PG – 957

IV Semester M.B.A. Degree Examination, July 2016
(2007-08 Scheme)
MANAGEMENT
F-5 : Strategic Financial Management

Time : 3 Hours   Max. Marks : 75

***Instruction** : Answer **all** Sections.*

SECTION – A

1. Answer **any six** of the following questions. **Each** question carries **two** marks. **(6×2=12)**
   a) What is golden parachute ?
   b) Distinguish between stock and cash dividend.
   c) What is economic depreciation ?
   d) List the two key elements of EVA bonus plan.
   e) What is spin off ?
   f) Explain the any two steps involved in merger.
   g) What is direct comparison approach ?
   h) Define NOPLAT.

SECTION – B

Answer **any three** of the following questions. **Each** question carries **eight** marks. **(3×8=24)**

2. The income statement for year 0 (the year which has just ended) and the Balance Sheet at the end of year 0 for Futura Limited as follows :

Income Statement		**Balance Sheet**			
Sales	10,000	Equity	6,000	Fixed assets	4,000
Gross margin (20%)	2,000			Current assets	2,000
Selling and General Administration (10%)	1,000				
Profit before tax	1,000				
Tax	300				
Profit after tax	700		**6,000**		**6,000**

P.T.O.

Futura Limited is debating whether it should maintain the *status quo* or adopt a new strategy. If it maintains the *status quo* :

The sales will remain constant at 10,000.

Gross margin will remain at 20% and the selling, general and administrative expenses will be 10% of sales.

- Depreciation charges will be equal to new investments
- The asset turnover ratio will remain constant
- The discount rate will be 15%
- The income tax rate will be 30%

If Futura Limited adopts a new strategy, its sales will grow at a rate of 20% per year for three years. The margin, the turnover ratio, the capital structure, income tax rates and discount rate, however will remain unchanged. Depreciation charges will be equal to 10% of the net fixed assets at the beginning of the year.

What value will the new strategy create ?

3. A new plant entails an investment of Rs. 300 million (Rs. 250 million in fixed assets and Rs. 50 million in net working capital). The plant has Economic life of 14 years and is expected to produce a NOPLAT of Rs. 21.085 million every year. After 14 years, the net working capital will be realised at par where as fixed assets will fetch nothing. The cost of capital for the project is 10%. The straight line method of depreciation will be used.

   a) What will be the ROCE for the year 5 ? Assume that the capital employed is measured at the beginning of the year.

   b) What will be ROGI for the year 5 ?

   c) What will be the economic depreciation for the year 5 ?

   d) What will be CVA for the year 5 ?

4. From the following data calculate the cost of merger :

   i) When merger is financed by cash and

   ii) When merger is financed by stock

Particulars	**Firm A**	**Firm B**
Market price per share (Rs.)	60	15
Number of shares	1,00,000	50,000
Market value of firm (Rs.)	60,00,000	7,50,000

Firm A intends to pay Rs. 10,00,000 cash for B, if B's market price reflects only its value as a separate entity.

5. What are the features or characteristics of EVA which make it as an anchor for an integrated financial management system ? Give the ways of calculating EVA with example.

6. Describe briefly the scope and constituents of strategic financial management.

SECTION – C

Answer **any two** of the following questions. **Each** question carries **twelve** marks. **(12×2=24)**

7. The Profit and Loss Account and Balance Sheet of Hitachi Limited is given for the three years (year 1, year 2, year 3) are given below :

Profit and Loss Account

(Rs. in millions)

	1	**2**	**3**
Net sales	350	400	460
Income from marketable securities	–	10	15
Non-Operating income	–	5	10
Total income	350	415	485
Cost of Goods Sold	200	230	270
Selling and General administration expenses	45	50	55
Depreciation	20	25	30

Interest Expenses	20	24	28
Total cost and expenses	285	329	383
PBT	65	86	102
Tax provision	20	26	32
PAT	45	60	70
Dividend	20	30	40
Retained earnings	25	30	30

Balance Sheet

	1	**2**	**3**
Equity capital	130	150	150
Reserves and surplus	90	120	150
Debt	150	180	210
Total	**370**	**450**	**510**
Fixed Assets	250	300	325
Investments	60	90	100
Net Current Asset	60	60	85
Total	**370**	**450**	**510**

The tax rate for Hitachi Limited is 40%. During year 2 the firm made a rights issue of Rs. 20 millions at par.

a) Calculate the following for the years 2 and 3

i) EBIT

ii) Taxes on EBIT

iii) NOPLAT

iv) Net investments

v) Operating free cash flow

vi) Net operating cash flow

vii) Free cash flow to the firm.

b) Give the breakup of the financing flow for years 2 and 3.

c) Calculate the following key drives of FCF for years 2 and 3

   i) Invested capital

   ii) ROIC

   iii) Growth rate.

8. ABC Ltd. is intending to acquire XYZ Ltd. By merger and the following information is available in respect of the companies :

Particulars	**ABC Ltd.**	**XYZ Ltd.**
Number of equity shares	10,00,000	6,00,000
Earnings after tax (Rs.)	50,00,000	18,00,000
Market value per share (Rs.)	42	28

Required :

   i) What is present EPS of both the companies ?

   ii) If the proposed merger takes place, what would be the earning per share for ABC Ltd. ? Assume that the merger takes place by exchange of equity shares and the exchange ratio is based on the current market price.

   iii) What should be exchange ratio, if XYZ Ltd. Wants to ensure the earnings to members are as before the merger takes place ?

9. What is meaning of corporate restructuring ? Explain the various forms of corporate restructuring.

SECTION – D

Compulsory. **(1×15=15)**

10. Multisoft Ltd. is expected to grow at a higher rate of 4 years; thereafter the growth rate will fall and stabilize at a lower level. The following information has been assembled.

Base yera (year 0) information :	
Revenue	Rs. 3,000 million
EBIT	Rs. 500 million
Capital expenditure	Rs. 350 million
Depreciation	Rs. 250 million
Working capital as a percentage of revenue	25%
Corporate tax rate (for all time)	30%
Paidup Equity capital (Rs. 10 par)	Rs. 400 million
Market value of debt	Rs. 1,200 million
Inputs for the high growth period	
Length of high growth period	4 years
Growth rate in revenue, depreciation, EBIT and capital expenditure	20%
Working capital as a percentage of revenues	25%
Cost of Debt (pre-tax)	13%
Debt-Equity ratio	1 : 1
Risk-free rate	11%
Market risk premium	7%
Equity beta	1.129
Expected growth rate in revenues and EBIT	10%
Capital expenditure are offset by depreciation	–

Working capital as a percentage of revenues	25%
Cost of Debt (pre-tax)	12.14%
Risk-free rate	10%
Market risk premium	6%
Equity beta	1.00
Debt-Equity ratio	2 : 3

Requirements :

i) What is the Weighted Average Cost of Capital (WACC) for the high growth period and the stable growth period ?

ii) What is the value of Multisoft Ltd. ?

Note : Extracted from the table of present value of Re. 1 :

PVIF/Year	**0**	**1**	**2**	**3**	**4**
at 13%	1.000	0.885	0.783	0.693	0.613
at 14%	1.000	0.877	0.769	0.675	0.592
at 15%	1.000	0.870	0.756	0.658	0.572