Test Series: April, 2022

MOCK TEST PAPER – II

INTERMEDIATE: GROUP – II

PAPER – 8: FINANCIAL MANAGEMENT& ECONOMICS FOR FINANCE

PAPER 8A : FINANCIAL MANAGEMENT

Answers are to be given only in English except in the case of the candidates who have opted for Hindi medium. If a candidate has not opted for Hindi medium his/ her answers in Hindi will not be valued.

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

*Attempt any **four** questions from the remaining **five** questions.*

Working notes should form part of the answer.

Time Allowed – 3 Hours (Total time for 8A and 8B) **Maximum Marks – 60**

1. Answer the following:

(a) Following data is available in respect of two companies having same business risk:

Capital employed = ₹ 4,00,000, EBIT = ₹ 60,000 and K_e = 12.5%

Sources	Levered Company (₹)	Unlevered Company (₹)
Debt (@10%)	2,00,000	Nil
Equity	2,00,000	4,00,000

An investor is holding 15% shares in levered company. CALCULATE the increase in annual earnings of investor if he switches his holding from Levered to Unlevered company.

(b) From the given details, PREPARE Income Statement for Alpha Ltd. and Beta Ltd.

Particulars	Alpha Ltd.	Beta Ltd.
Operating Leverage	1.875	1.800
Financial Leverage	1.600	1.250
PV Ratio	60%	50%
Profit after tax	₹ 3,00,000	₹ 2,40,000
Tax rate	40%	40%

(c) An enterprise is investing ₹ 100 lakhs in a project. The risk-free rate of return is 7%. Risk premium expected by the Management is 7%. The life of the project is 5 years. Following are the cash flows that are estimated over the life of the project.

Year	Cash flows (₹ in lakhs)
1	25
2	60
3	75
4	80
5	65

CALCULATE Net Present Value of the project based on Risk free rate and also on the basis of Risks adjusted discount rate.

(d) From the following information, you are required to PREPARE a summarised Balance Sheet for Rudra Ltd. for the year ended 31st March, 2022

Debt Equity Ratio	1:1
Current Ratio	3:1
Acid Test Ratio	8:3
Fixed Asset Turnover (on the basis of sales)	4
Stock Turnover (on the basis of sales)	6
Cash in hand	5,00,000
Stock to Debtor	1:1
Sales to Net Worth	4
Capital to Reserve	1:2
Gross Profit	20% of Cost
COGS to Creditor	10:1

Interest for entire year is yet to be paid on Long Term loan @ 10%. **(4 × 5 = 20 Marks)**

2. (a) The Modern Chemicals Ltd. requires ₹ 25,00,000 for a new plant. This plant is expected to yield earnings before interest and taxes of ₹ 5,00,000. While deciding about the financial plan, the company considers the objective of maximising earnings per share. It has three alternatives to finance the project- by raising debt of ₹ 2,50,000 or ₹ 10,00,000 or ₹ 15,00,000 and the balance, in each case, by issuing equity shares. The company's share is currently selling at ₹ 150, but is expected to decline to ₹ 125 in case the funds are borrowed in excess of ₹ 10,00,000. The funds can be borrowed at the rate of 10% upto ₹ 2,50,000, at 15% over ₹ 2,50,000 and upto ₹ 10,00,000 and at 20% over ₹ 10,00,000. The tax rate applicable to the company is 50%. ANALYSE, which form of financing should the company choose? **(7 Marks)**

(b) "Operating risk is associated with cost structure, whereas financial risk is associated with capital structure of a business concern." Critically EXAMINE this statement. **(3 Marks)**

3. The following annual figures relate to manufacturing entity:

A. Sales at one month credit — 84,00,000

B. Material consumption — 60% of sales value

C. Wages (paid in a lag of 15 days) — 12,00,000

D. Cash Manufacturing Expenses — 3,00,000

E. Administrative Expenses — 2,40,000

F. Creditors extend 3 months credit for payment.

G. Cash manufacturing and administrative expenses are paid 1 months in arrear.

The company maintains stock of raw material equal to economic order quantity. The company incurs ₹ 100 as per ordering cost per order and opportunity cost of capital is 15% p.a. The optimum cash balance is determined using Baumol's model. The bank charges ₹ 10 for each cash withdrawal. Finished goods are held in stock for 1 month. The company maintains a bank balance of ₹12,00,000 on an average. Creditors are paid through net banking and all other expenses are incurred in cash which is withdrawn from bank.

Assuming a 20% safety margin, you are required to ESTIMATE the amount of working capital that needs to be invested by the Company. **(10 Marks)**

4. Manoranjan Ltd is a News broadcasting channel having its broadcasting Centre in Mumbai. There are total 200 employees in the organisation including top management. As a part of employee benefit expenses, the company serves tea or coffee to its employees, which is outsourced from a third-party. The company offers tea or coffee three times a day to each of its employees. 120 employees prefer tea all three times, 40 employees prefer coffee all three times and remaining prefer tea only once in a day. The third-party charges ₹ 10 for each cup of tea and ₹ 15 for each cup of coffee. The company works for 200 days in a year.

Looking at the substantial amount of expenditure on tea and coffee, the finance department has proposed to the management an installation of a master tea and coffee vending machine which will cost ₹ 10,00,000 with a useful life of five years. Upon purchasing the machine, the company will have to enter into an annual maintenance contract with the vendor, which will require a payment of ₹ 75,000 every year. The machine would require electricity consumption of 500 units p.m. and current incremental cost of electricity for the company is ₹ 12 per unit. Apart from these running costs, the company will have to incur the following consumables expenditure also:

(1) Packets of Coffee beans at a cost of ₹ 90 per packet.

(2) Packet of tea powder at a cost of ₹ 70 per packet.

(3) Sugar at a cost of ₹ 50 per Kg.

(4) Milk at a cost of ₹ 50 per litre.

(5) Paper cup at a cost of 20 paise per cup.

Each packet of coffee beans would produce 200 cups of coffee and same goes for tea powder packet. Each cup of tea or coffee would consist of 10g of sugar on an average and 100 ml of milk.

The company anticipate that due to ready availability of tea and coffee through vending machines its employees would end up consuming more tea and coffee. It estimates that the consumption will increase by on an average 20% for all class of employees. Also, the paper cups consumption will be 10% more than the actual cups served due to leakages in them.

The company is in the 25% tax bracket and has a current cost of capital at 12% per annum. Straight line method of depreciation is allowed for the purpose of taxation. You as a financial consultant is required to ADVISE on the feasibility of acquiring the vending machine.

PV factors @ 12%:

Year	1	2	3	4	5
PVF	0.8929	0.7972	0.7118	0.6355	0.5674

(10 Marks)

5. The capital structure of RV Limited as on 31st March, 2022 as per its Balance Sheet is as follows:

Particulars	₹
Equity shares of ₹ 10 each	25,00,000
10% Preference shares of ₹ 100 each	5,00,000
Retained earnings	5,00,000
13% debentures of ₹ 100 each	20,00,000

The market price of equity shares is ₹ 50 per share. Expected dividend on equity shares is ₹ 3 per share. The dividend per share is expected to grow at the rate of 8%.

Preference shares are redeemable after eight years and the current market price is ₹ 80 per share.

Debentures are redeemable after five years and are currently selling at ₹ 90 per debenture.

The tax rate applicable to the company is 35%.

CALCULATE weighted average cost of capital using:

(i) Book value proportions

(ii) Market value proportions **(10 Marks)**

6. (a) DISCUSS in briefly any two long term sources of finance for a partnership firm.

(b) DISCUSS the limitations of financial ratios

(c) EXPLAIN the term 'Payback reciprocal'. **(4 + 4 + 2 =10 Marks)**

PAPER 8B: ECONOMICS FOR FINANCE

Time Allowed – 1:15 Hours **Maximum Marks - 40**

QUESTIONS

1. (a) Describe the system of regional accounts in India? **(3 Marks)**

   (b) What is the distinction between Production taxes and Product taxes? **(2 Marks)**

   (c) In an economy suppose **(5 Marks)**

	₹ Income
Consumption Function	100+ 0.60 Yd
Government Spending	150
Investment spending	125
Tax @ Tx	30+0.05Y
Transfer Payments	Tr = 50
Exports	X = 40
Import	M = 25+0.1Y

Yd = Disposable Income

Y = National Income

Calculate

1. The equilibrium level of national Income
2. Consumption
3. Net Export

2. (a) What will be the outcome when aggregate expenditure is more than the output ? **(3 Marks)**

   (b) Why is multiplier important in Keynesian theory of determination of National Income? **(2 Marks)**

   (c) Calculate National Income with the help of Income and Expenditure Method. **(5 Marks)**

	₹ in Crore
Compensation of employee	1000
Net Factor Income from Abroad	50
Indirect Tax	100
Subsidy	20
Private Final consumption expenditure	800
Government final Consumption Expenditure	900
Net Domestic Capital Formation	700
Consumption of fixed Capital	120
Operating Surplus	1400
Mixed Income	600
Employer's contribution to social feeling scheme	300
Net Export	20

3. (a) In the times of recession What should be the Public Revenue and Expenditure Policy? **(3 Marks)**

   (b) Why should government perform the allocation function in an economy? **(2 Marks)**

   (c) Elaborate on the redistribution effect of a tax and Transfer Policy? **(2 Marks)**

   (d) Comment on the role of bank rate as the instrument of monetary policy. **(3 Marks)**

4. (a) In the Context of International Trade, What do you understand by Factor Equalization Theorem? **(2 Marks)**

   (b) How is Anti-Dumping Duties constitute a threat to International Trade? **(3 Marks)**

   (c) What are different technical barrier to trade and their effect on trade? **(3 Marks)**

   (d) What is Free Trade area and how it is different from Trading Block? **(2 Marks)**

5. (a) What are the salient Feature of Modern theory of Trade? **(3 Marks)**

   (b) What are the major reasons for market failure? **(3 Marks)**

   (c) What are the important function of Money? **(2 Marks)**

   (d) What are the theories in respect of determination of money supply? **(2 Marks)**

   Or

   What are the direct forms of Foreign direct Investment?