13/02

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Bachelor of Business Administration
2nd Semester Examination

1047

FINANCIAL MANAGEMENT

Paper : BBA–126

Time : 3 Hours] **[Max. Marks : 80**

Note :– Attempt *four* questions from Section A each of 5 marks. Attempt *two* questions from each of Section B and Section C, each carrying 15 marks.

Section–A

1. How project selection is made under Capital Rationing ?

2. Alpha Ltd. has issued 14 percent preference shares of the face value of Rs. 100 each to be redeemed

after 10 years. Floatation cost is expected to be 5 percent. What is cost of preference shares ?

3. Present value of cash outflow for a project is Rs. 56,125. Find out IRR if at 18 percent NPV is (–) Rs. 572 and at 17 percent NPV is Rs. 853 following interpolation method.

4. A company has a sales of Rs. 20 lakhs, variable cost Rs. 14 lakhs and fixed cost Rs. 4 lakhs (including 15% interest on Rs. 10 lakhs). Calculate operating leverage and financial leverage.

5. For a company the capitalisation rate (Ke) is 11% and EPS is Rs. 20. When rate of return on investment (*r*) are 12% and 11%, determine value of its share as per Gordon's model when dividend payout ratio is 30%.

6. Explain traditional approach for capital structure.

Section–B

7. Write notes on the following :

   (a) Profit maximisation

   (b) Risk and Return

8. Compare and Contrast :

   (a) NPV and IRR

   (b) Weighted Average Cost of Capital and Marginal Cost of Capital

9. A paper company has the following specific cost of capital along with the indicated book and market value weights :

Type of Capital	Cost	Book Value Weights	Market Value Weights
Equity	18%	0.50	0.58
Reference shares	15%	0.20	0.17
Long-term debt	7%	0.30	0.25
		1.00	1.00

   (i) Calculate the weighted cost of capital, using book and market value weights.

(ii) Calculate the weighted average cost of capital, using marginal weights, if the company intended to raise the needed funds using 50% long-term debt, 35% preference shares and 15% retained earnings.

10. A firm whose cost of capital is 10% is considering two mutually exclusive projects X and Y, the details of which are :

		Project X	Project Y
		Rs.	Rs.
Investment		70,000	70,000
Cash inflow : Year	1	10,000	50,000
	2	20,000	40,000
	3	30,000	20,000
	4	45,000	10,000
	5	60,000	10,000
		1,65,000	1,30,000

Compute the net present value at 10%, profitability index and internal rate of return for the two projects.

Section–C

11. The management of Gemini Ltd. has called for a statement showing the working capital needed to finance a level of activity of 3,00,000 units of output for the year. The cost structure for the company's product for the above mentioned activity level, is detailed below :

	Cost per Unit (Rs.)
Raw materials	20
Direct labour	5
Overheads	15
Total Cost	40
Profit	10
Selling Price	50

Past trends indicate that the raw materials are held in stock, on an average, for two months. Work-in-process (50% complete) will approximate to half-a-month's production.

Finished goods remain in warehouse, on an average, for a month.

Suppliers of materials extend a month's credit. Two month's credit is normally allowed to debtors. A minimum cash balance of Rs. 25,000 is expected to be maintained.

The production pattern is assumed to be even during the year. Prepare the statement of working capital determination.

12. Companies U and L are identical in all respects except that the former does not use debt in its capital structure, while the latter employs Rs. 6 lakhs of 15 per cent debt. Assuming that (a) all the MM assumptions are met, (b) the corporate tax rate is 50% (c) the EBIT is Rs. 2 lakhs and (d) the equity capitalisation of U is 20%, what will be the value of the firms U & L ? Also determine the weighted average cost of capital for both the firms.

13. Discuss factors which help in determining capital structure of a company.

14. Critically evaluate MM Hypothesis for dividend irrelevance.