Test Series: May, 2020

MOCK TEST PAPER- 1

INTERMEDIATE (NEW): GROUP – II

PAPER – 8: FINANCIAL MANAGEMENT & ECONOMICS FOR FINANCE

PAPER 8A: FINANICAL 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) The data relating to two companies are as given below:

	Company A	Company B
Equity Capital	Rs.6,00,00,000	Rs.3,50,00,000
15% Debentures	Rs.40,00,000	Rs.65,00,000
Output (units) per annum	6,00,000	1,50,000
Selling price/ unit	Rs.60	Rs.500
Fixed Costs per annum	Rs.70,00,000	Rs.1,40,00,000
Variable Cost per unit	Rs.30	Rs.275

You are required to CALCULATE the Operating leverage, Financial leverage and Combined leverage of the two Companies.

(b) ABC Limited has the following book value capital structure:

Equity Share Capital (1 crore shares @ Rs.10 each)	Rs.1,000 lakh
Reserves and Surplus	Rs.2,250 lakh
9% Preference Share Capital (5 lakh shares @ Rs.100 each)	Rs.500 lakh
8.5% Debentures (1.5 lakh debentures @ Rs.1,000 each)	Rs.1,500 lakh
12% Term Loans from Financial Institutions	Rs.500 lakh

- The debentures of ABC Limited are redeemable at par after five years and are quoting at Rs.985 per debenture.
- The current market price per equity share is Rs.60. The prevailing default-risk free interest rate on 10-year GOI Treasury Bonds is 5.5%. The average market risk premium is 7%. The beta of the company is 1.85
- The preference shares of the company are redeemable at 10% premium after 5 years is currently selling at Rs.102 per share.

The applicable income tax rate for the company is 35%.

Required:

CALCULATE weighted average cost of capital of the company using market value weights.

(c) A company proposes to install a machine involving a Capital Cost of Rs.72,00,000. The life of the machine is 5 years and its salvage value at the end of the life is nil. The machine will produce the net operating income after depreciation of Rs.13,60,000 per annum. The Company's tax rate is 35%.

The Net Present Value factors for 5 years are as under:

Discounting Rate	:	14	15	16	17	18	19
Cumulative factor	:	3.43	3.35	3.27	3.20	3.13	3.06

You are required to COMPUTE the internal rate of return (IRR) of the proposal.

(d) A&R Ltd. is an all equity financed company with a market value of Rs.25,000 lakh and cost of equity (K_e) 18%. The company wants to buyback equity shares worth Rs.5,000 lakh by issuing and raising 10% debentures redeemable at 10% premium after 5 years. Rate of tax may be taken as 35%. Applying Modigliani-Miller (MM) (with taxes), you are required to CALCULATE after restructuring:

(i) Market value of A&R Ltd.

(ii) Cost of Equity (K_e)

(iii) Weighted average cost of capital (using market weights). **[4 × 5 Marks = 20 Marks]**

2. ZX Ltd. has a paid-up share capital of Rs.1,00,00,000, face value of Rs.100 each. The current market price of the shares is Rs.100 each. The Board of Directors of the company has an agenda of meeting to pay a dividend of 50% to its shareholders. The company expects a net income of Rs.75,00,000 at the end of the current financial year. Company also plans for a capital expenditure for the next financial year for a cost of Rs.95,00,000, which can be financed through retained earnings and issue of new equity shares.

Company's desired rate of investment is 15%.

Required:

Following the Modigliani- Miller (MM) Hypothesis, DETERMINE value of the company when:

(i) It does not pay dividend and

(ii) It does pay dividend **[10 Marks]**

3. A&R Ltd. has undertaken a project which has an initial investment of Rs.2,000 lakhs in plant & machinery and Rs.800 lakhs for working capital. The plant & machinery would have a salvage value of Rs. 474.61 lakhs at the end of the fifth year. The plant & machinery would depreciate at the rate of 25% p.a. on WDV method. The other details of the project for the five year period are as follows:

Sales	10,00,000 units p.a.
Selling price per unit	Rs.500
Variable cost	50% of selling price
Fixed overheads (excluding depreciation)	Rs.300 lakh p.a.
Corporate tax rate	35%
Rate of interest on bank loan	12%
After tax required rate of return	15%

Required:

(i) CACULATE net present value (NPV) of the project and DETERMINE the viability of the project.

(ii) DETERMINE the sensitivity of project's NPV under each of the following condition:

a. Decrease in selling price by 10%;

b. Increase in cost of plant & machinery by 10%.

PV factor	Year-1	Year-2	Year-3	Year-4	Year-5
12%	0.892	0.797	0.711	0.635	0.567
15%	0.869	0.756	0.657	0.571	0.497

[10 Marks]

4. The following accounting information and financial ratios of A&R Limited relate to the year ended 31st March, 2020:

Inventory Turnover Ratio	6 Times
Creditors Turnover Ratio	10 Times
Debtors Turnover Ratio	8 Times
Current Ratio	2.4
Gross Profit Ratio	25%

Total sales Rs.6,00,00,000; cash sales 25% of credit sales; cash purchases Rs.46,00,000; working capital Rs.56,00,000; closing inventory is Rs.16,00,000 more than opening inventory.

You are required to CALCULATE:

(i) Average Inventory

(ii) Purchases

(iii) Average Debtors

(iv) Average Creditors

(v) Average Payment Period

(vi) Average Collection Period

(vii) Current Assets

(viii) Current Liabilities.

Take 365 days a year **[10 Marks]**

5. (a) Cost sheet of A&R Ltd. provides the following particulars:

	Amount per unit (Rs.)
Raw materials cost	200.00
Direct labour cost	75.00
Overheads cost	150.00
Total cost	425.00
Profit	75.00
Selling Price	500.00

The Company keeps raw material in stock, on an average for four weeks; work-in-progress, on an average for one week; and finished goods in stock, on an average for two weeks.

The credit allowed by suppliers is three weeks and company allows four weeks credit to its debtors. The lag in payment of wages is one week and lag in payment of overhead expenses is two weeks.

The Company sells one-fifth of the output against cash and maintains cash-in-hand and at bank put together at Rs.2,50,000.

Required:

PREPARE a statement showing estimate of Working Capital needed to finance an activity level of 2,60,000 units of production. Assume that production is carried on evenly throughout the year, and wages and overheads accrue similarly. Work-in-progress stock is 80% complete in all respects.

(b) The following information is provided by the P Ltd. for the year ending 31st March, 2020.

Raw Material storage period	52 days
Work in progress conversion period	18 days
Finished Goods storage period	20 days
Debt Collection period	75 days
Creditors' payment period	25 days
Annual Operating Cost	45 crore
(Including depreciation of Rs.42,00,000)	

(1 year = 360 days)

You are required to CALCULATE Operating Cycle period and Number of Operating Cycles in a year. **[8 + 2 = 10 Marks]**

6. Answer the followings:

(a) EXPLAIN in brief the Pecking order theory.

(b) EXPLAIN Over-capitalisation. STATE its causes and consequences.

(c) EXPLAIN in short the term Letter of Credit.

OR

"Financing a business through borrowing is cheaper than using equity." Briefly EXPLAIN.

[4+4+2 = 10 Marks]

PAPER 8B: ECONOMICS FOR FINANCE

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

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 **7** is compulsory question.*

*Attempt any **three** from the remaining four questions*

In case, any candidate answers extra questions(s)/sub-question(s)/sub-question(s) over and above the required number, then only the requisite number of questions first answered will be the evaluated the rest answer shall be ignored

Working Notes should form part of the answer.

QUESTIONS

7. (a) How are the following transactions treated in national income calculation? What is the rationale in each case?

(i) Electricity sold to a steel plant

(ii) Electric power sold to a consumer household

(iii) A car manufacturer procuring parts and components from the market **(3 Marks)**

(b) What do you mean by price ceiling? Explain it with the help of examples. **(2 Marks)**

(c) How the following affect money multiplier and money supply?

(i) Banks open large number ATMs all over the country.

(ii) If banks decide to keep 100% reserves. **(3 Marks)**

(d) How does trade increase economic efficiency? **(2 Marks)**

8. (a) Examine the situation if aggregate expenditures exceeds the economy's production capacity.

(2 Marks)

(b) How do the markets fail in an economy? What are the main reasons behind this market failure and economic inefficiency? **(3 Marks)**

(c) Explain operating procedures in the context of monetary policy of India? **(2 Marks)**

(d) How does Escalated tariff structure work and discriminated ? **(3 Marks)**

9. (a) Fiscal policy achieve social justice and equity. Comment on this with the help of examples.

(5 Marks)

(b) What does the reserve money determine? Compute Reserve Money from the following data-

Particulars	**Rs. in Crore**
Currency in circulation	14903.90
RBI's net non-monetary liabilities	4945.80

Banker's deposits with RBI	5780.60	
Other deposits with RBI	317.20	
Long term deposits of residents	321.10	**(3 Marks)**

(c) What are the major functions of the WTO? **(2 Marks)**

10. (a) An increase in investment by Rs. 700 crore leads to increase in national income by Rs 3,500 crore. Calculate marginal propensity to consume and change in saving. **(3 Marks)**

(b) What effect does government expenditure have on money supply? **(2 Marks)**

(c) Define tariff and what are its effects on the importing and exporting countries? **(5 Marks)**

11. (a) Calculate the GNP at market price using value added method with the help of following data –

Particulars	Rs. in crore
Value of output in primary sector	1000
Net factor income from abroad	-20
Value of output in tertiary sector	700
Intermediate consumption in secondary sector	400
Value of output in secondary sector	900
Government transfer payments	600
Intermediate consumption in primary sector	500
Intermediate consumption in tertiary sector	400

(5 Marks)

(b) What do you mean by common pool resources and why producers and consumers do not pay for these resources? **(3 Marks)**

(c) What role does Market Stabilisation Scheme (MSS) play in our economy? **(2 Marks)**

OR

What is meant by import quotas? **(2 Marks)**