

M.com part I / sem II
CORPORATE FINANCE
MAY 2018
(2 Hours)

24/5/2018
Q.P.Code: 37756

[Total Marks: 60]

Instructions:

- All questions are compulsory subject to internal choice.
- Figures to the right indicate full marks.
- Make suitable assumptions wherever required and state them.
- Use of Simple calculator is allowed

Q.1) From the following particulars of Imperial Chemicals Ltd. and its industry averages assess 15
the company's strengths and weaknesses in terms of liquidity, solvency and profitability.

Imperial Chemicals Ltd. Balance Sheet as on 31st December, 2013

Liabilities	₹	Assets	₹
Equity Share Capital	2,00,000	Plant & Machinery	3,02,000
10% Preference Share Capital	80,000	Stock	1,21,600
Retained Earnings	54,800	Debtors	72,000
Long – term Debt	68,000	Cash	24,600
Sundry Creditors	63,000		
Outstanding Expenses	2,400		
Other Current Liabilities	52,000		
	5,20,200		5,20,200

Statement of profit for the year ended December 31, 2013

Particulars	₹	₹
Net Sales		4,80,000
Less : Cost of Goods sold	3,05,000	
Selling Expenses	62,000	
Administrative Expenses	39,600	
Interest	5,800	4,12,400
Earnings before Tax		67,600
Less : Income Tax		33,800
Net Income		33,800
Dividend paid to Equity Shareholders		12,000

Financial Ratios of Industry for 2013:

- (1) Current ratio-2.2 to 1
- (2) Stock turnover-2.8 times
- (3) Collection period -56 days
- (4) Income before tax / sales -11.9%
- (5) Return on shareholders equity -10.9%

OR

TURN OVER

Q.1) VRA Limited has provided the following information for the year ending 31st March 2015. 15

Debt Equity Ratio	2 : 1
14% Long Term Debt	₹ 50,00,000
Gross Profit Ratio	30%
Return on Equity (Post Tax)	50%
Income Tax Rate	35%
Capital Turnover Ratio	1.2 times
Opening Stock	₹ 4,50,000
Closing Stock	8% of Sales

You are required to prepare trading and Profit and Loss Account for the year ending 31st March 2015.

Q.2) ABC Ltd. Wishes to raise additional finance of ₹ 20 lakhs for meeting its investment plans. 15

The company has ₹ 4,00,000 in the form of retained earnings available for investment purpose. The following are the further details.

- Debt equity 25 : 75
- Cost of debt at the rate of 10% (before tax) up to ₹ 2,00,000 & 13% (before tax) beyond that.
- Earning per share, ₹12.
- Dividend payout 50% of earnings.
- Expected growth rate in dividend 10%.
- Current market price per share, ₹60.
- Company's tax rate is 30% and shareholder's personal tax rate is 20%.

Required :

- Calculate the post tax average cost of additional debt.
- Calculate the cost of retained earnings and cost of equity.
- Calculate the overall weighted average (after tax) cost of additional finance.

OR

Q.2) The capital structure of Hindustan Trades Ltd. as on 31-3-2014 is as follows : 15

Equity Capital : 100 lakhs equity share of ₹10 each	₹10 crores
Reserves	₹10 crores
14% Debentures of ₹100 each	₹10 crores

For the year ended 31-3-2014 the company has paid equity dividend at 20%. As the company is a market leader with good future, dividend is likely to grow by 5 % every year. The equity shares are now traded at ₹80 per share in the stock exchange. Income tax rate applicable to the company is 50%.

TURN OVER

Required :

- (a) The current weighted average cost of capital.
- (b) The company has plans to raise further ₹ 5 crores by way of long term loan at 16% interest. When this takes place the market value of the equity shares is expected to fall to ₹ 50 per share. What will be the new weighted average cost of capital of the company?

Q.3) The following details relating to a company are given:

15

Sales per annum	1,00,000 units
Variable Cost	₹90 per unit
Fixed Cost including Interest per annum	₹18,00,000
P/V Ratio	25%
10% Debentures	₹30,00,000
Equity Shares Capital (shares of ₹ 10 each)	₹40,00,000
Corporate Tax rate	30 %

Calculate: i) Operating Leverage ii) Financial Leverage iii) Combined Leverage iv) Earnings per share.

OR

Q.3) The capital structure of RST Ltd. is as follows:

15

Particulars	₹
Equity Share of ₹10 each	8,00,000
10 % Preference Share of ₹100 each	5,00,000
12 % Debentures of ₹100 each	7,00,000
	20,00,000

Additional information:

Profit after tax (Tax rate 30%) are ₹2,80,000.

Operating Expenses (including Depreciation ₹96,800) are 1.5 times of EBIT.

Equity Dividend paid is 15%.

Market price of Equity Share is ₹ 23.

Calculate :

- (i) Operating and Financial Leverage
 (ii) Cover for Preference and equity Dividend
 (iii) The Earning Yield ratio and Price Earning ratio

Note: All operating expenses (excluding depreciation) are variable.

Q.4. A) Multiple choice Questions:

(5)

- i) Profit maximization does NOT take into consideration
- a) Risk and cash flow b) Cash flow and stock price
 c) Risk and EPS d) EPS and stock price

TURN OVER

ii) Calculate the present value of ₹1000 to be received at the end of 8 years. Assume an interest rate of 7 percent.

- a) ₹582.00 b) ₹1,718.19
c) ₹531.82 d) ₹5,971.30

iii) Net Operating Profit Ratio

- a) Balance Sheet Ratio b) Revenue Statement Ratio
c) Composite ratio d) None of the above

iv) Marginal cost of Capital is the cost of

- a) Additional sales b) Additional Funds
c) Additional Interest d) None of the above

v) Debt Financing is a cheaper source of finance because of

- a) Time value of Money b) Rate of Interest
c) Tax- deductibility of Interest d) Dividends not Payable to lenders

B) Match the Column:

(5)

Column A	Column B
i) Value of Unlevered firm (V_u)	a) $\frac{\text{Percentage changes in EPS}}{\text{Percentage change in sales}}$
ii) Degree of Combined Leverage	b) Dividend payout ratio, Debt service ratio
iii) Cost of debenture issued / redeemable at par	c) Accounting Values
iv) Coverage ratios	d) $EBIT / K_d$
v) Book value weights	e) $K_d = i(1 - t)$

C) True or false:

(5)

- i) Operating leverage may be defined as $\text{Contribution} \div \text{EPS}$.
ii) The equity shareholders get the residual profit of the firm.
iii) Cost of equity share capital depends upon the market price of the share.
iv) Quick Assets = Current Assets – (Stock – Prepaid Expenses).
v) Effective and nominal rate of interest remain the same irrespective of the frequency of compounding.

OR

Q 4). Write Short notes:

(15)

- i) Perpetuity
ii) Importance of financial management for different stakeholders
iii) Debt Equity Ratio
iv) Cost of retained earnings
v) Features of optimal capital structure