MMS-III (Finance) (Uni. Exam.)

15 : 2nd half.13-Avi(ax) Advanced Financial Management 27.11.2013.

Con. 9027-13. **(FURTHER REVISED COURSE)** **VT-14528**

(3 Hours) **[Total Marks : 60**

N.B. : (1) Question No. **1** is **compulsory** carrying **20** marks.
(2) Attempt any **four** from the **rest** of the questions carrying **10** marks **each**.
(3) Answer **each new question** on a **fresh page**.
(4) Write **all sub-questions** of a main question **together**.
(5) **Don't write extra answers. Only first five** will be **assessed**.
(6) **Presentation** should be **neat** and **clean**. **Marks** will be **deducted** for **poor presentation**.

Q.1. The balance sheet of MGM Limited as at March 31, 2013 is shown below: (Rs Lakhs)

Liabilities	Rs	Assets	Rs.
Share Capital	4200	Fixed Assets	8870
Retained Earning	2480	Inventories	3480
Term Loan	3920	Receivables	2580
Short term Bank Borrowings	2490	Cash	180
Accounts Payable	1240		
Provisions	780		
	15110		**15110**

The sales of the firm for the year ending on March 31, 2013 were 31,410. Its profit margin on sales was 7 percent and its dividend payout ratio was 50 percent. The tax rate was 34 percent. MGM Limited expects its sales to increase by 30 percent (i.e by 9,423) in the year 2014. The ratio of assets to sales and spontaneous current liabilities to sales would remain unchanged. Likewise the profit margin ratio, the tax rate, and the dividend payout ratio would remain unchanged.

Required: a) Estimate the external funds requirement for the year 2014.

b) Prepare the following statements, assuming that the external funds requirement would be raised from term loans and short-term bank borrowings in the ratio 1:2 (i) projected balance sheet and (ii) projected profit and loss account.

Q.2A) The profit and loss account of KG Electronics Limited for years 1 and 2 is given below: Using the percent of sales method, prepare the *pro forma* profit and loss account for year 3. Assume that the sales will be 26,000 in year 3. If dividends are raised to 500, what amount of retained earnings can be expected for year 3?

	Year1	Year 2
Net sales	18,230	22,460
Cost of goods sold	13,210	16100
Gross profit	5020	6360
Selling expenses	820	890
General and administration expenses	1200	1210
Depreciation	382	364
Operating profit	2618	3896
Non-operating surplus deficit	132	82
Earnings before interest and tax	2750	3978
Interest	682	890
Earnings before tax	2068	3088
Tax	780	980
Earnings after tax	1288	2108
Dividends(given)	320	450
Retained earnings	968	1658

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Q.2B) The capital structure of BHEL Ltd is as under:

- 80,00,000 Equity shares of Rs. 10 each = Rs. 800 lakhs
- 1,00,000 12% Preference Shares of Rs. 250 each = 250 Lakhs
- 1,00,000 10% debentures of Rs. 500 each = 500 Lakhs
- 10% term loan from bank = 450 lakhs

The Company's Profit and Loss Account for the year showed a balance PAT of Rs. 110 Lakhs, after appropriating Equity Dividend at 20%. The company is in the 40% tax bracket. Treasury bonds carry 6.5% interest and beta factor for the company may be taken at 1.5. The long run market rate of return may be taken at 16.5%. Calculate EVA.

Q3. A) ABC company Ltd is expecting 10% return on total assets of Rs 50 Lac. The company has outstanding shares 20,000. The directors of the company have decided to pay 40% of the earnings as dividends. The rate of return required by the shareholders is 12.5%. Rate of return expected on investment is 15%.You are required to determine the price of the share as per Walter Model.

Q.3 B) What do you mean by Sensitivity Analysis? Explain the process of Identifying Feasible projects and role of sensitivity analysis.

Q.4A) The profit and loss account and balance sheet of a company for two years (1 and 2) are given below. Assume a tax rate of 30 percent for year 2.

Profit and Loss Account	1	2
• Net sales	30,000	35,000
• Income from marketable securities	600	1,000
• Non-operating income	400	800
• Total income	31,000	36,800
• Cost of goods sold	18,000	21,000
• Selling and administrative expenses	3,800	4,600
• Depreciation	1,900	2,200
• Interest expenses	1,700	1,600
• Total costs and expenses	25,400	29,400
• PBT	5,600	7,400
• Tax provision	1,400	1,900
• PAT	4,200	5,500
• Dividends	1,200	1,400
• Retained earnings	3,000	4,100
Balance Sheet		
• Equity capital	5,000	5,000
• Reserves and surplus	5,000	9,100
• Debt	15,000	14,900
	25,000	29,000
• Fixed assets	15,000	18,500
• Investments (marketable securities)*	5,000	6,500
• Net current assets	5,000	4,000
	25,000	29,000
* All of this represents excess marketable securities		

(i) What is the EBIT for year 2?
(ii) What is the tax on EBIT for year 2?
(iii) What is the FCFF for year 2?
(iv) Show the break-up of the financing flow

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Q.4.B) Simtek Limited is considering a capital project for which the following information is available.

Investment outlay :	8000	Depreciation method :	Sinking fund
Project life :	5 years	(for tax purposes)	
Salvage value :	0	Tax rate :	30 %
Annual revenues :	10000	Debt-equity ratio :	0.6 :1
Annual costs :	6400	Cost of equity :	15%
(excluding depreciation interest, and taxes)		Cost of debt (post-tax) :	7%

(i) What will be the depreciation charge for year 3?
(ii) What will be the EVA for year 3?
(iii) Over time will the EVA of this project, increase, decrease or remains unchanged?

Q.5.A) A company's present capital structure contains 4,000,000 equity shares and 100,000 preference shares. The firm's current EBIT is Rs.25 million. Preference shares carry a dividend of Rs.3 per share. The earnings per share is Rs.4. The firm is planning to raise Rs.40 million of external financing. Two financing alternatives are being considered:
(i) issuing 4,000,000 equity shares for Rs.10 each,
(ii) issuing debentures for Rs.40 million carrying 12 percent interest.

Required (a) Compute the EPS-EBIT indifference point.
(b) Define the alternative which maximises EPS for various levels of EBIT.

Q.5.B) What is NPV and how do you assess the desirability of any project based on this method.

Q.6.A) The following data is available for Newton Limited:
Earnings per share = Rs.6.00
Rate of return = 18 percent
Cost of capital = 15 percent
(a) If Walter's valuation formula holds, what will be the price per share when the dividend payout ratio is 30 percent? 40 percent?
(b) If Gordon's basic valuation formula holds, what will be the price per share when the dividend payout is 30 percent, 40 percent?

Q.6.B) What do you Understand by equivalent Annualized value (EAV)? Explain its meaning and way of computing by taking a suitable example.

Q.7. Explain in brief any 2 of the following:-

a. Due Diligence
b. Break even Analysis
c. Discounted Cash flow
d. P/E Approach