

M.Com. 2nd Semester Examination 2009

FINANCIAL MANAGEMENT

PAPER—CM-1201

Full Marks : 50

Time : 2 hours

The figures in the right-hand margin indicate marks

Candidates are required to give their answers in their own words as far as practicable

UNIT—I

1. Answer any *two* questions from the following: 5 × 2

- (a) Why is 'profit maximization' not regarded as a rational explanation about the objective of financial management? Which concept has been proved to be a rational one in this direction? Answer, in brief. 3 + 2

(Turn Over)

- (b) Describe the short-term sources of financing in case of a company. 5
- (c) "There is a reciprocal relationship between margin of safety ratio and degree of operating leverage." Examine the validity of this statement. 5
- (d) How would you measure cost of retained earnings? 5

2. Answer any *one* of the following questions: 10 × 1

- (a) X Co.Ltd. proposes to issue 1,000, 6% debentures of Rs.100 each to be sold for Rs. 89.40 (net). You are required to calculate the risk-free specific cost of such debentures. The debentures are repayable as per the following plan:

50% at the end of the second year at a discount of 10%, and

$12\frac{1}{2}\%$ at the end of each of the next four years at discounts of 8%, 5%, 2% and 1% respectively.

Cost of issue can be amortized in the proportion of the amount of debt on account of the debentures outstanding in each of the years.

Marginal corporate tax rate is 50%.

10

(b) (i) The following data are available for Anustup Technologies Ltd. :

<u>Capital Structure</u>	<u>Rs.</u>
Equity share capital (10,000 shares of Rs. 10 each)	100,000
Reserve & surplus	50,000
10% Preference share capital (5000 shares @ Rs. 10 each)	50,000
12% Debentures	150,000
	<u>350,000</u>

Current EBIT Rs. 100,000

Corporate income tax rate 50%

Compute (I) Degree of financial leverage,

(II) Capital Gearing ratio.

(ii) Discuss the factors underlying business risk. (3 + 2) + 5

UNIT—II

3. Answer any two of the following: 5 × 2

(a) From the following information of XYZ Limited calculate Cash Cycle: 5

	<u>Rs.</u>
Sales during the year	16,00,000
Cost of goods sold	14,40,000
Opening Stock	1,92,000
Closing stock	2,04,000
Opening Debtor	1,76,000
Closing Debtor	1,80,000
Opening Creditors	1,12,000
Closing Creditors	1,20,000

(b) What is Tandon Committee's recommendation in relation to Bank Finance? 5

(c) Kanchan Technologies Ltd. with earnings per share of Rs. 15 is capitalised at 14% and has a return on investment of 18%. What would be the optimal dividend payout ratio and the price per equity share at this payout ratio according to Walter's model? 5

(d) Briefly state the major costs involved in maintaining accounts receivables. 5

4. Answer any *one* of the following questions: 10 × 1

(a) What are the assumptions and arguments used by Miller and Modigliani in support of the irrelevance of dividends? Prove the M-M, 'dividend irrelevance theorem'. 4 + 6

(b) (i) What is the impact of credit period increase on the profitability of a firm ?

(ii) Find out impact of cash discount on profit of PQR Ltd. from the following information :

	<u>Rs.</u>
Sales Revenue 40,000 @ 12 =	4,80,000
Variable cost 40,000 @ Rs. 8 =	3,20,000
Fixed cost	80,000
	4,00,000
	80,000

Measure to be taken by the company :

2% cash discount for payment within two weeks.

Estimated impact for measures :

(1) Sales will increase by 15%.

- (2) Average collection period will reduce by 15 days.
- (3) Bad debt declined by 1 % on total sales.
- (4) 60% of total sales is on credit.
- (5) Rate of return on investment 15%. 3 + 7

[*Internal Assessment* : 10 Marks]
