(a) Raw materials will remain in stores for 1/2 month before being issued for production.
(b) Material will remain in process for further 1/2 month. The degree of completion is 50% in respect of all other elements of costs.
(c) Suppliers grant 2 month credit to the company.
(d) Finished goods remain in go down for 1 month.
(e) Debtors are allowed credit for 2 months. (50% of sales is on cash basis).
(f) Average time-lag in wages and overhead payments is 1/2 month and these expenses accrue evenly throughout the production cycle.
(g) No increase either in cost of inputs or selling price is envisaged.

Prepare a statement showing working capital requirement at the existing and new levels, assuming that a minimum cash balance of Rs 50,000 has to be maintained.

OR iii. From the following information, calculate minimum stock level, maximum stock level and re-ordering level **8**

(a)	Maximum Consumption	200 units per day
(b)	Minimum Consumption	150 units per day
(c)	Normal Consumption	160 units per day
(d)	Re-order period	10-15 days
(e)	Re-order quantity	1,600 units
(f)	Normal re-order period	12 days

Q.6 i. Explain a stock split? Why is it used? How does it differ from a bonus shares? **3**

ii. Describe the various models, regarding relevance and irrelevance of dividend. Also discuss the factors and conditions that are relevant in evolving a dividend policy. **7**

OR iii. From the following information, calculate the percentage of change in earning per share if sales are increased by 5% **7**

	(in Rs. Lakhs)
EBIT	1,120
PBT	320
Fixed Cost	700

******

Total No. of Questions: 6 Total No. of Printed Pages:4

Enrollment No....................................

Faculty of Management

End Sem (Even) Examination May-2018

MS5CO08 Corporate Finance

Programme: MBA Branch/Specialisation: Management

Duration: 3 Hrs. **Maximum Marks: 60**

Note: All questions are compulsory. Internal choices, if any, are indicated. Answers of Q.1 (MCQs) should be written in full instead of only a, b, c or d.

Q.1 i. Profit maximisation is - **1**
(a) It is indicator of economic efficiency
(b) Primary objective of business
(c) Measurement of Success of business decisions
(d) All of these

ii. Finance function involves - **1**
(a) Expenditure of funds only
(b) Procurement of finance only
(c) Safe custody of funds only
(d) Procurement and effective utilization of funds

iii. Lease which includes a third party (a lender) is known as – **1**
(a) Sale and leaseback (b) Direct Lease
(c) Financial Lease (d) Leveraged Lease

iv. Preference shares - **1**
(a) Not receive dividends
(b) Are not part of a company's share capital
(c) Have no voting rights
(d) All of these

v. Determination of cost of capital means to find out the cost of ….. **1**
(a) Debenture (b) Preference capital
(c) Equity capital (d) All of these

vi. The concept of cost of capital is used in….. **1**
(a) Capital structure decision (b) Investment decision
(c) Project evaluation (d) All of these

vii. Requirement of ……… working capital increases due to extension of business **1**
(a) Fixed (b) Variable
(c) Both (a) and (b) (d) Operating

viii. Excess working capital is the evidence of- **1**
(a) Idle funds (b) Defective credit policy
(c) Managerial inefficiency (d) All of these

ix. Dividends are – **1**
(a) Not paid to ordinary shareholders
(b) Not paid to preference shareholders
(c) Paid to lenders
(d) None of these

x. The word 'Leverage 'is originally related to …….. **1**
(a) Economics (b) Sociology (c) Biology (d) Engineering

Q.2 i. Discuss the objectives of modern financial management. **3**

ii. If the face value of debenture is Rs. 1000, and it is having annual interest rate of 12%. Maturity period of debenture is 5 years. Compute the present value of debenture, if – **7**
(a) Required rate of return is 12% (b) Required rate of return is 15%
(c) Required rate of return is 10%

OR iii. 'Financial management is more than procurement of the funds.' Explain. Also describe the three broad areas of financial decision making? Also comment on the emerging role of the finance manger in India. **7**

Q.3 i. What do you mean by shares? Also list its characteristics. **3**

ii. Explain the concept of hire purchase? Differentiate between leasing and hire purchase. **7**

OR iii. Z Ltd. needs land for 5 years. It has two options– **7**
(a) Takes the machinery on lease by paying equal annual instalments of Rs. 10,00,000
(b) Borrow Rs. 40 lacs and buy the machinery. The principal is repayable in 5 equal instalments. 12% interest is paid on the outstanding balance at the end of each year.

Depreciation is charged at 10% (consider SLM) on the original cost and tax rate is 30%. After tax discounting factor is 9%.
Which option should be considered by the Z Ltd? Justify your answer.

Q.4 i. What is meant by capital structure? Explain. **2**

ii. The capital structure of A Ltd is as follows – **8**

Equity Share Capital (4,000 shares fully paid up)	Rs. 4,00,000
7% Debenture of Rs. 100 each	Rs. 2,50,000
9% Preference Share Capital (Rs. 100 each)	Rs. 2,50,000
Retained Earnings	Rs. 1,00,000

The company has earned Rs. 20 per share on equity capital. The shares of the company are sold in the market at book value. The corporate tax rate is 50 percent. Calculate the weighted average cost of capital.

OR iii. ABC Ltd. is considering three financial plans. **8**
(a) Plan of financing proportion

Plan	Equity	Debt	Preference Share
A	100%	-	-
B	50%	50%	-
C	50%	-	50%

(b) Total investment to be raised Rs, 400,000
(c) Cost of Debt is 8% and Cost of Preference share is 8%
(d) Tax Rate is 50%
(e) Equity shares of face value Rs. 10 each will be issued at a premium of Rs. 10 per share.
(f) Given that EBIT is Rs. 5 lacs.

Determine for each plan EPS and comment which plan should be considered by the company.

Q.5 i. Discuss the significance of trade credit for any business organization. **2**

ii. Universal Food Suppliers is presently operating at 80 per cent level, producing 80,000 packets of item and proposes to increase its capacity utilization in the coming year by 25 over the existing level of production. The following data has been supplied: **8**

	Cost per unit (Rs.)
Raw material	130
Direct labour	40
Overheads (excluding depreciation)	30
Total Cost	**200**
Profit	20
Selling price	**220**

Additional information;
You may assume that production is carried on evenly throughout the year and wages and overheads accrue similarly.

Scheme of marking MBA - May-2018

MS5C008 - Corporate Finance

MCQ

Q.1 (i) (d) All of them

(ii) (d) Procurement & Effective utilisation of funds

(iii) (d) Leverages Leave

(iv) (c) have no voting rights

(v) (d) All of them

(vi) (d) All of them

(vii) (c) both (a) & (b)

(viii) (d) All of them

(ix) (d) None of them

(x) (d) Engineering

Q. 2 (i) = 1 marks for each objective (3)

Total (7) Marks

(ii)

Present value of Debenture = V_d

$$V_d = R(ADF) + M(DF)$$ (3)

(a) Required Rate of return is 12%.

$$V_d = 120(3.605) + 1000(.567)$$

$$V_d = 432.60 + 567$$

$$V_d = 999.60 \text{ or say Rs. } 1000$$ (2)

(b) Required Rate of return is 15%,

$$V_d = 120(3.352) + 1000(.497)$$

$$= 402.24 + 497$$

$$= 899.24$$

(1)

(2).

(c) required rate of return is 10%

$Vd = 120(3.791) + 1000(.621)$

$= 453.92 + 621$

$= 1075.92$ or Say 1076

2 (iii) Meaning = 2 marks

Three Area = 3 marks

Emerging Role = 2 marks

3 (i) Meaning of shares = 1.5 marks

Characteristics = 1.5 marks

(ii) Concept of hire Purchase = 3 marks

Diff. between leasing & hire Purchase = 4 marks

(iii) Leasing Evaluation - - - - - - 3 marks

(a) Present value of Post tax lease rental

Sr. No.	Lease rental	Post tax rental	P.V. factor at 9%	Present value Amount
1	10,00,000	7,00,000	.917	641900
2	10,00,000	7,00,000	.842	589400
3	10,00,000	7,00,000	.772	540400
4	10,00,000	7,00,000	.708	495600
5	10,00,000	7,00,000	.650	455000
				27,22,300

(2)

(b) borrowing Evaluation - - - - - - 3 marks

Year	Principal Repayment	Interest Payment	Depreciation	Tax saving on Interest & Depreciation	After Tax saving cash outflow
1	8,00,000	480000	4,00,000	264000	10,16,000
2	8,00,000	384000	4,00,000	235200	9,48,800
3	8,00,000	288000	4,00,000	206400	8,81,600
4	8,00,000	192000	4,00,000	177600	8,14,400
5	8,00,000	96000	4,00,000	148800	7,47,200

Year	P.V. fact.	Present value
1	.917	931672
2	.842	798890
3	.772	680595
4	.708	5,76,595
5	.650	4,85,680
		34,73,432

Decision

As Per Evaluation lease option is beneficial because its Present value is less compared to buying option - - - - - - - - (1 marks)
: decision - -

1 (i) Capital Structure meaning - - - 2 marks

(ii) $K_e = \frac{Earning}{Price} \times 100 = \frac{20}{100} \times 100 = 20\%$.

$K_d = (1-t)$ interest rate

$= (1-50\%)\ 7\% = 3.5\%$.

$K_p = 9\%$.

$K_R = 20\%$.

3

Weighted Average cost of capital

Source	Amount	Cost	Proportion	WACC
Equity	4,00,000	20	·4	8
Debenture	2,50,000	3·5	·25	·875
Preference share	2,50,000	9	·25	2·25
Retained Earning	1,00,000	20	·10	2
		WACC		13·125

[2 marks for each source Total 8 marks]

4(iii) Given that EBIT = 5,00,000

Calculation of EPS under each Plan

Particulars	A	B	C
EBIT	5,00,000	5,00,000	5,00,000
Less: Interest	—	16,000	—
EBT	5,00,000	4,84,000	5,00,000
Less: Tax @50%	2,50,000	2,42,000	2,50,000
EAT	2,50,000	2,42,000	2,50,000
Less: Preference Dividend	—	—	16,000
Profit available to Equity shareholders	2,50,000	2,42,000	2,34,000
No. of Equity share	20000	10000	10000
EPS	12·5	24·2	23·4

Plan B is selected by the company as its EPS is high

[2 marks for each Plan valuation = 6 marks]
[2 marks for Decision = 2 mark]

5 (i) Significance of trade credit = 2 marks

(ii) Statement showing working capital requirement at 80% level capacity units producing 80000

Particulars | Amount

1) Raw material $\frac{80000}{12} \times \frac{1}{2} \times 130$ — 4,33,333

2) Work in progress — 5,50,000

4,33,333	Raw material	= 130
66,667	Labour 50%	= 20
50000	Overhead 50%	= 15
5,50,000		165

$= \frac{80000}{12} \times \frac{1}{2} \times 165$

3) Finished goods $\frac{80000}{12} \times 200$ — 13,33,333

4) Debtors $\frac{40000}{12} \times 2 \times 200$ — 13,33,333

5) Cash balance — 50,000

Current Assets (A) — 36,99,999

1) Suppliers $\frac{80000}{12} \times 2 \times 130$ — 17,33,333

Wages $\frac{80000}{12} \times \frac{1}{2} \times 40$ — 1,33,333

Overhead $\frac{80000}{12} \times \frac{1}{2} \times 30$ — 1,00,000

Current Liabilities (B) — 19,66,666

Working capital (A − B) 17,33,333

Working capital at new level 100% capacity of 1,00,000 units is Rs 21,66,667

[7 marks for working capital calculation
1 mark for 100% capacity calculation]

5

Q 5 (iii)

(i) Reorder level = maximum usage × maximum Delivery Time

= 2000 × 15

= 3000 units ---- [2 marks]

(ii) minimum stock level = Reorder level − [Normal consumption × Normal Delivery Period]

= 3000 − [160 × 12]

= 3000 − 1920 = 1080 units

---- [3 marks]

(iii) maximum stock level = Reorder level − [minimum usage × minimum Delivery time] + Reorder quantity

= 3000 − [150 × 10] + 1600

= 3100 units ---- [3 marks]

Q. 6 (i) 1 + 1 + 1 = 3 marks

6(ii) model discussion = 4 marks

factors & condition = 3 marks

(iii) Leverage calculation & contribution calculation = 4 marks

Percentage change in EPS calculation = 3 marks

Contribution = fixed cost + EBIT

= 700 + 1120 = 1820

$$\text{O.P. Leverage} = \frac{C}{EBIT} = \frac{1820}{1120} = 1.625$$

∴ financial Leverage = $\frac{EBIT}{PBT} = \frac{1120}{320}$

$= 3.5$

Combined Leverage = operating Leverage × financial Leverage

$= 1.625 \times 3.5$

$= 5.69$

Percentage change in EPS = % change in Sales × Combined Leverage

$= 5 \times 5.69$

$= 28.45$

Percentage change in EPS = 28.45% if sales are increased by 5%.