Test Series: September 2023

MOCK TEST PAPER 1

INTERMEDIATE: GROUP – II

PAPER – 8: FINANCIAL MANAGEMENT & ECONOMICS FOR FINANCE

PAPER – 8A: FINANCIAL MANAGEMENT

*Question No. **1** is compulsory.*

*Attempt any **four** questions out of the remaining **five** questions.*

In case, any candidate answers extra question(s)/ sub-question(s) over and above the required number, then only the requisite number of questions first answered in the answer book shall be valued and subsequent extra question(s) answered shall be ignored.

Working notes should form part of the answer.

1. (a) Bhaskar Manufactures Ltd. have Equity Share Capital of ₹ 5,00,000 (face value ₹100) to meet the expenditure of an expansion programme, the company wishes to raise ₹ 3,00,000 and is having following four alternative sources to raise the funds:

Plan A: To have full money from equity shares.

Plan B: To have ₹ 1 lakhs from equity and ₹ 2 lakhs from borrowing from the financial institution @ 10% p.a.

Plan C: Full money from borrowing @ 10% p.a.

Plan D: ₹1 lakh in equity and ₹ 2 lakhs from preference shares at 8% p.a.

The company is expected to have an earning of ₹ 1,50,000. The corporate tax is 50%. Suggest a suitable plan of the above four plans to raise the required funds. **(5 Marks)**

(b) Following information has been provided from the books of Laxmi Pvt. Ltd. for the year ending on 31st March 2022:

Net Working Capital	₹ 5,40,000
Bank overdraft	₹ 1,00,000
Fixed Assets to Proprietary ratio	0.75
Reserves and Surplus	₹ 4,80,000
Current ratio	2.5
Liquid ratio (Quick Ratio)	1.5

You are required to PREPARE a summarised Balance Sheet as of 31st March 2022 assuming that there is no long-term debt. **(5 Marks)**

(c) A new project "Ambar" requires an initial outlay of ₹ 4,50,000. The company uses certainty equivalent method approach to evaluate the project. The risk-free rate is 7%. Following information is available:

Year	Cash Flow After Tax (₹)	Certainty Equivalent Coefficient
1	1,50,000	0.90
2	2,25,000	0.80
3	1,75,000	0.58
4	1,50,000	0.56
5	70,000	0.50

PV Factor at 7%

Year	1	2	3	4	5
PV Factor	0.935	0.873	0.816	0.763	0.713

Is investment in the project beneficial based on above information? **(5 Marks)**

(d) ABC Company's equity share is quoted in the market at ₹ 30 per share currently. The company pays a dividend of ₹ 3 per share and the investor's market expects a growth rate of 7% per year.

You are required to:

(i) CALCULATE the company's cost of equity capital.

(ii) If the company issues 10% debentures of face value of ₹ 100 each and realises ₹ 95 per debenture while the debentures are redeemable after 10 years at a premium of 10%, CALCULATE cost of debenture using YTM?

Assume Tax Rate to be 50%. **(5 Marks)**

2. ZX Ltd. has a paid-up share capital of ₹ 2,00,00,000, face value of ₹ 100 each. The current market price of the shares is ₹ 100 each. The Board of Directors of the company has an agenda of meeting to pay a dividend of 50% to its shareholders. The company expects a net income of ₹ 1,50,00,000 at the end of the current financial year. Company also plans for a capital expenditure for the next financial year for a cost of ₹ 1,90,00,000, which can be financed through retained earnings and issue of new equity shares.

Company's desired rate of investment is 15%.

Required:

Following the Modigliani- Miller (MM) Hypothesis, DETERMINE value of the company when:

(i) It does not pay dividend and

(ii) It does pay dividend **(10 Marks)**

3. Following are the selected financial information of A Ltd. and B Ltd. for the current Financial Year:

	A Ltd.	B Ltd.
Variable Cost Ratio	60%	50%
Interest	₹ 30,000	₹ 1,20,000
Operating Leverage	6	3
Financial Leverage	4	3
Tax Rate	30%	30%

You are required to FIND out:

(i) EBIT

(ii) Sales

(iii) Fixed Cost

(iv) Identify the company which is better placed with reasons based on leverages. **(10 Marks)**

4. A company needs ₹ 42,50,000 for the construction of a new plant. The following three plans are feasible:

I The company may issue 4,25,000 equity shares at ₹ 10 per share.

II The company may issue 2,12,500 equity shares at ₹ 10 per share and 21,250 debentures of ₹ 100 denominations bearing an 8% rate of interest.

III The company may issue 2,12,500 equity shares at ₹ 10 per share and 21,250 cumulative preference shares at ₹ 100 per share bearing an 8% rate of dividend.

(i) The company's earnings before interest and taxes are ₹ 75,000, ₹ 1,50,000, ₹ 3,00,000, ₹ 4,50,000 and ₹ 7,50,000. DETERMINE earnings per share under each of three financial plans? Assume a corporate income tax rate of 40%.

(ii) IDENTIFY which alternative would you recommend and why?

(iii) DETERMINE the EBIT-EPS indifference points by formulae between Financing Plan I and Plan II and Plan I and Plan III. **(10 Marks)**

5. A firm can make investment in either of the following two projects. The firm anticipates its cost of capital to be 10%. The pre-tax cash flows of the projects for five years are as follows:

Year	0	1	2	3	4	5
Project A (₹)	(3,00,000)	55,000	1,20,000	1,30,000	1,05,000	40,000
Project 8 (₹)	(3,00,000)	3,18,000	20,000	20,000	8,000	6,000

Ignore Taxation.

An amount of ₹ 45,000 will be spent on account of sales promotion in year 3 in case of Project A. This has not been considered in calculation of pre-tax cash flows.

The discount factors are as under:

Year	0	1	2	3	4	5
PVF (10%)	1	0.91	0.83	0.75	0.68	0.62

You are required to calculate for each project:

(i) The payback period

(ii) The discounted payback period

(iii) Desirability factor

(iv) Net Present Value **(10 Marks)**

6. (a) EXPLAIN the difference between Business risk and financial risk. **(4 Marks)**

(b) EXPLAIN in brief the features of Commercial Papers. **(4 Marks)**

(c) EXPLAIN in short, the term Letter of Credit. **(2 Marks)**

OR

"Financing a business through borrowing is cheaper than using equity." Briefly EXPLAIN.

PAPER 8B: ECONOMICS FOR FINANCE

Question 1 is compulsory

Students can answer 3 out of the 4 remaining

1. (a) What are the challenges involved in National Income Computation **(3 Marks)**

   (b) What are the challenges before the government to design the budgetary Policy? **(2 Marks)**

   (c) From the following data, calculate GNP at MP by Income and Expenditure Method **(5 Marks)**

S. No.	Particulars	₹ in crores
1.	Mixed income of self-employed	600
2.	Compensation of employees	400
3.	Private final consumption expenditure	800
4.	Net factor income from abroad	10
5.	Net indirect tax	200
6.	Consumption of fixed capital	320
7.	Net domestic capital formation	480
8.	Net exports	20
9.	Profit	650
10.	Rent	300
11.	Interest	250
12.	Government final consumption expenditure	350

2. (a) Identify the significance of intermediate good? **(3 Marks)**

   (b) How do imports effect investment multiplier? **(2 Marks)**

   (c) In a three-sector economy what role does the government play? **(2 Marks)**

   (d) An increase in investment by ₹ 800 Crore leads to increase in National Income by ₹ 4000 Crore. Calculate MPC and Change in saving. **(3 Marks)**

3. (a) How is the National Income Calculated by the Income Method? **(3 Marks)**

   (b) What are the Variety of allocation instruments available by the government which can influence resource allocation? **(2 Marks)**

   (c) What is the objective of Government Subsidy? **(2 Marks)**

   (d) What are the four possible type of externalities? **(3 Marks)**

4. (a) What is the aim of government distribution function? **(3 Marks)**

   (b) What is hybrid good? **(2 Marks)**

   (c) Explain the concept of Liquidity Trap? **(3 Marks)**

   (d) What are the modes of Foreign Direct Investment? **(2 Marks)**

5. (a) Distinguish between the Anti-Dumping Duties and Countervailing Duties? **(3 Marks)**

   (b) Distinguish between Nominal versus real exchange rate? **(3 Marks)**

(c) What could be the outcome of Free Rider Problem associated with Public Good? **(2 Marks)**

(d) Question: Given Consumption Function is C = 200 + 0.75 Y; Investment = ₹ 700; Net Imports = ₹ 300. **(2 Marks)**

Calculate equilibrium level of output.

Or

Define Real Effective Exchange Rate (REER)?