company has undistributed reserves and surplus of ` 20 lakhs. It is in need of `30 lakhs to pay off debentures and modernize its plants. It seeks your advise on the following alternative modes of raising finance:
Alternative 1: - Raising entire amount as term loan from bank @ 13%.
Alternative 2: - Raising part of the funds by issue of 1,00,000 shares of ` 20 each and rest by term loan at 12%.
The company expects to improve its rate of return by 3% as a result of modernization, but P/E ratio is likely to go down to 8 if the entire amount is raised as term loan.
(i) Advise the company on the financial plan to be selected.
(ii) If it is assumed that there will be no change in the P/E ratio if either of the two alternatives are adopted, would your advice still hold good? [6]

Ques.9 The following figures and ratios are related to a company :

(i) Credit Sales for the year (60% of Total Sales)	` 30,00,000
(ii) Gross Profit (on cost)	25 Percent
(iii) Fixed assets turnover (basis on cost of goods sold)	1.5
(iv) Stock turnover	2 months
(v) Liquid Ratio	1:1
(vi) Current Ratio	1.6:1
(vii) Debtors Velocity	2 months
(viii) Reserve and surplus to Share capital	0.6:1
(ix) Capital gearing ratio	0.5
(x) Fixed assets to net worth	1.20:1
(xi) Bank overdraft	25% of C. Liabilities

You are required to prepare:
(a) Balance Sheet of the company on the basis of above details.
(b) The statement showing working capital requirement, if the company wants to make a provision for contingencies @ 20 percent of net working capital including such provision. [9]