VPM's
DR VN BRIMS, Thane
Programme: PGDM (2019-21)
PGDM Trimester II Examination January 2020

Subject	**Corporate Finance**		
Roll No.		**Marks**	**60 Marks**
Total No. of Questions	7	**Duration**	**3 Hours**
Total No. of printed pages	3	**Date**	**04.01.2020**

Note: Q1 is compulsory and solve any FOUR from the remaining SIX questions.

Q1) 20 Marks (Compulsory) [8 + 4 + 8]

a) Flipkart is one of the most successful players in the Indian E-commerce industry and has a market share of 30% in the organized e-retail sector. It is planning to expand further in the rural areas in Maharashtra and hence require additional capital. You are the Credit Manager working in SBI Thane Branch for corporate loan department. Flipkart has approached SBI for a long-term loan facility of Rs.20 crores. It has submitted the following information to you for preliminary examination. You are in charge for undertaking ratio analysis using the given data.

Profit & Loss Statement (Extract)

Particulars	**Amount (Rs crores)**
Sales	500
COGS	200
Admin Expenses	50
S&D Expenses	20
12% Debentures	50
Loss on sale of Machinery	20
Provision for Tax	30%
No. of Equity Shares	20 crores

You have decided to calculate the following ratios based on profit and loss statements: Net profit ratio, Operating Profit Ratio, Interest Coverage Ratio & EPS. **[8 Marks]**

Balance Sheet (Extract)

Particulars	**Amount (Rs Crores)**
Equity Share Capital	70
12% Debentures	50
R&S	200
Current Liabilities	40
Current Assets	120
Fixed Assets	200
Long Term Investments	40

Based on balance sheet you have decided to calculate the following ratios: **[4 Marks]**
Proprietary Ratio & Debt to Equity Ratio
Some combined ratios are also required: Total Asset Turnover, ROCE, ROE & ROA
[8 Marks]

Attempt Any FOUR from the Remaining SIX Questions

Q2) ***Any two from (a) or (b) or (c) ————— (5x2) = 10 Marks***

a) Draw diagrams of Modigliani-Miller theory and Explain the same
b) Explain the use and types of Financial Ratios?
c) What is Financial Indifference Point? Describe its significance using the diagram.

Q3) ***Any one from (a) or (b) ————— (10x1) = 10 Marks***

a) Calculate Operating Leverage, Financial Leverage, Combined Leverage & EPS

Particulars	**Amount**

Sales per annum	50,000 units
Variable cost	Rs.45 per unit
Fixed cost (Excluding interest)	Rs.2,50,000
P/V Ratio	25%
10% Debentures	5,00,000
Total Equity Share Capital (share of Rs.10 each)	Rs.4,00,000
Corporate Tax Rate	30%

b) Equity Share Capital (Rs.10 each) Rs.6,00,000, 10% Preference Share Capital Rs.4,00,000, Net profit after tax Rs.5,00,000; equity dividend paid: 15%; Market price of equity shares, Rs 80. You are required to compute the following, showing the necessary workings:
1) Dividend yield on the equity shares
2) Cover for the equity & preference dividends
3) Earnings per share
4) Price earnings ratio.

Q4) ***Any one from (a) or (b) ————— (10x1) = 10 Marks***

a) Ambitious ltd. has the following book-value structure as on March, 31,2019

Particulars	Amount
Equity share capital	20,00,000
13% preference share	5,00,000
8% debenture	25,00,000
	50,00,000

The equity share of the company sells for Rs 40. It is expected that the company will pay next year a dividend of Rs 5 per equity share, which is expected to grow at 7% p.a forever. Assume a 35% corporate tax rate

Compute weighted average cost of capital (WACC) of the company based on the existing capital structure.

b) Write whether the following statements are True or False (Just write True or False; don't rewrite the entire sentence)

i. A company should always have higher financial leverage
ii. Cost of Capital acts as a Maximum Rate of Return that the company should earn on its capital employed
iii. Interest Coverage Ratio is a Turnover or Activity type of Ratio
iv. Capital Employed is equal to Net Worth
v. NOI theory of capital structure says that changes in capital structure do not affect the cost of capital
vi. D1 is the expected dividend in the next year
vii. In CAPM, the term 'Rm-Rf' is called as 'Market Return Premium'
viii. Market Value weights are preferred in reality over Book value weights to calculate WACC.
ix. If interest rates are positive in the economy then Future Value will always be higher than Present Value.
x. As per Walter Model, 0% dividend payout is optimum when R>Ke

Q5) ***Any one from (a) or (b) ————— (10x1) = 10 Marks***

a) The existing capital structure of Trim Ltd. is as under:

Equity Shares of Rs.100 each	Rs.20,00,000
Retained Earnings	Rs.10,00,000
9% Preference Shares	Rs.15,00,000
7% Debentures	Rs. 5,00,000

The existing rate of return on the company's capital is 10% and the income tax rate is 50%. The company requires a sum of Rs.25,00,000 to finance its expansion programme for which it is considering the following alternatives:

i. Issue of 20,000 Equity Shares at a premium of Rs.25 per share.
ii. Issue of 10% Preference Shares.
iii. Issue of 8% Debentures.

It is estimated that the Price Earnings Ratio in the cases of equity, preference and Debenture financing would be 20, 17 and 16 respectively.
Which of the above alternatives would you consider to be the best? Why?

b) Assuming the corporate tax rate of 30 per cent, compute the after-tax specific cost in the following situations:

i. 6-year 10% Debentures of Rs.2,000, redeemable at premium of 5 per cent & floatation costs of 5 per cent.

ii. 4-year 14% Preference Shares of Rs.100, Issued at a discount of 5 per cent with 10 per cent floatation costs. Dividend tax is 10 per cent.

iii. 5-year 7% Preference Shares of Rs.1,000, Issued at a premium of 15% with a floatation cost of 5%.

Q6) ***Any one from (a) or (b) ————— (10x1) = 10 Marks***

a)

i. Find the present value of Rs20,000 receivable after 7years if discount rate is 8%?

ii. You are investing Rs.2,00,000 today in FD scheme at the rate of 6% p.a. for 5 years, what will be its maturity value?

iii. Mr. X deposits Rs.15,000 every year for next 4 years @10%p.a. The annual payment is made at the beginning of the year. Find PV of annuity.

b) Big Ltd. is planning for the most desirable capital structure. The cost of debt (after tax) and equity capital at various levels of debt-equity mix are estimated as follows:

Equity as % of total capital employed	Cost of debt (%)	Cost of equity (%)
100	12	18
80	12	18
60	12	20
50	14	20
40	16	22

Q7) ***Any two from (a) or (b) or (c) ————— (5x2) = 10 Marks***

a) Glow Ltd. Has beta coefficient of 1.2. The company has been maintaining 15% rate of growth in dividends and earnings. The last dividend paid was Rs. 5 per share. Return on Government securities is 10%. Return on market portfolio is 15%. The current market price of one share of Target Ltd. is Rs. 85.

i. What will be the equilibrium price per share of glow Ltd.?

ii. Would you advise purchasing the share?

b) The following information pertains to M/s Lee Ltd.

Earnings of the company	Rs.10,00,000
Dividend Payout Ratio	40%
No. of shares outstanding	1,00,000
Equity Capitalization Rate	15%
Rate of Return on Investment	10%

i. What would be the market value per share as per Walter's model?

ii. What is the optimum dividend payout ratio according to Walter's model and the market value of Company's share at that payout ratio?

c) The selected financial data for A Ltd. for the current year ended March 31 are as follows:

Particulars	Values
Variable expenses as a percentage of sales	75%
Interest expenses (Rs.)	300
Degree of operating leverage	6
Degree of financial leverage	4
Income-tax rate	35%

Prepare income statement of co. A with as many details as possible.