**MASTER OF BUSINESS ADMINISTRATION (MBA)**

**DMBA202 &amp; FINANCIAL MANAGEMENT**

**Assignment Set – 1**

**1. a) “A rational human being has time preference for money” Give reasons.**

**Ans:** The time preference for money is generally expressed by an interest rate which remains positive even in the absence of any risk. It is called the riskfree rate.

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**b) Differentiate between compounding and discounting technique of time value of money.**

**Ans:**

|  |  |  |
| --- | --- | --- |
| **BASIS FOR COMPARISON** | **COMPOUNDING** | **DISCOUNTING** |

**2. Cost of various types of capital of Radha Ltd. is given below along with weight and cost of capital.**

|  |  |  |  |
| --- | --- | --- | --- |
| **Sources of Funds** | **Amount (Rs.)** | **Proportion (W) in total capital structure** | **Cost of Capital (k)** |
| **Debts** | **240000** | **30%** | **5.68** |
| **Preference share capital** | **80000** | **10%** | **9.33** |
| **Equity Share capital** | **400000** | **50%** | **13.30** |
| **Cost of retained earnings** | **80000** | **10%** | **13.00** |

**Compute weighted average cost of Capital as per:**

**1. Book value proportion.**

**2. What would be WACC in your opinion if company wants to change WACC approach from book value to market value? In market value the price of Equity share is Rs.250 per share instead of Rs.100 in book value.**

**Answer:**

**3. Write short notes on (any two)**

**1. NI approach of Capital structure**

**Ans:** Net Income **(NI)** approach is suggested by Durand. He is of the view that capital structure decision is relevant to the valuation of the firm. Any change in the financial leverage will have a corresponding change in the overall cost of capital and also the total value of the firm. As the ratio of

**3. Modigliani and Miller approach of Capital structure**

**Answer:**

Miller and Modigliani criticise traditional approach that the cost of equity remains unaffected by leverage up to a reasonable limit and K0 remains constant at all degrees of leverage. They state that the relationship between leverage and cost of capital is elucidated as in NOI approach. Table depicts the

**Q. No Assignment Set – 2**

**4. a. Elucidate the factors leading to Capital rationing.**

**Ans:** The various factors related to the internal constraints imposed by the management are: Private owned company

**b. Explain in brief the phases of operating cycle.**

**Ans:**

**5. “Efficient cash Management will aim at maximising the cash inflows and slowing cash outflows.” Discuss Identify the motives for holding cash by an organization.**

**Ans:** The main motives behind holding cash are:

* Transaction motive
* Precautionary motive
* Speculative motive
* Compensating motive

These are

**6. Solve and suggest which of the two projects should be accepted assuming a discount rate of 10% based on net present value of the two projects.**

|  |  |  |
| --- | --- | --- |
| **Detail** | **Project X** | **Project Y** |
| **Initial Investment** | **Rs.20000** | **Rs.30000** |
| **Estimated Life** | **5 Years** | **5 Years** |
| **Scrap Value** | **Rs.1000** | **Rs.2000** |

**The net cash flows are as follows:**

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
|  | **Year 1** | **Year 2** | **Year 3** | **Year 4** | **Year 5** |
| **Project X** | **5000** | **10000** | **10000** | **3000** | **2000** |
| **Project Y** | **20000** | **10000** | **5000** | **3000** | **2000** |

**The Discounted rate of return@10% is as follows:**

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
|  | **Year 1** | **Year 2** | **Year 3** | **Year 4** | **Year 5** |
| **PV@10%**  **Discount factor** | **0.909** | **0.826** | **0.751** | **0.683** | **0.621** |

**Answer:**