**JAIPURIA INSTITUTE OF MANAGEMENT, INDORE**

**PGDM**

**SECOND TRIMESTER (Batch 2020-22)**

**END TERM IMPROVEMENT EXAMINATION, APRIL-2021**

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| Course Name | **Corporate Finance** | Course Code | **FIN 201** |
| Max. Time | **2 hours** | Max. Marks | **40** |

**INSTRUCTIONS:**

All the questions are compulsory.

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**Questions.1 (10 Marks)**

ABC Ltd. needs Rs 500 lacs for an expansion plan that is expected to yield 15% return on assets. Currently its return on asset is 12% and the firm is all equity funded. For expansion it has alternatives of funding the entire expenditure either through debt or equity. Following information is available:

Nos. of shares already existing 20 lacs

Price at which the shares can be issued (Rs) Rs 50

Existing interest Rs 30 lacs

Interest rate on debt 10%

Tax rate 40%

Find out the new EPS with equity and debt financing. Also find at what level of earnings the firm is indifferent to mode of financing.

**Questions.2 (10 Marks)**

The following is the capital structure of Simons company Ltd. as on 31st March, current year Equity share: 10,000 shares (of Rs 100 each) Rs 10,00,000

12% Preference shares (of Rs 100 each) 4,00,000

10% Debentures 6,00,000

**20,00,000**

The market price of the company’s share is Rs 110 and it is expected that a dividend of Rs 10 per share would be declared at the end of the current year. The dividend growth rate is 6 per cent. (i) If the company is in the 35 per cent tax bracket, compute the weighted average cost of capital. (iii) Assuming that in order to finance an expansion plan, the company intends to borrow a fund of Rs 10 lakh bearing 12 per cent rate of interest, what will be the company’s revised weighted average cost of capital?

**Questions.3 (10 Marks)**

The present sales of Machete Productions are ₹.100 million. The firm classifies its customers into 3 credit categories: A, B, and C. The firm extends unlimited credit to customers in category A, limited credit to customers in category B, and no credit to customers in category C. As a result of this credit policy, the firm is foregoing sales to the extent of ₹10 million to customers in category B and ₹20 million to customers in category C. The firm is considering the adoption of a more liberal credit policy under which customers in category B would be extended unlimited credit policy and customers in category C would be provided limited credit. Such relaxation would increase the sales by ₹30 million on which bad debt losses would be 10 percent. The contribution margin ratio for the firm is 20 percent, the average collection period is 45 days, and the cost of capital is 16 percent.

Would you recommend relaxation of credit policy of the company? Show workings.

**Questions.4 (A) (5 Marks)**

AB Media Ltd. has retained earnings available of Rs.1.5 million. The firm has the plans to make investments in two projects which will require financing of Rs.6,50,000 and Rs. 1.2 million respectively. The CFO uses a target capital structure with 65% debt and 35% equity. He also intends to apply residual theory to determine what dividends, if any, can be paid out, and calculate the resulting dividend payout ratio. You are appointed to assist CFO and suggest the above query asked.

**Questions.4 (B) (5 Marks)**

What is the logic behind repurchasing shares of common stock to distribute the excess cash to the firm’s owners? Also compare the stock split and stock dividends.