



# BRAINWARE UNIVERSITY

Course – MBA

Corporate Finance (FM302)

(Semester – 3)

**Time allotted: 3 Hours**

**Full Marks: 70**

[The figure in the margin indicates full marks. Candidates are required to give their answers in their own words as far as practicable.]

## Group –A

(Multiple Choice Type Question)

**1. Choose the correct alternatives for the following:**

**10 x 1 = 10**

- I. Which of the following dividend model cannot find optimal dividend policy
  - a. Walter Model
  - b. Gordon Model
  - c. Modigliani Miller Hypothesis
  - d. None of them
- II. The basic drawback of NPV is that, it cannot consider initial investment. This drawback can be eliminated by
  - a. Capital Rationing
  - b. ROI
  - c. Both of them
  - d. None of them
- III. Relationship between Economic Value Added (EVA) and Net Present Value (NPV) is considered as
  - a. valued relationship
  - b. economic relationship
  - c. direct relationship
  - d. inverse relationship
- IV. Shareholders wealth increases with the increase in \_\_\_\_\_
  - a. EPS
  - b. Market value of the firm
  - c. Dividend & market value of the firm
  - d. Market price of the equity share
- V. Leasing of machinery can be categorized as \_\_\_\_\_
  - a. Fixed asset
  - b. Investment decision
  - c. Financing decision
  - d. Capital budgeting decision

- VI. What is the most important use of the P/E ratio for investors?
- It helps investors decide how much profit a company is likely to make in future.
  - It helps investors decide whether a company's shares are overpriced or underpriced.
  - It helps investors decide on the most appropriate risk to reward ratio.
  - None of the above
- VII. A merger in which an entirely new firm is created and both the acquired and acquiring firms cease to exist is called a:
- Divestiture.
  - Consolidation.
  - Tender offer.
  - Spinoff
- VIII. A project whose acceptance does not prevent or require the acceptance of one or more alternative projects is referred to as \_\_\_\_\_.
- a mutually exclusive project
  - an independent project
  - a dependent project
  - a contingent project
- IX. The required rate of return is influenced by
- Inflation
  - Risk free return
  - Risk involve in the project
  - All of the above
- X. In case of Spin-off, the
- Management and shareholders remain same of the new company
  - Management and shareholders changes from the new company
  - Management remain same but shareholders may change in the new company
  - None

### **Group - B**

#### **(Short Answer Type Questions)**

**Answer any three of the following**

**3 x 5 = 15**

- Discuss the conflicting situation between NPV and IRR.
- Discuss about the determinants of dividend policy.
- State the significance of Decision Tree approach in project decision making?
- Explain synergy in the context of Mergers and Acquisitions.
- State the significance of corporate restructuring.

**Group - C**  
**(Long Answer Type Questions)**

Answer any three of the following

3 x 15 = 45

7. Eagle Ltd. reported a profit of Rs. 77 lakhs after 30% tax for the financial year 2011-12. An analysis of the accounts revealed that the income included extraordinary items of Rs. 8 lakhs and an extraordinary loss of Rs. 10 lakhs. The existing operations, except for the extraordinary items, are expected to continue in the future. In addition, the results of the launch of a new product are expected to be as follows:

	Rs. In Lakhs
Sales	70
Material costs	20
Labour costs	12
Fixed costs	10

You are required to:

- (i) Calculate the value of the business, given that the capitalization rate is 14%.
- (ii) Determine the market price per equity share, with Eagle Ltd's share capital being comprised of 1,00,000, 13% preference shares of Rs. 100 each and 50,00,000 equity shares of Rs. 10 each and the P/E ratio being 10 times.

[15]

8. X Ltd. an existing profit-making company is planning to introduce a new product with a projected life of 8 years. Initial equipment cost will be Rs.120 lakhs and additional equipment costing Rs.10 lakhs will be needed at the beginning of third year. At the end of the 8 years, the original equipment will have resale value equivalent to the cost of removal, but the additional equipment would be sold for Rs.1 lakhs. Working Capital of Rs.15 lakhs will be needed. The 100% capacity of the plant is of 4,00,000 units per annum, but the production and sales-volume expected are as under:

Year	Capacity in percentage
1	20
2	30
3-5	75
6-8	50

A sale price of Rs. 100 per unit with a profit-volume ratio of 60% to be obtained. Fixed operating cash cost are likely to be Rs. 16 lakhs per annum. In addition to this the advertisement expenditure will have to be incurred as under:

Year	Expenditure in Rs lakhs each year
1	20
2	30
3-5	75
6-8	50

The company is subject to 50% tax, straight -line method of depreciation, (permissible for tax purposes also) and taking 12% as appropriate after tax Cost of Capital, should the project be accepted? [15]

9. A firm has an investment proposal, requiring an outlay of Rs.80,000. The investment proposal is expected to have two years economic life with no salvage value. In year 1, there is a 0.4 probability that cash inflow after tax will be Rs.50,000 and 0.6 probability that cash inflow after tax will be Rs.60,000. The probability assigned to cash inflow after tax for the year 2 is as follows:

The cash inflow year 1	Rs. 50,000		Rs. 60,000	
The cash inflow year 2	Cash Flow	Probability	Cash Flow	Probability
	Rs. 24000	0.2	Rs. 40000	0.4
	Rs. 32000	0.3	Rs. 50000	0.5
	Rs. 44000	0.5	Rs. 60000	0.1

The firm uses a 10% discount rate for this type of investment.

Required:

- (i) Construct a decision tree for the proposed investment project and calculate the expected net present value (NPV).
- (ii) What net present value will the project yield, if worst outcome is realized? What is the probability of occurrence of this NPV?
- (iii) What will be the best outcome and the probability of that occurrence?
- (iv) Will the project be accepted?

[15]

10. Write short notes on:

- i) Beta of a Capital Project
- ii) Company valuation process using dividend discount Model.
- iii) Decision or outcome from Walter Dividend Model.

[5x3=15]