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Reg. No.................................

Name....................................

M.Com. DEGREE (C.S.S.) EXAMINATION, OCTOBER 2019

First Semester

Faculty of Commerce

FM 01 C03—FINANCIAL MANAGEMENT PRINCIPLES

(2012—2018 Admissions)

Time : Three Hours | Maximum Weight : 30

Section A

Answer any **five** *questions.*
Each question carries 1 *weight.*

1. Define operating, financial and combined leverage.
2. How do you calculate the accounting rate of return ?
3. Describe the traditional view on the optimum capital structure.
4. Why is the consideration of time important in financial decision making ?
5. What are the basic financial functions ?
6. Explain the various concepts of cost of capital.
7. Explain the concept of financial leverage with example.
8. What is financial risk ? How does it differ from business risk ?

(5 × 1 = 5)

Section B

Answer any **five** *questions.*
Each question carries 2 *weights.*

9. What is multi-period compounding ? How does it affect the annual rate of interest ? If the annual interest rate is 12 % and if the compounding is done annually, half yearly and quarterly, what are the effective rates of interest ?
10. 'The equity capital is cost free'. Do you agree ? Give reasons. The basic formula to calculate the cost of equity is : (DIV1/ Po) + g. Explain its rationale.

Turn over

11. Describe the traditional view on the optimum capital structure. Compare and contrast this view with the NOI approach and the NI approach.

12. Explain the concept of operating leverage. How will you measure the degree of operating leverage?

13. 'The MM thesis is based on unrealistic assumptions'. Evaluate the reality of the assumptions made by MM.

14. Distinguish between "

    (i) ARR and IRR.

    (ii) Pay-back period and NPV.

15. Explain the effect on existing equity shareholders of additional financing through issue of preference shares and debentures.

16. The following estimates are given to you :

			Rs.
Sales		...	10,00,000
Less : Variable cost		...	4,00,000
	Contribution	...	6,00,000
Less : Fixed cost		...	4,00,000
	EBIT	...	2,00,000
Less : Interest on debt			1,00,000
	EBT	...	1,00,000

On the basis of above estimates, answer the following questions :

(i) If sales increase by 10 %, what will be the percentage increase in EBIT as a result of operating leverage ?

(ii) In case EBIT increase by 10 %, what will be the percentage increase in EBT as a result of financial leverage ?

(5 × 2 = 10)

Section C

Answer any **three** *questions.*
Each question carries 5 *weights.*

17. "The operative objective of financial management is to maximise wealth or net present value". Explain this statement and examine the finance function performed by finance manager to achieve this goal.

18. Shobhit Ltd is considering purchasing a machine. Two machines A and B are available at the cost of Rs. 1,20,000 each. Earning after tax but before depreciation are likely to be as under:

Year		*Machine* A	*Machine* B
		Rs.	Rs.
1	...	50,000	20,000
2	...	40,000	30,000
3	...	30,000	50,000
4	...	20,000	40,000
5	...	20,000	40,000

Evaluate the two alternatives by using :

(i) Pay-back period method.

(ii) Post pay - back profitability.

19. Explain M. M. Approach regarding relationship between capital structure, arbitrage and value of firm.

20. Jai Ltd has obtained capital from the following sources, the specific cost are also noted against them. You are required to calculate weighted average cost of capital using (i) Book value ; and (ii) Market value :

Source of capital		*Book value*	*Market value*	*Cost of Capital*
		Rs.	Rs.	
Debentures	...	4,00,000	3,80,000	5 %
Preference shares	...	1,00,000	1,10,000	8 %
Equity shares	...	6,00,000	12,00,000	13 %
Retained earnings	...	2,00,000	-	9 %

Turn over

21. The following data relates to ACL Ltd :

Selling price per unit	...	Rs. 100
Variable cost per unit	...	Rs. 60
Fixed operating cost	...	Rs. 40,000
Sales volume	...	1,200 units

What is the financial leverage of the company if 10 % change in sales will bring about 90 % change in EPS ?

What is the percentage increase in variable cost when OL is increased by 750 % ?

22. Define and explain the term capital structure. How does it differ from financial structure and asset structure ? Briefly explain the factors that influence the planning of capital structure of a company.

(3 × 5 = 15)