

CA Nitin Guru

Subject- **Financial Management - By CA NITIN GURU**

Mock Test – 4

Cost of Capital & Capital Structure

Time: 40 Minutes

M.M. – 25 Marks

Instructions-

1. This is a self paced test series, where you can do the test anytime after you complete your chapter and attempt the test and email it to us for checking or self evaluation with help of the solution set provided. For video solutions and test paper to be checked please email us at email id provided below.
2. Answer Sheet is in a single pdf format.
3. First Sheet contains all the information- Name, Registered Email id, Registered Mobile No., Test Number with Subject, website name through which you are watching our class..
4. NO late submission will be entertained.
5. NO answer sheet will be accepted over a chat box or telegram or any other mode other than email.
6. Test solutions should be emailed to test.canitinguru@gmail.com
7. Please give us at least 10 working days time to check and send back your test copy.
8. Sir, will record test paper discussion video as well, which you can watch and clarify your doubts if you have any. Solution videos will be available on youtube and please join our telegram channel [@canitinguru](https://t.me/canitinguru) to be updated with any announcement about test discussion.

Question 1.

[5 Marks]

Xylo Ltd. is considering two alternative financing plans as follows:

Particulars	Plan – A (₹)	Plan – B (₹)
Equity shares of ₹ 10 each	8,00,000	8,00,000
Preference Shares of ₹ 100 each	-	4,00,000
12% Debentures	4,00,000	-
	12,00,000	12,00,000

The indifference point between the plans is ₹ 4,80,000. Corporate tax rate is 30%. CALCULATE the rate of dividend on preference shares.

Question 2.

[10 Marks]

Blue Ltd., an all equity financed company is considering the repurchase of ₹ 275 lakhs equity shares and to replace it with 15% debentures of the same amount. Current market value of the company is ₹ 1,750 lakhs with its cost of capital of 20%. The company's Earnings before Interest and Taxes (EBIT) are expected to remain constant in future years. The company also has a policy of distributing its entire earnings as dividend .

Assuming the corporate tax rate as 30% , you are required to Calculate the impact on the following on account of the change in the capital structure as per Modigliani and Miller (MM) Approach:

- (i) Market Value of the Company
- (ii) Overall cost of capital
- (iii) Cost of equity

Question 3.

[10 Marks]

DETERMINE the cost of capital of Best Luck Limited using the book value (BV) and market value (MV) weights from the following information:

Sources	Book Value	Market Value
	(Rs)	(Rs)
Equity Shares	1,20,00,000	2,00,00,000
Retained Earnings	30,00,000	---
Preference Shares	36,00,000	33,75,000
Debentures	9,00,000	10,40,000

Additional information:

- I. Equity: Equity shares are quoted at Rs 130 per share and a new issue priced at Rs 125 per share will be fully subscribed; flotation costs will be Rs 5 per share.
- II. Dividend: During the previous 5 years, dividends have steadily increased from Rs 10.60 to Rs 14.19 per share. Dividend at the end of the current year is expected to be Rs 15 per share.
- III. Preference shares: 15% Preference shares with face value of Rs 100 would realise Rs 105 per share.
- IV. Debentures : The company proposes to issue 11-year 15% debentures but the yield on debentures of similar maturity and risk class is 16% ; flotation cost is 2%.
- V. Tax : Corporate tax rate is 35%. Ignore dividend tax. Floatation cost would be calculated on face value.