Total number of printed pages–6

47(4) MNSR 4·4

2013

FINANCIAL MANAGEMENT

Paper : ~~4·4~~ 4·3

Full Marks : 80

Time : Three hours

The figures in the margin indicate full marks for the questions.

1. Fill in the blanks by choosing the correct alternative : 10×1=10

   (a) EPS stands for

   (Equity per share / Earnings per share)

   (b) Degree of financial leverage = ________ $\left(\frac{EBIT}{EBT} / \frac{EPS}{EBIT}\right)$

   (c) When dividend is declared it becomes an/a ________ of the company. (obligation / reputation)

Contd.

(d) Right shares are issued to ________. (preference shareholders / equity shareholders)

(e) According to MM Theory, the total value of the firm is ________. (Static / non-static)

(f) SEBI stands for ________. (Security Employment Board of India / Securities and Exchange Board of India)

(g) The job of a financial manager covers raising and utilisation of ________. (funds / debt)

(h) When the book value of a company is less than the real value, the company is said to be ________.

(over capitalised / undercapitalised)

(i) The effective cost of debentures is ________ as compared to shares. (more/less)

(j) Cost of retained earnings is the ________ cost of dividend foregone by the shareholders. (financial / opportunity)

2. *Answer the following :* 5×2=10

(a) What do you mean by sweat equity shares ?

(b) Mention *any two* causes of under-capitalisation.

(c) What do you mean by operating leverage ?

(d) What do you mean by pre-emptive right ?

(e) What do you mean by capital structure ?

3. *Answer the following :* ***(any five)*** 5×4=20

(a) What are the objectives of financial management ? Explain.

(b) What is over-capitalisation ? What are the remedies of over-capitalisation ?

(c) Distinguish between equity shares and debentures.

(d) Explain *any five* factors affecting dividend decision.

(e) How is the cost of debt calculated ?

(f) (i) A company issues ₹ 10,00,000, 10% redeemable debentures at a discount of 5%. The costs of floatation amount to ₹ 30,000. The debentures are redeemable after 5 years. Calculate after tax cost of debt assuming a tax rate of 50%.

Contd.

(ii) The shares of a company are selling at ₹ 40 per share and it had paid a dividend of ₹ 4 per share last year. The investor's market expects a growth rate of 5% per year. compute the company's cost of equity capital.

(g) What are the components of cost of capital ?

4. *Answer the following : (any five)*

(a) Explain the net income approach of determining the capital structure. Also highlight the role of SEBI in issue of capital. 4+4

(b) Explain *any five* factors that determine the capital structure of a company. What are the limitations of trading on equity ? 5+3

(c) What is the argument given in MM approach of dividend decision ? What do you mean by price-earnings ratio ? 5+3

(d) What is finance function ? Elaborately discuss the nature and scope of financial management. 2+3+3

(e) Why is preference share known as hybrid form of security ? Critically examine the advantages and disadvantages of raising funds by issuing equity shares. 2+3+3

(f) What are the different types of debentures ? Also, discuss the earnings theory of capitalisation. 5+3

(g) The following information is available in respect of a firm :

Capitalisation rate = 10%

Earnings per share = ₹ 50

Assumed rate of return on investment is

(i) 12% (ii) 8% (iii) 10%

Show the impact of dividend policy on market price of shares by applying Walter's formula when dividend pay-out ratio is 60% and 100%. 5+3

(h) A company has equity share capital of ₹ 5,00,000 divided into shares of ₹ 100 each. It wishes to raise further ₹ 3,00,000 for expansion. The following options are available :

(i) all common stock

Contd.

(ii) ₹ 1,00,000 in common stock and ₹ 2,00,000 in 10% debentures.

(iii) all debt at 10% p.a.

(iv) ₹ 1,00,000 in common stock and ₹ 2,00,000 in 8% preference shares.

The company's existing earnings before interest and tax are ₹ 1,50,000. The corporate tax rate is 50%. Determine EPS of each plan and comment on the implications of financial leverage. 8
