

Question Paper

Financial Management - II (MB2E2): January 2009

- Answer all 69 questions.
- Marks are indicated against each question.

Total Marks : 100

1. Consider the following data:

Raw-material storage period	40 days
Average stock of raw materials	Rs.8,50,000
Average balance of trade creditors	Rs.5,00,000

Assume 360 days in a year and all purchases are made on credit.

If the closing stock of raw-materials is 50% higher than the opening stock of raw-materials, the amount of purchases is

- (a) Rs.57,85,000
- (b) Rs.65,25,200
- (c) Rs.67,97,000
- (d) Rs.79,90,000
- (e) Rs.97,90,000.

(2marks)

[<Answer>](#)

2. 'The marketing manager needs to analyze the effect of a change in the exchange rate and evaluate the strategy required to manage the exposure'. Which of the following strategies is **not** available to him?

- (a) Market selection
- (b) Product Sourcing
- (c) Pricing Strategy
- (d) Product strategy
- (e) Promotional strategy.

(1 mark)

[<Answer>](#)

3. Which of the following costs is **not** a cost of maintaining receivables?

- (a) Administrative costs
- (b) Collection costs
- (c) Ordering costs
- (d) Defaulting costs
- (e) Financing costs.

(1 mark)

[<Answer>](#)

4. Anil Enterprises Limited (AEL) has placed two orders to Sunil Enterprises Limited (SEL) in order to purchase lathe machines from them. Each machine is sold at a price of Rs.5,00,000 at a profit margin of 20%. It is estimated that the probability of default is 10% for the first order and 5% for the second order. What is the expected profit to SEL from granting the second credit to AEL, assuming that the first order has been paid?

- (a) Rs.57,500
- (b) Rs.59,500
- (c) Rs.67,500
- (d) Rs.75,600
- (e) Rs.79,600.

(1 mark)

[<Answer>](#)

5. The export-import policy in India is announced by

- (a) Reserve Bank of India
- (b) Ministry of Finance
- (c) Ministry of Commerce
- (d) Central Board of Direct Taxes
- (e) FEDAI.

(1 mark)

[<Answer>](#)

6. Which of the following is **not** an issue considered in the technical appraisal of a project? [<Answer>](#)
- (a) Assembly line balancing
 - (b) Optimality of the scale of operations
 - (c) Structure of competition
 - (d) Availability of the required quality and quantity of raw materials and other inputs
 - (e) Availability of power.
- (1 mark)
7. Which of the following statements is/are **not true** with respect to the situation of overtrading in a company? [<Answer>](#)
- I. The company is undercapitalized.
 - II. Funds are locked up in current assets resulting in a lower turnover of working capital.
 - III. It can be prevented by increasing the asset base through additional finances raised through the issuance of shares.
- (a) Only (I) above
 - (b) Only (II) above
 - (c) Both (I) and (II) above
 - (d) Both (II) and (III) above
 - (e) All (I), (II) and (III) above.
- (1 mark)
8. Which of the following factors does **not** influence the working capital management policies of a firm? [<Answer>](#)
- (a) Excise duties on the capital equipments
 - (b) Sudden increase in the demand for the product of the company
 - (c) Adoption of better technology leading to the reduction in production time
 - (d) Sudden stoppage of the supply of a major raw material
 - (e) Increase in the short-term interest rate.
- (1 mark)
9. Which of the following statements is/are **true** with respect to Short-term bank finance? [<Answer>](#)
- I. Under the cash credit arrangement, the customer is permitted to borrow up to a pre-fixed limit called the cash credit limit.
 - II. Cash credit account operates against security in the form of pledge of shares and other securities.
 - III. Under letter of credit agreement the bank assumes the risk and also provides the credit.
 - IV. Security in the form of hypothecation is limited to movable properties.
- (a) Only (II) above
 - (b) Only (IV) above
 - (c) Both (I) and (IV) above
 - (d) Both (II) and (III) above
 - (e) Both (III) and (IV) above.
- (1 mark)
10. Which of the following statements is/are **true** with respect to Factoring? [<Answer>](#)
- I. Under Invoice factoring sales ledger administration and collection of receivables are carried out by the client.
 - II. Under Recourse factoring credit protection is provided by the factor to the client.
 - III. Under Non-Recourse factoring credit protection is provided by the factor to the client.
 - IV. Factoring is related only to a specific transaction. It is not a continuous agreement between the Factor and the Seller of goods and services.
- (a) Only (I) above
 - (b) Only (II) above
 - (c) Both (I) and (III) above
 - (d) Both (II) and (IV) above
 - (e) Both (III) and (IV) above.
- (1 mark)

11. Which of the following statements is **not true** with respect to costs associated with inventories?

[<Answer>](#)

- (a) Material costs are the costs of purchasing the goods including transportation and handling costs
- (b) Ordering costs remain more or less constant irrespective of the size of the order although transportation and inspection costs may vary to a certain extent depending upon the order size
- (c) The cost of storing goods is known as carrying costs
- (d) Whenever a firm commits its resources to inventory, it is using its funds that otherwise might have been available for other purposes. This is its opportunity cost
- (e) Cost of funds tied up with inventory are costs associated with the inability to provide materials to the production department.

(1 mark)

12. Calculate the Normal consumption during Lead time, from the following data:

[<Answer>](#)

Average Daily Usage Rate (units)	Probability of Occurrence	Lead Time (no. of days)	Probability of Occurrence
400	0.25	12	0.25
1,000	0.50	18	0.50
800	0.25	20	0.25

- (a) 11,360 units
- (b) 13,600 units
- (c) 16,300 units
- (d) 18,360 units
- (e) 18,660 units.

(2marks)

13. Which of the following statements are **true** regarding cost of trade credit?

[<Answer>](#)

- I. Cost of trade credit is the implicit cost associated with not availing cash discount within the stipulated period.
 - II. Smaller the discount rate offered higher will be the cost of trade credit.
 - III. Larger the spread between credit and cash discount periods, the lower will be the cost of trade credit.
 - IV. Cash discount can be availed only when the cost of trade credit is lower than the opportunity cost of cash.
- (a) Both (I) and (III) above
 - (b) Both (II) and (IV) above
 - (c) (I), (II) and (III) above
 - (d) (I), (III) and (IV) above
 - (e) (II), (III) and (IV) above.

(1 mark)

14. Which of the following statements is **not true** with respect to current assets?

[<Answer>](#)

- (a) Cash and bank are most liquid form of current assets, but, they do not generate any return unless they are invested in some other form
- (b) For a company which is in the business of manufacturing various items of machinery, the machines manufactured by the company for the purpose of sale will be included under inventories
- (c) Stock-in-process, indicates partially finished goods which have been valued at the end of the year
- (d) Job contracts which are incomplete at the end of the accounting period and which are to be carried forward to the next accounting period, should be under inventories
- (e) Loans and advances do not include loans to subsidiaries of the company.

(1 mark)

15. Which of the following statements is **not true** with respect to Commercial Papers (CPs)?

[<Answer>](#)

- (a) These are short-term usance promissory notes with a fixed maturity period
- (b) It is also referred to as Corporate Paper
- (c) It is mostly used to finance the current transactions of a company
- (d) It helps to meet the seasonal need for funds
- (e) It cannot be issued by body corporate.

(1 mark)

16. Which of the following statements is **true** with regard to public deposit to a company?

[<Answer>](#)

- (a) The procedure involved in raising public deposit is fairly complex
- (b) A public deposit with maturity period of less than 1 year is also treated as long term liability
- (c) After-tax cost of public deposits will be much less than the after-tax cost of bank borrowing
- (d) Security is offered in the case of public deposit
- (e) Public deposit will have restrictive covenants in respect of dividends payments, and appointment of senior executives.

(1 mark)

17. Consider the following sales and receivable data of a company:

[<Answer>](#)

Sales And Receivables Data

Month	Sales	Receivables	Month	Sales	Receivable
January	350	400	July	650	750
February	450	500	August	720	755
March	650	710	September	780	850
April	750	750	October	800	900
May	550	600	November	780	850
June	500	655	December	820	950

How many days sales are outstanding at the end of third quarter?

- (a) 28 days
- (b) 33 days
- (c) 36 days
- (d) 40 days
- (e) 44 days.

(2marks)

18. Which of the following is a spontaneous source of financing current assets?

[<Answer>](#)

- (a) Accrued wages and salaries
- (b) Commercial paper
- (c) Public Deposits
- (d) Cash credit
- (e) Overdraft.

(1 mark)

19. Investing surplus cash involves two basic problems of determining the amount of cash surplus and determining the channels of investment. Which of the following statements is **not true** with respect to determination of channels of investment?

[<Answer>](#)

- (a) Security can be ensured by investing money in securities whose price remains same forever
- (b) Liquidity can be ensured by investing money in the Long-term securities
- (c) The corporate managers who follow aggressive investment policies maximize the yield on their investment
- (d) Permanent cash surplus consists of funds which are kept by the firm to use in some unforeseen profitable opportunity of expansion or acquisition of some assets
- (e) Permanent cash surplus is available for investment for a period ranging from six months to a year.

(1 mark)

20. Which of the following will cause a decrease in the net operating cycle of a firm?

[<Answer>](#)

- (a) Increase in the average collection period
- (b) Increase in the average payment period
- (c) Increase in the finished goods storage period
- (d) Increase in the raw materials storage period
- (e) Increase in the work-in-progress period.

(1 mark)

21. Which of the following is **not** an item of current liabilities?

[<Answer>](#)

- (a) Sundry creditors
- (b) Advance from customers
- (c) Hire purchase dues
- (d) Unclaimed dividend
- (e) Incomplete work on hand.

(1 mark)

22. Which of the following statements is **not true** with respect to Payback Period?

[<Answer>](#)

- (a) In order to use the payback period as a decision rule for accepting or rejecting the projects, the firm has to decide upon a appropriate cut-off period
- (b) Projects with payback periods less than or equal to the cut-off period will be accepted and others will be rejected
- (c) It is simple in both application and concept
- (d) It helps in weeding out risky projects by favoring only those projects which generate substantial inflows in the later years
- (e) It fails to consider time value of money.

(1 mark)

23. VED analysis is for

[<Answer>](#)

- (a) Monitoring and controlling of stores and spare parts
- (b) Monitoring and controlling of finished goods
- (c) Monitoring and controlling of work in process
- (d) Monitoring and controlling of production process
- (e) Monitoring and controlling of raw materials.

(1 mark)

24. Consider the following:

[<Answer>](#)

The Mumbai market rates are as under:

Spot Rs/€	58.88/91
1 month	12/10
2 months	22/20
3 months	27/25

If a bank requires an exchange margin of 2 paisa, what should be the rate quoted to an Indian importer who wants to have delivery in the second month?

- (a) Rs.56.83
- (b) Rs.57.93
- (c) Rs.58.73
- (d) Rs.59.13
- (e) Rs.59.68.

(2marks)

25. The discount rate used in the APV method to calculate savings due to concessionary loans is

[<Answer>](#)

- (a) Risk free rate of interest in home country
- (b) Competitive borrowing rate in home country
- (c) Risk free rate of interest in host country
- (d) Competitive borrowing rate in host country
- (e) The cost of capital for the parent company.

(1 mark)

26. Avik Century Ltd. is considering to avail the trade discount of 2% offered by one of its suppliers if it orders for minimum 4000 units. The annual usage is 8000 units and the cost per order is Rs.800 which is fixed. The cost of each unit is Rs.100 and the cost of carrying each unit is 20% p.a. of the inventory value. The change in profit, if the company accepts the discount is

[<Answer>](#)

- (a) -Rs. 8,800
- (b) -Rs.12,250
- (c) Rs. 8,800
- (d) Rs.12,250
- (e) Rs.16,250.

(2marks)

[<Answer>](#)

27. Consider the following data of a project:

Year	Cash flows (Rs.)
0	(1,50,000)
1	54,500
2	72,400
3	83,700
4	88,000
5	93,000

If the cost of capital is 15%, the discounted payback period is approximately

- (a) 1.8 years
- (b) 1.11 years
- (c) 2.3 years
- (d) 2.11 years
- (e) 3.8 years.

(2 marks)

[<Answer>](#)

28. Which of the following is **false** regarding the assumption of Black-Scholes model of option pricing?

- (a) The stock prices follow random walk which means that the proportional changes in the stock prices in a short period time are normally distributed
- (b) The risk-free rate is constant and to be a known rate
- (c) Dividend payments are made during the life of the option
- (d) People cannot predict the direction of the market or of an individual stock
- (e) There are no transaction costs and taxes.

(1 mark)

[<Answer>](#)

29. The value of the Special Drawing Rights (SDRs) fluctuates in accordance with value of all the following currencies except

- (a) Swiss Franc
- (b) Yen
- (c) Pound sterling
- (d) Euro
- (e) US Dollar.

(1 mark)

[<Answer>](#)

30. Which of the following statements is **not true** with respect to Ageing Schedule?

- (a) The age-wise distribution of accounts receivable at a given time is depicted in the ageing schedule
- (b) A comparison of ageing schedules at periodic intervals helps to identify changes in the payment behavior of customers
- (c) The ageing schedule can be compared with the credit period extended by the company
- (d) When the percentage of receivables belonging to higher age groups is above a stipulated norm, action has to be initiated before they turn into bad debts
- (e) If sales are decreasing, average collection period and the ageing schedule will not differ from what they would be if sales are constant.

(1 mark)

[<Answer>](#)

31. Which of the following statements is **true** with respect to Economic Order Quantity (EOQ)?

- (a) If inflation is predictable, EOQ formula cannot be modified
- (b) Inflation ratio should be added to the percentage of fixed cost
- (c) Average inventory and EOQ definitely increase during inflationary period
- (d) If inflation is known, it should be added to the annual carrying cost expressed in percentage
- (e) When a firm avails of discount on bulk purchase, then the carrying cost will increase if the EOQ is less than the minimum quantity for purchase.

(1 mark)

[<Answer>](#)

32. The following information pertains to Wahid Ltd.:

Year	Operating Costs (In Rs. Lakh)
0	55.0
1	6.7
2	4.2
3	5.9
4	4.8
5	6.6

The Cost of capital is 14%. The Annual Capital Charge is

- (a) Rs.11.85
- (b) Rs.14.56
- (c) Rs.15.46
- (d) Rs.21.66
- (e) Rs.26.11.

(2marks)

[<Answer>](#)

33. Karthik Automobiles Ltd., has forecast its sales to be as follows:

Month	January	February	March
Sales (Rs.)	10,00,000	12,00,000	14,00,000

All the sales are on cash basis. Purchases amount to 70% of the following month's sales and are paid in the following month of purchase. Wages and administrative expenses per month amount to Rs.1,00,000 and Rs.1,20,000 respectively and are paid in the month in which they are incurred. Depreciation and amortization of preliminary expenses amount to Rs.1,40,000 and Rs.60,000 respectively. If the opening cash balance in January is Rs.1,00,000, the closing cash balance in the month of February is

- (a) – Rs.2,00,000
- (b) – Rs.4,00,000
- (c) Rs.2,50,000
- (d) Rs.3,20,000
- (e) Rs.5,00,000.

(2marks)

[<Answer>](#)

34. Calculate the optimal Hedge Ratio from the following data:

- I. Standard deviation of the change in unit price for the next six months is 0.03.
- II. Standard deviation of the change in futures prices for the next six months is 0.036.
- III. The coefficient of correlation between change in futures prices for the next six months and the change in spot prices for the next six months is 0.72.

- (a) 0.20
- (b) 0.50
- (c) 0.60
- (d) 0.80
- (e) 0.90.

(2marks)

[<Answer>](#)

35. If the current assets and current liabilities are Rs.2,000 lakh and Rs.1,200 lakh respectively, how much amount can be borrowed towards working capital without reducing the current ratio below 1.5?

- (a) Rs.140 lakh
- (b) Rs.240 lakh
- (c) Rs.380 lakh
- (d) Rs.400 lakh
- (e) Rs.440 lakh.

(2marks)

36. Consider the following information pertaining to Archana Ltd.:

[<Answer>](#)

Particulars	Amount (Rs.)
Opening Stock of Finished Goods	40,000
Closing Stock of Finished Goods	70,000
Cost of Production	1,50,000
Selling, Administration and Financial Expenses	1,50,000
Customs and Excise Duties	90,000

The finished goods storage period, assuming 360 days in a year, is

- (a) 33 days
- (b) 48 days
- (c) 55 days
- (d) 63 days
- (e) 68 days.

(2marks)

37. The following information is available regarding a project being under consideration by Don-Bosco Industries Ltd.:

[<Answer>](#)

Initial outlay is Rs. 25 lakh. Operating and cash flows are as below:

Year	Operating costs (in Rs. Lakh)	Operating inflows (in Rs. Lakh)
1	4.70	8.50
2	3.20	10.70
3	4.90	13.60
4	3.80	16.80
5	5.60	12.50

Cost of capital is 14%. The Benefit-Cost Ratio is

- (a) 1.05
- (b) 1.06
- (c) 1.07
- (d) 1.09
- (e) 1.11.

(2marks)

38. The rates available in the Kolkata market are:

[<Answer>](#)

Rs./\$ Spot 45.78/79
£/\$ 0.5285/86

If an Indian importer requires pounds, the rate quoted to him is

- (a) Rs. 86.36/£
- (b) Rs. 86.51/£
- (c) Rs. 86.58/£
- (d) Rs. 86.64/£
- (e) Rs. 86.90/£.

(2marks)

39. Which of the following is **not** a motive for the companies to hold cash?

[<Answer>](#)

- (a) Transaction motive
- (b) Precautionary motive
- (c) Speculative motive
- (d) Lack of proper synchronization between the cash inflows and outflows
- (e) Capital investments.

(1 mark)

40. Which of the following is **not** a production strategy against operating exposure?

[<Answer>](#)

- (a) Input mix
- (b) Product sourcing
- (c) Pricing
- (d) Plant location
- (e) Raising productivity.

(1 mark)

41. Initial margin is also referred to as

[<Answer>](#)

- (a) Vertical margin
- (b) Variation margin
- (c) Performance margin
- (d) Spread margin
- (e) Maintenance margin.

(1 mark)

42. In which of the following swaps, the fixed rate payer has the right to terminate the swap at any time before the maturity?

[<Answer>](#)

- (a) Circus swaps
- (b) Deferred rate swaps
- (c) Callable swaps
- (d) Puttable swaps
- (e) Extendible swaps.

(1 mark)

43. The following table shows the sales estimates of Nova Industries Ltd., for the following months:

[<Answer>](#)

Month	Estimated sales (Rs.)
January	2,00,000
February	2,20,000
March	1,20,000
April	1,00,000
May	1,50,000
June	2,40,000
July	2,00,000
August	2,00,000

20% of sales are on cash basis and the remaining is on credit basis. 50% of the credit sales are collected in the month following the sales, 30% in the second month and 20% in the third month. The cash inflows in the month of August would be

- (a) Rs.1,42,800
- (b) Rs.1,51,200
- (c) Rs.1,60,000
- (d) Rs.1,88,000
- (e) Rs.2,01,600.

(2marks)

44. An Indian firm finds that by investing in a project in East Africa, its borrowing capacity will go up by Rs.70 million. If the firm's borrowing rate in India is 16% and the risk-free rate of interest is 5%, what is the amount of tax shield due to increased borrowing capacity? (Assume that the tax rate applicable is 40% in India and the life of the project is 5 years.)

[<Answer>](#)

- (a) Rs.13.396 million
- (b) Rs.13.996 million
- (c) Rs.16.996 million
- (d) Rs.19.396 million
- (e) Rs.19.996 million.

(2marks)

45. Which of the following statements is **not true** regarding the alternative methods suggested by the Tandon Committee for calculating the maximum permissible bank borrowing?

[<Answer>](#)

- (a) Under Method I, the bank will finance at most 75 percent of the working capital gap
- (b) Under Method II, the bank will finance at most 75 percent of total current assets
- (c) Method I will ensure a minimum current ratio of unity
- (d) Method II will ensure a minimum current ratio of 1.33
- (e) As per Method III, the amount of excess bank borrowing over the maximum permissible limit will be converted into a term loan, which is to be repaid over suitable period.

(1 mark)

46. A company has a total revenue of Rs.787.50 lakh a year, of which 80% are credit sales. The collections receivable occur at an even rate and the total working days of the firm in a year are 300. The cost of funds of the company is 11% p.a. The Accounts Department on an average takes 4 days to deposit the cheques for collection with the bank. If the internal delays are arrested, this could be reduced by 2 days. What is the annual savings of the firm if the delay in depositing cheques is reduced? (Assume that all credit sales payments are received by cheque.) [<Answer>](#)
- (a) Rs.23,100
 (b) Rs.29,800
 (c) Rs.46,200
 (d) Rs.43,100
 (e) Rs.48,890. (2marks)
47. Ganesh Enterprises Ltd., currently has sales of Rs.150 lakh. Its existing credit terms are 1/10, net 45 days and average collection period is 30 days. Forty percent of customers in terms of sales revenue are utilizing the cash discount incentive. The contribution to sales ratio of the company is 20 percent and cost of funds is 15 percent. [<Answer>](#)
- The company is contemplating liberalization of its existing credit terms to 2/10, net 45 days. Sales are expected to increase by Rs.15 lakh and average collection period would come down to 20 days. Eighty percent of customers in terms of sales revenue are expected to avail themselves of the cash discount under the liberalization scheme.
- The net incremental benefit to the company due to the liberalization of its existing credit terms is
- (a) – Rs.0.589 lakh
 (b) – Rs.0.767 lakh
 (c) Rs.1.485 lakh
 (d) Rs.1.857 lakh
 (e) Rs.1.968 lakh. (3marks)
48. Shyam Singh Corporation's budgeted sales for each month of a quarter are Rs.4,50,000. Forty percent of its customers pay in the first month and take 2 percent discount. The remaining sixty percent pay in the month following the sale and don't receive any discount. Purchases for next months' sales are made in cash during the current month and are constant at Rs.1,75,000 every month. Other payments for wages, rent, and taxes are constant at Rs.85,000 per month. The net cash inflows in a month for Shyam Singh Corporation will be [<Answer>](#)
- (a) Rs.2,26,400
 (b) Rs.2,24,600
 (c) Rs.2,23,400
 (d) Rs.1,86,400
 (e) Rs.1,55,300. (2marks)
49. Which of the following statements is **not true**? [<Answer>](#)
- (a) Any kind of trade barrier hampers the efficient allocation of resources and reduces the achievable level of standard of living
 (b) The imposition of tariff generates revenue for the government
 (c) Quotas are enforced by allowing imports only against import licenses, which are issued on a selective basis
 (d) The basis of selection for the grant of import license, is more transparent in case of quota as compared to tariff
 (e) When some foreign producer is found to be dumping some particular good, anti-dumping duty must be levied. (1 mark)
50. The annual cost of production is Rs.12,600 lakh and average conversion period is 3 days. The opening stock of work in process is 10% higher than the closing stock of work in process. Assuming 360 days in a year, the value of closing stock of work in process is [<Answer>](#)
- (a) Rs.100 lakh
 (b) Rs.110 lakh
 (c) Rs.120 lakh
 (d) Rs.125 lakh
 (e) Rs.130 lakh. (2marks)

51. The Rs/HK\$ spot exchange rate is Rs.5.9612/HK\$. If the expected inflation rates in Hong Kong and India for the next year are 3% and 9% respectively, what will be the Rs. /HK\$ spot rate after one year according to PPP theory? [<Answer>](#)

- (a) Rs.4.8712/HK\$
- (b) Rs.4.8865/HK\$
- (c) Rs.5.1122/HK\$
- (d) Rs.5.8712/HK\$
- (e) Rs.6.3084/HK\$.

(2marks)

52. Which of the following statements are **not true** with respect to Currency Board System? [<Answer>](#)

- I. Under this system, a country fixes the rate of its domestic currency in terms of foreign currency.
- II. The board fails to offer a stable exchange rate.
- III. The Board has discretionary powers over the monetary policy and is allowed to print unlimited amount of domestic currency.
- IV. The Board does not lend to even the domestic banks, as it cannot act as a lender of last resort.

- (a) Both (I) and (III) above
- (b) Both (II) and (III) above
- (c) Both (II) and (IV) above
- (d) (I), (II) and (III) above
- (e) (II), (III) and (IV) above.

(1 mark)

53. The current sales of Prakash Electricals Ltd., are Rs.100 lakh, the average collection period is 50 days, the bad debt losses amount to 5 percent of sales and collection expenses are Rs.1 lakh. The variable costs to sales ratio is 70%. The company's cost of funds is 15%. The company is planning to increase its collection effort through special programs to reduce the amount of receivables and the incidence of bad debt losses.

The new collection effort would increase the sales by Rs.10 lakh and would reduce the average collection period to 35 days, decrease the bad debt losses to 3% of sales but involve collection expenses of Rs.2.5 lakh.

The net incremental profit to the company due to new collection effort is approximately

- (a) Rs.2.053 lakh
- (b) Rs.2.545 lakh
- (c) Rs.3.723 lakh
- (d) Rs.3.943 lakh
- (e) Rs.4.165 lakh.

(3marks)

54. Which of the following is/are **true** if a firm uses its short term funds for financing fixed assets? [<Answer>](#)

- I. This will result in serious asset-liability mismatch.
- II. This will improve the liquidity position of the firm.
- III. Since interest on long term borrowing is higher than short term borrowings, it will help reduce the financing cost and thereby increase profitability.
- IV. This will lead to interest rate and liquidity risks.

- (a) Only (I) above
- (b) Only (II) above
- (c) Both (I) and (III) above
- (d) Both (I) and (IV) above
- (e) Both (II) and (III) above.

(1 mark)

55. Which of the following statements is **not true** with respect to Integration of Financial Markets? [<Answer>](#)

- (a) It leads to the development of new financial instruments
- (b) It leads to the liberalization of regulations governing the financial markets
- (c) It increases cross penetration of foreign ownership
- (d) Higher the integration lower will be the transmission effect
- (e) It leads to the development of technology for transfer of money and information.

(1 mark)

56. The Heckscher-Ohlin Model explores the possibility of two nations benefit by trading with each other. Which of the following statements is **not true** with respect to the assumptions of this Model? [<Answer>](#)
- (a) There are no trade controls and transportation costs
 - (b) Both commodity and factor markets are perfectly competitive
 - (c) There are constant or decreasing returns to scale
 - (d) Both the countries have the same technology
 - (e) Labour and capital are perfectly mobile for inter-company transfers. (1 mark)
57. The average conversion period of Neon Ltd. is 5 days and annual cost of production is Rs.20,00,000. The closing stock of work in process is 10% less than opening stock of work in process. The value of opening stock of work in process (360 days in a year) is [<Answer>](#)
- (a) Rs. 9033.66
 - (b) Rs.29239.79
 - (c) Rs.30032.86
 - (d) Rs.32239.70
 - (e) Rs.39162.72. (2marks)
58. Lucky Corp. is a retailer that can finance its purchases with trade credit under the terms, 1/20, net 30 days. Suppliers have also offered to “stretch out” the payments up to 50 days without facing any additional financing costs. A bank has also offered to finance the purchases with a loan at the rate of 15 percent p.a. How many days from the date of purchase would the firm wait to pay its suppliers so that the cost of the trade credit equals the cost of the bank loan? (Assume 360 days in a year) [<Answer>](#)
- (a) 44 days
 - (b) 48 days
 - (c) 55 days
 - (d) 58 days
 - (e) 60 days. (2marks)
59. If the net benefit cost ratio is 0.2, the net present value is Rs.40,000, the present value of the cash inflows associated with the project is [<Answer>](#)
- (a) Rs.1,80,000
 - (b) Rs.2,00,000
 - (c) Rs.2,40,000
 - (d) Rs.2,70,000
 - (e) Rs.3,00,000. (2marks)
60. For a manufacturing firm, the estimated annual usage of material is 3600 units and the cost per order is Rs.225. The carrying cost is Rs.200 per unit and the safety level stock is 10% of the EOQ. If the estimated daily usage is 15 units and the lead time is 8 days, what is the reorder point for the material? [<Answer>](#)
- (a) 109 units
 - (b) 116 units
 - (c) 129 units
 - (d) 135 units
 - (e) 149 units. (2marks)
61. Which of the following is not an item of Capital Account in the Balance of Payment statement? [<Answer>](#)
- (a) Rupee Debt Service
 - (b) Invisibles
 - (c) Banking capital
 - (d) NRI deposits
 - (e) Loans. (1 mark)
62. Which of the following is **not** a credit policy variable for a firm? [<Answer>](#)
- (a) Credit standards
 - (b) Credit evaluation
 - (c) Credit period
 - (d) Cash discount
 - (e) Collection program. (1 mark)

63. The current price of the stock of XYZ Ltd. is Rs.50 and it is expected that the stock price after one year will increase or decrease by 20%. If its exercise price is Rs.50 and the risk-free rate of return is 10%, the value of the call option on the stock is

[<Answer>](#)

- (a) 6.82
- (b) 6.96
- (c) 8.62
- (d) 8.82
- (e) 8.96.

(2marks)

64. What was the reserve currency under Bretton Woods system?

[<Answer>](#)

- (a) Sterling
- (b) Dollar
- (c) Special Drawing Rights (SDRs)
- (d) Gold
- (e) Deutschmark.

(1 mark)

65. A reputed manufacturing company plans to manufacture 24,000 sets of washing machines for the next year. The cost components are as follows:

[<Answer>](#)

Item	Unit Cost (Rs.)
Raw Material	7,000
Manufacturing Expenses	5,000
Selling, administrative and financial expenses	3,000

The selling price per unit is Rs.20,000 and sales may be assumed to be uniform throughout the year. The manufacturing expenses are expected to be incurred evenly throughout the month. The durations at various stages of the operating cycle are given below:

Raw material stage	1.5 months
Work in process stage	1 month
Finished goods stage	1 month
Debtors stage	2 months

If the minimum cash balance required is Rs.50,00,000, what is the estimate for the working capital requirement of the company?

- (a) Rs.1,450 lakh
- (b) Rs.1,500 lakh
- (c) Rs.1,550 lakh
- (d) Rs.1,600 lakh
- (e) Rs.1,620 lakh.

(3marks)

66. Dumping means

[<Answer>](#)

- (a) Destroying the goods to create scarcity
- (b) Throwing the goods in the sea to create scarcity
- (c) Donating the goods to least developed countries as charity
- (d) Selling the goods at actual cost
- (e) Selling the goods below the cost.

(1 mark)

67. Playing the float indicates

[<Answer>](#)

- (a) Issuing cheques without balance in the account
- (b) Purchasing machinery and dishonoring the instrument after the delivery of the machinery
- (c) Converting a credit customer into a cash customer
- (d) Expediting the implementation of a project to the firm's convenience before sanction of the loan
- (e) Manipulating the books of account.

(1 mark)

68. Which of the following elements of internal audit represents the professional aspects of the job?

[<Answer>](#)

- (a) Totality
- (b) Expertise
- (c) Independence
- (d) Objectivity
- (e) Utility.

(1 mark)

69. Given below are the cash flows pertaining to a project:

[<Answer>](#)

Year	Amount (Rs.)
0	-11,00,000
1	6,00,000
2	2,00,000
3	1,00,000
4	5,00,000

The IRR from the project approximately is

- (a) 10.25%
- (b) 10.55%
- (c) 11.25%
- (d) 12.25%
- (e) 12.75%.

(2marks)

END OF QUESTION PAPER

Suggested Answers

Financial Management - II (MB2E2): January 2009

Answer	Reason	
1.	<p>D Let opening stock = x Closing stock = 1.50 x</p> $\frac{x + 1.50x}{2} = 8,50,000$ <p>Then $\frac{x + 1.50x}{2} = 8,50,000$ Therefore opening stock = Rs.680,000 Closing stock = 1.50x = Rs.10,20,000</p> <p style="text-align: center;"><u>Average stock of Raw Material</u> Raw material storage period = $\frac{\text{Stock Consumed}}{\text{Average stock of Raw Material}}$</p> $\text{Or, } 40 = \frac{8,50,000}{\text{Stock Consumed}}$ $\text{Or, Stock Consumed} = \frac{8,50,000}{40}$ $= \text{Rs.21,250}$ <p>Purchases = Stock Consumed + Closing stock – Opening stock = (21,250*360) + 10,20,000 – 6,80,000 = Rs.79,90,000.</p>	≤
2.	<p>B Product Sourcing is done by the Production Manager, and not by the Marketing Manager. Hence, (b) is the answer.</p> <p>The following strategies available to Marketing Manager are</p> <ul style="list-style-type: none"> • Market selection <ul style="list-style-type: none"> • Pricing Strategy • Product strategy • Promotional strategy. 	≤
3.	<p>C Ordering costs are associated with maintaining inventories and not maintaining receivables. Hence (c) is the answer.</p>	≤
4.	<p>C The expected profit from granting the second credit to AEL, assuming the payment for the first order has been made by AEL, is</p> $0.90\{0.95*100000-0.05*400000\} = \text{Rs.67,500.}$	≤
5.	<p>C The Export-Import policy is announced by Ministry of Commerce.</p>	≤

13. A Cost of trade credit is the implicit cost associated with not availing cash discount within the stipulated period. Larger the spread between credit and cash discount periods, the lower will be the cost of trade credit. Statements (I) and (III) are correct option. Hence, (a) is the answer. ≤

Smaller the discount rate offered, lower will be the cost of trade credit. Cash discount can be availed only when the cost of trade credit exceeds the opportunity cost of cash. Hence, statement (II) and (IV) are false statements.

14. E Loans and advances include loans to subsidiaries of the company. ≤

Hence (e) is the answer.

15. E Commercial Papers can be issued by body corporate. Hence, (e) is the answer. ≤

16. C After-tax cost of public deposits will be much less than the after-tax cost of bank borrowing. Hence, option (c) is the answer. ≤

The procedure involved in raising public deposit is fairly simple. Hence, this is a false statement. No Security is offered in the case of public deposit. It does not have restrictive covenants in respect of dividends payments, and appointment of senior executives.

As public deposits with maturity periods of two and three years cannot be regarded as current liabilities, the calculation of ‘working capital gap’ by the bankers to provide short term finance is likely to be favorable from the company’s point of view. Hence, options (a), (b), (d) and (e) are false.

17. C Days sales Outstanding=Accounts receivable at the end of the quarter ÷ Average daily sales ≤

Quarter	Average Collection Period
First	$\frac{710}{(350 + 450 + 650) / 90} = 44 \text{ days}$
Second	$\frac{655}{(750 + 550 + 500) / 91} = 33 \text{ days}$
Third	$\frac{850}{(650 + 720 + 780) / 92} = 36 \text{ days}$
Fourth	$\frac{950}{(800 + 780 + 820) / 92} = 36 \text{ days}$

18. A Spontaneous liabilities generally occur during the normal course of business operations where a company will usually have a ready access to certain sources for financing its current assets. But a company is required to take proper initiative for the sources of finance as mentioned in the options (b), (c), (d) and (e) to finance its current assets. ≤

19. B Liquidity can be ensured by investing money in the short-term securities. Hence, statement (b) is a false statement. ≤
20. B Increase in the average collection period, increase in the finished goods storage period, increase in the raw materials storage period and increase in the work-in process period all result in increasing the operating cycle of the firm. Only increase in the average payment period decreases the net operating cycle of the firm. Hence option (b) is correct. ≤
21. E Current liabilities are economic obligations of a company to be paid within accounting period. Incomplete work on hand is not a current liability. Hence, (e) is the answer. ≤
22. D Payback Period helps in weeding out risky projects by favoring only those projects which generate substantial inflows in earlier years. Hence, option (d) is the answer. ≤
23. A VED analysis is for monitoring and controlling of stores and spare parts by classifying them into 3 categories viz., vital, essential and desirable. Hence, option (a) is the answer. ≤
24. C The rate quoted to the Indian importer is as follows: ≤
- | | |
|-------------------------|--------------|
| | 2 month |
| Spot rate | 58.91 |
| Deduct Swap for 1 month | <u>0.20</u> |
| Add exchange margin | <u>0.02</u> |
| | <u>58.73</u> |
25. D As the nominal foreign currency interest rate would have had to be paid in absence of the concessionary loan, that rate should be used as the discount rate for calculating the present value of the repayment of concessionary loan. ≤
Hence, (d) is the answer.

26. A Given the annual usage =8000units
 fixed cost per order =Rs.800
 Purchase price =Rs.100/unit
 Carrying cost as a percentage of inventory value=20%

$$EOQ = \sqrt{\frac{2 * 8000 * 800}{0.20 * 100}} = 800 \text{ units}$$

Change in the profit if the company accepts trade discount of 2% for the purchase of 4000 units

$$\Delta\pi = UD + \left[\frac{U}{Q'} - \frac{U}{Q} \right] * F - \left[\frac{Q'(P-D)C}{2} - \frac{Q'PC}{2} \right]$$

Where,

$\Delta\pi$ = Change in profit

U = annual usage

D = discount per unit when quantity discount is available

Q' = minimum order size required for quantity discount

F = fixed cost of placing an order

P = unit purchase price without discount

C = inventory carrying cost expressed as a percentage

$$\Delta\pi = 8000 * 2 + \left[\frac{8000}{800} - \frac{8000}{4000} \right] * 800 - \left[\frac{4000(100-2) * 0.20}{2} - \frac{800 * 100 * 0.20}{2} \right]$$

= -Rs.8,800.

27. D Calculation of discounted payback period:

Year	Cash flows Rs.	PVIF@15%	Present value Cash flows
1	54,500	0.870	47,415
2	72,400	0.756	54,734
3	83,700	0.658	55,075
4	88,000	0.572	50,336
5	93,000	0.497	46,221

Sum of first two years is= 47,415+54734= 102,149

1,50,000 – 102,149= 47,851

$$\frac{47,851}{55,075} \times 12 = 10.426 \approx 11 \text{ months.}$$

Discounted payback period is 2 years 11 months = 2.11 years.

28. C Assumptions of Black and Scholes model are:

- Returns are log normally distributed
- The risk-free rate is constant and to be a known rate
- The stock pays no dividends during the option's life
- The markets are efficient
- There are no transaction costs and taxes.

Hence (c) is the correct answer.

29. A The value of SDR is determined is a weighted average value of 4 currencies-US Dollar, Yen, Pound, Sterling, Euro. Therefore, the fluctuation in the SDRs is not caused by Swiss Franc.

30. E If sales are decreasing, average collection period and the ageing schedule will differ from what they would be if sales are constant. Hence (e) is a false statement. ≤

31. D EOQ does not take inflation into consideration. However, when the inflation is predictable accurately then the EOQ formula can be modified. If inflation rate is known, it should be added to the annual carrying cost expressed as a percentage. When the minimum order quantity for purchases is more than the economic order quantity, then there will be an increase in the average value of inventory which will result in higher incidence of carrying cost. ≤

32. D Annual Capital Charge ≤

	Operating Costs (In Rs. Lakh)	PV@14%	PV
0	55	1.000	55
1	6.70	0.877	5.88
2	4.20	0.769	3.23
3	5.90	0.675	3.98
4	4.80	0.592	2.84
5	6.60	0.519	3.43
			74.36

$$\text{Annual Capital Charge} = \frac{74.36}{\text{PVIFA}_{(14\%, 5 \text{ years})}}$$

$$\text{Annual Capital Charge} = \frac{74.36}{3.4331} = 21.66$$

33. D ≤

	(Rs.)	
	January	February
Opening balance	1,00,000	1,80,000
+ Receipts from sales	10,00,000	12,00,000
	11,00,000	13,80,000
- Wages and administration	2,20,000	2,20,000
- Purchases paid	7,00,000	8,40,000
Closing cash balance	1,80,000	3,20,000

Closing cash balance at the end of February is Rs.3,20,000.

Hence (d) is the answer.

34. C Optimal Hedge Ratio = [(standard deviation of change in spot price)/(standard deviation of change in future price)]×[correlation coefficient] = (.03/0.036)*(0.72)=0.60. ≤

35. D Current Ratio = Current Assets/ Current Liabilities = (2,000 + X)/ (1,200+X) = 1.5 X = Rs.400 lakh. ≤

36. C ≤
- $$\text{Finished goods storage period} = \frac{\text{Average stock of finished goods}}{\text{Average daily cost of sales}}$$
- Average stock of finished goods =
- $$\frac{\text{Opening stock of finished goods} + \text{Closing stock of finished goods}}{2}$$
- $$= \frac{40,000 + 70,000}{2} = 55,000$$
- Annual cost of sales = Opening stock of finished goods + Cost of production + Excise duty + Selling and distribution costs + General administrative costs + Financial costs – Closing stock of finished goods
- $$\text{Annual cost of sales} = \text{Rs.}(40,000 + 1,50,000 + 90,000 + 1,50,000 - 70,000)$$
- $$= \text{Rs.}3,60,000$$
- $$\text{Average daily cost of sales} = \frac{\text{Annual cost of sales}}{360}$$
- $$= \text{Rs.} \frac{3,60,000}{360}$$
- $$= \text{Rs.}1,000$$
- Hence, finished goods storage period is
- $$\frac{55,000}{1,000}$$
- $$= 55 \text{ days.}$$
37. A ≤
- Calculation of BCR is shown below:
- $$\text{PV} = \frac{3.8}{1.14} + \frac{7.5}{1.14^2} + \frac{8.7}{1.14^3} + \frac{13}{1.14^4} + \frac{6.9}{1.14^5}$$
- $$= 3.333 + 5.771 + 5.872 + 7.697 + 3.584$$
- $$= \text{Rs. } 26.257 \text{ lakh}$$
- $$\text{BCR} = 26.257 \div 25 = 1.05.$$
38. D ≤
- The rate to be quoted to the Importer is the ask rate
- $$= (\text{Rs./\$}) \text{ ask} \times (\$/\text{£}) \text{ ask}$$
- $$= (\text{Rs./\$}) \text{ ask} \times (1/\text{£}/\$) \text{ bid}$$
- $$= 45.79 \times (1/0.5285) = \text{Rs.}86.64/\text{£}.$$
39. E ≤
- Capital investment is a long-term objective and not a motive for companies to hold cash.

40. C Pricing is a marketing strategy. Hence (c) is the correct answer.

Production strategies:

- Input mix
- Product sourcing
- Plant location
- Raising productivity.

Marketing strategies:

- Market selection
- Pricing strategy
- Promotional strategy
- Product strategy.

41. C The initial margin is also known as the performance margin as it is kept with the exchange till the completion of all the obligations of the contract are fulfilled or as long as the investor to trade in the market.

42. C A callable swap gives the holder, i.e. the fixed rate payer, the right to terminate the swap at any time before its maturity. Should the interest rates fall, the fixed rate payer exercises his right and terminates the swap since the funds will be available at a lower rate now.
Hence (c) is the correct answer.

43. E

Particulars	March	April	May	June	July	August
Sales	1,20,000	1,00,000	1,50,000	2,40,000	2,00,000	2,00,000
Cash sales	24,000	20,000	30,000	48,000	40,000	40,000
Credit sales	96,000	80,000	1,20,000	1,92,000	1,60,000	1,60,000
Collection from the debtors:						
50 % in the following month	88,000	48,000	40,000	60,000	96,000	80,000
30% in the second month	48,000	52,800	28,800	24,000	36,000	57,600
20% in the third month	–	32,000	35,200	19,200	16,000	24,000
Cash inflows	1,60,000	1,52,800	1,34,200	1,51,200	1,88,000	2,01,600

Therefore total collection from the debtors in the month of August is Rs.2,01,600. Hence (e) is the answer.

44. D Interest on increased borrowing capacity = $0.16 \times 70 = \text{Rs.}11.20\text{million}$
Tax shield generated per year = $0.40 \times 11.20 \text{ million} = \text{Rs.}4.48\text{million}$
Present Value of the tax shields due to the increased borrowing capacity = $\text{Rs.}4.48\text{PVIFA}_{(5\%,5)}$
= Rs.19.396 million.

45. B According to Tandon Committee recommendations, ≤
- Under Method I, the bank will finance atmost 75 percent of the working capital gap. This method will ensure a minimum current ratio of unity.
 - Under Method II, the borrower will finance atmost 25 percent of total current assets through long-term sources. This method will ensure a current ratio of 1.33.
 - Under Method III, the amount of excess borrowing, which is calculated as the difference between the amount of bank borrowing and the maximum permissible bank borrowing to which the borrower is eligible will be converted into a term loan, which is to be repaid over suitable period. This will ensure further reduction in the current ratio.

46. C The total annual credit sales = Rs.787,50,000×0.8 = Rs.630,00,000 ≤
 Number of working days = 300
 Credit sales per day=630,00,000/300 = Rs.2,10,000
 Annual interest on Rs.2,10,000*2* @11% = Rs.46,200.

47. C The effect of the change in the existing credit policy can be estimated from the following formula: ≤

$$\Delta P = \Delta S(1 - V) + k\Delta I - \Delta DIS$$

Where

$$\Delta S = \text{Increase in sales} = \text{Rs.15 lakh}$$

$$V = \text{Variable cost to sales ratio} = 1 - \text{contribution/Sales} = 0.8$$

$$k = \text{cost of funds} = 15\%$$

$$\Delta I = \text{Savings in receivables} = \frac{S_0}{360} (ACP_O - ACP_N) - V \frac{\Delta S}{360} ACP_N$$

$$\Delta DIS = p_n (S_0 + \Delta S)d_n - p_0 S_0 d_0$$

Where

$$p_n = \text{proportion of discount sales after liberalizing} = 0.8$$

$$S_0 = \text{sales before liberalizing} = \text{Rs.150 lakh}$$

$$\Delta S = \text{Increase in sales} = \text{Rs.15 lakh}$$

$$d_n = \text{new discount percentage} = 0.02$$

$$p_0 = \text{proportion of discount sales after liberalizing} = 0.4$$

$$d_0 = \text{old discount percentage} = 0.01$$

$$\Delta DIS = p_n (S_0 + \Delta S)d_n - p_0 S_0 d_0 = 0.8 (150 + 15) 0.02 - 0.4 \times 150 \times 0.01 = \text{Rs.2.04 lakh}$$

$$\Delta I = \frac{S_0}{360} (ACP_O - ACP_N) - V \frac{\Delta S}{360} ACP_N$$

$$= \frac{150}{360} (30 - 20) - 0.8 \times \frac{15}{360} \times 20 = \text{Rs.3.5 lakh.}$$

$$\Delta P = \Delta S(1 - V) + k\Delta I - \Delta DIS = 15 (1 - 0.8) + 0.15 \times 3.5 - 2.04 = \text{Rs.1.485 lakh.}$$

There is net incremental profit of Rs.1.485 lakh on account of liberalizing the credit policy.
 Hence (c) is the answer.

48. D (in Rs.) ≤
- | | | | |
|----------------------------------|---|---------------------|----------------------------|
| Annual budgeted sales | = | <u>Rs.4,50,000</u> | |
| Collections (same month's sales) | = | 1,76,400 | (0.98 × 0.40 × Rs.450,000) |
| Collections (last month's sales) | = | <u>2,70,000</u> | (1.00 × 0.60 × Rs.450,000) |
| Total collections | = | <u>4,46,400</u> | |
| Purchases payments | = | 1,75,000 | |
| Other payments | = | <u>85,000</u> | |
| Total payments | = | <u>2,60,000</u> | |
| Net cash gain (loss) | = | <u>Rs. 186,400.</u> | |
49. D The basis of selection for the grant of import license, is more transparent in case of tariff as compared to quota. Hence, (d) is the answer. ≤
50. A ≤
- $$\text{Average conversion period} = \frac{\text{Average stock of WIP}}{\text{Average daily cost of production}}$$
- $$\text{Average stock of WIP} = \frac{\text{Opening WIP} + \text{Closing WIP}}{2}$$
- Substituting the given values, we get
- $$\text{Average stock of WIP} = \frac{1.10x + x}{2} = 1.05x$$
- Substituting the values in the formula, we get
- $$\text{Average daily cost of production} = \text{Rs.}12,600/360 = \text{Rs.} 35 \text{ lakh}$$
- $$3 = \frac{1.05x}{35} \Rightarrow x = 100 \text{ lakh}$$
- ∴ Closing stock of work in process = Rs.100 lakh.
51. E ≤
- $$= 5.9612 \times \frac{1.09}{1.03}$$
- $$= \text{Rs.}6.3084/\text{HK\$}.$$
52. B ≤
- The board offers a stable exchange rate. The Board does not have discretionary powers over the monetary policy and is not allowed to print unlimited amount of domestic currency. Hence, statements (II) and (III) are not true.
- Under this system, a country fixes the rate of its domestic currency in terms of foreign currency. The Board does not lend to even the domestic banks, as it cannot act as a lender of last resort. Hence, statements (I) and (IV) are true.

53. C The effect of the new collection programs on the profit can be estimated from the following formula: ≤
- $$\Delta P = \Delta S(1 - V) - k\Delta I - \Delta BD - \Delta C$$
- ΔP = Change in profits
 ΔS = Increase in sales
 V = Variable cost to sales ratio
 k = cost of funds
- $$\Delta I = \text{Savings in receivables} = \frac{S_0}{360} (ACP_O - ACP_N) - V \frac{\Delta S}{360} ACP_N$$
- $$= \frac{100}{360} (50 - 35) - 0.7 \times \frac{10}{360} \times 35 = \text{Rs.}3.486 \text{ lakh}$$
- $$\Delta BD = \text{increase in bad debts cost} = b_n (S_0 + \Delta S) - b_0 S_0 = 0.03 (100 + 10) - 0.05 \times 100$$
- $$= -\text{Rs.}1.7 \text{ lakh}$$
- $$\Delta C = \text{increase in collection expenses} = 2.5 - 1 = 1.5 \text{ lakh.}$$
- $$\Delta P = 10 \times 0.3 + 0.15 \times 3.486 - (-1.7) - 1.5 = \text{Rs.}3.7229 \text{ lakh} \approx \text{Rs.}3.723 \text{ lakh. Therefore (c) is the answer.}$$
54. D If a firm uses its short term funds for financing fixed assets this will result in serious asset-liability mismatch (I) An asset –liability mismatch will lead to interest rate risk thereby enhancing the interest burden of the firm and liquidity risk with the short term funds being held up in long term projects (IV). ≤
55. D Higher the integration higher will be the transmission effect. Hence, statement (d) is a false statement. ≤
56. E The assumptions of Heckscher-Ohlin Model , which explores the possibility of two nations benefit by trading with each other ,are ≤
- There are no trade controls and transportation costs
 - Both commodity and factor markets are perfectly competitive
 - There are constant or decreasing returns to scale
 - Both the countries have the same technology
 - Labor and capital are perfectly immobile for inter- company transfers.
- Hence (e) is the answer.

57. B ≤
- Average stock of WIP
- Average conversion period = $\frac{\text{Average stock of WIP}}{\text{Average daily cost of production}}$
- Average stock of WIP = $\frac{\text{Opening WIP} + \text{Closing WIP}}{2}$
- Substituting the given values, we get
- Average stock of WIP = $\frac{1x + 0.9x}{2} = 0.95x$
- Substituting the values in the formula, we get
- Average daily cost of production = Rs.20,00,000/360 = Rs. 5555.56
- $5 = \frac{0.95x}{5555.56} \Rightarrow x = 29239.79$
- ∴ Opening stock of work in process = Rs.29239.79.
58. A ≤
- Interest rate on bank loan = 15%
- N = Number of days the firm can delay the payment from the date of purchase
- Since cost of trade credit should be equal to the cost of bank loan,
- $$= \frac{\text{Rate of discount}}{1 - \text{Rate of discount}} \times \frac{360}{(\text{Credit period} - \text{Discount period})}$$
- $$= \frac{0.01}{1 - 0.01} \times \frac{360}{N - 20} = 0.15$$
- By simplification N = 44.242 ≈ 44 days.
59. C ≤
- NPV
- Net benefit cost ratio (NBCR) = $\frac{\text{Initial investment}}{\text{NPV}}$
- Therefore initial investment = $\frac{\text{NPV}}{\text{NBCR}} = \frac{40,000}{0.2} = \text{Rs.}2,00,000$
- NPV = PV of cash inflows – Initial investment
- PV of cash inflows = NPV + Initial investment = 40,000 + 2,00,000 = Rs.2,40,000.
- Hence (c) is the answer.
60. C ≤
- Reorder point = lead time * average usage + safety stock
- Lead time = 8 days
- Average usage = 15 units/day
- Safety stock = 10% of EOQ
- Reorder point = 8*15+10% EOQ
- $$\text{EOQ} = \sqrt{\frac{2 * 225 * 3600}{200}}$$
- = 90 units
- Safety stock = 10% of EOQ = 9 units
- Reorder point = 8*15+9 =129 units.
61. B ≤
- Invisibles is not an item of Capital account in the BoP statement. Hence, (b) is the answer.

62. B Credit evaluation is not a variable of credit policy for a firm. Hence,(b) is the answer. <

63. A Here, $C_u=10$
 $C_d= 0$
 Stock price = Rs.50
 $R=1+0.10 = 1.10$

$$\text{Probability of price increase} = \frac{R-d}{u-d} = \frac{1.10-0.8}{1.2-0.8} = 0.3/0.4 = 0.75$$

$$\text{Probability of the price decrease} = 1-p = 0.25$$

$$\text{Value of the call option} = \frac{C_u p - C_d (1-p)}{R}$$

$$= \frac{10 * 0.75 - 0}{1.10} = 6.82$$

64. B Dollar was the reserve currency under Bretton Woods system. <

65. C (in Rs. Lakh) <

Input	Period (months)	Raw materials	Work in Process	Finished Goods	Debtors	Total
Raw Material						
In raw material	1.5	210				
In W I P	1		140			
In finished Goods	1			140		
In debtors	2				280	770
Manufacturing Expenses						
In WIP	1/2		50			
In finished goods	1			100		
In debtors	2				200	350
Selling, Administrative and financial expenses						
In finished goods	1			60		
In debtors	2				120	180
Profit						
In debtors	2				200	200
Total		210	190	300	800	1500

Hence, the amount of working capital requirement is Rs1500 lakh + Rs.50 lakh = Rs.1,550 lakh.

66. E Dumping means selling the goods below the cost. <

67. A When a company has a positive float it may issue cheques to the extent that the amount shown in the bank books is higher than the amount shown in the company's books, even if the company's books indicate an overdrawn position. The company is then said to have been playing float. ≤

68. B The elements of the internal audit represent the basic procedures that will simplify the completion of internal audit. ≤
Expertise represents the professional aspects of a job. Hence (b) is the answer.

69. C IRR is that rate of return at which the NPV (PV of Cash inflows – PV of cash outflows) is zero. ≤

Therefore,

$$\frac{6,00,000}{(1+r)} + \frac{2,00,000}{(1+r)^2} + \frac{1,00,000}{(1+r)^3} + \frac{5,00,000}{(1+r)^4} - 11,00,000$$

'r' is the IRR and can be found out by trial and error and interpolation.

By trial and error,

When r = 11%, RHS = 11,05,349.65

When r = 12%, RHS = 10,84,090.00

k lies between 11% and 12%.

$$\text{By interpolation, } k = 11\% + \frac{11,05,349.65 - 11,00,000}{11,05,349.65 - 10,84,090} = 11\% + 0.25\% = 11.25\%.$$

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