MOCK TEST PAPER - 2

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) PREPARE a working capital estimate to finance an activity level of 52,000 units a year (52 weeks) based on the following data:

Raw Materials - ₹ 400 per unit

Direct Wages - ₹ 150 per unit

Overheads (Manufacturing) - ₹200 per unit

Overheads (Selling & Distribution) - ₹100perunit

Selling Price - ₹ 1,000 per unit, Raw materials & Finished Goods remain in stock for 4 weeks, Work in process takes 4 weeks. Debtors are allowed 8 weeks for payment whereas creditors allow us 4 weeks.

Minimum cash balance expected is ₹50,000. Receivables are valued at Selling Price.

(b) Axar Ltd. has a Sales of ₹ 68,00,000 with a Variable cost Ratio of 60%.

The company has fixed cost of ₹16,32,000. The capital of the company comprises of 12% long term debt, ₹1,00,000 Preference Shares of ₹ 10 each carrying dividend rate of 10% and 1,50,000 equity shares.

The tax rate applicable for the company is 30%.

At current sales level, DETERMINE the Interest, EPS and amount of debt for the firm if a 25% decline in Sales will wipe out all the EPS.

(c) Avesh Pvt. Ltd. is considering relaxing its present credit policy for accounts receivable and is in the process of evaluating two proposed policies. Currently, the company has annual credit sales of ₹ 55 lakhs and accounts receivable turnover ratio of 5 times a year. The current level of loss due to bad debts is ₹ 2,00,000. The company is required to give a return of 15% on the investment in new accounts receivable. The company's variable costs are 75% of the selling price. Given the following information, IDENTIFY which is the better policy?

(Amount in ₹)

Particulars	Present Policy	Proposed Policy 1	Proposed Policy 2
Annual credit sales	55,00,000	65,00,000	70,00,000

Accounts receivable turnover ratio	5 times	4 times	3 times
Bad debt losses	2,00,000	3,50,000	5,00,000

(d) The annual report of XYZ Ltd. provides the following information for the Financial Year 2019-20:

Particulars	**Amount (₹)**
Net Profit	78 lakhs
Outstanding 15% preference shares	120 lakhs
No. of equity shares	6 lakhs
Return on Investment	20%
Cost of capital i.e. (K_e)	16%

CALCULATE price per share using Gordon's Model when dividend pay-out is-

(i) 30%;

(ii) 50%;

(iii) 100%. **[4 × 5 Marks = 20 Marks]**

2. The financial advisor of Sun Ltd is confronted with following two alternative financing plans for raising ₹ 10 lakhs that is needed for plant expansion and modernization

Alternative I: Issue 80% of funds with 14% Debenture [Face value (FV) ₹ 100] at par and redeem at a premium of 10% after 10 years and balance by issuing equity shares at $33\frac{1}{3}$ % premium.

Alternative II: Raise 10% of funds required by issuing 8% Irredeemable Debentures [Face value (FV) ₹ 100] at par and the remaining by issuing equity shares at current market price of ₹125.

Currently, the firm has an Earnings per share (EPS) of ₹ 21

The modernization and expansion programme is expected to increase the firm's Earnings before Interest and Taxation (EBIT) by ₹ 200,000 annually.

The firm's condensed Balance Sheet for the current year is given below:

Balance Sheet as on 31.3.2022

Liabilities	**Amount (₹)**	**Assets**	**Amount (₹)**
Current Liabilities	5,00,000	Current Assets	16,00,000
10% Long Term Loan	15,00,000	Plant & Equipment (Net)	34,00,000
Reserves & Surplus	10,00,000		
Equity Share Capital (FV: ₹ 100 each)	20,00,000		
TOTAL	50,00,000	TOTAL	50,00,000

However, the finance advisor is concerned about the effect that issuing of debt might have on the firm. The average debt ratio for firms in industry is 35%.He believes if this ratio is exceeded, the P/E ratio of the company will be 7 because of the potentially greater risk.

If the firm increases its equity capital by more than 10 %, he expects the P/E ratio of the company will increase to 8.5 irrespective of the debt ratio.

Assume Tax Rate of 25%. Assume target dividend pay-out under each alternative to be 60% for the next year and growth rate to be 10% for the purpose of calculating Cost of Equity

SUGGEST with reason which alternative is better on the basis of each of the below given criteria:

I. Earnings per share (EPS) & Market Price per share (MPS)

II. Financial Leverage

III. Weighted Average Cost of Capital & Marginal Cost of Capital (using Book Value weights)

[10 Marks]

3. From the following information and ratios, PREPARE the Balance sheet as at 31st March 2022 and Income statement for the year ended on that date for M/s Ganguly & Co -

Average Stock	₹10 lakh
Current Ratio	3:1
Acid Test Ratio	1:1
PBIT to PBT	2.2:1
Average Collection period (Assume 360 days in a year)	30 days
Stock Turnover Ratio (Use sales as turnover)	5 times
Fixed assets turnover ratio	0.8 times
Working Capital	₹10 lakh
Net profit Ratio	10%
Gross profit Ratio	40%
Operating expenses (excluding interest)	₹ 9 lakh
Long term loan interest	12%
Tax	Nil

[10 Marks]

4. The initial investment outlay for a capital investment project consists of ₹ 150 lacs for Plant & machinery and ₹ 60 lacs for Working Capital. Other details are summarized below:

Sales – 1.5 lakh units of output per year for years 1 to 5

Selling Price - 120 per unit of output

Variable cost - 60 per unit of output

Fixed overheads (excluding depreciation) - 22.5 lakhs per year for years 1 to 5

Salvage value of Plant & machinery Equal to the Written Down Value (WDV) at the end of year 5

Tax rate 40%

Time horizon 5 years

Post tax cut off rate 12%. PVAF (12%,5 Years) is 3.6048.PV @12% 5th year is 0.5674.

Rate of depreciation 20% on the Straight-Line Method (SLM)

Required:

(a) INDICATE the financial viability of the project by calculating the NPV

(b) DETERMINE the sensitivity of the project's NPV under each of the following conditions:

(i) Decrease in selling price by 10%

(ii) Increase in variable cost by 10%

(iii) Increase in cost of Plant & machinery by 10% **[10 Marks]**

5. (a) The following information is related to Navya Company Ltd. for the year ended 31st March 2022:

Equity share capital (₹ 10 each)	₹ 65,50,000
12% Bonds of ₹ 1,00 each	₹ 60,91,400
Sales	₹ 111 lakhs
Fixed cost (excluding interest)	₹ 7,15,000
Financial leverage	1.55
Profit-volume Ratio	25%
Income Tax Applicable	30%

You are required to CALCULATE:

(i) Operating Leverage.

(ii) Combined leverage; and

(iii) Earnings per share.

Show calculations upto two decimal points. **[8 Marks]**

(b) Write a short note on seed capital assistance. **[2 Marks]**

6. (a) DISTINGUISH between Net Present Value and Internal Rate of Return. **[4 Marks]**

(b) EXPLAIN in brief the features of Commercial Papers. **[4 Marks]**

(c) What do you UNDERSTAND by desirability factor/profitability index? **[2 Marks]**

Or

WRITE a short note on "Cut-off Rate".

PAPER 8B: ECONOMICS FOR FINANCE

Question 1 is compulsory

Students can answer 3 out of the 4 remaining

1. (a) What is the distinction between Production Taxes and Product Taxes? **(3 Marks)**

   (b) What is the System of National Accounts (SNA)? **(2 Marks)**

   (c) Calculate the Operating Surplus with the help of the following data- **(5 Marks)**

Particulars	₹ in Crores
Sales	3000
Compensation of employees	700
Intermediate consumption	500
Rent	300
Interest	200
Net indirect tax	800
Consumption of Fixed Capital	100
Mixed Income of Self Employed	200

2. (a) Calculate Marginal Propensity to Save (MPS) and Marginal Propensity to Consume (MPC) from the following data: **(3 Marks)**

Income (₹) (Y)	Consumption (₹) (C)
6000	5000
10000	7000

   (b) What is Circular flow of Income? **(2 Marks)**

   (c) What do you understand by Inflationary gap? **(2 Marks)**

   (d) What are the reasons for government intervention in the market? **(3 Marks)**

3. (a) Why do government gives Subsidies? **(3 Marks)**

   (b) Environmental pollution is regarded as a source of market failure: Comment. **(2 Marks)**

   (c) What is Tragedy of commons? **(2 Marks)**

   (d) Explain the concept of Price Floor? **(3 Marks)**

4. (a) What is Government Spending Multiplier? **(2 Marks)**

   (b) What are the limitation of Fiscal Policy? **(2 Marks)**

   (c) What is the effect of Government Expenditure on Money Supply? **(3 Marks)**

   (d) Calculate Narrow Money (M_1) from the following data **(3 Marks)**

Currency with public	80000 cr
Demand Deposits with Banking System	100000 cr
Time Deposits with Banking System	200000 cr
Other Deposits with RBI	250000 cr
Saving Deposits of Post office saving banks	50000 cr

5. (a) Explain in brief The factor price equalisation theorem? **(3 Marks)**

(b) What is meant by an 'Anti-dumping' measure? **(3 Marks)**

(c) What are the advantage of fixed exchange rate regime? **(2 Marks)**

(d) Distinguish between horizontal, vertical, type of foreign Investments. **(2 Marks)**

OR

What is Import subsidies?