20. (a) The following information is available in respect of the rate of return on investments (r), the capitalization rate (Ke) and earnings per share (E) of hypothetical Ltd.

(i) r = 12%

(ii) r = 11%

(iii) r = 10%

Ke =11% E = Rs. 20.

Determine the value of its shares, assuming the following

	D/P ratio (1-b)	Retention ratio (b)
(1)	10%	90%
(2)	40%	60%
(3)	70%	30%

Or

(b) The following information is available in respect of a firm :

Capitalization rate (Ke) = 10%

Earnings per share (E) = Rs. 10.

Assumed rate of return on investments :

(i) r = 15 %

(ii) r = 8%

(iii) r = 10%.

Show the effect of dividend policy on the market price of shares, using Walter's model.

Reg. No. : ....

Code No. : 5769 **Sub. Code : HKCM 22/ HKAM 22**

M.Com./M.Com. Computer Application (CBCS) DEGREE EXAMINATION, APRIL 2015.

Second Semester

Commerce/Commerce with Computer Application

FINANCIAL MANAGEMENT

(For those who joined in July 2012 and afterwards)

Time : Three hours Maximum : 75 marks

PART A — (10 × 1 = 10 marks)

Answer ALL questions.

Choose the correct answer :

1. Financial management is mainly concerned with

(a) Arrangement of funds

(b) Efficient management of business

(c) All aspects of acquiring and utilizing financial resources

(d) Utilization of finance

2. Early stage financing is a method of

(a) Seed capital (b) Expansion finance

(c) Working capital (d) Additional capital

3. The return after pay – back period is not considered in case of

(a) Pay back method (b) ARR method

(c) IRR method (d) NPV method

4. While evaluating capital investment proposals, the time value of money is considered in case of

(a) Urgency method

(b) Discounted cash flow method

(c) ARR

(d) Pay-back method

5. Which among these is not a specific cost?

(a) Cost of debt

(b) Cost of equity

(c) Cost of asset

(d) Cost of preference share

6. Financial leverage is related to

(a) financing activities of the firm

(b) fixed financial charges

(c) operating expenses

(d) fixed expenses

7. According to MM theory, the firm can be classified into ———— risk classes

(a) Homogeneous (b) Heterogeneous

(c) Financial (d) Operating

8. The arbitrage process is the behavioural foundation for the

(a) MM hypothesis

(b) Net income approach

(c) Net operating income approach

(d) Traditional approach

9. Dividend is a distribution of divisible profit among the

(a) Equity share holders

(b) Preference share holders

(c) Debenture holders

(d) Partners

10. A stable divided policy refers to

(a) The consistency or lack of variability in the stream of dividend

(b) Same dividend to be paid every year

(c) Shareholder's wishes regarding dividends

(d) Bonus shares

PART B — (5 × 5 = 25 marks)

Answer ALL questions choosing either (a) or (b).

Each answer should not exceed 250 words.

11. (a) Explain about wealth maximization.

Or

(b) Explain the routine functions of financial management.

12. (a) Determine the pay-back period for a project which requires a cash outlay of Rs. 10,000 and generate cash inflows of Rs. 2,000, Rs. 4,000, Rs. 3,000 and Rs. 20,000 in the first, second, third and fourth year respectively.

Or

(b) A company has an investment opportunity costing Rs. 40,000 with the following expected net cash flow (ie after tax and before depreciation).

Year	1	2	3	4	5
Net cash flow	7000	7000	7000	7000	7000
Year	6	7	8	9	10
Net cash flow	8000	10000	15000	10000	4000

Using 10% as the cost of capital determine the profitability of the proposal under profitability index method.

13. (a) Distinguish between operating and financial leverage.

Or

(b) The operating and cost data of ABC Ltd. Are:

	Rs.
Sales	20,00,000
Variable cost	14,00,000
Fixed cost	4,00,000 (including 15% interest On Rs. 10,00,000)

Calculate its operating, financial and combined leverages.

14. (a) From the following particulars calculate : (i) Earnings per share (ii) The price-earning ratio.

	Rs.
Equity capital (Rs. 10 shares)	7,00,000
10%, 20,000 preference shares of	2,00,000
Profit and tax of 35%	3,20,000
Market price of equity shares	60

Or

(b) Critically examine the net income and net operating income approach to capital structure.

15. (a) A company's equity shares are being traded in the market at Rs. 48 per share with a price earning ratio of 8. The company's dividend payout ratio is 80%. It has 1,00,000 equity shares of Rs. 10 each and no preference shares. Book value per share is Rs. 40.

Calculate :

(i) Earnings per share

(ii) Net income

(iii) Dividend yield and

(iv) Return on equity.

Or

(b) The Apex company which earns Rs. 5 per share, is capitalized at 105 and has a return on investment of 12%. Using Walter's dividend policy model, determine

(i) the optimum payout and

(ii) the price of share at this payout.

PART C — ($5 \times 8 = 40$ marks)

Answer ALL questions choosing either (a) or (b).

Each answer should not exceed 600 words.

16. (a) Explain the modern functions of financial management.

Or

(b) Why is it inappropriate to seek profit maximization as the goal of financial decision making? Give reasons for your answer.

17. (a) From the following information suggest which of the two projects should accept on the basis of Net Present Value method.

	Project A (Rs.)	Project B (Rs.)
Initial outlay	10,000	20,000
Cash inflows after taxes and depreciation : year 1	8,000	8,000
2	7,000	9,000
3	Nil	7,000
4	Nil	6,000
Service life	2 years	4 years
Required rate of return	10%	10%

Or

(b) A choice is to be made between two competing projects which requrie an equal investment of Rs. 50,000 and are expected to generate net cash flows as under :

	Project I (Rs.)	Project II (Rs.)
End of year 1	25,000	10,000
End of year 2	15,000	12,000
End of year 3	10,000	18,000
End of year 4	Nil	25,000
End of year 5	12,000	8,000
End of year 6	6,000	4,000

The cost of capital of the company is 10%

Year	1	2	3	4	5	6
P/V factor	0.909	0.826	0.751	0.683	0.621	0.564

Which project proposal should be chosen and why? Evaluate the project proposals under discounted pay back period method.

18\. (a) A company issues 10% irredeemable debentures of Rs. 2,00,000. The company is in the 50% tax bracket. Calculate the cost of debt (before as well as after tax) if the debentures are issued at

(i) Par

(ii) 10% discount and

(iii) 10% premium.

Or

(b) Explain the different types of costs.

19\. (a) The following is the capital structure of a company.

Equity shares of Rs. 100 each	Rs. 2,00,000
Reserves and Surplus	Rs. 80,000
9% preference shares	Rs. 1,20,000
7% debentures	Rs. 1,00,000
Total Capital	Rs. 5,00,000

The company earns 12% on its total capital. The company proposes to invest Rs. 2,50,000 in an expansion programme. The following alternatives are available :

Plan A Issue of 2,000 equity shares at a premium of Rs. 25

Plan B Issue of 10% preference shares.

The price earnings ratios are estimated as follows :

Plan A – 13

Plan B – 12

Evaluate the financing plans and make your recommendation, assuming a corporate tax rate of 50%.

Or

(b) Calculate indifference points for each financial plan assuming 35% corporate tax and face value of equity shares as Rs. 100 and the amount to be realized is Rs. 30,00,000.

(i) Either equity capital of Rs. 30,00,000 or Rs. 15,00,000 10% debentures and Rs. 15,00,000 equity.

(ii) Either equity capital of Rs. 30,00,000 or 13% preference shares Rs. 10,00,000 and Rs. 20,00,000 equity.