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RB-1752-N

Third Year B. B. A. Examination
April / May – 2010
Advanced Financial Management

Time : 3 Hours] [Total Marks : **70**

Instructions :

(1)

નીચે દર્શાવેલ ☛ નિશાનીવાળી વિગતો ઉત્તરવહી પર અવશ્ય લખવી.
Fillup strictly the details of ☛ signs on your answer book.

Name of the Examination :

☛ **T. Y. B. B. A.**

Name of the Subject :

☛ **Advanced Financial Management**

☛ Subject Code No. : **1 7 5 2** ☛ Section No. (1, 2,.....) : **Nil**

Seat No. :

Student's Signature

(2) Question **one** is **compulsory.**

(3) All questions carry **equal** marks.

1 (a) International Food Limited has the following capital structure : **10**

Sources	**Book Value (Rs.)**	**Market Value (Rs.)**
Equity shares (25,000 shares of Rs. 10 each)	250,000	450,000
13% Preference Share (500 shares of Rs. 100 each)	50,000	45,000
Reserves and Surplus	150,000	—
14% Debenture (1500 debenture of Rs. 10 each)	150,000	145,000

The expected dividend per share is Rs. 1.40 and the dividend per share is expected to grow at a rate of 8% forever. Preference share is redeemable after 5 years at par whereas debentures are redeemable after 6 years at par. The tax rate for the company is 50%. You are required to compute the WACC for the existing capital structure using market value as weights.

(b) Consider the bonds of the United Pharam, which are selling for Rs. 119, the bonds carry a coupon interest rate of 15% and mature in 10 years with Rs. 100 par value. Although they are selling for Rs. 119, T.N. Verma, a potential investor, considers them to be worth only Rs. 109. What are the expected rates of return for the bonds and Verma's required rate of return? **4**

2 (a) What are the different payout methods? How do shareholders react to these methods? **7**

(b) Clay Product Limited is an all equity firm with the market value of its equity at Rs. 20,00,000. Its current cost of equity capital is 15%. The management is planning a capital expenditure of Rs. 15,00,000 that would increase the earning level by 1.5 times. **7**

For the first time in the history of the enterprise, the management is motivated by enthusiastic bankers to avail debt and have been offered very attractive and competitive interest rate slabs as follows :

Plan	I	II	III	IV	V
Amount of debt (Rs.)	3,00,000	6,00,000	9,00,000	12,00,000	15,00,000
Cost of debt (%)	8.00%	8.50%	9.50%	10.00%	11.00%

The finance manager of the firm believes that the cost of equity which is currently at 15% would increase with the increasing amount of debt. His estimate of the equity is as follows :

Plan	I	II	III	IV	V
Cost of Equity (%)	15.50%	15.50%	16.00%	18.00%	21.00%

Examine how much amount of debt Clay Products should have. Assume tax rate at 36%.

OR

2 (a) Explain the following term : **7**

(i) Personal Leverage

(ii) Optimal Capital Structure

(b) Calculate the following : **7**

(i) Exponent Ltd. had 50,000 equity shares of Rs. 10 each outstanding on 1^{st} April. The shares are being quoted at par in the market. The company intends to pay a dividend of Rs. 2 per share for current financial year. It belongs to a risk class whose appropriate capitalization rate is 15%.

Using M-M model and assuming no taxes, ascertain in price of company's share as it is likely to prevail at the end of the year when (i) dividend is declared; and (ii) when dividend is not declared.

(ii) A large sized chemical company has been expected to grow at 14% per year for the next four years and then to grow indefinitely at the same rate as the national economy, i.e. 5%. The required rate of return on the equity shares is 12%. Assume that the company paid a dividend of Rs. 2 per share last year (DO=2). Determine the market price of the shares today.

3 (a) Write a short note on Situational Analysis. **7**

(b) A company has examined two mutually exclusive **7**

investment proposal. The management of the company uses certainty equivalent to evaluate new investment proposal from the following information available to this project. Advice the company as two which project should be taken up. The firms risk free return is 6% and risk premium is also 6%.

	Proposal A		Proposal B	
Year	CFAT	C.E. Factor	CFAT	C.E. Factor
0	(25,000)	1	(25,000)	1
1	15,000	0.8	9,000	0.9
2	15,000	0.7	18,000	0.8
3	15,000	0.6	12,000	0.7
4	15,000	0.5	16,000	0.4

OR

3 Dream Well Co Ltd. has an investment proposal that requires an investment outlay of Rs. 2,50,000. The following information is available. **14**

Year 1 :

Possible Event	Cash Flow (Rs.)	Probability
A	100,000	0.2
B	125,000	0.4
C	180,000	0.4

Year 2 : Cash flow after Tax possibilities depend on the happening a year 1 CFAT :

	Rs. 100,000/-		**Rs. 125,000/-**		**Rs. 180,000/-**	
Event	**CFAT (Rs.)**	**Pro.**	**CFAT (Rs)**	**Pro**	**CFAT (Rs.)**	**Pro**
A	45,000	0.2	140,000	0.2	190,000	0.3
B	120,000	0.3	180,000	0.6	210,000	0.3
C	180,000	0.5	190,000	0.2	260,000	0.4

You are required to advice the company regarding the financial feasibility of the project using decision tree approach. Company's cost of capital is 10%.

4 (a) What are different ways of financing merger? **7**

(b) What is the hire purchase financing? How does it differ from the lease financing? **7**

OR

4 (a) What are the similarities and difference between lease financing and debt financing? In what cases, lease may be referred? **7**

(b) What are the risk management tools? Explain briefly. **7**

5 Write short notes on any **two** : **14**

(a) Private Placement

(b) The steps involved in a Venture Capital Investment Process.

(c) Significance of Cost of capital

(d) Joint Venture in India.