

Mock Test Paper - Series I: March, 2026

Date of Paper: 18th March, 2026

Time of Paper: 2 P.M. to 5 P.M.

FINAL COURSE: GROUP – I

PAPER – 2: ADVANCED FINANCIAL MANAGEMENT

Time Allowed – 3 Hours

Maximum Marks – 100

1. The question paper comprises two parts, Part I and Part II.
2. Part I comprises Case Scenario based Multiple Choice Questions (MCQs)
3. Part II comprises questions which require descriptive type answers.

PART I – Case Scenario based MCQs (30 Marks)

Part I is compulsory.

Case Scenario I

P Ltd. is studying the possible acquisition of Q Ltd. which is also in same industry by way of merger. The following data are available:

Firm	After-tax earnings	No. of equity shares	Market price per share	Book Value Per share
P Ltd.	₹ 10,00,000	2,00,000	₹ 75	₹ 210
Q Ltd.	₹ 3,00,000	50,000	₹ 60	₹ 105

Board of Directors of both the companies are in the process of negotiating the terms of proposed merger. In case if P Ltd. considers to buyout Q Ltd. by paying in cash, then it shall borrow the required funds @ 15% rate of interest per annum.

Both companies are in the tax bracket of 35%.

1. In case P Ltd. wants to be sure that its EPS is not diminished by the merger, the relevant exchange ratio to achieve the same objective should be.....
 - (a) 0.33
 - (b) 1.20
 - (c) 1.30
 - (d) 1.10

2. The type of Merger of P Ltd. & Q Ltd. shall be
- (a) Horizontal Merger
 - (b) Vertical Merger
 - (c) Congeneric Merger
 - (d) Reverse Merger
3. Suppose if P Ltd. is exchanging its share on one-to-one basis for Q Ltd. and post-merger there is no change in PE Ratio of any of the company then post-merger market capitalization shall be
- (a) ₹ 125.00 Lakh
 - (b) ₹ 130.00 Lakh
 - (c) ₹ 187.50 Lakh
 - (d) ₹ 195.00 Lakh
4. Suppose if P Ltd. is offering about ₹ 35 Lakh to Q Ltd. for the proposed acquisition it will result in.....
- (a) EPS accretion
 - (b) EPS dilution
 - (c) No Change
 - (d) Risk free EPS
5. Suppose instead of a friendly takeover, P Ltd. attempts a hostile takeover of Q Ltd. To defend itself, Q Ltd. offers substantial compensation to its managers in the event they are removed due to the takeover. This defensive tactic adopted by Q Ltd. is called.....
- (a) Crown Jewels
 - (b) Poison Pill
 - (c) White Knight
 - (d) Golden Parachutes
- (5 x 2 = 10 Marks)**

Case Scenario II

Mr. A is interested in investing ₹ 10,00,000 for which he is considering following three alternatives:

- (i) Invest ₹ 10,00,000 in Mutual Fund X (MFX)

- (ii) Invest ₹ 10,00,000 in Mutual Fund Y (MFY)
- (iii) Portfolio - Invest ₹ 6,00,000 in Mutual Fund X (MFX) and ₹ 4,00,000 in Mutual Fund Y (MFY)

Average annual return earned by MFX and MFY is 12% and 11% respectively. Risk free rate of return is 8% and market rate of return is 10%.

Covariance of returns of MFX, MFY and market portfolio Mix are as follow:

	MFX	MFY	Mix
MFX	4.400	4.300	3.370
MFY	4.300	4.200	2.800
Mix	3.370	2.800	4.200

Based on the above information answer the following questions:

6. Standard Deviation of Market Mix Portfolio is
 - (a) 2.0736
 - (b) 2.0976
 - (c) 1.8358
 - (d) 2.0494
7. Beta of MFY will be approximately.....
 - (a) 1.024
 - (b) 1.048
 - (c) 1.065
 - (d) 0.667
8. Based on CAPM, MFX is:
 - (a) Overvalued
 - (b) Undervalued
 - (c) Correctly valued
 - (d) Risk free
9. If Mr. A invests only in MFY, the risk premium earned would be:
 - (a) 2%

- (b) 3%
 - (c) 1.33%
 - (d) 4%
10. The portfolio beta (60% in MFX and 40% in MFY) would be approximately:
- (a) 0.748
 - (b) 0.802
 - (c) 0.900
 - (d) 0.667
- (5 x 2 = 10 Marks)**

Case Scenario III

X and Y are two friends. Since Y has earned a lot of profit from trading in financial derivative market, X is also considering speculating on Gamma Corporation's shares which is currently trading at ₹ 700 per share through taking positions in options in stocks of same company. Accordingly, X took following contract positions in the options on Gama Corporation's stock:

- (i) Purchasing one contract of 2-month call option with a premium of ₹ 35 and an exercise price of ₹ 750.
- (ii) Purchasing one contract of 2-month put option with a premium of ₹ 25 and an exercise price of ₹ 600.

After some time, trading in Option Market and understanding the nitty-gritties of same, X being CEO in an organization advised his team to implement the concept of Financial Options in the Capital Budgeting decisions called 'Real Option'.

Note: Contract size of each option contract is 100.

Based on the above information answer the following questions:

11. If the share price after two months rises to ₹ 800, the net pay-off to X will be.....
- (a) ₹ 1,500 profit
 - (b) ₹ 1,000 profit
 - (c) ₹ 1,000 loss
 - (d) ₹ 1,500 loss
12. If the share price remains between ₹ 600 and ₹ 750 at maturity, X will.....
- (a) Earn profit
 - (b) Incur loss equal to total premium

- (c) Break even
 - (d) Earn unlimited profit
13. The upper break-even price for X's strategy will be.....
- (a) ₹ 785
 - (b) ₹ 810
 - (c) ₹ 760
 - (d) ₹ 775
14. In Real Options, the "option to abandon" is similar to.....
- (a) Call option
 - (b) Put option
 - (c) Forward contract
 - (d) Swap
15. Real options add value to a project primarily because they.....
- (a) Reduce accounting profits
 - (b) Ignore uncertainty
 - (c) Capture managerial flexibility
 - (d) Eliminate business risk
- (5 x 2 = 10 Marks)**

PART – II DESCRIPTIVE QUESTIONS

Question No.1 is compulsory. Candidates are required to answer any four questions from the remaining five questions.

Working notes should form part of the answers.

Maximum Marks – 70 Marks

1. (a) KLM Ltd., is considering taking up one of the two projects-Project-A and Project-B. Both the projects having same life require equal investment of ₹ 8.00 crore each. Both are estimated to have almost the same yield. As the company is new to this type of business, the cash flow arising from the projects cannot be estimated with certainty. An attempt was therefore, made to use probability to analyse the pattern of cash flow from other projects during the first year of operations. This pattern is likely to continue during the life of these projects. The results of the analysis are as follows:

Project A		Project B	
Cash Flow (in ₹ Crore)	Probability	Cash Flow (in ₹ Crore)	Probability
1.10	0.10	0.90	0.10
1.30	0.20	1.30	0.25
1.50	0.40	1.70	0.30
1.70	0.20	2.10	0.25
1.90	0.10	2.50	0.10

Advise which of the two projects is riskier? **(6 Marks)**

- (b) In International Monetary Market an international forward bid for December 15 on pound sterling is \$ 1.2816 at the same time that the price of IMM sterling future for delivery on December 15 is \$ 1.2806. The contract size of pound sterling is £ 62,500. Suggest how could the dealer use arbitrage in profit from this situation and how much profit is earned? **(4 Marks)**
- (c) State the difference between Peer-to-peer lending and Crowdfunding? **(4 Marks)**
2. (a) EFD Ltd. is an export business house. The company prepares invoice in customers' currency. Its debtors of US\$. 10,000,000 is due on April 1, 2025.

Market information as at January 1, 2025 is:

Exchange rates US\$/INR		Currency Futures US\$/INR	
Spot	0.011765	Contract size:	₹ 35,66,334
1-month forward	0.011627	1-month	0.011617
3-months forward	0.011227	3-month	0.011216
	Initial Margin	Interest rates in India	
1-Month	₹ 1,750	6.5%	
3-Months	₹ 2,250	7%	

On April 1, 2025, the spot rate US\$/INR is 0.011234 and currency future rate is 0.011232.

Which of the following methods would be most advantageous to EFD Ltd?

- (i) Using forward contract
- (ii) Using currency futures
- (iii) Not hedging the currency risk **(10 Marks)**
- (b) Financial Risk can be evaluated from different points of views. Explain. **(4 Marks)**

3. (a) Following Financial data are available for PQR Ltd. for the year 2018:

	(₹ in lakh)
8% debentures	1250
10% bonds (2017)	500
Equity shares (₹ 100 each)	1000
Reserves and Surplus	3000
Total Assets	6000
Assets Turnovers ratio	1.1
Effective interest rate	8%
Effective tax rate	40%
Operating margin	10%
Dividend pay-out ratio	16.67%
Current market Price of Share	₹ 140
Required rate of return of investors	15%

You are required to:

- (i) Draw income statement for the year
- (ii) Calculate its sustainable growth rate of earnings
- (iii) Calculate the fair price of the Company's share using dividend discount model, and
- (iv) What is your opinion on investment in the company's share at current price? **(10 Marks)**
- (b) Critically evaluate the various types of risks inherent in a Securitization transaction. **(4 Marks)**
4. (a) Eagle Ltd. reported a profit of ₹ 770 lakhs after 30% tax for the financial year 2021-22. An analysis of the accounts revealed that the income included extraordinary items of ₹ 80 lakhs and an extraordinary loss of ₹ 100 lakhs. The existing operations, except for the extraordinary items, are expected to continue in the future. In addition, the results of the launch of a new product are expected to be as follows:

	₹ In lakhs
Sales	700
Material costs	200

Labour costs	120
Fixed costs	100

You are required to suggest the value of the business, given that the capitalization rate is 14%. **(6 Marks)**

- (b) State the challenges to the Efficient Market Theory. **(4 Marks)**

Either

- (c) State the key decisions falling within the scope of financial strategy.

Or

Critically examine the concept of Credit Default Swaps (CDSs). Analyze their structural features and evaluate the key purposes for which CDS instruments are used in modern financial markets. **(4 Marks)**

5. (a) A multinational company is planning to set up a subsidiary company in India (where hitherto it was exporting) in view of growing demand for its product and competition from other MNCs. The initial project cost (consisting of Plant and Machinery including installation) is estimated to be US\$ 500 million. The net working capital requirements are estimated at US\$ 50 million. The company follows straight line method of depreciation. Presently, the company is exporting two million units every year at a unit price of US\$ 80, its variable cost per unit being US\$ 40.

The Chief Financial Officer has estimated the following operating cost and other data in respect of proposed project:

- (i) Variable operating cost will be US \$ 20 per unit of production.
- (ii) Additional cash fixed cost will be US \$ 30 million p.a. and project's share of allocated fixed cost will be US \$ 3 million p.a. based on principle of ability to share.
- (iii) Production capacity of the proposed project in India will be 5 million units.
- (iv) Expected useful life of the proposed plant is five years with no salvage value.
- (v) Existing working capital investment for production & sale of two million units through exports was US \$ 15 million.
- (vi) Export of the product in the coming year will decrease to 1.5 million units in case the company does not open subsidiary company in India, in view

of the presence of competing MNCs that are in the process of setting up their subsidiaries in India.

- (vii) Applicable Corporate Income Tax rate is 35%, and
- (viii) Required rate of return for such project is 12%.

Assuming that there will be no variation in the exchange rate of two currencies and all profits will be repatriated, as there will be no withholding tax, estimate Net Present Value (NPV) of the proposed project in India.

Present Value Interest Factors (PVIF) @ 12% for five years are as below:

Year	1	2	3	4	5
PVIF	0.8929	0.7972	0.7118	0.6355	0.5674

(10 Marks)

- (b) Advise Mr. S a speculator the net position to be taken on the Index Future that will give a complete hedge against the following transactions:
 - (i) He has a long position in the share on the cash market of ₹ 50 lakhs on the R Limited. The beta of the R Limited is 1.25 and it is expected that the prices its shares is going to rise.
 - (ii) He has a short position on the cash market of ₹ 25 lakhs on the W Limited. The beta of the W Limited is 0.90 and it is expected that the prices its shares is going to depreciate.

(4 Marks)

- 6. (a) Mr. A will need ₹ 1 Crore after two years for which he wants to make one-time necessary investment now. He has a choice of two types of bonds. Their details are as below:

	Bond X	Bond Y
Face value	₹ 1,00,000	₹ 1,00,000
Coupon	7% payable annually	8% payable annually
Years to maturity	1	4

Advice Mr. A whether he should invest all his money in one type of bond or he should buy both the bonds and, if so, in which quantity?

- Note: 1.** Assume that there will not be any call risk or default risk and both Bonds are trading at yield of 10%.
- 2.** All calculations should be rounded off to three decimal places. However, the number of bonds should be rounded off to the nearest whole number, without any fractional value.

(8 Marks)

(b) Suppose a dealer quotes 'All-in-cost' for a generic swap at 8% against six month SOFR flat. If the notional principal amount of swap is \$ 5 Million.

- (i) Calculate semi-annual fixed payment.
- (ii) Find the first floating rate payment for (i) above if the six-month period from the effective date of swap to the settlement date comprises 181 days and that the corresponding SOFR was 6% on the effective date of swap.

In (ii) above, if the settlement is on 'Net' basis, how much the fixed rate payer would pay to the floating rate payer?

- Note:**
- 1. Generic swap is based on 30/360 days basis.
 - 2. All calculations should be rounded off to three decimal places. However, the final amounts should be rounded off to the nearest whole number, without any fractional value. **(6 Marks)**