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Third Semester MBA Degree Examination, Feb./Mar. 2022 Advanced Financial Management

Time: 3 hrs.

Max. Marks: 100

**Note: 1. Answer any FOUR full questions from Q1 to Q7.
2. Question No. 8 is compulsory.**

- 1 a. State the motives for holding cash. (03 Marks)
 b. What is operating cycle and how it is computed? (07 Marks)

c.

Particulars	L	U
S	3,12,500	8,00,000

An inventory holds 10% in the firm 'L'. The firm has debentures of Rs.500,000, with interest 10%. The returns available to the equity holders in the firm 'L' is Rs.50,000 and in the firm 'U' is Rs.100,000. K_e for 'L' is 0.16 and for 'U' is 0.125. You are required to show the arbitrage process. (10 Marks)

- 2 a. What do you mean by Arbitrage? (03 Marks)
 b. Explain briefly the strategies available to a firm for managing surplus fund. (07 Marks)
 c. Explain the various ways of financing working capital requirements of a firm. (10 Marks)

- 3 a. State the assumptions of NI approach. (03 Marks)
 b. The company's annual EBIT is Rs.50,000, it has Rs.200,000, 10% debentures. Its overall cost of capital is 12.5%. What would be the total value of the firm and cost of equity (K_e). (07 Marks)
 c. The following information is available in respect of a firm's capital rate :
 $K_e - 10\%$, $E - Rs. 10$. Assume ROI as $\rightarrow 15\%$, $\rightarrow 8\%$, $\rightarrow 10\%$. Show the effect of dividend policy on the market price of the shares using Watters model. Assume D/P ratio = 0, 25, 50, 75, 100. (10 Marks)

- 4 a. From the following determine EOQ, Annual Requirement $\rightarrow 12,00,000$ units purchase price $\rightarrow 3$ per unit ordering cost $\rightarrow Rs.50$ per order, Carrying cost of inventory $\rightarrow 10\%$. (03 Marks)
 b. Discuss the factors affecting working capital management. (07 Marks)
 c. From the following information of AB Ltd, compute :
 i) Re - order level
 ii) Minimum level
 iii) Maximum level
 iv) Average stock level

The company uses two components X and Y for its manufacturing a products :

Normal usage - 100 units per week

Maximum usage - 150 units per week

Minimum usage - 50 units for week

Re - order period - component 'X' 4 - 10 Weeks Component 'Y' 2 - 8 weeks.

Re - order quantity - Component 'X' 600 units component 'Y' 900 units. (10 Marks)

- 5 a. What is the annual percentage interest cost associated with the following credit terms. Assume 360 days in a year. 2/15 Net 45. (03 Marks)
- b. ABC Ltd estimates its total cash requirements as Rs. 2 crore next year. The company's opportunity cost of fund is 15% p.a. The company will have to incur Rs. 150 per transaction when it converts its short term securities to cash. Determine the optimum cash balance. How much is the total annual cost of the demand for the optimum cash balance. How many deposits will have to be made during the year. (07 Marks)
- c. A firm's inventory planning period is 1 year. Its inventory requirements for this year is 1600 units. Assume that its acquisition cost are Rs. 50/order The carrying cost are expected to be Rs. 1 per unit, per year for an item. The firm can procure inventories in various lots as follows : 1600 units, 800 units, 400 units, 200 units, 100 units
Which of these order quantities is the Economic Order Quantity (EOQ)? (10 Marks)

- 6 a. Following is the information relating to 'A' and 'B' Ltd.,

Particulars	Rs in Million	
	'A' Ltd	'B' Ltd
Current Assets	200	80
NFA	80	200
TA	280	280
EBIT	700	700
ROI	25%	25%

You are required to compute the WCL

→ For 20% ↑ in CA of 'B' Ltd

→ For 20% ↓ in level of CA of 'A' Ltd.

(03 Marks)

- b. Briefly explain the different theories of dividend policy. (07 Marks)

- c. 'A' Ltd belongs to a risk class of which the appropriate capital rate is 10%. It currently has 100,000 shares selling @ Rs. 100 each. The firm is contemplating the declaration of the Rs. 6 dividend @ the end of the current fiscal year. Which has just began. Answer the following questions based on the M – M Hypothesis :

- i) What will be the price of share @ the end of the year. If dividend is not declared. What will it be if it is declared.
- ii) Assuming that the firm pays dividend has a net income of Rs. 10,00,000 and makes new investment of Rs. 20,00,000. During the period, how many new shares must be issued?

(10 Marks)

- 7 a. Which are the 5c's used in traditional credit analysis. (03 Marks)
- b. State the assumptions of Baumol's model of cash management? (07 Marks)
- c. 'A' Ltd has current sales of Rs. 600,000 p.a. To push up sales, it is considering a more liberal credit policy as one of the strategy. The current average collection period is 30 days.

The following plans are available :

Credit policy	↑ in collection period	↑ in sales	Default rate
1	15	25,000	0.5%
2	30	60,000	1%
3	40	70,000	2%

It is selling its products @ Rs.10 each, Avg cost/unit at current level is Rs. 8, V_e /unit, Rs.6. If required ROI is 20% on its investment. Which credit policy do you recommend and why? Assume 360 days in a year. (10 Marks)



8 CASE STUDY [Compulsory]

Prepare a each budget for the period from Jan – June from the following information.

i) The estimated sales and expenses are as follows :

Particulars	Nov	Dec	Jan	Feb	Mar	April	May	June
Sales	2,00,000	2,20,000	1,20,000	1,00,000	15,0000	2,40,000	2,00,000	2,00,000
Wage and Salary	30,000	30,000	24,000	24,000	24,000	30,000	27,000	27,000
Mise. Expenses	27,000	27,000	21,000	30,000	24,000	27,000	27,000	27,000

- ii) 20% of the total sales are on cash and balance on credit
 iii) The firm has a G/P margin of 25% on sales
 iv) 50% of the credit sales are collected in the following month after sales, 30% in 2nd month and 20% in 3rd month.
 v) Material for the sale of each month is purchased one month in advance on a credit for 2 months.
 vi) Debenture worth Rs.40,000 were sold in Jan.
 vii) The time lag in payment of wages and salaries 1/3 of a month and that of Mise. Expenses 1 month.
 viii) Cash balance @ the end of December is Rs.60,000, the firm maintains a minimum of Rs.40,000 every month, borrowing can be made in the multiple of Rs.1,000 interest is paid on monthly basis @12% p.a.

(20 Marks)

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