IIT Delhi

B. Tech – MSL302 – Management Accounting & Financial Management

Major Test – November 23, 2015

Max Marks: 35 Duration: 2 hours

Attempt any 5 questions.

1. What are the factors determining working capital for a company? What is the financing mix in context of working capital management? What are its sources? [7 marks]

2. What are the two basic techniques deployed in the context of time value of money? Illustrate with examples. [7 marks]

3. Explain the Modigliani Miller approach with respect to capital structure. [7 marks]

4. The High-Flying Growth Company (HFGC) has been growing very rapidly in recent years, making its shareholders rich in the process. The average annual rate of return on the stock in the last few years has been 8%, and HFGC managers believe that 8% is a reasonable figure for the firm's cost of capital. To sustain a high growth rate, the HFGC CEO argues that the company must continue to invest in projects that offer the highest rate of return possible. Two projects are currently under review. The first is an expansion of the firm's production capacity, and the second project involves introducing one of the firm's existing products into a new market. Cash flows from each project appear in the following table.
   a. Calculate the NPV, IRR, and PI for both projects.
   b. Rank the projects based on their NPVs, IRRs, and PIs.
   c. Do the rankings in part **b** agree or not?
   d. The firm can only afford to undertake one of these investments, and the CEO favors the plant expansion because it offers a higher rate of return (that is, a higher IRR) than the product introduction. What do you think the firm should do? Why?

Year	Plant expansion	Product introduction
0	-$105,000	-$105,000
1	60,000	15,000
2	45,000	30,000
3	30,000	45,000
4	15,000	75,000

[7 marks]

5. Webster Company has compiled the information shown in the following table.

Source of capital	Book value	Market value	After-tax cost
Long-term debt	$4,000,000	$3,840,000	6.0%
Preferred stock	40,000	60,000	13.0
Common stock equity	1,060,000	3,000,000	17.0
Totals	$5,100,000	$6,900,000	

   a) Calculate the weighted average cost of capital using *book value weights.*
   b) Calculate the weighted average cost of capital using *market value weights.*

c) Compare the answers obtained in parts **a** and **b.** Explain the differences.

[7 marks]

6. The following trial balance is extracted from the books of a merchant on 31st December 2014:

PARTICULARS	Dr. Rs.	Cr. Rs.
Furniture and Fittings	640	
Motor Vehicles	6,250	
Buildings	7,500	
Capital Account		12,500
Bad Debts	125	
Provision for Bad Debts		200
Sundry Debtors and Creditors	3,800	2,500
Stock on January 1, 2014	3,460	
Purchases and Sales	5,475	15,450
Bank Overdraft		2,850
Sales and Purchases Returns	200	125
Advertising	450	
Interest Account	118	
Commission		375
Cash	650	
Taxes and Insurance	1,250	
General Expenses	782	
Salaries	3,300	
	34,000	**34,000**

The following adjustments are to be made:

(a) Stock in Hand on 31st December, 2014 was Rs. 3,250.

(b) Depreciate Building @5%, Furniture and Fitting @ 10% and Motor Vehicle @ 20%.

(c) Rs. 85 is due for interest on bank Overdraft.

(d) Salaries Rs. 300 and Taxes Rs. 120 are outstanding.

(e) Insurance amounting to Rs. 100 is prepaid.

(f) One-third of the commission received is in respect of work to be done next year.

(g) Write off further Rs. 100 as Bad Debts and Provision for Bad Debts is to be made equal to 5% on Sundry Debtors.

Prepare a Trading and Profit and Loss Account for the year ending 31st December, 2014 and a Balance Sheet as on that date.