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Code No. : 7769 **Sub. Code : HKCM 22/ HKAM 22**

M.Com./M.Com. with Computer Application (CBCS) DEGREE EXAMINATION, APRIL 2016.

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. Profit maximization is concerned with maximization of

   (a) NPV

   (b) EPS

   (c) EPIT

   (d) Profit

2. Which type of decision helps to the management in the declaration of dividend to the shareholders?

(a) Investment decision

(b) Financing decision

(c) Dividend decision

(d) Decision making

3. 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

4. The capital rationing involves

(a) finding ways to reduce the cost

(b) choice of combination of available projects in a way to maximize the total NPV

(c) increasing the amount of investment

(d) increasing the projects

5. Financial leverage is related to

(a) financing activities of the firm

(b) fixed financial charges

(c) operating expenses

(d) fixed expenses

6. Combined leverage is a combination of ______.

(a) various costs

(b) financial leverage and EPS

(c) financial and operating leverage

(d) total fixed cost

7. The optimum capital structure is obtained when the market value per equity share is the

(a) Minimum (b) Maximum

(c) Low (d) Medium

8. The value of a firm is independent of its capital structure under

(a) Traditional approach

(b) NOI approach

(c) MM approach

(d) NI approach

9. Walter's model is based on the relationship between

(a) 'r' and 'k' (b) 'r' > 'k'

(c) 'r' = k (d) 'r' < 'k'

10. Distribution of earnings of a company among its shareholders is

(a) dividend (b) profit

(c) capital (d) interest

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) Calculate the average rate of return for project X and Y from the following :

	Project X Rs.	Project Y Rs.
Investment	30,000	40,000
Net profit for year		
1	6,000	12,000
2	6,000	10,000
3	4,000	8,000
4	4,000	6,000
5	–	4,000

Or

(b) What are the objectives of capital expenditure budget?

13. (a) The following information relate to two companies :

Company	Sales Rs.	Variable cost Rs.	Fixed cost Rs.	Interest Rs.
P Ltd	5,00,000	2,00,000	1,50,000	50,000
Q Ltd	10,00,000	3,00,000	4,00,000	1,00,000

You are required to calculate the various leverages and comment upon it.

Or

(b) A company issues 10% irredeemable debentures of Rs. 1,00,000. The company is in the 55% tax bracket. Calculate the cost of debt (before as well as after tax) if the debentures are issued at

(i) par and

(ii) 10% discount.

14. (a) Critically examine the Net Income and Net Operating Income approach to capital structure.

Or

(b) Calculate Return on Equity capital and Return on Net worth ratio form the following data :

	Rs.
10,000 Equity shares of Rs.10 each	1,00,000
10% 5,000 preference shares of Rs.10 each	50,000
10% Debentures	50,000
Reserves and Surplus	1,50,000
Current liabilities	1,00,000
Profit before interest and tax	2,00,000
Tax liability at 50%	

15. (a) What is "Reverse split"? Under what circumstances should a company take this measure?

Or

(b) The capital M Ltd. is as follows :

	Rs.
9% preference shares of Rs.10 each	3,00,000
Equity shares of Rs.10 each	8,00,000
	11,00,000

	Rs.
Additional information :	
Profit (after tax @ 35%)	2,70,000
Depreciation	60,000

Equity dividend paid – 20%

Market price of equity share Rs.40.

Compute the following :

(i) Dividend yield on equity shares

(ii) Earnings per share

(iii) Price-earnings ratio.

PART C — (5 × 8 = 40 marks)

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

Each answer should not exceed 600 words.

16. (a) Explain the relationship between financial management and other areas of management.

Or

(b) State the objectives of financial management.

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.)	P.V. Factor @10%
Initial outlay	10,000	20,000	–
Cash inflows after taxes and depreciation : year 1	8,000	8,000	0.909
2	7,000	9,000	0.826
3	Nil	7,000	0.751
4	Nil	6,000	0.683
Service life	2 years	4 years	
Required rate of return	10%	10%	

Or

(b) X company has Rs.20,00,000 to invest. The following proposals are under consideration. The cost of capital for the company is estimated to be 15%.

Project	Initial outlay	Annual cash inflow	Life of the project
A	1,00,000	25,000	10
B	70,000	20,000	8
C	30,000	6,000	20
D	50,000	15,000	10
E	50,000	12,000	20

Rank the projects on the basis of

(i) NPV method and

(ii) Profitability index method.

18. (a) Explain the significance of cost of capital.

Or

(b) From the following capital structure of a company, calculate the overall cost of capital, using :

(i) Book value weights and

(ii) Market value weights.

Source	Book value Rs.	Market value Rs.
Equity share capital (Rs.10 per share)	45,000	90,000
Retained earnings	15,000	Nil
Preference share capital	10,000	10,000
Debentures	30,000	30,000

The after-tax cost of different sources of finance is as follows :

Equity share capital : 14%;

Retained earnings : 13%

Preference share capital : 10%

Debentures : 5%.

19. (a) What factors should be considered in determining the capital structure of a company?

Or

(b) A company expects a net operating income of Rs.1,00,000. It has Rs.5,00,000, 6% debentures. The overall capitalization rate is 10%.

(i) Calculate the value of the firm and the equity capital rate according to the Net Operating Income Approach.

(ii) If the debenture debt is increased to Rs.7,50,000, what will be the effect on the value of the firm and equity capitalization ratio?

20. (a) The Agro-chemicals company belongs to risk class for which the appropriate capitalization rate is 10%. It currently has 1,00,000 shares selling at Rs.100 each. The firm is contemplating the declaration of Rs.5 as dividend at the end of the current financial year. Which just begun. What will be the price of the share at the end of the year, if a dividend is not declared? What will it be if one is? Answer these on the basis of M-M model and assume no taxes.

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.

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