



Institute of Management
JK Lakshmipat University, Jaipur
END TERM EXAMINATION -2018

Pinnacle MBA (Term II)
Subject Code: P 201
MM: 40Marks

Introduction to Corporate Finance
Time: 2 Hours

Instructions:

- a) *All questions are compulsory.*
- b) *There are varied patterns of the question. Read the question very carefully.*
- c) *Questions in section A carries one marks only.*

Section A

1. Financing timeline is the relation between the business and its:
A. Debt holders
B. Equity Shareholders
C. Both the above
D. None of the Above
2. A capital project is producing NIL NPV. This situation is represented by which of the following:
A. Profitability Index = 1 and IRR > Cost of Capital
B. Profitability Index > 1 and IRR = Cost of Capital
C. Profitability Index = 1 and IRR = Cost of Capital
D. Profitability Index < 1 and IRR > Cost of Capital
3. Which of the following is the incorrect definition of Net Present Value?
A. It's a cash flow at T0.
B. It's a hypothetical value, representative of the series of cash flows on the timeline.
C. It's a function of more than one variable.
4. Pay back method has the following challenges for it to be used in the capital budgeting exercise:
A. It is neither based on TVM nor on cash flows.
B. It is based on TVM, but not on cash flows.
C. It is not based on TVM, but on cash flows.
5. A Bank, while planning a loan proposal, has estimated 3% as the expected inflation during the loan period. The actual inflation turns out to be 2.5%. Due to this error, the bank has:

P.T.O.

- A. Gained B. Lost C. Not been affected D. Similar situation

6. Calculation of cost of capital and IRR has the following relationship:

- A. Cost of capital depends upon IRR but not vice versa.
- B. IRR depends upon Cost of capital but not vice versa.
- C. Both IRR and Cost of capital are inter-dependent.
- D. Both IRR and Cost of capital are independent.

7. A company has just paid stock dividends. The impact on financials will most likely be:

- A. Increase in Equity, Increase in retained earnings.
- B. No change in Equity, No change in retained earnings.
- C. No change in Equity, decrease in Retained Earnings.

8. A company wants to increase its leverage without impacting its variability in earning. The above objective is:

- A. Practically possible but not theoretically possible.
- B. Theoretically possible but not practically possible.
- C. Neither practically possible nor theoretically possible.

9. We make the entire capital budgeting analysis on an after-tax basis because:

- A. Taxes are a reality of life.
- B. Equity shareholders receive any value only after payment of taxes.
- C. Taxes keep on changing and we need to be dynamic.

10. When is it possible to have Marginal Cost of Capital as well as Weighted Average Cost of Capital being calculated together in the same scenario?

11. What are the three component of any rate of return?

12. If a company wants to increase its return and has stable cash flows from the project, _____ source of financing is the best choice.

13. If a company does not want Dilution of control and has unstable cash flows from the project, _____ source of financing is the best choice.

14. Stock-split in the ratio of 2 for 1 will increase the wealth of the equity shareholders of the company by _____ percent.

15. In case of an investing time line, cash flows at the maturity will most likely have a _____ sign.

16. Stock dividends affect liquidity as well as financial leverage ratios of firm

A. True

B. False

17. Degree of Total / Combined Leverage = DFL + DOL. The statement is

A. True

B. False

18. Consider a company with an asset base of Rs. 500 and liabilities of Rs. 100. One investor, Mr. John Smith, owns 3 shares out of total 10 shares in the company. The company is contemplating various options to distribute wealth to the investors. What shall be the wealth of the investor and in which form if the company decides to buy back shares worth Rs. 150?

19. Using the above case facts, would your answer change in case the company decides to go for cash dividend?

20. A company has total fixed cost of Rs. 400 million and Interest Cost Rs. 160 million. What shall be the operational break even if the contribution per unit is Rs. 5 and variable cost per unit is Rs. 3?

Section B

1. Compare various source of long term financing (Capital Structure) in terms of High/Low or Yes/No. (2.5 Marks)

Sources	Cost	Dilution of Control	Risk	Restraint on Managerial Freedom
Equity Capital				
Retained Earnings				
Preference Capital				
Long term Loans				
Debentures				

2. The Relevant financial information for Xavier Ltd. for the year ending 2019 is giving below:

Profit & Loss A/C data		Balance Sheet Data	
Rs. (in Million)		Beginning of 2019	Ending of 2019
Sales	80	Inventory	9
Cost of goods sold	56	Accounts Receivable	12
		Accounts Payable	7

P.T.O.

Inventory holding period, accounts receivable period and accounts payable periods are respectively 68.4, 63.9 and 55.4 days. Compute operating cycle as well as length of net operating cycle. (2.5 Marks)

3. Calculate EPS of Solid Ltd. and Sound Ltd. assuming (a) 20% EBIT of return on assets, (b) 10% EBIT of return on assets based on the following data:

	Solid Ltd. Rs. in Lacks	Sound Ltd. Rs. in Lacks
Assets	100	100
Debt (12% Debentures)	-----	50
Equity (Share of Rs. 10 each)	100	50

Assume a 50% income tax in both the cases. Give your comments on the financial Leverage.

(5 Marks)

Section C (Case Study)

M.C. Ltd. is planning an expansion programme which will require Rs. 30 crores and can be funded through one of the three following options:

- Issue further equity share of Rs. 100 each at par,
- Raise loans at 15% Interest
- Issue preference shares at 12%.

Present paid up capital is Rs. 60 Crores and average annual EBIT is Rs. 12 Crores. Assume I.T. rate at 50%. After the expansion, EBIT is expected to be Rs. 15 crores per annum.

Calculate EPS under the three financing options indicating the alternative giving the highest return to the equity shareholders. Considering yourself as finance manager of M.C. Ltd what option you will consider for fund raising and why. (10 Marks)