

MOCK TEST PAPER 1
FINAL 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) ZX Ltd. has made purchases worth USD 80,000 on 1st May 2020 for which it has to make a payment on 1st November 2020. The present exchange rate is INR/USD 75. The company can purchase forward dollars at INR/USD 74. The company will have to make an upfront premium @ 1 per cent of the forward amount purchased. The cost of funds to ZX Ltd. is 10 per cent per annum.

The company can hedge its position with the following expected rate of USD in foreign exchange market on 1st May 2020:

Exchange Rate	Probability
(i) INR/USD 77	0.15
(ii) INR/USD 71	0.25
(iii) INR/USD 79	0.20
(iv) INR/USD 74	0.40

You are required to advise the company for a suitable cover for risk.

(8 Marks)

- (b) An investor has recently purchased substantial number of 7 year 6.75% ₹ 1,000 bond with 5% premium payable on maturity at a required Yield to Maturity (YTM) of 9%. However, due to a financial crunch he is looking to sell these bonds and has got a proposal from another investor, who is willing to purchase these bonds by shelling out a maximum amount of ₹ 897 per bond. Investors follow intrinsic value method for valuation of bonds.

- (i) You are required to determine

- (1) The Market Price, Duration and Volatility of the bond and
- (2) Required YTM of the new investor

- (ii) What is relationship between the price of the bond and YTM?

Period (t)	1	2	3	4	5	6	7
PVIF (9%, t)	0.917	0.842	0.772	0.708	0.650	0.596	0.547

(8 Marks)

- (c) Describe the main features of Value-at-Risk (VAR).

(4 Marks)

2. (a) Herbal Box is a small but profitable producer of beauty cosmetics using the plant, Aloe Vera. Though it is not a high-tech business, yet Herbal's earnings have averaged around ₹ 18.5 lakhs after tax, mainly on the strength of its patented beauty cream to remove the pimples.

The patent has nine years to run, and Herbal Box has been offered ₹ 50 lakhs for the patent rights. Herbal's assets include ₹ 50 lakhs of property, plant, and equipment, and ₹ 25 lakhs of working capital. However, the patent is not shown on the books of Herbal Box. Assuming Herbal's cost of capital being 14 percent, calculate its Economic Value Added (EVA). **(6 Marks)**

- (b) An importer booked a forward contract with his bank on 1st September, for US \$ 5,00,000 due on 1st February @ ₹ 82.60. The bank covered its position in the market @ ₹ 80.90

The exchange rates for dollar in the interbank market on 1st February and 15th February were:

	1 st February	15 th February
Spot USD 1 =	₹ 80.10/18	₹ 80.01/12
Spot/February	₹ 80.35/45	₹ 80.10/30
March	₹ 80.55/65	₹ 80.45/55
April	₹ 80.70/80	₹ 80.65/75
May	₹ 80.85/95	₹ 80.80/90

Exchange margin is 0.18% and interest on outlay of funds is @ 15%. The importer requested on 15th February for the extension of contract with due date on 1st May.

Rates rounded to 2 decimals.

On 1st February, Bank swaps by selling spot and buying one month forward.

Calculate:

- Cancellation rate.
- Amount payable on \$5,00,000.
- Swap loss.
- Interest on outlay of funds, if any.
- New contract rate.
- Total cost.

(Note: Assume 365 days in a Year)

(10 Marks)

- (c) Peer-to-Peer Lending and Crowd funding are same and traditional methods of funding. Do you agree? Justify your stand.

(4 Marks)

OR

Write any four differences between 'Systematic risk' and 'Unsystematic risk'.

(4 Marks)

3. (a) The Balance Sheet of M/s. Sundry Ltd. as on 31-03-2020 is follows:

(₹ in lakhs)

Liabilities	₹	Assets	₹
Share Capital	300	Fixed Assets	600
Reserves	200	Inventory	500
Long Term Loan	400	Receivables	240
Short Term Loan	300	Cash	60
Payables & Provisions	200		
Total	1400	Total	1400

Sales for the year was ₹ 600 lakhs. The sales are expected to grow by 20% during the year. The profit margin and dividend pay-out ratio are expected to be 4% and 50% respectively.

The company further desires that during the current year Sales to Short Term Loan and Payables and Provision should be in the ratio of 4 : 3. Ratio of fixed assets to Long Term Loans should be 1.5. Debt Equity Ratio should not exceed 1.5.

You are required to determine:

- (i) The amount of External Fund Requirement (EFR)
 - (ii) The amount to be raised from Short Term, Long Term and Equity funds. **(8 Marks)**
- (b) Mr. K has invested in three Mutual fund schemes as per details below:

	Scheme A	Scheme B	Scheme C
Date of Investment	01-12-2018	01-01-2019	01-03-2019
Amount of Investment	₹ 5,00,000	₹ 10,00,000	₹ 5,00,000
Net Asset Value at entry date	₹ 10.50	₹ 10.00	₹ 10.00
Dividend received up to 31-03-2019	₹ 9,500	₹ 15,000	₹ 5,000
NAV as at 31-3-2019	₹ 10.40	₹ 10.10	₹ 9.80

You are required to calculate the effective yield on per annum basis in respect of each of the three schemes to Mr. K upto 31-03-2019, taking the year consisting of 365 days.

Provide a brief comment on the course of action he should take for future period.

(Calculation should be upto three decimal places) **(8 Marks)**

- (c) As a financial strategist you will depend on certain key financial decisions. Discuss. **(4 Marks)**
4. (a) A proposed foreign investment involves creation of a plant with an annual output of 1 million units. The entire production will be exported at a selling price of USD 10 per unit. At the current rate of exchange dollar cost of local production equals to USD 6 per unit. Dollar is expected to decline by 10% or 15%. The change in local cost of production and probability from the expected current level will be as follows:

Decline in value of USD (%)	Reduction in local cost of production (USD/unit)	Probability
0	-	0.4
10	0.30	0.4
15	0.15 Additional reduction	0.2

The plant at the current rate of exchange will have a depreciation of USD 1 million annually. Assume local Tax rate as 30%.

You are required to find out:

- (i) Annual Cash Flow After Tax (CFAT) under all the different scenarios of exchange rate.
 - (ii) Expected value of CFAT assuming no repatriation of profits.
 - (iii) Viability of the investment proposal assuming an initial investment of USD 25 million on plant and working capital with a required rate of return of 11% on investment and on the basis of CFAT arrived under option. (ii). The CFAT will grow @ 3% per annum in perpetuity. **(8 Marks)**
- (b) On 1st January, 2020, an open ended scheme of mutual fund had outstanding units of 300 lakhs with a NAV of ₹ 20.25. At the end of January 2020, it had issued 5 lakhs units at an opening NAV plus a load of 2%, adjusted for dividend equalisation. At the end of February 2020, it had repurchased 2.5 lakhs units at an opening NAV less 2% exit load adjusted for dividend equalisation. At the end of March 2020, it had distributed 70 per cent of its available income.

In respect. of January - March quarter, the following additional information is available:

Value appreciation of the portfolio	₹ 460 lakhs
Income for January	₹ 24 lakhs
Income for February	₹ 36 lakhs
Income for March	₹ 47 lakhs

You are required to calculate:

- (i) Income available for distribution
- (ii) Issue price at the end of January
- (iii) Repurchase price at the end of February
- (iv) Closing value of Net Assets at the end of March **(8 Marks)**

- (c) Different participants are required for the success of the securitisation process. Discuss their roles. **(4 Marks)**

5. (a) A company has a choice of investments between several different equity oriented mutual funds. The company has an amount of ₹ 100 lakhs to invest. The details of the mutual funds are as follows:

Mutual Funds	A	B	C	D	E
Beta	1.5	1.0	0.8	2.0	0.7

PLAN I

If the company invests 20% of its investments in each of the first two mutual funds (A and B) and balance in equal amounts in the mutual funds C, D and E, what is the beta of the portfolio?

PLAN II

If the company invests 15% of its investment in C, 15% in A, 10% in E and the balance in equal amounts in the other two mutual funds, what is the beta of the portfolio?

If the expected return of market portfolio is 12% at a beta factor of 1.0, what will be the expected return on the portfolio in both the plans given above? **(8 Marks)**

- (b) IB an Indian firm has its subsidiary in Japan and Zaki a Japanese firm has its subsidiary in India and face the following interest rates:

Company	IB	Zaki
INR floating rate	BPLR + 0.50%	BPLR + 2.50%
JPY (Fixed rate)	2%	2.25%

Zaki wishes to borrow Rupee Loan at a floating rate and IB wishes to borrow JPY at a fixed rate. The amount of loan required by both the firms is same at the current exchange rate. A financial institution may arrange a swap and requires 25 basis points as its commission. Gain, if any, is to be shared by the firms equally.

You are required to find out:

- (i) Whether a swap can be arranged which may be beneficial to both the firms?
- (ii) What rate of interest will the firms end up paying? **(8 Marks)**
- (c) "Securitisation is beneficial from the angle of various parties involved in it". Explain. **(4 Marks)**

6. (a) Long Ltd., is planning to acquire Tall Ltd., with the following data available for both the companies:

	Long Ltd.	Tall Ltd.
Expected EPS	₹ 12	₹ 5
Expected DPS	₹ 10	₹ 3
No. of Shares	30,00,000	18,00,000
Current Market Price of Share	₹ 180	₹ 50

As per an estimate Tall Ltd., is expected to have steady growth of earnings and dividends to the tune of 6% per annum. However, under the new management the growth rate is likely to be enhanced to 8% per annum without additional investment.

You are required to:

- Calculate the net cost of acquisition by Long Ltd., if ₹ 60 is paid for each share of Tall Ltd.
 - If the agreed exchange ratio is one share of Long Ltd., for every three shares of Tall Ltd., in lieu of the cash acquisition as per (i) above, what will be the net cost of acquisition?
 - Calculate Gain from acquisition. **(8 Marks)**
- (b) The price of March Nifty Futures Contract on a particular day was 9170. The minimum trading lot on Nifty Futures is 50. The initial margin is 8% and the maintenance margin is 6%. The index closed at the following levels on next five days:

Day	1	2	3	4	5
Settlement Price (₹)	9380	9520	9100	8960	9140

You are required to calculate:

- Mark to market cash flows and daily closing balances on account of
 - An investor who has taken a long position at 9170
 - An investor who has taken a short position at 9170
 - Net profit/ loss on each of the contracts **(8 Marks)**
- (c) "Investing in Stock Futures differs from investing in Equity Options in several ways". Explain. **(4 Marks)**