PGDM

Corporate Finance

DM 302

Trimester – III, End-Term Examination: March 2017

Time allowed: 2 Hrs 30 Min
Max Marks: 50

Roll No: _____

Instruction: Students are required to write Roll No on every page of the question paper, writing anything except the Roll No will be treated as Unfair Means. All other instructions on the reverse of Admit Card should be followed meticulously.

Sections	No. of Questions to attempt	Marks	Marks
A	3 out of 5 (Short Questions)	5 Marks each	3*5 = 15
B	2 out of 3 (Long Questions)	10 Marks each	2*10 = 20
C	Compulsory Case Study	15 Marks	15
		Total Marks	**50**

SECTION A

A1) When do you think NPV and IRR will produce conflicting results? If so which would be relied upon?

A2) M and N are two critical components that the firm requires. The usage, reorder quantity and the delivery time of these two components are given below:

	Component M	Component N
Normal Usage	40 units per week	50 units per week
Minimum Usage	15 Units per week	25 Units per week
Maximum Usage	55 Units per week	70 Units per week
Re-order quantity	200 units	500 units
Delivery Time	4 to 6 weeks	3 to 5 weeks

Firm wants you to calculate the following for each of the component:
Reorder Level
Minimum Stock Level
Maximum Stock Level

A3) Current net operating income (NOI) of a firm is Rs. 50 lakh. At present the firm's capital structure has debt financing of 20% of the total capital of Rs. 500 lakh, at 12% interest rate. Its equity capitalization (cost of equity) is estimated to be 15%. Find out the following;

A. Current value of the firm, using traditional approach
B. Firm's overall cost of capital (WACC).

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A4) You are given the following information:

Variance of net daily cash flows	$100,000
Annual rate of return on short term investments	6%
Lower cash limit	$ 100
Transaction Costs	$ 10

a. Calculate the Target Cash Balance
b. Calculate the Upper Cash Limit

A5) A firm purchases machinery of Rs 8,00,000.by making a down payment of Rs 1,50,000 and remainder in equal installments of Rs 1,50,000 for six years . What is the rate of interest to the firm?

SECTION B

B1) Calculate the degree of operating leverage, degree of financial Leverage and degree of combined leverage for the following firms and also interpret the results obtained

	Firm X	Frim Y	Firm Z
Output Units	80,000	22,500	1,50,000
Variable Cost Per Unit Rs	1.5	1.1	1.2
Fixed Cost Rs	10,000	20,000	8000
Interest on Loan Funds Rs	6000	10,000	--
Selling Price Per Unit Rs	2.5	5.0	1.5

B2) Alliance Ltd. having annual sales of 80 lakh extends 30 days credit period to its debtors. The variable cost is estimated at 80% on sales and fixed costs are 8 lakh. The company intends to change the credit policy for which the following information is given :

Credit policy	Average collection period (days)	Annual sales (in lakh)
A	45	86
B	60	90
C	75	92

Rate of return (pre-tax) required on investment is 20%.

You are required to assess the most profitable policy with the help of incremental approach. Calculations may be restricted to two decimal points. Assume 365 days in a year.

B3) Firms consider large number of factors in determining dividend policy of the firm. List down and discuss key factors.

SECTION C - COMPULSORY CASE

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An eatery is located in its own premises at Street A in a city. The Management is planning a relocation to a nearby new location, College Road , also owned by it so that it can attract new clients. Two years ago College Road was considered and Rs 2,00,000 was paid to the consultant for site study. Due to the metro construction the idea had to be abandoned. Now the road is fit for easy access. Until now, the College Road premises could not be let out and was idle. But now it can be let out on an annual year end lease rental of Rs 1,20,000. On similar terms, Street A premises would fetch Rs 2,50,000. The eatery would have to spend Rs 10,00,000 on initial refurbishment if it relocates. This will entail the bank loan at 12% interest. 25% of its new sales would be from old customers at the Street A premises which represented 25% of the Street A sales value. Other information is given below

Figures (Rs /Per Annum) Valid for next five years	Street A Same as per existing Values	College Road
Sales	15,00,000	21,00,000
Variable Cost	10,00,000	11,00,000
Contribution	5,00,000	10,00,000
Fixed Cost (excluding Depreciation)	1,50,000	2,40,000
Depreciation		

1. Depreciation is on straight line basis over five years. Assume that the life of the project is five years from now in both the premises
2. Income tax rate applicable is 35% and taxes are payable at the end of the year
3. Cash flow from operations arise at the end of the year
4. There is no salvage value at the end of the project life.
5. Both the sites are meant for long term usage. There is no sale of premises envisaged.
6. Weighted average cost of capital until the project begins is 10%
7. The bank loan has to be repaid in equal instalments of principal at the end of each year together with the applicable interest on outstanding principal
8. Assume no time lag between the capital expenditure and commencement of operations
9. No significant changes in the working capital requirements

You are required to present a statement showing the evaluation on an incremental basis of relocating to the new premises showing the rationale behind the cash flow you considered and those that you do not for evaluation. Recommend from the financial prospective using the NPV Method, whether the eatery should relocate to the college road premises.

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