19P348 (Pages: 3) Name……………………..

Reg. No…………………..

THIRD SEMESTER M.Com. DEGREE EXAMINATION, NOVEMBER 2020

(CBCSS-PG)

CC19P MCM3 C11 - FINANCIAL MANAGEMENT

(Commerce)

(2019 Admission Regular)

Time: Three Hours Maximum: 30 Weightage

Part A

Answer any ***four*** questions. Each question carries 2 weightage.

1. Define corporation finance.
2. How operating leverage is helpful in capital budgeting decision?
3. What is indifference point?
4. What you mean by finance function?
5. What is hardcore working capital?
6. What is scrip dividend?
7. What is marginal cost of capital?

(4 x 2 = 8 Weightage)

Part B

Answer any ***four*** questions. Each question carries 3 weightage.

8. Give arguments for profit maximization as an objective of a firm.
9. Give a critical appraisal of the traditional approach and Modigliani-Millers approach to the problem of capital structure.
10. X Ltd. is currently earning Rs. 1,00,000 and its share is selling at a market price of Rs. 80. The firm has 10,000 share outstanding and has no debt. The earnings of the firm are expected to remain stable, and it has a payout ratio of 100%. What is the cost of equity? If the firm's payout ratio is assumed to be 60% and that it earns 15% rate of return on its investment opportunities, then what would be the firm's cost of equity?
11. Prepare an estimate of working capital requirements from the following information of a trading concern?

Projected annual sales	-	Rs.650000
Percentage of net profit on sales	-	25%
Average credit period allowed to debtors	-	10 weeks
Average credit period allowed to creditors	-	4 weeks
Average stock holding in terms of sales requirements	-	8 weeks

Allow 20% for contingencies

12. X Corporation has estimated that for a new product its break-even point is, 2000 units, if the item is sold for Rs.14 per unit. The cost account department has currently identified variable cost of Rs. 9 per unit. Calculate the degree of operating leverage for sales volume of 2,500 units and 3,000 units. What do you infer from the degree of operating leverage at the sales volume of 2,500 units and 3,000 units and their difference, if any?
13. The earnings per share of a company is Rs. 10 and the rate of capitalization applicable to it is 10%. The company has before it the options of adopting a payout of 20% or 40% or 80%. Using Walter's formula, compute the market value of the company's share if the productivity of retained earnings is (i) 20%, (ii) 10% and (iii) 8%.
14. There are two firms X and Y which are exactly identical except that X does not use any debt in its financing, while Y has Rs. 1,00,000, 5% Debentures in its financing. Both the firms have earnings before interest and tax of Rs. 25,000 and the equity capitalization rate is 10%. Assuming the corporation tax of 50% calculate the value of the firm using M&M approach.

(4 x 3 = 12 Weightage)

Part C

Answer any ***two*** questions. Each question carries 5 weightage.

15. It is well documented that share prices tend to go up when the companies announce increase in their dividend payout. How, then, can it be said that dividend policy is irrelevant.
16. From the information given below you are required to prepare an estimate of working capital requirements:
    (a) Issued share capital Rs. 3,00,000
    6% debentures Rs. 2,00,000
    Fixed assets at cost Rs. 2,00,000
    (b) The expected ratios to selling price are:
    Raw materials – 50%
    Labour – 20%
    Overhead – 20%
    Profit – 10%
    (c) Raw materials are kept in store for an average of two months.
    (d) Finished goods remain in stock for an average period of three months.
    (e) Production during the year was 1,80,000 units and it is planned to maintain the same in the current year also.
    (f) Each unit of production is expected to be in process for half a month.

    (g) Credit allowed to customers is three months and given by suppliers is two months.
    (h) Selling price is Rs. 14 per unit.
    (i) There is a regular production and sales cycle.
    (j) Calculation of debtors may be made at selling price.
17. XYZ Limited is presently financed entirely by equity shares. The current market value is Rs. 6,00,000. A dividend of Rs. 1,20,000 has just been paid. This level of dividend is expected to be paid immediately. The company is thinking of investing in a new project involving an outlay of Rs. 6,00,000 now and is expected to generate net cash receipts of Rs. 1,30,000 per annum indefinitely. The project would be financed by issuing Rs. 5,00,000 debentures at the market interest rate of 18%.
    Ignoring tax consideration:
    (i) Calculate the value of equity shares and the gain made by the shareholders if the cost of equity rises to 21.5%.
    (ii) Prove that the weighted average cost of capital is not affected by gearing.
18. (a) A company is expecting an annual earnings, before interest and tax, of Rs. 5,00,000. The company is its capital structure has 12%. Debentures of Rs. 15,00,000. The cost of equity or capitalization rate is 16%. You are required to calculate the value of the firm and overall cost of capital according to the Net Income Approach.
    (b) If the firm decides to raise further Rs. 10,00,000 by the issue of debentures and to use the proceeds thereof to redeem equity shares, what shall be the value of the firm and overall capitalization rate according to Net Income approach.

(2 x 5 = 10 Weightage)

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