CA INTERMEDIATE NOV'19

SUBJECT- F.M. AND ECONOMICS

Test Code – CIM 8408

(Date :)

(Marks - 100)

SECTION -A

Question No. 1 is compulsory.

Attempt any four questions from the remaining five questions.

Maximum Marks – 60

QUESTION NO.1 **(5 MARKS X 4 = 20 MARKS)**

A. With the help of the following information **ANALYSE and complete the Balance Sheet of Anup Ltd.:**

Equity share capital	Rs. 1,00,000
The relevant ratios of the company are as follows:	
Current debt to total debt	0.40
Total debt to Equity share capital	0.60
Fixed assets to Equity share capital	0.60
Total assets turnover	2 Times
Inventory turnover	8 Times

B. With the help of following figures **CALCULATE the market price of a share** of a company by using:

(i) Walter's formula

(ii) Dividend growth model (Gordon's formula)

Earnings per share (EPS)	Rs. 10
Dividend per share (DPS)	Rs. 6
Cost of capital (k)	20%
Internal rate of return on investment	25%
Retention Ratio	60%

C. Annual sales of a company is Rs. 60,00,000.Sales to variable cost ratio is 150 per cent and Fixed cost other than interest is Rs. 5,00,000 per annum. Company has 11 per cent debentures of Rs. 30,00,000.

You are required to calculate the operating, Financial and combined leverage of the company.

D. **Determine the risk adjusted net present value** of the following projects:

	X	Y	Z
Net cash outlays (Rs.)	2,10,000	1,20,000	1,00,000
Project life	5 years	5 years	5 years
Annual Cash inflow (Rs.)	70,000	42,000	30,000
Coefficient of variation	1.2	0.8	0.4

The Company selects the risk-adjusted rate of discount on the basis of the coefficient of variation:

Coefficient of Variation	Risk-Adjusted Rate of Return	P.V. Factor 1 to 5 years At risk adjusted rate of discount
0.0	10%	3.791
0.4	12%	3.605
0.8	14%	3.433
1.2	16%	3.274
1.6	18%	3.127
2.0	22%	2.864
More than 2.0	25%	2.689

QUESTION NO.2

A. Navya Ltd has annual credit sales of Rs. 45 lakhs. Credit terms are 30 days, but its management of receivables has been poor and the average collection period is 50 days, Bad debt is 0.4 per cent of sales. A factor has offered to take over the task of debt administration and credit checking, at an annual fee of 1 per cent of credit sales. Navya Ltd. estimates that it would save Rs. 35,000 per year in administration costs as a result. Due to the efficiency of the factor, the average collection period would reduce to 30 days and bad debts would be zero. The factor would advance 80 per cent of invoiced debts at an annual interest rate of 11 per cent. Navya Ltd. is currently financing receivables from an overdraft costing 10 per cent per year.

If occurrence of credit sales is throughout the year, **COMPUTE whether the factor's services should be accepted or rejected.** Assume 365 days in a year.

(6 Marks)

B. EXPLAIN the limitations of Leasing? **(4 Marks)**

QUESTION NO.3 **(10 MARKS)**

X Ltd. is considering to select a machine out of two mutually exclusive machines. The company's cost of capital is 15 per cent and corporate tax rate is 30 per cent. Other information relating to both machines is as follows:

	Machine – I	Machine – II
Cost of Machine	Rs. 30,00,000	Rs. 40,00,000
Expected Life	10 years.	10 years.
Annual Income (Before Tax and Depreciation)	Rs. 12,50,000	Rs. 17,50,000

Depreciation is to be charged on straight line basis:

You are required to CALCULATE:

(i) Discounted Pay Back Period

(ii) Net Present Value

(iii) Profitability Index

The present value factors of Re.1 @ 15% are as follows:

Year	01	02	03	04	05
PV factor @ 15%	0.870	0.756	0.658	0.572	0.497.

QUESTION NO.4 **(10 MARKS)**

Best of Luck Ltd., a profit making company, has a paid-up capital of Rs. 100 lakhs consisting of 10 lakhs ordinary shares of Rs. 10 each. Currently, it is earning an annual pre-tax profit of Rs. 60 lakhs. The company's shares are listed and are quoted in the range of Rs. 50 to Rs. 80.The management wants to diversify production and has approved a project which will cost Rs. 50 lakhs and which is expected to yield a pre-tax income of Rs. 40 lakhs per annum. To raise this additional capital, the following options are under consideration of the management:

(a) To issue equity share capital for the entire additional amount. It is expected that the new shares (face value of Rs. 10) can be sold at a premium of Rs. 15.

(b) To issue 16% non-convertible debentures of Rs. 100 each for the entire amount.

(c) To issue equity capital for Rs. 25 lakhs (face value of Rs. 10) and 16% non-convertible debentures for the balance amount. In this case, the company can issue shares at a premium of Rs. 40 each.

You are required to advise the management as to how the additional capital can be raised, keeping in mind that the management wants to maximise the earnings per share to maintain its goodwill. The company is paying income tax at 50%.

QUESTION NO.5 **(10 MARKS)**

The following data relates to four Firms -

Firm	**A**	**B**	**C**	**D**
EBIT	Rs.2,00,000	Rs.3,00,000	Rs.5,00,000	Rs.6,00,000
Interest	Rs.20,000	Rs.60,000	Rs.2,00,000	Rs.2,40,000
Equity Capitalization Rate	12%	16%	15%	18%

Assuming that there are no taxes and Interest Rate on Debt is 10%, determine the Value and WACC of each Firm using the Net Income Approach. What happens if Firm A borrows Rs. 2 Lakhs at 10% to repay Equity Capital ?

QUESTION NO.6

A. EXPLAIN as to how the wealth maximisation objective is superior to the profit maximisation objective What is the cost of these sources? **(4 MARKS)**

B. DESCRIBE Bridge Finance. **(4 MARKS)**

C. EXPLAIN Concentration Banking **(2 MARKS)**

SECTION –B

Question 1 is compulsory question.

Attempt any three from the remaining four questions

1. (a) Suppose in an economy:

Consumption Function (C) = 100 + 0.9 Yd, where Yd = Y-T

Autonomous Investment (I) = Rs. 100 crores

Government Expenditure G = Rs. 120 crores

Taxes (T) = Rs.50 crores

Exports (X) = Rs.200 crores

Import Function (M) = 100 + 0.15Y

Where Y and Yd National Income and Personal Disposable Income respectively. All the figures are in Rupees. Find the Equilibrium level of GDP? **(3 Marks)**

(b) Define permanent income and state its relationship to demand for real money balances? **(3 Marks)**

(c) Explain why government imposes price ceilings? **(2 Marks)**

(d) What is meant by trade distortion? **(2 Marks)**

2. (a) (i) Explain how decline in interest rates influence economic activity by changing the incentives for households and businesses to save or invest? **(3 Marks)**

(ii) Define Information Failure **(3 Marks)**

(b) (i) What is meant by nominal GDP-growth? **(2 Marks)**

(ii) Define optimal output from the point of view of social welfare? **(2 Marks)**

3. (a) (i) Explain the effects of monetary policy through balance sheet channel **(3 Marks)**

(ii) What is the major determinant of the economic functions of a government? **(2 Marks)**

(b) Calculate (a) GDPMP and (b) NNPFC from the following data: **(5 Marks)**

Particulars		(Rs) In Crore
(i)	Net indirect tax	208
(ii)	Consumption of fixed capital	42
(iii)	Net factor income from abroad	-40
(iv)	Rent	311
(v)	Profits	892
(vi)	Interest	81
(vii)	Royalty	6
(viii)	Wages and salary	489
(ix)	Employer's contribution to Social Security Scheme	50

4. (a) (i) How do foreign direct investments enhance human capital in recipient countries? **(5 Marks)**

(b) (i) What do you understand by the term 'final good"? **(2 Marks)**

(ii) Explain the different types of Externalities? How Externalities lead to welfare loss of markets? **(3 Marks)**

5. (a) (i) What is the rationale for government intervention in allocation of resources? **(3 Marks)**

(ii) Distinguish between 'non tariff measures' and 'non tariff barriers' **(3 Marks)**

(b) (i) What do you understand by the term 'cross rate'? **(2 Marks)**

(ii) What is the objective of policies requiring foreign entities to procure local contents?

(2 Marks)

OR

What is meant by open market operations?