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Total No. of Questions: 10 **Total No. of Pages: 04**

MBA/MBA (IB) (Sem. 2)
FINANCIAL MANAGEMENT
Subject Code: MBA-205
Paper ID: C0250

Time: 3 Hrs. **Max. Marks: 60**

INSTRUCTION TO CANDIDATES:

1. **Attempt any FOUR questions from SECTION A. Each question carries FIVE marks.**
2. **SECTION B contains FOUR SUBSECTIONS. Attempt ONE question from every subsection. Each question carries EIGHT marks.**
3. **SECTION C is COMPULSORY carrying EIGHT marks each.**

SECTION A

1.

a) Define profit maximization.
b) What do you mean by Private Placement?
c) Describe Average rate of return.
d) State CAPM.
e) Describe financial leverage.
f) Elaborate ROE.

SECTION B

SUB SECTION I

2. When can there arise a conflict between shareholders and managers goals? How does wealth maximization goal take care of this conflicts?

3. What sources of long term finance are available for companies?

SUB SECTION II

4. Explain the merits and demerits of the time-adjusted methods os evaluating investment projects.

5. "An individual s time preference for money may be expressed as a rate " Explain.

SUB SECTION III

6. Two firms A and B have following information.

	Sales (Rs. in lakh)	Sales (Rs. in lakh)	Sales (Rs. in lakh)
FIRM A	1800	450	900
FIRM B	1500	750	375

you are required to calculate a) Profit to sales ratio, b) break-even point, and
c) degree of operating leverage for both firms.

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

SUB SECTION IV

8. Briefly explain factors that determine the working capital need of a firm.

9. How do companies can finance their current assets?

SECTION C

10. Analyze the facts given in the case and answer the given questions. (*on next page)*

Indus Engineering Limited

Indus Engineering Limited (IEL) is a well-known manufacturer of engineering products. The company's product line includes about 100 models of various products. Table 29.l.l gives the company for the current year. As compared to the last year, sales have grown by 15 per cent. The managing director is expecting sales to grow at this rate next year as well. She also to grow at this rate next year as well. She also thinks that there will be no change in the gross margin and working capital ratios.

Summarised Profit and Loss Statement and Balance Sheet

Items		**Rs (in Crore)**
Profit and Loss Statement		
Sales		876
Less: Cost of goods sold		673
Gross profit		203
Less: Other expenses, including interest		117
Profit before tax		86
Less: Tax		32
Profit after tax		54
Balance Sheet		
Share capital		100
Reserve and surplus		204
Shareholders' Funds		304
Borrowings		458
Total Funds		762
Net fixed assets		504
Current Assets :		
Cash		
Cash	9	
Receivable	195	
Inventories		
Raw Materials	44	
Work-in process	32	
Finished goods	50	
Total	330	
Less: Current liabilities	72	
Net Current assets		258
Total Assets		762

The company produces and stocks goods according to the sales forecasts for each item. Given sales forecasts, goods are produced in quantities that raise levels of stocks to estimated sales requirements. Recently, the company has introduced a tight inventory control system because of the shortage of financial resources, and it has been maintaining inventories below the target levels. It was thought by many company executives that the policy of tight inventory control has resulted in substantial loss of sales. It was noticed that the company has been frequently losing orders to competitors because of stock-outs.

The problem of lost sales forced management to reconsider its inventory policy. The company therefore appointed a committee, consisting of general managers of finance; marketing and production to determine whether finished goods inventory levels should be increased. The committee reported that more than the tightness of the current inventory control system; it was based on inaccurate sales forecasts. It was noted that it was very difficult to make prediction of new demand since customers erratically placed orders.

The committee recommended that the company should adopt a system of safety stocks to avoid stock-out problem. It was suggested that safety stocks should be determined after a careful consideration of (i) costs, (ii) return, and (iii) risks associated with inventory maintenance. It was, therefore, thought necessary to compile data on possible inventory levels, lost sales on account of stock-outs and annual cost of maintaining higher level s of finished goods inventory. Table provides such estimates. The company's after-tax required rate of return is 12 percent. Assume 35 per cent tax rate.

Alternative Inventory Policies

Inventory Options Policy	Inventory Level (Rs in crore) `	Lost Sales (Rs in crore)	Carrying Cost (Rs in crore)
Current	50	75	2.2
A	60	55	3.0
B	80	40	4.1
C	100	20	5.9
D	130	10	7.1
E	140	5	7.7

Discussion Questions

1. What are Indus' problems in managing inventories?
2. Which inventory policy is the optimum for Indus? Why? Show calculations.