PG – 594

First Semester M.Com. Examination, March/April 2025
(CBCS) (2020-21 and Onwards)
COMMERCE
Paper – 1.5 : Managerial Finance

Time : 3 Hours

Max. Marks : 70

SECTION – A

Answer **any seven** questions out of ten. **Each** question carries **two** marks :   **(7×2=14)**

1. a) State the features of trade off theory.
   b) What do you mean by optimum dividend payout ratio ?
   c) Give the meaning of incremental IRR.
   d) Define capital rationing.
   e) What are the perspectives of risk ?
   f) State the objectives of capital budgeting.
   g) Distinguish between MBO and MBI.
   h) What do you understand by slump sale ?
   i) State the Walter's model of dividend decision.
   j) List out the evils of excess working capital.

SECTION – B

Answer **any four** questions out of six. **Each** question carries **five** marks :   **(4×5=20)**

2. Briefly explain the factors influencing financial decisions.

3. Why capital budgeting decisions are important ? Explain.

4. Briefly explain the factors affecting dividend policies.

5. The Globe Manufacturing Company Ltd., is considering an investment in one of the two mutually exclusive proposals – projects X and Y, which require cash outlays of Rs. 3,40,000 and Rs. 3,30,000 respectively. The Certainty – Equivalent

P.T.O.

(C. E.) approach is used in incorporating risk in capital budgeting decisions. The current yield on government bond is 8% and this be used as the risk less rate. The expected net cash flows and their certainty equivalents are as follows :

Year end	Project X		Project Y	
	Cash Flow (Rs.)	C.E.	Cash Flow (Rs.)	C.E.
1	1,80,000	0.8	1,80,000	0.9
2	2,00,000	0.7	1,80,000	0.8
3	2,00,000	0.5	2,00,000	0.7

Present value factor of Rs. 1 discounted at 8% at the end of year 1, 2 and 3 are 0.926, 0.857 and 0.794 respectively. Required :

a) Which project should be accepted ?

b) If risk adjusted discount rate method is used, which project would be analysed with a higher rate ?

6. Company 'S' has forced to choose between two machines P and R. The two machines are designed differently, but have identical capacity and do exactly the same job. Machine P costs ₹ 3,00,000 and will last for 3 years. It costs ₹ 80,000 per year to run. Machine R is an economy model costing only ₹ 2,00,000, but will last only for 2 years, and costs ₹ 1,20,000 per year to run. These are real cash flows. The costs are forecasted in rupees of constant purchasing power. Ignore tax. Opportunity cost of capital is 10%. Which Machine Company 'S' should buy ?

7. Krishna Ltd. is considering merger with Sudhama Ltd. There are no gains from merging. If it is given that total earnings of the merged firm likely to have no synergy, calculate the exchange ratio for a combined EPS of ₹ 2.80.

	Krishna Ltd.	Sudhama Ltd.
Outstanding shares	5 million	2.5 million
P/E	20	10
Total market value	250 million	50 million

SECTION – C

Answer **any two** questions out of four. **Each** question carries **twelve** marks : **(2×12=24)**

8. Write a note on Simulation as a tool of risk analysis in capital budgeting decisions.

9. Tulsian Ltd. is considering an investment in a project that required an initial investment of Rs. 50 lakhs with an expected cash flow after tax over 3 years as follows :

Year 1		Year 2		Year 3	
CFAT	Probability	CFAT	Probability	CFAT	Probability
10	0.4	15	0.3	20	0.2
20	0.3	25	0.4	30	0.3
30	0.2	35	0.2	40	0.4
40	0.1	45	0.1	50	0.1

Required :

i) What is the expected NPV of this project ? (assume the cash flows are independent, firm's cost of capital is 10% and the firm can invest in 5% treasury bills).

ii) Compute standard deviation about the expected value.

iii) Compute the coefficient of variation about the expected value.

10. Rajan Ltd. Provides you the following information :

Purchase price of each machine	₹ 12,00,000
Working capital	₹ 6,00,000
Useful life of each machine	5 years
Estimated salvage value at the end of useful life is	₹ 2,00,000
Actual salvage value realised at the end of useful life	₹ 2,40,000
Method of depreciation	Straight line
Tax rate	30%

Earnings before depreciation and tax :

Machine	Year 1	Year 2	Year 3	Year 4	Year 5
A	6,00,000	6,00,000	6,00,000	6,00,000	6,00,000
B	– –	2,00,000	4,00,000	6,00,000	24,00,000
C	10,00,000	8,00,000	6,00,000	4,00,000	– –

Required : Which of the above machines should be purchased on the basis of internal rate of return.

11. The capital structure of Yellow Ltd. is as follows :

Equity share capital (₹ 100 each)	₹ 100 lakhs
Earnings for equity shareholders	₹ 10 lakhs
Price of shares in the beginning	₹ 100
Equity capitalisation rate	10%

Required :

a) Calculate the theoretical market price of equity share under MM model, if the company is considering a payout of (i) 0%, (ii) 80%.

b) Calculate the value of the firm using MM model if dividend payout ratio is (i) 0%, (ii) 80%. The company proposes to make a new investment of ₹ 12,20,000.

SECTION – D

Answer the following question :   (1×12=12)

12. Shiva Ltd. has recently approached the shareholders of Vishnu Ltd., which is engaged in the same line of business as that of Shiva Ltd., with a bid of 4 new shares in Shiva Ltd., for every 5 Vishnu Ltd. Shares, or a cash alternative of ₹ 360 per share. Past records of earnings of Vishnu Ltd. had been poor and the company's shares have been out of favour with the stock market for some time.

Both Shiva Ltd. and Vishnu Ltd. Pay income tax @ 30%. Current earnings growth forecast is 4% for the foreseeable future of both the companies. Pre-bid information for the year ended 31st March, are as follows :

Firm	Equity capital	No. of shares	Pre-Tax profit	P/E Ratio	Estimated Post tax cost of equity p.a.
Shiva Ltd.	₹ 60 lakhs	24 lakhs	₹ 125 lakhs	11	12%
Vishnu Ltd.	₹ 170 lakhs	17 lakhs	₹ 110 lakhs	7	10%

Assuming no synergy exists, you are required to evaluate whether proposed share to share offer is likely to be beneficial to the shareholders of both the companies using merger terms available. Shiva Ltd.'s Directors might expect their own pre-bid P/E ratio to be applied to combined earnings.

Also comment on the two companies from the constant growth form of dividend valuation model, assuming all earnings are paid out as dividends.

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