# MOCK TEST PAPER

## FINAL (NEW) COURSE: GROUP – I

## PAPER – 2: STRATEGIC FINANCIAL MANAGEMENT

*Question No. **1** is compulsory. Attempt any **four** questions from the remaining **five** questions.*

*Working notes should form part of the answer.*

**Time Allowed – 3 Hours** **Maximum Marks – 100**

1\. (a) Derivative Bank entered into a swap arrangement on a principal of ₹ 10 crores and agreed to receive MIBOR overnight floating rate for a fixed payment on the principal. The swap was entered into on Monday, 19th August, 2019 and was to commence on 20th August, 2019 and run for a period of 7 days.

Respective MIBOR rates for Tuesday to Monday were:

8.15%, 7.98%, 7.95%, 8.12%, 8.15%, 7.75%.

If Fixed Rate of Interest is 8%, then evaluate

(i) the nature of this Swap arrangement.

(ii) the Net Settlement amount.

Notes:

(1) Sunday is Holiday.

(2) Work in rounded rupees and avoid decimal working.

(3) Consider 365 days in a year. **(8 Marks)**

(b) The following are the data on five portfolios:

| Portfolio | Return | Standard Deviation | Beta |
|---|---|---|---|
| A | 15 | 7 | 1.25 |
| B | 18 | 10 | 0.75 |
| C | 14 | 5 | 1.40 |
| D | 12 | 6 | 0.98 |
| E | 16 | 9 | 1.50 |

You are required to evaluate the Reward to Volatility of these portfolio using:

- Sharpe method and
- Treynor's method

assuming the risk free rate is 6%. **(8 Marks)**

(c) Explain the problems that are faced in International Capital Budgeting Decision and how these can be overcome. **(4 Marks)**

2\. (a) You as a dealer in foreign exchange have the following position in GBP on 31st October, 2019:

| | GBP |
|---|---|
| Balance in the Nostro A/c Credit | 2,00,000 |
| Opening Position Overbought | 1,00,000 |
| Purchased a bill on London | 1,60,000 |

| | |
|---|---:|
| Sold forward TT | 1,20,000 |
| Forward purchase contract cancelled | 60,000 |
| Remitted by TT | 1,50,000 |
| Draft on London cancelled | 60,000 |

Decide the steps would you take, if you are required to maintain a credit Balance of GBP 65,000 in the Nostro A/c and keep as oversold position on GBP 20,000? **(8 Marks)**

(b) SAM Ltd. has just paid a dividend of ₹ 2 per share and it is expected to grow @ 6% p.a. After paying dividend, the Board declared to take up a project by retaining the next three annual dividends. It is expected that this project is of same risk as the existing projects. The results of this project will start coming from the 4th year onward from now. The dividends will then be ₹ 2.50 per share and will grow @ 7% p.a.

An investor has 1,000 shares in SAM Ltd. and wants a receipt of at least ₹ 2,000 p.a. from this investment.

Interpret how the market value of the share is affected by the decision of the Board. Also advise as to how the investor can maintain his target receipt from the investment for first 3 years and improved income thereafter, given that the cost of capital of the firm is 8%. **(8 Marks)**

(c) "Sustainable growth is important to enterprise long-term development". Explain this statement in context of planning healthy corporate growth. **(4 Marks)**

3. (a) MK Ltd. is considering acquiring NN Ltd. The following information is available:

| Company | Earning after Tax (₹) | No. of Equity Shares | Market Value Per Share (₹) |
|---|---|---|---|
| MK Ltd. | 60,00,000 | 12,00,000 | 200.00 |
| NN Ltd. | 18,00,000 | 3,00,000 | 160.00 |

Exchange of equity shares for acquisition is based on current market value as above. There is no synergy advantage available.

(i) Find the earning per share for company MK Ltd. after merger, and

(ii) Find the exchange ratio so that shareholders of NN Ltd. would not be at a loss.

**(8 Marks)**

(b) Mr. Y has invested in the three mutual funds (MF) as per the following details:

| Particulars | MF 'X' | MF 'Y' | MF 'Z' |
|---|---:|---:|---:|
| Amount of Investment (₹) | 2,00,000 | 4,00,000 | 2,00,000 |
| Net Assets Value (NAV) at the time of purchase (₹) | 10.30 | 10.10 | 10 |
| Dividend Received up to 31.03.2018 (₹) | 6,000 | 0 | 5,000 |
| NAV as on 31.03.2018 (₹) | 10.25 | 10 | 10.20 |
| Effective Yield per annum as on 31.03.2018 (percent) | 9.66 | -11.66 | 24.15 |

Assume 1 Year = 365 days

Mr. Y has misplaced the documents of his investment. Help him in finding the date of his original investment after ascertaining the following:

(i) Number of units in each scheme;

(ii) Total NAV;

(iii) Total Yield; and

(iv) Number of days investment held. **(8 Marks)**

(c) Explain various Asset Allocation Strategies. **(4 Marks)**

4. (a) Ram buys 10,000 shares of X Ltd. at a price of ₹ 22 per share whose beta value is 1.5 and sells 5,000 shares of A Ltd. at a price of ₹ 40 per share having a beta value of 2. He obtains a complete hedge by Nifty futures at ₹ 1,000 each. He closes out his position at the closing price of the next day when the share of X Ltd. dropped by 2%, share of A Ltd. appreciated by 3% and Nifty futures dropped by 1.5%.

Interpret the overall profit/loss of Ram? **(6 Marks)**

(b) STR Ltd.'s current financial year's income statement reported its net income after tax as ₹ 50 Crore.

Following is the capital structure of STR Ltd. at the end of current financial year:

| | ₹ |
|---|---|
| Debt (Coupon rate = 11%) | 80 Crore |
| Equity (Share Capital + Reserves & Surplus) | 250 Crore |
| Invested Capital | 330 Crore |

Following data is given to estimate cost of equity capital:

| | |
|---|---|
| Asset Beta of TSR Ltd. | 1.11 |
| Risk –free Rate of Return | 8.5% |
| Average market risk premium | 9% |

The applicable corporate income tax rate is 30%.

Estimate Economic Value Added (EVA) of RST Ltd. in ₹ lakh. **(8 Marks)**

(c) TRC Cables Ltd. (an Indian Company) is in the business of manufacturing Electrical Cables and Data Cables including Fiber Optics cables. While mainly it exports the manufactured cables to other countries it has also established its production facilities at some African countries' due availability of raw material and cheap labour there. Some of the major raw material such as copper, aluminum and other non-ferrous metals are also imported from foreign countries. Hence overall TRC has frequent receipts and expenditure items denominated in Non-INR currencies.

Though TRC make use of Long-Term Debts and Equity to meet its long term fund requirements but to finance its operations it make use of short-term financial instruments such as Commercial Papers, Bank Credit and Term Loans from the banks etc. If any surplus cash is left with TRC it is invested in interest yielding securities. Recently due to stiff competition from its competitors TRC has relaxed its policy for granting credit and to manage receivables it has formed a separate credit division.

Further to hedge itself against the various risk it has entered into various OTC Derivatives Contracts settled outside the Exchange.

Required:

Evaluate the major risks to which TRC Ltd. is exposed to. **(6 Marks)**

5. (a) Mr. A, a HNI invested on 1.4.2014 in certain equity shares as below:

| Name of Co. | No. of shares | Cost (₹) |
|---|---|---|
| X Ltd. | 1,00,000 (₹ 100 each) | 2,00,00,000 |
| Y Ltd. | 50,000 (₹ 10 each) | 1,50,00,000 |

In September 2014, 10% dividend was paid out by X Ltd. and in October 2014, 30% dividend paid out by Y Ltd. On 31.3.2015 market quotations showed a value of ₹ 220 and ₹ 290 per share for X Ltd. and Y Ltd. respectively.

On 1.4.2015, a technical analyst indicated as follows:

(1) that the probabilities of dividends from X Ltd. and Y Ltd. for the year ending 31.3.2016 are as below:

| Probability factor | Dividend from X Ltd. (%) | Dividend from Y Ltd. (%) |
|---|---|---|
| 0.2 | 10 | 15 |
| 0.3 | 15 | 20 |
| 0.5 | 20 | 35 |

(2) that the probabilities of market quotations on 31.3.2016 are as below:

| Probability factor | Price/share of X Ltd. | Price/share of Y Ltd. |
|---|---|---|
| 0.2 | 220 | 290 |
| 0.5 | 250 | 310 |
| 0.3 | 280 | 330 |

You are required to:

(i) Analyze the average return from the portfolio for the year ended 31.3.2015;

(ii) Analyze the expected average return from the portfolio for the year 2015-16; and

(iii) Advise Mr. A, of the comparative risk in the two investments. **(12 Marks)**

(b) Explain the various problems that are faced in growth of Securitization of Instruments in Indian context. **(4 Marks)**

(c) Explain various Market Indicators.

**OR**

Explain the term Angel Investor. **(4 Marks)**

6. (a) XYZ Ltd. has imported goods to the extent of US$ 8 Million. The payment terms are as under:

(1) 1% discount if full amount is paid immediately or

(2) 60 days interest free credit. However, in case of a further delay up to 30 days, interest at the rate of 8% p.a. will be charged for additional days after 60 days. M/s XYZ Ltd. has ₹ 25 Lakh available and for remaining it has an offer from bank for a loan up to 90 days @ 9.0% p.a.

The quotes for foreign exchange are as follows:

| | |
|---|---|
| Spot Rate INR/ US$ (buying) | ₹ 66.98 |
| 60 days Forward Rate INR/ US$ (buying) | ₹ 67.16 |
| 90 days Forward Rate INR/ US$ (buying) | ₹ 68.03 |

Advise which one of the following options would be better for XYZ Ltd.

(i) Pay immediately after utilizing cash available and for balance amount take 90 days loan from bank.

(ii) Pay the supplier on 60th day and avail bank's loan (after utilizing cash) for 30 days.

(iii) Avail supplier offer of 90 days credit and utilize cash available.

Further presume that the cash available with XYZ Ltd. will fetch a return of 4% p.a. in India till it is utilized.

Assume year has 360 days. Ignore Taxation.

Compute your working upto four decimals and cash flows in ₹ in Crore. **(10 Marks)**

(b) A company is long on 10 MT of copper @ ₹ 534 per kg (spot) and intends to remain so for the ensuing quarter. The variance of change in its spot and future prices are 16% and 36% respectively, having correlation coefficient of 0.75. The contract size of one contract is 1,000 kgs.

Required:

(i) Calculate the Optimal Hedge Ratio for perfect hedging in Future Market.

(ii) Advice the position to be taken in Future Market for perfect hedging.

(iii) Determine the number and the amount of the copper futures to achieve a perfect hedge.

**(6 Marks)**

(c) Examine briefly the various innovative methods of funding the Startups. **(4 Marks)**