

Roll No.....

Time allowed : 3 hours

Maximum marks : 100

Total number of questions : 7

Total number of printed pages : 6

NOTE : 1. Answer FIVE questions including Question No.1 which is compulsory. All working notes should be shown distinctly.

2. Tables showing the present value of Re.1 and the present value of an annuity of Re.1 for 15 years are annexed.

1. Comment on **any four** of the following :

- (i) Failure of a firm is technical if it is unable to meet its current obligations.
- (ii) In addition to transaction motive, more motives force corporate to hold inventory.
- (iii) CAPM is a tool to workout cost of equity.
- (iv) 'Counter party risk' is faced in forward transactions.
- (v) The function of treasury management is concerned with both macro and micro facets of the economy.

(5 marks each)

2. (a) The following financial data relates to XYZ Ltd. :

Year	Earnings Per Share (Rs.)	Dividend Per Share (Rs.)	Share Price (Rs.)
2004	42	17	252
2005	46	18	184
2006	51	20	255
2007	55	22	275
2008	62	25	372

A firm of market analysts which specialises in the industry in which XYZ Ltd. operates has recently re-evaluated the company's future prospects. The analysts estimate that XYZ Ltd.'s earnings and dividend will grow at 25% for the next three years. Thereafter, earnings are likely to increase at a lower rate of 10%. If this reduction in earnings growth occurs, the analysts consider that the dividend payout ratio will be increased to 50%.

XYZ Ltd. is all equity financed and has 10 lakh ordinary shares in issue. The tax rate of 33% is not expected to change in the foreseeable future. Calculate the estimated share price; and the P/E ratio by using dividend valuation model. For this purpose, you can assume a constant post-tax cost of capital of 18%.

(12 marks)

- (b) An investor buys a NIFTY futures contract for Rs.2,80,000 (lot size 200 futures). On the settlement date, the NIFTY closes at 1,378. Find out his profit or loss, if he pays Rs.1,000 as brokerage. What would be the amount of profit or loss, if he has sold the futures contract ?

(4 marks)

- (c) Ankush Ltd. has a plan to raise an amount of Rs.50 crore for a period of 3 months, 6 months from now. The current rate of interest is 9% but it may rise in 6 months time. The company wants to hedge itself against the increase in interest rate. Bank of India has quoted a forward rate agreement (FRA) at 9.1% per annum. Find out the effect of FRA and actual interest cost to Ankush Ltd., if the actual rate after 6 months happens to be 9.5% or 8.5%.

(4 marks)

3. (a) The management of Laxmi Ltd. has called for a statement showing the working capital needed to finance a level of activity of 6,00,000 units of output for the year 2009. The cost structure for the company's product for the abovementioned level is given as under :

	<i>Cost Per Unit</i> (Rs.)
Raw materials	20
Direct labour	5
Overheads	<u>15</u>
Total costs	40
Profit	<u>10</u>
Selling price	<u><u>50</u></u>

Past trends indicate that raw materials are in stock on an average for three months.

Work-in-progress will approximate to half a month's production. Finished goods remain in warehouse on an average for two months. Suppliers of materials extend one month's credit.

Two months' credit is normally allowed to debtors. A minimum cash balance of Rs.1,00,000 is expected to be maintained. The production pattern is assumed to be even during the year.

You are required to prepare the statement of working capital determination.

(12 marks)

- (b) You sold Hong Kong \$1,00,00,000 value spot to your customer at Rs.5.70/HK \$ and covered yourself in London market on the same day, when the exchange rates were :

US \$1=HK \$7.5880 and HK \$7.5920.

Local inter-bank market rates for US\$ were -

Spot US \$1=Rs.42.70 and Rs.42.85.

Calculate – (i) cover rate; and (ii) ascertain profit or loss in transaction. Ignore taxation.

(4 marks)

- (c) "Discounted cash flow is very close to economic value added." Comment.

(4 marks)

4. Distinguish between **any four** of the following :

- (i) 'Financing of current assets' and 'financing of fixed assets'.
- (ii) 'Financial derivatives' and 'commodity derivatives'.
- (iii) 'Interest rate parity' and 'purchasing power parity'.
- (iv) 'Capital structure' and 'financial structure'.
- (v) 'Liquidity management' and 'treasury management'.

(5 marks each)

5. (a) Sumati Ltd. is considering three finance plans. Total investments required is Rs.2,00,000.

Plan	Equity	Debt	Preference Shares
A	100%	—	—
B	50%	50%	—
C	50%	—	50%

Cost of debt : 8%

Cost of preference shares : 8%

Tax rate : 30%.

Equity shares of face value of Rs.10 each will be issued at a premium of Rs.10 per share.

Expected EBIT is Rs.80,000.

You are required to calculate for each finance plan –

- (i) Earnings per share (EPS); and
- (ii) EBIT range among the EPS equivalency point.

(6 marks each)

- (b) Rosa Chemicals Ltd. has outstanding 1,20,000 shares selling at Rs.20 per share. The company hopes to make a net income of Rs.3,50,000 during the year ending 31st March, 2009. The company is thinking of paying a dividend of Rs.2 per share at the end of current year. The capitalisation rate for risk class of this firm has been estimated to be 15%. Assuming no taxes, answer the questions listed below on the basis of the Modigliani Miller dividend valuation model :

- (i) What will be the price of share at the end of 31st March, 2009, if - (a) the dividend is paid; and (b) the dividend is not paid ?

(6 marks)

- (ii) How many new shares the company must issue if the dividend is paid and company needs Rs.9,50,000 for an approved investment expenditure during the year ?

(2 marks)

6. An iron ore company is considering investing in a new processing facility. The company extracts ore from an open pit mine. During a year, 1,00,000 tons of ore is extracted. If the output from the extraction process is sold immediately upon removal of dirt, rocks and other impurities, a price of Rs.1,000 per ton of ore can be obtained. The company has estimated that its extraction costs amount to 70% of the net realisable value of the ore.

As an alternative to selling all the ore at Rs.1,000 per ton, it is possible to process further 25% of the output. The additional cash cost of further processing would be Rs.100 per ton. The processed ore would yield 80% final output and can be sold at Rs.1,350 per ton.

For additional processing the company would have to install equipments costing Rs.100 lakh. The equipment is expected to have a useful life of 5 years with no salvage value. The company follows the straight line method of depreciation. Additional working capital requirement is estimated at Rs.10 lakh. The company's cut-off rate for such investments is 15%. Assume corporate tax rate 30% (including surcharge and education cess).

Should the company install the equipment for further processing of the iron ore ?

(20 marks)

7. Write notes on **any four** of the following :

- (i) Participating preference shares
- (ii) Credit investigation factors
- (iii) Transfer pricing
- (iv) Risks in forex market
- (v) Financial distress.

(5 marks each)

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TABLE – 1 : PRESENT VALUE OF RUPEE ONE

RATE	YEAR	YEAR	YEAR	YEAR	YEAR	YEAR	YEAR	YEAR	YEAR	YEAR	YEAR	YEAR	YEAR	YEAR	YEAR	YEAR	YEAR	YEAR
	1	2	3	4	5	6	7	8	9	10	11	12	13	14	15			
5%	0.9524	0.9070	0.8638	0.8227	0.7835	0.7462	0.7107	0.6768	0.6446	0.6139	0.5847	0.5568	0.5303	0.5051	0.4810			
6%	0.9434	0.8900	0.8396	0.7921	0.7473	0.7050	0.6651	0.6274	0.5919	0.5584	0.5268	0.4970	0.4688	0.4423	0.4173			
7%	0.9346	0.8734	0.8163	0.7629	0.7130	0.6663	0.6227	0.5820	0.5439	0.5083	0.4751	0.4440	0.4150	0.3878	0.3624			
8%	0.9259	0.8573	0.7938	0.7350	0.6806	0.6302	0.5835	0.5403	0.5002	0.4632	0.4289	0.3971	0.3677	0.3405	0.3152			
9%	0.9174	0.8417	0.7722	0.7084	0.6499	0.5963	0.5470	0.5019	0.4604	0.4224	0.3875	0.3555	0.3262	0.2992	0.2745			
10%	0.9091	0.8264	0.7513	0.6830	0.6209	0.5645	0.5132	0.4665	0.4241	0.3855	0.3505	0.3186	0.2897	0.2633	0.2394			
11%	0.9009	0.8116	0.7312	0.6587	0.5935	0.5346	0.4817	0.4339	0.3909	0.3522	0.3173	0.2858	0.2575	0.2320	0.2090			
12%	0.8929	0.7972	0.7118	0.6355	0.5674	0.5066	0.4523	0.4039	0.3606	0.3220	0.2875	0.2567	0.2292	0.2046	0.1827			
13%	0.8850	0.7831	0.6931	0.6133	0.5428	0.4803	0.4251	0.3762	0.3329	0.2946	0.2607	0.2307	0.2042	0.1807	0.1599			
14%	0.8772	0.7695	0.6750	0.5921	0.5194	0.4556	0.3996	0.3506	0.3075	0.2697	0.2366	0.2076	0.1821	0.1597	0.1401			
15%	0.8696	0.7561	0.6575	0.5718	0.4972	0.4323	0.3759	0.3269	0.2843	0.2472	0.2149	0.1869	0.1625	0.1413	0.1229			
16%	0.8621	0.7432	0.6407	0.5523	0.4761	0.4104	0.3538	0.3050	0.2630	0.2267	0.1954	0.1685	0.1452	0.1252	0.1079			
17%	0.8547	0.7305	0.6244	0.5337	0.4561	0.3898	0.3332	0.2848	0.2434	0.2080	0.1778	0.1520	0.1299	0.1110	0.0949			
18%	0.8475	0.7182	0.6086	0.5158	0.4371	0.3704	0.3139	0.2660	0.2255	0.1911	0.1619	0.1372	0.1163	0.0985	0.0835			
19%	0.8403	0.7062	0.5934	0.4987	0.4190	0.3521	0.2959	0.2487	0.2090	0.1756	0.1476	0.1240	0.1042	0.0876	0.0736			
20%	0.8333	0.6944	0.5787	0.4823	0.4019	0.3349	0.2791	0.2326	0.1938	0.1615	0.1346	0.1122	0.0935	0.0779	0.0649			
21%	0.8264	0.6830	0.5645	0.4665	0.3855	0.3186	0.2633	0.2176	0.1799	0.1486	0.1228	0.1015	0.0839	0.0693	0.0573			
22%	0.8197	0.6719	0.5507	0.4514	0.3700	0.3033	0.2486	0.2038	0.1670	0.1369	0.1122	0.0920	0.0754	0.0618	0.0507			
23%	0.8130	0.6610	0.5374	0.4369	0.3552	0.2888	0.2348	0.1909	0.1552	0.1262	0.1026	0.0834	0.0678	0.0551	0.0448			
24%	0.8065	0.6504	0.5245	0.4230	0.3411	0.2751	0.2218	0.1789	0.1443	0.1164	0.0938	0.0757	0.0610	0.0492	0.0397			
25%	0.8000	0.6400	0.5120	0.4096	0.3277	0.2621	0.2097	0.1678	0.1342	0.1074	0.0859	0.0687	0.0550	0.0440	0.0352			

TABLE – 2 : PRESENT VALUE OF AN ANNUITY OF RUPEE ONE

RATE	YEAR	YEAR	YEAR	YEAR	YEAR	YEAR	YEAR	YEAR	YEAR	YEAR	YEAR	YEAR	YEAR	YEAR	YEAR	YEAR	YEAR	YEAR
	1	2	3	4	5	6	7	8	9	10	11	12	13	14	15			
5%	0.9524	1.8594	2.7232	3.5460	4.3295	5.0757	5.7864	6.4632	7.1078	7.7217	8.3064	8.8633	9.3936	9.8986	10.3797			
6%	0.9434	1.8334	2.6730	3.4651	4.2124	4.9173	5.5824	6.2098	6.8017	7.3601	7.8869	8.3838	8.8527	9.2950	9.7122			
7%	0.9346	1.8080	2.6243	3.3872	4.1002	4.7665	5.3893	5.9713	6.5152	7.0236	7.4987	7.9427	8.3577	8.7455	9.1079			
8%	0.9259	1.7833	2.5771	3.3121	3.9927	4.6229	5.2064	5.7466	6.2469	6.7101	7.1390	7.5361	7.9038	8.2442	8.5595			
9%	0.9174	1.7591	2.5313	3.2397	3.8897	4.4859	5.0330	5.5348	5.9952	6.4177	6.8052	7.1607	7.4869	7.7862	8.0607			
10%	0.9091	1.7355	2.4869	3.1699	3.7908	4.3553	4.8684	5.3349	5.7590	6.1446	6.4951	6.8137	7.1034	7.3667	7.6061			
11%	0.9009	1.7125	2.4437	3.1024	3.6959	4.2305	4.7122	5.1461	5.5370	5.8892	6.2065	6.4924	6.7499	6.9819	7.1909			
12%	0.8929	1.6901	2.4018	3.0373	3.6048	4.1114	4.5638	4.9676	5.3282	5.6502	5.9377	6.1944	6.4235	6.6282	6.8109			
13%	0.8850	1.6681	2.3612	2.9745	3.5172	3.9975	4.4226	4.7988	5.1317	5.4262	5.6869	5.9176	6.1218	6.3025	6.4624		..	
14%	0.8772	1.6467	2.3216	2.9137	3.4331	3.8887	4.2883	4.6389	4.9464	5.2161	5.4527	5.6603	5.8424	6.0021	6.1422		o	
15%	0.8696	1.6257	2.2832	2.8550	3.3522	3.7845	4.1604	4.4873	4.7716	5.0188	5.2337	5.4206	5.5831	5.7245	5.8474		..	
16%	0.8621	1.6052	2.2459	2.7982	3.2743	3.6847	4.0386	4.3436	4.6065	4.8332	5.0286	5.1971	5.3423	5.4675	5.5755			
17%	0.8547	1.5852	2.2096	2.7432	3.1993	3.5892	3.9224	4.2072	4.4506	4.6586	4.8364	4.9884	5.1183	5.2293	5.3242			
18%	0.8475	1.5656	2.1743	2.6901	3.1272	3.4976	3.8115	4.0776	4.3030	4.4941	4.6560	4.7932	4.9095	5.0081	5.0916			
19%	0.8403	1.5465	2.1399	2.6386	3.0576	3.4098	3.7057	3.9544	4.1633	4.3389	4.4865	4.6105	4.7147	4.8023	4.8759			
20%	0.8333	1.5278	2.1065	2.5887	2.9906	3.3255	3.6046	3.8372	4.0310	4.1925	4.3271	4.4392	4.5327	4.6106	4.6755			
21%	0.8264	1.5095	2.0739	2.5404	2.9260	3.2446	3.5079	3.7256	3.9054	4.0541	4.1769	4.2784	4.3624	4.4317	4.4890			
22%	0.8197	1.4915	2.0422	2.4936	2.8636	3.1669	3.4155	3.6193	3.7863	3.9232	4.0354	4.1274	4.2028	4.2646	4.3152			
23%	0.8130	1.4740	2.0114	2.4483	2.8035	3.0923	3.3270	3.5179	3.6731	3.7993	3.9018	3.9852	4.0530	4.1082	4.1530			
24%	0.8065	1.4568	1.9813	2.4043	2.7454	3.0205	3.2423	3.4212	3.5655	3.6819	3.7757	3.8514	3.9124	3.9616	4.0013			
25%	0.8000	1.4400	1.9520	2.3616	2.6893	2.9514	3.1611	3.3289	3.4631	3.5705	3.6564	3.7251	3.7801	3.8241	3.8593			