K.J. Somaiya Institute of Management Studies & Research
Course: MFM – III Sem. (2017-20 Batch) End Term Exam
Sub: Advanced Financial Management

Date of Exam: 19th Nov., 2018 Time: 3 Hrs. Marks: 50

1. Solve any FIVE 10 marks each.
2. Correction of first five answers will be considered.
3. New answer on fresh page.
4. Use of scientific calculator is allowed but not financial calculator or mobile phone.

Question No.1
Alpha Limited has furnished the following balance sheet:

Liabilities	**Amount**	**Assets**	**Amount**
Equity Capital (Rs. 10 per share) 15% Debt Retained Earnings Current Liabilities	1000000 2800000 200000 800000	Net Fixed Assets Current Assets	3000000 1800000
Total	4800000	Total	4800000

Additional Information:
The company's total assets turnover is 2.5, its fixed operating costs are Rs.2800000 and the variable operating costs ratio is 60%. The income tax rate is 30%.

(a) Calculate all the three types of leverages
(b) Determine the likely level of EBIT if EPS is (i) Re.1 (ii) Re. 3.

Question No.2
Alpha Ltd. requires funds amounting to Rs.80 lakhs for its new project. To raise funds, the company has following two alternatives:

(A) To issue equity shares amounting toRs.60 lakhs and borrow the balance amount at the interest of 12% p.a.

Or

(B) To issue equity shares and 12% debentures in equal proportion.

The income tax rate is 30%.
Find out the point of indifference between the available two methods of financing and state which option will be beneficial in different situations.

Question No.3
Vijaya Steel Tubes has net operating income (EBIT) of Rs.5000000 and pays a coupon rate of 10% on all debt. Assume there are no taxes and all debt is issued at par.

(a) Under the NI approach, assuming a cost of equity of 15%, computes the value of the firm and overall cost of capital for: (i) An all equity capital structure, (ii) Debt of Rs.23000000, (iii) An all debt capital structure.
(b) Under NOI approach, assuming a cost of capital of 12.5%, computes the value of firm and cost of equity capital for: (i) An all equity capital structure, (ii) Debt of Rs.23000000, (iii) An all debt capital structure.
(c) Explain the basic preposition of NI and NOI Approach.

Question No. 4 (A)
Super Industries had capitalization as shown:

Equity share capital (Rs.10, 1000000 shares)	Rs.10000000
Share premium	50000000
Retained earnings	140000000
Total owners' equity	200000000

Super paid 20% stock dividend. At the time of the stock dividend, the stock was selling at Rs.60 per share.

Show the new capitalization. Explain impact on bonus shares on EPS, P/E and Market price.

Question No. 4 (B)

The following information is available for AC Ltd.:

EPS	Rs. 4
Rate of return on Investment	18%
Rate of return required by shareholder	15%

What will be the price per share as per the Walter Model if the payout ratio is 40%? 50%? 60%?

Question No. 5

The income statement & balance sheet of ME Limited for yr.1 & yr.2 are as follows:

Profit & Loss Account (Rs. In lakhs)	Year 1	Year 2
Net sales	2400	2670
Cost of goods sold	1830	2040
Gross profit	570	630
Selling expenses	180	195
General & administration exp.	180	156
Depreciation	150	192
Operating profit	60	87
Non-operating surplus/deficit	24	30
Profit before interest & tax	84	117
Interest	30	33
Profit before tax	54	84
Tax	21	30
Profit after tax	33	54
Dividends	18	21
Retained earnings	15	33

BALANCE SHEET (Rs. In lakhs)	Year 1	Year2
Assets		
Fixed assets (net)	900	1140
Investments	60	60
Current assets, loans & advances		
• Cash & bank	36	42
• Receivables	540	600
• Inventories	519	576
• Prepaid expenses	123	135
Miscellaneous expenditure & losses	45	42
Total	**2223**	**2595**
Liabilities		
Share capital		
Equity	450	450
Reserves & surplus	354	387
Secured loans		
Term loans	432	525
Bank borrowings	489	597
Current liabilities		
Trade creditors	378	501
Provisions	120	135
Total	**2223**	**2595**

a) Using the percent of sales method (except, assume that dividends are raised to 24, depreciation to 180 & interest to 36) prepare the pro forma income statement for the year 3. Assume that the sales will be Rs 3060 in year 3.
b) Assume that all items on the assets side, except investment & miscellaneous expenditures & losses, will grow proportionally to sales likewise, trade credit will be proportional to sales. Finally estimate the amount of external financing needed for year 3.

The tax rate expected is 35%. This will be the only provision in the year 3.

Question No. 6

From the following information concerning Nebula Limited, prepare a statement showing computation of EVA for the year ended 31st March, 2010. The expectation return of shareholder is 12%.

Summarized Profit and Loss Account

	Amount	**Amount**
Sales		2000000
Less: Expenses		
Less: Cost of goods sold	1200000	
General	200000	
Office and administration	250000	
Selling and distribution	64000	
Interest	36000	1750000
PBIT		250000
Tax @ 40%		100000
Net profit		150000

Summarized Balance Sheet

Liabilities	**Amount**	**Assets**	**Amount**
Equity shares	240000	Fixed assets	600000
Reserves	160000	Stock	120000
Term Loan	240000	Debtors	60000
Current Liabilities	160000	Bank	20000
Total	800000	Total	800000

Question No. 7

Explain various markets in Indian Financial System. What are the various functions performed by SEBI and RBI?

Question No. 8

Lawrence McKibben is preparing a valuation of Tele Norte Leste Participacoes SA (NYSE: TNE), a telecom service company headquartered in Rio de Janeiro, Brazil. McKibben has decided to use three-stage FCFE valuation model and the following estimates. The FCFE per share for current year is $0.75. FCFE is expected to grow at 10% for next year, than at 26% annually for the following three year, and then grow at 6% in year 5 and thereafter. TNE's estimated beta is 2 with risk free rate of return at 4.5% and 5% equity risk premium. What is the value of Tele Norte Leste Participacoes?

Question No. 9

Short Notes (Any two)

1. Sensitivity analysis for project risk analysis
2. Signaling theory
3. Bird in hand argument
4. Residual dividend policy

****