NOVEMBER/DECEMBER 2018

MCM11 — ADVANCED FINANCIAL MANAGEMENT

Time : Three hours Maximum : 75 marks

SECTION A — (5 × 6 = 30 marks)

Answer ALL questions.

1. (a) Discuss the nature of financial management.

Or

(b) Explain the basic financial decisions of financial management.

2. (a) Describe the various sources of short-term working capital finance for a business.

Or

(b) Briefly explain the factors that determine the working capital needs of a firm.

3. (a) Explain the different types of dividend policies.

Or

in payment of wages — one and half weeks ; Lag in payment of overhead expenses — one month. Cash balance is expected to be its. 25,000. You are required to prepare a statement showing the working capital needed to finance a level of activity of 1,04,000 units of output. You may assume that production is carried out on evenly throughout the year and wages ad overheads accrue similarly and a time period of 4 weeks is equivalent to a month.

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5. (a) A company has a total investment of Rs. 5,00,000 in assets, and 50,000 outstanding common shares (par value). It earns a rate of 15% on its investment, and has a policy of retaining 50% of the earnings. If the appropriate discount rate of the firm is 10 percent, determine the price of its share using Gordon's model. What shall happen to the price of the share if the company has payout of 80 percent or 20 percent?

Or

(b) Write down the objectives of inventory management.

SECTION B — (3 × 15 = 45 marks)

Answer any THREE questions.

6. Explain the relationship between financial management and other areas of management.

7. From the following capital structure of a company, calculate the overall cost of capital, using (a) book value weights, and (b) market value weighs.

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

(b) A company has 1,00,000 outstanding shares selling at Rs.100 each. The firm has net profits of Rs. 10 lakhs and wants to make new investment of its. 20 lakhs during the period. The firm is also thinking of declaring a dividend of Rs. 5 per share at the end of the current fiscal year. The firm's opportunity cost of capital is 10%. What will be the price of the share at the end of the year if (1) dividend is not declared; (2) a dividend is declared; and (3) How many new shares must be issued according to MM theory?

4. (a) Describe the need and importance of capital budgeting.

Or

(b) A company is considering the purchase of the two machines with the following details :

	Machine I	Machine II
Life Estimated	3 years	3 years
	Rs.	Rs.
Capital Cost	10,000	10,000
Net earnings after tax :		
1^{st} year	8,000	2,000
2^{nd} year	6,000	7,000
3^{rd} year	4,000	10,000

Evaluate the above machines by using Net Present Value at 10% discount rate and suggest which machine should be preferred.

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

Equity share capital	-	14%
Preference share capital	-	10%
Debentures	-	5%
Retained earnings	-	13%

8. Calculate the market price of a share of ABC Ltd., under (a) Walter's Formula, and (b) Gordon's Model from the following data :

Earnings per share	Rs. 5
Dividend per share	Rs. 3
Cost of capital	16%
Internal rate of return on investment	20%
Retention ratio	50%

9. From the following information calculate Pay-back period, Net Present Value and Profitability Index.

The initial cash outlay of a project is Rs. 1,00,000.

Estimated cash inflows :

1st year	-	Rs. 40,000
2nd year	-	Rs. 45,000
3rd year	-	Rs. 40,000
4th year	-	Rs. 20,000

The following are the present value factors @ 10% p.a.

Year 1	Year 2	Year 3	Year 4
0.909	0.826	0.751	0.683

10. A cost sheet of a company provides the following data :

	Cost per unit (Rs.)
Raw Materials	80
Direct Labour	30
Overheads	60
Total cost per unit	170
Profit	30
Selling price	200

The following is the additional information available :

Average raw material in stock: one month, average materials in processes, on average, half a month. Credit allowed by suppliers — one month, Credit allowed to debtors — two months. Time lag