15803

I Semester M.Com. Degree Examination, Dec. 2013/Jan. 2014
(CBCS)
Commerce
HC : Financial Management

Time : 3 Hours | Max. Marks : 70

***Note :** Statistical/Financial Tables and Calculators **permitted** inside the examination hall.*

PART – A

Note : Answer **any five** questions. **Each** question carries **five** marks. **(5×5=25)**

1. How wealth maximisation as a financial goal is superior to profit maximisation ?

2. What is the problem of multiple IRR ? Explain with suitable example.

3. What do you mean by home-made-leverage ? Explain with a suitable example.

4. Briefly explain the traditional theory on corporate leverage.

5. HP Ltd. requires Rs. 6 million in cash every year. Each sale of T-bills costs Rs. 50. The current risk-free interest rate is 8%.

   a) What is the optimum conversion size of T-bills each time ?

   b) How many times HP Ltd. converts T-bills to cash in a year ?

   c) Determine the average investment in cash.

6. A company has to select one of the following two projects. Cash flows after tax are as follows :

Year	0	1	2	3	4
Project X	– 11,000	6,000	2,000	1,000	5,000
Project Y	–10,000	1,000	1,000	2,000	10,000

   Calculate NPV of both the projects at 10% discount rate.

P.T.O.

7. ESS ESS Ltd.'s present book value capital structure is as follows :

	Rs.
Equity shares (Rs. 10 each)	40 Lakhs
10% Preference shares (Rs. 100 per share)	16 Lakhs
12% Debentures (Rs. 100 per debenture)	44 Lakhs
	100 Lakhs

All these securities are traded in the secondary market and their recent prices are :

Equity stock Rs. 25 per share ; Preference stock Rs. 130 per share; and debentures Rs. 120 per debenture. ESS ESS Ltd.'s earnings are growing at 6% p.a. and current dividends are Rs. 12 per share. Compute cost of capital of the firm.

8. Briefly explain the merits of stable dividend policy.

PART – B

Answer **any three** questions. **Each** question carries **10** marks. **(3x10=30)**

9. Discuss the limitations of ARR in evaluating capital projects.

10. Explain the procedure for selection of projects under a situation of capital rationing.

11. What do you mean by 'trading on equity' ? Illustrate with a suitable example.

12. The variance of daily cash balance of TT Ltd. is determined as Rs. 12,000, opportunity cost of funds to be invested in short-term investment is 10 pc. p.a., transaction cost amount to Rs. 150 each. (Assume 360 working days).

   a) Determine the amount represented by Return Point.

   b) What would be the decision if cash balance on a particular day happens to be

      i) Rs. 1,000 ?

      ii) Rs. 15,000 ?

13. An electricity generation company is considering a project which would involve capital expenditure as follows :

Year	Capital expenditure (Rs. Millions)
0	22
1	14
2	10

The project would yield cash flow income of Rs. 6 million each year starting from 3rd year for perpetuity. The company applies a discount rate of 10%.

Required :

1) Determine NPV and IRR of the project.

2) Is the project acceptable ? Justify your answer.

PART – C

Case study (**Compulsory**) : **(1×15=15)**

14. EM ES Ltd. is considering two investment projects, each of which requires a cash outlay of Rs. 30 million. Company estimates that the cost of capital is 10 percent and that the investment will produce the following after-tax cash flows (in millions of rupees) :

Year	Project A	Project B
1	5	20
2	10	10
3	15	8
4	20	6

a) What is the regular payback period for each of the projects ?

b) What is the discounted payback period for each of the projects ?

c) If the two projects are independent and the cost of capital is 10 percent, which project should the firm undertake ?

d) If the two projects are mutually exclusive and the cost of capital is 5 percent, which project or projects should the firm undertake ?

e) If the two projects are mutually exclusive and the cost of capital is 15 percent, which project or projects should the firm undertake ?