2025

BUSINESS ADMINISTRATION — HONOURS

Paper : BBAA-401-CC5

(Financial Management)

Full Marks : 75

The figures in the margin indicate full marks.

Candidates are required to give their answers in their own words as far as practicable.

Group - A

1. Answer ***any ten*** questions : 2×10

(a) What are the three major financial decisions in a business?

(b) What is the difference between explicit and implicit cost of capital?

(c) Define Retained Earnings.

(d) What is the Internal Rate of Return (IRR)?

(e) How does combined leverage affect a firm's earnings?

(f) Mention (any two) factors influence the determination of working capital.

(g) What does the Net Income (NI) approach on Capital Structure states?

(h) What is Non-Systematic Risk?

(i) Why is MM theory in Dividend policy referred to as 'Dividend Irrelevance Theory'?

(j) How does floatation cost impact the calculation of Cost of Debentures?

(k) Define Economic Order Quantity.

(l) Mention (any two) capital budgeting evaluation techniques.

(m) What is Beta?

(n) What is Optimum Credit Policy?

(o) What is unlevered firm?

Group - B

2. Answer ***any five*** questions : 5×5

(a) Why is wealth maximization considered superior to profit maximization criteria? 5

(b) What is capital rationing? Differentiate between divisible and indivisible projects. 2+3

(c) Mr. Agarwal deposits ₹ 10,000 every year for 4 years into a scheme of ABZ Bank, earning 8% annual interest, compounded annually. What will be the future value of his investment at the end of 4 years? 2+3

(d) State the operating concept of working capital. 5

(e) ABC Ltd. has annual demand of 5000 units of material. Ordering cost is ₹ 500 per order and carrying costs are ₹ 100 per unit. The safety stock is 25% of EOQ. The daily usage is 20 units and lead time is 5 days. Calculate (i) EOQ (ii) Safety Stock (iii) Reorder Point. 5

(f) Explain the concept of Indifference point with respect to leverage analysis. 5

(g) The following three companies are identical in all respect, except their capital structure. You are required to find out which company's capital structure is optimum under given circumstances, considering the assumptions of NI approach : 5

Capital Structure	**Alpha Ltd.**	**Beta Ltd.**	**Gama Ltd.**
Equity Capital	600,000	400,000	300,000
15% Debentures	—	200,000	300,000
Total	**600,000**	**600,000**	**600,000**
Other Information			
Sales	12,00,000	12,00,000	12,00,000
Variable cost to sales ratio	75%	75%	75%
Fixed Operating Cost	120,000	120,000	120,000
Equity capitalization rate	20%	20%	20%
Corporate Tax	NIL	NIL	NIL

(h) RCB Ltd. has a total investment of ₹ 375,000 in assets and 25,000 outstanding ordinary shares at ₹ 15 per share (Per value). The profitability rate of the company is 10%. If the capitalization rate is 12%. 5

(i) What should be the optimum dividend payout ratio according to Walter's Model?

(ii) What should be the maximum price of the share under the current circumstances?

(iii) How the price of the share will affect if the payout ratio will change?

Group - C

3. Answer ***any three*** questions : 10×3

(a) Calculate the Operating Leverage, Financial Leverage and Combined Leverage from the following data under situation 1 and 2 and Financial Plan A and B : 10

Installed Capacity	4000 units
Actual production and Sales	75% of the capacity
Selling price	₹ 30 per unit
Variable cost	₹ 5 per unit
Fixed Cost :	
Under Situation 1	₹ 15,000
Under Situation 2	₹ 20,000

Financial Plan	**A**	**B**
Equity	10000	15000
Debt (Rate of interest at 20%)	10000	5000
Total	20000	20000

(b) X Ltd. has a machine which has been in operation for 6 years. The management is considering a proposal to purchase an improved model of a similar machine which gives an increased output. The following information is given below :

	Old machine (₹)	**New machine (₹)**
Purchase price of machine	60,000	1,20,000
Expenditure p. a. on account of-		
Power consumption	7000	8000
Consumable stores	4000	5000
Repairs and maintenance	5000	4000
Labour cost per running hours	2	2.25
Material cost per unit	0.40	0.40
Selling price p.u.	1	1

Other information are as follows :

	Old machine (₹)	**New machine (₹)**
Output per hour (unit)	40	60
Machine running hours p. a.	2000	2000
Estimated life (years)	10	10

(i) Compute the ARR of the machines and decide whether the machine should be replaced or not under ARR method. The company follows straight line method for charging depreciation. Tax rate is 35%.

(ii) Give your valuable comment. 8+2

(c) From the following information prepare a statement showing the Estimated Working Capital Requirements : 10

(i) Projected Annual Sales = 36,000 units

(ii) Analysis of Sales :

Raw Materials	= ₹ 6 per unit
Labour	= ₹ 4 per unit
Overhead	= ₹ 3 per unit
Profit	= ₹ 2 per unit
Selling Price	₹ 15 per unit

(iii) Additional Information :

(A) Raw materials in Stock = 1 month

(B) Production process = 2 months

(C) Finished goods in store = 3 months

(D) Credit allowed to Debtor = 4 months

(E) Credit allowed by suppliers = 2 months

(F) Monthly wages and expenses are paid twice on 1st and 16th of each month.

(G) Production is carried on evenly during the year and expenses and wages accrue similarly.

(iv) Cash is to be kept at 10% of the Net Working Capital.

(d) XY Ltd. has the following Capital Structure :

Particulars	**Amount (₹ in lakhs)**
Equity Share Capital (20 lakh shares at par value)	200
10% Preference Capital (20,000 shares at par value)	20
Retained Earnings	100
12% Debentures (80,000 Debentures at FV)	80
16% Term Loan from IDBI	100
Total	**500**

The market price per equity share is ₹ 35. The net expected dividend/share after 1 year is ₹ 5 and the dividend per share is expected to grow at a constant rate of 9.5%. The preference shares are redeemable after 8 years, at par, and are currently quoted at ₹ 85 per share on the stock exchange. The debentures are redeemable after 5 years, at par, and the current market quotation is ₹ 95 per share. The tax rate applicable to the firm is 40%. Calculate the WACC considering :

(i) Book value as the weights

(ii) Market value as the weights. 5+5

(e) National Electronics Ltd. an electronic goods manufacturing company, is producing a large range of electronic goods. It has under consideration two Projects X and Y, each having an Initial Investment of ₹ 120,00,000.

The projects are mutually exclusive and the company is considering the question of selecting any one of the two. Earnings Before Depreciation and Tax (EBDT) have been worked out for both the Projects and the details are given in the table below. Project X has a life of 8 years and Project Y has a life of 6 years. Both will have zero salvage value at the end of their operational lives. The tax rate is 50% and cost of capital is 15%.

Year	Project X EBDT(₹)	Project Y EBDT (₹)	Present Value of Re. 1 @15%
1	25,00,000	40,00,000	0.870
2	35,00,000	60,00,000	0.756
3	45,00,000	80,00,000	0.658
4	65,00,000	50,00,000	0.572
5	65,00,000	30,00,000	0.497
6	55,00,000	20,00,000	0.432
7	35,00,000	—	0.376
8	15,00,000	—	0.327

The Company follows the straight-line method of Depreciation. Advise the Company regarding the selection of the Project using Net Present Value Method. 10