**BIYANI INSTITUTE OF SCIENCE AND MANAGEMENT**

**MBA II Sem**

**MODEL ANSWER PAPER-2018**

**FINANCIAL MANAGEMENT**

**“SECTION A”**

1. **What is financial Management? Explain its Importance in the Modern era.**

**Ans.**

Financial Management means planning, organizing, directing and controlling the financial activities such as procurement and utilization of funds of the enterprise. It means applying general management principles to financial resources of the enterprise.

**Scope/Elements**

1. Investment decisions includes investment in fixed assets (called as capital budgeting). Investment in current assets are also a part of investment decisions called as working capital decisions.
2. Financial decisions - They relate to the raising of finance from various resources which will depend upon decision on type of source, period of financing, cost of financing and the returns thereby.
3. Dividend decision - The finance manager has to take decision with regards to the net profit distribution. Net profits are generally divided into two:
   1. Dividend for shareholders- Dividend and the rate of it has to be decided.
   2. Retained profits- Amount of retained profits has to be finalized which will depend upon expansion and diversification plans of the enterprise.

**IMPORTANCE / SIGNIFICANCE OF FINANCIAL MANAGEMENT**

* Economic growth and development: through investing decision, financing decision, dividend decision, and risk management decision, better and more economically viable projects are undertaken by companies. The resultant effect on the economy is economic growth and development. Financial management serve as a [good guide to online investing](https://hubpages.com/money/ONLINE-INVESTMENT-BASIC-REQUIREMENTS-FOR-INVESTING-ONLINE).
* Improved standard of living: growth and development in the economy that is brought about by financial management will ultimately translate into improved standard of living for all.
* Improved health: again, good economic condition and improved standard of living culminates into improved health as a lot of ‘[**financial stress**](http://www.chinweike-okwuduche.com/fighting-stress-through-financial-independence/)’ related sicknesses will be completely eliminated or reasonably reduced.
* Allows for better financial decision
* Creates jobs – those that teach financial management and the jobs that are created as a result of flourishing economy. Better financial decisions will lead to profitability, and profitability will eventually lead to expansion which will in turn mean more jobs.
* Alleviation of poverty
* Preserve our environment
* Promotes efficiency: good financial management does not give room for wastes and inefficiencies that characterizes poor financial management and decision making.

**Q2. Write a detail note on the following:**

* 1. **Venture capital:**

Start up companies with a potential to grow need a certain amount of investment. Wealthy investors like to invest their capital in such businesses with a long-term growth perspective. This capital is known as venture capital and the investors are called venture capitalists.

Such investments are risky as they are illiquid, but are capable of giving impressive returns if invested in the right venture. The returns to the venture capitalists depend upon the growth of the company. Venture capitalists have the power to influence major decisions of the companies they are investing in as it is their money at stake.

## Features of Venture Capital investments

* High Risk
* Lack of Liquidity
* Long term horizon
* Equity participation and capital gains
* Venture capital investments are made in innovative projects
* Suppliers of venture capital participate in the management of the company

## Methods of Venture capital financing

* Equity
* participating debentures
* conditional loan
  1. **Hire Purchase**

Hire purchase is a method of financing of the fixed asset to be purchased on future date. Under this method of financing, the purchase price is paid in installments. Ownership of the asset is transferred after the payment of the last installment.

#### Features of Hire Purchase:

**The main features of hire purchase finance are:**

1.The hire purchaser becomes the owner of the asset after paying the last installment.

2. Every installment is treated as hire charge for using the asset.

3. Hire purchaser can use the asset right after making the agreement with the hire vendor.

4. The hire vendor has the right to repossess the asset in case of difficulties in obtaining the payment of installment.

#### Advantages of Hire Purchase:

i Financing of an asset through hire purchase is very easy.

ii. Hire purchaser becomes the owner of the asset in future.

iii. Hire purchaser gets the benefit of depreciation on asset hired by him/her.

iv. Hire purchasers also enjoy the tax benefit on the interest payable by them.

**Q3.** Suppose you deposit $1,000 in an account pays simple interest. What will be the future value of the account if:

* 1. The annual simple interest rate is 7% for the first 5 years, 10% for the next 10 years, and 12% for the last 5 years?
  2. 5% for the first 10 years, 10% for the next 10 years, 15% for the last 10 years?

**Ans.**

1. P = $1,000, k1 = 7%, n1 = 5

k2 = 10%, n2 = 10

k3 = 12%, n3 = 5

FV = $1,000(1 + .07 × 5 + .10 × 10 + .12 × 5) = $1,000(2.95) = $2,950.

(b) FV = $1,000(1 + .05 × 10 + .10 × 10 + .15 × 10) = $1,000(4) = $4,000.

Q4. Calculate the ‘pay back period’, average rate of return’ and ‘net present value’ for a project which requires an initial outlay of Rs. 10,000 and generates year ending cash flows (after tax but before depreciation) of Rs.6,000; Rs.3,000; Rs 2,000; Rs 5,000; and Rs. 5,000 from the end of the first year to the end of fifth year. The required rate of return is 10 percent and pays tax at 50 percent rate. The project has a life of five years and depreciated on straight line basis.

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
| Year | 1 | 2 | 3 | 4 | 5 |
| Discount rate at 10% | .909 | .826 | .751 | .683 | .620 |

**Ans 4.**

***Pay-back Period Method***

Pay- back Period = 2 + = 2.5 years

**(ii) *Average Rate of Return Method***

ARR =

= x100

= Rs. 2,200/ Rs. 5,000 x 100 = 44%

Average Annual Cash Inflows = = = Rs. 4,200

**(iii) *Net Present Value Method***

|  |  |  |  |
| --- | --- | --- | --- |
| Year | Cash Inflows | P.V factor at 10% | Present |
| 1  2  3  4  5 | Rs.  6,000  3,000  2,000  5,000  5,000 | .909  .826  .751  .683  .621 | Rs.  3,000  20,000  17,000  55,000  17,000 |
| Total Present Value | 15,954 |

Net present Value = Present Value – Initial Investment

= Rs. 15,954 – Rs. 10,000

= Rs. 5,954

**“Section B”**

Q.1 Case study

You have been appointed as a finance manager of a firm in the IT sector. Your job responsibility includes among others, financing and investment decision –making subject to approval by the M.D. You have been advised by your M.D to gain some experience on the basis of published data of a good company in the IT sector, you have been provided with the following figures of the balance sheet of Rajasthan computer services ltd. for the financial year 2016-2017.

|  |  |  |  |
| --- | --- | --- | --- |
| Assets | Amt (in crores) | Liabilities | Amt (in crores |
| In shares of other companies | 201.15 | Equity capital | 133.44 |
| Loans and advances | 261.75 | Secured loans | 13.79 |
| Cash and bank bal | 3959.82 | creditors | 444.56 |
|  |  | Advances from customers | 87.52 |

Your M.D wants to know the investment and financing pattern of the company. classify the items into long –term and short investments and financing.

**Solution:**

|  |  |  |
| --- | --- | --- |
| Investment: |  |  |
| Long term: in share of other companies |  | 201.15 |
| Short term: |  |  |
| Loans and advance | 261.75 |  |
| Cash and Bank Bal | 3959.82 | **4221.57** |
|  |  | **4422.72** |
| Financing: |  |  |
| Short term |  |  |
| Sundry creditors | 444.56 |  |
| Advances | 87.52 |  |
|  |  | **532.08** |
| Long-term: |  |  |
| Secured loans | 13.79 |  |
| Equity | 133.44 | **147.23** |
|  |  | 679.31 |