



M.Com. (Semester – I) Examination, April 2018
COC 101 : ADVANCED FINANCIAL MANAGEMENT (OA – 18)

Duration : 3 Hours

Max. Marks : 60

Instructions : 1) This paper consists of **nine** questions carrying **equal** marks.

2) Question 1 consists of **5 compulsory** questions of **2 marks each**.

3) Answer **any 5** questions from question Nos. **2, 3, 4, 5, 6, 7, 8 and 9**.

4) **Each** question carries **10** marks. Figure to the **right** indicates marks.

1. A) What is Wealth Maximisation of a Firm ? How do you measure it ? 2
B) How do you compute an expected return using Capital Asset Pricing Model (CAPM) ? 2
C) Define the term Leverage. Explain in brief types of leverages. 2
D) A company requires a maximum inventory of 1000 units of a material where the carrying cost per unit is ₹ 25, the cost per order is ₹ 250 and there are 6 orders per year. Assume the assumptions of Economic Order Quantity holds good. Compute total Cost of Inventory. 2
E) Total current assets of a company are ₹ 960 lakh while the current liabilities (other than bank borrowings) are ₹ 300 lakh. If the company borrowed ₹ 350 lakh, what will be the amounts of Maximum Permissible Bank Finance (MPBF) for Working Capital under the methods I and II of the Tandon Committee recommendations ? 2
2. What are important Financial Decisions ? Explain with the help of examples. 10
3. What is Cost of Capital ? How do you estimate the Cost of Debt and Cost of equity ? Illustrate. 10
4. What is Optimum Capital Structure ? Discuss in brief M-M theory of Capital Structure. 10



5. A) A firm is considering replacing an old machine and has two types of machines in view. The Machine "A" is expensive but gives high production rate, while the other Machine "B" is less expensive and with lower production rate. Both the machines are better than the existing machine. The opportunity cost of capital is 10 per cent.

The cash flows (in Lakhs.) of two options are assessed as follows.

Year	0	1	2	3	4	5
Machine A	(-80)	20	25	25	30	30
Machine B	(-60)	–	25	30	20	20

Calculate :

NPV, Profitability Index of the two machines and indicate which machine should be accepted ?

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Present Value Interest Factors (PVIF) at 10 per cent :

Year	1	2	3	4	5
PVI Factor	0.909	0.826	0.751	0.683	0.621

- B) A firm is considering two mutually exclusive projects A and B. The following information is available for the two projects :

Project A		Project B	
Probability	Net Cash Flow (₹)	Probability	Net Cash Flow (₹)
0.2	(3,00,000)	0.3	2,00,000
0.5	2,00,000	0.3	2,50,000
0.2	4,00,000	0.2	3,00,000
0.1	7,00,000	0.2	3,50,000

Evaluate the project using Coefficient Variation (CV) method and suggest which of the project should be accepted if the firm is risk averse.

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6. A) Calculate the Weighted Average Cost of Capital (WACC) from the following information :

Capital Structure of AB Ltd.

Source of Capital	Amount in ₹
Equity Capital : Shares of ₹ 10 each fully paid	1,00,000
Reserves	50,000
Long-term Debt	1,00,000
Total	2,50,000

Market Price per share of AB Ltd., is ₹ 60 and Earnings Per Share is ₹ 6. The expected growth rate of earnings is 5 per cent. Cost of Debt (before-tax) is 11 per cent. Corporate tax rate is 40 per cent. Use the market values as weights and show your workings.

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- B) i) A company issued 12 per cent Debentures of face value of ₹ 100 at discount of 4 per cent for 10 years. The redemption is planned at premium of 10 per cent. Tax rate is 40 per cent. Calculate Cost of Debt (before and after tax).

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- ii) An ordinary share of a company, which engages no external financing, is selling for ₹ 50. The Earnings Per Share (EPS) is ₹ 7.50 of which 60 per cent is paid in dividends. The company reinvests retained earnings at a rate of 10 percent. Compute Cost of Equity.

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7. A) Raashi Ltd., has 10% Debentures of the face value of ₹ 8 Crore in its Capital structure. The Operating Profit of the company before interest and tax is ₹ 2 Crore with the Cost of equity capital or equity capitalization rate at 12.5 per cent. Find out total value and Over-all Cost of Capital of the firm under Net Income Approach.

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- B) Given that :

Particulars	
Average Cost of Capital (WACC) (%)	12
Cost of Debt (%)	10
Net Operating Income (EBIT)	₹ 15,000
Total Capital Structure Value	₹ 1,00,000
Leverages (Debt/Equity) (%)	50 and 80

Calculate the Cost of Equity K_e and Value of the firm, V , for each of the leverages under the Net Operating Income (NOI) Approach.

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8. From the following information, determine the effect of different dividend policies on the share price of RS Ltd., for the below mentioned three alternative levels of rate of return using Walter's Model of Dividend Theory and what dividend policy do you recommend and why ?

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Particulars	
Cost of Capital (%)	10
Earnings Per Share (₹)	10
Return on Investment (%)	a.15 b.10 c.8
Dividend Pay-out Ratio (%)	50, 75 and 100

9. As the Management Account of a Limited Company, you are required to prepare a Statement showing the Working Capital needed to finance a level of activity of 12000 units a year. The following information may be of interest :

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Elements of Cost	Per Unit (₹)
Direct Material	12
Direct Labour	4
Overheads	100% of Direct Labour
Profit	20 per cent of Selling Price
Additional information :	
Raw materials are expected to remain in stock for an average of	2 months
Processing time	1 month
Finished goods are expected to remain in store, on average of	2 months
Credit allowed to Debtors	3 months
Credit allowed by Creditors	1 month
Time lag in wage payments	0.5 month