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MS-42

01805

MANAGEMENT PROGRAMME

Term-End Examination

December, 2013

MS-42 : CAPITAL INVESTMENT AND FINANCING DECISIONS

Time : 3 hours *Maximum Marks : 100*

Weightage : 70%

Note : *Attempt* ***any five*** *questions. All questions carry* ***equal*** *marks. Use of* ***calculators*** *is allowed.*

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1. Distinguish between Mergers and Take-overs. How are Mergers and Take-overs regulated in India ? Discuss the legal procedure adopted in case of mergers.

2. (a) Explain the meaning and significance of the terms Stock Options and Non-Voting Right shares.

(b) What are Right shares ? How is the value of a Right determined ? Does a shareholder suffer a loss if he does not buy the rights ? Explain with example.

3. What do you understand by Economic Appraisal of a project ? What aspects are evaluated under economic appraisal ? Discuss the meaning and significance of Social Cost Benefit Analysis in this regard.

4. Distinguish between :

   (a) Venture Capital and Development Finance.

   (b) Foreign Direct Investment and Portfolio Investment.

   (c) Underwriting of Securities and Rating of Securities.

   (d) Convertible Debentures and Debentures with a Call Option.

5. (a) Why do companies prefer stable dividend policy ? In what ways is stability achieved in dividend distribution ?

   (b) What is 'factoring' ? How does it differ from discounting of bills ? Discuss the salient features of the factoring business.

6. Explain and distinguish between internal Rate of Return Method and Net Present Value Method of evaluating investment proposals. Which one would you prefer and why ? Why is Profitability Index prepared for evaluating the projects ?

7. The latest Balance Sheet items of D. Ltd. are given below :

	(Rs. '000)
Equity Share (50,000 shares)	500
Share Premium	100
Retained Profits	600
8% Pref. Shares	400
13% Perpetual Debt (face value Rs. 100 each)	600
	2200

The equity shares are currently priced at Rs. 39 ex-dividend each and Rs. 25 Preference Share is priced at Rs. 18 cum-dividend. The debentures are selling at 110% ex-Interest and tax is paid by D. Ltd. at 40%.

D.Ltd's Cost of equity has been estimated at 19%. Calculate The weighted average cost of Capital (based on market value).

8. The following figures of K. Ltd. are presented to you :

		Rs.
Earnings before Interest and Tax		23,00,000
Less Debenture Interest @ 8%	80,000	
Less Long Term loan Interest @ 11%	2,20,000	
Profit before Tax		3,00,000
Less Income Tax		20,00,000
Earning after Tax		10,00,000
No. of Equity Shares of Rs. 10 each		10,00,000
Market Price per share		5,00,000
P.E. Ratio		Rs. 20/- 10

The Company has undistributed resources and surplus of Rs. 10 lakh.

It is in need of Rs. 30 lakh to pay off debentures and modernise its plants. It seeks your advise on the following alternative modes of raising finance for this purpose.

Alternative 1 : Raising entire amount as term loan from banks @ 12%.

Alternative 2 : Raising part of the funds by issue of 1,00,000 shares of Rs. 20 each and the rest by way of term loans @ 12%.

The Company expects to improve its rate of return by 2% as a result of modernisation but PE ratio is likely to go down to 8 if the entire amount is raised as term loan.

(a) Advise the company on the financial plan to be selected.

(b) If it is assumed that there will be no change in the PE ratio even, if any of the two alternatives is adopted, would your advice still be the same ?