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**PRESIDENCY UNIVERSITY**

**Bengaluru**

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| **End - Term Examinations – MAY 2025** |
| **Date:** 22-05-2025 **Time:** 01:00 pm – 04:00 pm |

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| **School:** SOC | **Program:** B.COM (ACCA) | |
| **Course Code:** COM1031 | **Course Name:** Financial Management | |
| **Semester**: II | **Max Marks**: 100 | **Weightage**:50% |

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| **CO - Levels** | **CO1** | **CO2** | **CO3** | **CO4** | **CO5** |
| **Marks** | **14** | **70** | **14** | **-** | **2** |

**Instructions:**

1. *Read all questions carefully and answer accordingly.*
2. *Do not write anything on the question paper other than roll number.*

**Part A**

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| **Answer ALL the Questions. Each question carries 2 marks. 10Q x 2M=20M** | | | | |
| **1.** | With increased focus on sustainable finance and stakeholder engagement, Vertex Holdings Ltd. modified its strategic direction by shifting from a short-term profit-centric model to one that emphasizes long-term value creation. Which of the following results best explains the financial benefit of this transition? A) Immediate surge in cash inflows  B) Reduction in stakeholder interference  C) Enhanced long-term shareholder value through ESG integration D) Simplification of investment risk disclosures | **2 Marks** | **L2** | **CO1** |
| **2.** | Sigma Technologies Ltd., a publicly traded company, has been repeatedly criticized by investors for approving capital projects that significantly benefit executive bonuses but add limited value for shareholders. According to agency theory, what does this reflect? A) Sound financial planning with performance pays  B) A conflict between management incentives and shareholder goals C) Effective dividend payout design  D) Involvement of independent boards in credit decisions | **2 Marks** | **L2** | **CO1** |
| **3.** | The finance director at NextWave Instruments advocates the use of Net Present Value (NPV) for evaluating long-term investments, while a senior analyst suggests using Payback Period for quicker results. What is the strongest argument for favoring NPV?  A) NPV is simpler to compute and interpret  B) NPV incorporates time value of money and promotes long-term value creation  C) NPV always leads to higher profitability  D) Payback is not suitable for short-term returns | **2 Marks** | **L2** | **CO2** |
| **4.** | SparTech Ltd. is weighing a shift from the Economic Order Quantity (EOQ) model to a Just-in-Time (JIT) system. While EOQ minimizes order frequency, JIT limits inventory holding. Which of the following best highlights the risk of adopting JIT?  A) Higher warehouse maintenance costs B) Increased dependency on timely supplier delivery C) Excessive storage of obsolete items D) Lower frequency of cash flow updates | **2 Marks** | **L2** | **CO2** |
| **5.** | TrailGear Ltd. provides the following financial data: Current Assets: $950,000 (includes $250,000 in inventory and $150,000 in accounts receivable)  Current Liabilities: $475,000  What is the quick ratio, and how should liquidity be interpreted? A) Quick Ratio = 1.3; High liquidity risk  B) Quick Ratio = 1.0; Low liquidity risk  C) Quick Ratio = 1.47; Low liquidity risk  D) Quick Ratio = 1.2; High liquidity risk | **2 Marks** | **L3** | **CO2** |
| **6.** | A firm commits $115,000 to a capital project yielding the following cash flows: Year 1 = $38,000; Year 2 = $30,000; Year 3 = $26,000; Year 4 = $28,000. What is the payback period for this investment? A) 2.5 years B) 3.1 years C) 3.3 years D) 3.6 years | **2 Marks** | **L3** | **CO2** |
| **7.** | Nova Tools Ltd. anticipates sales of 6,000 units annually. Each order costs $60 to place, and the holding cost per unit per year is $3. What is the EOQ? A) 300 units B) 360 units C) 447 units D) 510 units | **2 Marks** | **L3** | **CO2** |
| **8.** | An investment worth $95,000 has a salvage value of $15,000 at the end of five years. If the average annual accounting profit is $7,000, what is the Return on Capital Employed (ROCE)? A) 8.2% B) 9.3% C) 10.5% D) 11.1% | **2 Marks** | **L3** | **CO2** |
| **9.** | Oceanic Parts Ltd. expects to receive €85,000 in three months. The current spot rate is ₹89/€, and the forward rate is ₹86/€. What is the INR value using the forward rate? A) ₹7,650,000  B) ₹7,310,000 C) ₹7,255,000 D) ₹7,460,000 | **2 Marks** | **L3** | **CO5** |
| **10.** | Vertex Motors Ltd., a company specializing in electric vehicle (EV) manufacturing, is evaluating the financial viability of launching a new SUV model. To assess funding options, the CFO wants to estimate the firm's cost of equity using the Capital Asset Pricing Model (CAPM), which will also help in setting the minimum return expectations for investors.  The financial data available is:   * The risk-free rate (Rf) is 4.5%. * The expected market return (Rm) is 11.5%. * The company’s beta (β), based on industry comparisons, is 1.4.   Based on the CAPM model, what is the cost of equity for Vertex Motors Ltd.?  A) 12.2% B) 14.1% C) 14.6% D) 13.3% | **2 Marks** | **L3** | **CO3** |

**Part B**

**Answer ALL the Questions. Each question carries 10 Marks. Total Marks 50M**

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| 11. |  | NextGen Appliances Ltd. is a growing company that manufactures home appliances such as air conditioners and washing machines. Recently, the management has decided to closely monitor its working capital cycle to improve liquidity and efficiency. The CFO has gathered the following information for the financial year ending March 31, 2025:   * The company holds an average inventory of ₹9,00,000 during the year. * The cost of goods sold (COGS) for the year is ₹45,00,000. * The average accounts receivable balance stands at ₹7,50,000, and the net credit sales total ₹50,00,000. * Average accounts payable amount to ₹6,00,000, while annual purchases on credit are ₹30,00,000. * Assume a 360-day operational year.   The CFO now seeks your assistance in analyzing the company's cash conversion cycle to guide future improvements.  Tasks: (a) Calculate: – Inventory Conversion Period (ICP) – Receivables Collection Period (RCP) – Payables Deferral Period (PDP) (4 Marks)  (b) Compute the Cash Conversion Cycle (CCC) for NextGen Appliances Ltd. (4 Marks)  (c) If the management wants to improve the company's cash flow by shortening the CCC by at least 8 days next year, suggest two practical measures they could implement. (2 Marks) | 10 Marks | L3 | CO2 |

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| 12. |  | Crestline Fabrics Pvt. Ltd., a growing mid-tier textile manufacturer, has been witnessing strong demand and healthy revenue growth. Despite this performance, the company regularly relies on short-term bank overdrafts to meet essential obligations such as employee salaries and vendor payments. A recent evaluation of its working capital management revealed two key issues: sluggish inventory turnover, largely due to excessive production, and a receivables collection period averaging 68 days, significantly above the industry benchmark of 42 days.  To drive sales, Crestline has been extending lenient credit terms to wholesale buyers. Concerned by rising liquidity constraints, the finance department has proposed implementing Just-in-Time (JIT) inventory practices and shortening credit periods. However, the operations manager is worried that this may disrupt customer satisfaction and reduce delivery consistency.  From a financial standpoint, Crestline maintains a current ratio of 1.6, but the quick ratio stands at only 0.75, signalling that most current assets are tied up in inventory and receivables, leaving little liquidity for short-term needs.   1. How is Crestline’s current working capital policy contributing to liquidity stress, despite strong sales? (4 Marks) 2. Discuss the trade-offs between aggressive inventory reduction and customer relationship management. (4 Marks) 3. How can Crestline improve its quick ratio without compromising operational efficiency? (2 Marks) | 10 Marks | L3 | CO2 |

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| 13. |  | Amanah Foods Ltd., a certified halal food manufacturing company, is planning to upgrade its supply chain by acquiring cold storage facilities valued at $160,000. To stay consistent with its Shariah-based financing principles, the company approached an Islamic bank to explore funding options. The bank has proposed two compliant structures:   * Murabaha: The bank would first purchase the equipment and then sell it to Amanah Foods at a pre-agreed markup price. * Ijara: The bank retains ownership of the equipment and leases it to Amanah for a fixed rental over a specified term.   The Chief Financial Officer (CFO) prefers the Murabaha arrangement because it grants the company direct ownership and provides a clear repayment structure. In contrast, the Shariah compliance advisor leans toward Ijara, citing its lower upfront payments and greater financial flexibility during early growth phases. While both modes meet Islamic finance standards, they vary in their implications regarding accounting, risk-sharing, and asset management.   1. Compare Murabaha and Ijara in terms of asset ownership, financial risk, and Shariah compliance. (4 Marks) 2. Which structure is more appropriate for an asset-heavy, growth-focused business, and why? (3 Marks) 3. How do these financing tools avoid riba while still generating returns for the bank? (3 Marks) | 10 Marks | L2 | CO1 |

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| 14. |  | Modern Appliances Co. specializes in high-end kitchen appliances and is looking to optimize inventory levels for their best-selling dishwasher model due to fluctuating demand. The management has provided the following data to help analyse inventory strategy:  Annual Demand (D): 3,000 dishwashers  Cost per Order (S): $75  Annual Holding Cost per Unit (H): $8   1. Calculate the Economic Order Quantity (EOQ) for the dishwashers at Modern Appliances Co. (5 Marks) 2. Determine how many times per year the company needs to reorder based on the EOQ. (2 Marks) 3. Estimate the total inventory cost for the year using the EOQ model. (3 Marks) | 10 Marks | L3 | CO2 |

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| 15. |  | Planta Ltd., a European technology firm, is evaluating its capital cost to make strategic investment decisions. The company has a well-diversified capital structure consisting of equity, debt, and preferred stock. The board has requested the finance team to calculate the Weighted Average Cost of Capital (WACC) to assess future projects.  Financial Information:   |  |  |  | | --- | --- | --- | | Component | Market Value (In millions) | Proportion (%) | | Equity (E) | 90 | 60% | | Debt (D) | 45 | 30% | | Preferred Stock (P) | 15 | 10% | | Total Capital (V) | 150 | 100% |   Additional Data:   * The risk-free rate is 3% per annum. * The expected market return is 9%. * The company’s beta is 1.1. * The before-tax cost of debt is 6%. * The corporate tax rate applicable is 20%. * The cost of preferred stock is 7%.   Calculate:   1. Determine the Cost of Equity for Planta Ltd. (3 Marks) 2. Compute the After-Tax Cost of Debt. (3 Marks) 3. Calculate Planta Weighted Average Cost of Capital (WACC). (4 Marks) | 10 Marks | L3 | CO3 |

**Part C**

**Answer all Questions. Each question carries 15 marks 2Q x 15M=30M**

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| 16. |  | Paisley Co., a wholesaler in the industrial equipment industry, recorded $20 million in annual credit sales last year. At year-end, its accounts receivable balance stood at $4 million, indicating an average collection period of around 73 days. The company finances its receivables using a short-term bank overdraft facility at an interest rate of 12% per annum, which incurs a significant cost on tied-up capital.  To accelerate cash inflows and reduce interest expense, the finance director has proposed introducing an early settlement discount of 2% to encourage faster payments. Under the proposal, customers will receive the 2% discount if they pay their dues within 10 days, rather than the standard 60-day credit period.  The marketing team estimates that 40% of customers are likely to take advantage of the discount, which would reduce the receivables balance and related financing cost. However, the finance manager cautions that the revenue loss from the discount must be weighed against the interest savings from reduced receivables.  1. Should an early settlement discount be introduced if 40% of customers take it up? Justify your answer by comparing the cost of the discount against the savings in financing costs. (10 Marks)  2. Explain the financial advantages and risks of offering early settlement discounts as a receivables management strategy. Under what circumstances might such a policy be inappropriate? (5 Marks) | 15 Marks | L3 | CO2 |

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| 17. |  | Acorn Co., a manufacturing firm, is evaluating the purchase of an automated machine costing $110,400. The machine is expected to improve efficiency and reduce operating labour expenses. It will be used for 4 years, with an estimated residual (salvage) value of $9,600 at the end of Year 4. The company depreciates the asset on a straight-line basis and finances the investment internally.  Forecasted annual operating profits (before depreciation) from the machine are:   |  |  | | --- | --- | | Year | Operating Profit ($) | | 1 | 39,600 | | 2 | 19,600 | | 3 | 22,400 | | 4 | 32,400 |   Acorn Co. wants to assess the investment using the following methods:   1. Payback Period (PP) (4 Marks) 2. Return on Capital Employed (ROCE) based on average investment. (3 Marks) 3. Net Present Value (NPV) – discounting future profits at a cost of capital of 10% and assuming cash flows equal to operating profits. (3 Marks) | 15 Marks | L3 | CO2 |