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Register Number:

Date:

**ST. JOSEPH’S COLLEGE (AUTONOMOUS), BANGALORE-27**

**M.COM – II SEMESTER**

**SEMESTER EXAMINATION: APRIL 2022**

**(Examination conducted in July-August 2022)**

**MCO 8220: Advanced Corporate Finance**

**Time-21/2 hours Max Marks-70**

**This paper contains \_3\_printed pages and four parts**

**SECTION A**

**Answer any TEN of the following. Each question carries two marks. (10x2=20)**

1. Mention the important decisions in Financial Management
2. Define optimal capital structure
3. What is Stable dividend policy?
4. What do you understand by unadjusted rate of return in capital budgeting?
5. Define sensitivity analysis.
6. Name the quantitative techniques for incorporating risk in capital budgeting decisions.
7. Mention the assumptions of MM hypothesis.
8. Define pecking order theory
9. State two important external factors which influence the dividend policy of a firm.
10. Differentiate between NI and NOI approach.
11. What do you understand by Mergers and acquisitions?
12. What do you mean by a leveraged buyout?

**SECTION B**

**Answer any THREE of the following. Each question carries five marks. (3x5=15)**

1. X Ltd. is expecting an annual EBIT of Rs. 1 lakh. The company has Rs.4 lakhs in 10% debentures. The equity capitalization rate is 12%. The company decided to raise Rs.1 lakh by issue of 10% debentures and use the proceeds to redeem the equity shares. Calculate the total value of the firm and also the overall cost of capital.
2. A Limited company is considering investing in a project requiring a capital outlay of ₹20,00,000. Forecast for annual income after depreciation but before tax is as follows:

Year 1 2 3 4 5

Amount (₹) 1,00,000 1,00,000 80,000 80,000 40,000

PV factor 0.909 0.826 0.751 0.683 0.621

Depreciation may be taken at 20% of original cost and tax rate at 50% of net income. Evaluate the project according to NPV method taking cost of capital at 10%. The present values of Re.1 @10% through the life of the project are also provided above.

1. ‘A stock split is when a company divides its existing number of shares into multiple shares. For example, a 3-for-1 split would mean a shareholder who owns 1 share in a company will receive 3 shares after the stock split. Companies go in for stock splits to boost the liquidity of their shares and make them more affordable for investors.’ In this context, analyze the implication of stock split on the valuation of a company.
2. XYZ limited is considering a project “A” with an initial outlay of Rs. 14,00,000 and possible three cash inflow attached with the project is as follows:

|  |  |  |  |
| --- | --- | --- | --- |
| Particulars | Year 1 | Year 2 | Year 3 |
| Worst Case | 4,50,000 | 4,00,000 | 7,00,000 |
| Most Likely | 5,50,000 | 4,50,000 | 8,00,000 |
| Best Case | 6,50,000 | 5,00,000 | 9,00,000 |

Assuming the cost of capital at 9%, determine the NPV in each scenario. If XYZ limited is certain about the most likely result but uncertain about the third year’s cash flow, what will be the NPV expecting worst case scenario in the third year.

17. Explain briefly the rationale of corporate restructuring.

**SECTION C**

**Answer any TWO of the following. Each question carries ten marks. (2x10=20)**

1. The following is the data regarding two companies’ ‘X’ and ‘Y’ belonging to the same equivalent risk class:

|  |  |  |
| --- | --- | --- |
| Particulars | Company X | Company Y |
| Number of equity shares | Rs. 90,000 | 1,50,000 |
| Market price per share | Rs. 1.20 | Rs. 1.00 |
| 6% Debentures | Rs. 60,000 | Nil |
| Profit before interest | Rs. 18,000 | Rs. 18,000 |

All profits after paying debenture interest are distributed as dividends. You are required to explain how under Modigliani and Miller approach, an investor holding 10% of shares in company ‘X’ will be better off in switching his holding to company ‘Y’.

1. S Limited has Rs.10,00,000 for capital budgeting purpose. The following projects with their profitability index is available:

|  |  |  |
| --- | --- | --- |
| Projects | Amount (Rs.) | Profitability Index |
| 1 | 3,00,000 | 1.22 |
| 2 | 1,50,000 | 0.95 |
| 3 | 3,50,000 | 1.20 |
| 4 | 4,50,000 | 1.18 |
| 5 | 2,00,000 | 1.20 |
| 6 | 4,00,000 | 1.05 |

Which of the above projects should be undertaken? Assume that projects are indivisible and there is no alternative use of money allocated for capital budgeting. Justify your answer.

1. Proposal X requires an initial capital outlay of Rs. 2,00,000, with no salvage value, and will be depreciated on a straight-line basis for tax purposes. The earnings before depreciation and taxed (EBDT) during its 5 years life are:

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
| Year | 1 | 2 | 3 | 4 | 5 |
| EBDT | 70,000 | 76,000 | 80,000 | 60,000 | 52,000 |

The corporate tax rate is 35% and the company evaluates projects at 12% cost of capital. Advise the company whether the project should be accepted.

1. When there is no inflation and
2. When there is inflation at the rate of 15% p.a. And the stated gross earnings are also expected to grow at this rate of inflation.

**SECTION D**

**Answer the following compulsory question. The question carries fifteen marks. (1x15=15)**

1. Malabar gold is considering to venture into gold mining business at an estimated cost of Rs. 80 crores. As per the prediction the gold reserve of the mine would exhaust in 2 years. There is 60% possibility that the company would get export orders in addition to domestic sales and in this case, company would generate a net revenue of Rs. 60 crores. There is 40% possibility that the revenue of Rs. 40 crores can still be generated without export sales.

In the second year the company may earn following revenue depending on the outcome of demand.

If cash inflows in year 1 are;

|  |  |  |
| --- | --- | --- |
| DemandOutcome | Scenario 1 | Scenario 2 |
| Rs. 60 Cr | Rs. 40 Cr |
| 2nd Yr.Cash inflows (Rs.)  | Prob | 2nd Yr.Cash inflows (Rs.) | Prob |
| 1. Low
 | 40 Cr | 0.4 | 24 Cr | 0.2 |
| 1. Moderate
 | 50 Cr | 0.5 | 32 Cr | 0.3 |
| 1. High
 | 60 Cr | 0.1 | 44 Cr | 0.5 |

Using 10% discount rate, advise about the acceptability of the proposal based on decision tree analysis.

\*\*\*\*\*\*\*\*END OF PAPER\*\*\*\*\*\*\*\*