MOCK TEST PAPER –2

INTERMEDIATE: GROUP – II

PAPER – 8: FINANCIAL MANAGEMENT & ECONOMICS FOR FINANCE

PAPER 8A: FINANICAL MANAGEMENT

Answers are to be given only in English except in the case of the candidates who have opted for Hindi medium. If a candidate has not opted for Hindi medium his/ her answers in Hindi will not be valued.

Question No. **1** is compulsory.

Attempt any **four** questions from the remaining **five** questions.

Working notes should form part of the answer.

Time Allowed – 3 Hours (Total time for 8A and 8B) **Maximum Marks – 60**

1. Answer the following:

(a) Rambow Ltd. is contemplating purchasing machinery that would cost ₹ 10,00,000 plus GST @ 18% at the beginning of year 1. Cash inflows after tax from operations have been estimated at ₹ 2,56,000 per annum for 5 years. The company has two options for the smooth functioning of the machinery - one is service, and another is replacement of parts. The company has the option to service a part of the machinery at the end of each of the years 2 and 4 at ₹ 1,00,000 plus GST @ 18% for each year. In such a case, the scrap value at the end of year 5 will be ₹ 76,000. However, if the company decides not to service the part, then it will have to be replaced at the end of year 3 at ₹ 3,00,000 plus GST@ 18% and in this case, the machinery will work for the 6th year also and get operational cash inflow of ₹ 1,86,000 for the 6th year. It will have to be scrapped at the end of year 6 at ₹ 1,36,000.

Assume cost of capital at 12% and GST paid on all inputs including capital goods are eligible for input tax credit in the same month as and when incurred.

(i) DECIDE whether the machinery should be purchased under option 1 or under option 2 or it shouldn't be purchased at all.

(ii) If the supplier gives a discount of ₹ 90,000 for purchase, WHAT would be your decision?

Note: The PV factors at 12% are:

Year	0	1	2	3	4	5	6
PV Factor	1	0.8928	0.7972	0.7118	0.6355	0.5674	0.5066

(5 Marks)

(b) Sundaram limited a plastic manufacturing company had invested enormous amount of money in a new expansion project. Due to such a great amount of capital investment, Company needs an additional ₹ 2,00,00,000 in working capital immediately. The CFO has determined the following three feasible sources of working capital funds:

Bank Loan: The company's bank will lend ₹2,30,00,000 at 12% per annum. However, the bank will require 15% of the loan granted to be kept in a current account as the minimum average balance which otherwise would have been just ₹ 50,000.

Trade Credit: A major supplier with 2/20 net 80 credit terms has approached for supply of raw material worth ₹1,90,00,000 p.m.

Factoring: factoring firm will buy the companies receivables of ₹ 2,50,00,000 per month, which have a collection period of 60 days. factor will advance up to 75% of the face value of the receivables at 14 percent per annum. Factor Commission will amount to 2% on all receivables purchased. Factoring will save credit department expense and bad debts of ₹ 1,75,000 p.m. and ₹ 2,25,000 p.m.

Based on annual percentage cost, ADVISE which alternative should the company select. Assume 360 days a year **(5 Marks)**

(c) Manchow Limited and Noodles Limited are generating same level of Operating Income. The margin of safety for Manchow Ltd is 0.4 and for Noodles Limited it is 1.25 times of Manchow Ltd. The Interest expense of Manchow Limited is ₹ 22,50,000 and it is 40% lower for Noodles Limited. Financial Leverages of Manchow Limited and Noodles Limited are 3 and 2 respectively. Profit Volume Ratio for both companies stand as 40% and 50% respectively. Assuming a tax rate of 30%, PREPARE income statement for both companies **(5 Marks)**

(d) Using the following information, PREPARE the balance sheet:

Long-term debt to net worth	0.25
Total asset turnover	3
Average collection period	9 days
Inventory turnover	13
Gross profit margin	20%
Acid-test ratio	1.5

*Assume a 360-day year and all sales on credit.

Liabilities	₹	Assets	₹
Notes and payables	2,50,000	Cash	?
Long-term debt	?	Accounts receivable	?
Common stock	8,00,000	Inventory	?
Retained earnings	16,00,000	Plant and equipment	?
Total liabilities and equity	?	Total assets	?

(5 Marks)

2. Based on the details given below, you are required to UNDERTAKE NPV sensitivity analysis for the factors of Sales Price, Sales units, Variable cost, Fixed Cost and Initial Investment for a 10% adverse variation in each of the mentioned factors Assume straight line depreciation is allowed for tax purpose

Initial Investment	₹ 15,00,000
Tenure of Project (Years)	4
Sales Units	6000
Sales Price p.u.	₹ 250
Variable Cost p.u.	₹ 80
Fixed Cost	₹ 2,00,000
Tax Rate	30%
Salvage Value	₹ 1,50,000
Cost of Capital	14%

Use the below PV factors for calculation purpose

Year	0	1	2	3	4
PVF @ 14%	1.00	0.8772	0.7695	0.6750	0.5921

(10 Marks)

3. Rex Ltd has 20 lakh equity shares outstanding at the start of the accounting year 2023. The existing market price per share is ₹ 300. Expected dividend is ₹ 20 per share. The rate of capitalization appropriate to the risk class to which the company belongs is 20%.

   CALCULATE the market price per share when expected dividends are: (a) declared, and (b) not declared, based on the Miller – Modigliani approach.

   CALCULATE number of shares to be issued by the company at the end of the accounting year on the assumption that the net income for the year is ₹ 5 crore; investment budget is ₹ 8 crores, when (a) Dividends are declared, and (b) Dividends are not declared.

   PROVE that the market value of the shares at the end of the accounting year will remain unchanged irrespective of whether (a) Dividends are declared, or (ii) Dividends are not declared.

   WHAT is the implied growth rate in dividends as per Gordon's model, if expected dividend payment is considered imminent? **(10 Marks)**

4. Following data is available in respect of two companies having same business risk:

   Capital employed = ₹ 12,00,000, EBIT = ₹ 2,40,000 and Ke = 15%

Sources	Dumbo Ltd (₹)	Jumbo Ltd (₹)
Debt (@12%)	4,00,000	Nil
Equity	8,00,000	12,00,000

   An investor is holding 20% shares in the levered company. CALCULATE the increase in annual earnings of investor if arbitrage process is undertaken.

   Also EXPLAIN the arbitrage process if Ke = 20% for Dumbo Ltd instead of 15%. **(10 Marks)**

5. Genzy Ltd. is planning to introduce a new product with a project life of 10 years. The initial equipment cost will be ₹ 2.5 crores. At the end of 10 years, the equipment will have a resale value of 50 lakhs. A working capital of ₹ 30,00,000 will be needed and it will be released at the end of the tenth year. The project will be financed with the following capital sources.

Particulars	Amount (₹)	Issue Price (Market price)
Equity Share Capital of Face value ₹ 10 each	1,50,00,000	₹30
Debentures of face value ₹ 100 each with a maturity of 10 years	90,00,000	₹90
Preference shares of ₹ 100 each with a maturity of 10 years	60,00,000	₹96

   The existing yield on T-bills is averaging 8% p.a. The systematic risk measure for the proposed project is 1.6. NSE NIFTY is expected to yield 14% p.a. on average for the foreseeable future. Debenture holders have been promised a coupon of 12% and preference shareholders have been committed a dividend of 15%.

The sales volumes over 10 years have been estimated as follows:

Year	1	2	3-5	6-8	9-10
Units per year	70,000	98,000	2,10,000	2,50,000	1,20,000

A sales price of ₹ 300 per unit is expected and variable expenses will amount to 60% of sales revenue. Fixed cash operating costs will amount to ₹ 40,00,000 per year. The loss of any year will be set off from the profits of subsequent years.

The company is subject to a 30 per cent tax rate. The company follows straight line method of depreciation which is to be assumed to be admissible for tax purpose also.

CALCULATE the net present value of the project for the company and advise the management to take appropriate decision.

The PV factors are to be taken as rounded figures upto 2 decimals. Use market value weights to COMPUTE overall cost of capital. **(10 Marks)**

6. Attempt any **2**

(i) DISTINGUISH between Profit maximisation vis-a-vis wealth maximization.

(ii) WRITE a note on agency problem and agency cost.

(iii) EXPLAIN the determinants of dividend decisions. **(10 Marks)**

PAPER 8B: ECONOMICS FOR FINANCE

Question 1 is compulsory.

Students can answer 3 out of the 4 remaining.

Maximum Marks – 40

1. (a) What is the distinction between the Personal Income and Disposal Personal Income? **(2 Marks)**

(b) What are the significance of Gross Investment? **(3 Marks)**

(c) From the following data, calculate National income by Income and Expenditure Method: **(5 Marks)**

S. No.	Particulars	₹ in crores
1	Government final consumption expenditure	I65
2	Compensation of Employees	200
3	Rent	300
4	Private final consumption expenditure	600
5	Gross domestic capital formation	80
6	Mixed Income of self employed	75
7	Net factor income paid from abroad	60
8	Interest	40
9	Profit	230
10	Net exports	60

2. (a) What is the classical theory of determination of National Income? **(3 Marks)**

(b) What is the relationship between marginal propensity to Consume (MPC) and Multiplier? **(2 Marks)**

(c) In a three-sector economy what role does the Government Play? **(3 Marks)**

(d) From the Following data calculate Y:

Particulars	₹ Crores
Consumption	800
Investment	400
Government Purchases	100
Exports	200
Imports	300

(2 Marks)

3. (a) What is the rationale of government Subsidy? **(3 Marks)**

(b) What are the government initiative towards negative externalities? **(2 Marks)**

(c) What do you understand by depreciation of a currency? **(2 Marks)**

(d) What is Market Stabilization Scheme? **(3 Marks)**

4. (a) What are the non-technical measure of an instrument of trade Policy? **(3 Marks)**

(b) What are the main Characteristics of merit goods? **(2 Marks)**

(c) What is the relationship between Interest rate and demand for money? **(2 Marks)**

(d) What is the distinction between Anti-Dumping Duties and Countervailing Duties? **(3 Marks)**

5. (a) What is Consumer Price Index (CPI) **(2 Marks)**

(b) What do you understand by Free Rider Problem? **(3 Marks)**

(c) What is the essence of “MFN Principle”? **(3 Marks)**

(d) What is the Social Cost? **(2 Marks)**

OR

What is Credit Money?