



CATestSeries.org (Since 2015)

CA Final | CA Inter | CA IPCC | CA Foundation Online Test Series

| Question Paper | |
|-----------------------------------------|---------------------|
| ADVANCED FINANCIAL MANAGEMENT | Duration: 70 |
| Details: Test 3 (Ch-5, 9 and 15) | Marks: 40 |

Instructions:

- All the questions are compulsory
- Properly mention test number and page number on your answer sheet, Try to upload sheets in arranged manner.
- In case of multiple choice questions, mention option number only Working notes are compulsory wherever required in support of your solution
- Do not copy any solution from any material. Attempt as much as you know to fairly judge your performance.

Legal: Material provided by catestseries.org is subject to copyright. No part of this publication may be reproduced, distributed, or transmitted in any form or by any means, including photocopying, recording, or other electronic or mechanical methods, without the prior written permission of the publisher. For permission requests, write to the publisher, addressed "Attention: Permissions Coordinator," at exam@catestseries.org. If any person caught of copyright infringement, strong legal action will be taken. For more details check legal terms on the website: catestseries.org

Q-1

Mr. X, is a Senior Portfolio Manager at ABC Asset Management Company. He expects to purchase a portfolio of shares in 90 days. However, he is worried about the expected price increase in shares in coming day and to hedge against this potential price increase he decides to take a position on a 90-day forward contract on the Index. The index is currently trading at 2290. Assuming that the continuously compounded dividend yield on the same index is 1.75% and risk-free rate of interest is 4.16%, you are required to determine:

- (a) The justified forward price on this contract.
- (b) The position Mr. X should take in forward contract on the Index.
- (c) Gain/ loss on the position taken if after 28 days of the purchase of the contract the Index value stands at 2450.
- (d) Gain/ loss on the position taken if at expiration of 90 days the Index Value is 2470.

Note: Take 365 days in a year and value of $e^{0.005942} = 1.005960$, $e^{0.001849} = 1.001851$.

(6 Marks)

Q-2

Share of Beta Ltd. is being quoted at a Price-Earning ratio of 10 times. In the coming year the company is expected to retain Rs. 10 per share which is 45% of its Earning Per Share.

You are required to evaluate: (i) The cost of equity to the company if the market expects a growth rate of 10% p.a.

(ii) If the anticipated growth rate is 12% per annum, calculate the indicative market price with the same cost of capital.

(5 Marks)

Q-3

"A Limited Partnership Entity, in India, is not recognized for the purpose of Venture Capital Fund." Do you agree? Briefly explain the structure of Venture Capital Fund in India.

(6 Marks)

Q-4 The Bank PK enters into a Repo for 9 days with Bank JJ in 6% Government Bonds 2022 for an amount of Rs. 20 crore. The other relevant details are as follows:

| | |
|----------------------------------------|------------------|
| First Leg Payment (Start Proceed) | Rs. 20,00,67,500 |
| Second Leg Payment (Repayment Proceed) | Rs. 20,03,17,590 |
| Initial Margin | 1.25% |
| Days of accrued interest | 240 |

Assume 360 days in a year.

Calculate:

- (a) Repo Rate
- (b) Dirty Price and
- (c) Clean Price

(7 Marks)

Q-5

Mr. H is holding 100 equity shares of V Ltd. which is being quoted at Rs. 2,100 per share. He is interested in hedging downside risk of his holding as he is going to sell them after 2 months. A 2-month Call option is available at a premium of Rs. 60 per share and a 2-month

put option is available at a premium of Rs. 50 per share. The strike price in both cases is Rs. 2,200. You are required to: (i) Suggest the position Mr. H should take in the option market to hedge his holding in the V Ltd.

(ii) Calculate his final position if after 2 months i.e., on the day of exercise the actual market price of per share of V Ltd. happens to be Rs. 2000, Rs. 2100, Rs. 2200, Rs. 2300 and Rs. 2400.

(6 Marks)

Q-6

NIYA Healthcare is a proprietary concern engaged in the manufacture and development of Pharmaceutical products since last five years. To scale up the business operations and increase the present turnover which is hovering around 500 Million, the proprietor decides to convert his existing business into a Private Limited Company. He also wants to get access to various tax benefits, easier compliances under the startup India initiative and get recognized as a startup company.

Advise whether NIYA Healthcare can be recognized as a startup company in view of the criteria considered eligible for the startup recognition initiated by the Government of India?

(5 Marks)

MCQs:-

1. In December 2011, the share of AB Co. was trading at Rs. 146. The company is expected to pay a dividend of Rs. 3.36 per share, with a long-term dividend growth rate of 7.5% per annum. AB Co. earns 10% on book equity and retains 60% of its earnings. An investor wishes to calculate the expected rate of return and examine how it would change if the growth rate adjusts based on the retention ratio and return on equity.

Based on the Dividend Discount Model (DDM), what will be the new expected rate of return (K_e) if AB Co. retains 60% of its earnings and earns 10% on book equity?

- A) 9.80%
- B) 9.75%
- C) 9.68%
- D) 10.00%

2. Anand Ltd.'s share is currently trading at Rs. 1,800. The 6-month futures price for the same share is Rs. 1,950. The risk-free borrowing rate in the market is 12% per annum. An investor is exploring whether an arbitrage opportunity exists.

What is the theoretical minimum futures price, and what arbitrage profit can an investor earn if any?

- A) Rs. 1,908; Profit Rs. 42
- B) Rs. 1,950; Profit Rs. 0
- C) Rs. 1,890; Profit Rs. 60
- D) Rs. 1,930; Profit Rs. 20

3. XYZ Ltd. is planning to expand its operations and raise funds for different stages of the project. The company requires funding in different phases, from seed money to going public. Based on the stages outlined, XYZ Ltd. needs to assess the risk perception and activities to be financed.

At which stage does the company face "Extreme" risk, as per the risk matrix, and what is the primary activity financed at this stage?

- A) Seed Money - For supporting a concept or idea or R&D for product development

B) Start-Up - Initializing prototypes operations or developing products and marketing

C) First Stage - Started commercial production and marketing

D) Fourth Stage - Facilitating public issue i.e., going public

4. ABC Power Corporation is a large electricity generating company that operates in multiple states. They have recently entered into a 3-year Power Purchase Agreement (PPA) with XYZ Distribution Company, where they have agreed to supply a fixed amount of electricity at a pre-determined price. However, ABC Power Corporation is concerned about the potential price volatility in the spot electricity market, which could adversely affect their profitability if the spot prices rise significantly during the contract period.

To hedge against this price risk, which of the following derivative instruments would be the most suitable for ABC Power Corporation?

A) Electricity Futures

B) Electricity Forwards

C) Electricity Swaps

D) Electricity Locational Basis Swaps

5. TN Ltd. has Rs. 600 lakh worth of 10% bonds outstanding with 5 years left to maturity. The company is considering refunding these bonds by issuing Rs. 600 lakh of new 5-year bonds at a 7% coupon rate due to falling interest rates. The issue cost for the new bonds is Rs. 12 lakh, and the call premium on the old bonds is 3%. The unamortized issue cost of the old bonds is Rs. 18 lakh, and the tax rate is 30%. You are given the following PVIFAs:

PVIFA @ 4.9% for 5 years = 4.341

PVIFA @ 7% for 5 years = 4.100

Based on the bond refunding decision, what should TN Ltd. do?

- A) Do not refund, as the net present value is negative
- B) Refund the bonds, as the net present value is Rs. 19.20 lakh
- C) Refund the bonds, as the net present value is Rs. 33.93 lakh
- D) Wait until interest rates fall below 6% to refund

(5 x 1 = 5 Marks)

