RD-3531
Second Year B. B. A. (Sem. IV) Examination
April/May – 2017
Financial Management - II

Time : 2 Hours] [Total Marks : 50

Instruction :

1 Answer in brief : (any five) 10
   (a) Explain the role of ‘Operational efficiency’ in the
determination of working capital requirement.
   (b) Depreciation, a non-cash cost, is a prominent part of cash
flow analysis for investment decision. Explain.
   (c) What do you mean by discounted cash flow ?
   (d) State the difference between gross working capital and
net working capital.
   (e) What is inventory ? What are its types ?
   (f) Explain precautionary motive for maintaining cash
balance.

2 Explain non-discounted cash flow techniques for 13
evaluation of capital budgeting proposals. Also, state the
advantages and disadvantages of these techniques.

OR

RD-3531] 1 [Contd...
Sagar Industries Ltd. is planning to introduce a new product with a projected life of 8 years. The project, to be set up in a backward region, qualifies for a one-time (at its starting) tax-free subsidy from the government of Rs. 20,00,000. Initial equipment cost will be Rs. 1,40,00,000 and additional equipment costing Rs 10,00,000 will be needed at the beginning of the third year. At the end of 8 years, the original equipment will have no resale value, but the supplementary equipment can be sold for Rs. 1,00,000. A working capital of Rs. 15 lakh will be needed. The sales volume (units) over the 8-year period has been forecasted as follows:

<table>
<thead>
<tr>
<th>Year</th>
<th>Sales Volume (units)</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>80,000</td>
</tr>
<tr>
<td>2</td>
<td>1,20,000</td>
</tr>
<tr>
<td>3-5</td>
<td>3,00,000</td>
</tr>
<tr>
<td>6-8</td>
<td>2,00,000</td>
</tr>
</tbody>
</table>

A sale price of Rs. 100 per unit is expected and variable cost will amount to 40 per cent of sales revenue. Fixed cash operating costs will amount to Rs. 16,00,000 per year. In addition, an extensive advertising campaign will be implemented, requiring annual outlays as follows:

<table>
<thead>
<tr>
<th>Year</th>
<th>Advertising expenses (Rs.)</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>30,00,000</td>
</tr>
<tr>
<td>2</td>
<td>15,00,000</td>
</tr>
<tr>
<td>3-5</td>
<td>10,00,000</td>
</tr>
<tr>
<td>6-8</td>
<td>4,00,000</td>
</tr>
</tbody>
</table>

The company is subject to 35% tax rate and considers 12% to be the appropriate after-tax cost of capital rate for this type of project. The company follows the straight line method of depreciation and the same is accepted for tax purposes.

<table>
<thead>
<tr>
<th>Year</th>
<th>1</th>
<th>2</th>
<th>3</th>
<th>4</th>
<th>5</th>
<th>6</th>
<th>7</th>
<th>8</th>
</tr>
</thead>
<tbody>
<tr>
<td>PVIF</td>
<td>0.893</td>
<td>0.797</td>
<td>0.712</td>
<td>0.636</td>
<td>0.567</td>
<td>0.507</td>
<td>0.452</td>
<td>0.404</td>
</tr>
</tbody>
</table>

Should the project be accepted? Assume that the company has enough income from its existing products.
3  (a) Define economic order quantity (EOQ). What are the assumptions of the model? How can it be computed?
(b) What is factoring? Using a diagram explain the steps involved in factoring.

OR

3 Prepare a working capital forecast from the following information for ABC Limited.
Production during the previous year is 1.00 lakh units. The same level of activity is intended to be maintained during the current year.
The expected ratios of cost of selling price are
Raw Materials ................. 50%
Direct Wages ................. 10%
Overheads ................. 25%
- The raw materials ordinarily remain in stores for 2 months before production.
- Every unit of production remains in process for 2 months. Labour and overheads accrue evenly during the year.
- Finished goods remain in the warehouse for 4 months.
- Credit allowed by creditors is 3 months from the date of delivery of raw materials and credit given to debtors is 3 months from the date of dispatch.
- Selling price is Rs. 6 per unit.
- Both the production and sales are in a regular cycle.

4 Write short notes: (any two)
(a) Credit Policy Variables
(b) Concept of Float
(c) Maximum Permissible Bank Finance.