LOYOLA COLLEGE (AUTONOMOUS), CHENNAI – 600 034

B.Com. DEGREE EXAMINATION – **COMMERCE**

SIXTH SEMESTER – **APRIL 2016**

CO 6608 – FINANCIAL MANAGEMENT

Date: 15-04-2016 Dept. No. Max. : 100 Marks

Time: 09:00-12:00

PART – A **(10x2=20 marks)**

ANSWER ALL QUESTIONS:

1. Define financial management
2. What are the functions of Financial Management?
3. What is composite leverage?
4. Define capital structure
5. What is meant by WACC?
6. Janaki ltd., issued 12,000 10% debentures of Rs.100 each at par. The tax rate is 50%. Calculate before tax and after tax cost of debt
7. Calculate the payback period for a project which requires a cash outlay of Rs.1, 00,000 and generates cash flows of Rs. 25,000 Rs. 35,000, Rs. 30,000, and Rs. 25,000 in the first, second, third and fourth years respectively.
8. A company is contemplating investment in a project which requires an initial investment of Rs. 2,00,000 generating a cash flow of Rs.80,000 every year for 4 years. Calculate the internal rate of return.
9. Brown ltd. has total sales revenue of Rs.120lakh a year, of which 75% are credit sales. The firm has an investment opportunity in the money market to earn a return of 18% p.a. if the firm could reduce its float by 3 days, what would be the annual savings for it?
10. The daily demand for an item X is about 45 units. Every time an order is placed, a fixed cost of Rs. 75 is incurred. The daily holding cost per unit is Rs. 120. Determine the economic size.

PART–B

ANSWER ANY FOUR QUESTIONS: **(4x10=40 marks)**

11. Discuss the functions of financial management.
12. Explain the factors affecting capital structure of a firm.
13. The following projections have been given in respect of companies X and Y.

Particulars	**Company X**	**Company Y**
Volume of output and sales	80,000 units	1,00,000 units
Fixed cost	Rs. 2,40,000	Rs. 2,50,000
Selling price per unit	Rs. 10	Rs.8
Variable cost per unit	Rs.4	Rs.8
Interest	Rs.1,20,000	Rs.50,000

On the basis of above information calculate

(a) Operating leverage

(b) Financial leverage

(c) combined leverage

14. a) Your company's share is quoted in the market at Rs.20 currently. The company pays a dividend of Rs.1 per share and the investors expect a growth rate of 5% per year.

(i) Compute the company's cost of equity capital.

(ii) If the anticipated growth rate is 6% per annum calculate the indicated market price per share if company's cost of equity capital is maintained.

(iii) If the company's cost of capital is 8% and the anticipated growth rate is 5% per annum calculate the indicated market price, if the dividend of Rs.1 per share is to be maintained.

b) Write short notes on Net operating Income approach. (3 marks)

15. A company was recently formed to manufacture a new product. It has the following capital structure:

	Rs.
(i) 9% debentures (Face Value Rs.100)	10,00,000
(ii) 7% preference shares (Face Value Rs.100)	4,00,000
(iii) Equity share (48,000 shares)	16,00,000
(iv) Retained earnings	10,00,000
Total	40,00,000

The market price of equity share is Rs.80 and a dividend of Rs.8 per share is proposed. The Preference shares can be redeemed at Rs.110 and the debenture can be redeemed at Rs.105 each. The company has marginal tax rate of 50% and shareholders individual tax rate is 25%. Compute after tax weighted average cost of capital of the company based on a) Book Value b) Market Value.

16. It is proposed to introduce a new machine to increase the production capacity of department X. two machines are available, Type 'A' and type 'B'. The following information is available:

Details	A(Rs)	B (Rs.)
Cost of machine	3,50,000	6,30,000
Estimated life(years)	7	10
Estimated savings in scrap p.a	20,000	32,000
Additional cost of indirect materials p.a	10,000	16,000
Estimated savings in wages:		
Employees not required	15	20
Wages per employee per annum	10,000	16,000
Additional cost of maintenance p.a	7,200	12,000
Additional cost of supervision p.a	24,000	36,000

The rate of taxation can be regarded as 50% of profits. Which machine can be recommended for purchase according to Pay Back Period?

17. X ltd., is carrying on business of purchase and sale of a item. Selling price is Rs.80 and purchase price is Rs.60. during Dec 2007, Jan 2008, feb2008, and March 2008, its sales were 300 units, 400units, 500units, and 600units respectively. 10% of sales are on cash basis and the balance on one month's credit basis. Its office expenses are Rs.3,000 per month. Cash balance on 1.1.2008 Rs.10,000. At the end of each month, the stock was nil.

Prepare a cash budget for the months Jan, Feb., and March 2008.

PART – C

Answer any TWO questions: (2x20=40 marks)

18. Explain the objectives and goals of financial management
19. Logan ltd. wants to raise RS.2,50,000 as additional capital. It has two mutually exclusive alternative financial plans. The current EBIT is Rs.8,50,000 which is likely to remain unchanged. The relevant information is:

Present capital structure: 1,50,000 equity shares of Rs.10 each and 10% bonds of Rs.10,00,000

Tax rate: 50%
Current EBIT: Rs.8,50,000
Current EPS: Rs.2.50
Current market price: Rs. 25 per share
Financial plan I: 10,000 equity shares at Rs.25 per share
Financial plan II: 12% debentures of Rs.2,50,000
You are required to calculate:

(a) earnings per share; (b) financial B.E.P; (C) indifference point between plan I and plan II

20. X Ltd, is considering investing in a project requiring a capital outlay of Rs.8,00,000. Forecast for annual net incomes after depreciation but before tax are as follows:

Year	1	2	3	4	5
Profits(Rs.) Before tax	4,00,000	4,00,000	3,20,000	3,20,000	1,60,000

Depreciation may be taken as 20% on original cost and taxation at 50% of net income. You are required to evaluate the project according to each of the following methods:
(a) payback method; (b) rate of return on original investment method; (c) rate of return on average investment method; (d) NPV method taking cost of capital as 10%; (e) P.I method.

21. A company has prepared its annual budget, relevant details which are reproduced below:

(i) Sales Rs.46.80 lakh (25% cash sales and balance on credit)	78,000 units
(ii) Raw material cost	60% of the sales value
(iii) Labour cost	Rs. 6 per unit
iv) Variable over heads	Re. 1 per unit
(v) Fixed over heads (Including Rs.1,10,000 as depreciation)	Rs.5 lakhs
(vi) Budgeted stock levels:	
Raw materials	3 weeks
Work in progress	1 week (material 100%) labour and Overheads approx. 50%)
Finished goods	2 weeks
(vii) Debtors are allowed credits for	4 weeks
(viii) Creditors allow	4 weeks credit
(ix) Wages are paid bimonthly	
(x) Lag in payment of overheads	2 weeks
(xi) Cash in hand required	Rs.50,000

Prepare the working capital budget for the year for the company making whatever assumptions that you may find necessary.

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