Paper-12: FINANCIAL MANAGEMENT & INTERNATIONAL FINANCE

Time Allowed: 3 Hours **Full Marks: 100**

Answer Question No. 1 from Part A which is compulsory and any five questions from Part B.
Working notes should form a part of the answer
"Wherever necessary, suitable assumptions should be made and indicated in answers by the candidates"

Question 1.

(a) In each of the cases given below, one out of four answers is correct. Indicate the correct answer (= 1 mark) and give workings/reasons briefly in support of your answer (= 1 mark): **[10×2]**

(i) The average daily sales of a company are ₹ 5 lac. The company normally keeps a cash balance of ₹ 80,000.If the weighted operating cycle of the company is 45 days, its working capital will be:

A. ₹ 112.9 lac;
B. ₹ 113.3 lac;
C. ₹ 5.8 lac;
D. ₹ 225.8 lac.

(ii) The Degree of Operating Leverage (DOL) and the Degree of Financial Leverage (DFL) of Araska Ltd. are 3 and 1.67 respectively. If the management of the company targets to increase the EPS by 10%, by how much percentage should sales volume be increased? (Rounded off your answer to the nearest integer.)

A. 5.00 %;
B. 3.00 %;
C. 2.00 %;
D. 4.00 %.

(iii) The following various currency quotes are available from a leading bank: ₹/£ 75.31/75.33 £ / $ 0.6391/0.6398 $ /¥ 0.01048/0.01052. The rate at which yen (¥) can be purchased with rupees will be:

A. ₹ 0.5070
B. ₹ 1.5030
C. ₹ 1.7230
D. None of the above.

(iv) The P/V ratio of a firm dealing in precision instruments is 50% and margin of safety is 40%. Calculate net profit, if the sales volume is ₹ 12,50,000.

A. ₹ 25,000;
B. ₹ 1,25,000;
C. ₹ 2,50,000;

D. ₹ 1,50,000.

(v) Xee Ltd. paid a dividend of ₹4.00 per share for the year 2013-14. If the expected growth rate is 12% and the rate of return is 20%, the intrinsic value for its share would be:
A. ₹ 50;
B. ₹ 200;
C. ₹ 100;
D. ₹ 55.

(vi) The stock of Blue Company sells for ₹ 120. The present value of exercise price and the value of a call option are ₹ 108.70 and ₹ 19.80 respectively. Hence the value of the put option is:
A. ₹ 8.50
B. ₹ 9.00
C. ₹ 10
D. Zero

(vii) The spot and 6 month forward rates of $ in relation to rupee are ₹60.34/ 72 and 61.02/66 respectively. What would be the annualized forward margin (premium with respect to bid price)?
A. 15.32%
B. 12.32%
C. 13.52%
D. 15.23%

(viii) The total asset – turnover ratio and total asset to net- worth ratio of a company are 2.10 and 2.50 respectively. If the net profit margin of the company is 6%, what would be the return on equity?
A. 30.50%
B. 31.50%
C. 30.00%
D. 32.50%

(ix) Calculate the price of 3 months ADS futures, if ADS (FV ₹ 10) quotes ₹ 440 on NSE and 3 months future price quotes at ₹ 430 and the 1 month borrowing rate is given as 15% and the expected annual dividend yield is 25% per annum payable before expiry.
A. ₹ 454
B. ₹ 464
C. ₹ 444
D. ₹ 450

(x) S Limited earns ₹ 6 per share, has capitalisation rate of 10% and has a return on investment at the rate of 20%. According to Walter's model, what should be the price per share at 30% dividend payout ratio?

A. ₹ 120
B. ₹ 102
C. ₹ 112
D. ₹ 106

b) State whether the following statements are true or false: [1 × 5 = 5]

(i) The amount of cheques issued by a company not yet paid out is referred to as net float.

(ii) Annual capital charge method is used for evaluating projects having different life spans.

(iii) According to Modigliani and Miller Theory on dividends, dividend pay-out ratio is irrelevant for all firms.

(iv) Simulation is done for capturing the different possible outcomes and determining the probability of a particular event happening.

(v) A call option is the right to sell, whereas a put option is a right to buy.

PART B (75 MARKS)

Question 2.

(a) The sales turnover and profit during 2012-13 and 2013-14 are as follows.

	Sales (₹)	Profit (₹)
Year 2012-13	20,00,000	2,00,000
Year 2013-14	30,00,000	4,00,000

Calculate:

i) Profit Volume Ratio.
ii) Sales required to earn a profit of ₹ 5,00,000
iii) Profit when sales is ₹ 10,00,000 **[1+2+2]**

(b) Ashi Ltd furnishes the following information for the year, 2013 from which you are required to determine the indifference point.

1. Funds required, ₹ 50,000
2. Existing number of Equity shares outstanding, 5000 @ ₹10 per share
3. Existing 10% debt, ₹ 20,000
4. Funds required can be raised either by
(A) issue of 2,000 equity shares, netting ₹ 25 per share or (B) new 15% debt
5. The P/E Ratio will be 7 times in equity alternative and 6 times in debt alternative
6. Corporate tax is levied @ 40%. **[5]**

(c) What is 'Covered Interest Arbitrage'? Briefly state the role of an arbitrageur under covered interest arbitrage. [1+4]

Question 3.

(a) The financial position (extract) of Anju Ltd. On Apr. 1, 2013 and Mar. 31, 2014 is as follows:

Liabilities	Apr. 1, 2013 (₹)	Mar. 31, 2014 (₹)	Assets	Apr. 1, 2013 (₹)	Mar. 31, 2014 (₹)
Current Liabilities for goods	36,000	40,600	Cash	4,000	3,600
			Debtors	35,000	38,000
Loan from ABC Co.		20,000	Stock	25,000	22,000
Loan from Bank	30,000	25,000	Land	20,000	30,000
Hire-purchase Vendor		20,000	Building	50,000	55,000
Capital	1,48,000	1,54,000	Machinery	80,000	86,000
			Delivery Van		25,000
	2,14,000	2,59,600		2,14,000	2,59,600

The delivery van was purchased in March, 2014 on hire-purchase basis; a payment of ₹ 5,000 was made immediately and the balance of amount is to be paid in 10 monthly installments of ₹ 2000 each together with an interest @ 15% p.a. During the year the partners withdrew ₹ 20,000 for personal expenditure. The provision for depreciation against machinery on 31-03-2013 was ₹ 27,000 and 31-03-2014 was ₹ 36,000. You are requested to prepare the Cash Flow Statement. [10]

(b) What is meant by Capital Asset Pricing Model (CAPM)? State the underlying assumptions of CAPM. [1+4]

Question 4.

(a) An Indian bank sells FF 10,00,000 spot to a customer at ₹6.40. At that point of time, the following rates were being quoted.
FF/$: 5.5880/5.5920
₹/$: 35.50/35.60
How much profit do you think the bank has made in the transaction? [5]

(b) Explain the term "Swaps". Outline the possible benefits to Company of undertaking an Interest rate Swap. [2+3]

(c) Given the following quotes for per unit of each currency against US dollar, on two different dates:

	Date 1	Date 2

British Pound	1.5398	1.6385
Canadian Dollar	0.6308	0.6591
EMU euro	0.9666	1.0835
Japanese yen	0.008273	0.008343
Mexican peso	0.1027	0.0917
Swedish Krona	0.1033	0.1179

What is the rate of appreciation or depreciation of each currency over the period?

[5]

Question 5:

(a) AB Ltd. Is considering to buy an equipment and it has two options. The cost of the equipment is ₹100000.
Option I – to buy with borrowed funds at a cost of 18% p.a repayable in five equal installments of ₹ 32000.
Option II – to take the equipment on lease on an annual rental of ₹ 32,000.
The salvage value of the equipment at the end of five year period will be zero. The company uses straight –line depreciation. Assume tax @ 30%.
Which of the two options would you recommend?

Discounting factors are:

	Year 1	Year 2	Year 3	Year 4	Year 5
@ 11%	0.901	0.812	0.731	0.659	0.593
@ 13 %	0.885	0.783	0.693	0.613	0.543
@ 18 %	0.847	0.718	0.609	0.516	0.437

[10]

(a) Role of a Financial Adviser in a Public Sector Undertaking. **[5]**

Question 6:

(a) X Ltd. is foreseeing a growth rate of 14% per annum in the next 2 years. The growth rate is likely to fall to 12 % for the third year and fourth year. After that the growth rate is expected to stabilize at 10% per annum. If the last dividend paid was ₹ 2.25 per share and the investors' required rate of return is 18%, find out the intrinsic value per share of X Ltd. as of date. You may use the following table:

Years	0	1	2	3	4	5
Discounting Factor at 18%	1	0.85	0.72	0.61	0.52	0.44

[8]

(b) Calculate economic value added (EVA) with the help of the following information of HPC Limited:

Financial leverage : 1.4 times

Capital structure	:	**Equity Capital ₹ 425 lacs** **Reserves and surplus ₹ 325 lacs** **10% Debentures ₹ 1000 lacs**
Cost of Equity	:	**17.9%**
Income Tax Rate	:	**30%.**

[7]

Question 7:

(a) The net Sales of W Ltd. is ₹ 45 crores. An earnings before interest and tax of the company as a percentage of net sales is 12%. The capital employed comprises ₹ 15 crores of equity, ₹ 3 crores of 12% Cumulative Preference Share Capital and 13% Debentures of ₹ 9 crores. Income-tax rate is 30%.

(i) Calculate the Return-on-equity for the company

(ii) Calculate the Operating Leverage of the Company given that combined leverage is 4.5

[5+4]

(b) Explain the interrelationship between Investment, Finance and Dividend Decisions. [6]

Question 8:

Write short notes (on any three) [3 ×5 = 15]

(a) Green shoe option

(b) Forward as hedge instrument

(c) Foreign Exchange Risk

(d) 'Financial Engineering'