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Mock Test Paper - Series I: March, 2024

Date of Paper: 16 March, 2024

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

INTERMEDIATE: GROUP – II

PAPER – 6A : FINANCIAL MANAGEMENT & STRATEGIC MANAGEMENT

PAPER 6A: FINANCIAL MANAGEMENT

Time Allowed – 3 Hours (Total time for 6A and 6B) Maximum Marks – 50

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.*
4. *Working note should form part of the answer. Wherever necessary, suitable assumptions may be made by the candidates and disclosed by way of note. However, in answers to Questions in Division A, working notes are not required.*

PART I – Case Scenario based MCQs (15 Marks)

Write the most appropriate answer to each of the following multiple choice questions by choosing one of the four options given. All questions are compulsory.

1. NV Industries Ltd. is a manufacturing industry which manages its accounts receivables internally by its sales and credit department. It supplies small articles to different industries. The total sales ledger of the company stands at ₹ 200 lakhs of which 80% is credit sales. The company has a credit policy of 2/40, net 120. Past experience of the company has been that on average out of the total, 50% of customers avail of discount and the balance of the receivables are collected on average in 120 days. The finance controller estimated, bad debt losses are around 1% of credit sales.

   With escalating cost associated with the in-house management of the debtors coupled with the need to unburden the management with the task so as to focus on sales promotion, the CFO is examining the possibility of outsourcing its factoring service for managing its receivables. Currently, the firm spends about ₹ 2,40,000 per annum to administer its credit sales. These are avoidable as a factoring firm is prepared to buy the firm's receivables. The main elements of the proposal are : (i) It will charge 2% commission (ii) It will pay advance against receivables to the firm at an interest rate of 18% after withholding 10% as reserve.

   Also, company has option to take long term loan at 15% interest or may take bank finance for working capital at 14% interest.

   You were also present at the meeting; being a financial consultant, the CFO has asked you to be ready with the following questions:

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Consider year as 360 days.

I. What is average level of receivables of the company?

a. ₹ 53,33,333

b. ₹ 35,55,556

c. ₹ 44,44,444

d. ₹ 71,11,111

II. How much advance factor will pay against receivables?

a. ₹ 31,28,889

b. ₹ 39,11,111

c. ₹ 30,03,733

d. ₹ 46,93,333

III. What is the annual cost of factoring to the company?

a. ₹ 8,83,200

b. ₹ 4,26,667

c. ₹ 5,51,823

d. ₹ 4,00,000

IV. What is the net cost to the company on taking factoring service?

a. ₹ 4,00,000

b. ₹ 4,26,667

c. ₹ 3,50,000

d. ₹ 4,83,200

V. What is the effective cost of factoring on advance received?

a. 16.09%

b. 13.31%

c. 12.78%

d. 15.89% **(5 x 2 = 10 Marks)**

2. Ramu Ltd. wants to implement a project for which ₹ 25 lakhs is required. Following financing options are at hand:

Option 1:

Equity Shares	25,000 @ ₹ 100

Option 2:

Equity Shares	10,000 @ ₹ 100
12% Preference Shares	5,000@ ₹ 100
10% Debentures	10,000@ ₹ 100

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What is the indifference point & EPS at that level of EBIT assuming corporate tax to be 35%.

(a) ₹ 2,94,872; ₹ 11.80

(b) ₹ 3,20,513; ₹ 8.33

(c) ₹ 2,94,872; ₹ 7.67

(d) ₹ 3,20513; ₹ 12.82 **(2 Marks)**

3. "If EBIT increases by 6%, net profit increases by 6.9%. If sales increase by 6%, net profit will increase by 24%.

Financial leverage must be -............"

(a) 1.19

(b) 1.13

(c) 1.12

(d) 1.15 **(2 Marks)**

4. What is the maximum period for which company can accept Public Deposits?

(a) 1 year

(b) 6 months

(c) 3 years

(d) 5 years **(1 Marks)**

PART II – Descriptive Questions (35 Marks)

Question No. ***1*** *is compulsory.*

Attempt any ***two*** *questions out of the remaining* ***three*** *questions.*

1. (a) The following figures have been extracted from the annual report of Xee Ltd.:

Net Profit	₹ 54 lakhs
Outstanding 12% preference shares	₹ 200 lakhs
No. of equity shares	2 lakhs
Return on Investment	22%
Cost of capital i.e. (K_e)	15%

COMPUTE the approximate dividend pay-out ratio so as to keep the share price at ₹ 120 by using Walter's model?

(Decimal may be taken up to 2 units) **(5 Marks)**

(b) Capital structure (in market-value terms) of AN Ltd is given below:

Company	Debt	Equity
AN Ltd.	50%	50%

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The borrowing rate for the company is 10% in a no-tax world and capital markets are assumed to be perfect.

Required:

(i) If Mr. R, owns 8% of the equity shares of AN Ltd., DETERMINE his return if the Company has net operating income of ₹ 10,00,000 and the overall capitalization rate of the company (K_o) is 20%.

(ii) CALCULATE the implied required rate of return on equity of AN Ltd.

(5 Marks)

(c) ANVY Ltd. has furnished the following ratios and information for the year end 31st March, 2023:

Equity share capital	₹ 2,00,000
The relevant ratios of the company are as follows:	
Current debt to total debt	0.50
Total debt to Equity share capital	0.60
Fixed assets to Equity share capital	0.70
Total assets turnover	2.5 Times
Inventory turnover	10 Times

You are required to PREPARE the Balance Sheet of ANVY Ltd. as on 31st March, 2023. **(5 Marks)**

2. (a) NC Ltd. Is considering purchasing a new machine to increase its production facility. At present, it uses an old machine which can process 5,000 units of TVs per week. NC could replace it with new machine, which is product specific and can produce 15,000 units per week. New machine cost ₹ 100 crores and requires the working capital of ₹ 3 crores, which will be released at the end of 5th year. The new machine is expected to have a salvage value of ₹ 20 crores.

The company expects demand for TVs to be 10,000 units per week. Each TV sells for ₹ 30,000 and has Profit Volume Ratio (PV) of 0.10. The company works for the 56 weeks in the year. Additional fixed costs (excluding depreciation) are estimated to increase by ₹ 10 crores. The company is subject to a 40% tax rate and its after-tax cost of capital is 20%. The relevant rate of depreciation is 25 % for both taxation and accounts. The company uses the WDV method of depreciation. The existing machine will have no scrap value.

You are required to:

ADVISE whether the company should replace the old machine.

(Decimal may be taken up to 2 units) **(8 Marks)**

(b) WRITE a short note on "Cut-off Rate". **(2 Marks)**

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3. (a) Ram Ltd evaluates all its capital projects using discounting rate of 16%. Its capital structure consists of equity share capital, retained earnings, bank term loan and debentures redeemable at par. Rate of interest on bank term loan is 1.4 times that of debenture. Remaining tenure of debenture and bank loan is 4 years and 6 years respectively. Book value of equity share capital, retained earnings and bank loan is ₹ 20,00,000, ₹ 30,00,000 and ₹ 20,00,000 respectively. Debentures which are having book value of ₹ 30,00,000 are currently trading at ₹ 98 per debenture. The ongoing PE multiple for the shares of the company stands at 4.

You are required to:

(i) CALCULATE the rate of interest on bank loan and

(ii) CALCULATE the rate of interest on debentures

Tax rate applicable is 30%. **(8 Marks)**

(b) DISCUSS the dividend-price approach to estimate cost of equity capital.

(2 Marks)

4. (a) EXPLAIN the limitations of profit maximization objective of Financial Management. **(4 Marks)**

(b) WHAT are the methods of venture capital financing? **(4 Marks)**

(c) WHAT is 'Optimum Capital Structure'? **(2 Marks)**

OR

EXPLAIN the concept of Financial Leverage as 'Trading on Equity'.

(2 Marks)

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INTERMEDIATE COURSE: GROUP II

PAPER 6B: STRATEGIC MANAGEMENT

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 (15 Marks)

Question 1.(A) (Compulsory)

1. (A) In the fiercely competitive automotive industry, Zing, a promising newcomer, set out on a strategic journey with ambitions of making a substantial impact. Recognizing the significance of a robust distribution network early on, Zing forged partnerships with established dealerships, offering them attractive margins. This strategic move significantly enhanced Zing's reach, with a presence in 80% of the nation's dealerships by 2022, expanding its coverage significantly.

To differentiate themselves from competitors, Zing adopted two key strategies. Firstly, they prioritized product design, investing heavily in aesthetics and incorporating innovative features and environmentally friendly technologies. This focus on design led to their vehicles receiving excellent reviews and achieving an impressive 15% year-on-year growth in sales.

Secondly, Zing implemented switching costs to discourage customers from switching to other brands. Their vehicles featured branded software, making it both expensive and cumbersome for customers to transition to alternative brands. This strategic move effectively protected Zing's market share.

Zing's overarching goal was to position itself as a premium automotive brand, blending luxury with sustainability. However, their execution fell down as they challenged with maintaining consistent quality and service levels, resulting in mixed customer reviews.

Despite their best efforts, Zing's differentiation strategy fell short due to issues with inconsistent quality and service. Negative word-of-mouth and declining customer satisfaction scores tarnished their brand image, leading to stagnating sales. This failure to deliver on their brand promise proved to be a significant setback.

As Zing's reputation suffered from execution failures, securing additional funds for international expansion became challenging. Consequently, they made the difficult decision to postpone their global ambitions for the next five years, focusing instead on stabilizing their finances and rebuilding their brand image.

In summary, Zing's strategic journey illustrates the importance of not only crafting a compelling differentiation strategy but also executing it flawlessly. In the competitive automotive landscape, maintaining

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consistent quality and service is paramount to sustaining brand loyalty and achieving long-term success.

Based on the above Case Scenario, answer the Multiple Choice Questions.

(i) What key strategic approach did Zing use to expand its market presence in the automotive industry?

(a) Product innovation and design

(b) Cost leadership strategy

(c) Entering new international markets

(d) Vertical integration **(2 Marks)**

(ii) How did Zing protect its market share from potential competitors?

(a) Price-cutting strategy

(b) Branded software and switching costs

(c) Aggressive marketing campaigns

(d) International expansion **(2 Marks)**

(iii) Why did Zing's differentiation strategy fall short in the market?

(a) Intense price competition

(b) Poor marketing strategy

(c) Inconsistent quality and service

(d) Lack of international expansion **(2 Marks)**

(iv) Forging partnerships with established dealerships to enhance its distribution network falls under which level of strategy?

(a) Corporate level strategy

(b) Business level strategy

(c) Functional level strategy

(d) Competitive level strategy **(2 Marks)**

(v) How did Zing initially expand its market presence across the nation?

(a) Aggressive marketing campaigns

(b) Developing low-cost vehicles

(c) Partnering with established dealerships

(d) Launching a luxury brand **(2 Marks)**

(B) Compulsory Application Based Independent MCQs

(i) TechMex Inc., a leading technology company, offers a diverse portfolio of products ranging from established cash cows to promising question marks. As part of its strategic planning process,

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the company aims to assess its product portfolio's performance and allocate resources effectively. In which quadrant of the BCG Matrix would TechMex's new innovative product, recently launched in a rapidly growing market, likely fall into?

(a) Cash Cow

(b) Dog

(c) Question Mark

(d) Star **(2 Marks)**

(ii) BlueSky Enterprises, a multinational corporation specializing in renewable energy solutions, is undergoing a strategic transformation to enhance its competitive position in the market. As part of this initiative, the company is reevaluating its organizational structure, processes, and culture. Which aspect of the McKinsey 7S Model is most relevant for BlueSky Enterprises during this strategic transformation?

(a) Strategy

(b) Structure

(c) Systems

(d) Skills **(2 Marks)**

(iii) The threat of substitutes is high when:

(a) There are few substitute products available

(b) Switching costs are low

(c) Suppliers have high bargaining power

(d) There is strong brand loyalty **(1 Mark)**

PART II – Descriptive Questions (35 Marks)

*Question No. **1** is compulsory.*

*Attempt any **two** questions out of the remaining **three** questions.*

1. (a) Swati is the marketing manager at a software company. She is responsible for developing and implementing marketing strategies for the company’s products. Swati leads a team of marketing professionals and works closely with the product development and sales teams to ensure that the company's products are effectively promoted in the market. She also analyzes market trends and customer feedback to refine the marketing strategies. Which level is she working at, discuss the roles and responsibilities of this level in organization? **(5 Marks)**

(b) ABC Corp, a multinational consumer electronics company, is planning to expand its operations into a new country. The company's senior management is evaluating the potential risks and opportunities of entering this new market. As part of their analysis, they decide to use

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the PESTLE framework to assess the external factors that could impact their decision. How can the PESTLE framework help ABC Corp assess the external factors affecting its decision to expand into a new country? **(5 Marks)**

(c) Imagine you are a consultant advising a small manufacturing company embarking on a digital transformation journey. The company's leadership is concerned about managing the change effectively. Using the best practices for managing change in small and medium-sized businesses, outline a strategy to help the company navigate this transformation successfully. **(5 Marks)**

2. (a) Imagine you are a strategic consultant advising a retail company that is facing increasing competition from online retailers. The company is considering several strategic options to improve its market position. Using the concept that strategy is partly proactive and partly reactive, explain how the company can develop a strategic approach to address this challenge. **(5 Marks)**

(b) You are a strategic manager for a tech company launching a new smartphone model. The company wants to target tech-savvy consumers who value innovation and cutting-edge technology. Using the concept of customer behavior, develop a marketing strategy to promote the new smartphone. **(5 Marks)**

3. (a) A beverage company is launching a new line of energy drinks targeted at health-conscious consumers. The strategic manager wants to study the market position of rival companies in the energy drink segment. Which tool can be used for this analysis, and what is the procedure to implement it effectively? **(5 Marks)**

(b) The CEO of a textile mill believes that his company, currently operating at a loss, can be turned around. Develop an action plan outlining steps the CEO can take to achieve this turnaround. **(5 Marks)**

4. (a) Why Strategic Performance Measures are essential for organizations?

(5 Marks)

(b) How can Mendelow's Matrix be used to analyze and manage the stakeholders effectively?

OR

Distinguish between Concentric Diversification and Conglomerate Diversification. **(5 Marks)**

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PAPER – 6: FINANCIAL MANAGEMENT & STRATEGIC MANAGEMENT

PAPER 6A : FINANCIAL MANAGEMENT

Suggested Answers/ Hints

PART I

1. I. (b) ₹ 35,55,556

II. (c) ₹ 30,03,733

III. (a) ₹ 8,83,200

IV. (d) ₹ 4,83,200

V. (a) 16.09%

Working Note

Particulars	**(₹)**
Total Sales	₹ 200 lakhs
Credit Sales (80%)	₹ 160 lakhs
Receivables for 40 days	₹ 80 lakhs
Receivables for 120 days	₹ 80 lakhs
Average collection period [(40 x 0.5) + (120 ×0.5)]	80 days
Average level of Receivables (₹ 1,60,00,000 × 80/360)	₹ 35,55,556
Factoring Commission (₹ 35,55,556 × 2/100)	₹ 71,111
Factoring Reserve (₹ 35,55,556 × 10/100)	₹ 3,55,556
Amount available for advance {₹ 35,55,556 - (3,55,556 + 71,111)}	₹ 31,28,889
Factor will deduct his interest @ 18%: Interest = $\frac{₹31,28,889 \times 18 \times 80}{100 \times 360}$	₹ 1,25,156
Advance to be paid (₹ 31,28,889 – ₹ 1,25,156)	₹ 30,03,733

(i) Statement Showing Evaluation of Factoring Proposal

		₹
A.	**Annual Cost of Factoring to the Company:**	
	Factoring commission (₹ 71,111 × 360/80)	3,20,000
	Interest charges (₹ 1,25,156 × 360/80)	5,63,200
	Total	8,83,200

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B.	**Company's Savings on taking Factoring Service:**	₹
	Cost of credit administration saved	2,40,000
	Bad Debts (₹ 160,00,000 x 1/100) avoided	1,60,000
	Total	4,00,000
C.	Net Cost to the company (A – B) (₹ 8,83,200 – ₹ 4,00,000)	4,83,200

Effective cost of factoring = $\frac{₹\ 4,83,200}{₹30,03,733} \times 100$ = 16.09%

2. B. ₹ 3,20,513; ₹ 8.33

$$\frac{(EBIT - I)(1 - t) - D_p}{N_1} = \frac{(EBIT - I)(1 - t) - D_p}{N_2}$$

$$\frac{(x - 0)(1 - 0.35)}{25,000} = \frac{(x - 1,00,000)(1 - 0.35) - 60,000}{10,000}$$

x = EBIT = ₹ 3,20,513

At EBIT of ₹ 3,20,513, EPS under both options will be the same i.e., ₹ 8.33 per share

3. D. 1.15

FL= % change in NP/%change in EBIT=6.9/6=1.15

4. C. 3 years

These deposits may be accepted for a period of six months to three years.

PART II

1. (a)

Particulars	**(₹' in lakhs)**
Net Profit	54
Less: Preference dividend	24
Earnings for equity shareholders	30
Earnings per share	30/2 = ₹ 15

Let, the dividend per share be D to get share price of ₹ 120.

$$P = \frac{D + \frac{r}{Ke}(E - D)}{K_e}$$

Where,

P = Market price per share.

E = Earnings per share = ₹ 15

D = Dividend per share

R = Return earned on investment = 22%

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K_e = Cost of equity capital = 15%

$$120 = \frac{D + \frac{0.22}{0.15}(15-D)}{0.15}$$

$$18 = \frac{0.15D + 3.3 - 0.22D}{0.15}$$

$$0.07D = 3.3 - 2.7$$

$$D = 8.57$$

$$\text{D/P ratio} = \frac{DPS}{EPS} \times 100 = \frac{8.57}{15} \times 100 = 57.13\%$$

So, the required dividend pay-out ratio will be = 57.13%

(b) Value of AN Ltd. = $\frac{NOI}{K_o} = \frac{₹\ 10,00,000}{20\%}$ = ₹ 50,00,000

(i) Return on Shares of Mr. R on AN Ltd.

Particulars	Amount (₹)
Value of the company	50,00,000
Market value of debt (50% x ₹ 50,00,000)	25,00,000
Market value of shares (50% x ₹ 50,00,000)	**25,00,000**
Particulars	**Amount (₹)**
Net operating income	10,00,000
Interest on debt (10% × ₹ 25,00,000)	2,50,000
Earnings available to shareholders	**7,50,000**
Return on 8% shares (8% × ₹ 7,50,000)	**60,000**

(ii) Implied required rate of return on equity of AN Ltd. = $\frac{₹\ 7,50,000}{₹\ 25,00,000}$ = **30%**

(c) **ANVY Ltd**

Balance Sheet as on 31st March, 2023

Liabilities	₹	Assets	₹
Equity share capital	2,00,000	Fixed assets	1,40,000
Current debt	60,000	Cash (balancing figure)	1,00,000
Long term debt	60,000	Inventory	80,000
	3,20,000		3,20,000

Working Notes

1. Total debt = 0.60 x Equity share capital = 0.60 × ₹ 2,00,000 = ₹ 1,20,000

   Further, Current debt to total debt = 0.50. So, current debt = 0.50 x ₹1,20,000 = ₹ 60,000,

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Long term debt = ₹1,20,000 - ₹60,000= ₹ 60,000

2. Fixed assets = 0.70 × Equity share Capital = 0.70 × ₹ 2,00,000 = ₹ 1,40,000

3. Total assets to turnover = 2.5 Times: Inventory turnover = 10 Times

Hence, Inventory /Total assets = 2.5/10=1/4, Total assets = ₹ 3,20,000

Therefore Inventory = ₹ 3,20,000/4 = ₹ 80,000

2. (a) Cash inflows after tax (CFAT)

Particular	₹
Current production (units per week)	5,000 units
New capacity (units per week)	15,000 units
Demand (units per week)	10,000 units
Increase in sales (units per week) A.	5,000 units
Contribution per unit (₹ 30,000 x 0.10) B.	3,000
Increase in contribution A x B x 56	84 crores
Less: Additional fixed cost	10 crores
Increase in profit	74 crores
Less: Tax @ 40%	29.6 crores
Profit after tax	44.4 crores

Tax shield due to depreciation

Year	Depreciation (₹ in Crore)	Tax Shield (₹ in Crore)	PV Factor @ 20%	Total Present Value (₹ in Crore)
1	25.00	10	0.83	8.33
2	18.75	7.5	0.69	5.18
3	14.06	5.62	0.58	3.26
4	10.55	4.22	0.48	2.03
5	7.91	3.16	0.40	1.27
Total				20.07

Tax shield on capital loss = (23.73-20.00) x 30% = ₹ 1.12 crores

Net Present Value (NPV)

Particulars	Year	Cash Flow (₹ in Crores)	PVAF @ 20%	Present Value (₹ in Crores)
Initial Investment	0	(100)	1	(100)
Working capital	0	(3)	1	(3)
Profit after tax	1-5	44.4	2.99	132.76
Salvage value	5	20	0.40	8.00

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Tax shield on Depreciation	1-5			20.07
Tax shield on capital loss	5	1.12	0.40	0.45
Release of Working Capital	5	3	0.40	1.20
NPV				59.47

The company is advised to replace the old machine since the NPV of the new machine is positive.

(b) **Cut-off Rate:** It is the minimum rate which the management wishes to have from any project. Usually this is based upon the cost of capital. The management gains only if a project gives return of more than the cut - off rate. Therefore, the cut - off rate can be used as the discount rate or the opportunity cost rate.

3. (a) Working Note:

Let the rate of Interest on debenture be x

∴ Rate of Interest on loan = 1.4x

$$\therefore k_d \text{ on debentures} = \frac{Int\,(1-t) + \frac{RV-NP}{n}}{\frac{RV+NP}{2}}$$

$$= \frac{100x(1-0.30) + \frac{100-98}{4}}{\frac{100+98}{2}}$$

$$= \frac{70x+0.5}{99}$$

∴ K_d on bank loan = 1.4 x (1 – 0.30) = 0.98x

$$K_e = \frac{EPS}{MPS} = \frac{1}{MPS/EPS} = \frac{1}{PE} = \frac{1}{4} = 0.25$$

K_e = 0.25

Computation of WACC

Capital	Amount	Weights	Cost	Product
Equity	20,00,000	0.2	0.25	0.05
Reserves	30,00,000	0.3	0.25	0.075
Debentures	30,00,000	0.3	(70x+0.5)/99	(21x+0.15)/99
Bank Loan	20,00,000	0.2	0.98x	0.196x
	1,00,00,000	1		$0.125+0.196x + \frac{21x+0.15}{99}$

WACC = 16%

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$\therefore$ $0.125+0.196x+\frac{21x+0.15}{99} = 0.16$

$\therefore$ $12.375+19.404x+21x+0.15 = (0.16)(99)$

$\therefore$ $40.404x = 15.84 - 12.525$

$\therefore$ $40.404x = 3.315$

$\therefore$ $x = \frac{3.315}{40.404}$

$\therefore$ $x = 8.20\%$

(i) Rate of interest on debenture = x = 8.20%

(ii) Rate of interest on Bank loan = 1.4x = (1.4)(8.20%) = 11.48%.

(b) In dividend price approach, cost of equity capital is computed by dividing the expected dividend by market price per share. This ratio expresses the cost of equity capital in relation to what yield the company should pay to attract investors. It is computed as:

$$K_e = \frac{D_1}{P_0}$$

Where,

K_e= Cost of equity

D = Expected dividend (also written as D_1)

P_0 = Market price of equity (ex- dividend)

4. (a) Limitations of Profit Maximisation objective of financial management.

(i) **The term profit is vague. It does not clarify what exactly it means.** It conveys a different meaning to different people. For example, profit may be in short term or long term period; it may be total profit or rate of profit etc.

(ii) **Profit maximisation has to be attempted with a realisation of risks involved.** There is a direct relationship between risk and profit. Many risky propositions yield high profit. Higher the risk, higher is the possibility of profits. If profit maximisation is the only goal, then risk factor is altogether ignored. This implies that finance manager will accept highly risky proposals also, if they give high profits. In practice, however, risk is very important consideration and has to be balanced with the profit objective.

(iii) **Profit maximisation as an objective does not take into account the time pattern of returns.** Proposal A may give a higher amount of profits as compared to proposal B, yet if the returns of proposal A begin to flow say 10 years later, proposal B may be preferred

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which may have lower overall profit but the returns flow is more early and quick.

(iv) **Profit maximisation as an objective is too narrow.** It fails to take into account the social considerations as also the obligations to various interests of workers, consumers, society, as well as ethical trade practices. If these factors are ignored, a company cannot survive for long. Profit maximization at the cost of social and moral obligations is a short sighted policy.

(b) Some common methods of venture capital financing are as follows:

(i) **Equity financing:** The venture capital undertakings generally require funds for a longer period but may not be able to provide returns to the investors during the initial stages. Therefore, the venture capital finance is generally provided by way of equity share capital. The equity contribution of venture capital firm does not exceed 49% of the total equity capital of venture capital undertakings so that the effective control and ownership remains with the entrepreneur.

(ii) **Conditional loan:** A conditional loan is repayable in the form of a royalty after the venture is able to generate sales. No interest is paid on such loans. In India venture capital financiers charge royalty ranging between 2 and 15 per cent; actual rate depends on other factors of the venture such as gestation period, cash flow patterns, risk and other factors of the enterprise. Some Venture capital financiers give a choice to the enterprise of paying a high rate of interest (which could be well above 20 per cent) instead of royalty on sales once it becomes commercially sound.

(iii) **Income note:** It is a hybrid security which combines the features of both conventional loan and conditional loan. The entrepreneur has to pay both interest and royalty on sales but at substantially low rates. IDBI's VCF provides funding equal to 80 – 87.50% of the projects cost for commercial application of indigenous technology.

(iv) **Participating debenture:** Such security carries charges in three phases — in the start-up phase no interest is charged, next stage a low rate of interest is charged up to a particular level of operation, after that, a high rate of interest is required to be paid.

(c) **Optimum Capital Structure:** The capital structure is said to be optimum when the firm has selected such a combination of equity and debt so that the wealth of firm is maximum. At this capital structure, the cost of capital is minimum and the market price per share i.e. value of the firm is maximum.

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OR

Financial leverage indicates the use of funds with fixed cost like long term debts and preference share capital along with equity share capital which is known as trading on equity. The basic aim of financial leverage is to increase the earnings available to equity shareholders using fixed cost fund.

A firm is known to have a positive/favourable leverage when its earnings are more than the cost of debt. If earnings are equal to or less than cost of debt, it will be an negative/unfavourable leverage. When the quantity of fixed cost fund is relatively high in comparison to equity capital it is said that the firm is **''trading on equity".**

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INTERMEDIATE COURSE: GROUP II

PAPER 6B: STRATEGIC MANAGEMENT

ANSWERS

PART I

1. (A) (i) (a) (ii) (b) (iii) (c) (iv) (b) (v) (c)

1. (B) (i) (c) (ii) (b) (iii) (b)

PART II

1. (a) Swati operates at the functional level of management, specifically as the marketing manager at a software company. Functional managers like Swati oversee specific departments or functions within an organization, such as marketing, finance, or operations. Their primary responsibilities include implementing corporate strategies and policies within their area of expertise and ensuring that daily operations are conducted efficiently and effectively.

In Swati's case, as a marketing manager, her role involves developing and executing marketing strategies for the company's products. This includes leading a team of marketing professionals, collaborating with product development and sales teams, and analyzing market trends and customer feedback to refine strategies. By working closely with these teams, Swati ensures that the company's products are effectively promoted in the market and that marketing efforts align with overall business goals.

Functional managers like Swati play a critical role in the organization by bridging the gap between corporate strategy and daily operations. They are responsible for translating high-level strategic goals into actionable plans for their departments and ensuring that these plans are executed effectively. Additionally, they are often key decision-makers within their areas of responsibility, making strategic choices that impact on the company's success. Overall, Swati's role as a marketing manager exemplifies the importance of functional managers in driving the success of their organizations.

(b) The PESTLE framework can help ABC Corp assess the external factors affecting its decision to expand into a new country by considering the following aspects:

- **Political Factors**: These include the stability of the government, government policies on foreign investment, trade agreements, and regulatory frameworks. By analyzing these factors, ABC Corp can assess the political risks associated with entering the new market.
- **Economic Factors**: Economic factors such as GDP growth rate, inflation rate, exchange rates, and economic stability can impact ABC Corp's decision. By analyzing these factors, the company can

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understand the economic environment of the new market and its potential impact on business operations.

- **Social Factors**: Social factors such as cultural norms, demographics, and lifestyle trends can influence consumer behavior and demand for ABC Corp's products. Understanding these factors can help the company tailor its marketing strategies to the new market.
- **Technological Factors**: Technological factors such as infrastructure, technological advancements, and the level of technology adoption in the new market can impact ABC Corp's operations. By assessing these factors, the company can determine the technological requirements for entering the new market.
- **Legal Factors**: Legal factors such as laws and regulations related to foreign investment, intellectual property rights, and labor laws can impact ABC Corp's decision. By analyzing these factors, the company can ensure compliance with legal requirements in the new market.
- **Environmental Factors**: Environmental factors such as climate change, environmental regulations, and sustainability practices can impact ABC Corp's operations and reputation. By considering these factors, the company can assess the environmental risks and opportunities in the new market.

Overall, the PESTLE framework can provide ABC Corp with a comprehensive analysis of the external factors that could impact its decision to expand into a new country, helping the company make informed and strategic decisions.

(c) To help the small manufacturing company navigate its digital transformation successfully, we would recommend the following strategy:

1. **Begin at the top:** The leadership team should be united and committed to the digital transformation. They should communicate a clear vision for the future of the company and lead by example.
2. **Ensure that the change is necessary and desired:** Before implementing any changes, the company should assess its current state and identify areas where digital transformation can add value. It's important to involve employees in this process to ensure their buy-in.
3. **Reduce disruption:** Employee perceptions of change can vary, so it's important to minimize disruption. This can be done by communicating early and often about the changes, providing training and support for employees, and empowering change agents within the organization.

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4. **Encourage communication:** Create channels for employees to ask questions and provide feedback. Encourage collaboration between departments to share ideas and innovations. Effective communication can help alleviate fears and keep everyone aligned.

5. **Recognize that change is the norm:** Digital transformation is not a one-time project but an ongoing process. The company should be prepared to adapt to new technologies and market conditions continuously.

By following these best practices, the small manufacturing company can successfully navigate its digital transformation and position itself for future growth and success.

2. (a) The retail company can develop a strategic approach that is both proactive and reactive to address the challenge of increasing competition from online retailers. To achieve this, the company can:

- **Proactive Strategy:** The company can proactively analyze market trends and customer preferences to identify opportunities for growth. For example, it can invest in market research to understand what customers value in a retail experience and tailor its offerings to meet those needs. This proactive approach can help the company stay ahead of competitors and attract new customers.

- **Reactive Strategy:** In addition to proactive measures, the company should also be prepared to react to changes in the market environment. For example, if a competitor launches a new online shopping platform, the company should quickly assess the impact on its business and develop a response. This reactive strategy can help the company adapt to changing market conditions and maintain its competitiveness.

By combining proactive and reactive strategies, the retail company can develop a comprehensive approach to addressing the challenge of increasing competition from online retailers. This approach will allow the company to capitalize on opportunities for growth while also mitigating risks and responding to threats in the market.

(b) To target tech-savvy consumers for the new smartphone model, the tech company can develop a marketing strategy based on customer behavior. Consumer behaviour may be influenced by a number of things. These elements can be categorised into the following conceptual domains:

- **External Influences:** Utilize online platforms and tech forums to generate buzz around the new smartphone. Partner with tech influencers and bloggers to review the product and create awareness among tech-savvy consumers.

- **Internal Influences:** Appeal to the desire for innovation and advanced features among tech-savvy consumers. Highlight the

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unique selling points of the new smartphone, such as its cutting-edge technology, performance, and design.

- **Decision Making:** Recognize that tech-savvy consumers are early adopters who value functionality and performance. Provide detailed specifications and comparisons with other smartphones to help them make an informed decision.
- **Post-decision Processes:** Offer excellent customer service and support to address any technical issues or concerns. Encourage customers to provide feedback and reviews to build credibility and trust among tech-savvy consumers.

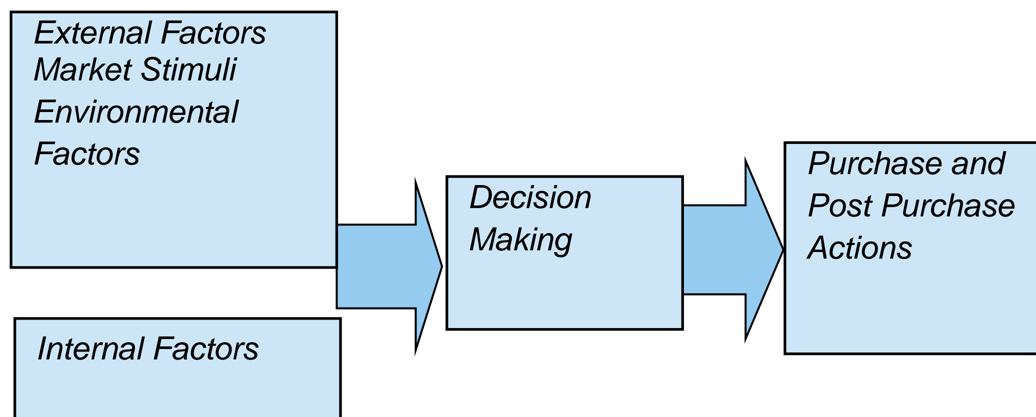

Figure: Process of consumer behaviour

By understanding the behavior of tech-savvy consumers and aligning the marketing strategy with their preferences, the tech company can effectively promote the new smartphone and attract this demographic.

3. (a) To study the market position of rival companies in the energy drink segment, the strategic manager can use **strategic group mapping.** This tool helps identify strategic groups, which consist of rival firms with similar competitive approaches and positions in the market. The procedure for implementing strategic group mapping effectively is as follows:

1. **Identify the competitive characteristics** that differentiate firms in the industry typical variables that are price/quality range (high, medium, low); geographic coverage (local, regional, national, global); degree of vertical integration (none, partial, full); product-line breadth (wide, narrow); use of distribution channels (one, some, all); and degree of service offered (no-frills, limited, full).
2. **Plot the firms on a two-variable map** using pairs of these differentiating characteristics.

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3. **Assign firms that fall in about the same strategy space** to the same strategic group.

4. **Draw circles around each strategic group** making the circles proportional to the size of the group's respective share of total industry sales revenues.

By following these steps, the strategic manager can gain valuable insights into the competitive landscape of the energy drink segment and identify potential positioning strategies for the new line of energy drinks targeted at health-conscious consumers.

(b) A workable action plan for turnaround of the textile mill would involve:

- **Stage One – Assessment of current problems**: In the first step, assess the current problems and get to the root causes and the extent of damage.
- **Stage Two – Analyze the situation and develop a strategic plan:** Identify major problems and opportunities, develop a strategic plan with specific goals and detailed functional actions after analyzing strengths and weaknesses in the areas of competitive position.
- **Stage Three – Implementing an emergency action plan**: If the organization is in a critical stage, an appropriate action plan must be developed to stop the bleeding and enable the organization to survive.
- **Stage Four – Restructuring the business**: If the core business is irreparably damaged, then the outlook for the entire organization may be bleak. Efforts to be made to position the organization for rapid improvement.
- **Stage Five – Returning to normal**: In the final stage of turnaround strategy process, the organization should begin to show signs of profitability, return on investments and enhancing economic value-added.

4. (a) Strategic performance measures are essential for organizations for several reasons:

♦ **Goal Alignment:** Strategic performance measures help organizations align their strategies with their goals and objectives, ensuring that they are on track to achieve their desired outcomes.

♦ **Resource Allocation:** Strategic performance measures provide organizations with the information they need to make informed decisions about resource allocation, enabling them to prioritize their

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efforts and allocate resources to the areas that will have the greatest impact on their performance.

- **Continuous Improvement:** Strategic performance measures provide organizations with a framework for continuous improvement, enabling them to track their progress and make adjustments to improve their performance over time.
- **External Accountability:** Strategic performance measures help organizations demonstrate accountability to stakeholders, including shareholders, customers, and regulatory bodies, by providing a clear and transparent picture of their performance.

(b) Mendelow's Matrix can be used effectively to analyze and manage stakeholders through a grid-based approach by the following steps:

1. **Identify Stakeholders:** Begin by identifying all relevant stakeholders for your project or organization. This includes individuals, groups, or organizations that may be impacted by or have an impact on your activities.
2. **Assess Power and Interest:** For each stakeholder, assess their power to influence your project or organization and their level of interest in its success. Power can be assessed based on factors such as authority, resources, and expertise, while interest can be gauged by their level of involvement, expectations, and potential benefits or risks.
3. **Plot Stakeholders on the Grid:** Create a grid with Power on one axis and Interest on the other. Plot each stakeholder on the grid based on your assessment. Stakeholders with high power and high interest are placed in the "Key Players" quadrant, those with high power but low interest are in the "Keep Satisfied" quadrant, those with low power but high interest are in the "Keep Informed" quadrant, and those with low power and low interest are in the "Low Priority" quadrant.

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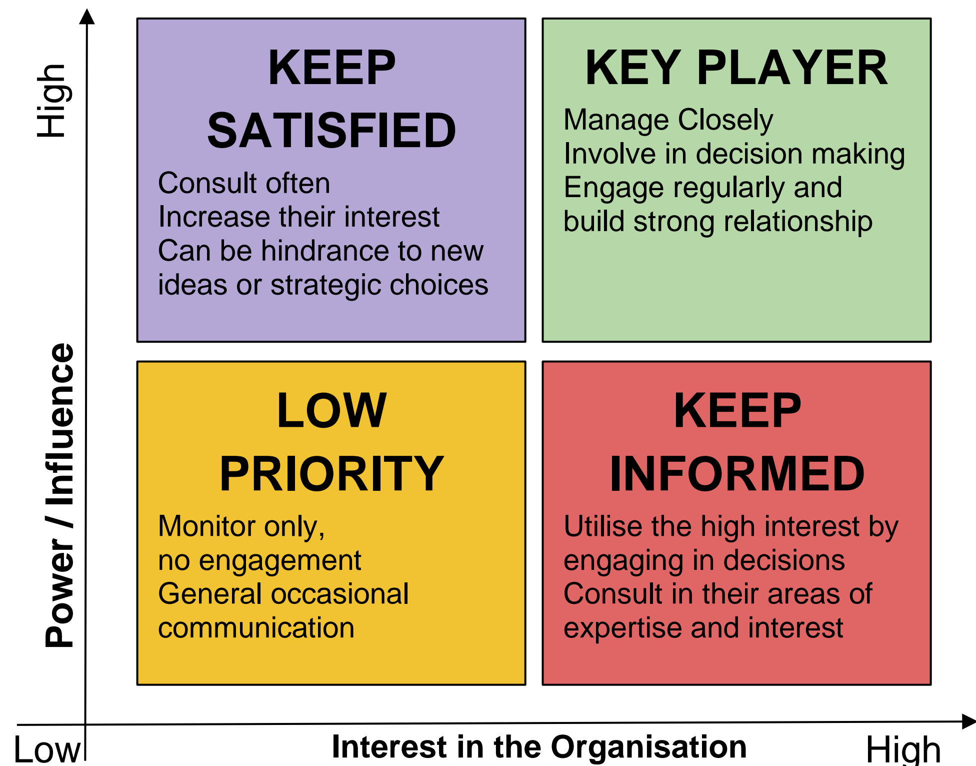

4. **Develop Strategies for each Quadrant:** Based on the placement of stakeholders in the grid, develop specific strategies for managing each quadrant:

   - **Key Players:** Fully engage with these stakeholders, seek their input, and keep them informed. They are crucial for the success of your project, so their needs and expectations should be a top priority.
   - **Keep Satisfied:** These stakeholders have significant power but may not be as interested in your project. Keep them satisfied by providing regular updates and addressing any concerns they may have to prevent them from becoming detractors.
   - **Keep Informed:** While these stakeholders may not have much power, they are highly interested in your project. Keep them informed to ensure they remain supportive and to leverage their insights and feedback.
   - **Low Priority:** These stakeholders have low power and interest. Monitor them for any changes but allocate minimal resources to managing their expectations.

5. **Monitor and Adapt:** Continuously monitor the power and interest of stakeholders and adjust your strategies accordingly. Stakeholders may move between quadrants based on changing circumstances, so it's important to remain flexible and responsive.

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By using Mendelow's Matrix as a grid-based tool, you can effectively analyze and manage stakeholders by tailoring your engagement strategies to their specific needs and expectations, ultimately increasing the likelihood of project success.

OR

The following are the principal points of distinction between concentric diversification and conglomerate diversification:

(i) Concentric diversification occurs when a firm adds related products or markets. On the other hand, conglomerate diversification occurs when a firm diversifies into areas that are unrelated to its current line of business.

(ii) In concentric diversification, the new business is linked to the existing businesses through process, technology or marketing. In conglomerate diversification, no such linkages exist; the new business/product is disjointed from the existing businesses/ products.

(iii) The most common reasons for pursuing concentric diversification are that opportunities in a firm’s existing line of business are available. However, common reasons for pursuing a conglomerate growth strategy are that opportunities in a firm's current line of business are limited or opportunities outside are highly lucrative.

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Mock Test Paper - Series II: April, 2024

Date of Paper: 15 April, 2024

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

INTERMEDIATE GROUP – II

PAPER – 6A : FINANCIAL MANAGEMENT & STRATEGIC MANAGEMENT

PAPER 6A: FINANCIAL MANAGEMENT

Time Allowed – 3 Hours (Total time for 6A and 6B) Maximum Marks – 50

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.*
4. *Working note should form part of the answer. Wherever necessary, suitable assumptions may be made by the candidates and disclosed by way of note. However, in answers to Questions in Division A, working notes are not required.*

PART I – Case Scenario based MCQs (15 Marks)

Write the most appropriate answer to each of the following multiple choice questions by choosing one of the four options given. All questions are compulsory.

1. Tiago Ltd is an all-equity company engaged in manufacturing of batteries for electric vehicles. There has been a surge in demand for their products due to rising oil prices. The company was established 5 years ago with an initial capital of ₹ 10,00,000 and since then it has raised funds by IPO taking the total paid up capital to ₹ 1 crore comprising of fully paid-up equity shares of face value ₹ 10 each. The company currently has undistributed reserves of ₹ 60,00,000. The company has been following constant dividend payout policy of 40% of earnings. The retained earnings by company are going to provide a return on equity of 20%. The current EPS is estimated as Rs 20 and prevailing PE ratio on the share of company is 15x. The company wants to expand its capital base by raising additional funds by way of debt, preference and equity mix. The company requires an additional fund of ₹ 1,20,00,000. The target ratio of owned to borrowed funds is 4:1 post the fund-raising activity. Capital gearing is to be kept at 0.4x.

   The existing debt markets are under pressure due to ongoing RBI action on NPAs of the commercial bank. Due to challenges in raising the debt funds, the company will have to offer ₹ 100 face value debentures at an attractive yield of 9.5% and a coupon rate of 8% to the investors. Issue expenses will amount to 4% of the proceeds.

   The preference shares will have a face value of ₹ 1000 each offering a dividend rate of 10%. The preference shares will be issued at a premium of

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5% and redeemed at a premium of 10% after 10 years at the same time at which debentures will be redeemed.

The CFO of the company is evaluating a new battery technology to invest the above raised money. The technology is expected to have a life of 7 years. It will generate a after tax marginal operating cash flow of ₹ 25,00,000 p.a. Assume marginal tax rate to be 27%.

1. Which of the following is best estimate of cost of equity for Tiago Ltd?

   (a) 12.99%

   (b) 11.99%

   (c) 13.99%

   (d) 14.99%

2. Which of the following is the most accurate measure of issue price of debentures?

   (a) 100

   (b) 96

   (c) 90.58

   (d) 95.88

3. Which of the following is the best estimate of cost of debentures to be issued by the company? (Using approximation method)

   (a) 7.64%

   (b) 6.74%

   (c) 4.64%

   (d) 5.78%

4. Calculate the cost of preference shares using approximation method

   (a) 10.23%

   (b) 11.22%

   (c) 12.12%

   (d) 12.22%

5. Which of the following best represents the overall cost of marginal capital to be raised?

   (a) 11.76%

   (b) 17.16%

   (c) 16.17%

   (d) 16.71% **(5 x 2 = 10 Marks)**

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2. Ranu & Co. has issued 10% debenture of face value 100 for ₹ 10 lakh. The debenture is expected to be sold at 5% discount. It will also involve floatation costs of ₹ 10 per debenture. The debentures are redeemable at a premium of 10% after 10 years. Calculate the cost of debenture if the tax rate is 30%.

   (a) 8.97%

   (b) 9.56%

   (c) 8.25%

   (d) 10.12% **(2 Marks)**

3. Given Data: Sales is ₹ 10,00,000, Break even sales is ₹ 6,00,000.

   What is the Degree of operating leverage?

   (a) 3

   (b) 2

   (c) 2.5

   (d) 2.2 **(2 Marks)**

4. A project requires an initial investment of ₹ 20,000 and it would give annual cash inflow of ₹ 4,000. The useful life of the project is estimated to be 10 years. What is payback reciprocal/Approximated IRR?

   (a) 20%

   (b) 15%

   (c) 25%

   (d) 12% **(1 Mark)**

PART II – Descriptive Questions (35 Marks)

*Question No. **1** is compulsory.*

*Attempt any **two** questions out of the remaining **three** questions.*

1. (a) The below information for Lever Ltd is provided on annual basis:

	₹
Sales at 3 months credit	48,00,000
Materials consumed (suppliers extend 2 months credit)	12,00,000
Wages paid (one month lag in payment)	9,60,000
Cash manufacturing expenses (paid on month in arrear)	12,00,000
Administrative expense (one month lag in payment)	3,60,000
Sales promotion expense (paid monthly in advance)	1,20,000

The Company sells its products at a gross profit of 20%.

The Company keeps two months stock of raw materials and two months stock of finished goods.

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Depreciation is considered as a part of cost of production.

Cash balance is retained at ₹ 1,00,000,

Assuming a 15% margin, COMPUTE the working capital requirements of the Company on cash cost basis. Ignore work-in progress.

(5 Marks)

(b) SOC Ltd has 10 lakh equity shares outstanding at the beginning of the accounting year 2024. The existing market price per share is Rs 600. Expected dividend is Rs 40 per share. The rate of capitalization appropriate to the risk class to which the company belongs is 20%.

(i) CALCULATE the market price per share by the end of the year when expected dividends are: (a) declared, and (b) not declared, based on the Miller – Modigliani approach.

(ii) CALCULATE the number of shares to be issued by the company at the end of the accounting year on the assumption that the net income for the year is Rs 15 crore; investment budget is Rs 20 crores, when (a) Dividends are declared, and (b) Dividends are not declared.

(iii) PROVE that the market value of the shares at the end of the accounting year will remain unchanged irrespective of whether (a) Dividends are declared, or (ii) Dividends are not declared.

(5 Marks)

(c) An existing profitable company, RMC World Ltd. is considering a new project for manufacture of home automation gadget involving a capital expenditure of ₹ 1000 Lakhs and working capital of ₹ 150 Lakhs. The capacity of the plants for an annual production of 3 lakh units and capacity utilization during 5 year life of the project is expected to be as indicated below:

Year	1	2	3	4	5
Capacity Utilization (%)	50	65	80	100	100

The average price per unit of product is expected to be ₹600 netting a contribution of 60 percent. The annual fixed costs, excluding depreciation, are estimated to be ₹500 Lakhs per annum from the third year onwards. For the first and second year, it would be ₹ 200 lakhs and ₹ 350 lakhs respectively.

Scrap value of the capital asset at the end of 5th year is ₹ 200 Lakhs. Depreciation on capital asset is provided on written down value basis @ 40% p.a. for income tax purpose. The rate of income tax may be taken at 30%. The cost of capital is 12%. At end of the third year an additional investment of ₹ 200 lakhs would be required for working capital. There is no capital gain tax applicable.

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COMPUTE the NPV of the project. RMC World Ltd. is about to make a presentation to Secure Venture Capital Firm. Secure Venture Capital Firms will invest in any project if the net addition to shareholder wealth from the project is above ₹ 100 lakhs. **(5 Marks)**

2. (a) From the following PREPARE Income statement of company P and Q.

	P	Q
No. of Equity Shares	1,00,000	70,000
Financial leverage	3 : 1	4 : 1
Operating Leverage	2 : 1	3 : 1
Variable cost to sales	67%	50%
Interest	₹ 5,50,000	₹ 6,00,000
Income tax rate	30%	30%

Also CALCULATE EPS of the company. **(4 Marks)**

(b) The GT Limited is willing to expand its business for which it requires an additional finance of ₹ 50,00,000. At present, the capital structure of the company is as under:

- 7,00,000 Equity shares of ₹ 10 each
- 10% Debentures ₹ 63,00,000
- 12% Term loan ₹ 54,00,000
- Retained earnings ₹ 1,30,00,000

At present, the company's EBIT is ₹ 54,00,000. However, the company, after expansion, expects ROI 2% greater than the present ROI, Income Tax Rate is 30%.

Following two options, for getting additional finance, are available-

(a) To raise funds as term loan @ 12%

(b) To raise funds by issuing 1,00,000 equity shares at ₹ 20 per share and balance by issuing 11% debentures at par.

Required:

(i) FIND out the market price of shares, if the P/E ratio is 10.

(ii) RECOMMEND the suitable option of raising funds with reason.

(6 Marks)

3. (a) EOC Ltd is a listed company and has presented the below abridged financial statements below.

Statement of Profit and Loss	**₹**	**₹**
Sales		1,25,00,000
Cost of goods sold		(76,40,000)
Gross Profit		48,60,000

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Less: Operating Expenses		
Administrative Expenses	13,20,000	
Selling and Distribution Expenses	15,90,000	(29,10,000)
Operating Profit		19,50,000
Add: Non Operating Income		3,28,000
Less: Non Operating Expenses		(1,27,000)
Profit before Interest and taxes		21,51,000
Less: Interest		(4,39,000)
Profit before tax		17,12,000
Less: Taxes		(4,28,000)
Profit after Tax		12,84,000

Balance Sheet

Sources of Funds	₹	₹
Owned Funds		
Equity Share Capital	30,00,000	
Reserves and Surplus	18,00,000	48,00,000
Borrowed Funds		
Secured Loan	10,00,000	
Unsecured Loan	4,30,000	14,30,000
Total Funds Raised		**62,30,000**
Application of Funds		
Non-Current Assets		
Building	7,50,000	
Machinery	2,30,000	
Furniture	7,60,000	
Intangible Assets	50,000	17,90,000
Current Assets		
Inventory	38,60,000	
Receivables	39,97,000	
ST investments	3,00,000	
Cash and Bank	2,30,000	83,87,000
Less: Current Liabilities		
Creditors	25,67,000	
ST loans	13,80,000	(39,47,000)
Total Funds Employed		**62,30,000**

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The company has set certain standards for the upcoming year financial status.

All the ratios are based on closing figures in financial statements.

Equity SC to Reserves=	1	
Net Profit Ratio=	15%	
Gross Profit Ratio=	50%	
Long Term Debt to Equity=	0.5	
Debtor Turnover=	100	Days
Creditor Turnover (based on COGS)=	100	Days
Inventory=	70%	of Opening inventory

Cash Balance is assumed to remain same for next year

You are required to -

(1) CALCULATE inventory turnover ratio in days for current year

(2) CALCULATE receivables turnover ratio in days for current year

(3) CALCULATE the projected receivables, inventory, payables and long term debt **(8 Marks)**

(b) NAME the various financial instruments dealt with in the International market. **(2 Marks)**

4. (a) WRITE short notes on Inter relationship between investment, financing and dividend decisions. **(4 Marks)**

(b) DISCUSS the liquidity vs. profitability issue in management of working capital. **(4 Marks)**

(c) EXPLAIN the concept of discounted payback period. **(2 Marks)**

OR

(c) EXPLAIN the concept of Indian depository receipts. **(2 Marks)**

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INTERMEDIATE COURSE: GROUP II

PAPER 6B: STRATEGIC MANAGEMENT

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 (15 Marks)

Question 1.(A) (Compulsory)

1. (A) Café Delight, a thriving restaurant chain known for its unique blend of Australian and Indian culinary experiences, embarked on a remarkable journey from its humble beginnings as a small café in Australia to becoming a renowned player in the Indian restaurant industry. This case study digs into the strategic decisions and market dynamics that fueled Café Delight's growth, highlighting its transition from a single café in Powai, Mumbai, to a flourishing chain with a presence in five cities and over 25 stores. It explores how Café Delight effectively leveraged social media and adapted its pricing strategy to compete with global brands while maintaining a healthy profit margin.

In 2005, Café Delight was founded in Melbourne, Australia, by a passionate entrepreneur with a vision to bring the flavors of Australia and India together. The first café established in Powai, Mumbai, received accolades for its unique menu, blending Australian coffee culture with Indian culinary traditions. Over the course of five years, Café Delight expanded to three stores in Mumbai, driven by exceptional mouth publicity, customer loyalty, and consistent quality.

As the social media landscape evolved, Café Delight recognized the power of online platforms in reaching a wider audience. By effectively utilizing social media and online marketing, Café Delight expanded its presence to five cities across India and established over 25 stores. Customer engagement through social media platforms enabled the brand to create a strong and vibrant community, driving organic growth.

Café Delight's customer-centric approach involved continuously evolving its menu to cater to the changing tastes and dietary preferences of its patrons. By understanding the evolving needs of its customers, Café Delight could offer personalized menu items, seasonal specials, and dietary alternatives. This approach created a sense of loyalty and engagement among customers, strengthening the brand's appeal. Not just customers but High-power, low-interest stakeholders, including regulatory authorities, were addressed with careful compliance and adherence to industry standards. Low-power, high-interest stakeholders, like potential customers and local communities, were engaged through

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targeted marketing campaigns and community involvement initiatives. This meticulous stakeholder analysis allowed Café Delight to build and maintain strong relationships with each group, effectively managing their influence and impact on the brand.

With its expanding presence and increasing popularity, Café Delight underwent a shift in its pricing strategy. It transitioned from a pocket-friendly pricing model to a skimming strategy, capitalizing on its unique blend of Australian and Indian flavors to position itself as a premium restaurant. Café Delight faced stiff competition from global brands entering the Indian market but maintained a profit margin of approximately 30% through menu engineering and targeted pricing.

In one of its kind, using strategic tools enabled Café Delight to identify and act on opportunities while mitigating threats, contributing to its long-term success in the highly competitive restaurant industry.

Based on the above Case Scenario, answer the Multiple-Choice Questions.

(i) Café Delight effectively leveraged social media and adapted its pricing strategy as it stepped into which phase of business life cycle of operations?

(a) Introduction Stage

(b) Growth Stage

(c) Maturity Stage

(d) Decline Stage **(2 Marks)**

(ii) What stakeholder group did Café Delight engage through targeted marketing campaigns and community involvement initiatives?

(a) High-power, high-interest stakeholders

(b) Low-power, low-interest stakeholders

(c) Low-power, high-interest stakeholders

(d) High-power, low-interest stakeholders **(2 Marks)**

(iii) What best describes Café Delight's initial expansion strategy when it expanded from one café to three in Mumbai?

(a) Aggressive price reduction

(b) Leveraging customer loyalty and word-of-mouth publicity

(c) Extensive online marketing

(d) Embracing global branding strategies **(2 Marks)**

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(iv) At which level of strategic management does Café Delight's transition from a pocket-friendly pricing model to a skimming strategy fit?

(a) Corporate level

(b) Business level

(c) Functional level

(d) Operational level **(2 Marks)**

(v) What type of strategy did Café Delight use to differentiate itself from competitors in the Indian restaurant industry?

(a) Cost leadership strategy

(b) Focused differentiation strategy

(c) Cost focus strategy

(d) Hybrid strategy **(2 Marks)**

(B) Compulsory Application Based Independent MCQs

(i) Shamita joined GlobalX Consulting firm as an Analyst in financial fraud mitigation. In her very first assignment she faced an integrity dilemma where her subordinates had missed calling out a potential financial risk which could impact the overall fraud rating of the organisation. She quickly reached out to her seniors who appreciated her diligence and immediately reported the same to senior management. In this scenario which element, soft or hard, is acting in favor of GlobalX?

(a) Strategy

(b) Systems

(c) Shared Value

(d) Staff **(2 Marks)**

(ii) Chocopo, an ice cream company run by Shri Shyam Kumar since 1985, now had its management change to his two daughters, who came in and wanted to experiment with a lot of flavors. They introduced 21 new flavors in a span of 6 months while not losing out of 2 legendary flavors of their dad i.e. Stick Kulfi and Mango Bar. After year 1 of operations, 9 out of the 21 flavors had to be stopped, while 10 flavors were still kept, extending the experimentation. The early sense from market was that they would have to be stopped too, but the sisters decided to extend their timelines. What category as per BCG Matrix would the 10 flavors fall into?

(a) Cash Cow

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(b) Dog

(c) Question Mark

(d) Star **(2 Marks)**

(iii) A company negotiating the best prices and quality from its suppliers to add to customer's delight is an example of?

(a) Value Creation by improving primary activity

(b) Value Creation by improving support activity

(c) Competitive Advantage Creation

(d) Stakeholder Management **(1 Mark)**

PART II – Descriptive Questions (35 Marks)

*Question No. **1** is compulsory.*

*Attempt any **two** questions out of the remaining **three** questions.*

1. (a) ABC retail chain regularly monitors consumer trends and supply chain flexibility. The retail chain tracks consumer trends to adjust its offerings, ensuring they meet customer needs. Simultaneously, it maintains a flexible supply chain to respond swiftly to demand fluctuations. This strategy enables ABC retail chain to anticipate market shifts and adapt to them effectively, ensuring its competitiveness and customer satisfaction. Which type of strategy is the retail chain employing?

(5 Marks)

(b) A Mumbai-based conglomerate, PQR Ltd., has announced a major restructuring of its business operations. The company has decided to split its business into four separate units: Manufacturing, Retail, Services, and Technology. Each unit will operate as a separate business, with delegated responsibility for day-to-day operations and strategy to the respective unit managers. Identify the organization structure that PQR Ltd. has planned to implement. Discuss any four attributes and the benefits the firm may derive by using this organization structure. **(5 Marks)**

(c) *GreenThrift Inc.,* a sustainable clothing retailer, is experiencing a surge in popularity due to the growing awareness of environmental issues among consumers. The company specializes in selling second-hand clothing and upcycled garments, offering an eco-friendly alternative to traditional fast fashion.

A major concern for GreenThrift Inc. is the emergence of new sustainable fashion brands in the market. These brands focus on using organic and recycled materials, as well as ethical manufacturing practices, which align with the values of environmentally conscious consumers.

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Identify and explain that competition from new sustainable fashion brands falls under which category of Porter's Five Forces Model for Competitive Analysis? **(5 Marks)**

2. (a) *"*Each organization must build its competitive advantage keeping in mind the business warfare. This can be done by following the process of strategic management." Considering this statement, explain major benefits of strategic management. **(5 Marks)**

   (b) *Reshuffle Corp* is a company that manufactures and sells office furniture. They offer a range of products, from desks and chairs to cabinets and shelves. Recently, the company has been facing increased competition from online retailers offering similar products at lower prices.

   Analyzing the characteristics of products in the furniture industry, discuss how *Reshuffle Corp* can differentiate its products to maintain a competitive edge in the market. **(5 Marks)**

3. (a) *EasyLife Corporation,* a leading manufacturer of consumer electronics, is considering launching a new line of smart home devices. As a strategic manager, conduct a SWOT analysis for *EasyLife Corporation* to assess the feasibility and potential success of this new venture. Consider both internal and external factors that could impact the success of the new product line. **(5 Marks)**

   (b) Explain the concept of forward and backward linkages between strategy formulation and implementation in strategic management, using relevant examples. How do these linkages impact the overall strategic decision-making process of an organization? **(5 Marks)**

4. (a) Define Strategic Performance Measures (SPM). Explain various types of strategic performance measures. **(5 Marks)**

   (b) *StarTech Solutions*, an aerospace technology firm, operates in a highly competitive industry. Despite the fierce competition in the aerospace sector, *StarTech* has carved out a niche for itself by focusing on serving unique, high-end clients. Unlike its competitors, *StarTech* has chosen not to diversify its target market and instead specializes in providing cutting-edge solutions to this niche market.

   Identify and explain the strategy adopted by *StarTech Solutions*. Discuss the advantages and disadvantages of this strategy.

   OR

   Strategic alliances are formed if they provide an advantage to all the parties in the alliance. Do you agree? Explain in brief the advantages of a strategic alliance. **(5 Marks)**

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Mock Test Paper - Series II: April, 2024

Date of Paper: 15 April, 2024

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

INTERMEDIATE: GROUP – II

PAPER – 6: FINANCIAL MANAGEMENT & STRATEGIC MANAGEMENT

PAPER 6A : FINANCIAL MANAGEMENT

Suggested Answers/ Hints

PART I – Case Scenario based MCQs

1. 1. (d) 14.99%

B = retention ratio=0.6, r=return on equity=20%, DPS=D0=20 x 0.4= 8,

MPS = P0 = EPS x PE = 20 x 15=300

G = b.r =0.6 x 20% = 12%

D1 = D0(1+g) = 8 (1.12) = 8.96

Ke = D1/P0 + g = 8.96/300 + 0.12 = 14.99%

2. (c) 90.58

Price of debentures= PV of future cash flows for investor discounted at their yield

= 8 x PVAF(9.5%,10 years)+ 100 x PVF(9.5%, 10 years)

= 8 x 6.2788 + 100 x 0.4035

=50.2304 + 40.35

=90.58

3. (a) 7.64%

NP = 90.58 x 96%=86.96, RV= 100, Interest=8, t=0.27, n= 10

$$Kd = \frac{Int(1-t)+(RV-NP)/n}{(RV+NP)/2}$$

$$= \frac{8(1-0.27)+(100-86.96)/10}{(100+86.96)/2}$$

= 7.64%

4. (b) 11.22%

$$Kp = \frac{PD+(RV-NP)/n}{(RV+NP)/2}$$

$$= \frac{100+(1100-950)/10}{(1100+950)/2}$$

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= 11.22%

5. (a) 11.76%

	Existing	Total	Additional	
Equity Funds	1,60,00,000	2,00,00,000	40,00,000	
Preference Shares		24,00,000	24,00,000	
Debt		56,00,000	56,00,000	
	1,60,00,000	2,80,00,000	1,20,00,000	
Capital gearing =	0.4			
(PSC + Debt)/Equity =	0.4			
(Total Funds -Equity)/ Equity = 0.4				
(2.8 crores-Equity)/ equity = 0.4				
Equity =	2 crores			
Weighted avg cost of marginal capital		**Weights**	**Cost**	**W.C**
Equity Funds	40,00,000	0.333333333	14.99%	5.00%
Preference Shares	24,00,000	0.2	11.22%	1.53%
Debt	56,00,000	0.466666667	7.64%	5.24%
Total	**1,20,00,000**			**11.76%**

2. (a) 8.97%

$$K_d = \frac{[I + \frac{1}{n}(RP - NP)](1 - t)}{1/2(RP + NP)}$$

$$K_d = \frac{[10 + \frac{1}{10}(110 - 85)](1 - 0.30)}{1/2(110 + 85)}$$

= 8.75/97.5 = 8.97%

3. (c) 2.5

Margin of safety = (sales – BEP sales)/sales x 100

= 40%

Degree of operating leverage = 1/MOS

= 1/40% = 2.5

4. (a) 20%

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$$\text{Payback Reciprocal} = \frac{\text{Average annual cash in flow}}{\text{Initial investment}}$$

$$= \frac{₹\ 4,000 \times 100}{₹\ 20,000} = 20\%$$

PART II – Descriptive Questions

1. (a) (i) Working Notes:

(i) Computation of Annual Cash Cost of Production	**(₹)**
Material consumed	12,00,000
Wages	9,60,000
Manufacturing expenses	12,00,000
Total cash cost of production	**33,60,000**
(ii) Computation of Annual Cash Cost of Sales:	**(₹)**
Total Cash cost of production as in (i) above	33,60,000
Administrative Expenses	3,60,000
Sales promotion expenses	1,20,000
Total cash cost of sales	**38,40,000**
Add: Gross Profit @ 20% on sales (25% on cost of sales)	9,60,000
Sales Value	**48,00,000**

Statement of Working Capital requirements (cash cost basis)

	(₹)	**(₹)**
A. Current Assets		
Inventory:		
- Raw materials $\left(\frac{₹\ 12,00,000}{12\text{ months}} \times 2\text{ months}\right)$	2,00,000	
- Finished Goods $\left(\frac{₹\ 33,60,000}{12\text{ months}} \times 2\text{ months}\right)$	5,60,000	
Receivables (Debtors) $\left(\frac{₹\ 38,40,000}{12\text{ months}} \times 3\text{ months}\right)$	9,60,000	
Sales Promotion expenses paid in advance $\left(\frac{₹1,20,000}{12\text{ months}} \times 1\text{ month}\right)$	10,000	
Cash balance	1,00,000	18,30,000

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Gross Working Capital		18,30,000
B. Current Liabilities:		
Payables:		
- Creditors for materials $\left(\frac{₹\,12,00,000}{12\,months} \times 2\ months\right)$	2,00,000	
Wages outstanding $\left(\frac{₹\,9,60,000}{12\,months} \times 1\ month\right)$	80,000	
Manufacturing expenses outstanding $\left(\frac{₹\,12,00,000}{12\,months} \times 1\ month\right)$	1,00,000	
Administrative expenses outstanding $\left(\frac{₹\,3,60,000}{12\,months} \times 1\ month\right)$	30,000	4,10,000
Net working capital (A - B)		14,20,000
Add: Safety margin @ 15%		2,13,000
Total Working Capital requirements		16,33,000

(b) (i) Calculation of market price per share

According to Miller – Modigliani (MM) Approach:

$$P_o = \frac{P_1 + D_1}{1 + K_e}$$

Where,

Existing market price (P_o) = ₹ 600

Expected dividend per share (D_1) = ₹ 40

Capitalization rate (k_e) = 0.20

Market price at year end (P_1) = ?

a. If expected dividends are declared, then

600=(P1+40)/(1+0.2)

600 x 1.2 = P1+40

P1 = 680

b. If expected dividends are not declared, then

600 = (P1+0)/(1 + 0.2)

600 x 1.2 = P1

P1= 720

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(ii) Calculation of number of shares to be issued

	(a)	(b)
	Dividends are declared (₹ lakh)	Dividends are not Declared (₹ lakh)
Net income	1500	1500
Total dividends	(400)	-
Retained earnings	1100	1500
Investment budget	2000	2000
Amount to be raised by new issues	900	500
Relevant market price (₹ per share)	680	720
No. of new shares to be issued (in lakh) (₹ 900 ÷ 680; ₹ 500 ÷ 720)	1.3235	0.6944

(iii) Calculation of market value of the shares

	(a)	(b)
Particulars	**Dividends are declared**	**Dividends are not Declared**
Existing shares (in lakhs)	10.00	10.00
New shares (in lakhs)	1.3235	0.6944
Total shares (in lakhs)	11.3235	10.6944
Market price per share (₹)	680	720
Total market value of shares at the end of the year (₹ in lakh)	11.3235 × 680 = 7,700 (approx.)	10.6944 × 720 = 7,700 (approx.)

Hence, it is proved that the total market value of shares remains unchanged irrespective of whether dividends are declared, or not declared.

(c) Calculation of Cash Flow after Tax

	Year 1	Year 2	Year 3	Year 4	Year 5
Capacity	50%	65%	80%	100%	100%
Units	1,50,000	1,95,000	2,40,000	3,00,000	3,00,000
Contribution p.u.	360	360	360	360	360
(600 x 60%)					
Total Contribution	5,40,00,000	7,02,00,000	8,64,00,000	10,80,00,000	10,80,00,000
Less: Fixed Asset	2,00,00,000	3,50,00,000	5,00,00,000	5,00,00,000	5,00,00,000
Less: Depreciation (W.N.)	4,00,00,000	2,40,00,000	1,44,00,000	86,40,000	51,84,000

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PBT	(60,00,000)	1,12,00,000	2,20,00,000	4,93,60,000	5,28,16,000
Less: Tax	(18,00,000)	33,60,000	66,00,000	1,48,08,000	1,58,44,800
PAT	(42,00,000)	78,40,000	1,54,00,000	3,45,52,000	3,69,71,200
Add: Depreciation	4,00,00,000	2,40,00,000	1,44,00,000	86,40,000	51,84,000
CFAT	3,58,00,000	3,18,40,000	2,98,00,000	4,31,92,000	4,21,55,200

Calculation of NPV

Year	Description	Cash Flow	PVF @12%	PV
0	Initial Investment	(10,00,00,000)	1	(10,00,00,000)
0	WC introduced	(1,50,00,000)	1	(1,50,00,000)
3	WC introduced	(2,00,00,000)	0.7118	(1,42,36,000)
1	CFAT	3,58,00,000	0.8929	3,19,65,820
2	CFAT	3,18,40,000	0.7972	2,53,82,848
3	CFAT	2,98,00,000	0.7118	2,12,11,640
4	CFAT	4,31,92,000	0.6355	2,74,48,516
5	CFAT	4,21,55,200	0.5674	2,39,18,860
5	WC released	3,50,00,000	0.5674	1,98,59,000
5	Scrap Sale	2,00,00,000	0.5674	1,13,48,000
	Net Present Value			**3,18,98,684**

Working Notes (W.N.)

Calculation of Depreciation

Year	Opening WDV	Depreciation	Closing WDV
1	10,00,00,000	4,00,00,000	6,00,00,000
2	6,00,00,000	2,40,00,000	3,60,00,000
3	3,60,00,000	1,44,00,000	2,16,00,000
4	2,16,00,000	86,40,000	1,29,60,000
5	1,29,60,000	51,84,000	77,76,000

2. (a) Income statement

	Particulars	P	Q
		(₹)	(₹)
	Sales	50,00,000	48,00,000
(–)	Variable Cost	33,50,000	24,00,000
	Contribution	16,50,000	24,00,000
	Fixed Cost	8,25,000	16,00,000
	EBIT	8,25,000	8,00,000
(–)	Interest	5,50,000	6,00,000
	EBT	2,75,000	2,00,000

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(–)	Tax	82,500	60,000
	EAT	1,92,500	1,40,000
(÷)	No. of Shares	1,00,000	70,000
	EPS	**₹ 1.93**	**₹ 2.00**

Working Note :

1. Financial Leverage	=	EBIT / EBT	=	EBIT / (EBIT – Int.)
Let the EBIT be X				
	P		**Q**	
	3 = X/(X – 5,50,000) 3(X – 5,50,000) = X 3X – 16,50,000 = X 2X = 16,50,000		4 = X/(X – 6,00,000) 4(X – 6,00,000) = X 4X – 24,00,000 = X 3X = 24,00,000	
	X = 8,25,000		**X = 8,00,000**	
2. Operating Leverage	=	Contribution/EBIT		
Let the Contribution be X				
	P		**Q**	
	2 = X/8,25,000		3= X/8,00,000	
	X = 16,50,000		**X = 24,00,000**	

3. Sales

Let the Sales be 100

Sales – Variable Cost = Contribution

	P		Q
Contribution =	100 – 67	=	100 – 50
=	33	=	50
Sales =			
	P		**Q**
For 33	= 16,50,000	For 50	= 24,00,000
For 100	**= 50,00,000**	For 100	**= 48,00,000**

(b) Expected return on capital employed

Capital Employed = Debt + Equity

= (₹ 63,00,000 + ₹ 54,00,000) + (₹ 70,00,000 + ₹ 1,30,00,000)

= ₹ 3,17,00,000

Return on capital employed/ROI = $\left(\frac{\text{EBIT}}{\text{Capital employed}}\right)$ x 100

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At present:

$$= \left(\frac{54,00,000}{3,17,00,000}\right) \times 100$$

= 17.03%

Now company expects 2% more as ROI

So, Expected ROI = 17.03% + 2%

= 19.03%

Proposed EBIT = Proposed Capital Employed x Return on capital employed

= (₹ 3,17,00,000 + ₹ 50,00,000) x 19.03% = ₹ 69,84,010

(i) Market Price per Share:

Particular	Financial Options	
	Option – I 12% term loan of ₹ 50,00,000	**Option II 1,00,000 equity shares @ ₹ 20 and 11% debentures of ₹ 30,00,000**
	(₹)	**(₹)**
EBIT	69,84,010	69,84,010
Less: Interest		
- 10% on old debentures	6,30,000	6,30,000
- 11% on new debentures	-	3,30,000
- 12% on old term loan	6,48,000	6,48,000
- 12% on new term loan	6,00,000	
Total Interest	18,78,000	16,08,000
EBT	51,06,010	53,76,010
Less Tax @ 30%	15,31,803	16,12,803
EAT	35,74,207	37,63,207
No. of equity shares	7,00,000	8,00,000
Earnings per share	**5.11**	**4.70**
P/E ratio	10	10
Market Price per Share = EPS x P/E ratio	**51.06**	**47.04**

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(ii) Recommendation:

The option I is better and may be opted as both EPS and MPS are higher.

3. (a) Inventory Turnover = $\frac{\text{Inventory}}{\text{COGS}} \times 365 = \frac{38,60,000 \times 365}{76,40,000} = 184.41$ days = 185 days (apx)

Receivables Turnover = $\frac{\text{Receivables}}{\text{Sales}} \times 365 = \frac{39,97,000 \times 365}{1,25,00,000} = 116.71$ = 117 days (apx)

Equity to Reserves = 1

Reserves = 1 x 30,00,000 = 30,00,000

Projected profit = 30,00,000 - 18,00,000 = 12,00,000

Net Profit Margin = 15%

12,00,000/ Sales = 0.15

Sales = 80,00,000

Gross Profit = 80,00,000 x 50% = 40,00,000

COGS = 80,00,000 - 40,00,000 = 40,00,000

Projected Debtors Turnover = 100 days = $\frac{\text{Closing Receivables}}{\text{Sales}} \times 365$

$$100 = \frac{\text{Closing Receivables}}{80,00,000} \times 365$$

$$\text{Closing Receivables} = \frac{80,00,000 \times 100}{365} = 21,91,781$$

Projected Closing Inventory = 70% of opening inventory = 70% of 38,60,000 = 27,02,000

Projected Creditor Turnover= 100 days = $\frac{\text{Closing Creditors}}{\text{COGS}} \times 365$

$$\text{Closing Creditors} = \frac{\text{COGS}}{365} \times 100$$

$$\text{Closing Creditor} = \frac{40,00,000}{365} \times 100 = 10,95,890$$

Equity Share Capital + Reserves = 30,00,000 + 30,00,000 = 60,00,000

Long Term Debt to Equity = 0.5

$$\frac{\text{LTD}}{60,00,000} = 0.5$$

Long Term Debt = 0.5 x 60,00,000

Long Term Debt = 30,00,000

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(b) Financial Instruments in the International Market

Some of the various financial instruments dealt with in the international market are:

(a) Euro Bonds

(b) Foreign Bonds

(c) Fully Hedged Bonds

(d) Medium Term Notes

(e) Floating Rate Notes

(f) External Commercial Borrowings

(g) Foreign Currency Futures

(h) Foreign Currency Option

(i) Euro Commercial Papers.

4. (a) Inter-relationship between Investment, Financing and Dividend Decisions: The finance functions are divided into three major decisions, viz., investment, financing and dividend decisions. It is correct to say that these decisions are inter-related because the underlying objective of these three decisions is the same, i.e. maximisation of shareholders' wealth. Since investment, financing and dividend decisions are all interrelated, one has to consider the joint impact of these decisions on the market price of the company's shares and these decisions should also be solved jointly. The decision to invest in a new project needs the finance for the investment. The financing decision, in turn, is influenced by and influences dividend decision because retained earnings used in internal financing deprive shareholders of their dividends. An efficient financial management can ensure optimal joint decisions. This is possible by evaluating each decision in relation to its effect on the shareholders' wealth.

The above three decisions are briefly examined below in the light of their inter-relationship and to see how they can help in maximising the shareholders' wealth i.e. market price of the company's shares.

***Investment decision**:* The investment of long term funds is made after a careful assessment of the various projects through capital budgeting and uncertainty analysis. However, only that investment proposal is to be accepted which is expected to yield at least so much return as is adequate to meet its cost of financing. This have an influence on the profitability of the company and ultimately on its wealth.

***Financing decision**:* Funds can be raised from various sources. Each source of funds involves different issues. The finance manager has to maintain a proper balance between long-term and short-term funds. With the total volume of long-term funds, he has to ensure a proper mix of loan funds and owner's funds. The optimum financing mix will increase return to equity shareholders and thus maximise their wealth.

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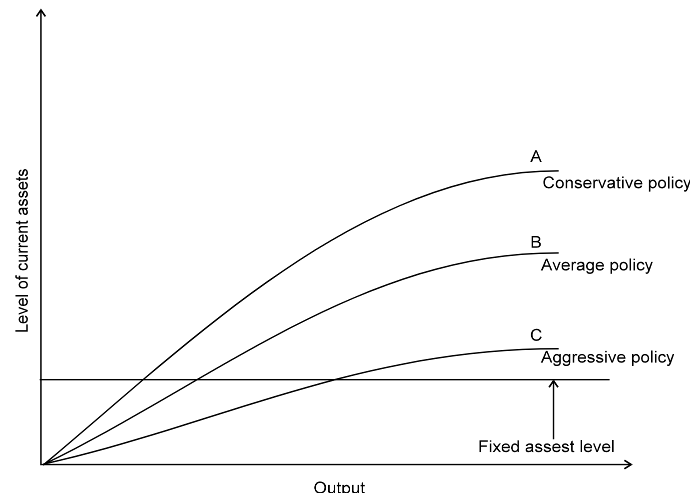
Dividend decision: The finance manager is also concerned with the decision to pay or declare dividend. He assists the top management in deciding as to what portion of the profit should be paid to the shareholders by way of dividends and what portion should be retained in the business. An optimal dividend pay-out ratio maximises shareholders' wealth.

The above discussion makes it clear that investment, financing and dividend decisions are interrelated and are to be taken jointly keeping in view their joint effect on the shareholders' wealth.

(b) Liquidity versus Profitability Issue in Management of Working Capital

Working capital management entails the control and monitoring of all components of working capital i.e. cash, marketable securities, debtors, creditors etc. Finance manager has to pay particular attention to the levels of current assets and their financing. To decide the level of financing of current assets, the risk return trade off must be taken into account. The level of current assets can be measured by creating a relationship between current assets and fixed assets. A firm may follow a conservative, aggressive or moderate policy.



A conservative policy means lower return and risk while an aggressive policy produces higher return and risk. The two important aims of the working capital management are profitability and solvency. A liquid firm has less risk of insolvency i.e. it will hardly experience a cash shortage or a stock out situation. However, there is a cost associated with maintaining a sound liquidity position. So, to have a higher profitability the firm may have to sacrifice solvency and maintain a relatively low level of current assets.

(c) Concept of Discounted Payback Period

Payback period is time taken to recover the original investment from project cash flows. It is also termed as break even period. The focus of the analysis is on liquidity aspect and it suffers from the limitation of ignoring time value of money and profitability. Discounted payback

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period considers present value of cash flows, discounted at company's cost of capital to estimate breakeven period i.e. it is that period in which future discounted cash flows equal the initial outflow. The shorter the period, better it is. It also ignores post discounted payback period cash flows.

OR

(c) **Concept of Indian Depository Receipts:** The concept of the depository receipt mechanism which is used to raise funds in foreign currency has been applied in the Indian capital market through the issue of Indian Depository Receipts (IDRs). Foreign companies can issue IDRs to raise funds from Indian market on the same lines as an Indian company uses ADRs/GDRs to raise foreign capital. The IDRs are listed and traded in India in the same way as other Indian securities are traded.

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INTERMEDIATE COURSE: GROUP II

PAPER 6B: STRATEGIC MANAGEMENT

ANSWERS

PART I - Case Scenario based MCQs

1. (A) (i) (b) (ii) (c) (iii) (b) (iv) (b) (v) (b)

(B) (i) (c) (ii) (b) (iii) (b)

PART II - Descriptive Questions

1. (a) The retail chain is employing a strategy that combines both proactive and reactive elements. Monitoring consumer trends and adjusting product offerings accordingly demonstrates a proactive approach to anticipate and meet customer needs. On the other hand, maintaining a flexible supply chain to respond quickly to changes in demand reflects a reactive strategy to address unforeseen shifts in the market.

This combination allows the retail chain to both anticipate future trends and react effectively to immediate market changes, making its strategy partly proactive and partly reactive. This dual strategy of proactive trend monitoring and reactive supply chain flexibility enables the retail chain to anticipate market shifts and adapt to them effectively, ensuring its competitiveness and customer satisfaction.

(b) PQR Ltd. has planned to implement the Strategic Business Unit (SBU) structure. Very large organisations, particularly those running into several products, or operating at distant geographical locations that are extremely diverse in terms of environmental factors, can be better managed by creating strategic business units. SBU structure becomes imperative in an organisation with increase in number, size and diversity.

The attributes of an SBU and the benefits a firm may derive by using the SBU Structure are as follows:

- A scientific method of grouping the businesses of a multi – business corporation which helps the firm in strategic planning.
- An improvement over the territorial grouping of businesses and strategic planning based on territorial units.
- Strategic planning for SBU is distinct from rest of businesses. Products/ businesses within an SBU receive same strategic planning treatment and priorities.
- Each SBU will have its own distinct set of competitors and its own distinct strategy.
- The CEO of SBU will be responsible for strategic planning for SBU and its profit performance.

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- Products/businesses that are related from the standpoint of function are assembled together as a distinct SBU.
- Unrelated products/ businesses in any group are separated into separate SBUs.
- Grouping the businesses on SBU lines helps in strategic planning by removing the vagueness and confusion.
- Each SBU is a separate business and will be distinct from one another on the basis of mission, objectives etc.

(c) Competition from new sustainable fashion brands falls under the "Threat of New Entrants" category of Porter's Five Forces Model for Competitive Analysis. These new entrants pose a threat to existing sustainable clothing retailers like *GreenThrift Inc.* by increasing competition and potentially eroding market share. The emergence of these brands, focusing on using organic and recycled materials along with ethical manufacturing practices, aligns with the values of environmentally conscious consumers, making them strong competitors in the sustainable fashion market.

2. (a) Each organization has to build its competitive advantage over the competitors in the business warfare in order to win. This can be done only by following the process of strategic management. Strategic Management is very important for the survival and growth of business organizations in dynamic business environments. Other major benefits of strategic management are as follows:

- Strategic management helps organizations to be more proactive rather than reactive in dealing with its future. It facilitates to work within vagaries of environment and remains adaptable with the turbulence or uncertain future. Therefore, they are able to control their own destiny in a better way.
- It provides better guidance to entire organization on the crucial point – what it is trying to do. Also provides frameworks for all major business decisions of an enterprise such as on businesses, products, markets, organizational structures, etc.
- It facilitates to prepare the organization to face the future and act as pathfinder to various business opportunities. Organizations are able to identify the available opportunities and identify ways and means as how to reach them.
- It serves as a corporate defence mechanism against mistakes and pitfalls. It helps organizations to avoid costly mistakes in product market choices or investments.

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- ♦ Over a period of time strategic management helps organization to evolve certain core competencies and competitive advantages that assist in the fight for survival and growth.

(b) To maintain a competitive edge in the face of increased competition, *Reshuffle Corp* can differentiate its products in several ways:

- **Tangible and Intangible Aspects:** *Reshuffle Corp* can focus on the tangible aspects of its products, such as using high-quality materials and innovative designs to create furniture that is both functional and aesthetically pleasing. Additionally, they can emphasize the intangible aspects of their products, such as excellent customer service and a strong brand reputation for reliability and durability.
- **Pricing Strategies:** While market prices are often dictated by competition, *Reshuffle Corp* can work on cost optimization to maintain profitability. They can also consider offering value-added services, such as free installation or extended warranties, to justify a higher price point.
- **Product Features:** By continually optimizing their product features based on customer feedback and market trends, *Reshuffle Corp* can ensure that their products deliver maximum satisfaction to their target customers. This may include features that enhance functionality, design, quality, and overall user experience.
- **Product Centric Approach:** *Reshuffle Corp* should keep their products at the center of their strategic activities, ensuring that all business processes, from production to sales and marketing, are aligned to meet customer needs and expectations.
- **Product Life Cycle Management:** *Reshuffle Corp* should be aware of the life cycle of their products and plan for reinvention or replacement accordingly. They can introduce new product lines or upgrade existing ones to keep up with changing customer preferences and market trends.

3. (a) SWOT Analysis for *EasyLife Corporation's* New Smart Home Devices Venture:

Strengths	**Weaknesses**
• Strong brand reputation in consumer electronics. • Established distribution network. • Access to technological expertise for product development.	• Limited experience in the smart home devices market. • May require additional investments in research and development.

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• Financial resources to support product launch and marketing.	• Potential challenges in integrating a new product line with existing offerings. • Lack of established customer base for smart home devices.
Opportunities • Growing market for smart home devices due to increasing consumer interest in home automation. • Possibility of partnering with existing smart home platform providers. • Potential to leverage brand loyalty from existing customers. • Ability to differentiate through innovative features and design.	**Threats** • Intense competition from established players in the smart home devices market. • Rapid technological advancements lead to short product life cycles. • Potential for cybersecurity threats in connected devices. • Economic factors impacting consumer spending on discretionary items.

The SWOT analysis highlights that while *EasyLife Corporation* has several strengths that can support the launch of a new smart home devices line, there are also significant weaknesses and threats to consider. To maximize the chances of success, *EasyLife Corporation* should focus on leveraging its brand reputation and distribution network while carefully addressing the weaknesses and threats identified. Additionally, staying informed about technological developments and consumer trends will be essential for maintaining competitiveness in the dynamic smart home devices market.

(b) The concept of forward and backward linkages between strategy formulation and implementation in strategic management highlights the interconnected nature of these two phases and their impact on the overall strategic decision-making process of an organization.

Forward Linkages: Forward linkages refer to the impact of strategy formulation on strategy implementation. When an organization formulates a new strategy or revises an existing one, it sets the direction for the organization's future actions. For example, if a company decides to expand its product line to target a new market segment, this decision will require changes in the organization's structure, resources allocation, and possibly its leadership style. These changes are necessary to align the organization's operations with the new strategic direction. Thus, the formulation of strategies has forward linkages with their implementation, as it sets the stage for how the strategy will be executed.

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Backward Linkages: Backward linkages, on the other hand, refer to the impact of implementation on strategy formulation. As an organization implements its strategies, it gains valuable insights and feedback from the implementation process. This feedback can influence future strategic decisions. For example, if a company faces unexpected challenges or discovers new opportunities during the implementation of a strategy, it may need to reevaluate its strategic choices. Similarly, past strategic actions and their outcomes can also influence the formulation of future strategies. Over time, these incremental changes in strategy and implementation take the organization from its current state to where it aims to be, reflecting the dynamic nature of strategic management.

In conclusion, the forward and backward linkages between strategy formulation and implementation highlight the iterative and interconnected nature of strategic management. By understanding and leveraging these linkages, organizations can enhance their strategic decision-making process and improve their overall performance.

4. (a) Strategic Performance Measures (SPM) are metrics used by organizations to evaluate and track the effectiveness of their strategies in achieving strategic goals and objectives. SPM provides a framework for measuring the performance of key areas critical to the success of the organization's strategy. These measures help in assessing whether the organization is progressing towards its desired outcomes and allow for adjustments to be made to improve performance.

Types of Strategic Performance Measures

There are various types of strategic performance measures, including:

- **Financial Measures**: Financial measures, such as revenue growth, return on investment (ROI), and profit margins, provide an understanding of the organization's financial performance and its ability to generate profit.
- **Customer Satisfaction Measures**: Customer measures, such as customer satisfaction, customer retention, and customer loyalty, provide insight into the organization's ability to meet customer needs and provide high-quality products and services.
- **Market Measures**: Market measures, such as market share, customer acquisition, and customer referrals, provide information about the organization's competitiveness in the marketplace and its ability to attract and retain customers.
- **Employee Measures**: Employee measures, such as employee satisfaction, turnover rate, and employee engagement, provide insight into the organization's ability to attract and retain talented employees and create a positive work environment.

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- **Innovation Measures:** Innovation measures, such as research and development (R&D) spending, patent applications, and new product launches, provide insight into the organization's ability to innovate and create new products and services that meet customer needs.

- **Environmental Measures:** Environmental measures, such as energy consumption, waste reduction, and carbon emissions, provide insight into the organization's impact on the environment and its efforts to operate in a sustainable manner.

(b) The strategy adopted by *StarTech Solutions* is Focused differentiation. This strategy involves targeting a specific segment of the market with unique products or services that are perceived as valuable by customers in that segment. By specializing in serving unique, high-end clients, *StarTech* is able to differentiate itself from competitors and create a competitive advantage.

Advantages of Focused Differentiation:

- **Strong Customer Loyalty:** By catering to a specific niche market, *StarTech* can build strong relationships with its customers, leading to higher customer loyalty and retention.

- **Higher Profit Margins:** Serving a niche market allows *StarTech* to command higher prices for its specialized products or services, leading to higher profit margins.

- **Reduced Competition:** By focusing on a niche market that other firms are not targeting, *StarTech* faces less competition, allowing it to establish itself as a leader in that segment.

- **Better Resource Allocation:** Focusing on a specific market segment allows *StarTech* to allocate its resources more efficiently, concentrating on areas that will provide the greatest return on investment.

Disadvantages of Focused Differentiation:

- **Limited Market Size:** The niche market that StarTech is targeting may be limited in size, restricting the company's potential for growth.

- **Risk of Market Changes:** Changes in the market or customer preferences could impact on the demand for *StarTech's* specialized products or services, leading to potential revenue loss.

- **Higher Costs:** Serving a niche market may require specialized resources and expertise, leading to higher costs of operation.

- **Imitation by Competitors:** If *StarTech's* success in the niche market attracts competitors, they may attempt to imitate its strategy, eroding its competitive advantage.

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Overall, the focused differentiation strategy adopted by *StarTech Solutions* has allowed it to differentiate itself in a competitive industry and build a strong position in the market. However, the company must be aware of the potential challenges and risks associated with this strategy and continue to innovate and adapt to maintain its competitive edge.

OR

Strategic alliances are formed if they provide an advantage to all the parties in the alliance. These advantages can be broadly categorised as follows:

(i) **Organizational:** Strategic alliances may be formed to learn necessary skills and obtain certain capabilities from the strategic partner. Strategic partners may also help to enhance productive capacity, provide a distribution system, or extend supply chain. A strategic partner may provide a good or service that complements each other, thereby creating a synergy. If one partner is relatively new or untried in a certain industry, having a strategic partner who is well-known and respected will help add legitimacy and creditability to the venture.

(ii) **Economic:** Alliances can reduce costs and risks by distributing them across the members of the alliance. Partners can obtain greater economies of scale in an alliance, as production volume increase, causing the cost per unit to decline. Finally, partners can take advantage of co-specialization, where specializations are bundled together, creating additional value.

(iii) **Strategic:** Organizations may join to cooperate instead of compete. Alliances may also create vertical integration where partners are part of supply chain. Strategic alliances may also be useful to create a competitive advantage by the pooling of resources and skills. This may also help with future business opportunities and the development of new products and technologies. Strategic alliances may also be used to get access to new technologies or to pursue joint research and development.

(iv) **Political:** Sometimes there is need to form a strategic alliance with a local foreign business to gain entry into a foreign market either because of local prejudices or legal barriers to entry. Forming strategic alliances with politically-influential partners may also help improve overall influence and position.

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Mock Test Paper - Series I: July, 2024

Date of Paper: 3rd August, 2024

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

INTERMEDIATE: GROUP – II

PAPER – 6A : FINANCIAL MANAGEMENT & STRATEGIC MANAGEMENT

PAPER 6A: FINANCIAL MANAGEMENT

Time Allowed – 3 Hours (Total time for 6A and 6B) Maximum Marks – 50

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.*
4. *Working note should form part of the answer. Wherever necessary, suitable assumptions may be made by the candidates and disclosed by way of note. However, in answers to Questions in Division A, working notes are not required.*

PART I – Case Scenario based MCQs (15 Marks)

Write the most appropriate answer to each of the following multiple choice questions by choosing one of the four options given. All questions are compulsory.

Kaivalyabodhi Limited **(KbL)** has completed 35 years of operations in India. It has many subsidiary & associate companies in more than 100 countries. KbL's business s include home and personal care, foods and beverages, and industrial, agricultural and other products. It is one of the largest producers of soaps and detergents in India. The company has grown organically as well as through acquisitions. Over the years, the company has built a diverse portfolio of powerful brands, some being household names.

It is planning to acquire one of its competitors named Prestige Limited, which would enhance the growth of 'KbL'. The consideration amount will be 1.5X of its average Market Capitalization. Prestige limited has 1,30,000 outstanding equity shares and its shares were traded at an average market price of ₹ 45 as on the valuation date. The consideration amount will be paid equally in 5 years where the first installment is to be paid immediately. Prestige Limited has Ko of 15%

KbL will raise the funds required through debt and equity in the ratio of 30:70. The company requires the cost of capital estimates for evaluating its acquisitions, investment decisions and the performance of its businesses.

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KbL's share price has grown from ₹ 150 to ₹ 301 in the last 5 years and it will continue to grow at the same rate. KbL pays dividends regularly. The company has recently paid a dividend of ₹ 8. For the calculation of equity, an average of 52 weeks high market price in the last 5 years is to be considered, which is as follows:

Yr 1	Yr 2	Yr 3	Yr 4	Yr 5
MPS 185	MPS 210	MPS 252	MPS 325	MPS 280

Ke calculated as per growth model holds a weight of 0.6.

The company also wishes to calculate the equity's expectation using CAPM which holds a weight of 0.4. The risk-free rate is assumed as the yield on long-term government bonds that the company regards as about 8%. KbL regards the market-risk premium to be equal to 11 per cent. Its estimation on the Beta is 0.78.

KbL will issue debentures with FV of ₹ 10,500 which is to be amortised equally over the life of 7 years. The company considers the effective rate of interest applicable to an 'AAA' rated company with a markup of 200 basis points as its coupon rate. It thinks that considering the trends over the years, 'AAA' rate is 7.5%.

Ignore taxation. Based on the above details, answer the question 1 to 5:

1. Calculate the cost of equity under both the methods

   (a) 11%, 16%

   (b) 18.65%, 10.34%

   (c) 18.65%, 16.58%

   (d) 16.5%, 9%

2. Calculate the overall cost of equity

   (a) 17.82%

   (b) 17.63%

   (c) 15.37%

   (d) 35.25%

3. Calculate the cost of debt, if the intrinsic value of debenture today is close to ₹ 9,740

   (a) 15%

   (b) 12%

   (c) 9.5%

   (d) 7.5%

4. Calculate the WACC & the amount of purchase consideration

   (a) 18%, ₹ 90,00,000

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(b) 15.21%, ₹ 87,75,000

(c) 16.07%, ₹ 87,75,000

(d) 15.94%, ₹ 58,50,000

5. Present Value of Purchase consideration is close to ₹

(a) 58,83,032

(b) 67,65,487

(c) 57,35,680

(d) 66,58,997 **(5 x 2 = 10 Marks)**

6. X ltd has actual Sales of ₹ 20 lakhs and its Break-even sales are at ₹ 15 lakhs. The degree of total risk involved in the company is 6.5. Calculate the % impact on EPS, if EBIT is affected by 12%.

(a) 40%

(b) 78%

(c) 312%

(d) 19.5% **(2 Marks)**

7. Assuming Ke = 11%, Kd = 8% and Ko = 10%, Debt Equity ratio of the company

(a) 2:3

(b) 3:2

(c) 1:2

(d) 2:1 **(2 Marks)**

8. Given:

Earnings available to the equity shareholders ₹ 30 Lakhs,

Cost of equity is 15%,

Debt outstanding ₹ 150 Lakhs

Value of the firm will be –

(a) ₹ 200 Lakhs

(b) ₹ 250 Lakhs

(c) ₹ 350 Lakhs

(d) ₹ 300 Lakhs **(1 Mark)**

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PART II – Descriptive Questions (35 Marks)

*Question No. **1** is compulsory.*

*Attempt any **two** questions out of the remaining **three** questions.*

1. (a) You are required to CALCULATE the Total Current Assets of Ananya Limited from the given information:

Stock Turnover	= 5 times
Sales (All credit)	= ₹ 7,20,000
Gross Profit Ratio	= 25%
Current Liabilities	= 2,40,000
Liquidity Ratio	= 1.25

Stock at the end is ₹ 30,000 more than stock in the beginning.

(5 Marks)

(b) Gitarth Limited has a current debt equity ratio of 3:7. The company is presently considering several alternative investment proposals costing less than ₹ 25 lakhs. The company will always raise the funds required without disturbing its current capital structure ratio.

The cost of raising debt and equity are as follows-

Cost of Project	**Kd**	**Ke**
Upto 5 lakhs	10%	12%
Above 5 lakhs & upto 10 lakhs	12%	13.5%
Above 10 lakhs & upto 20 lakhs	13%	15%
Above 20 lakhs	14%	16%

Corporate tax rate is 30%, CALCULATE:

i) Cut off rate for two Projects I & Project II whose fund requirements are 15 lakhs & ₹ 26 lakhs respectively.

ii) If a project is expected to give an after-tax return of 13%, determine under what conditions it would be acceptable. **(5 Marks)**

(c) From the following details of X Ltd, PREPARE the Income Statement for the year ended 31st December:

Financial Leverage	2
Interest	₹ 2,000
Operating Leverage	3
Variable Cost as a Percentage of Sales	75%
Income Tax Rate	30%

(5 Marks)

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2. (a) The financial statements of Gurunath Ltd is furnished below –

Balance Sheet as at 31st March

	Particulars as at 31st March	Note	₹
I	**EQUITY AND LIABILITIES:**		
(1)	Shareholders' Funds:		10,00,000
(2)	Non–Current Liabilities: 10% Debt		6,00,000
(3)	Current Liabilities		1,56,000
	Total		17,56,000
II	**ASSETS**		
(1)	Non–Current Assets		16,56,000
(2)	Current Assets – Trade Receivables		1,00,000
	Total		17,56,000

Additional Information:

1. The existing credit terms are 1/10, net 45 days and average collection period is 30 days. The current bad debts loss is 1.5%. In order to accelerate the collection process further as also to increase sales, the company is contemplating liberalization of its existing credit terms to 2/10, net 45 days.
2. It is expected that sales are likely to increase by 1/3 of existing sales, bad debts increase to 2% of sales and average collection period to decline to 20 days.
3. Credit period allowed by the supplier is 60 days. Generally, operating expenses are paid 2 months in arrears. Total Variable expenses of the company constitute Purchases of stock in trade and operating expenses only.
4. Opportunity cost of investment in receivables is 15%. 50% and 80% of customers in terms of sales revenue are expected to avail cash discount under existing and liberalization scheme respectively. The tax rate is 30%.
5. The Company considers only the relevant or variable costs for calculating the opportunity costs on the funds blocked in receivables. Assume 360 days in a year and 30 days in a month.

Should the company change its credit terms? **(6 Marks)**

(b) The following information is given for QB Ltd.

Earnings per share	₹ 180
Dividend per share	₹ 45
Cost of capital	17%
Internal Rate of Return on investment	20%

CALCULATE the market price per share using -

(a) Gordon's formula

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(b) Walter's formula **(4 Marks)**

3. (a) Parmarth Limited is a manufacturer of computers. Owing to recent developments in Artificial Intelligence (AI), it is planning to introduce AI in its computer process. This would result into an estimated annual savings as follows:

(i) Savings of ₹ 3,50,000 in production delays caused by inventory problem.

(ii) Savings in Salaries of 5 employees with an annual pay of ₹ 4,20,000 per annum

(iii) Reduction in Lost sales of ₹ 1,75,000

(iv) Gain due to timely billing is ₹ 3,25,000

The project would result in annual maintenance and operating costs as follows, which are to be paid in advance (at the beginning)

YEAR	1	2	3	4	5
COST	1,80,000	2,00,000	1,20,000	1,10,000	1,30,000

Furthermore, the new system would need 2 AI specialists' professional drawing salaries of ₹ 6,50,000 per annum per person. The purchase price of the new system for installing AI into computers would involve an outlay of ₹ 21,50,000 and installation cost of ₹ 1,50,000.

75% of the total value for depreciation would be paid in the year of purchase and the balance would be paid at the end of the 1st year. The new system will be sold for ₹ 1,90,000. This is the only asset in the block for Income tax purpose.

The life of the system would be 5 years with the hurdle rate of 12%. Depreciation will be charged at 40% on WDV basis, corporate tax rate is 25% and capital gains tax rate is at 20%.

CALCULATE NPV and advise the management on the acceptability of the proposal. Also calculate ARR & PI. **(8 Marks)**

(b) DISCUSS the parameters of Lintner's Model. **(2 Marks)**

4. (a) DISCUSS the Costs of Availing Trade Credit **(4 Marks)**

(b) Briefly EXPLAIN the following –

i. Fully Hedged Bonds

ii. Medium Term Notes

iii. Floating Rate Notes

iv. Euro Commercial Papers **(4 Marks)**

(c) WHAT is the range of DOL? **(2 Marks)**

OR

DISCUSS the role of a chief financial officer. **(2 Marks)**

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PAPER 6B: STRATEGIC MANAGEMENT

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 (15 Marks)

Question 1. (A) (Compulsory)

1. (A) Kriti Pvt. Ltd. has been importing French gourmet cheeses under the brand name of 'Fromage' since 2017. The company was amongst the first in India to introduce innovative unbreakable cheese packaging. Their affiliate, a French company owning Fromage, had entered into a progressive deal, wherein products would be sourced to India via their logistics, and all marketing expenditures would be covered by them. However, customer management and nationwide distribution would be taken care of by Kriti Pvt. Ltd. This required an English-speaking skilled workforce, which has been a constant challenge for the company in India.

The owners of Kriti Pvt. Ltd. have been regular attendees at industry-relevant conclaves, both national and international. Leaders of the company are passionate readers of business magazines. Following that, it was observed that the recent sentiment of the country towards 'Vocal for Local' could disrupt their French brand's marketability. An extraordinary meeting was set up, and the steps ahead were planned.

The outcome of the meeting was to partner with local producers of traditional Indian cheeses in phase one of the change strategy. For this, seven state governments were approached. The team was successful in taking contracts from all the government departments of these seven states and could position themselves fairly in the market. To fund this new investment, they have planned to slowly sell off their French business assets as well as the brand, to probable buyers.

This timely shift is proving to be a game-changer for the company, and the leadership is quite happy with better than before earnings and a much greater response from the customers. They find it easier to operate with domestic producers and vendors, and a sense of patriotism is instilled in the consumers' minds.

Based on the above Case Scenario, answer the Multiple-Choice Questions.

(i) Which of the following actions taken by Kriti Pvt. Ltd. is an example of a proactive strategy?

(a) Selling off their French business assets.

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(b) Responding to the 'Vocal for Local' sentiment by partnering with local cheese producers.

(c) Managing customer relations and nationwide distribution.

(d) Covering all marketing expenditures for 'Fromage' in India.

(2 Marks)

(ii) Which of the following types of strategic control did the owners and leadership of Kriti Pvt. Ltd. deploy that eventually turned out to be one of the most effective strategic decisions for the company?

(a) Premise control

(b) Special alert control

(c) Implementation control

(d) Strategic surveillance **(2 Marks)**

(iii) 'Vocal for Local' is a market sentiment that changed customers' preferences for the majority of products across all industries. Based on that, Kriti Pvt. Ltd. gauged the competition it might face in the coming months and agreed to change its own product. Which of the following forces, as per Michael Porter's five forces of competitive analysis, is most relevant in this case?

(a) Threat of new entrants

(b) Nature of rivalry in the industry

(c) Threat of substitutes

(d) Bargaining power of the buyer **(2 Marks)**

(iv) Which of the following aspects of value chain analysis was the most challenging for Kriti Pvt. Ltd. at the time of selling the Fromage brand?

(a) Manufacturing

(b) Outsourcing

(c) Customer service

(d) Procurement **(2 Marks)**

(v) To strategically revamp their business, partnerships were done with Indian local producers from seven states, and to fund it, the existing arm of the business was to be sold off. Which of the following strategies has Kriti Pvt. Ltd. opted for?

(a) Turnaround strategy

(b) Divestment strategy

(c) Liquidation strategy

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(d) Intensification strategy **(2 Marks)**

(B) **Compulsory Application Based Independent MCQs**

(i) TechWave, a software development firm, aims to gain a competitive edge in the rapidly evolving tech industry. To achieve this, they focus on building their strength in artificial intelligence (AI) and machine learning (ML). TechWave invests heavily in R&D, hires top talent with specialized skills, and forms partnerships with leading AI research institutions. They also provide continuous training for their employees to keep them updated with the latest advancements. By developing these, TechWave can create innovative AI-driven solutions that differentiate them from competitors and attract a growing number of clients seeking cutting-edge technology. What strategy is TechWave using to gain a competitive edge in the tech industry?

(a) Market segmentation

(b) Diversification

(c) Core competency building

(d) Cost leadership **(2 Marks)**

(ii) StreamlineCo is examining its internal capabilities to ensure that employees possess advanced knowledge of emerging technologies crucial for the company's future success. This involves investing in specialized training programs and updating job roles to match the latest industry standards. Which aspect of StreamlineCo is being enhanced through specialized training and updated job roles?

(a) Structure

(b) Systems

(c) Skills

(d) Style **(2 Marks)**

(iii) XYZ Corporation has launched AlphaTech to enter the consumer electronics industry with a focus on offering high-performance devices and innovative features at competitive prices. Which competitive strategy is AlphaTech employing?

(a) Differentiation strategy

(b) Cost leadership strategy

(c) Best-cost provider strategy

(d) Focus strategy **(1 Mark)**

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PART II – Descriptive Questions (35 Marks)

*Question No. **1** is compulsory.*

*Attempt any **two** questions out of the remaining **three** questions.*

1. (a) Mr. Arun has been hired as the CEO by ABC Ltd, a pharmaceutical company that has diversified into affordable wellness supplements. The company intends to launch the HealthPlus brand of supplements. ABC wishes to enhance the well-being of people with its products that are beneficial for health and are produced in an environmentally sustainable manner using natural ingredients. Draft a vision and mission statement that may be formulated by Arun. **(5 Marks)**

   (b) GreenGardens, a small but growing organic farm, is assessing its business environment to strategically plan for future growth. The farm boasts high-quality, pesticide-free crops, but faces challenges with its limited distribution channels. As the demand for organic products continues to rise, GreenGardens recognizes the potential to broaden its market reach. However, unpredictable weather conditions and competition from larger farms present significant obstacles. To effectively navigate these challenges and opportunities, GreenGardens needs to conduct a comprehensive evaluation. Identify the type of analysis GreenGardens should conduct to strategically plan for its future growth and outline the grid. **(5 Marks)**

   (c) FreshDelight, renowned for its organic fruit juices, aims to expand its market presence by identifying emerging markets in countries where organic products are gaining popularity. To achieve this, FreshDelight launches targeted marketing campaigns and partners with local distributors to introduce its juices to these new regions. This strategy involves adapting product packaging and marketing messages to align with local preferences and regulations. By entering these new markets, FreshDelight hopes to increase its customer base and drive sales growth. What strategy is FreshDelight using to expand its market presence? **(5 Marks)**

2. (a) The CEO of a textile mill is convinced that his loss-making company can be turned around. Suggest an action plan for a turnaround to the CEO.

   (5 Marks)

   (b) Write a short note on Matrix Structure. **(5 Marks)**

3. (a) "Understanding the competitive landscape is important to build upon a competitive advantage". Explain. **(5 Marks)**

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(b) XYZ Corporation operates in a diverse range of industries, including fashion, lifestyle products, furniture, real estate, and electrical goods. The company is seeking to hire a suitable Chief Executive Officer. As the HR consultant for XYZ Corporation, you have been tasked with outlining the activities involved in the role of the Chief Executive Officer. Identify the strategic level associated with this role and list the activities it encompasses. **(5 Marks)**

4. (a) Buyers can exert considerable pressure on business. Do you agree? Discuss. **(5 Marks)**

(b) Major core competencies are identified in three areas - competitor differentiation, customer value and application to other markets. Discuss.

OR

What factors should organizations consider when choosing strategic performance measures, and why are these factors important?

(5 Marks)

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INTERMEDIATE: GROUP – II

PAPER – 6: FINANCIAL MANAGEMENT & STRATEGIC MANAGEMENT

PAPER 6A : FINANCIAL MANAGEMENT

Suggested Answers/ Hints

DIVISION A

1. (c) 18.65%, 16.58%

Ke under two approaches

Calculation of Ke (Using Gordon's Model)

Ke = $\frac{D1}{Po} + g$

Share Price has grown from 150 to 301 in 5 years,

$150 (1 + g)^5 = 301.$

$(1 + g)^5 = 2.01$

Therefore, g = 15%, (From Annuity table – Re 1 after 5 years becomes ₹ 2.01 at rate of 15%)

D1 = 8 + 15% of 8 = 9.2

Po = Average of 52 weeks High price in last 5 years

Po = (185 + 210 +252 +325 +280) / 5

= 252.40

Ke = 9.2 / 252.40 + 0.15

= 18.65%

Calculation of Ke (Using CAPM)

Ke = Rf + (Rm – Rf) X Beta

= 8 + (11 x 0.78)

= 16.58%

2. (a) 17.82%

Overall Ke for the company

Approach	Cost of Equity (k)	Weight (w)	K x w
Gordon's	18.65%	0.6	11.19%
CAPM	16.58%	0.4	6.63% **Total Ke = 17.82%**

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3. (b) 12%

Intrinsic Value of Debentures today is ₹ 9,740

WN 1 – Calculation of the Pattern of Future Cash flows

YR	PRINCIPAL (I)	INTEREST (II) = Coupon Rate = 9.5% (7.5% + 2%)	PV OF (I + II) @ 10%	PV OF (I + II) @ 15%
1	1,500	997.50	2270.45	2171.74
2	1,500	855	1946.28	1780.72
3	1,500	712.5	1662.28	1454.75
4	1,500	570	1413.84	1183.53
5	1,500	427.50	1196.83	958.31
6	1,500	285	1007.59	771.70
7	1,500	142.50	842.86	617.48
			10340.13	8938.23

$= 10\% + \frac{(10,340.13 - 9,740)}{(10,340.13 - 8,938.23)} x5\%$ = 12.14% = 12% (approx.)

4. (c) 16.07%, ₹ 87,75,000

Ko = Wd x Kd + We x Ke

= 0.3 X 12 + 0.7 X 17.82

= 16.07%

Purchase Consideration using M-Cap method

= 1,30,000 eq shares x 45 MPS x 1.5X

= ₹ 87,75,000

5. (d) ₹ 66,58,997

It is to be paid equally over 5 years and first instalment is to be paid immediately at Yr 0

Discount rate will be the Ko calculated as above of the company and not 15% which is Ko of Prestige Limited

Year	Amount each year	PV @ 16.07%	PV (₹)
0	17,55,000	1.0000	17,55,000
1	17,55,000	0.8615	15,11,933
2	17,55,000	0.7423	13,02,737
3	17,55,000	0.6395	11,22,323
4	17,55,000	0.5510	9,67,005
	TOTAL PV		**66,58,997**

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6. (d) 19.5%

Financial Leverage (FL) indicates % impact in EPS, if EBIT is affected by 12%

FL = Combined Leverage (CL) /Operating Leverage (OL)

CL = 6.5 (Measure of total risk)

OL = 1 / Margin of Safety

Margin of Safety (MOS) = $\frac{\text{Actual Sales} - \text{B.E Sales}}{\text{Actual Sales}}$

MOS = 20 lakhs – 15 lakhs / 20 lakhs = 0.25

Therefore, OL = 1 / 0.25 = 4

So, FL = 6.5 / 4 = 1.625

So % Change in EPS = 12 x 1.625 = 19.5%

7. (c) 1:2

Item	Cost	Weight	Product
Debt	8%	W	8W
Equity	11%	1 – W	11 – 11W
			WACC = 10

Wd = 1/3 and We = 2/3 Debt Equity Ratio = 1/2

8. (c) ₹ 350 Lakhs

Value of Equity = 30 Lakhs ÷ 15% = ₹ 200 Lakhs

Value of Debt = ₹ 150 Lakhs

Value of Firm = 200 Lakhs + 150 Lakhs = ₹ 350 Lakhs

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DIVISION B – Descriptive Questions

1. **(a)** 1. Cost of Goods Sold = Sales – Gross Profit

= ₹ 7,20,000 – 25% x ₹ 7,20,000 = ₹ 5,40,000

2. Stock Turnover $= \frac{\text{Cost of Goods Sold}}{\text{Average Stock}} = \frac{₹\ 5{,}40{,}000}{\text{Average Stock}}$ = 5 times.

Average Stock $= \frac{₹\ 5{,}40{,}000}{5}$ = ₹ 1,08,000

3. Let Opening Stock be x.

Closing Stock is ₹ 30,000 more than Opening Stock.

Closing Stock = (x + 30,000)

Average Stock $= \frac{x + x + 30{,}000}{2}$ = 1,08,000.

2x = 2,16,000 – 30,000

x $= \frac{1{,}86{,}000}{2}$ = 93,000 = Opening Stock.

Closing Stock = x + 30,000

= 93,000 + 30,000 = ₹ 1,23,000

4. Liquid Ratio $= \frac{\text{Liquid Assets}}{\text{Current Liabilities}} = \frac{\text{Liquid Assets}}{2{,}40{,}000}$ = 1.25.

Liquid Assets = ₹ 3,00,000

5. Current Assets = Liquid Assets + Closing Stock

= ₹ 3,00,000 + ₹ 1,23,000 = ₹ 4,23,000

(b) Calculation of slab wise Overall Cost of Capital

(i)

Project Cost	Capital Source	Weights (w)	Cost (k)	w x k (%)
Upto 5 Lakhs	Debt	0.3	10	3
	Equity	0.7	12	8.4
			Ko	**11.4**
Above 5 lakhs upto 10 lakhs	Debt	0.3	12	3.6
	Equity	0.7	13.5	9.45
			Ko	**13.05**
Above 10 lakhs upto 20 lakhs	Debt	0.3	13	3.9
	Equity	0.7	15	10.5

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			Ko	14.4
Above 20 lakhs	Debt	0.3	14	4.2
	Equity	0.7	16	11.2
			Ko	**15.4**

Cost of Raising funds for Project I

Total Capital	Ko(%)	Total Cost (in ₹)
5,00,000	11.40	57,000
5,00,000	13.05	65,250
5,00,000	14.40	72,000
15,00,000		**1,94,250**

Overall COC (%) = Total Cost (in ₹) / Total Capital

= 1,94,250/15,00,000 * 100

= 12.95 %

Cost of Raising funds for Project II

Total Capital	Ko(%)	Total Cost (in ₹)
5,00,000	11.4	57,000
5,00,000	13.05	65,250
10,00,000	14.4	1,44,000
6,00,000	15.4	92,400
26,00,000		**3,58,650**

Overall COC (%) = 358650 / 2600000 * 100 **= 13.79%**

(ii) If any project is expected to give an after-tax return of 13%, it can be accepted only if the maximum Overall COC (%) of that project equals 13% or less, as at 13%, project would be at break-even i.e earning 13% from the project and incurring 13% COC.

So, under that scenario, Project I can be taken as its COC is 12.95% whereas Project II can't be taken as its COC is 13.79%.

Maximum Value of the Project that can be taken at 13% is approx. (Using IRR technique Interpolation)

At 15 Lakhs Ko = 12.95%

At 26 Lakhs Ko = 13.79%

By interpolation, maximum value of Project at 13% will be

15 Lakhs + {(0.05 x 11)/0.84}

= 15.6548 lakhs

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(c) Income Statement

$$DFL = \frac{EBIT}{EBT} = \frac{EBT + Interest}{EBT} = \frac{EBT + 2{,}000}{EBT} = \frac{2}{1}.$$

EBT + ₹ 2000 = 2 EBT.

EBT = ₹ 2,000

EBIT = EBT + Interest = ₹ 2000 + ₹ 2000 = ₹ 4,000.

Contribution $\frac{Contribution}{EBIT} = \frac{Contribution}{4{,}000} = \frac{3}{1}$

Sales $\frac{Contribution}{PVR} = \frac{12{,}000}{25\%}$	48,000
Less: Variable Cost Given = 75%	(36,000)
Contribution	12,000
Less: Fixed Cost(Contribution - EBIT = ₹ 12,000 – ₹ 4,000)	(8,000)
EBIT	4,000
Less: Interest	(2,000)
EBT	2,000
Less: Tax at 30%	(600)
EAT	1,400

2. (a)

Particulars	Result
Current liabilities	1,56,000
Total Variable expenses = Purchases & Operating Expenses	1,56,000 ÷ 60 × 360 = 9,36,000
Variable expenses % of Sales	9,36,000 ÷ 12,00,000 × 100 = 78%

Particulars	Present	Proposed
1. Sales	1 Lakh ÷ 30 × 360 = 12,00,000	12 Lakhs + 1/3rd = 16,00,000
2. Variable Cost at 78%	9,36,000	12,48,000
3. Cash Discount	12 Lakh × 50% × 1% = 6,000	16 Lakh × 80% × 2% = 25,600
4. Bad debts	12 Lakh × 1.5% = 18,000	16 Lakh × 2% = 32,000
5. Profit before Tax	2,40,000	2,94,400
6. Tax @ 30%	72,000	88,320
7. Profit after Tax	1,68,000	2,06,080

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Particulars	Present	Proposed
8. Opportunity Cost of Invest. in Debtors	9,36,000 × 30/360 × 70% ×15% = 8,190	12,48,000 × 20/360 × 70% × 15% = 7,280
9. **Net Benefit**	**1,59,810**	**1,98,800**

Advise: Proposed policy should be adopted since the net benefit is increased by (₹ 1,98,800 - 1,59,810) = ₹ 38,990.

(b) **(i)** As per **Gordon's Model**, Price per share is computed using the formula:

$$P_0 = \frac{E_1(1-b)}{K_e - br}$$

Where,

P_0 = Price per share

E_1 = Earnings per share

Payout ratio = 45/180 = 25%

b = Retention ratio; (1 - b = Pay-out ratio) = 1-0.25 = 0.75

K_e = Cost of capital

r = IRR

br = Growth rate (g)

Applying the above formula, price per share

$$P_0 = \frac{180(1-0.75)}{0.17-0.75\times0.2} = \frac{45}{0.02} = ₹\ 2,250$$

(ii) **As per Walter's Model, Price per share is computed using the formula:**

$$\text{Price } \mathbf{(P)} = \frac{D+\frac{r}{K_e}(E-D)}{K_e}$$

Where,

P = Market Price of the share.

E = Earnings per share.

D = Dividend per share.

K_e = Cost of equity/ rate of capitalization/ discount rate.

r = Internal rate of return/ return on investment

Applying the above formula, price per share

$$P = \frac{45+\frac{0.20}{0.17}(180-45)}{0.17}$$

$$\text{Or,} \quad P = \frac{45+158.82}{0.17} = ₹\ 1,200 \text{ (approx..)}$$

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3. (a) Calculation of Present value of cash inflows (PVCI)

	Year 0	Year 1	Year 2	Year 3	Year 4	Year 5
Savings in cost due to Production Delays	-	3,50,000	3,50,000	3,50,000	3,50,000	3,50,000
Savings in Salaries	-	21,00,000	21,00,000	21,00,000	21,00,000	21,00,000
Reduction in lost sales	-	1,75,000	1,75,000	1,75,000	1,75,000	1,75,000
Gain due to timely billing	-	3,25,000	3,25,000	3,25,000	3,25,000	3,25,000
	-	29,50,000	29,50,000	29,50,000	29,50,000	29,50,000
Less:						
Salary of AI specialists	-	13,00,000	13,00,000	13,00,000	13,00,000	13,00,000
Annual Maint. & Op Cost	-	1,80,000	2,00,000	1,20,000	1,10,000	1,30,000
NPBDT	-	14,70,000	14,50,000	15,30,000	15,40,000	15,20,000
(-) Depreciation	-	9,20,000	5,52,000	3,31,200	1,98,720	1,19,232
NPBT	-	5,50,000	8,98,000	11,98,800	13,41,280	14,00,768
(-) Tax @ 25%	-	1,37,500	2,24,500	2,99,700	3,35,320	3,50,192
NPAT	-	4,12,500	6,73,500	8,99,100	10,05,960	10,50,576
(+) Depreciation	-	9,20,000	5,52,000	3,31,200	1,98,720	1,19,232
(+) Annual Maint. & Op Cost	-	1,80,000	2,00,000	1,20,000	1,10,000	1,30,000
Gross Cash Inflows	-	15,12,500	14,25,500	13,50,300	13,14,680	12,99,808
(-) Annual Maint. & Op Cost actually paid	1,80,000	2,00,000	1,20,000	1,10,000	1,30,000	-
Net Cash Inflows	-1,80,000	13,12,500	13,05,500	12,40,300	11,84,680	12,99,808
(+) Sale Value at the end of life	-	-	-	-	-	1,90,000
	-1,80,000	13,12,500	13,05,500	12,40,300	11,84,680	14,89,808
PV Factor @ 12%	1	0.8929	0.7`972	0.7118	0.6355	0.5674
PV of Cash Inflows	-1,80,000	11,71,875	10,40,737	8,82,821	7,52,886	8,45,357
Total PV of Cash Inflows	45,13,675					

Calculation of Present value of cash outflows (PVCO)

As mentioned in the question, 75% of the depreciable value will be paid at the beginning. Depreciable value means purchase price plus the installation cost.

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	Year 0	Year 1
Purchase Price & Installation Cost	17,25,000	5,75,000
PV Factor @ 12%	1	0.8929
PVCO	17,25,000	5,13,418

(2) Total PVCO = 22,38,418

(3) PV of Tax on Capital Gains (Only asset in the block) - 5th Year end

Capital Gains = Sale Price (-) Closing WDV at 5th year

= 1,90,000 (-) 1,78,848

= 11,152

Tax @ 20% on above = 2230.40

PV = 2,230.40 x 0.5674 = 1,266

Net PVCI = PVCI - PV of Tax on Capital Gains

= 45,13,675 - 1,266 = 45,12,409

NPV = Net PVCI – PVCO

= 45,12,409 - 22,38,418

= 22,73,991

(II) PI = PVCI / PVCO = 45,12,409/ 22,38,418 = 2.0158

(III) ARR = Average NPAT / Initial Investment

= 8,08,327.2/23,00,000 x 100 = 35.145**%**

Note – ARR is calculated based on Initial Investment, similarly it can be calculated based on Average Investment

(b) Lintner's model has two parameters:

i. The target payout ratio,

ii. The spread at which current dividends adjust to the target.

4. (a) Normally it is considered that the trade credit does not carry any cost. However, it carries the following costs:

(i) **Price:** There is often a discount on the price that the firm undergoes when it uses trade credit, since it can take advantage of the discount only if it pays immediately. This discount can translate into a high implicit cost.

(ii) **Loss of goodwill:** If the credit is overstepped, suppliers may discriminate against delinquent customers if supplies become short. As with the effect of any loss of goodwill, it depends very much on the relative market strengths of the parties involved.

(iii) **Cost of managing:** Management of creditors involves administrative and accounting costs that would otherwise be incurred.

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(iv) **Conditions:** Sometimes most of the suppliers insist that for availing the credit facility the order should be of some minimum size or even on regular basis.

(b) (i) **Fully Hedged Bonds:** In foreign bonds, the risk of currency fluctuations exists. Fully hedged bonds eliminate the risk by selling in forward markets the entire stream of principal and interest payments.

(ii) **Medium Term Notes (MTN):** Certain issuers need frequent financing through the Bond route including that of the Euro bond. However, it may be costly and ineffective to go in for frequent issues. Instead, investors can follow the MTN programme. Under this programme, several lots of bonds can be issued, all having different features e.g. different coupon rates, different currencies etc. The timing of each lot can be decided keeping in mind the future market opportunities. The entire documentation and various regulatory approvals can be taken at one point of time.

(iii) **Floating Rate Notes (FRN):** These are issued up to seven years maturity. Interest rates are adjusted to reflect the prevailing exchange rates. They provide cheaper money than foreign loans.

(iv) **Euro Commercial Papers (ECP):** ECPs are short term money market instruments. They have maturity period of less than one year. They are usually designated in US Dollars.

(c) DOL can never be between zero and one. It can be zero or less or it can be one or more.

When Sales is much higher than BEP sales, DOL will be slightly more than one. With decrease in sales, DOL will increase. At BEP, DOL will be infinite. When sales is slightly less than BEP, DOL will be negative infinite. With further reduction in sale, DOL will move towards zero. At zero sales, DOL will also be zero.

OR

The finance executive of an organisation plays an important role in the company's goals, policies, and financial success. His responsibilities include:

(a) **Financial analysis and planning:** Determining the proper amount of funds to employ in the firm, i.e. designating the size of the firm and its rate of growth.

(b) **Investment decisions:** The efficient allocation of funds to specific assets.

(c) **Financing and capital structure decisions:** Raising funds on favourable terms as possible i.e. determining the composition of liabilities.

(d) **Management of financial resources** (such as working capital).

(e) **Risk management:** Protecting assets.

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PAPER 6B: STRATEGIC MANAGEMENT

ANSWERS

PART I

1. (A) (i) (b) (ii) (d) (iii) (c) (iv) (c) (v) (b)

1. (B) (i) (c) (ii) (c) (iii) (c)

PART II

1. **(a)** The HealthPlus brand of wellness supplements may have the following vision and mission:

Vision: Vision implies the blueprint of the company's future position. It describes where the organization wants to land. Mr. Arun should aim to position "HealthPlus" as India's leading wellness supplements brand. It may have the vision to be India's largest wellness supplements company that enhances health, promotes extraordinary well-being, and brings happiness to people.

Mission: Mission delineates the firm's business, its goals, and ways to reach the goals. It explains the reason for the existence of the firm in society. It is designed to help potential shareholders and investors understand the purpose of the company. Mr. Arun may identify the mission in the following lines:

- To be in the business of wellness supplements to enhance the lives of people and give them the confidence to lead a healthy life.
- To protect health by providing supplements that counteract harmful elements in the environment.
- To produce wellness supplements using natural ingredients in an environmentally sustainable manner.

(b) GreenGardens should conduct a SWOT analysis to strategically plan for future growth. This analysis will help them understand their internal strengths and weaknesses, as well as external opportunities and threats.

SWOT Analysis Grid for GreenGardens:

Strengths	Weaknesses
High-quality, pesticide-free produce	Limited distribution channels
Strong brand reputation for organic products	Small scale of operations
Dedicated and knowledgeable workforce	Limited marketing and sales reach
Opportunities	**Threats**
Rising demand for organic products	Unpredictable weather conditions

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Potential to expand into new markets	Intense competition from larger farms
Increased consumer awareness of health and sustainability	Regulatory changes affecting organic farming

By systematically evaluating these areas, GreenGardens can leverage its strengths, address its weaknesses, capitalize on opportunities, and mitigate threats. This strategic planning will guide them toward sustainable growth and success in the organic farming industry.

(c) FreshDelight is employing a **market development strategy** to expand its market presence. This approach involves introducing their existing organic fruit juices to new markets, specifically targeting countries where the demand for organic products is on the rise. To achieve this, FreshDelight is launching targeted marketing campaigns and partnering with local distributors to effectively introduce their products to these new regions. Additionally, they are adapting their product packaging and marketing messages to align with local preferences and regulations, ensuring their offerings resonate with the new customer base. By entering these emerging markets, FreshDelight aims to increase its customer base and drive sales growth, leveraging the growing popularity of organic products.

2. (a) A workable action plan for turnaround of the textile mill would involve:

- **Stage One – Assessment of current problems**: In the first step, assess the current problems and get to the root causes and the extent of damage.
- **Stage Two – Analyze the situation and develop a strategic plan:** Identify major problems and opportunities, develop a strategic plan with specific goals and detailed functional actions after analyzing strengths and weaknesses in the areas of competitive position.
- **Stage Three – Implementing an emergency action plan**: If the organization is in a critical stage, an appropriate action plan must be developed to stop the bleeding and enable the organization to survive.
- **Stage Four – Restructuring the business**: If the core business is irreparably damaged, then the outlook for the entire organization may be bleak. Efforts to be made to position the organization for rapid improvement.
- **Stage Five – Returning to normal**: In the final stage of turnaround strategy process, the organization should begin to show signs of profitability, return on investments and enhancing economic value-added.

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(b) In matrix structure, functional and product forms are combined simultaneously at the same level of the organization. Employees have two superiors, a product / project manager and a functional manager. The “home” department - that is, engineering, manufacturing, or marketing - is usually functional and is reasonably permanent. People from these functional units are often assigned temporarily to one or more product units or projects.

The product units / projects are usually temporary and act like divisions in that they are differentiated on a product-market basis. The matrix structure may be very appropriate when organizations conclude that neither functional nor divisional forms, even when combined with horizontal linking mechanisms like strategic business units, are right for the implementation of their strategies. Matrix structure was developed to combine the stability of the functional structure with flexibility of the product form. It is very useful when the external environment (especially its technological and market aspects) is very complex and changeable.

A matrix structure is most complex of all designs because it depends upon both vertical and horizontal flows of authority and communication. It may result in higher overhead costs due to more management positions.

The matrix structure is often found in an organization when the following three conditions exist:

1. Ideas need to be cross-fertilized across projects or products;
2. Resources are scarce; and
3. Abilities to process information and to make decisions need to be improved.

3. (a) Competitive landscape is a business analysis which identifies competitors, either direct or indirect. Competitive landscape is about identifying and understanding the competitors and at the same time, it permits the comprehension of their vision, mission, core values, niche market, strengths and weaknesses.

An in-depth investigation and analysis of a firm’s competition allows it to assess the competitors’ strengths and weaknesses in the marketplace and helps it to choose and implement effective strategies that will improve its competitive advantage.

Steps to understand the competitive landscape for building competitive advantage are:

(i) **Identify the competitor:** The first step to understanding the competitive landscape is to identify the competitors in the firm’s industry and have actual data about their respective market share.

(ii) **Understand the competitors:** Once the competitors have been identified, the strategist can use market research report, internet, newspapers, social media, industry reports, and various other

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sources to understand the products and services offered by them in different markets.

(iii) Determine the strengths of the competitors: What are the strengths of the competitors? What do they do well? Do they offer great products? Do they utilize marketing in a way that comparatively reaches out to more consumers? Why do customers give them their business?

(iv) Determine the weaknesses of the competitors: Weaknesses (and strengths) can be identified by going through consumer reports and reviews appearing in various media. After all, consumers are often willing to give their opinions, especially when the products or services are either great or very poor.

(v) Put all of the information together: At this stage, the strategist should put together all information about competitors and draw inference about what they are not offering and what the firm can do to fill in the gaps. The strategist can also know the areas which need to be strengthened by the firm.

(b) The role of Chief Executive Officer pertains to corporate level.

The corporate level of management consists of the Chief Executive Officer (CEO) and other top-level executives. These individuals occupy the apex of decision making within the organization.

The role of Chief Executive Officer is to:

1. oversee the development of strategies for the whole organization;
2. defining the mission and goals of the organization;
3. determining what businesses, it should be in;
4. allocating resources among the different businesses;
5. formulating, and implementing strategies that span individual businesses;
6. providing leadership for the organization;
7. ensuring that the corporate and business level strategies which company pursues are consistent with maximizing shareholders wealth; and
8. managing the divestment and acquisition process.

4. (a) Buyers of an industry's products or services can sometimes exert considerable pressure on existing firms to secure lower prices or better services. This is evident in situations where buyers enjoy a superior position than the seller of the product. This leverage is particularly evident when:

(i) Buyers have full knowledge of the sources of products and their substitutes.

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(ii) They spend a lot of money on the industry's products, i.e., they are big buyers.

(iii) The industry's product is not perceived as critical to the buyer's needs and buyers are more concentrated than firms supplying the product. They can easily switch to the substitutes available.

(b) According to C.K. Prahalad and Gary Hamel, major core competencies are identified in three areas - competitor differentiation, customer value, and application to other markets.

- **Competitor differentiation:** The company can consider having a core competence if the competence is unique and it is difficult for competitors to imitate. This can provide a company an edge compared to competitors. It allows the company to provide better products or services to market with no fear that competitors can copy it.

- **Customer value:** When purchasing a product or service it has to deliver a fundamental benefit for the end customer in order to be a core competence. It will include all the skills needed to provide fundamental benefits. The service or the product has to have real impact on the customer as the reason to choose to purchase them. If customer has chosen the company without this impact, then competence is not a core competence.

- **Application of competencies to other markets:** Core competence must be applicable to the whole organization; it cannot be only one particular skill or specified area of expertise. Therefore, although some special capability would be essential or crucial for the success of business activity, it will not be considered as core competence, if it is not fundamental from the whole organization's point of view. Thus, a core competence is a unique set of skills and expertise, which will be used throughout the organisation to open up potential markets to be exploited.

OR

Organizations should consider the following factors when choosing strategic performance measures:

1. **Relevance:** The measure should be relevant to the organization's goals and objectives, providing actionable and meaningful information. This ensures that the performance measures are directly aligned with what the organization aims to achieve, and that the information obtained can drive improvements and strategic decisions.

2. **Data Availability:** The measure should be based on data that is readily available and can be collected and analyzed in a timely manner. This is important to ensure that the organization can efficiently gather and utilize data without significant delays or obstacles.

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3. **Data Quality:** The measure should be based on high-quality data that is accurate and reliable. Accurate and reliable data are crucial for making informed decisions and assessing the true performance of the organization.
4. **Data Timeliness:** The measure should be based on data that is current and up-to-date. Timely data allows organizations to make informed decisions quickly, enabling them to respond promptly to changes and emerging challenges.

These factors are important because they provide a framework for organizations to assess the success of their strategies, identify areas for improvement, and make informed decisions about resource allocation and strategic adjustments. Effective strategic performance measures should be relevant, meaningful, easy to understand, and regularly reviewed and updated to ensure their continued alignment with the organization's goals and objectives.

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Mock Test Paper - Series II: August, 2024

Date of Paper: 23rd August, 2024

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

INTERMEDIATE GROUP – II

PAPER – 6A : FINANCIAL MANAGEMENT & STRATEGIC MANAGEMENT

PAPER 6A: FINANCIAL MANAGEMENT

Time Allowed – 3 Hours (Total time for 6A and 6B) Maximum Marks – 50

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.*
4. *Working note should form part of the answer. Wherever necessary, suitable assumptions may be made by the candidates and disclosed by way of note. However, in answers to Questions in Division A, working notes are not required.*

PART I – Case Scenario based MCQs (15 Marks)

Write the most appropriate answer to each of the following multiple choice questions by choosing one of the four options given. All questions are compulsory.

Mathangi Ltd. is a News broadcasting channel having its broadcasting Centre in Chennai. There are total 200 employees in the organisation including top management. As a part of employee benefit expenses, the company serves tea to its employees, which is outsourced from a third-party. The company offers tea three times a day to each of its employees. The third-party charges ₹ 10 for each cup of tea. The company works for 200 days in a year.

Looking at the substantial amount of expenditure on tea, the finance department has proposed to the management an installation of a master tea vending machine from Nirmal Ltd which will cost ₹ 5,00,000 with a useful life of five years. Upon purchasing the machine, the company will have to incur annual maintenance which will require a payment of ₹ 25,000 every year. The machine would require electricity consumption of 500 units p.m. and current incremental cost of electricity for the company is ₹ 24 per unit. Apart from these running costs, the company will have to incur ₹ 8,00,000 for consumables like milk, tea powder, paper cup, sugar etc. The company is in the 25% tax bracket. Straight line method of depreciation is allowed for the purpose of taxation.

Nirmal Ltd sells 100 master tea vending machines. Variable cost is ₹ 4,50,000 per machine and fixed operating cost is ₹ 25,00,000. Capital Structure of Mathangi Ltd and Nirmal Ltd consists of the following –

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Particulars	Mathangi Ltd.	Nirmal Ltd.
Equity Share Capital (Face value ₹ 10 each)	40,00,000	40,00,000
Reserves & Surplus	25,00,000	50,00,000
12% Preference Share Capital	12,00,000	Nil
15% Debentures	20,00,000	40,00,000

Risk free rate of return = 5%, Market return = 10%, Beta of the Mathangi Ltd. = 1.9

You are required to answer the following five questions based on the above details:

1. If sales of Nirmal Ltd are up by 10%, impact on its EBIT is
   - (a) 30%
   - (b) 60%
   - (c) 5%
   - (d) 20%
2. Combined leverage of Nirmal Ltd is
   - (a) 1.63
   - (b) 2.63
   - (c) 1.315
   - (d) 2
3. Discount rate that can be applied for making investment decisions of Mathangi Ltd is
   - (a) 12%
   - (b) 13.52%
   - (c) 15%
   - (d) 20%
4. Incremental cash flow after tax per annum attributable to Mathangi Ltd due to investment in the machine is
   - (a) ₹ 2,39,438
   - (b) ₹ 1,98,250
   - (c) ₹ 98,250
   - (d) ₹ 1,31,000
5. Net present value of investment in the machine by Mathangi Ltd is
   - (a) ₹ 6,88,522
   - (b) ₹ 1,88,522
   - (c) ₹ 9,91,250
   - (d) ₹ 4,91,250

(5 x 2 = 10 Marks)

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6. Total Assets & Current liabilities of the Vitrag Limited are 50 lakhs & 10 lakhs respectively. ROCE is 15%, measure of business operating risk is at 3.5 & P/V ratio is 70%. Calculate Sales.

   (a) 21 lakhs

   (b) 30 lakhs

   (c) 37.50 lakhs

   (d) 40 lakhs **(2 Marks)**

7. A company has issued bonds with a face value of ₹ 100,000 at an annual coupon rate of 8%. The bonds are currently trading at 95% of their face value. What is the approximate cost of debt for the company before taxes.

   (a) 9.00%

   (b) 7.65%

   (c) 8.00%

   (d) 8.42% **(2 Marks)**

8. A company is considering changing its capital structure by increasing its debt ratio from 40% to 55%. What is the likely impact on the company's cost of equity, assuming all other factors remain constant?

   (a) Cost of equity will be unaffected by debt ratio

   (b) Cost of equity will remain unchanged

   (c) Cost of equity will decrease

   (d) Cost of equity will increase **(1 Mark)**

PART II – Descriptive Questions (35 Marks)

*Question No. **1** is compulsory.*

*Attempt any **two** questions out of the remaining **three** questions.*

1. (a) X Ltd is willing to raise funds for its New Project which requires an investment of ₹ 84 Lakhs. The Company has two options:

   Option I: To issue Equity Shares (₹ 10 each) only

   Option II: To avail Term Loan at an interest rate of 12%. But in this case, as insisted by the Financing Agencies, the Company will have to maintain a Debt–Equity proportion of 2:1.

   The Corporate Tax Rate is 30%. FIND out the point of indifference for the project. **(5 Marks)**

   (b) Mr. Anand is thinking of buying a Share at ₹ 500 whose Face Value per share is ₹ 100. He is expecting a bonus at the ratio 1 : 5 at the end of the fourth year. Annual expected dividend is 20% and the same rate is expected to be maintained on the expanded capital base. He intends to sell the Shares at the end of seventh year at an expected price of ₹ 900

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each. Incidental Expenses for purchase and sale of Shares are estimated to be 5% of the Market Price. Assuming a Discount rate of 12% per annum, COMPUTE the Net Present Value from the acquisition of the shares. **(5 Marks)**

(c) Paarath Limited had recently repurchased 20,000 equity shares at a premium of 10% to its prevailing market price. The book value per share (after repurchasing) is ₹ 193.20.

Other Details of the company are as follows:

Earnings of the company (before buyback) = ₹ 18,00,000

Current MPS is ₹ 270 with a P/E Ratio of 18.

CALCULATE the Book Value per share of the company before the re-purchase. **(5 Marks)**

2. (a) Sukrut Limited has annual credit sales of ₹ 75,00,000/-. Actual credit terms are 30 days, but its management of receivables has been poor, and the average collection period is about 60 days. Bad debt is 1 per cent of total sales.

A factor has offered to take over the task of debt administration and credit checking, at an annual fee of 1.5 per cent of credit sales.

Sukrut Limited estimates that it would save ₹ 45,000 per year in administration costs as a result. Due to the efficiency of the factor, the average collection period would come back to the original credit offered of 30 days and bad debts would come to 0.5% on recourse basis.

The factor would pay net advance of 80 percent to the company at an annual interest rate of 12 per cent after withholding a reserve of 10%. Sukrut Limited is currently financing its receivables from an overdraft costing 10 per cent per year and will continue to finance the balance fund needed (which is not financed by factor) through the overdraft facility

If occurrence of credit sales is throughout the year, COMPUTE whether the factor's services should be accepted or rejected. Assume 360 days in a year. **(7 Marks)**

(b) Determining the amount to be invested in current assets as working capital is a crucial policy decision for any entity. What FACTORS should a company consider when deciding the level of investment in working capital? **(3 Marks)**

3. (a) Calculate the WACC using the following data by using Market Value weights:

Particulars	₹
Equity Shares (₹ 10 per equity share)	15,00,000
Reserves & Surplus	5,00,000
Preference Shares (₹ 100 per preference share)	7,50,000
Debentures (₹ 100 per debenture)	5,50,000

The market prices of these securities are:

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Debentures - ₹ 105 per debenture,

Preference shares - ₹115 per preference share

Equity shares - ₹ 27 per equity share

Additional information:

(1) ` 100 FV per debenture redeemable at premium of 10%, 10% coupon rate, 4% floatation costs, 10-year maturity.

(2) ` 100 FV per preference share redeemable at par, 12% coupon rate, 2% floatation cost and 10-year maturity.

(3) Equity shares have ₹ 4.5 floatation cost and market price of 27 per share.

The last dividend paid by the company was ` 2 which is expected to grow at an annual growth rate of 9%. The firm has the practice of paying all earnings as a dividend.

The corporate tax rate is 25%. To calculate the overall cost of debt & preference shares, take the average of their respective costs using YTM & approximation method. **(6 Marks)**

(b) EPL Ltd. has furnished the following information relating to the year ended 31st March 2023 and 31st March, 2024:

	31st March, 2023	**31st March, 2024**
Share Capital	50,00,000	50,00,000
Reserve and Surplus	20,00,000	25,00,000
Long term loan	30,00,000	30,00,000

- Net profit ratio: 8%
- Gross profit ratio: 20%
- Long-term loan has been used to finance 40% of the fixed assets.
- Stock turnover with respect to cost of goods sold is 4.
- Debtors represent 90 days sales.
- The company holds cash equivalent to 1½ months cost of goods sold.
- Ignore taxation and assume 360 days in a year.

You are required to PREPARE Balance Sheet as on 31st March 2024 in following format:

Liabilities	**(₹)**	**Assets**	**(₹)**
Share Capital	-	Fixed Assets	-
Reserve and Surplus	-	Sundry Debtors	-
Long-term loan	-	Closing Stock	-
Sundry Creditors	-	Cash in hand	-

(4 Marks)

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4. (a) The agency problem is one of the key concepts in corporate governance and financial management. On the light of this statement, EXPLAIN agency problem, consequences of agency problem and how to overcome the issue. **(4 Marks)**

(b) Operating leases and financial leases are traditionally the most important types of leases in financial management. However, in recent years, other types of leases have also gained significance due to their unique benefits and applications. IDENTIFY AND EXPLAIN at least four other types of leases that have become increasingly important in modern business practices. **(4 Marks)**

(c) EXPLAIN the Relationship between EBIT-EPS-MPS **(2 Marks)**

OR

(c) EXPLAIN Financial Leverage as a 'Double edged Sword' **(2 Marks)**

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PAPER 6B: STRATEGIC MANAGEMENT

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 (15 Marks)

Question 1. (Compulsory)

1. (A) Sneha Rao, founder and CEO of DEF Technologies, is renowned for her technological insight and visionary leadership style. She cultivates a culture of collaboration, continuous learning, and innovative problem-solving, encouraging her employees to think outside the box and embrace new challenges. Her exceptional ability to foresee technological trends and navigate complex market dynamics has propelled DEF Technologies to impressive growth over the past decade.

Sneha started DEF Technologies in 2010 as a small software development firm. With a vision to transform DEF Technologies into a leading tech company, she initially focused on developing custom software solutions for local businesses. However, intense competition and limited market demand led to financial difficulties. Undeterred, Sneha pivoted the business towards developing cloud-based solutions, leveraging the growing trend of digital transformation. This strategic shift, along with aggressive marketing, helped DEF Technologies capture a significant market share and become a leader in cloud services, setting new industry standards.

In 2015, Sneha's brother, Raj, joined the company, and together they crafted an ambitious expansion strategy. DEF Technologies entered the global market, partnering with international tech firms to launch a new line of AI-driven cybersecurity solutions. This venture was highly successful, establishing DEF Technologies as a global brand and a key player in the cybersecurity industry.

Raj then led the company’s diversification into the healthcare sector with a new brand, MedTech Solutions. Recognizing the potential for technology to revolutionize healthcare, Sneha and Raj focused on developing affordable telemedicine platforms and AI-driven diagnostic tools. Their approach disrupted the market, providing high-quality healthcare solutions at lower costs and gaining widespread trust from healthcare providers and patients alike. MedTech Solutions experienced rapid growth, especially during the COVID-19 pandemic, as demand for remote healthcare services surged.

At the beginning of 2023, DEF Technologies launched another new business, GreenTech Innovations, to address environmental challenges through technology. DEF Technologies continues to explore new opportunities and ventures to stay at the forefront of the tech industry.

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Based on the above Case Scenario, answer the Multiple-Choice Questions.

(i) Sneha Rao's vision to transform DEF Technologies into a leading tech company illustrates which type of strategic intent?

(a) Goal

(b) Mission

(c) Vision

(d) Objective **(2 Marks)**

(ii) Sneha's leadership style, which promotes collaboration, continuous learning, and innovative problem-solving, can best be described as:

(a) Transactional leadership

(b) Transformational leadership

(c) Autocratic leadership

(d) Laissez-faire leadership **(2 Marks)**

(iii) When DEF Technologies expanded into the global market with AI-driven cybersecurity solutions, which of Porter's Five Forces was most likely mitigated by forming partnerships with international tech firms?

(a) Threat of Substitute Products or Services

(b) Bargaining Power of Suppliers

(c) Threat of New Entrants

(d) Intense Rivalry Among Existing Competitors **(2 Marks)**

(iv) By entering the global market and launching AI-driven cybersecurity solutions, DEF Technologies pursued which expansion strategy from Ansoff's Product-Market Growth Matrix?

(a) Diversification

(b) Market Penetration

(c) Product Development

(d) Market Development **(2 Marks)**

(v) MedTech Solutions' focus on developing affordable telemedicine platforms and AI-driven diagnostic tools reflects which of the following competitive strategies?

(a) Differentiation strategy

(b) Cost leadership strategy

(c) Best-cost provider strategy

(d) Focus Strategy **(2 Marks)**

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(B) Compulsory Application Based Independent MCQs

(i) A traditional desi ghee company modernized its production and introduced pro-biotic desi ghee, facing initial market doubts. Aggressive marketing campaigns highlighted its benefits, gaining acceptance. During which stage of the product life cycle did the desi ghee company face doubts but gained acceptance through aggressive marketing campaigns?

(a) Introduction stage

(b) Growth stage

(c) Maturity stage

(d) Decline stage **(2 Marks)**

(ii) ValueMart is a discount retail chain that targets budget-conscious consumers by offering a wide range of products at the lowest possible prices. The company achieves this by sourcing goods in bulk, negotiating lower prices with suppliers, and maintaining lean operations. ValueMart's goal is to dominate the market by attracting price-sensitive customers from competitors. Which of Michael Porter's Generic Strategies is ValueMart primarily employing?

(a) Differentiation

(b) Focused Cost Leadership

(c) Cost Leadership

(d) Focused Differentiation **(2 Marks)**

(iii) A women's clothing brand recognized new opportunities and researched emerging trends and consumer preferences. They introduced a new clothing line, received positive feedback from initial trials, and grew through strategic partnerships and targeted advertising. What strategic choice best describes this approach?

(a) Product Development

(b) Market Development

(c) Market Penetration

(d) Diversification **(1 Mark)**

PART II – Descriptive Questions (35 Marks)

*Question No. **1** is compulsory.*

*Attempt any **two** questions out of the remaining **three** questions.*

1. (a) *TechNova,* a leading software development firm known for its cutting-edge operating systems, is developing a groundbreaking new platform. *ElectroWave,* an emerging player in the electronics and hardware industry, specializes in manufacturing advanced devices. *TechNova* and *ElectroWave* have decided to join forces to design innovative laptops

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and smartphones, aiming to tap into new markets and broaden their business horizons. What kind of external growth strategy is being considered by *TechNova* and *ElectroWave*? **(5 Marks)**

(b) Vikram Patel owns a chain of ten bookstores across the Mumbai region. Three of these stores were launched in the past two years. He has always believed in strategic management and enjoyed robust sales of books, magazines, and educational materials until about five years ago. However, with the increasing preference for online shopping, the sales at his physical stores have declined by approximately sixty percent over the last five years. Analyze Vikram Patel's current position in light of the limitations of strategic management. **(5 Marks)**

(c) Orion Tech Solutions Pvt. Ltd. is renowned for its ability to launch groundbreaking software products. Despite the relaxed and casual work environment at Orion, there is a strong commitment to meeting deadlines. Employees at Orion believe in the "work hard, play hard" ethic. The company has shifted from a formal, hierarchical structure to a more results-oriented approach. Employees are deeply committed to the company's strategies and work diligently to achieve them. They safeguard innovations and maintain strict confidentiality and secrecy in their operations. Their work culture is closely aligned with the organization's values, practices, and norms. What aspects of an organization are being discussed? Explain. **(5 Marks)**

2. (a) Analyze the role of Key Success Factors (KSFs) in determining competitive success within an industry. **(5 Marks)**

(b) What are distribution channels, and why is analyzing them crucial for business expansion? Describe the three main types of channels explaining their roles in ensuring products reach customers efficiently and with the necessary support. **(5 Marks)**

3. (a) What is a strategic vision, and what are the essential components that make it an effective tool for guiding an organization's future? **(5 Marks)**

(b) Which strategy is implemented by redefining the business, by enlarging its scope of business and substantially increasing investment in the business? Explain the major reasons for adopting this strategy. **(5 Marks)**

4. (a) Describe the principal aspects of strategy-execution process, which are included in most situations. **(5 Marks)**

(b) How does the PESTLE framework assist in analyzing the macro-environment?

OR

A manufacturing company is in direct competition with fifteen companies at the national level. The head of marketing department of this company wishes to study the market position of rival companies by grouping them into like positions. Name the tool that may be used by him/her. Explain the procedure that may be used to implement the techniques. **(5 Marks)**

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Mock Test Paper - Series II: August, 2024

Date of Paper: 23rd August, 2024

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

INTERMEDIATE: GROUP – II

PAPER – 6: FINANCIAL MANAGEMENT & STRATEGIC MANAGEMENT

PAPER 6A : FINANCIAL MANAGEMENT

Suggested Answers/ Hints

PART I – Case Scenario based MCQs

1. (d)

2. (b)

Particulars	Computation	Result
Sales	100 × 5,00,000	5,00,00,000
Less Variable cost	100 × 4,50,000	4,50,00,000
Contribution		**50,00,000**
Less Fixed cost		25,00,000
EBIT		**25,00,000**
Less Interest	15% × 40,00,000	6,00,000
EBT		**19,00,000**

Operating leverage = Contribution ÷ EBIT = 50 Lakhs ÷ 25 Lakhs = 2 times

Operating leverage = % Change in EBIT ÷ % Change in Sales i.e. if sales increase by 10%, EBIT increase by 20%.

Financial leverage = EBIT ÷ EBT = 25 Lakhs ÷ 19 Lakhs = 1.315 times

Combined leverage = Operating leverage × Financial leverage = 2 × 1.315 = 2.63 times

3. (b)

Particulars	Weights	Cost in %	Weights × Cost
Share Capital	40,00,000	5 + 1.9 × (10 – 5) = 14.5	5,80,000
Reserves & Surplus	25,00,000	14.5	3,62,500
Preference Share Capital	12,00,000	12	1,44,000
15% Debentures	20,00,000	15 × (1 – 25%) = 11.25	2,25,000
Total	**97,00,000**	**Total Cost**	**13,11,500**

Discount rate = WACC = 13,11,500 ÷ 97,00,000 × 100 = 13.52%

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4. (b)

Particulars	Computation	Result
Savings in Tea cost	200 Employees × 200 days × 3 times × ₹ 10	12,00,000
Less: Annual maintenance		(25,000)
Less: Cost of Electricity	500 units × ₹ 24 per unit × 12 months	(1,44,000)
Less: Consumables		(8,00,000)
Less: Depreciation	5,00,000 ÷ 5 years	(1,00,000)
Profit before tax		**1,31,000**
Less: Tax	1,31,000 × 25%	32,750
Profit after tax		**98,250**
Add: Depreciation		1,00,000
Cash flow after tax	98,250 + 1,00,000	**1,98,250**

5. (b)

Year	Particulars	Cash flow	PVF@13.52%	PV
0	Initial investment	5,00,000	1	(5,00,000)
1 to 5	Savings	1,98,250	3.473	6,88,522
	Net present value			**1,88,522**

6. (b) ROCE = EBIT / Total Capital Employed

Total Capital Employed = Total Assets – Current Liabilities

= 50 lakhs – 10 lakhs

= 40 lakhs

EBIT = 40 lakhs x 15%

= 6 lakhs

Now, OL of 3.5 = Contribution / EBIT

Therefore Contribution = 6 Lakhs X 3.5 = 21 lakhs

Sales = **Contribution / PV Ratio = 21 lakhs / 0.7 = 30 lakhs**

7. (d) Calculation: Cost of Debt = (Interest Payment/ Market Price of Bond)

= (8,000 / 95,000) = 8.42%

8. (d) Cost of equity will increase. As the company increases its debt ratio, the financial risk increases, which typically leads to an increase in the cost of equity as equity investors demand a higher return for the additional risk.

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PART II – Descriptive Questions

1. (a) **Let the EBIT at the Indifference Point level be E**

Particulars	Alternative 1	Alternative 2
Description	**Fully Equity of 84 Lakhs**	**Debt = 56 Lakhs, Equity = 28 Lakhs**
EBIT	E	E
Less: Interest at 12% of ₹ 56 Lakhs	Nil	6.72
EBT	E	E – 6.72
Less: Tax at 30%	0.3 E	0.3 E – 2.016
EAT	0.7 E	0.7 E – 4.704
Less: Preference Dividend	Nil	Nil
Residual Earnings	0.7 E	0.7 E – 4.704
No. of Equity Shares (Face Value ₹ 10)	8.4 Lakh Shares	2.8 Lakh Shares
EPS = $\frac{\text{Residual Earnings}}{\text{No. of Equity Shares}}$	$\frac{0.7\text{ E}}{8.4\text{ Lakh Shares}}$	$\frac{0.7\text{ E - 4.704}}{2.8\text{ Lakh Shares}}$

For indifference between the above alternatives, EPS should be equal.

So, $\frac{0.7\text{ E}}{8.4\text{ Lakh Shares}} = \frac{0.7\text{ E - 4.704}}{2.8\text{ Lakh Shares}}$

On cross multiplication and simplification, 2.1 E – 14.112 = 0.7 E. So, 1.4 E = 14.112

So, E = $\frac{14.112}{1.4}$ = 10.08

So, for same EPS, required EBIT = ₹ 10.08 Lakhs. EPS at that level = ₹ 0.84

Note: Presentation of solution may differ.

(b) **Computation of PV of Future Cash Flows**

Year	Nature	Cash Flow	DF @ 12%	DCF
1	Dividends (₹ 100 × 20%)	20	0.893	17.86
2	Dividends (₹ 100 × 20%)	20	0.797	15.94
3	Dividends (₹ 100 × 20%)	20	0.712	14.24
4	Dividends (₹ 100 × 20%)	20	0.636	12.72
5	Dividends (₹ 100 × 1.2 × 20%)	24	0.567	13.61
6	Dividends (₹ 100 × 1.2 × 20%)	24	0.507	12.17
7	Dividends (₹ 100 × 1.2 × 20%)	24	0.452	10.85
7	Net Sale Proceeds (₹ 900 × 1.2 – 5%)	1,026	0.452	463.75

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	Present Value of Cash Inflows			561.14
0	Less: Initial Investment (₹ 500 + 5%)	525	1	525.00
	Net Present Value			36.14

Note: At the end of Year 4, Anand will have 1.2 Share i.e. 1 Bought Share + 1/5th Bonus Share.

(c) i. No of Eq. Shares (before buyback) = Total Earnings (before buyback)/EPS

= 18,00,000/(270/18)

= 1,20,000 shares

ii. Buyback price = 270 + 10% premium = 297

iii. No of Eq. shares (after buyback) = 1,20,000 (-) 20,000 = 1,00,000 shares

iv. Total Book Value of Equity (after buyback) = 1,00,000 X 193.20 = 1,93,20,000

Now,

Total BV of Eq. (after buyback) = Total BV of Eq.(before buyback) (-) Amt of buyback

1,93,20,000 = x (-) (20,000 X 297)

Therefore x = Total BV (before buyback)

= 2,52,60,000

BV per share (before buyback) = 2,52,60,000 / 1,20,000

= 210.50 per share

2. **(a)** Evaluation of Factoring Proposal -

	PARTICULARS	**₹**	**₹**
(A)	**Savings (Benefit) to the firm**		
	Administration Cost	45,000	45,000
	Bad Debts Cost (On Recourse basis) In House – 75 lakhs X 1% Factoring – 75 lakhs X 0.5% **Net Savings in bad debts cost**	(75 lakhs X 0.5%)	37,500
	Cost of Carrying Debtors Cost	**(WN – 1)**	1,06,750
	TOTAL		**1,89,250**
(B)	**Cost to the Firm:**		

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	Factor Commission [Annual credit Sales × % of Commission]	75 lakhs X 1.5%	1,12,500
	Interest Cost on Net advances	**(See WN – 1)**	53,100
	TOTAL		**1,65,600**
(C)	**Net Benefits to the Firm (A – B)**		**23,650**

Advice: Since the savings to the firm exceed the cost due to factoring, the proposal is acceptable.

WN-1 : Calculation of Savings in Interest Cost of Carrying Debtors

(I) In house Management:

Interest Cost = Credit Sales X Avg Collection Period / 360 X Interest (%) p.a

= 75,00,000 x 60/360 x 10%

= 1,25,000

(II) If Factoring services availed: If factoring services are availed, then Sukrut Limited must raise the funds blocked in receivables to the extent which is not funded by the factor (i.e amount of factor reserve **(+)** amount of factor commission for 30 days **(+)** 20% of net advances)

Calculation of Net Advances to the firm -

Debtors = 75 lakhs x 30/360 = 6,25,000

(-) Factor Reserve = 10% of above = (62,500)

(-) Factor Commission = 1.5% of Debtors = (9,375)

Net Advance = 5,53,125

Advance from Factor = 5,53,125 x 80% = 4,42,500

Int cost on Advance from Factor = 4,42,500 x 12% = 53,100

Now, the amount that is not funded by the factor (6,25,000 - 4,42,500) needs to be funded by Sukrut Limited from overdraft facility at 10%

Therefore, Int cost on Overdraft (Cost of carrying debtors) = **1,82,500 x 10% = 18,250**

Net Savings in Interest Cost of Carrying Debtors = 1,25,000 (-) 18,250 = 1,06,750

(b) Level of investment depends on the various factors listed below:

(a) Nature of Industry: Construction companies, breweries etc. requires large investment in working capital due long gestation period.

(b) Types of products: Consumer durable has large inventory as compared to perishable products.

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(c) **Manufacturing Vs Trading Vs Service:** A manufacturing entity has to maintain three levels of inventory i.e. raw material, work-in-process and finished goods whereas a trading and a service entity has to maintain inventory only in the form of trading stock and consumables respectively.

(d) **Volume of sales:** Where the sales are high, there is a possibility of high receivables as well.

(e) **Credit policy:** An entity whose credit policy is liberal has not only high level of receivables but may require more capital to fund raw material purchases as that will depend on credit period allowed by suppliers.

3. (a) **WN-1 : Calculation of Cost of Debt (Kd)**

Approximation Method = $\frac{\text{Int (1-t)+(RV – NP)/N}}{\text{(RV + NP) / 2}}$

RV = 100 + 10% = 110, NP = 105 - 4% = 100.8

$= \frac{10\ (1-0.25)+(110 – 100.8)/10}{(110 + 100.8) / 2} = 7.99\%$

YTM Method:

CMP (Po) (-) Floatation Cost = {Int(1-t) × PVAF (r%,10years)} + {RV × PVIF (r%,10th Year)}

105 - 4% = {10 (1 – 0.25) × PVAF (r%,10 years)} + {110 × PVIF (r%,10th year)}

Using trial and error method, NPV at 5% & 10%

Year	Cash flows	Disc Factor @ 5%	PV (₹)	Disc Factor @ 10%	PV (₹)
0	-100.8	1	-100.8	1	-100.8
1 to 10	7.5	7.7217	57.91275	6.1446	46.0845
10	110	0.6139	67.529	0.3855	42.405
			24.64175		**-12.3105**

IRR = $5+\frac{24.64175}{24.64175-(-12.3105)} \times (10-5) = \mathbf{8.33\%}$

Therefore overall cost of debt (Kd) = (7.99 + 8.33) / 2 = 8.16%

WN-2 : Calculation of Cost of Preference (Kp)

Approximation Method = $\frac{\text{Pref. Div.+(RV – NP)/N}}{\text{(RV + NP) / 2}}$

RV = 100 NP = 115 - 2% = 112.7

$= \frac{12 +(100 – 112.7)/10}{(100 + 112.7) / 2} = \mathbf{10.09\%}$

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YTM Method:

CMP (Po) (-) Floatation Cost = {Pref Div × PVAF (r%,10years)} + {RV × PVIF (r%,10th Year)}

115 - 2% = {12 × PVAF (r%,10 years)} + {100 × PVIF (r%,10th year)}

Using trial and error method, NPV at 5% & 10%

Year	Cash flows	Disc Factor @ 5%	PV (₹)	Disc Factor @ 10%	PV (₹)
0	-112.7	1	-112.7	1	-112.7
1 to 10	12	7.7217	92.6604	6.1446	73.7352
10	100	0.6139	61.39	0.3855	38.55
			41.3504		**-0.4148**

IRR = $5+\frac{41.3504}{41.3504 -(-0.4148)}$ X (10-5) = **9.95%**

Therefore, overall cost of debt (Kp) = (10.09 + 9.95) / 2 = 10.02%

WN-3 : Calculation of Cost of equity (Ke)

Ke = {D1 / (Po - Floatation)} + G

= {2+9% / 27 – 4.5} + 0.09

= 18.69%

Calculation of WACC using market value weights

Source of Capital	Working	Market Value	Weights	Cost (K)	WACC (Ko)
		(₹)	**(A)**	**(B)**	**(A x B)**
Equity	27 x 150000	40,50,000	0.7377	18.69	13.7877
Reserves	Included in equity	-	-	-	-
Preference	115 x 7500	8,62,500	0.1571	10.02	1.5741
Debentures	105 x 5500	5,77,500	0.1052	8.16	0.8584
		54,90,000	**1**		**16.22%**

WACC (Ko) = 16.22%

(b) Change in Reserve & Surplus = ₹ 25, 00,000 – ₹ 20,00,000 = ₹ 5,00,000

So, Net profit = ₹ 5, 00,000

(i) Net Profit Ratio = 8%

$\therefore$ Sales = $\frac{5,00,000}{8\%}$ =₹ 62,50,000

(ii) Cost of Goods sold

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= Sales – Gross profit Margin

= ₹ 62, 50,000 – 20% of ₹ 62, 50,000

= ₹ 50, 00,000

(iii) Fixed Assets = $\frac{₹\ 30,00,000}{40\%} = ₹\ 75,00,000$

(iv) Stock = $\frac{\text{Cost of Goods Sold}}{\text{STR}} = \frac{50,00,000}{4} = ₹\ 12,50,000$

(v) Debtors = $\frac{62,50,000}{360} \times 90 = ₹\ 15,62,500$

(vi) Cash Equivalent = $\frac{50,00,000}{12} \times 1.5 = ₹\ 6,25,000$

Balance Sheet as on 31st March 2024

Liabilities	(₹)	Assets	(₹)
Share Capital	50,00,000	Fixed Assets	75,00,000
Reserve and Surplus	25,00,000	Sundry Debtors	15,62,500
Long-term loan	30,00,000	Closing Stock	12,50,000
Sundry Creditors (Balancing Figure)	4,37,500	Cash in hand	6,25,000
	1,09,37,500		1,09,37,500

4. (a) Though in a sole proprietorship firm, partnership etc., owners participate in management but in corporates, owners are not active in management so, there is a separation between owner/ shareholders and managers. In theory managers should act in the best interest of shareholders however in reality, managers may try to maximise their individual goal like salary, perks etc., so there is a **principal agent relationship between managers and owners, which is known as Agency Problem**. In a nutshell, Agency Problem is the chances that managers may place personal goals ahead of the goal of owners. Agency Problem leads to Agency Cost. Agency cost is the additional cost borne by the shareholders to monitor the manager and control their behaviour so as to maximise shareholders wealth. Generally, Agency Costs are of four types (i) monitoring (ii) bonding (iii) opportunity (iv) structuring.

Addressing the agency problem

The agency problem arises if manager's interests are not aligned to the interests of the debt lender and equity investors. The agency problem of debt lender would be addressed by imposing negative covenants i.e. the managers cannot borrow beyond a point. This is one of the most important concepts of modern day finance and the application of this would be applied in the Credit Risk Management of Bank, Fund Raising, Valuing distressed companies.

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Agency problem between the managers and shareholders can be addressed if the interests of the managers are aligned to the interests of the share- holders. It is easier said than done.

However, following efforts have been made to address these issues:

- Managerial compensation is linked to profit of the company to some extent and also with the long term objectives of the company.
- Employee is also designed to address the issue with the underlying assumption that maximisation of the stock price is the objective of the investors.
- Effecting monitoring can be done.

(b) **(i)** **Sales and Lease Back:** Under this type of lease, the owner of an asset sells the asset to a party (the buyer), who in turn leases back the same asset to the owner in consideration of a lease rentals. Under this arrangement, the asset is not physically exchanged but it all happen in records only. The main advantage of this method is that the lessee can satisfy himself completely regarding the quality of an asset and after possession of the asset convert the sale into a lease agreement.

Under this transaction, the seller assumes the role of lessee (as the same asset which he has sold came back to him in the form of lease) and the buyer assumes the role of a lessor (as asset purchased by him was leased back to the seller). So, the seller gets the agreed selling price and the buyer gets the lease rentals.

(ii) **Leveraged Lease:** Under this lease, a third party is involved besides lessor and the lessee. The lessor borrows a part of the purchase cost (say 80%) of the asset from the third party i.e., lender and asset so purchased is held as security against the loan. The lender is paid off from the lease rentals directly by the lessee and the surplus after meeting the claims of the lender goes to the lessor. The lessor is entitled to claim depreciation allowance.

(iii) **Sales-aid Lease:** Under this lease contract, the lessor enters into a tie up with a manufacturer for marketing the latter's product through his own leasing operations, it is called a sales-aid lease. In consideration of the aid in sales, the manufacturer may grant either credit or a commission to the lessor. Thus, the lessor earns from both sources i.e. From lessee as well as the manufacturer.

(iv) **Close-ended and Open-ended Leases:** In the close-ended lease, the assets get transferred to the lessor at the end of lease, the risk of obsolescence, residual value etc., remain with the lessor being the legal owner of the asset. In the open-ended lease, the lessee has the option of purchasing the asset at the end of the lease period.

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(c) The basic objective of financial management is to design an appropriate capital structure which can provide the highest wealth, i.e., highest MPS, which in turn depends on EPS.

Given a level of EBIT, EPS will be different under different financing mix depending upon the extent of debt financing. The effect of leverage on the EPS emerges because of the existence of fixed financial charge i.e., interest on debt, financial fixed dividend on preference share capital. The effect of fixed financial charge on the EPS depends upon the relationship between the rate of return on assets and the rate of fixed charge. If the rate of return on assets is higher than the cost of financing, then the increasing use of fixed charge financing (i.e., debt and preference share capital) will result in increase in the EPS. This situation is also known as favourable financial leverage or Trading on Equity. On the other hand, if the rate of return on assets is less than the cost of financing, then the effect may be negative and, therefore, the increasing use of debt and preference share capital may reduce the EPS of the firm.

The fixed financial charge financing may further be analysed with reference to the choice between the debt financing and the issue of preference shares. Theoretically, the choice is tilted in favour of debt financing for two reasons: (i) the explicit cost of debt financing i.e., the rate of interest payable on debt instruments or loans is generally lower than the rate of fixed dividend payable on preference shares, and (ii) interest on debt financing is tax-deductible and therefore the real cost (after-tax) is lower than the cost of preference share capital.

OR

(c) When the cost of 'fixed cost fund' is less than the return on investment, financial leverage will help to increase return on equity and EPS. The firm will also benefit from the saving of tax on interest on debts etc. However, when cost of debt will be more than the return it will affect return of equity and EPS unfavourably and as a result firm can be under financial distress. Therefore, financial leverage is also known as "**double edged sword".**

Effect on EPS and ROE:

When, ROI > Interest – Favourable – Advantage

When, ROI < Interest – Unfavourable – Disadvantage

When, ROI = Interest – Neutral – Neither advantage nor disadvantage

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PAPER 6B: STRATEGIC MANAGEMENT

ANSWERS

PART I

1. (A)	(i)	(c)	(ii)	(b)	(iii)	(c)	(iv)	(a)	(v)	(c)
1. (B)	(i)	(a)	(ii)	(c)	(iii)	(a)				

PART II

1. (a) The collaboration between TechNova, a software development firm, and ElectroWave, an electronics and hardware manufacturing company, represents a **co-generic merger**. This type of external growth strategy involves the merger of companies from related but non-competing industries, allowing them to leverage complementary strengths and diversify their product offerings.

TechNova specializes in creating cutting-edge software, while ElectroWave focuses on manufacturing advanced electronic devices. By joining forces, they can combine their expertise to design innovative laptops and smartphones, creating products that neither company could have developed as effectively on their own. This strategic partnership allows them to enter new markets, enhance their competitive advantage, and explore synergies between software and hardware.

The co-generic merger provides significant opportunities for both companies to capitalize on shared technologies, streamline their operations, and expand their customer base. It is a strategic move that enables them to diversify while maintaining a strong focus on their core competencies, ultimately helping them to grow and compete more effectively in the global market.

(b) Vikram Patel is facing declining sales due to a significant shift of customers toward online platforms. Although he employs strategic management tools, they cannot always overcome every obstacle or guarantee success. The limitations of strategic management in Vikram's situation include:

- The environment in which strategies are developed is highly complex and unpredictable. The entry of online bookstores, a new type of competitor, introduced a different dynamic to the book retail industry. These online platforms, with their extensive reach and pricing power, have dominated the market, posing a formidable challenge to traditional bookstores.
- Another limitation of strategic management is the difficulty in forecasting future developments. Despite his strategic management efforts, Vikram Patel did not anticipate the extent to which online bookstores would impact his sales.
- While strategic management is a time-consuming process, it is crucial for Vikram to continue managing strategically. These

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challenging times demand increased effort and adaptability on his part.

- Strategic management can be costly. Vikram Patel might consider hiring experts to understand customer preferences better and adjust his strategies to offer more personalized services. These customized offerings could be difficult for online stores to replicate, giving him a competitive edge.
- The bookstores owned by Vikram Patel are much smaller in scale compared to online stores. This makes it challenging for him to predict how online platforms will manoeuvre strategically.

(c) The scenario being referred to is the organizational culture at *Orion Tech Solutions Pvt. Ltd.* A strong culture encourages effective strategy execution when there is alignment and drives performance even when there is minimal alignment. A culture rooted in values, practices, and behavioural norms that align with the requirements for successful strategy execution energizes employees across the organization to perform their roles in a manner that supports the strategy. Orion's culture, built around principles such as listening to customers, encouraging employees to take pride in their work, and providing a high degree of decision-making autonomy, is highly conducive to successfully executing a strategy focused on delivering superior software solutions.

A strong strategy-supportive culture at Orion makes employees feel genuinely better about their jobs, work environment, and the organization's goals. It motivates them to embrace the challenge of realizing the company's vision, perform their duties competently and enthusiastically, and collaborate effectively with others.

2. (a) As industry's Key Success Factors (KSFs) are those things that most affect industry members' ability to prosper in the marketplace – the particular strategy elements, product attributes, resources, competencies, competitive capabilities and business outcomes that spell the difference between profit & loss and ultimately, between competitive success or failure. KSFs by their very nature are so important that all firms in the industry must pay close attention to them. They are the prerequisites for industry success, or, to put it in another way, KSFs are the rules that shape whether a company will be financially and competitively successful.

(b) Channels represent the **distribution system** through which organizations distribute their products or provide services to customers. They play a pivotal role in reaching target markets, maximizing sales, and establishing competitive advantages.

Channel analysis is important when the business strategy is to scale up and expand beyond the current geographies and markets. When a business plans to grow to newer markets, they need to develop or leverage existing channels to get to new customers. Thus, analysis of channels that suit one's products and customers is of utmost importance.

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There are typically three channels that should be considered: sales channel, product channel and service channel.

- **The sales channel** - These are the intermediaries involved in selling the product through each channel and ultimately to the end user. The key question is: Who needs to sell to whom for your product to be sold to your end user? **For example**, many fashion designers use agencies to sell their products to retail organizations, so that consumers can access them.
- **The product channel** - The product channel focuses on the series of intermediaries who physically handle the product on its path from its producer to the end user. This is true of Australia Post, who delivers and distributes many online purchases between the seller and purchaser when using eBay and other online stores.
- **The service channel** - The service channel refers to the entities that provide necessary services to support the product, as it moves through the sales channel and after purchase by the end user. The service channel is an important consideration for products that are complex in terms of installation or customer assistance. **For example**, a Bosch dishwasher may be sold in a Bosch showroom, and then once sold it is installed by a Bosch contracted plumber.

3. (a) A strategic vision serves as a roadmap for a company’s future, detailing the specifics of technology, customer focus, geographic and product markets, and the capabilities the organization aims to develop. It answers the critical question, “Where are we going?” and provides a compelling rationale for the chosen direction, ensuring it aligns with the company’s long-term objectives.

A strategic vision outlines the organization’s aspirations, offering a broad, panoramic view of where it aims to be. It provides a clear direction, charts a strategic path for future endeavors, and helps in shaping the organizational identity.

Essentials of a strategic vision

- The entrepreneurial challenge in developing a strategic vision is **to think creatively about how to prepare a company for the future.**
- Forming a strategic vision is **an exercise in intelligent entrepreneurship**.
- A well-articulated strategic vision **creates enthusiasm among the members of the organization.**
- The best-worded vision statement **clearly illuminates the direction** in which organization is headed.

(b) The strategy in question is the **growth/expansion** strategy.

The Growth/Expansion strategy involves redefining the business, expanding its scope, and significantly increasing investments. This dynamic and vigorous approach is synonymous with promise and

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success. It entails a substantial reformulation of goals, major initiatives, and strategic moves, including investments, exploration into new products, technologies, and markets, and innovative decision-making. While promising growth, this strategy navigates the enterprise through relatively unknown and risky paths, rich with potential but also pitfalls.

Major Reasons for Adopting Growth/Expansion Strategy:

- It may become imperative when environment demands increase in pace of activity.
- Strategists may feel more satisfied with the prospects of growth from expansion; chief executives may take pride in presiding over organizations perceived to be growth-oriented.
- Expansion may lead to greater control over the market vis-a-vis competitors.
- Advantages from the experience curve and scale of operations may accrue.
- Expansion also includes intensifying, diversifying, acquiring and merging businesses.

4. **(a)** **Implementation or execution** is an operations-oriented, activity aimed at shaping the performance of core business activities in a strategy-supportive manner. In most situations, strategy-execution process includes the following principal aspects:

- ♦ **Developing budgets** that steer ample resources into those activities that are critical to strategic success.
- ♦ **Staffing the organization with the needed skills and expertise**, consciously building and strengthening strategy-supportive competencies and competitive capabilities and organizing the work effort.
- ♦ **Ensuring that policies and operating procedures facilitate** rather than impede effective execution.
- ♦ **Using the best-known practices to perform core business activities** and pushing for continuous improvement.
- ♦ **Installing information and operating systems** that enable company personnel to better carry out their strategic roles day in and day out.
- ♦ **Motivating people to pursue the target objectives energetically.**
- ♦ **Creating culture and climate conducive** to successful strategy implementation and execution.
- ♦ **Exerting the internal leadership** needed to drive implementation forward and keep improving strategy execution.

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(b) The PESTLE framework assists in analyzing the macro-environment by systematically evaluating six external factors that impact an organization's operations and strategy.

1. **Political Factors:** This includes government policies, regulations, political stability, and taxation. Understanding these factors helps organizations anticipate regulatory changes and government interventions that could affect their business environment.

2. **Economic Factors:** This involves assessing economic conditions such as interest rates, inflation, exchange rates, and economic growth. These factors influence business costs, consumer purchasing power, and overall market conditions.

3. **Social Factors:** This examines demographic trends, lifestyle changes, cultural norms, and consumer attitudes. Insights into social factors help businesses align their products and services with evolving consumer preferences and societal trends.

4. **Technological Factors:** This includes technological advancements, innovation rates, and technological infrastructure. These factors impact production processes, product development, and competitive positioning.

5. **Legal Factors:** This involves understanding business laws, employment regulations, health and safety standards, and compliance requirements. Legal factors are crucial for ensuring regulatory compliance and avoiding legal risks.

6. **Environmental Factors:** This covers ecological issues, sustainability practices, and environmental regulations. Awareness of environmental factors helps businesses adapt to climate change and meet sustainability goals.

   By analyzing these factors, the PESTLE framework provides a comprehensive understanding of the macro-environment, helping organizations anticipate changes, adapt strategies, and make informed decisions.

OR

A tool to identify the market positions of rival companies by grouping them into like positions is ***strategic group mapping.*** A strategic group consists of those rival firms which have similar competitive approaches and positions in the market.

The **procedure for constructing a strategic group map** and deciding which firms belong in which strategic group are as follows:

1. **Identify the competitive characteristics** that differentiate firms in the industry typical variables that are price/quality range (high, medium, low); geographic coverage (local, regional, national, global); degree of vertical integration (none, partial, full); product-line breadth (wide, narrow); use of distribution channels (one, some, all); and degree of service offered (no-frills, limited, full).

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2. **Plot the firms on a two-variable map** using pairs of these differentiating characteristics.
3. **Assign firms that fall in about the same strategy space** to the same strategic group.
4. **Draw circles around each strategic group** making the circles proportional to the size of the group's respective share of total industry sales revenues.

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Mock Test Paper - Series I: November, 2024

Date of Paper: 23rd November, 2024

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

INTERMEDIATE GROUP – II

PAPER – 6A : FINANCIAL MANAGEMENT & STRATEGIC MANAGEMENT

PAPER 6A: FINANCIAL MANAGEMENT

Time Allowed – 3 Hours (Total time for 6A and 6B) Maximum Marks – 50

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.*
4. *Working note should form part of the answer. Wherever necessary, suitable assumptions may be made by the candidates and disclosed by way of note. However, in answers to Questions in Division A, working notes are not required.*

PART I – Case Scenario based MCQs (15 Marks)

Write the most appropriate answer to each of the following multiple choice questions by choosing one of the four options given. All questions are compulsory.

Case Scenario I:

Small bus Company is into manufacturing mini buses. Since its establishment it has seen a phenomenal growth in both its market share and profitability. The financial statements (Statement of P&L and Balance Sheet) are shown below. The company enjoys the confidence of its shareholders who have been rewarded with growing dividends year after year. Last year too, the company had announced 20 per cent dividend, which was the highest in the automobile sector. The company has never defaulted on its loan payments and enjoys a favourable face with its lenders, which include financial institutions, commercial banks and other private debenture holders. The competition in the bus industry has increased in the past few years and the company foresees further intensification of competition with the entry of several foreign bus manufacturers; many of whom are market leaders in their respective countries. The mini bus segment especially, will witness entry of foreign majors in the near future, with latest technology being offered to the Indian customer. Small bus company's management realises the need for large scale investment in upgradation of technology and improvement of manufacturing facilities to beat competition.

While on one hand, the competition in the industry has been intensifying, on the other hand, there has been a slowdown in the Indian economy, which has not only reduced the demand for buses, but also led to adoption of price cutting strategies by various bus manufacturers.

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The Company needs ₹ 3,12,50,000 for the investment in technology and improvement of manufacturing facilities. Company has three options for the funds:

I The Company may issue 31,25,000 equity shares at ₹ 10 per share.

II The Company may issue 15,62,500 equity shares at ₹ 10 per share and 1,56,250 debentures of ₹ 100 denomination bearing an 9% rate of interest.

III The Company may issue 15,62,500 equity shares at ₹ 10 per share and 1,56,250 preference shares at ₹ 100 per share bearing an 10% rate of dividend.

The company's earnings before interest and taxes after investment is ₹ 37,50,000. Income tax rate applicable to the company is 40%.

Based on the above facts, the management of the company asked you to answer the following questions (MCQs 1 to 5):

1. What is the EPS under financial plan I?
   (a) ₹ 0.50
   (b) ₹ 0.62
   (c) ₹ 0.72
   (d) ₹ 0.44

2. What is the EPS under financial plan II?
   (a) ₹ 0.70
   (b) ₹ 0.90
   (c) ₹ 0.42
   (d) ₹ 1.10

3. What is the EPS under financial plan III?
   (a) ₹ 0.44
   (b) ₹ 0.70
   (c) ₹ 0.85
   (d) ₹ 1.20

4. What is the EBIT-EPS indifference points by formulae between Financing Plan I and Plan II?
   (a) ₹ 28,12,500.00
   (b) ₹ 29,00,000.00
   (c) ₹ 32,50,666.66
   (d) ₹ 45,15,253.56

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5. What is the EBIT-EPS indifference points by formulae between Financing Plan I and Plan III?
   (a) ₹ 36,36,666.66
   (b) ₹ 45,25,000.00
   (c) ₹ 28,56,256.25
   (d) ₹ 52,08,333.33 **(5 x 2 = 10 Marks)**

6. A company has a degree of operating leverage is 2 and degree of financial leverage is 3. If the sales of the company increase by 5% during the next quarter, the Earning Per Share (EPS) will increase by?
   (a) 20%
   (b) 30%
   (c) 50%
   (d) 60% **(2 Marks)**

7. Following are the data on a capital project being evaluated by the management of Aman Ltd.

Particulars	Project A
Annual cost saving	₹ 1,80,000
Useful life	5 years
Internal rate of return	10%
Salvage value	0
PVAF (15,4 years)	3.79

   Based upon the information, the payback period of the project will be
   (a) 2.652
   (b) 2.850
   (c) 3.790
   (d) 3.855 **(2 Marks)**

8. Under Modigliani and Miller's Dividend Irrelevance Theory, a company has ₹1,00,000 to distribute. If it chooses to retain the earnings instead of paying dividends, what happens to shareholder wealth?
   (a) Increases due to reinvestment opportunities.
   (b) Decreases due to lower immediate returns.
   (c) Remains unchanged because value depends on earnings and investment policy.
   (d) Depends on the dividend payout ratio **(1 Mark)**

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PART II – Descriptive Questions (35 Marks)

*Question No. **1** is compulsory.*

*Attempt any **two** questions out of the remaining **three** questions.*

1. (a) ABC Industries is a mid-sized company manufacturing consumer goods. Last quarter, the company reported sales of ₹ 2,00,000. The production process involves significant variable costs, which account for 50% of the sales value. Additionally, the company incurs ₹ 40,000 as fixed operating costs for rent, utilities, and management expenses. ABC Industries has also borrowed funds, leading to ₹ 10,000 as annual interest on long-term debt.

The company is currently planning to launch a new marketing campaign aimed at boosting sales by 10%. As a financial analyst at ABC Industries, you are required to:

1. CALCULATE the combined leverage.
2. ILLUSTRATE the impact of the 10% sales increase using the combined leverage. **(5 Marks)**

(b) P Ltd. has the following capital structure at book-value as on 31st March, 2024:

Particulars	(₹)
Equity share capital (1,00,000 shares)	10,00,000
12% Preference shares	15,00,000
10% Debentures	15,00,000
	40,00,000

Additional Information:

1. The equity shares of P Ltd. are currently traded at ₹ 100 per share.
2. The company expects to pay a dividend of ₹ 5 per equity share next year, with dividends projected to grow perpetually at a rate of 5% p.a.
3. The corporate tax rate is 35%.

Requirements:

1. CALCULATE the Weighted Average Cost of Capital (WACC) based on the current capital structure.
2. RECALCULATE the WACC if the company raises an additional ₹ 5 lakhs of debt by issuing 12% debentures. This change will result in:
   - An increase in the expected equity dividend to ₹ 7 per share while the growth rate remains constant at 5%.
   - A decrease in the market price of equity shares to ₹90 per share **(5 Marks)**

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(c) Vyom Limited, an IT conglomerate, is planning to take over Aryayash Limited, a startup company incorporated 2 years ago but holding a lot of prospects. To determine the buyout consideration, Vyom Limited has approached you as a Finance controller to estimate the fair value of the startup company today based on future earnings estimates. Following details of the startup company are as below -

Expected Sales in the coming year are ₹ 25 lakhs with P/V ratio of 40%. The sales are expected to grow at a rate of 20% for the next 2 years, to 40% for another 2 years, 25% in the 6th year and thereafter cash flows will grow at a steady rate of 10%. Fixed cost for the upcoming year is expected to be 12 lakhs for the first two years, ₹ 10 lakhs thereafter. Loss in any year can be set-off only against the profits of the immediate next year.

Corporate taxes applicable are 25% & 20% to Vyom Limited & Aryayash Limited respectively. Vyom Limited's desired rate of return is 15% & Cost of Capital of Aryayash Limited is 17%.

As a finance controller, CALCULATE the Fair value of Aryayash Limited.

(5 Marks)

2. (a) From the following information pertaining to M/s Anya Co. Ltd., PREPARE its trading, Profit & Loss Account for the year ended on 31 March, 2024 and a summarized Balance Sheet as at that date:

	Amt in ₹
Current Ratio	2.5
Quick Ratio	1.3
Proprietary Ratio (Fixed Assets/ Proprietary Fund)	0.6
Gross Profit to Sale Ratio	10%
Debtors Velocity	40 days
Sales	730,000
Working Capital	120,000
Bank Overdraft	15,000
Share Capital	2,50,000

Closing Stock is 10% more than opening Stock.

Net Profit is 10% of Proprietary Funds. **(6 Marks)**

(b) Paras TMT Ltd. is a TMT manufacturing company with a face value of ₹ 10 per share.

The following information is given about the company:

- The company is expected to grow @ 10% p.a. for next four years then 5% for an indefinite period.
- Rate of return expected by the shareholders on their share investments is 15%.

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- Company paid ₹ 4 as dividend per share for the current Financial Year.

FIND out the intrinsic value per share **(4 Marks)**

3. Zomo Ltd. currently has a turnover of ₹ 120 lakhs, 75% of which is on credit. The variable cost ratio is 80%, and the credit terms offered are 2/10, net 30. On the current sales volume, the bad debts are 1%, and the company spends ₹ 1,20,000 annually on administering its credit sales, including staff salaries for credit checking and collection. These costs are avoidable.

   In addition:

   - 60% of customers avail of the 2% cash discount, and the remaining customers take 60 days on average to pay after the date of sale.
   - The book debts are financed by a mix of bank borrowings and owned funds in a 1:1 ratio, with annual costs of 15% and 14%, respectively.

   However, Zomo Ltd. is also considering dynamic discounting for its cash customers, which might incentivize more customers to pay earlier by increasing the discount rate. This could lead to a potential reduction in bad debts to 0.8% but may also increase the cost of the discount offered to 2.5%.

   A factoring firm has proposed a deal with the following terms: (i) Factor reserve: 12% (ii) Guaranteed payment: 25 days (iii) Interest charges: 15% (iv) Commission: 4% of receivables.

   In addition, the company also has the option to extend the credit period for its remaining customers (who do not avail of the discount) to 75 days, which might increase sales by 10% but could result in an increase in bad debts to 1.5%.

   Given:

   1. The cost of funds is expected to rise to 16% next year.
   2. Zomo Ltd. plans to introduce late payment penalties (for customers who take more than 60 days) at 5% of outstanding receivables after 60 days.

   Assume a 360-day year.

   Required:

   - SHOULD Zomo Ltd. opt for dynamic discounting or the factoring firm's offer?
   - ANALYZE the impact of extending the credit period on the company's finances.

   COMPARE all options and RECOMMEND whether to continue with in-house management, dynamic discounting, or accept the factoring firm's offer.

   (10 Marks)

4. (a) A company is evaluating two options for financing its current assets: using short-term loans or long-term loans. HOW should the company balance risk and return in making this decision, and WHAT factors should it consider to ensure optimal financing? **(4 Marks)**

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(b) You are a financial consultant for a company that has a very high capital base but low earnings per share (EPS). EXPLAIN over-capitalization. What are the causes and consequences of over-capitalization?"

(4 Marks)

(c) "XYZ Corp. has adopted a strategy to maximize short-term profits by increasing product prices significantly. ANALYZE why this might not be a feasible operational criterion for sustainable growth." **(2 Marks)**

OR

(c) DEFINE Modified Internal Rate of Return method. **(2 Marks)**

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PAPER 6B: STRATEGIC MANAGEMENT

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 (15 Marks)

Question 1. (A) (Compulsory)

1. (A) EcoForge, a startup specializing in eco-friendly building materials crafted from agricultural waste, entered the highly competitive manufacturing industry with a vision of promoting sustainability. Despite its innovative approach, the company faced significant challenges as a new entrant, including high production costs, limited market visibility, regulatory hurdles, and fierce competition from established players. However, through strategic planning and effective execution, EcoForge successfully navigated these obstacles and positioned itself for sustainable growth.

The company's leadership recognized the importance of understanding its internal strengths and weaknesses, along with external opportunities and threats. This analysis revealed EcoForge's core advantage in sustainability and innovation, contrasted with scalability issues and market pressure from cheaper alternatives. Additionally, market analysis uncovered the potential of urban housing projects as an opportunity, while intense competition posed a significant threat.

EcoForge's leadership focused on creating unique value propositions by emphasizing its eco-friendly materials. This differentiation helped the company appeal to environmentally conscious builders and developers. To expand its market reach, EcoForge adopted strategies to deepen its presence in existing markets and explore new ones. Concurrently, it analyzed the industry landscape and identified the critical influence of regulatory policies and socio-cultural factors shaping consumer preferences.

Internally, EcoForge implemented structural and cultural changes to enhance its operational efficiency and responsiveness. By adopting a Strategic Business Unit (SBU) model, the company streamlined its decision-making process, allowing each product line to adapt quickly to market demands.

Recognizing the need for collaborative leadership, EcoForge's CEO, Ms. Aarti Mehra, invested in leadership training programs for senior managers. This shifted the company's culture from hierarchical to team-driven, encouraging innovation and cross-functional collaboration.

To enhance its competitiveness, EcoForge optimized its production and supply chain processes by addressing inefficiencies and partnering with technology providers. These efforts significantly reduced costs and

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improved product quality. Simultaneously, the company pursued green certifications and localized marketing efforts to build brand recognition, attracting environmentally conscious clients. Over three years, these initiatives enabled EcoForge to expand into new markets, secure partnerships with leading developers, and increase its revenue by 40%.

By integrating market analysis, operational improvements, and a focus on cost efficiency, EcoForge transitioned from a struggling startup to a leader in sustainable building materials, setting a benchmark for innovation and environmental stewardship in the industry.

Based on the above Case Scenario, answer the Multiple-Choice Questions.

(i) The SBU model adopted by EcoForge is an example of strategic decision-making at which level?

(a) Corporate Level

(b) Business Level

(c) Functional Level

(d) Operational Level **(2 Marks)**

(ii) EcoForge's strategy of appealing to environmentally conscious builders and developers by emphasizing its eco-friendly materials is an example of which type of generic strategy by Michael Porter?

(a) Cost Leadership

(b) Differentiation

(c) Focussed Cost Leadership

(d) Focussed Differentiation **(2 Marks)**

(iii) The case mentions EcoForge identifying "critical influence of regulatory policies and socio-cultural factors shaping consumer preferences." Which strategic analysis framework is most relevant here?

(a) SWOT Analysis

(b) Value Chain Analysis

(c) PESTLE Analysis

(d) Ansoff's Matrix **(2 Marks)**

(iv) EcoForge's strategy to deepen its presence in existing markets and explore new ones corresponds to which growth strategy in Ansoff's Matrix?

(a) Market Penetration

(b) Market Development

(c) Product Development

(d) Diversification **(2 Marks)**

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(v) Which key industry force, as per Porter's Five Forces, is reflected in EcoForge's challenges from cheaper alternatives and intense competition?

(a) Threat of New Entrants

(b) Bargaining Power of Suppliers

(c) Bargaining Power of Buyers

(d) Threat of Substitutes **(2 Marks)**

(B) Compulsory Application Based Independent MCQs

(i) The CEO of GoFlyHigh Airlines has built a high-performance team over five years by closely monitoring performance metrics, setting clear expectations, and motivating employees through rewards and structured improvement plans. Her disciplined and results-focused approach has driven organizational success by fostering accountability and maintaining high standards. This leadership style emphasizes achieving defined goals through a structured framework, balancing performance recognition with corrective measures for sustained excellence. What strategic leadership style does the CEO exhibit?

(a) Entrepreneur Leadership

(b) Transformational Leadership

(c) Transactional Leadership

(d) Intrapreneur Leadership **(2 Marks)**

(ii) UN&T reached out to Mukesh S, an entrepreneur from India to get his team to work on a mega solar energy project and enter India's deccan plateau which enjoys an abundance of sunshine. What strategy is UN&T trying to implement?

(a) Market Penetration

(b) Market Development

(c) Strategic Alliance

(d) Diversification **(2 Marks)**

(iii) Urbankey has a unique capability in rapid prototyping, allowing them to bring new products to market faster than the competitors. Such an advantage can be termed as?

(a) Market Expansion Strategy

(b) Core Competency

(c) Cost Leadership Strategy

(d) Appropriate SWOT Analysis **(1 Mark)**

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PART II – Descriptive Questions (35 Marks)

*Question No. **1** is compulsory.*

*Attempt any **two** questions out of the remaining **three** questions.*

1. (a) *Chic Threads*, a boutique fashion brand renowned for its commitment to sustainability and ethical practices, has recently launched a new line of eco-friendly clothing made from recycled materials. The brand recognizes the growing influence of environmentally conscious consumers who actively shape industry standards through their advocacy and purchasing decisions. These consumers align with *Chic Threads'* values and have a significant impact on its market position and reputation. How should *Chic Threads* effectively manage its relationship with environmentally conscious consumers, considering their high power and high interest in shaping the brand's success? **(5 Marks)**

(b) You are a strategic manager for a tech company launching a new smartphone model. The company wants to target tech-savvy consumers who value innovation and cutting-edge technology. Using the concept of customer behavior, develop a marketing strategy to promote the new smartphone. **(5 Marks)**

(c) *GreenEdge Solutions*, a mid-sized technology company, has implemented a new strategic plan focused on achieving sustainable growth and strengthening its market presence. The leadership team is determined to monitor the effectiveness of their strategies to ensure they align with the organization's overall goals and objectives. They seek a systematic approach to assess key performance areas critical to their success. What are Strategic Performance Measures (SPM), and how can *GreenEdge Solutions* effectively use them to evaluate and enhance the success of their strategic plan? **(5 Marks)**

2. (a) *Connect Group* was one of the leading makers of the mobile handsets till a few years ago and which went at the bottom of the heap. *Connect Group* didn't adapt to the current market trends, which eventually led to its downfall. Which would have helped *Connect Group* to change, adapt and survive? Explain the steps to initiate the change. **(5 Marks)**

(b) Define strategic management. Also discuss the limitations of strategic management. **(5 Marks)**

3. (a) *Easy Access* is a marketing services company providing consultancy to a range of business clients. *Easy Access* and its rivals have managed to persuade the Government to require all marketing services companies to complete a time-consuming and bureaucratic registration process and to comply with an industry code of conduct. Do you think that by doing this *Easy Access* and its rivals has an advantage in some ways to fight off competitors? Explain. **(5 Marks)**

(b) Explain in brief the various basis of differentiation strategies. **(5 Marks)**

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4. (a) *Leatherite Ltd.* was started as a leather company to manufacture footwear. Currently, they are in the manufacturing of footwears for males and females. The top management desires to expand the business in leather manufacturing goods. To expand they decided to purchase more machines to manufacture leather bags for males and females. Identify and explain the strategy opted by the top management of *Leatherite Ltd.*

(5 Marks)

(b) Major core competencies are identified in three areas - competitor differentiation, customer value and application to other markets. Discuss.

OR

Differentiation between Strategic Planning and Operational Planning.

(5 Marks)

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Mock Test Paper - Series I: November, 2024

Date of Paper: 23rd November, 2024

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

INTERMEDIATE: GROUP – II

PAPER – 6: FINANCIAL MANAGEMENT & STRATEGIC MANAGEMENT

PAPER 6A : FINANCIAL MANAGEMENT

Suggested Answers/ Hints

PART I – Case Scenario based MCQs

1. (c) ₹ 0.72

Computation of EPS under financial plan I: Equity Financing

	(₹)
EBIT	37,50,000.00
Interest	-
EBT	37,50,000.00
Less: Taxes 40%	(15,00,000.00)
PAT	22,50,000.00
No. of equity shares	31,25,000.00
EPS	0.72

2. (b) ₹ 0.90

Computation of EPS under financial plan II: Debt – Equity Mix

	(₹)
EBIT	37,50,000.00
Less: Interest	(14,06,250.00)
EBT	23,43,750.00
Less: Taxes 40%	(9,37,500.00)
PAT	14,06,250.00
No. of equity shares	15,62,500.00
EPS	0.90

3. (a) ₹ 0.44

Computation of EPS under financial plan III: Preference Shares – Equity Mix

	(₹)
EBIT	37,50,000.00
Less: Interest	-

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EBT	37,50,000.00
Less: Taxes (40%)	(15,00,000.00)
PAT	22,50,000.00
Less: Pref. dividend	(15,62,500.00)
PAT for equity shareholders	6,87,500.00
No. of Equity shares	15,62,500.00
EPS	0.44

4. (a) ₹ 28,12,500

EBIT – EPS Indifference Point- Plan I and Plan II:

$$\frac{(EBIT) \times (1 - T_C)}{N_1} = \frac{(EBIT - Interest) \times (1 - T_C)}{N_2}$$

$$\frac{EBIT(1 - 0.40)}{31,25,000} = \frac{(EBIT - 14,06,250) \times (1 - 0.40)}{15,62,500}$$

0.6EBIT = 1.2 EBIT – 16,87,500

= ₹ 28,12,500

5. (d) ₹ 52,08,333.33

EBIT – EPS Indifference Point: Plan I and Plan III

$$\frac{EBIT(1 - T_c)}{N_1} = \frac{EBIT(1 - T_c) - Pref.\ Div.}{N_2}$$

$$\frac{EBIT(1 - 0.4)}{31,25,000} = \frac{EBIT(1 - 0.4) - 15,62,500}{15,62,500}$$

0.6EBIT = 1.2EBIT – 31,25,000

EBIT = ₹ 52,08,333.33

6. (b) 30%

The formula for Degree of Combined Leverage (DCL) is:

DCL=DOL×DFL

DCL=2×3=6

The percentage change in EPS is:

% Δ EPS = DCL × % Δ Sales

% Δ EPS = 6 × 5% = 30%

7. (c) 3.79

Initial Investment = Annual Cost Savings × PVAF

Annual cost savings = ₹ 1,80,000

PVAF (10%, 5 years) = 3.79

Initial Investment = 1,80,000 × 3.79 = 6,82,200

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Payback Period = Initial Investment/ Annual Cost Savings

= 6,82,200/1,80,000

= 3.79 years

8. (c) **Remains unchanged because value depends on earnings and investment policy.**

(Explanation: M&M's theory suggests that dividend policy has no impact on shareholder wealth in a perfect market.)

PART II – Descriptive Questions

1. (a) **Statement showing Computation of Combined leverage**

	₹
Sales	2,00,000
Less: Variable costs (50%)	1,00,000
Contribution	1,00,000
Less: Fixed operating costs	40,000
EBIT	60,000
Less: Interest	10,000
Taxable Income (PBT)	50,000

Combined leverage $= \frac{C}{PBT} = \frac{1,00,000}{50,000} = 2$

The combined leverage of '2' indicates that with every increase of ₹ 1 in sales, the taxable income will increase by ₹ 2 (i.e. 1×2). This can be verified by the following computations when the sales increase by 10%

	₹
Sales	2,20,000
Less: variable costs (50%)	1,10,000
Contribution	1,10,000
Less: Fixed operating costs	40,000
EBIT	70,000
Less: Interest	10,000
Taxable Income (PBT)	60,000

It is clear from the above computation that on account of increase in sales by 10%, the profit before tax has increased by 20%.

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(b) (i) Computation of Weighted Average Cost of Capital based on existing capital structure

Source of Capital	Existing Capital structure (₹)	Weights (a)	After tax cost of capital (%) (b)	WACC (%) (a) × (b)
Equity share capital (W.N.1)	10,00,000	0.250	10.000	2.500
12% Preference share capital	15,00,000	0.375	12.000	4.500
10% Debentures (W.N.2)	15,00,000	0.375	6.500	2.438
Total	40,00,000	1.000		9.438

Working Notes:

1. Cost of Equity Capital:

$$K_e = \frac{\text{Expected dividend}(D_1)}{\text{Current Market Price}(P_0)} + \text{Growth}(g)$$

$$= \frac{₹\,5}{₹\,100} + 0.05$$

$$= 10\%$$

2. Cost of 10% Debentures

$$K_d = \frac{\text{Interest}(1-t)}{\text{Net proceeds}}$$

$$= \frac{₹\,1,50,000\,(1-0.35)}{₹\,15,00,000}$$

$$= 0.065 \text{ or } 6.5\%$$

(ii) Computation of Weighted Average Cost of Capital based on new capital structure

Source of Capital	New Capital structure (₹)	Weights (a)	After tax cost of capital (%) (b)	WACC (%) (a) x (b)
Equity share capital (W.N.3)	10,00,000	0.222	12.777	2.836
12% Preference share capital	15,00,000	0.334	12.000	4.000
10% Debentures (W.N.2)	15,00,000	0.333	6.500	2.165

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12% Debentures (W.N.4)	5,00,000	0.111	7.800	0.866
Total	45,00,000	1.000		9.867

Working Notes:

3. Cost of Equity Capital:

$$K_e = \frac{₹\,7}{₹\,90} + 0.05$$

= 12.777%

4. Cost of 12% Debentures

$$K_d = \frac{₹\,60,000\,(1-0.35)}{₹\,5,00,000}$$

= 0.078 or 7.8%

(c) Fair Value of Company = Present Value all future cash flows discounted at the expected Rate of return of acquiring company.

WN 1 – Calculation of Cash flows **₹ in Lakhs**

YEAR	**1**	**2**	**3**	**4**	**5**	**6**
Contribution (40% on sales)	10	12	14.4	20.16	28.22	35.28
(-) Fixed Cost	-12	-12	-10	-10	-10	-10
NPBT (A)	-2	0	4.4	10.16	18.22	25.28
(-) Losses Set Off	0	0	-2(Setoff)	0	0	0
Taxable Income	0	0	2.4	10.16	18.22	25.28
(-) Tax @ 25% **(B)**	0	0	0.6	2.54	4.55	6.32
Cash Flow (A – B)	**-2**	**0**	**3.8**	**7.62**	**13.66**	**18.96**
PV OF CASH FLOWS @ 15%	-1.740	0	2.50	4.35	6.79	8.19

Total PV of cash flows (yr 1 to 6) = 20.08 lakhs

(+) PV of cash flow at terminal value (end of Year 6) = $\frac{18.96 + 10\%}{0.15 - 0.10}$

= 417.12 Lakhs

Therefore, PV of above = 417.12 X PV factor (15%, 6th Year) = 180.20 lakhs

Total fair value of Aryayash limited = 20.08 + 180.20 = 200.28 Lakhs

Note – 1. Discounting rate should be the desired rate of acquiring company i.e. of Vyom Limited

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2. Terminal value of cash flows means the cash flows at that point from where it would grow at constant rate. Here it assumed that from 7th year, Cash flows/NPAT will grow at a constant rate and not sales

2. (a) Working Note:

1. Current Liabilities and Current Assets:

Let Current Liabilities be x

Given Current ratio = 2.5

Current Assets = 2.5x

Working Capital = 2.5x- x =1.5x

or x = 1,20,000/1.5 = 80,000

So Current Liabilities = 80,000

And Current Assets = 80,000 x 2.5 = 2,00,000

2. Closing Stock

Given, Quick Ratio = 1.3

$$\frac{\text{CurrentAssets - Closing Stock}}{\text{CurrentLiabilities - Bank Overdraft}} = 1.3$$

$$\frac{\text{2,00,000 - Closing Stock}}{\text{80,000 - 15,000}} = 1.3$$

or Closing Stock = 2,00,000-84,500 =1,15,500

Opening Stock = 1,15,000 x 100/110 =1,05,000

3. Debtors

Given Debtors Velocity = 40 days

$$\frac{\text{Debtors}}{\text{Sales}} \times 365 = 40$$

$$\text{Debtors} = \frac{7,30,000 \times 40}{365} = 80,000$$

4. Gross Profit = 7,30,000 x 10/100 = 73,000

5. Proprietary Fund:

Proprietary Ratio = 0.6

$$\frac{\text{Fixed Assets}}{\text{Proprietary Fund}} = 0.6$$

$$\frac{\text{Working Capital}}{\text{Proprietary Fund}} \quad 0.4$$

$$\text{Proprietary Fund} = \frac{1,20,000}{0.4} = 3,00,000$$

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Fixed Assets = 3,00,000 x 0.6 = 1,80,000

Net Profit = 10% of Proprietary Fund = 30,000

M/s Anya Co Ltd.

Trading and Profit and loss Account for the year ended 31 March 2024

Particulars	Amount in ₹	Particulars	Amount in ₹
To Opening Stock	1,05,000	By Sales	7,30,000
To Purchase (Balancing Fig.)	6,67,500	By Closing Stock	1,15,500
To Gross Profit	73,000		
	8,45,500		**8,45,500**
To Operating Expenses (Balancing Figure)	43,000	By Gross Profit	73,000
To Net Profit	30,000		
	73,000		**73,000**

Balance Sheet as on 31 March 2024

Liabilities	Amount in ₹	Assets	Amount in ₹
Share Capital	2,50,000	Fixed Assets	1,80,000
Reserves & Surplus (Opening bal. + current profit)	50,000		
Current Liabilities		*Current Assets*	
Bank Overdraft	15,000	Stock	1,15,500
Other Current Liabilities	65,000	Debtors	80,000
		Other Current Assets	4,500
	3,80,000		**3,80,000**

(b) As per Dividend discount model, the price of share is calculated as follows:

$$P = \frac{D_1}{(1+K_e)^1} + \frac{D_2}{(1+K_e)^2} + \frac{D_3}{(1+K_e)^3} + \frac{D_4}{(1+K_e)^4} + \frac{D_5}{(K_e - g)} \times \frac{1}{(1+K_e)^4}$$

Where,

P = Price per share

K_e = Required rate of return on equity

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g = Growth rate

Calculation PV of Dividends

Year	Dividend per share	PVF @ 15%	PV
1	4.4	0.870	3.828
2	4.84	0.756	3.660
3	5.324	0.658	3.503
4	5.856	0.572	3.350
Total			14.341

PV of Terminal Value = $\frac{₹5.856x1.05}{(0.15-0.05)^1} \times \frac{1}{(1+0.15)^4}$ = 61.488 x .572 = 35.171

Intrinsic value of share = PV of Dividends + PV of terminal value

= 14.341 + 35.171 = ₹ 49.512

3. 1. In-House Management of Receivables (With Dynamic Discounting)

Particulars:

1. **Cash Discount Cost:**
   - Revised discount rate: 2.5%
   - 60% of customers avail discount.
   - **Cost of Discount:** ₹ 90,00,000 × 60% × 2.5% = ₹ 1,35,000
2. **Bad Debts (Reduced to 0.8% due to dynamic discounting):**
   - ₹ 90,00,000 × 0.8% = ₹ 72,000
3. **Administration Cost:** ₹ 1,20,000
4. **Cost of Financing Receivables:**
   - **Working Note 1 (Average Collection Period):** (10 days × 60%) + (60 days × 40%) = 30 days
   - **Working Note 2 (Average Receivables):** ₹ 90,00,000 × (30/360) = ₹ 7,50,000
   - **Working Note 3 (Cost of Financing):**
     - Cost of Bank Funds: ₹ 7,50,000 × 1/2 × 15% = ₹ 56,250
     - Cost of Owned Funds: ₹ 7,50,000 × 1/2 × 14% = ₹ 52,500
     - **Total Cost of Financing Receivables:** ₹ 1,08,750

Total Cost with In-House Receivables Management and Dynamic Discounting:

Particulars	Amount (₹)
Cash Discount (₹ 90,00,000 × 60% × 2.5%)	1,35,000
Bad Debts (₹ 90,00,000 × 0.8%)	72,000
Admin Cost	1,20,000

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Cost of Financing Receivables	1,08,750
Total Cost (In-House with Dynamic Discounting):	**4,35,750**

2. Factoring Firm's Offer:

Particulars:

1. **Factoring Commission:** ₹ 90,00,000 × 4% = ₹ 3,60,000
2. **Interest Charges on Receivables:** Factor Reserve: 12%, so financing on 88% of receivables. Interest for 25 days: (₹ 90,00,000-3,60,000) × 88% × 15% × (25/360) = ₹ 79,200
3. **Cost of Owned Funds (Receivables not factored):** ₹ 13,96,800 × 14% × (25/360) = ₹ 13580

Owned Funds: (₹ 90,00,000-3,60,000) × 12% + 3,60,000 = ₹ 13,96,800

Total Cost with Factoring Firm:

Particulars	Amount (₹)
Factoring Commission (₹ 90,00,000 × 4%)	3,60,000
Interest Charges on Receivables	79,200
Cost of Owned Funds	13,580
Total Cost with Factoring:	**4,52,780**

3. Impact of Extending Credit Period:

If Zomo Ltd. extends the credit period to 75 days:

- **Sales increase:** 10% of ₹ 120,00,000 = ₹ 12,00,000

  New total turnover = ₹ 120,00,000 + ₹ 12,00,000 = ₹ 1,32,00,000

  Credit Sales (75%) = ₹ 99,00,000
- **Increased Bad Debts (1.5%):** ₹ 99,00,000 × 1.5% = ₹ 1,48,500
- **Late Payment Penalty:** Customers delaying beyond 60 days (40%): ₹ 99,00,000 × 40% × 5% = ₹ 1,98,000

A. Cash Discount Cost:

- **Discount rate:** 2% (since there's no mention of dynamic discounting in this case)
- **Percentage of customers availing discount:** 60%
- **Calculation:** ₹ 99,00,000 × 60% × 2% = ₹ 1,18,800

B. Bad Debts (Increased to 1.5%):

- **Calculation:** ₹ 99,00,000 × 1.5% = ₹ 1,48,500

C. Administration Costs (Remains the same):

- The administration cost stays fixed at ₹ 1,20,000, as no change in admin structure is mentioned.

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D. **Cost of Financing Receivables (Based on the new extended credit period):**

- **Working Note 1 (Average Collection Period):** Credit period has been extended to 75 days for customers who don't take the discount (40% of customers).
    - **Revised Average Collection Period:** (10 days × 60%) + (75 days × 40%) = 36 days
- **Working Note 2 (Average Receivables):** ₹ 99,00,000 × (36/360) = ₹ 9,90,000
- **Working Note 3 (Cost of Financing Receivables):**
    - **Cost of Bank Funds (15%):** ₹ 9,90,000× 1/2 × 15% = ₹ 74,250
    - **Cost of Owned Funds (14%):** ₹ 9,90,000 × 1/2 × 14% = ₹ 69,300
    - **Total Cost of Financing Receivables:** ₹ 74,250 + ₹ 69,300 = ₹ 1,43,550

Revised Bad Debts after Penalty:

- **Bad debts before penalty:** ₹ 1,48,500
- **Penalty earned:** ₹ 1,98,000
- **Net effect on bad debts:** ₹ 1,48,500 - ₹ 1,98,000 = (-₹ 49,500) (Zomo Ltd. would effectively earn ₹ 49,500 from penalties, reducing bad debt cost.)

4. **Total Cost Calculation:**

Now, summing up all the components:

Particulars	Amount (₹)
Cash Discount (₹ 99,00,000 × 60% × 2%)	1,18,800
Net Bad Debts after Penalty (–₹ 49,500)	-49,500
Administration Costs	1,20,000
Cost of Financing Receivables	1,43,550
Total Cost (In-House with Extended Credit Period)	**₹ 3,32,850**

5. **Final Decision:**

Option	Total Cost (₹)
In-House with Dynamic Discounting	4,35,750
Factoring Firm's Offer	4,52,780
In-House with Extended Credit Period	**3,32,850**

Recommendation: Zomo Ltd. should **extend the credit period** and continue in-house management. This option will not only reduce costs

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(due to lower bad debts offset by penalties) but also increase sales by 10%. Factoring is the least beneficial due to its high commission charges, and dynamic discounting offers only marginal savings compared to the credit extension option.

4. (a) The financing of current assets involves a trade off between risk and return. A firm can choose from short or long term sources of finance. Short term financing is less expensive than long term financing but at the same time, short term financing involves greater risk than long term financing.

Depending on the mix of short term and long term financing, the approach followed by a company may be referred as matching approach, conservative approach and aggressive approach.

In matching approach, long-term finance is used to finance fixed assets and permanent current assets and short term financing to finance temporary or variable current assets. Under the conservative plan, the firm finances its permanent assets and also a part of temporary current assets with long term financing and hence less risk of facing the problem of shortage of funds.

An aggressive policy is said to be followed by the firm when it uses more short term financing than warranted by the matching plan and finances a part of its permanent current assets with short term financing.

(b) Over-capitalization and its Causes and Consequences

It is a situation where a firm has more capital than it needs or in other words assets are worth less than its issued share capital, and earnings are insufficient to pay dividend and interest.

Causes of Over Capitalization

Over-capitalisation arises due to following reasons:

(i) Raising more money through issue of shares or debentures than company can employ profitably.

(ii) Borrowing huge amount at higher rate than rate at which company can earn.

(iii) Excessive payment for the acquisition of fictitious assets such as goodwill etc.

(iv) Improper provision for depreciation, replacement of assets and distribution of dividends at a higher rate.

(v) Wrong estimation of earnings and capitalization.

Consequences of Over-Capitalisation

Over-capitalisation results in the following consequences:

(i) Considerable reduction in the rate of dividend and interest payments.

(ii) Reduction in the market price of shares.

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(iii) Resorting to "window dressing".

(iv) Some companies may opt for reorganization. However, sometimes the matter gets worse and the company may go into liquidation.

(c) "The profit maximisation is not an operationally feasible criterion." This statement is true because Profit maximisation can be a short-term objective for any organisation and cannot be its sole objective. Profit maximization fails to serve as an operational criterion for maximizing the owner's economic welfare. It fails to provide an operationally feasible measure for ranking alternative courses of action in terms of their economic efficiency. It suffers from the following limitations:

(i) Vague term: The definition of the term profit is ambiguous. Does it mean short term or long term profit? Does it refer to profit before or after tax? Total profit or profit per share?

(ii) Timing of Return: The profit maximization objective does not make distinction between returns received in different time periods. It gives no consideration to the time value of money, and values benefits received today and benefits received after a period as the same.

(iii) It ignores the risk factor.

(iv) The term maximization is also vague.

OR

(c) **Modified Internal Rate of Return (MIRR):** There are several limitations attached with the concept of the conventional Internal Rate of Return. The MIRR addresses some of these deficiencies. For example, it eliminates multiple IRR rates; it addresses the reinvestment rate issue and produces results, which are consistent with the Net Present Value method.

Under this method, all cash flows, apart from the initial investment, are brought to the terminal value using an appropriate discount rate (usually the cost of capital). This results in a single stream of cash inflow in the terminal year. The MIRR is obtained by assuming a single outflow in the zeroth year and the terminal cash inflow as mentioned above. The discount rate which equates the present value of the terminal cash inflow to the zeroth year outflow is called the MIRR.

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PAPER 6B: STRATEGIC MANAGEMENT

ANSWERS

PART I

1. (A) (i) (a) (ii) (b) (iii) (c) (iv) (b) (v) (d)

1. (B) (i) (c) (ii) (c) (iii) (b)

PART II

1. (a) According to Mendelow's Matrix, environmentally conscious consumers who influence industry standards fall into the **Key Players** quadrant. These stakeholders possess both high power and high interest, making them crucial to the success of *Chic Threads'* sustainability-focused initiatives. Their high interest stems from their alignment with the brand's ethical and eco-friendly values, while their high power arises from their ability to shape market trends, advocate for sustainable practices, and impact on the brand's reputation through their purchasing decisions and influence within the industry.

As Key Players, these consumers require active engagement. *Chic Threads* must focus on satisfying their expectations by providing regular updates on sustainability efforts, maintaining transparent communication, and incorporating their feedback to ensure continued support. The brand should actively involve these stakeholders in its decision-making processes by seeking their input on product design and sustainability measures. Additionally, building strong relationships through targeted marketing campaigns, collaborations, and awareness initiatives will further solidify their trust and advocacy. Effectively managing this stakeholder group is vital, as their support and satisfaction directly contribute to the success of the brand's eco-friendly clothing line.

(b) To target tech-savvy consumers for the new smartphone model, the tech company can develop a marketing strategy based on customer behavior. Consumer behaviour may be influenced by a number of things. These elements can be categorised into the following conceptual domains:

- **External Influences:** Utilize online platforms and tech forums to generate buzz around the new smartphone. Partner with tech influencers and bloggers to review the product and create awareness among tech-savvy consumers.
- **Internal Influences:** Appeal to the desire for innovation and advanced features among tech-savvy consumers. Highlight the unique selling points of the new smartphone, such as its cutting-edge technology, performance, and design.
- **Decision Making:** Recognize that tech-savvy consumers are early adopters who value functionality and performance. Provide detailed specifications and comparisons with other smartphones to help them make an informed decision.

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- **Post-decision Processes:** Offer excellent customer service and support to address any technical issues or concerns. Encourage customers to provide feedback and reviews to build credibility and trust among tech-savvy consumers.

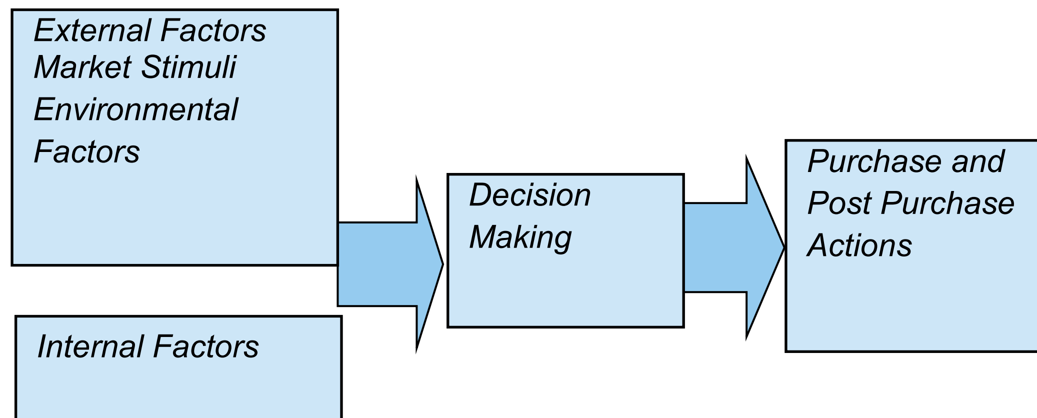

Figure: Process of consumer behaviour

By understanding the behavior of tech-savvy consumers and aligning the marketing strategy with their preferences, the tech company can effectively promote the new smartphone and attract this demographic.

(c) Strategic Performance Measures (SPM) are metrics organizations use to evaluate and track the effectiveness of their strategies in achieving their goals and objectives. SPM provides a framework for monitoring key areas critical to the organization's success, ensuring progress toward desired outcomes and enabling timely adjustments to improve performance. For *GreenEdge Solutions*, various types of SPM can be utilized:

- **Financial Measures:** Metrics like revenue growth, return on investment (ROI), and profit margins help evaluate the company's financial health and profitability.
- **Customer Satisfaction Measures:** Assessments of customer satisfaction, retention, and loyalty indicate how well the company meets customer needs.
- **Market Measures:** Market share, customer acquisition, and referral rates reflect competitiveness and market position.
- **Employee Measures:** Employee satisfaction, engagement, and turnover rate help track workplace culture and talent retention.
- **Innovation Measures:** R&D spending, patent filings, and new product launches gauge the company's innovation capabilities.
- **Environmental Measures:** Monitoring energy consumption, waste reduction, and carbon emissions ensures the company aligns with sustainability goals.

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Using these measures, *GreenEdge Solutions* can systematically assess its strategy and make informed decisions to drive sustainable growth and success.

2. **(a)** *Connect Group* has to make strategic changes for its survival. The changes in the environmental forces often require businesses to make modifications in their existing strategies and bring out new strategies. Strategic change is a complex process that involves a corporate strategy focused on new markets, products, services and new ways of doing business. Unless companies embrace change, they are likely to freeze and unless companies prepare to deal with sudden, unpredictable, discontinuous, and radical change, they are likely to be extinct.

Three steps for initiating strategic change are:

(i) **Recognise the need for change** – The first step is to diagnose the which facets of the present corporate culture are strategy supportive and which are not.

(ii) **Create a shared vision to manage change** – Objectives of both individuals and organisation should coincide. There should be no conflict between them. This is possible only if the management and the organisation members follow a shared vision.

(iii) **Institutionalise the change** – This is an action stage which requires the implementation of the changed strategy. Creating and sustaining a different attitude towards change is essential to ensure that the firm does not slip back into old ways of doing things.

(b) The term '**strategic management'** refers to the managerial process of developing a strategic vision, setting objectives, crafting a strategy, implementing and evaluating the strategy, and initiating corrective adjustments were deemed appropriate.

The presence of strategic management cannot counter all hindrances and always achieve success as there are limitations attached to strategic management. These can be explained in the following lines:

- **The environment is highly complex and turbulent.** It is difficult to understand the complex environment and exactly pinpoint how it will shape up in future. The organisational estimate about its future shape may awfully go wrong and jeopardise all strategic plans. The environment affects as the organisationhas to deal with suppliers, customers, governments and other external factors.

- **Strategic management is a time-consuming process.** Organisations spend a lot of time preparing, communicating the strategies that may impede daily operations and negatively impact on routine business.

- **Strategic management is a costly process.** Strategic management adds a lot of expenses to an organization. Expert strategic planners need to be engaged, efforts are made for analysis of external and internal environments devise strategies

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and properly implement. These can be really costly for organisations with limited resources particularly when small and medium organisation create strategies to compete.

- **Competition is unpredictable.** In a competitive scenario, where all organisations are trying to move strategically, it is difficult to clearly estimate the competitive responses to the strategies.

3. (a) Yes, *Easy Access* and its rivals get advantage by this move. The new bureaucratic process is making it more complicated for organizations to start up and enter the *Easy Access* market, increasing barriers to entry and thereby reducing the threat of new entrants. New entrants can reduce an industry's profitability, because they add new production capacity, leading to increase in supply of the product, sometimes even at a lower price and can substantially erode existing firm's market share position. However, New entrants are always a powerful source of competition. The new capacity and product range they bring in throws up a new competitive pressure. The bigger the new entrant, the more severe the competitive effect. New entrants also place a limit on prices and affect the profitability of existing players, which is known as Price War.

(b) There are several basis of differentiation, major being: Product, Pricing and Organization.

Product: Innovative products that meet customer needs can be an area where a company has an advantage over competitors. However, the pursuit of a new product offering can be costly – research and development, as well as production and marketing costs can all add to the cost of production and distribution. The payoff, however, can be great as customers' flocks are among the first to have the new product.

Pricing: It fluctuates based on its supply and demand and may also be influenced by the customer's ideal value for a product. Companies that differentiate based on product price can either determine to offer the lowest price or can attempt to establish superiority through higher prices.

Organisation: Organisational differentiation is yet another form of differentiation. Maximizing the power of a brand or using the specific advantages that an organization possesses can be instrumental to a company's success. Location advantage, name recognition and customer loyalty can all provide additional ways for a company to differentiate itself from the competition.

4. (a) *Leatherite Ltd.* is currently manufacturing footwears for males and females and its top management has decided to expand its business by manufacturing leather bags for males and females. Both the products are similar in nature within the same industry. The strategic diversification that the top management of *Leatherite Ltd.* has opted for is concentric in nature. They were in business manufacturing leather footwear and now they will manufacture leather bags as well. They will be able to use existing infrastructure and distribution channels.

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Concentric diversification amounts to related diversification.

In concentric diversification, the new business is linked to the existing businesses through process, technology or marketing. The new product is a spin-off from the existing facilities and products/processes. This means that in concentric diversification too, there are benefits of synergy with the current operations.

(b) According to C.K. Prahalad and Gary Hamel, major core competencies are identified in three areas - competitor differentiation, customer value, and application to other markets.

- **Competitor differentiation:** The company can consider having a core competence if the competence is unique and it is difficult for competitors to imitate. This can provide a company an edge compared to competitors. It allows the company to provide better products or services to market with no fear that competitors can copy it.
- **Customer value:** When purchasing a product or service it has to deliver a fundamental benefit for the end customer in order to be a core competence. It will include all the skills needed to provide fundamental benefits. The service or the product has to have real impact on the customer as the reason to choose to purchase them. If customer has chosen the company without this impact, then competence is not a core competence.
- **Application of competencies to other markets:** Core competence must be applicable to the whole organization; it cannot be only one particular skill or specified area of expertise. Therefore, although some special capability would be essential or crucial for the success of business activity, it will not be considered as core competence, if it is not fundamental from the whole organization's point of view. Thus, a core competence is a unique set of skills and expertise, which will be used throughout the organisation to open up potential markets to be exploited.

OR

Strategic planning	Operational planning
Strategic planning shapes the organisation and its resources.	Operational planning deals with current deployment of resources.
Strategic planning assesses the impact of environmental variables.	Operational planning develops tactics rather than strategy.
Strategic planning takes a holistic view of the organisation.	Operational planning projects current operations into the future.

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Strategic planning develops overall objectives and strategies.	Operational planning makes modifications to the business functions but not fundamental changes.
Strategic planning is concerned with the long-term success of the organisation.	Operational planning is concerned with the short-term success of the organisation.
Strategic planning is a senior management responsibility.	Operational planning is the responsibility of functional managers.

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Mock Test Paper - Series II: December, 2024

Date of Paper: 14th December, 2024

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

INTERMEDIATE GROUP – II

PAPER – 6A : FINANCIAL MANAGEMENT & STRATEGIC MANAGEMENT

PAPER 6A: FINANCIAL MANAGEMENT

Time Allowed – 3 Hours (Total time for 6A and 6B) Maximum Marks – 50

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.*
4. *Working note should form part of the answer. Wherever necessary, suitable assumptions may be made by the candidates and disclosed by way of note. However, in answers to Questions in Division A, working notes are not required.*

PART I – Case Scenario based MCQs (15 Marks)

Write the most appropriate answer to each of the following multiple choice questions by choosing one of the four options given. All questions are compulsory.

Case Scenario I:

MNP Ltd. is a multinational company having its operations spread mostly in India and neighbouring countries of India. The promotors of the company believed that capital structure of a company must be kept flexible and balanced, where proper mix should always be maintained between debt and equity. Such mix of debt and equity should be reviewed from time to time keeping in mind the changing situation of India and the global scenario.

The capital structure of MNP Ltd. is as under:

9% Debentures	Rs. 2,75,000
11% Preference shares	Rs. 2,25,000
Equity shares (face value: Rs. 10 per share)	Rs. 5,00,000
Total capital of the company	Rs. 10,00,000

The following are some of the additional information provided by MNP Ltd. relating to the above mentioned capital structure.

(i) Rs. 100 per debenture redeemable at par has 2% floatation cost and 10 years of maturity. The market price per debenture is Rs. 105.

(ii) Rs. 100 per preference share redeemable at par has 3% floatation cost and 10 years of maturity. The market price per preference share is Rs. 106.

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(iii) Equity share has Rs. 4 floatation cost and market price per share of Rs. 24. The next year expected dividend is Rs. 2 per share with an annual growth of 5%. The firm has a practice of paying all earnings in the form of dividends.

(iv) Corporate Income-tax rate is 35%.

Since the company is a multinational company market value weights are preferred over book value weights when calculating the Weighted Average Cost of Capital (WACC) for several reasons. The company believes that market values reflect the current market perception of a company's financial health and future prospects. This is more relevant for calculating the cost of capital today, as investors base their decisions on current market conditions. Book values, based on historical accounting principles, may not accurately represent the true economic value of the company's capital components. Market values capture the actual cost that a company would incur if it were to raise new capital in the current market. Book values might not reflect the true cost of debt due to factors like changes in interest rates or creditworthiness. Similarly, book value of equity might not reflect the current investor expectations for future dividends and growth. Market values are readily available through stock prices and market interest rates. Obtaining accurate book values, especially for intangible assets, can be a complex and time-consuming process.

On the basis of this information provided above you are required to answer the following MCQs (1 to 5):

1. Calculate the cost of equity and choose the correct answer from the following?

   (a) 14%

   (b) 15%

   (c) 16%

   (d) 17%

2. Calculate the cost of debt and choose the correct answer from the following?

   (a) 6.11%

   (b) 5.48%

   (c) 9%

   (d) 10.55%

3. Calculate the cost of preference shares and choose the correct answer from the following?

   (a) 10.57 %

   (b) 5.11%

   (c) 9%

   (d) 10%

4. Calculate the WACC using market value weights and choose the correct answer from the following?

   (a) 12.80 %

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(b) 5.11%

(c) 9%

(d) 10.55%

5. What will be the current market price of MNP Ltd.'s equity shares if Ke = 10%, expected dividend is Rs. 2 per share and annual growth rate is 5% from the following options:

(a) 40 per share

(b) 20 per share

(c) 30 per share

(d) 45 per share **(5 x 2 = 10 Marks)**

6. EBIT = 4,00,000

EBT = 3,00,000

Sales = 16,00,000

Which of the following is / are correct?

1. DFL is 1.33
2. Interest coverage ratio is 3
3. Operating profit margin is 25%

Select the correct answer using the code given below:

(a) 1, 2 and 3

(b) 1 and 2 only

(c) 1 and 3 only

(d) 3 only **(2 Marks)**

7. If velocity of stock is 3 months, annual sales amount to Rs.6 lakh at 20% gross profit margin and opening stock is Rs.90,000; what is the closing stock value?

(a) Rs. 90,000

(b) Rs. 70,000

(c) Rs. 1,50,000

(d) Rs. 1,00,000 **(2 Marks)**

8. Margin of safety is affected if:

1. P/V ratio changes
2. Fixed cost changes
3. Volume of sales changes

(a) 1 only

(b) 1 and 2 only

(c) 2 and 3 only

(d) 1, 2 and 3 **(1 Mark)**

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PART II – Descriptive Questions (35 Marks)

*Question No. **1** is compulsory.*

*Attempt any **two** questions out of the remaining **three** questions.*

1. (a) The financial statement and operating results of Alpha Limited revealed the following position as on 31st March, 2023:

—	Equity share capital (Rs. 10 fully paid share)	Rs. 20,00,000
—	Working capital	Rs. 6,00,000
—	Bank overdraft	Rs. 1,00,000
—	Current ratio	2.5 : 1
—	Liquidity ratio	1.5 : 1
—	Proprietary ratio (Net fixed assets/Proprietary fund)	.75 : 1
—	Cost of sales	Rs. 14,40,000
—	Debtors velocity	2 months
—	Stock turnover based on cost of sales	4 times
—	Gross profit ratio	20% of sales
—	Net profit ratio	15% of sales

Closing stock was 25% higher than the opening stock. There were also free reserves brought forward from earlier years. Current assets include stock, debtors and cash only. The current liabilities expect bank overdraft treated as creditors.

Expenses include depreciation of Rs. 90,000.

The following information was collected from the records for the year ended 31st March, 2024:

— Total sales for the year were 20% higher as compared to previous year.

— Balances as on 31st March, 2024 were : Stock Rs. 5,20,000, Creditors Rs. 4,15,000, Debtors Rs. 4,95,000 and Cash balance Rs. 3,10,000.

— Percentage of Gross profit on turnover has gone up from 20% to 25% and ratio of net profit to sales from 15% to 16%.

— A portion of Fixed assets was very old (book values Rs. 1,80,000) disposed for Rs. 90,000. (No depreciations to be provided on this item).

— Long-term investments were purchased for Rs. 2,96,600.

— Bank overdraft fully discharged.

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— Percentage of depreciation to Fixed assets to be provided at the rate in the previous year.

PREPARE Balance Sheet as on 31st March, 2023 and 31st March, 2024.

(5 Marks)

(b) Theta Limited is expecting an annual earning of Rs. 3 Lakhs before paying any interest and taxes. The company has Rs. 10 lakhs of 10% debentures in its capital structure. The capitalisation rate is 12.5%. You are required to calculate the value of Theta Limited as per the NI approach. Also, COMPUTE the overall cost of capital. **(5 Marks)**

(c) The following data relates to Beta Limited:

	Rs.
Sales	2,00,000
Less: Variable Expenses (30%)	60,000
Contribution	1,40,000
Fixed operating expenses	1,00,000
EBIT	40,000
Less: Interest	5,000
EBT	35,000

(i) CALCULATE by what percentage will EBT increase if sales increases by 6 percent.

(ii) CALCULATE by what percentage will EBIT increase if there is 10 per cent increase in sales?

(iii) CALCULATE by what percentage EBT increase if EBIT increases by 6 per cent? **(5 Marks)**

2. (a) ABC Ltd., a newly formed company has applied to the Private Bank for the first time for financing it's Working Capital Requirements. The following information is available about the projections for the current year: Estimated Level of Activity Completed Units of Production 31,200.

Raw Material Cost	Rs 40 per unit
Direct Wages Cost	Rs 25 per Unit
Overhead	Rs 40 per Unit (Incl Rs 10 of Depreciation)
Selling Price	Rs 150 per unit
GP Ratio (Cash Cost)	30%
Net Profit Ratio	25% (On Total cost)
Raw Material in Stock	Avg of 30 days consumption
Work in Progress Stock at 30% of FG Produced Units	****Valued at Prime Cost** Material – 90% into process

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	Relevant Conversion Cost – 60% completed
Finished Goods Stock	2,500 units
Credit Allowed by the supplier	30 Days
Credit Allowed to Purchasers	45 Days
Direct Wages [Lag in payment]	15 Days
Expected Cash Balance	1,25,000

Safety margin is to be kept at 15% of the net working capital required inclusive of the margin amount. Assume that production is carried on evenly throughout the year (360 days) and wages and overheads accrue similarly. All sales are on the credit basis. You are required to CALCULATE the Net Working Capital Requirement. **(6 Marks)**

(b) Return on Equity (ROE) is Satva Limited is 15% and the capitalization rate applicable to the company is at 20%. Satva Limited's Book Value per share (BVPS) is Rs 125. Calculate the intrinsic value of the share today using Gordon's model and Walter's model if the company's policy is to retain 65% of the earning**.** **(4 Marks)**

3. Hemsparsh Private Limited is globally recognized consultancy firm having its presence in various countries across the globe and is currently headquartered at Ahmedabad, India.

It plans to commence a new branch in the Australia owing to the untapped opportunities available there in the outsourcing business. The company hired a professional for the preparation of the Project report and the fee paid was Rs 2,00,000. The company also incurred Rs 5,00,000 in the form R&D costs. As per the project report, the Company will require an initial fund outlay of Rs 25 crores for buying property & setting up the other infrastructure. It will also require working capital amounting to Rs 5 crore. The company is planning to operate for a very long period of time, however for the sake of simplicity, calculations shall end at the end of the 10th year. The Earnings before tax but after deducting Interest Exp (EBT) estimated would be as follows –

YEAR	EBT (Amount in Rs)
1	2,00,00,000
2	2,50,00,000
3	4,00,00,000
4	4,75,00,000
5	6,00,00,000
6	6,40,00,000
7	6,15,00,000
8	5,25,00,000
9	3,80,00,000
10	2,90,00,000

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The above amounts also include an allocated common cost of Rs 12,50,000. Company will distribute 10% dividends every year on post-tax earnings. Company intends to borrow funds of 3 crores at a post-tax Interest rate of 6.5% in India. As per the tax treaty between India & Australia (Tax Agreement between two nations), first 3 years are tax free and from 4th year 75% of corporate taxes are to be paid in the country where it is headquartered and balance in the other nation. Total Corporate tax rate applicable to the company is 30%. However, tax on capital gains is to be paid at 15%, only in the headquarters. Salvage value for depreciation purpose is estimated at Rs. 90,00,000. The assets would be disposed of in the market at Rs. 3,50,00,000 at the end. Hemsparsh Private Limited desires a premium of 3% to the current MCLR of 12% (Marginal Cost of Funds based Lending Rate). Assume no other assets in the block.

CALCULATE NPV for the project and advise only from Indian law perspective.

If the company wishes to recoup its investment within 3.5 years, STATE any two measures that the company shall take. **(10 Marks)**

4. (a) EXPLAIN the difference between factoring and forfaiting **(4 Marks)**

   (b) DESCRIBE some of the tasks that demonstrate the importance of good financial management **(4 Marks)**

   (c) EXPLAIN the concept of Drop – Lock Bond (DL Bonds) **(2 Marks)**

   OR

   (c) MENTION any one advantage of stock dividend – to the company as well as to the investor **(2 Marks)**

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PAPER 6B: STRATEGIC MANAGEMENT

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 (15 Marks)

Question 1. (A) (Compulsory)

1. (A) Galaxy Enterprises Limited (GEL) operates as a diversified conglomerate with a significant presence in various industries, including electronics, packaged foods, textiles, heavy machinery, and renewable energy. Leveraging its substantial free reserves of ₹85,000 crores, GEL has built a strong brand reputation, largely driven by its market leadership across multiple sectors.

In the renewable energy sector, GEL has been the industry leader for over 15 years. The division's recent performance has been exceptional. A significant market development occurred when two competitors, Nova Green Energy Limited and Zenith Solar Limited – previously ranked second and third in market share, respectively – merged to create a new entity, Synergy Renewables Ltd (SRL). Following the merger, SRL has claimed the top spot in market share, intensifying competition.

Against this backdrop, the Chairman of GEL convened a strategic meeting with the Board of Directors, divisional heads, marketing executives, and the Group CFO. The meeting focused on formulating growth strategies for the renewable energy division, identifying opportunities for diversification, and announcing an interim dividend in honour of GEL's platinum jubilee celebrations.

Mr. Arvind Malhotra, CEO of the renewable energy division, emphasized the industry's slow pace of modernization compared to global standards. He highlighted the potential in emerging product categories, such as next-generation solar panels, energy storage systems, and advanced wind turbines. He proposed a modernization initiative requiring an investment of ₹7,000 crores. This transformation is projected to reduce operational costs by 20% and minimize wastage by 12%.

The CFO presented an analysis revealing that competitors are unlikely to invest in significant upgrades or expansions for the next 6–8 years due to financial constraints. In response, the Board approved the modernization initiative and allocated an additional ₹1,500 crores to strengthen the division's supply chain.

Another proposal discussed was GEL's entry into the electric vehicle (EV) segment. The Board approved this diversification strategy, allocating ₹8,000 crores to establish a foothold in this rapidly growing

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market. Additionally, the Board authorized the distribution of an interim dividend of ₹75 per share to commemorate GEL's platinum jubilee.

In preparing for these strategic initiatives, the Board also evaluated key stakeholders to determine their influence and interest. Shareholders and the Board of Directors emerged as primary stakeholders with both high influence and interest, necessitating active engagement to secure their support. Regulatory authorities were recognized as influential but less interested in the immediate plans, requiring regular updates to ensure compliance. Customers and employees, while not as powerful, were identified as highly interested stakeholders, particularly concerning the renewable energy division's modernization and the entry into the EV market.

Based on the above Case Scenario, answer the Multiple-Choice Questions.

(i) GEL has approved significant investments in modernizing its renewable energy division and entering the electric vehicle segment. Analyze the level of strategy these decisions represent and identify the correct justification for your answer.

(a) Functional level, as these are related to operational improvements within the renewable energy division.

(b) Business level, as these initiatives align with the goals of a single division to gain a competitive edge.

(c) Corporate level, as they involve decisions impacting the overall portfolio and diversification of GEL.

(d) Operational level, as these focus on day-to-day activities within the divisions. **(2 Marks)**

(ii) With the merger of Nova Green Energy Limited and Zenith Solar Limited into Synergy Renewables Ltd (SRL), how does this development influence GEL's strategic priorities in the renewable energy sector under Porter's Five Forces framework?

(a) The merger reduces the threat of substitutes by consolidating competing technologies.

(b) It increases the bargaining power of buyers by providing them with a stronger alternative supplier.

(c) It heightens the intensity of industry rivalry by creating a stronger competitor with greater market share.

(d) The merger strengthens the bargaining power of suppliers due to greater reliance on key inputs. **(2 Marks)**

(iii) GEL's decision to enter the EV market represents a diversification strategy. Evaluate which type of diversification strategy is being pursued and the reasoning behind this classification.

(a) Concentric diversification, as the EV market shares synergies with renewable energy technologies.

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(b) Vertical integration, as GEL seeks to integrate upstream or downstream activities in the automotive value chain.

(c) Horizontal diversification, as GEL expands into a market unrelated to its existing renewable energy operations.

(d) Conglomerate diversification, as GEL enters an entirely unrelated and independent business segment. **(2 Marks)**

(iv) GEL identified shareholders and the Board of Directors as key stakeholders. Analyze the rationale for classifying them as both high influence and high interest and how this influences strategic communication.

(a) They directly impact compliance with regulatory standards, necessitating regular updates.

(b) Their vested interest in dividends and long-term value creation makes their engagement essential for approval of key initiatives.

(c) They represent the end consumers whose perceptions directly influence GEL's market reputation.

(d) Their role in operational execution requires constant communication and support for strategy implementation. **(2 Marks)**

(v) By approving modernization in renewable energy and diversification into EVs, what corporate strategy is GEL pursuing, and how does it position the company as per Ansoff's product market growth matrix?

(a) Cost leadership, to lower operational expenses and offer competitive pricing.

(b) Product differentiation, by leveraging innovation in both existing and new markets.

(c) Market penetration, through deeper investments in existing product lines.

(d) Market expansion and diversification, to capture growth opportunities across unrelated industries. **(2 Marks)**

(B) Compulsory Application Based Independent MCQs

(i) Harish, a middle manager, is confused about the difference between flexibility and resilience while working around an uncertain situation in the organization. Can you help find the right difference between the two?

(a) Flexibility is about adapting to new things quickly, while resilience is about holding on to the current position of the things for the short-term as the organisation is confident of its efficiencies.

(b) Flexibility is a subset of resilience, and to be flexible means to be resilient.

(c) Flexibility is the opposite of resilience, where, if the organisation is flexible, it changes and if it is resilient it doesn't change at all.

(d) Both are the same. **(2 Marks)**

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(ii) Suman, the marketing head of Jalwa Music Co., was doing research on the online music streaming business in India for her new age music for youngsters. She analyzed that though the players in the market were innovating rapidly, it was difficult to maintain a sustainable competitive advantage. Which aspect of strategic management best reflects this challenge?

(a) The need for continuous innovation.

(b) The importance of understanding the competitive landscape.

(c) The dynamic and unpredictable nature of the industry.

(d) The difficulty in estimating competitors' responses. **(2 Marks)**

(iii) During which stage of the Product Life Cycle would you typically expect the highest marketing expenditure per unit sold as companies aggressively promote their product?

(a) Maturity

(b) Introduction

(c) Growth

(d) Decline **(1 Mark)**

PART II – Descriptive Questions (35 Marks)

*Question No. **1** is compulsory.*

*Attempt any **two** questions out of the remaining **three** questions.*

1. (a) *Jupiter Electronics Ltd.* is known for its ability to come out with path-breaking products. Though the work environment at Jupiters is relaxed and casual, there is a very strong commitment to deadlines. The employees believe in a “work hard play hard" ethic. The organisation has moved away from formal and hierarchical set up to a more results-driven approach. Employees are committed to strategies and work towards achieving them. They guard innovations, maintain confidentiality and secrecy in their work. They are closely related to values, practices, and norms of organisations. What aspects of an organization are being discussed? Explain. **(5 Marks)**

(b) *Reshuffle Corp* is a company that manufactures and sells office furniture. They offer a range of products, from desks and chairs to cabinets and shelves. Recently, the company has been facing increased competition from online retailers offering similar products at lower prices.

Analyzing the characteristics of products in the furniture industry, discuss how *Reshuffle Corp* can differentiate its products to maintain a competitive edge in the market. **(5 Marks)**

(c) A business consultancy firm focuses on providing specialized services in environmental management consultancy. It assists client companies in establishing robust environmental management accounting systems

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for the measurement, recording, and analysis of environmental costs. A significant portion of the firm's operations involve conducting environmental audits to verify compliance with international assurance standards in environmental management—an exclusive service not offered by its competitors. While the firm also undertakes other management consultancy projects, these constitute only a minor share of its total annual revenue. Identify the strategy categories by Michael Porter which best describes the strategy of this firm. **(5 Marks)**

2. (a) Analyze the role of Key Success Factors (KSFs) in determining competitive success within an industry. **(5 Marks)**

   (b) How the 'Strategic Business Unit' (SBU), structure becomes imperative in an organization with increase in number, size and diversity of divisions? **(5 Marks)**

3. (a) Rohit Patel has a small chemist shop in the central part of Ahmedabad. What kind of competencies Rohit can build to gain competitive advantage over online medicine sellers? **(5 Marks)**

   (b) Distinguish between Vision and Mission. **(5 Marks)**

4. (a) Vikram Patel owns a chain of ten bookstores across the Mumbai region. Three of these stores were launched in the past two years. He has always believed in strategic management and enjoyed robust sales of books, magazines, and educational materials until about five years ago. However, with the increasing preference for online shopping, the sales at his physical stores have declined by approximately sixty percent over the last five years. Analyze Vikram Patel's current position in light of the limitations of strategic management. **(5 Marks)**

   (b) Explain the strategic implications of each of the following types of business in a corporate portfolio:

   (a) Stars (b) Question Marks (c) Cash Cows (d) Dogs

   OR

   Strategic alliances are formed if they provide an advantage to all the parties in the alliance. Do you agree? Explain in brief the advantages of a strategic alliance. **(5 Marks)**

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Mock Test Paper - Series II: December, 2024

Date of Paper: 13th December, 2024

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

INTERMEDIATE: GROUP – II

PAPER – 6: FINANCIAL MANAGEMENT & STRATEGIC MANAGEMENT

PAPER 6A : FINANCIAL MANAGEMENT

Suggested Answers/ Hints

PART I – Case Scenario based MCQs

1. (b) $Ke = \frac{D1}{P0} + g$

$= \frac{2}{20} + 0.05 = 15\%$

2. (b) $K_d = \frac{I(1-t) + \frac{(RV-NP)}{n}}{\frac{(RV+NP)}{2}} = \frac{9(1-0.35) + \frac{(100-102.90)}{10}}{\frac{(100+102.90)}{2}} = 5.48\%$

3. (a) $K_p = \frac{PD + \frac{(RV-NP)}{n}}{\frac{(RV+NP)}{2}}$

$K_p = \frac{11 + \left(\frac{100-102.82}{10}\right)}{\left(\frac{100+102.82}{2}\right)} = 10.57\%$

4. (a) Calculation of WACC using market value weights

Source of capital	**Market Value**	**Weights**	**After tax cost of capital**	**WACC (K_o)**
	(₹)	**(a)**	**(b)**	**(c) = (a)×(b)**
Debentures (₹ 105 per debenture)	2,88,750	0.1672	0.0548	0.0092
Preference shares (₹ 106 per preference share)	2,38,500	0.1381	0.1057	0.0146
Equity shares (₹ 24)	12,00,000	0.6947	0.1500	0.1042
	17,27,250	1.00		0.1280

WACC (K_o) = 12.80%

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5. (a) Current Market Price $= \frac{D_1}{Ke-g}$

$= \frac{2}{0.10-0.05}$ = ₹ 40 per share

6. (c) DFL $= \frac{EBIT}{EBT}$

DFL = 4,00,000/3,00,000 = 1.33

Interest Coverage Ratio $= \frac{EBIT}{\text{Interest Expense}}$

= 4,00,000/1,00,000 = 4

Operating Profit Margin $= \frac{Sales}{EBIT} x100$

Operating Profit Margin = (4,00,000/16,00,000) × 100 = 25%

7. (c) COGS = Sales x (1−Gross Profit Margin)

COGS = 6,00,000 x (1−0.20) = 6,00,000 x 0.80 = 4,80,000

The velocity of stock is 3 months.

stock turnovers per year (12/3) = 4

Stock Turnover Ratio = COGS / Average Stock

Average Stock = 4,80,000/4 = 1,20,000

Average Stock = (Opening Stock + Closing Stock)/2

Closing Stock = 1,50,000

8. (d) 1, 2 and 3

PART II – Descriptive Questions

1. (a) Balance Sheets of Alpha Limited

Liabilities	₹		*Assets*	₹	
	31 March 2023	*31 March 2024*		*31 March 2023*	*31 March 2024*
Equity share capital (₹ 10 each fully paid)	20,00,000	20,00,000	Fixed Assets (₹18,90,000– ₹90,000)	18,00,000	15,39,000
Reserve and Surplus (balancing)	1,30,000	1,30,000	Long term investment	–	2,96,600
Profit & Loss A/c (15% of sales)	2,70,000	6,15,600	**Current Assets** (₹ 10,00,000)		

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Current Liabilities			Stock	4,00,000	5,20,000
Bank Overdraft	1,00,000	–	Sundry Debtors	3,00,000	4,95,000
Creditors	3,00,000	4,15,000	Cash at Bank (Balancing)	3,00,000	3,10,000
Total	**28,00,000**	**31,60,600**	**Total**	**28,00,000**	**31,60,600**

Calculation for 31st March, 2023

(i) Calculation of Current Liabilities

Suppose that Current Liabilities = x, then current assets will be 2.5 x

Working capital = Current Assets – Current Liabilities

6,00,000 = 2.5x – x

x = 6,00,000 / 1.5 = ₹ 4,00,000 (C.L.)

Other Current Liabilities = Current Liabilities – Bank Overdraft

(Creditors) = 4,00,000 – 1,00,000 = ₹ 3,00,000

Current Assets = 2.5 x 4,00,000 = ₹ 10,00,000

(ii) Liquid Ratio = $\frac{\text{Liquid Assets}}{\text{Current Liabilities}}$

1.5 = $\frac{\text{Liquid Assets}}{4,00,000}$

Liquid assets = ₹6,00,000

Liquid assets = Current Assets – Stock

6,00,000 = 10,00,000 – Stock

So, Stock = ₹ 4,00,000

(iii) Calculation of fixed assets: Fixed assets to proprietary fund is 0.75, working capital is therefore 0.25 of proprietary fund. So,

Fixed Assets = 6,00,000 / 0.25 x 0.75 = ₹ 18,00,000

(iv) Sales = (14,40,000 / 80) × 100 = ₹ 18,00,000

(v) Debtors = $\frac{2}{12}$ x Sales

2 / 12 × 18,00,000 = ₹ 3,00,000

(vi) Net profit = 15% of ₹18,00,000 = ₹ 2,70,000

Calculation for the year 31st March, 2024

(vii) Sales = 18,00,000 + (18,00,000 × 0.2) = 21,60,000

(viii) Calculation of fixed assets

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	₹		₹
To Opening balance	18,00,000	By Banks (Sale)	90,000
		By Loss on sales of Fixed asset	90,000
		By P & L (Dep.) (5% as in previous year)	81,000
		By Balance b/d	15,39,000
Total	18,00,000		18,00,000

(ix) Net profit for the year 2011, 16% × 21,60,000 = ₹ 3,45,600

Total Profit = 2,70,000 + 3,45,600 = ₹ 6,15,600

(b) EBIT = ₹ 3,00,000

Less: Interest = ₹ 10,00,000 × 10% = ₹ 1,00,000

Earnings available to equity shareholders = ₹ 2,00,000

Equity capitalization rate = 12.5%

Market value of equity = $\frac{₹\ 2,00,000}{12.5\%}$ = ₹ 16,00,000

Market value of debt = ₹ 10,00,000

Market value of the firm = ₹ 26,00,000

Overall cost of capital = $\frac{₹\ 3,00,000 \times 100}{₹\ 26,00,000}$ = 11.54%

(c) (i) **Increase in taxable income if sales increase by 6%.**

Combined Leverage= $\frac{\text{Contribution}}{\text{EBT}} = \frac{₹\ 1,40,000}{₹\ 35,000} = 4$

If the sales increases by 6%, EBT will increase by 24%. (4 × 6%)

(ii) Increase in EBIT if sales increase by 10%.

Operating Leverage= $\frac{\text{Contribution}}{\text{Earnings before interest and tax}} = \frac{₹1,40,000}{₹\ 40,000} = 3.5$

If sales increases by 10%, EBIT will increase by (3.5× 10) 35%.

(iii) Increase in taxable income if EBIT increase by 6%.

Financial Leverage = $\frac{\text{Earnings before interest and tax(EBIT)}}{\text{EBT}} = \frac{₹\ 40,000}{₹35,000}$

=1.14

If EBIT increases by 6%, EBT will increase by 6.8%. (1.14 × 6%)

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2. (a) Problem mentions that the company has applied to the Private Bank for financing its working capital needs. Ideally, banks would not finance for Depreciation cost being a non-cash cost and it would also not finance the profit for you. So, problem needs to be solved using Cash Cost Basis.

Estimation of working capital required (cash cost basis)

	Particulars		**Amount**
	A) Current Assets		
	A1) Stock of RM	15,84,960 x 30/360	1,32,080.00
	A2) Stock of WIP	(From Cost Statement)	4,77,360.00
	A3) Stock of FG	(From Cost Statement)	2,37,500.00
	A4) Debtors	32,74,686 x 45/360	4,09,335.75
	A5) Cash & Cash Equivalents	(Given)	1,25,000.00
	Gross Working Capital		**13,81,275.75**
Less:	**B) Current Liabilites**		
	B1) Creditors	17,17,040 x 30/360	1,43,086.67
	B2) Lag in Wages Payment	9,20,400 x 15/360	38,350.00
	Excess of Current Assets Over Current Liabilites	(A) - (B)	**11,99,839.08**
Add:	Safety Margin @ 15% Of Net Working Capital		2,11,736.31
	Net Working Capital		**14,11,575.39**

WN -1: Calculation of Profit

Profit = 25% of total cost i.e 20% of sales price

= {(31,200-2,500) x 150} x 20% = Rs. 8,61,000

WN – 2:

	Completed Units	**WIP Units**
	31,200	9,360
Raw Mat. Consumed	12,48,000	3,36,960
Direct Wages	7,80,000	1,40,400
Overheads	9,36,000	1,68,480
	29,64,000	6,45,840
Gross Factory Cost	**36,09,840**	

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Add: Op WIP	-
Less: Cl. WIP **(At Prime Cost)**	4,77,360
Cost of Production	**31,32,480**
Add: Op FG Stock	-
Less: Cl. FG Stock	2,37,500
Cash Cost of Goods Sold	**28,94,980**
Add: Selling & Distribution Expenses (Bal. Figure)	3,79,706
Cost Of Sales	**32,74,686**
Profit*	8,61,000
Sales	**41,35,686**

*It is assumed that profit is unchanged

WN 3 - Calculation of WIP stock (units) and WIP stock amount

WIP UNITS = 30% of FG produced units i.e 30% of 31,200 units

= 9,360 units

WIP amount (at prime cost)

Raw materials = 9,360 x 40 x 90% = 3,36,960

Direct wages = 9,360 x 25 x 60% = 1,40,400

WN 4 - Calculation of purchases from suppliers

Raw Materials Consumed = OP RM Stock + Purchases - Closing RM Stock

15,84,960 = 0 + Purchases – 1,32,080

Purchases = 17,17,040

WN 5 – Calculation of safety margin

Safety Margin = 15% Of Net Working Capital Needs

Excess Of CA Less CL	85	11,99,839.08
Safety Margin	15	2,11,736.31
Net Working Capital	100	1411575.388

(b) EPS = ROE x BVPS (WN 1)

EPS = 0.15 x 125 = ₹ 18.75

Growth = ROE x Retention Ratio

= 0.15 x 0.65

= 9.75%

D1 = Do (1 + g)

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= (18.75 x 35%)(1 + 0.0975)

= ₹ 7.20

Intrinsic Value of share today - Gordon's Formula

$$Po = \frac{D_1}{Ke - g}$$

$$= \frac{7.20}{0.20 - 0.0975}$$

Po = ₹ 70.24

Intrinsic Value of share today - Walter's Model

$$Po = \frac{D + \frac{r}{K_e}(E - D)}{K_e}$$

Here D = Do assuming it would remain constant through infinity

$$Po = \frac{6.5625 + \frac{0.15}{0.20}(18.75 - 6.5625)}{0.20}$$

Po = ₹ 78.51

WN 1 - Relationship between ROE-EPS-BVPS

$$ROE = \frac{\text{Earnings for Equity Shareholders}}{\text{Equity shareholders funds}}$$

If we divide the numerator and denominator with "**No of equity shares**"

$$ROE = \frac{\text{Earnings for Equity Shareholders / No of equity shares}}{\text{Equity shareholders funds / No of equity shares}}$$

Therefore, ROE = EPS / BVPS

3. Calculation of NPV (Amount in crores)

Year	1	2	3	4	5	6	7	8	9	10
EBT	2.000	2.500	4.000	4.750	6.000	6.400	6.150	5.250	3.800	2.900
Add: Interest	0.195	0.195	0.195	0.252	0.252	0.252	0.252	0.252	0.252	0.252
Add: Allocated Common Cost	0.125	0.125	0.125	0.125	0.125	0.125	0.125	0.125	0.125	0.125
Project Profit Before Tax	2.320	2.820	4.320	5.127	6.377	6.777	6.527	5.627	4.177	3.277
Less: Tax	-	-	-	1.154	1.435	1.525	1.469	1.266	0.940	0.737
Profit After Tax	2.320	2.820	4.320	3.973	4.942	5.252	5.058	4.361	3.237	2.539
Add: Depreciation	2.410	2.410	2.410	2.410	2.410	2.410	2.410	2.410	2.410	-
Cash Inflows	4.730	5.230	6.730	6.383	7.352	7.662	7.468	6.771	5.647	2.539

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Add: Release Of Working Capital	-	-	-	-	-	-	-	-	-	5.000
Add: Net Cash Inflow from sale of asset (Net Of Tax) (WN-3)	-	-	-	-	-	-	-	-	-	3.471
Total Cash Inflows	4.730	5.230	6.730	6.383	7.352	7.662	7.468	6.771	5.647	11.010
DF @ 15%	0.870	0.756	0.658	0.572	0.497	0.432	0.376	0.327	0.284	0.247
PV Cash Inflow	4.113	3.955	4.425	3.650	3.655	3.312	2.808	2.213	1.605	2.722

TOTAL PV CI = 32.458 Crores

(-) TOTAL PVCO = 30.000 Crores (Initial Outlay + Working Capital)

NPV = 2.458 Crores

ADVISE - Since NPV is positive, company should go for the project.

Notes - 1. Allocated common costs are to be excluded from cash inflows

2. Dividend distribution are deemed irrelevant for cash flow analysis
3. Discounting rate = MCLR + premium = 12 + 3 = 15%
4. Interest exp is to be excluded from the cash inflows as it is already getting covered in the discounting rate above
5. Professional fees paid for project report and R&D costs being sunk costs are irrelevant for decision making

WN 1 – Calculation of applicable taxes each year

For the first 3 years, tax will be zero and for the next 7 years tax rate applicable would 22.5% (30 x 0.75) as balance tax will be paid in Australia, so it will have no relevance under India perspective calculations.

WN – 2 Calculation of interest expense each year

Since post tax interest rate is given in the question, firstly it needs to be converted to pre-tax rate. However, for the first 3 years of the project, post-tax and pre-tax rate would be same owing to zero taxes

Interest Expense (first 3 years) = 3,00,00,000 X 6.5% = 19,50,000 or 0.195 crores

Interest Expense (next 7 years) = 3,00,00,000 x 8.39% = 25,17,000 or 0.2517 crores

Pre-tax Interest Rate $= \frac{\text{Post tax Rate}}{1 - \text{India Tax Rate}}$

= 6.5 / (1 - 0.225)

= 8.39%

WN 3 – CALCULATION OF CAPITAL GAINS INCOME IN YEAR 10

Cost of Asset remaining in the block at the beginning of Year 10

= 3,31,00,000 (2,41,00,000 + 90,00,000)

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(+) New Asset purchased during the year = 0

(-) Sale Value of the Asset = 3,50,00,000

Capital Gains Income before tax = 19,00,000

(-) Capital Gains tax = 19,00,000 x 15% = 2,85,000

Net Cash Inflow after tax = 3,50,00,000- 2,85,000

= 3,47,15,000

B) Current Payback Period = 4 + 1.927 /7.352

= 4.262 years

Target Payback Period = 3.5 years

Some key measures to reduce your Payback period are as follows (Only illustrative):

i. Emphasizing on reduction of operational costs

ii. Improving marketing thereby resulting into higher sales

iii. Incorporate product-led growth strategies

iv. Judicious efforts in bringing down the overall cost of capital thereby reducing the discounting rate and in turn better Payback period.

v. Leveraging out the presence of the fixed cost

4. (a)

Particulars	Factoring	Forfaiting
A) Meaning	**Factoring** involves sales of receivables to the financial institution called factor in exchange for immediate cash payment	**Forfaiting** is a form of export financing where the exporter sells the rights to trade receivables to a forfaiter and receives instant cash
B) Recourse or non-recourse	May be on Recourse or Non-recourse basis	Always non-recourse
C) Amount paid	Firms are generally paid 80% to 90% upfront	100% on the value of exported goods is paid
D) Type of receivables	Receivables may either domestic or international	Receivables are international
E) Cost	Factoring cost in the form of factor commission or fees is to be borne by the seller	Overseas Buyer bears the forfaiting cost, if any

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F) **Secondary market**	Factoring does not involve a secondary market for the receivables, meaning that the transaction is complete once the receivables are sold to the factor.	Forfaiting has a secondary market where the receivables can be traded, enhancing liquidity and providing additional opportunities for investors

(b) Some of the tasks that demonstrate the importance of good financial management

- Taking care not to over invest in fixed assets
- Balancing cash-outflows with cash-inflows
- Ensuring that there is a sufficient level of working capital
- Setting sales revenue targets that will deliver growth
- Increasing the Gross profit by setting the correct pricing for products or services
- Controlling the level of general and administration expenses by finding more cost-efficient ways of running the day-to-day business operations
- Tax Planning that will minimize the taxes a business has to pay

(c) A drop lock is an arrangement whereby the interest rate on a floating-rate note becomes fixed if it falls to a specified level. Above that level the rate floats based on a benchmark market rate, typically with a semi-annual reset. In other words, drop lock bonds marry the attributes of both floating-rate securities and fixed-rate securities. The drop lock effectively sets a floor on the rate and a guaranteed minimum return to

Or

(c) **Advantage to the Company -** Stock dividends are suitable in the situation of cash crunch and deficiency faced by the company and suitable when restrictions are imposed by lenders to pay the cash dividend

Advantage to the investor – Improves liquidity in the hands of the investors as bonus shares leads to breaking down of higher priced shares into lower priced shares and hence give a choice to shareholders to sell some of the lower priced shares and get some liquidity

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PAPER 6B: STRATEGIC MANAGEMENT

ANSWERS

PART I

1. (A)	(i)	(c)	(ii)	(c)	(iii)	(d)	(iv)	(b)	(v)	(d)
1. (B)	(i)	(a)	(ii)	(c)	(iii)	(b)				

PART II

1. (a) The scenario being referred to is culture in *Jupiter Electronics*. Strong culture promotes good strategy execution when there's fit and impels execution when there's negligible fit. A culture grounded in values, practices, and behavioral norms that match what is needed for good strategy execution helps energize people throughout the organization to do their jobs in a strategy-supportive manner. A culture built around such business principles as listening to customers, encouraging employees to take pride in their work, and giving employees a high degree of decision-making responsibility. This is very conducive to successful execution of a strategy of delivering superior customer service.

A strong strategy-supportive culture makes employees feel genuinely better about their jobs and work environment and the merits of what the company is trying to accomplish. Employees are stimulated to take on the challenge of realizing the organizational vision, do their jobs competently and with enthusiasm, and collaborate with others.

(b) To maintain a competitive edge in the face of increased competition, *Reshuffle Corp* can differentiate its products in several ways:

- **Tangible and Intangible Aspects:** *Reshuffle Corp* can focus on the tangible aspects of its products, such as using high-quality materials and innovative designs to create furniture that is both functional and aesthetically pleasing. Additionally, they can emphasize the intangible aspects of their products, such as excellent customer service and a strong brand reputation for reliability and durability.
- **Pricing Strategies:** While market prices are often dictated by competition, *Reshuffle Corp* can work on cost optimization to maintain profitability. They can also consider offering value-added services, such as free installation or extended warranties, to justify a higher price point.
- **Product Features:** By continually optimizing their product features based on customer feedback and market trends, *Reshuffle Corp* can ensure that their products deliver maximum satisfaction to their target customers. This may include features that enhance functionality, design, quality, and overall user experience.
- **Product Centric Approach:** *Reshuffle Corp* should keep their products at the center of their strategic activities, ensuring that all

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business processes, from production to sales and marketing, are aligned to meet customer needs and expectations.

- **Product Life Cycle Management:** *Reshuffle Corp* should be aware of the life cycle of their products and plan for reinvention or replacement accordingly. They can introduce new product lines or upgrade existing ones to keep up with changing customer preferences and market trends.

(c) By concentrating primarily on the market for consultancy services in environmental management, the firm is pursuing a **focus strategy**. Its provision of audit services, which rival firms do not offer, highlights a **differentiation strategy** within this specific market niche. Therefore, the firm is following a **focused differentiation strategy**.

A focused differentiation strategy involves offering unique features that cater to the specific needs of a narrow market segment. As with the focused low-cost strategy, narrow markets can be defined differently depending on the context. For instance, some firms using this strategy focus on a particular sales channel, such as exclusively selling online, while others may target specific demographic groups. Firms that compete on uniqueness while addressing the needs of a narrow market exemplify the **focused differentiation strategy**.

2. **(a)** As industry's Key Success Factors (KSFs) are those things that most affect industry members' ability to prosper in the marketplace – the particular strategy elements, product attributes, resources, competencies, competitive capabilities and business outcomes that spell the difference between profit & loss and ultimately, between competitive success or failure. KSFs by their very nature are so important that all firms in the industry must pay close attention to them. They are the prerequisites for industry success, or, to put it in another way, KSFs are the rules that shape whether a company will be financially and competitively successful.

(b) SBU is a part of a large business organization that is treated separately for strategic management purposes. The concept of SBU is helpful in creating an SBU organizational structure. It is a separate part of large business serving product markets with readily identifiable competitors. It is created by adding another level of management in a divisional structure after the divisions have been grouped under a divisional top management authority based on the common strategic interests.

Very large organisations, particularly those running into several products, or operating at distant geographical locations that are extremely diverse in terms of environmental factors, can be better managed by creating strategic business units. SBU structure becomes imperative in an organisation with increase in number, size and diversity. SBUs helps such organisations by:

- Establishing coordination between divisions having common strategic interest.

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- Facilitate strategic management and control.
- Determine accountability at the level of distinct business units.
- Allow strategic planning to be done at the most relevant level within the total enterprise.
- Make the task of strategic review by top executives more objective and more effective.
- Help to allocate resources to areas with better opportunities.

3. (a) Capabilities that are valuable, rare, costly to imitate, and non-substitutable are core competencies. A small chemist shop has a local presence and functions within a limited geographical area. Still, it can build its own competencies to gain competitive advantage. Rohit Patel can build competencies in the areas of:

(i) Developing personal and cordial relations with the customers.

(ii) Providing home delivery with no additional cost.

(iii) Developing a system of speedy delivery that can be difficult to match by online sellers. Being in the central part of the city, he can create a network to supply at wider locations in the city.

(iv) Having extended working hours for convenience of buyers.

(v) Providing easy credit or a system of monthly payments to the patients consuming regular medicines.

(b) The vision describes a future identity while the Mission serves as an on-going and time-independent guide.

The vision statement can galvanize the people to achieve defined objectives, even if they are stretch objectives, provided the vision is specific, measurable, achievable, and relevant and time bound. A mission statement provides a path to realize the vision in line with its values. These statements have a direct bearing on the bottom line and success of the organization.

A mission statement defines the purpose or broader goal for being in existence or in the business and can remain the same for decades if crafted well while a vision statement is more specific in terms of both the future state and the time frame. Vision describes what will be achieved if the organization is successful.

4. (a) Vikram Patel is facing declining sales due to a significant shift of customers toward online platforms. Although he employs strategic management tools, they cannot always overcome every obstacle or guarantee success. The limitations of strategic management in Vikram's situation include:

- The environment in which strategies are developed is highly complex and unpredictable. The entry of online bookstores, a new

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type of competitor, introduced a different dynamic to the book retail industry. These online platforms, with their extensive reach and pricing power, have dominated the market, posing a formidable challenge to traditional bookstores.

- Another limitation of strategic management is the difficulty in forecasting future developments. Despite his strategic management efforts, Vikram Patel did not anticipate the extent to which online bookstores would impact his sales.
- While strategic management is a time-consuming process, it is crucial for Vikram to continue managing strategically. These challenging times demand increased effort and adaptability on his part.
- Strategic management can be costly. Vikram Patel might consider hiring experts to understand customer preferences better and adjust his strategies to offer more personalized services. These customized offerings could be difficult for online stores to replicate, giving him a competitive edge.
- The bookstores owned by Vikram Patel are much smaller in scale compared to online stores. This makes it challenging for him to predict how online platforms will manoeuvre strategically.

(b) In the BCG growth-share matrix portfolio of investments are represented in two-dimensional space. The vertical axis represents market growth rate, and the horizontal axis represents relative market share. The strategic implications for various business types under BCG in the corporate portfolio are:

Stars are products or businesses that are growing rapidly and are the best opportunity for expansion. *Stars may follow the Build* strategy. They need heavy investments to maintain their position and finance their rapid growth potential.

Cash Cows are low-growth, high market share businesses or products. They generate cash and have low costs. They are established, successful, and need less investment to maintain their market share. *A strategic alternative advocated for cash cows is Harvest.*

Question Marks are low market share businesses in high-growth markets. *A strategic option for them is Hold for which t*hey need heavy investments. Question marks if left unattended are capable of becoming cash traps.

Dogs are low-growth, low-share businesses and products. *The relevant strategy is Divest.* Dogs may generate enough cash to maintain themselves, but do not have much future. Dogs should be minimized by means of divestment or liquidation.

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OR

Strategic alliances are formed if they provide an advantage to all the parties in the alliance. These advantages can be broadly categorised as follows:

(i) **Organizational:** Strategic alliances may be formed to learn necessary skills and obtain certain capabilities from the strategic partner. Strategic partners may also help to enhance productive capacity, provide a distribution system, or extend supply chain. A strategic partner may provide a good or service that complements each other, thereby creating a synergy. If one partner is relatively new or untried in a certain industry, having a strategic partner who is well-known and respected will help add legitimacy and creditability to the venture.

(ii) **Economic:** Alliances can reduce costs and risks by distributing them across the members of the alliance. Partners can obtain greater economies of scale in an alliance, as production volume increases, causing the cost per unit to decline. Finally, partners can take advantage of co-specialization, where specializations are bundled together, creating additional value.

(iii) **Strategic:** Organizations may join to cooperate instead of competing. Alliances may also create vertical integration where partners are part of the supply chain. Strategic alliances may also be useful to create a competitive advantage by the pooling of resources and skills. This may also help with future business opportunities and the development of new products and technologies. Strategic alliances may also be used to get access to new technologies or to pursue joint research and development.

(iv) **Political:** Sometimes there is need to form a strategic alliance with a local foreign business to gain entry into a foreign market either because of local prejudices or legal barriers to entry. Forming strategic alliances with politically influential partners may also help improve overall influence and position.

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6A: FINANCIAL MANAGEMENT

QUESTIONS

Division A: Case Scenario

Working Capital

1. ArMore LLP is a newly established startup dealing in manufacture of a revolutionary product HDHMR which is a substitute to conventional wood and plywood. It is an economical substitute for manufacture of furniture and home furnishing. It has been asked by a venture capitalist for an estimated amount of funds required for setting up plant and also the amount of circulating capital required. A consultant hired by the entity has advised that the cost of setting up the plant would be ₹ 5 Crores and it will require 1 year to make the plant operational. The anticipated revenue and associated cost numbers are as follows:

   Units to be sold = 3 lakh sq metres p.a.

   Sale Price of each sq mtr = ₹ 1000

   Raw Material cost = ₹ 200 per sq mtr

   Labour cost = ₹ 50 per hour

   Labour hours per sq mtr = 3 hours

   Cash Manufacturing Overheads = ₹ 75 per machine hour

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Machine hours per sq mtr = 2 hours

Selling and credit administration Overheads = ₹ 250 per sq mtr

Being a new product in the industry, the firm will have to give a longer credit period of 3 months to its customers. It will maintain a stock of raw material equal to 15% of annual consumption. Based on negotiation with the creditors, the payment period has been agreed to be 1 month from the date of purchase. The entity will hold finished goods equal to 2 months of units to be sold. All other expenses are to be paid one month in arrears. Cash and Bank balance to the tune of ₹ 25,00,000 is required to be maintained.

The entity is also considering reducing the working capital requirement by either of the two options: a) reducing the credit period to customers by a month which will lead to reduction in sales by 5%. b) Engaging with a factor for managing the receivables, who will charge a commission of 2% of invoice value and will also advance 65% of receivables @ 12% p.a. This will lead to savings in administration and bad debts cost to the extent of ₹ 20 lakhs and 16 lakhs respectively.

The entity is also considering funding a part of working capital by bank loan. For this purpose, bank has stipulated that it will grant 75% of net current assets as advance against working capital. The bank has quoted 16.5% rate of interest with a condition of opening a current account with it, which will require 10% of loan amount to be minimum average balance.

You being an finance manager, has been asked the following questions:

(i) The anticipated profit before tax per annum after the plant is operational is ....

(A) 750 Lakhs

(B) 570 Lakhs

(C) 370 Lakhs

(D) 525 Lakhs

(ii) The estimated current assets requirement in the first year of operation (debtors calculated at cost) is ....

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(A) 9,42,50,000

(B) 2,17,08,333

(C) 7,25,41,667

(D) 67,08,333

(iii) The net working capital requirement for the first year of operation is ....

(A) 9,42,50,000

(B) 2,17,08,333

(C) 7,25,41,667

(D) 67,08,333

(iv) The annualised % cost of two options for reducing the working capital is ....

(A) 18.18% and 16.92%

(B) 18.33% and 16.92%

(C) 18.59% and 18.33%

(D) 16.92% and 19.05%

(v) What will be the Maximum Permissible Bank Finance by the bank and annualised % cost of the same?

(A) 4,55,03,630 and 18.33%

(B) 5,44,06,250 and 18.33%

(C) 4,45,86,025 and 18.59%

(D) 3,45,89,020 and 19.85%

Division B: Descriptive Questions

Ratio Analysis

1. From the following information and ratios, PREPARE the Balance Sheet as on 31st March 2023 and Income Statement for the year ended on that date for Limelite & Co.

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Gross Profit	₹ 1,20,000
Shareholders' Funds	₹ 5,00,000
Gross Profit margin	40%
Net Profit Margin	10%
PBIT to PBT	2:1
Credit sales to Total sales	80%
Total Assets turnover	0.4 times
Inventory turnover (Use sales as turnover)	5 times
Average collection period (a 360 days year)	30 days
Current ratio	2
Operating expenses (excluding interest)	₹ 60,000
Long-term Debt to Equity	40%
Tax	Nil

Cost of Capital

2. Totto Ltd. has following capital structure as on 31st December 2023, which is considered to be optimum:

	(₹)
12% Debenture	4,50,000
10% Preference share capital	1,50,000
Equity shares capital (2,00,000 shares)	24,00,000

The company's share has a current market price of ₹ 30.25 per share. The expected dividend per share in next year is 50 percent of the 2023 EPS. The EPS of last 10 years is as follows. The past trends are expected to continue:

Year	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
EPS (₹)	1.180	1.311	1.456	1.616	1.794	1.99	2.209	2.452	2.723	3.023

The company can issue 14 percent new debenture and 12 percent new preference share. The company's debenture is currently selling at ₹ 99.

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The new preference issue can be sold at a net price of ₹ 9.90, paying a dividend of ₹ 1.25 per share. The company's marginal tax rate is 50%.

(i) CALCULATE the after-tax cost (a) of new debts and new preference share capital, (b) of ordinary equity, assuming new equity comes from retained earnings.

(ii) CALCULATE the marginal cost of capital for the new funds raised.

(iii) How much can be spent for capital investment before new ordinary share must be sold? Marginal cost of capital remains to be constant. (Assuming that retained earnings available for next year's investment is 50% of 2023 earnings.)

(iv) What will be marginal cost of capital (cost of fund raised in excess of the amount calculated in part (iii) if the company can sell new ordinary shares of ₹ 22 per share? Assuming both the cost of debt and of preference share capital to be constant.

Capital Structure

3. Following data is available in respect of two companies having same business risk:

Capital employed = ₹ 3,00,000, EBIT = ₹ 45,000 and K_e = 12.5%

Sources	A Ltd	B Ltd
	Levered Company (₹)	Unlevered Company (₹)
Debt (@10%)	1,50,000	Nil
Equity	1,50,000	3,00,000

An investor is holding 20% shares in levered company. CALCULATE the increase in annual earnings of investor if he switches his holding from Levered to Unlevered company.

Leverage

4. From the following financial data of Company A and Company B, PREPARE their Income Statements.

	Company A (₹)	Company B (₹)
Variable Cost	88,000	50% of sales

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Fixed Cost	26,500	-
Interest Expenses	14,000	11,000
Financial Leverage	5 : 1	-
Margin of Safety	-	0.25
Income Tax Rate	30%	30%
EBIT	-	14,000

Investment Decisions

5. HMR Ltd. is considering replacing a manually operated old machine with a fully automatic new machine. The old machine had been fully depreciated for tax purpose but has a book value of ₹ 2,50,000 on 31st March. The machine has begun causing problems with breakdowns and it cannot fetch more than ₹ 40,000 if sold in the market at present. It will have no realizable value after 10 years. The company has been offered ₹ 1,50,000 for the old machine as a trade in on the new machine which has a price (before allowance for trade in) of ₹ 6,00,000. The expected life of new machine is 10 years with salvage value of ₹ 35,000.

   Further, the company follows written down value method depreciation @ 10% but for tax purpose, straight line method depreciation is used considering that this is the only machine in the block of assets. A working capital of ₹ 50,000 will be needed and it will be released at the end of tenth year.

   Given below are the expected sales and costs from both old and new machine:

	Old machine	New machine
Annual output	60,000 units	80,000 units
Selling price per unit	₹ 18	₹ 18
Annual operating hours	2,800	2,800
Material cost per unit	₹ 5	₹ 5
Labour cost per hour	₹ 50	₹ 75
Indirect cash cost per annum	₹ 1,00,000	₹ 1,75,000

   From the above information, ANALYSE whether the old machine should be replaced or not if the opportunity cost of capital of the Company is 10%?

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The Income tax rate is 30%. Further assume that book profit is treated as ordinary income for tax purpose.

Also ESTIMATE the internal rate of return of the replacement decision.

All calculations to be calculated to 3 decimal places.

Dividend Decision

6. MCO Ltd. has a paid-up share capital of ₹ 10,00,000, face value of ₹ 10 each. The current market price of the shares is ₹20 each. The Board of Directors of the company has an agenda of meeting to pay a dividend of 25% to its shareholders. The company expects a net income of ₹ 5,20,000 at the end of the current financial year. Company also plans for a capital expenditure for the next financial year for a cost of ₹ 7,50,000, which can be financed through retained earnings and issue of new equity shares.

   Company's desired rate of investment is 15%.

   Required:

   Following the Modigliani- Miller (MM) Hypothesis, DETERMINE value of the company when:

   (i) It does not pay dividend and

   (ii) It does pay dividend

Working Capital

7. PQ Ltd. has commenced new business segment in 2023-24. The following information has been ascertained for annual production of 25,000 units which is the full capacity.

	Cost per unit (₹)
Material	100
Labour and variable overhead expenses	50
Fixed manufacturing expenses	35
Depreciation	15
Selling expenses (80% variable)	10

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In the first two years of operations, production and sales are expected to be as follows:

Year	Production (No. of units)	Sales (No. of units)
1	12,000	10,000
2	18,000	19,000

The selling price is expected to be ₹ **250** .

To assess the working capital requirements, the following additional information is available:

(a)	Stock of materials	2 months' average consumption
(b)	Debtors	1.5 month's average sales.
(c)	Cash balance	₹ 50,000
(d)	Creditors for supply of materials	1 month's average purchase during the year.
(e)	Expenses	All expenses will be paid 1 month in advance during the year.

Goods equal to 15% of the year's production (in terms of physical units) will be in process on the average requiring full materials but only 40% of the other expenses.

The management is also of the opinion to make 10% margin for contingencies on computed figure and value the closing stock at cost of production.

PREPARE, for the two years:

(i) A projected statement of Profit/Loss (Ignoring taxation); and

(ii) A projected statement of working capital requirements on a cash cost basis.

Miscellaneous

8. (i) EXPLAIN as to how the wealth maximisation objective is superior to the profit maximisation objective

(ii) EXPLAIN the importance of trade credit and accruals as source of working capital. What is the cost of these sources?

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SUGGESTED ANSWERS/HINTS

Division A: Case Scenario

1. **(i)** **(A)** 750 Lakhs

	Units	Per unit (₹)	Amount (₹)
Raw Material consumption	3,50,000	200	7,00,00,000
labour cost	3,50,000	150	5,25,00,000
Production Overheads	3,50,000	150	5,25,00,000
Cost of Production	**3,50,000**	**500**	**17,50,00,000**
Less: Stock of FG	50,000	500	2,50,00,000
COGS	**3,00,000**	**500**	**15,00,00,000**
Selling and admin exp	3,00,000	250	7,50,00,000
Cost of Sales	**3,00,000**	**750**	**22,50,00,000**
Sales	3,00,000	1000	30,00,00,000
Profit	**3,00,000**	**250**	**7,50,00,000**

Stock of FG (sq. mtr.) = 30,00,000x2/12 = 50,000

Units sold = 3,00,000

Raw material consumed (sq. mtr.) = 3,50,000

Raw Material Purchases = Consumption + RM stock (15%)
= 7,00,00,000 + 1,05,00,000

= ₹ 8,05,00,000

(ii) **(A)** **9,42,50,000**

Stock of Raw Material (15% of 7,00,00,000) = 1,05,00,000

Stock of finished goods = 2,50,00,000

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Debtors (22,50,00,000 x 3/12) = 5,62,50,000

Cash = 25,00,000

Total Current Assets = 9,42,50,000

(iii) (C) 7,25,41,667

Working Capital Statement

	Amount (₹)
Stock of Raw Material (15% of 7,00,00,000)	1,05,00,000
Stock of finished goods	2,50,00,000
Debtors (22,50,00,000 x 3/12)	5,62,50,000
Cash	25,00,000
Total Current Assets	**9,42,50,000**
Creditors (8,05,00,000 x 1/12)	67,08,333
O/s Exp (18,00,00,000 x 1/12)	1,50,00,000
Total Current Liabilities	**2,17,08,333**
Net Working Capital	**7,25,41,667**

(iv) (A) 18.18% and 16.92%

Cost reducing debtors credit period

Debtors credit period = 2 months

Debtors balance = 21,37,50,000(2,85,000 units) x 2/12 = ₹3,56,25,000

Debtors credit period = 3 months

Debtors balance = 22,50,00,000 x 3/12 = ₹ 5,62,50,000

Amount released from debtors = ₹ 2,06,25,000

reduction in profit (15,000 units x ₹ 250) = ₹ 37,50,000

% p.a. cost (37,50,000/2,06,25,000) = **18.18%**

Costs of factoring

Commission (2% of 30 crores) = ₹ 60,00,000

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Interest = ₹ 58,50,000

(30cr x 65% x 12% x 3/12)

savings = ₹ 36,00,000

Net cost of factoring $\frac{82,50,000}{65\% \text{ of } 30cr. \text{ i.e. } 19,50,00,000} \times \frac{12}{3}$

= ₹ 82,50,000

% p.a. cost = **16.92%**

(v) (B) 5,44,06,250 and 18.33%

Maximum Permissible Bank Finance = 75% of 7,25,41,667 = ₹ 5,44,06,250

Annualised cost of bank loan = 16.5/90% = 18.33%

Division A: Descriptive Questions

1. Gross Profit = ₹ 1,20,000

Gross Profit Margin = 40%

∴ Sales = $\frac{\text{Gross Profit}}{\text{Gross Profit Margin}}$ = ₹ 1,20,000 / 0.40 = ₹ 3,00,000

Net profit (PBT) = 3,00,000 x 10% = ₹ 30,000

PBIT/PBT = 2

PBIT = 2 x 30,000

PBIT = 60,000

Interest = 60,000 – 30,000 = ₹ 30,000

Credit Sales to Total Sales = 80%

∴Credit Sales = ₹ 3,00,000×0.80 = ₹ 2,40,000

Total Assets Turnover = 0.4 times

∴Total Assets = $\frac{\text{Sales}}{\text{Total Assets Turnover}}$

= $\frac{₹\ 3,00,000}{0.4}$ = ₹ 7,50,000

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Inventory turnover = 5 times

Inventory $= \frac{\text{Sales}}{\text{Inventory turnover}} = \frac{3,00,000}{5}$ = ₹ 60,000

Average Collection Period = 30 days

$\therefore$ Debtors turnover $= \frac{360}{\text{Average Collection Period}}$ = 360/30 = 12

$\therefore$ Debtors $= \frac{\text{Credit Sales}}{\text{Debtors turnover}} = \frac{₹\ 2,40,000}{12}$ = ₹ 20,000

Current ratio = 2

2 $= \frac{\text{Debtors} + \text{Inventory} + \text{Cash (Current Assets)}}{\text{Creditors (Current Liabilities)}}$

2 Creditors = (₹ 20,000 + ₹ 60,000 + Cash)

2 Creditors = ₹ 80,000 + Cash ------------- (i)

Long-term Debt to Equity = 40%

Shareholders' Funds (Equity) = ₹ 5,00,000

$\therefore$ Long-term Debt = ₹ 5,00,000 × 40% = ₹ 2,00,000

Creditors = Total Assets – (Shareholder's fund + Long term debt)

= ₹ 7,50,000 – (5,00,000 + 2,00,000) = ₹ 50,000

$\therefore$ Cash = (₹ 50,000×2) – ₹ 80,000 = ₹ 20,000 [From equation (i)]

Income Statement

	(₹)
Sales	3,00,000
Less: Cost of Goods Sold	1,80,000
Gross Profit	1,20,000
Less: Operating Expenses	60,000
PBIT	60,000
Less: Interest	30,000
Net Profit	30,000

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Balance Sheet

Liabilities	₹	Assets		₹
Equity share capital	5,00,000	Fixed asset (bal. fig.)		6,50,000
Long term debt	2,00,000	Current assets:		
Current liability	50,000	Stock	60,000	
		Receivables	20,000	
		Cash	20,000	1,00,000
	7,50,000			7,50,000

2. (i) Calculation of after-tax cost of the followings:

(a) New 14% Debentures (K_d) $= \frac{I(1-t)}{NP} = \frac{₹\,14(1-0.5)}{₹\,99}$

$= 0.0707$ or 7.07%

New 12% Preference Shares (K_p) $= \frac{PD}{NP} = \frac{₹\,1.25}{₹\,9.90}$

$= 0.1263$ or 12.63%

Where,

I = Interest

t = Tax rate

PD = Preference dividend

NP = Net proceeds

(b) Equity Shares (Retained Earnings) (K_e)

$$= \frac{\text{Expected dividend}(D_1)}{\text{Current market price}(P_0)} + \text{Growth rate}(G)$$

$$= \frac{50\% \text{ of } ₹\,3.023}{₹\,30.25} + 0.11^* = 0.16 \text{ or } 16\%$$

* Growth rate (on the basis of EPS) is calculated as below :

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$$\frac{\text{EPS in current year - EPS in previous year}}{\text{EPS in previous year}} = \frac{₹\,3.023 - ₹\,2.723}{₹\,2.723} = 0.11$$

(Students may verify the growth trend by applying the above formula to last three or four years. Growth Rate is rounded off)

(ii) Calculation of marginal cost of capital (on the basis of existing capital structure):

Source of capital	Weight (a)	After tax Cost of capital (%) (b)	WACC (%) (a) × (b)
14% Debenture	0.15	7.07	1.0605
12% Preference shares	0.05	12.63	0.6315
Equity shares	0.80	16.00	12.800
Marginal cost of capital			14.492

(iii) The company can spend for capital investment before issuing new equity shares and without increasing its marginal cost of capital:

Retained earnings can be available for capital investment

= 50% of 2023 EPS × equity shares outstanding

= 50% of ₹ 3.023 × 2,00,000 shares = ₹3,02,300

Since, marginal cost of capital is to be maintained at the current level i.e. 14.492%, the retained earnings should be equal to 80% of total additional capital for investment.

Thus, investment before issuing equity $\left(\frac{₹\,3,02,300}{80} \times 100\right)$

= ₹ 3,77,875

The remaining capital of ₹ 75,575 i.e. ₹ 3,77,875– ₹ 3,02,300 shall be financed by issuing 14% Debenture and 12% preference shares in the ratio of 3 : 1 respectively.

(iv) If the company spends more than ₹ 3,77,875 as calculated in part (iii) above, it will have to issue new shares at ₹ 22 per share.

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The cost of new issue of equity shares will be:

$$K_e = \frac{\text{Expected dividend}(D_1)}{\text{Current market price}(P_0)} + \text{Growth rate}(g) = \frac{50\% \text{ of } ₹ 3.023}{₹ 22} + 0.11$$

= 0.1787 or 17.87%

Calculation of marginal cost of capital (assuming the existing capital structure will be maintained):

Source of capital	Weight (a)	Cost (%) (b)	WACC (%) (a) × (b)
14% Debenture	0.15	7.07	1.0605
12% Preference shares	0.05	12.63	0.6315
Equity shares	0.80	17.87	14.296
Marginal cost of capital			15.988

3. (i) Valuation of firms

Particulars	A Ltd	B Ltd
	Levered Firm (₹)	Unlevered Firm (₹)
EBIT	45,000	45,000
Less: Interest on debt (10% × ₹ 1,50,000)	15,000	Nil
Earnings available to Equity shareholders	30,000	45,000
Ke	12.5%	12.5%
Value of Equity (S) (Earnings available to Equity shareholders/Ke)	2,40,000	3,60,000
Debt (D)	1,50,000	Nil
Value of Firm (V) = S + D	3,90,000	3,60,000

Value of Levered company is more than that of unlevered company. Therefore, investor will sell his shares in levered company and buy shares in unlevered company. To maintain the

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level of risk he will borrow proportionate amount and invest that amount also in shares of unlevered company.

(ii) Investment & Borrowings

	₹
Sell shares in Levered company (₹ 2,40,000 x 20%)	48,000
Borrow money (₹ 1,50,000 x 20%)	30,000
Buy shares in Unlevered company	78,000

(iii) Change in Return

	₹
Income from shares in Unlevered company	
(₹ 78,000 x 12.5%)	9,750
Less: Interest on loan (₹ 30,000 x 10%)	3,000
Net Income from unlevered firm	6,750
Less: Income from Levered firm (₹ 48,000 x 12.5%)	6,000
Incremental Income due to arbitrage	750

4. Income Statements of Company A and Company B

	Company A (₹)	Company B (₹)
Sales	1,32,000	1,12,000
Less: Variable cost	88,000	56,000
Contribution	44,000	56,000
Less: Fixed Cost	26,500	42,000
Earnings before interest and tax (EBIT)	17,500	14,000
Less: Interest	14,000	11,000
Earnings before tax (EBT)	3,500	3,000
Less: Tax @ 30%	1,050	900
Earnings after tax (EAT)	2,450	2,100

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Working Notes:

Company A

(i) Financial Leverage = $\frac{\text{EBIT}}{\text{EBT i.e EBIT - Interest}}$

So, 5 = $\frac{\text{EBIT}}{\text{EBIT - 14,000}}$

Or, 5 (EBIT – 14,000) = EBIT

Or, 4 EBIT = 70,000

Or, EBIT = ₹17,500

(ii) Contribution = EBIT + Fixed Cost

= ₹ 17,500 + ₹ 26,500 = ₹ 44,000

(iii) Sales = Contribution + Variable cost

= ₹ 44,000 + ₹ 88,000

= ₹ 1,32,000

Company B

(i) Operating Leverage =1/Margin of Safety = $\frac{\text{Contribution}}{\text{EBIT}}$

1/0.25 = $\frac{\text{Contribution}}{₹14,000}$

4 = $\frac{\text{Contribution}}{₹14,000}$

Contribution = ₹14,000 x 4 = ₹56,000

(ii) Fixed Cost = Contribution – EBIT = 56,000 – 14,000 = ₹ 42,000

(iii) Contribution = 50% of Sales (as Variable Cost is 50% of Sales)

Sales = 56,000 x 2 = ₹1,12,000

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5. Workings:

(i) Initial Cash Outflow:

	Amount (₹)
Cost of new machine	6,00,000
Less: Sale Price of existing machine Net of Tax (₹ 1,50,000 × 0.70)	1,05,000
	4,95,000

(ii) Terminal Cash Flows:

New Machine

	Amount (₹)
Salvage value of Machine	35,000
Less: Depreciated WDV {₹ 6,00,000 - (₹ 56,500 × 10 years)}	35,000
Short Term Capital Gain (STCG)	Nil
Tax	Nil
Net Salvage Value (cash flows)	35,000

(iii) Computation of additional cash flows (yearly)

Particulars	**Existing machine**	**New Machine**	**Incremental**
(1)	(2)	(3)	(4)=(3)–(2)
Annual output	60,000 units	80,000 units	20,000 units
	₹	₹	₹
(A) Sales revenue @ ₹ 18 per unit	10,80,000	14,40,000	3,60,000
(B) Less: Cost of Operation			
Material @ ₹ 5 per unit	3,00,000	4,00,000	1,00,000
Labour			
Old = 2,800 x ₹ 50	1,40,000		70,000

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New = 2,800 x ₹ 75		2,10,000	
Indirect cash cost	1,00,000	1,75,000	75,000
Total Cost (B)	5,40,000	7,85,000	2,45,000
Profit Before Tax and depreciation (PBTD) (A – B)	5,40,000	6,55,000	1,15,000
Less: Depreciation $\left(\frac{6,00,000 - 35,000}{10}\right)$			56,500
Earning after depreciation before Tax			58,500
Less: Tax @30%			17,550
Earning after depreciation and Tax			40,950
Add: Depreciation			56,500
Net Cash inflow			97,450

Analysis: Since the Incremental Cash flow is positive, the old machine should be replaced.

Note: As mentioned in the question WDV of Machine is zero for tax purpose hence no depreciation shall be provided in existing machine.

(iv) Calculation of IRR

Computation of NPV @ 10%

	Period	Cash flow (₹)	PVF @ 10%	PV (₹)
Incremental cash flows	1-10	97,450	6.144	5,98,733
Add: Release of Working Capital	10	50,000	0.386	19,300
Add: Terminal year cash	10	35,000	0.386	13,510
				6,31,543

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Less: Initial cash outflow	0	4,95,000	1	4,95,000
Less: Working capital	0	50,000	1	50,000
			NPV	86,543

Since NPV computed in Part (i) is positive. Let us discount cash flows at higher rate say at 20%

	Period	Cash flow (₹)	PVF @ 20%	PV (₹)
Incremental cash flows	1-10	97,450	4.192	4,08,510
Add: Release of Working Capital	10	50,000	0.162	8,100
Add: Terminal year cash	10	35,000	0.162	5,670
				4,22,280
Less: Initial cash outflow	0	4,95,000	1	4,95,000
Less: Working capital	0	50,000	1	50,000
			NPV	(1,22,720)

Now we use interpolation formula:

$$10\% + \frac{86,543}{86,543 - (-1,22,720)} \times 10\%$$

$$10\% + \frac{86,543}{2,09,263} \times 10\%$$

IRR = 10% + 4.14% = 14.14%

Summary of Results

		Decision
Incremental Cash Flow	₹ 97,450	Accept
IRR	14.14% > Cost of Capital (10%)	Accept

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6. As per MM Hypothesis, value of firm/ company is calculated as below:

$$Vf \text{ or } nP_0 = \frac{(n+\Delta n)P_1 - I + E}{(1+K_e)}$$

Where,

V_f = Value of firm in the beginning of the period

n = number of shares in the beginning of the period

Δn = number of shares issued to raise the funds required

I = Amount required for investment

E = total earnings during the period

(i) Value of the ZX Ltd. when dividends are not paid.

$$nP_o = \frac{(n+\Delta n)P_1 - I + E}{1+K_e}$$

$$nP_0 = \frac{\left(1,00,000 + \frac{2,30,000}{23}\right) \times ₹23 - ₹7,50,000 + ₹5,20,000}{(1+0.15)}$$

$$= \frac{₹25,30,000 - ₹7,50,000 + ₹5,20,000}{(1+0.15)} = ₹20,00,000$$

Working notes:

1. Price of share at the end of the period (P_1)

$$P_o = \frac{P_1 + D_1}{1+K_e}$$

$$20 = \frac{P_1 + 0}{1+0.15} \qquad \text{or,} \quad P_1 = ₹\ 23$$

2. Calculation of funds required for investment

Earnings	₹ 5,20,000
Dividend distributed	Nil

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Fund available for investment	₹5,20,000
Total Investment	₹7,50,000
Balance Funds required	₹2,30,000

3. Calculation of no. of shares required to be issued for balance fund

No. of shares (Δn) $= \dfrac{\text{Funds required}}{\text{Price at end}(P_1)} = \dfrac{2,30,000}{23}$ shares

= 10,000 shares

(ii) Value of the ZX Ltd. when dividends are paid.

$$nP_o = \frac{(n+\Delta n)P_1 - I + E}{1+K_e}$$

$$nP_0 = \frac{\left(1,00,000 + \dfrac{4,80,000}{20.5}\right) \times ₹\,20.5 - ₹\,7,50,000 + ₹\,5,20,000}{(1+0.15)}$$

$$= \frac{₹25,30,000 - ₹7,50,000 + ₹5,20,000}{(1+0.15)} = ₹20,00,000$$

Working notes:

4. Price of share at the end of the period (P_1)

$$P_o = \frac{P_1 + D_1}{1+K_e}$$

$$20 = \frac{P_1 + 2.5}{1+0.15} \quad \text{or,} \quad P_1 = ₹\,20.5$$

5. Calculation of funds required for investment

Earnings	₹ 5,20,000
Dividend distributed	₹ 2,50,000
Fund available for investment	₹ 2,70,000
Total Investment	₹ 7,50,000
Balance Funds required	₹ 4,80,000

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6. Calculation of no. of shares required to be issued for balance fund

$$\text{No. of shares } (\Delta n) = \frac{\text{Funds required}}{\text{Price at end}(P_1)} = \frac{4,80,000}{20.5}$$

= 23,415 shares(approx.)

Note- As per MM-hypothesis of dividend irrelevance, value of firm remains same irrespective of dividend paid. In the solution, there may be variation in value, which is due to rounding off error.

7. (i) PQ Limited

Projected Statement of Profit / Loss

(Ignoring Taxation)

	Year 1	**Year 2**
Production (Units)	12,000	18,000
Sales (Units)	10,000	19,000
	(₹)	**(₹)**
Sales revenue (A) (Sales unit × ₹ 250)	25,00,000	47,50,000
Cost of production:		
Materials cost (Units produced × ₹ 100)	12,00,000	18,00,000
Direct labour and variable expenses (Units produced × ₹ 50)	6,00,000	9,00,000
Fixed manufacturing expenses (Production Capacity: 25,000 units × ₹ 35)	8,75,000	8,75,000
Depreciation (Production Capacity: 25,000 units × ₹ 15)	3,75,000	3,75,000
Gross Factory Cost	**30,50,000**	**39,50,000**

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Add: Opening W.I.P.	-	2,91,000
Less: Closing W.I.P.	2,91,000	3,99,000
Cost of goods produced	**27,59,000**	**38,42,000**
Add: Opening stock of finished goods (Year 1 : Nil; Year 2 : 2,000 units)	-	4,59,833
Cost of Goods available for sale (Year 1: 12,000 units; Year 2: 20,000 units)	27,59,000	43,01,833
Less: Closing stock of finished goods at average cost (year 1: 2000 units, year 2 : 1000 units) (Cost of Production × Closing stock/ units produced)	4,59,833	2,13,444
Cost of Goods Sold	**22,99,167**	**40,88,389**
Add: Selling expenses – Variable (Sales unit × ₹ 8)	80,000	1,52,000
Add: Selling expenses -Fixed (25,000 units × ₹ 2)	50,000	50,000
Cost of Sales : (B)	24,29,167	42,90,389
Profit (+) / Loss (-): (A - B)	**70,833**	**4,59,611**

Working Notes:

Calculation of Stock of Work-in-progress

Particulars	**Year 1**	**Year 2**
	(₹)	**(₹)**
Raw Material (material cost × 15%)	1,80,000	2,70,000
Labour & Mfg. Expenses (Labour & mfg. expenses × 15% × 40%)	88,500	1,06,500
Depreciation (Depreciation × 15% × 40%)	22,500	22,500
Total	2,91,000	3,99,000

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1. Calculation of creditors for supply of materials:

	Year 1 (₹)	Year 2 (₹)
Materials consumed during the year	12,00,000	18,00,000
Add: Closing stock (2 month's average consumption)	2,00,000	3,00,000
	14,00,000	21,00,000
Less: Opening Stock	-	2,00,000
Purchases during the year	14,00,000	19,00,000
Average purchases per month (Creditors)	1,16,667	1,58,333

2. Prepayment for expenses:

	Year 1 (₹)	Year 2 (₹)
Direct labour and variable expenses	6,00,000	9,00,000
Fixed manufacturing expenses	8,75,000	8,75,000
Selling expenses (variable + fixed)	1,30,000	2,02,000
Total	16,05,000	19,77,000
Average per month	1,33,750	1,64,750

(ii) Projected Statement of Working Capital Requirement (Cash Cost Basis)

	Year 1 (₹)	Year 2 (₹)
(A) Current Assets		
Inventories:		
- Stock of Raw Material (12,000 units ₹ 100 2/12); (18,000 units ₹ 100 2/12)	2,00,000	3,00,000
- Finished Goods (Refer working note 3)	4,01,083	1,92,611
- Work In Process (Refer working note 5)	2,68,500	3,76,500

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	Receivables (Debtors) (Refer working note 4)	2,66,927	4,84,684
	Prepayment for Expenses (Refer working note 2)	1,33,750	1,64,750
	Minimum Cash balance	50,000	50,000
	Total Current Assets/ Gross working capital (A)	13,20,260	15,68,545
(B)	**Current Liabilities**		
	Creditors for raw material (Refer working note 1)	1,16,667	1,58,333
	Total Current Liabilities	1,16,667	1,58,333
	Net Working Capital (A – B)	12,03,594	14,10,212
	Add: 10% contingency margin	1,20,359	1,41,021
	Total Working capital required	**13,23,953**	**15,51,233**

Working Note:

3. Cash Cost of Production:

	Year 1 (₹)	Year 2 (₹)
Gross Factory Cost as per projected Statement of P&L	30,50,000	39,50,000
Add: Opening W.I.P	-	2,68,500
Less: Closing W.I.P	2,68,500	3,76,500
Cost of goods produced	27,81,500	38,42,000
Less: Depreciation	(3,75,000)	(3,75,000)
Cash Cost of Production	24,06,500	34,67,000
Add: Opening Stock at Average Cost:	-	4,01,083
Cash Cost of Goods Available for sale	24,06,500	38,68,083
Less: Closing Stock at Avg. Cost	4,01,083	1,92,611

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$\left(\frac{₹\,24,06,500 \times 2,000}{12,000}\right)$		
$\left(\frac{₹\,34,67,000 \times 1,000}{18,000}\right)$		
Cash Cost of Goods Sold	20,05,417	36,75,472

4. Receivables (Debtors)

	Year 1 (₹)	Year 2 (₹)
Cash Cost of Goods Sold	20,05,417	36,75,472
Add: Selling expenses – Variable (Sales unit × ₹ 8)	80,000	1,52,000
Add: Selling expenses -Fixed (25,000 units × ₹ 2)	50,000	50,000
Cash Cost of Debtors	21,35,417	38,77,472
Average Debtors	2,66,927	4,84,684

Calculation of Stock of Work-in-progress (Cash Cost Basis)

Particulars		(₹)
Raw Material (material cost × 15%)	1,80,000	2,70,000
Labour & Mfg. Expenses (Labour & mfg. expenses × 15% × 40%)	88,500	1,06,500
Total	2,68,500	3,76,500

8. (i) A firm's financial management may often have the following as their objectives:

(a) The maximisation of firm's profit.

(b) The maximisation of firm's value / wealth.

The maximisation of profit is often considered as an implied objective of a firm. To achieve the aforesaid objective various type of financing decisions may be taken. Options resulting into maximisation of profit may be selected by the firm's decision makers. They even sometime may adopt policies yielding

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exorbitant profits in short run which may prove to be unhealthy for the growth, survival and overall interests of the firm. The profit of the firm in this case is measured in terms of its total accounting profit available to its shareholders.

The value/wealth of a firm is defined as the market price of the firm's stock. The market price of a firm's stock represents the focal judgment of all market participants as to what the value of the particular firm is. It takes into account present and prospective future earnings per share, the timing and risk of these earnings, the dividend policy of the firm and many other factors that bear upon the market price of the stock.

The value maximisation objective of a firm is superior to its profit maximisation objective due to following reasons.

1. The value maximisation objective of a firm considers all future cash flows, dividends, earning per share, risk of a decision etc. whereas profit maximisation objective does not consider the effect of EPS, dividend paid or any other returns to shareholders or the wealth of the shareholder.

2. A firm that wishes to maximise the shareholders wealth may pay regular dividends whereas a firm with the objective of profit maximisation may refrain from dividend payment to its shareholders.

3. Shareholders would prefer an increase in the firm's wealth against its generation of increasing flow of profits.

4. The market price of a share reflects the shareholders expected return, considering the long-term prospects of the firm, reflects the differences in timings of the returns, considers risk and recognizes the importance of distribution of returns.

The maximisation of a firm's value as reflected in the market price of a share is viewed as a proper goal of a firm. The profit maximisation can be considered as a part of the wealth maximisation strategy.

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(ii) Trade credit and accruals as source of working capital refers to credit facility given by suppliers of goods during the normal course of trade. It is a short-term source of finance. SSI firms in particular are heavily dependent on this source for financing their working capital needs. The major advantages of trade credit are – easy availability, flexibility and informality.

There can be an argument that trade credit is a cost-free source of finance. But it is not. It involves implicit cost. The supplier extending trade credit incurs cost in the form of opportunity cost of funds invested in trade receivables. Generally, the supplier passes on these costs to the buyer by increasing the price of the goods or alternatively by not extending cash discount facility.

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6B: STRATEGIC MANAGEMENT

QUESTIONS

Multiple Choice Questions

1. Swasthya, a rising star in India's dynamic healthcare sector, stands out as a prime example of smart strategic management.

   At Swasthya, the compass guiding their endeavors is a compelling thought: to emerge as the finest healthcare provider renowned for delivering accessible, top-notch healthcare services. This overarching goal is not an isolated vision, but a thread woven into the very fabric of the organization, driving every facet of their operations. The people of the organization play a pivotal role in this journey. They are entrusted with translating this vision into tangible outcomes at the grassroots level, ensuring that local operations are aligned with the grand aspiration of becoming a healthcare leader.

   Swasthya works meticulously towards optimizing each link of the patient experience. From streamlining appointment scheduling to expediting test result delivery, every facet of the healthcare journey is scrutinized. Swasthya's strategy is not merely about being a player in the market but about strategically positioning themselves as leaders. They proactively recognize the constant innovations that could disrupt their areas of expertise. To counter this, they introduced value-added offerings such as telemedicine and wellness programs. This addition not only mitigates the risk but also fortifies their long-term viability.

   Beyond competition, ensuring the quality and safety of patient care is paramount at Swasthya. Stringent hygiene protocols, equipment maintenance regimens, and adherence to healthcare regulations form the cornerstone of their business. In parallel, the organization meticulously undertakes regular assessment as a central element of its decision-making apparatus. This forward-looking exercise encompasses

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identifying and assessing potential risks such as regulatory changes, medical malpractice vulnerabilities, or shifts in market dynamics, all of which could have far-reaching consequences for their long-term objectives.

The implementation of Swasthya's strategy is steered by the McKinsey 7S model, which ensures a harmonious alignment of seven critical elements: strategy, structure, systems, shared values, skills, style, and staff. It emphasizes that the success of a long-term objective is contingent on the synchronization of these seven elements, reinforcing the idea that strategic management is not a compartmentalized process but a comprehensive activity.

Swasthya's strategic journey through India's healthcare landscape is a testament to the seamless integration of core management concepts, guiding its actions and strategies, while keeping the vision and intent at the core.

Based on the above Case Scenario, answer the Multiple Choice Questions.

(i) How does Swasthya's approach to premise control, including stringent hygiene protocols and equipment maintenance, contribute to their long-term objectives and which concept does it align with?

(a) It reduces immediate costs and aligns with strategic risk assessment.

(b) It safeguards quality and aligns with strategic risk assessment.

(c) It enhances immediate profitability and aligns with shared values.

(d) It streamlines administrative processes and aligns with value chain analysis.

(ii) How does Swasthya counter the risk posed by constant innovations and disruptions in their areas of expertise?

(a) By aggressively acquiring innovative startups.

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(b) By introducing value-added services like telemedicine and wellness programs.

(c) By downsizing their operations.

(d) By focusing exclusively on urban healthcare markets.

(iii) Why is the McKinsey 7S model significant in Swasthya's strategic management approach, and which elements of the model ensure a holistic alignment of their strategy?

(a) It facilitates short-term profit maximization, with a focus on structure and style.

(b) It emphasizes a compartmentalized approach to strategy, focusing on shared values and skills.

(c) It ensures a comprehensive alignment of strategy, structure, systems, shared values, skills, style, and staff.

(d) It prioritizes immediate cost reduction by aligning systems and strategy.

(iv) Why is the focus on local operations essential for Swasthya in the context of their long-term objective, and how does it contribute to their overall strategy?

(a) It reduces strategic risk by minimizing the need for strategic risk assessment.

(b) It aligns with their commitment to immediate profitability.

(c) It translates the organization's vision into tangible outcomes and aligns with their long-term objective.

(d) It diversifies their portfolio and aligns with competitive landscape analysis.

(v) The case talks about scrutiny of every facet of the healthcare journey and also emphasizes the fact that people of the organization play a pivotal role in this journey. Based on your reading, which level of management has the most crucial part to play here to ensure the sense of customer-first is imbibed in the organization?

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(a) Top Management (C-Suite) which sets the tone and strategy of the organization

(b) Middle Management (Divisional Managers) who have the responsibility of translating strategy to real-time objectives

(c) Functional Managers who actually do the work on the field

(d) Board of Directors who are responsible for wealth creation of the shareholders

2. ABC Foundation envisages a world where every individual, regardless of background, has access to quality education, eradicating illiteracy globally. ABC Foundation is committed to establishing 1000 learning centers, with a target to reach 1 million learners in the next five years. Their core values emphasize equality, empowerment, and knowledge-sharing. What represents the fundamental purpose and long-term aspirations of ABC Foundation?

(a) Vision

(b) Values

(c) Mission

(d) Goals and Objectives

3. Kanika, known as "Desi Taylor Swift," launched the lipstick brand Kolor among intense global and domestic competition. Despite a lack of groundwork, her substantial 45 million social media following gained significant attention. Which aspect of Michael Porter's force multiplier is working in favour of Kolor?

(a) Social Media Influence

(b) Threat of New Entrants

(c) Supplier Bargaining Power

(d) Buyer Bargaining Power

4. Mukul faced intense competition in an undifferentiated industry. To address this, he opted for a cost-cutting strategy to attract customers

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with lower pricing. Which factor could pose a risk to Mukul's cost-cutting strategy?

(a) Prompt forecasting of demand for the product or service

(b) Investing in cost-saving technologies and using advanced technology for smart, efficient working

(c) Technological breakthroughs in the industry

(d) Resistance to differentiation until it becomes essential

5. Quntik operates in the software industry and enjoys a strong position in the market. They have identified an opportunity to acquire a smaller company to expand their product offerings. Which quadrant of Medelow's Matrix would the CEO of a smaller company fall into?

(a) Keep Satisfied

(b) Key Player

(c) Low Priority

(d) Keep Informed

6. What organizational structure is best suited for House of Jani's strategic need for dynamic allocation of resources, ensuring each project and department is mentored, monitored, and maximized via multiple leaders?

(a) Functional Structure

(b) Matrix Structure

(c) Hourglass Structure

(d) Network Structure

Descriptive Questions

Chapter 1-Introduction to Strategic Management

7. ABC Pharmaceuticals, a leading pharmaceutical company, is in the process of formulating its strategic intent. The top management of ABC Pharmaceuticals wants to define the company's future direction, objectives, and goals. Their aim is to create a vision that sets the

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organization apart and provides a roadmap for future growth. ABC Pharmaceuticals aspires to enrich the lives of people by producing high-quality pharmaceutical products at competitive prices and wants to become the world's leading pharmaceutical company by 2030." Based on this context, draft a vision and mission statement that could be formulated by the top management of ABC Pharmaceuticals.

8. Define Strategic Management. Also discuss the limitations of Strategic Management.

Chapter 2-Strategic Analysis: External Environment

9. Riya Sharma owns a confectionery business in Jaipur, specializing in homemade chocolates and candies. Despite holding a substantial market share in the central region, her business has experienced declining sales of these products over the last few years. Concerned about the market dynamics, Riya consults a management expert for guidance. The consultant recommends a comprehensive understanding of the competitive landscape. Explain the steps to be followed by Riya Sharma to understand the competitive landscape to address the sales decline.

10. Explain the concept of Experience Curve and highlight its relevance in strategic management.

Chapter 3-Strategic Analysis: Internal Environment

11. ABC Ltd. is a beverage manufacturing company. It chiefly manufactures soft drinks. The products are priced on the lower side, which has made the company a leader in the business. Currently it holds 35 percent of the market share. The R & D of the company developed a formula for manufacturing sugar-free beverages. On successful trial and approval by the competent authorities, the company was granted to manufacture sugar free beverages. This company is the pioneer to launch sugar free beverages which are sold at a relatively higher price. This new product has been accepted widely by a class of customers. These products have proved profitable for the company. Identify the strategy employed by the company ABC Ltd. and mention what measures could be adopted by the company to achieve the employed strategy.

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12. There are four specific criteria of sustainable competitive advantage that firms can use to determine those capabilities that are known as core competencies. Explain.

Chapter 4-Strategic Choices

13. XYZ Corporation is a multinational conglomerate operating in various industries. They have a diverse portfolio of businesses, including a leading consumer electronics division, a growing e-commerce platform, a mature industrial machinery division, and a newly established software development unit. Which division of XYZ Corporation would most likely be classified as a "Star" in the BCG Growth-Share Matrix?

14. Justify the statement "Stability strategy is opposite of Expansion strategy".

Chapter 5-Strategy Implementation and Evaluation

15. York Investors, recognizing the importance of aligning its organizational elements with strategic objectives, has strategically invested in training programs, technology, and communication systems. The company aims to enhance the skills and capabilities of its workforce through comprehensive training initiatives. Simultaneously, York Investors leverages cutting-edge technology to streamline its operations and improve overall efficiency. The investment in communication systems ensures seamless collaboration and information flow across various departments. Identify and explain the model used by York Investors to achieve its strategic objectives.

16. Why is change management crucial during digital transformation, and what are some key strategies for navigating change effectively?

SUGGESTED ANSWERS/HINTS

1.	(i)	(b)	(ii)	(b)	(iii)	(c)	(iv)	(c)	(v)	(b)

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2. **(a)**

3. **(b)**

4. **(c)**

5. **(b)**

6. **(b)**

7. ABC Pharmaceuticals may have following vision and mission:

Vision: Vision implies the blueprint of the company's future position. It describes where the organisation wants to land. ABC Pharmaceuticals may have vision "To be the globally recognized leader in pharmaceutical innovation and enriching the lives of people worldwide by providing high-quality, affordable, and accessible pharmaceutical products."

Mission: Mission delineates the firm's business, its goals and ways to reach the goals. It explains the reason for the existence of the firm in society. It is designed to help potential shareholders and investors understand the purpose of the company.

ABC Pharmaceuticals may identify mission in the following lines:

- To improve the well-being of individuals and communities by relentlessly pursuing excellence in pharmaceutical research, development, and manufacturing.
- Committed to producing safe, effective, and sustainable medicines that address unmet medical needs and enhance the quality of life for patients.
- Through innovation, collaboration, and ethical practices, we aim to make a positive impact on global healthcare and become the trusted partner of healthcare providers and patients alike.

8. The term '**strategic management'** refers to the managerial process of developing a strategic vision, setting objectives, crafting a strategy, implementing and evaluating the strategy, and initiating corrective adjustments were deemed appropriate.

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The presence of strategic management cannot counter all hindrances and always achieve success as there are limitations attached to strategic management. These can be explained in the following lines:

- **Environment is highly complex and turbulent.** It is difficult to understand the complex environment and exactly pinpoint how it will shape-up in future. The organisational estimate about its future shape may awfully go wrong and jeopardise all strategic plans. The environment affects as the organisationhas to deal with suppliers, customers, governments and other external factors.
- **Strategic Management is a time-consuming process.** Organisations spend a lot of time in preparing, communicating the strategies that may impede daily operations and negatively impact the routine business.
- **Strategic Management is a costly process.** Strategic management adds a lot of expenses to an organization. Expert strategic planners need to be engaged, efforts are made for analysis of external and internal environments, devise strategies and properly implement. These can be really costly for organisations with limited resources particularly when small and medium organisation create strategies to compete.
- **Competition is unpredictable.** In a competitive scenario, where all organisations are trying to move strategically, it is difficult to clearly estimate the competitive responses to the strategies.

9. Steps to understand the competitive landscape are as follows:

(i) **Identify the competitor:** The first step to understanding the competitive landscape is to identify the competitors in the firm's industry and have actual data about their respective market share.

(ii) **Understand the competitors:** Once the competitors have been identified, the strategist can use market research report, internet, newspapers, social media, industry reports, and various other sources to understand the products and services offered by them in different markets.

(iii) **Determine the strengths of the competitors:** What is the strength

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of the competitors? What do they do well? Do they offer great products? Do they utilize marketing in a way that comparatively reaches out to more consumers. Why do customers give them their business?

(iv) **Determine the weaknesses of the competitors:** Weaknesses (and strengths) can be identified by going through consumer reports and reviews appearing in various media. After all, consumers are often willing to give their opinions, especially when the products or services are either great or very poor.

(v) **Put all of the information together:** At this stage, the strategist should put together all information about competitors and draw inference about what they are not offering and what the firm can do to fill in the gaps. The strategist can also know the areas which need to be strengthened by the firm.

10. Experience curve akin to a learning curve which explains the efficiency increase gained by workers through repetitive productive work. Experience curve is based on the commonly observed phenomenon that unit costs decline as a firm accumulates experience in terms of a cumulative volume of production. It is based on the concept, "we learn as we grow".

The implication is that larger firms in an industry would tend to have lower unit costs as compared to those for smaller companies, thereby gaining a competitive cost advantage.

Experience curve results from a variety of factors such as learning effects, economies of scale, product redesign and technological improvements in production.

Experience curve has following features:

- As business organisation grow, they gain experience.
- Experience may provide an advantage over the competition. Experience is a key barrier to entry.
- Large and successful organisation possess stronger "experience effect".

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A typical experience curve may be depicted as follows:

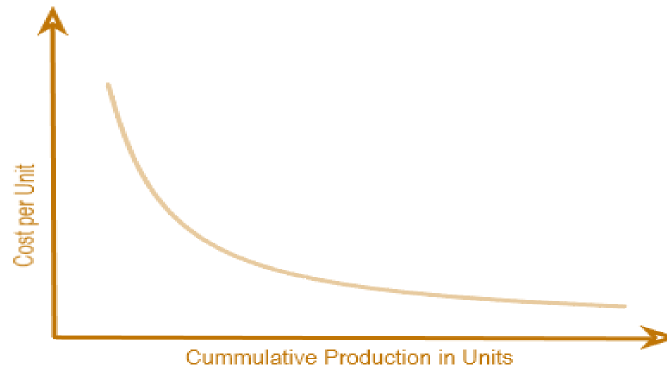

Figure: Experience curve

As a business grows, it understands the complexities and benefits from its experiences.

The concept of experience curve is relevant for a number of areas in strategic management. For instance, the experience curve is considered a barrier for new firms contemplating entry in an industry. It is also used to build market share and discourage competition.

11. According to Porter, strategies allow organizations to gain competitive advantage from three different bases: cost leadership, differentiation, and focus. Porter called these base generic strategies.

ABC Ltd. has opted for the Differentiation Strategy. The company has invested a huge amount in R & D and developed a formula for manufacturing sugar-free beverages to give the customer value and quality. They are **pioneers and serve specific customer needs that are not met by other companies** in the industry. The new product has been accepted by a class of customers. **Differentiated and unique sugar-free beverages** enable ABC Ltd. to charge **relatively higher** for its products, hence making higher profits and maintaining its competitive position in the market.

Sugar free beverage of ABC Ltd. is being accepted widely by a class of customers. Differentiation strategy is aimed at a broad mass market and involves the creation of a product or service that is perceived by the customers as unique. The uniqueness can be associated with product

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design, brand image, features, technology, and dealer network or customer service.

Achieving Differentiation Strategy

To achieve differentiation, following strategies are generally adopted by an organization:

1. Offer utility to the customers and match products with their tastes and preferences.
2. Elevate/Improve performance of the product.
3. Offer a high-quality product/service for buyer satisfaction.
4. Rapid product innovation to keep up with dynamic environment.
5. Taking steps to enhance brand image and brand value.
6. Fixing product prices based on the unique features of product and buying capacity of the customer.

12. Four specific criteria of sustainable competitive advantage that firms can use to determine those capabilities that are core competencies. Capabilities that are valuable, rare, costly to imitate, and non-substitutable are core competencies.

i. **Valuable:** Valuable capabilities are the ones that allow the firm to exploit opportunities or avert the threats in its external environment. A firm created value for customers by effectively using capabilities to exploit opportunities. Finance companies build a valuable competence in financial services. In addition, to make such competencies as financial services highly successful requires placing the right people in the right jobs. Human capital is important in creating value for customers.

ii. **Rare:** Core competencies are very rare capabilities and very few of the competitors possess these. Capabilities possessed by many rivals are unlikely to be sources of competitive advantage for any one of them. Competitive advantage results only when firms develop and exploit valuable capabilities that differ from those shared with competitors.

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iii. **Costly to imitate:** Costly to imitate means such capabilities that competing firms are unable to develop easily.

iv. **Non-substitutable:** Capabilities that do not have strategic equivalents are called non-substitutable capabilities. This final criterion for a capability to be a source of competitive advantage is that there must be no strategically equivalent valuable resources that are themselves either not rare or imitable.

13. In the BCG Growth-Share Matrix, divisions or business units are classified into four categories: Stars, Cash Cows, Question Marks, and Dogs. These classifications are based on a combination of market share and market growth rate.

A "Star" in the BCG Matrix represents a business unit with a high market share in a high-growth market. In the scenario, the newly established software development unit would be classified as a "Star." The software development unit is described as "newly established," suggesting that it is operating in a high-growth market. Additionally, the potential for high market share can be inferred if the unit is strategically positioned to become a leader in the software development industry.

Stars typically require significant investment to fuel their growth, but they have the potential to become future Cash Cows as the market matures. Therefore, the software development unit's high growth potential and the opportunity to capture a substantial market share align with the characteristics of a BCG Matrix "Star."

14. Stability Strategies, as the name suggests, are intended to safeguard the existing interests and strengths of business. It involves organisations pursuing established and tested objectives, continue on the chosen path, maintaining operational efficiency and so on. A stability strategy is pursued when a firm continues to serve in the same or similar markets and deals in the same products and services. In stability strategy, few functional changes are made in the products or markets, however, it is not a 'do nothing' strategy. This strategy is typical for mature business organizations. Some small organizations also frequently use stability as a strategic focus to maintain comfortable market or profit position.

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On the other hand, expansion strategy is an aggressive strategy as it involves redefining the business by adding the scope of business substantially, increasing the efforts of the current business. In this sense, it becomes the opposite to stability strategy. Expansion is a promising and popular strategy that tends to be equated with dynamism, vigor, promise and success. Expansion also includes diversifying, acquiring and merging businesses. This strategy may take the enterprise along relatively unknown and risky paths, full of promises and pitfalls.

15. York Investors is employing the McKinsey 7S Model to achieve its strategic objectives. The model focuses on seven interdependent elements within an organization, categorized into "Hard Ss" and "Soft Ss." In this case:

- **Strategy (Hard S):** Investing in training programs and technology aligns with the strategic objective of enhancing workforce skills and operational efficiency.
- **Structure (Hard S):** The investment suggests a structural alignment to support the strategic initiatives, indicating a deliberate organization of resources.
- **Systems (Hard S):** The use of cutting-edge technology and communication systems reflects a commitment to optimizing daily tasks and improving overall efficiency, addressing the system component of the model.
- **Shared Values (Soft S):** The emphasis on comprehensive training initiatives indicates a commitment to shared values, reflecting a focus on developing a skilled and capable workforce.
- **Style (Soft S):** The leadership style is implied in the strategic decision to invest in technology and training for workforce development and operational efficiency.
- **Staff (Soft S):** The commitment to enhancing skills and capabilities reflects a focus on the talent pool within the organization.
- **Skills (Soft S):** The strategic investment in training programs directly addresses the development of key skills within the workforce.

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York Investors' approach demonstrates a holistic application of the McKinsey 7S Model, emphasizing the interconnectedness of both hard and soft elements to achieve strategic alignment and organizational effectiveness.

16. Change management is essential during digital transformation to ensure the success of the process. Here are some key strategies to navigate change effectively:

- **Specify the digital transformation's aims and objectives:** Clearly defining the intended outcomes and objectives helps ensure everyone is aligned and working towards the same goals.
- **Always communicate:** Regular and transparent communication is crucial to help people understand the goals of digital transformation and how it will impact various stakeholders, including employees, clients, and other parties.
- **Be ready for resistance:** Change, even if beneficial, can be met with resistance. Having a strategy in place to address resistance is important for overcoming challenges and ensuring a smooth transition.
- **Implement changes gradually:** Instead of making all changes at once, gradual implementation allows individuals to adapt to new ways of doing things without feeling overwhelmed by too much change simultaneously.
- **Offer assistance and training:** Providing support, guidance, and training for employees is crucial as they navigate new procedures, software applications, and other aspects of digital transformation.

In conclusion, meticulous planning and effective change management are vital for the successful completion of digital transformation projects. Without proper change management, these efforts are more likely to fail, and organizations can enhance the integration of new digital systems by anticipating and managing the necessary changes.

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6B: STRATEGIC MANAGEMENT

QUESTIONS

Multiple Choice Questions

1. Once upon a time in the land of sun, sand, and vibrant cultures, there existed a company named "MuseoGoa" - a company that managed museums in the beautiful state of Goa. MuseoGoa had a vision to celebrate the rich history and culture of Goa, but their journey was not without its fair share of challenges.

   MuseoGoa had chosen a picturesque location in a quaint village to build their first museum. However, this initial enthusiasm was met with an uproar from the local communities. The villagers were concerned about the impact on their way of life and traditions. They worried that the influx of tourists might disrupt their peaceful existence.

   To address this challenge, MuseoGoa applied Mendelow's matrix, identifying the local communities as key stakeholders. They decided to engage in open dialogues, understanding and respecting the villagers' concerns. MuseoGoa initiated community-building activities, such as involving locals in museum operations, supporting local artisans, and organizing cultural events that showcased the village's heritage. Slowly but steadily, the company transformed from being perceived as a threat to a valued partner within the community.

   While MuseoGoa had successfully resolved their initial issues with the local community, they faced another challenge. Their location, although idyllic, was a bit off the beaten path. Tourists typically preferred the bustling beaches closer to the city, and this posed a real challenge. MuseoGoa decided to employ a pricing strategy. They priced their tickets affordably, significantly cheaper than the city's attractions. This strategy attracted budget-conscious tourists who were looking for unique experiences in Goa without burning a hole in their pockets. As

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word spread about the cultural gem tucked away in the village, visitors started flocking in, drawn not just by the museum's charm but also the economical ticket prices.

In the age of social media, MuseoGoa knew that word-of-mouth was no longer limited to whispers. They tapped into the power of social media to promote their unique museum experience. MuseoGoa ran interactive campaigns, encouraging visitors to share their experiences on various platforms. One particular Instagram post featuring a vibrant Goan mural in the museum went viral. This was the turning point. The picture-perfect aesthetics of the museum attracted influencers, bloggers, and travel enthusiasts, making MuseoGoa a social media sensation. Visitors came pouring in, not just from India but from across the globe, eager to capture their own moments at the "Instagrammable Museum of Goa."

With success came ambition. MuseoGoa decided to expand its footprint beyond Goa. To guide this expansion, they conducted a strategy audit and trend analysis. They identified emerging cultural and tourism trends and found potential markets in Pune and Trivandrum.

In Pune, MuseoGoa curated a special exhibition that celebrated the fusion of Goan and Maharashtrian cultures. They strategically partnered with local influencers and travel agencies to market the new experience. The expansion into Pune was met with resounding success.

For Trivandrum, MuseoGoa recognized the importance of local traditions and the distinct flavor of Kerala. They tailored their offerings to harmonize with the regional culture. MuseoGoa became the gateway for tourists to explore Kerala's rich heritage, with the museum acting as a bridge between Goa and Kerala's cultural tapestry.

MuseoGoa's journey from initial uproar to expansion was a testament to their commitment to community building, strategic pricing, social media savvy, and a keen eye for trends. The company continued to flourish, celebrating the diverse cultural tapestry of India and making history come alive in every location they touched.

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Based on the above Case Scenario, answer the Multiple Choice Questions.

(i) Which strategic management concept did MuseoGoa use to address the initial concerns of the local community?

(a) SWOT analysis

(b) Mendelow's matrix

(c) Cost leadership strategy

(d) Porter's Five Forces model

(ii) MuseoGoa's idyllic location in a quaint village posed a challenge as tourists preferred beaches closer to the city. To attract visitors, MuseoGoa priced their tickets affordably, cheaper than city attractions, drawing budget-conscious tourists looking for unique experiences. What business strategy did MuseoGoa employ to attract more tourists?

(a) Cost leadership strategy

(b) Differentiation strategy

(c) Focus strategy

(d) Diversification strategy

(iii) How did MuseoGoa approach its expansion into new markets such as Pune and Trivandrum?

(a) Outsourcing strategy

(b) Franchising strategy

(c) Product diversification strategy

(d) Market development strategy

(iv) Which element of the 7S McKinsey model is demonstrated by MuseoGoa's strategic use of social media and pricing strategies to attract visitors?

(a) Style

(b) Strategy

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(c) Shared Values

(d) Skills

(v) What played a crucial role in MuseoGoa's success in Pune and Trivandrum?

(a) Strategic partnerships

(b) Aggressive advertising

(c) Product differentiation

(d) Vertical integration

2. Jaago Lights, a successful brand from Jalandhar, aimed to enter the Middle East market by teaming up with major industry players. They needed to reorganize internal operations and refine product designs, facing pressure to expand quickly and turbulence in existing operations. What is the primary limitation of strategic management highlighted in the business case?

(a) Lack of senior management support

(b) Time-consuming and complex nature

(c) Inability to adapt to market changes

(d) Excessive focus on short-term goals

3. A traditional desi ghee company modernized its production and introduced pro-biotic desi ghee, facing initial market doubts. Aggressive marketing campaigns highlighted its benefits, gaining acceptance. During which stage of the product life cycle did the desi ghee company face doubts but gained acceptance through aggressive marketing campaigns?

(a) Introduction stage

(b) Growth stage

(c) Maturity stage

(d) Decline stage

4. A small tech company focused on enhancing their main product, which became crucial across various industries due to its increased power and

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adaptability. Their early partnerships and smart decisions facilitated rapid growth, leading to a $5 billion valuation in just five years. According to C.K. Prahalad and Gary Hamel, which area represents the tech company's core competency?

(a) Customer Value

(b) Competitor Differentiation

(c) Product Differentiation

(d) Application to Other Markets

5. A women's clothing brand recognized new opportunities and researched emerging trends and consumer preferences. They introduced a new clothing line, received positive feedback from initial trials, and grew through strategic partnerships and targeted advertising. What strategic choice best describes this approach?

(a) Product Development

(b) Market Development

(c) Market Penetration

(d) Diversification

6. For over a hundred years, the KDH business has thrived by leveraging strategic control as a cornerstone of its strategic approach. Regular evaluations of goals and performance ensured they stayed responsive to shifting market trends and evolving customer needs. Which type of strategic control is highlighted here?

(a) Premise Control

(b) Special Alert Control

(c) Implementation Control - Milestone Reviews

(d) Implementation Control - Monitoring Strategic Thrusts

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Descriptive Questions

Chapter 1-Introduction to Strategic Management

7. Tech Innovators Inc., a rapidly expanding technology company, aims to lead in artificial intelligence (AI) and machine learning (ML). With recent growth, the company is evaluating which organizational structure will best support its vision for innovation and leadership in AI technologies. They are considering three options: the Functional and Divisional Relationship for specialization, the Horizontal Relationship for flat, collaborative management, and the Matrix Relationship for cross-functional teams. Which of these relationships—Functional and Divisional, Horizontal, or Matrix—will most effectively achieve Tech Innovators Inc.'s strategic goals, and why?

8. Strategic management helps an organization to work through changes in the environment to gain competitive advantage. In light of statement discuss its benefits.

Chapter 2-Strategic Analysis: External Environment

9. A company has recently launched a new product in the market. Initially, it faced slow sales growth, limited markets, and high prices. However, over time, the demand for the product expanded rapidly, prices fell, and competition increased. Identify the stages of the product life cycle (PLC) that the company went through.

10. Rajiv Arya owns an electrical appliance company specializing in the manufacture of domestic vacuum cleaners. The market is competitive, with four other manufacturers offering similar products and achieving comparable sales volumes. Additionally, these rival firms hold several patents related to the vacuum cleaner technology. The supplier base for raw materials is extensive, with multiple suppliers available. Identify and explain the significant forces from Porter's Five Forces framework that are relevant to Rajiv Arya's company.

Chapter 3-Strategic Analysis: Internal Environment

11. Inspite of high commodity inflation, shortage of components and the threat of third wave of COVID-19 pandemic in India, manufacturers of packaged goods, home appliances and consumer electronics are

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expecting the business to grow by 12 to 25 percent in the coming months. After one-and-a-half years of disruption, manufacturers are now confident about managing their inventories better, keeping their supply channels well-stocked and preparing themselves to minimalize the impact of any COVID related restrictions even as they gear up for the festive season, which usually accounts for 25 to 35 percent of their yearly sales.

The home appliances sector could be an example. After a dismal April-June quarter in the year 2021, producers of air conditioners, refrigerators and washing machines are expecting their business to grow by 15-20 percent in the months to come. All the companies operating in the sector have geared up to grab the opportunities available in the market.

A leading company in the home appliances domain, XXP India, is planning to launch various innovative product designs and offer loyalty programmes to lure consumers.

With reference to Michael Porter's generic strategies, identify which strategy XXP India has planner for? Explain how this strategy will be advantageous to the company to remain profitable?

12. How can Mendelow's Matrix be used to analyze and manage the stakeholders effectively?

Chapter 4-Strategic Choices

13. Pizza Galleria was India's first pizza delivery chain enjoying monopoly for several years. However, after the entry of Modino and Uncle Jack it is struggling to compete. Both Modino and Uncle Jack have opened several eateries and priced the product aggressively. In the last four years the chain has suffered significant losses. The chain wishes to know whether they should go for a turnaround strategy. List out components of action plan for turnaround strategy.

14. Distinguish between Concentric Diversification and Conglomerate Diversification. ".

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Chapter 5-Strategy Implementation and Evaluation

15. A Mumbai-based conglomerate, PQR Ltd., has announced a major restructuring of its business operations. The company has decided to split its business into four separate units: Manufacturing, Retail, Services, and Technology. Each unit will operate as a separate business, with delegated responsibility for day-to-day operations and strategy to the respective unit managers. Identify the organization structure that PQR Ltd. has planned to implement. Discuss any four attributes and the benefits the firm may derive by using this organization structure.

16. Why Strategic Performance Measures are essential for organizations?

SUGGESTED ANSWERS/HINTS

MCQ No.	Answer	
1.	(i)	(b)
	(ii)	(a)
	(iii)	(d)
	(iv)	(b)
	(v)	(a)
2.		(b)
3.		(a)
4.		(d)
5.		(a)
6.		(c)

7. The Matrix Relationship is the most effective structure for Tech Innovators Inc. to achieve its vision of leadership in AI technologies. This structure promotes cross-functional collaboration, essential for managing complex AI projects and fostering innovation. By integrating expertise from various departments into temporary, task-based teams,

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the Matrix Relationship supports dynamic project management and aligns well with the company's strategic goals for advancing AI technologies. Despite its complexity, this approach provides the flexibility and collaboration necessary for a leading-edge AI and ML focus.

Relationship	Benefits	Drawbacks	Suitability for AI Leadership
Functional and Divisional	Specialization, clear management of functions and products.	Potential for departmental isolation, limited collaboration.	Less effective for cross-functional AI projects.
Horizontal	Open communication, encourages innovation and fast idea sharing.	Hard to scale, unclear roles and responsibilities.	Suitable for startups, less for large AI initiatives.
Matrix	Facilitates cross-functional collaboration, flexible resource management for complex projects.	Complex reporting structures, potential conflicts.	Ideal for managing diverse, innovative AI projects.

8. Strategic management involves developing the company's vision, environmental scanning, strategy formulation, implementation, evaluation and control. It emphasizes the monitoring and evaluation of external opportunities and threats in the light of a company's strengths and weaknesses and designing strategies for survival and growth. It helps in the creation of a competitive advantage to outperform the competitors and also guides the company successfully through all changes in the environment.

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The major benefits of strategic management are:

- Strategic management gives directions to the company to move ahead. It defines the goals and mission.
- It helps organisations to be proactive instead of reactive in shaping their future.
- It provides frameworks for all major decisions of an enterprise such as decisions on businesses, products, markets, manufacturing facilities, investments and organisational structure. It provides better guidance to the entire organisation on the crucial point - what it is trying to do.
- It helps organisations to identify the available opportunities and identify ways and means to achieve them.
- It serves as a corporate defence mechanism against mistakes and pitfalls.
- It helps to enhance the longevity of the business.
- It helps the organisation to develop certain core competencies and competitive advantages that would facilitate survival and growth.

9. The company went through the following stages of the product life cycle (PLC):

Introduction stage: Initially, the company faced slow sales growth, limited markets, and high prices, which are characteristic of the introduction stage. During this stage, competition is almost negligible, and customers have limited knowledge about the product.

Growth stage: Over time, the demand for the product expanded rapidly, prices fell, and competition increased. These are typical features of the growth stage in the PLC. In this stage, the product gains market acceptance, and customers become more aware of the product's benefits and show interest in purchasing it.

10. The competitive rivalry will be a significant force in case of company of Rajiv Arya as all the rivals are similar in sizes and are manufacturing similar products. It is difficult for any single manufacturer to dominate the market. Large number of patents will make it difficult for new

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entrants to break into the market. Further, as there are a large number of small suppliers the power that suppliers can exert will also be low.

There is no information relating to substitutes and bargaining power of customers in the information given in scenario. However, a domestic vacuum cleaner will directly compete with other options such as house maids. Availability of house maids at low cost can significantly disturb the sales of products.

Further, as the products are similar customers can easily shift from one company to another. This will only enhance competitive rivalry.

11. According to Michael Porter, strategies allow organizations to gain competitive advantage from three different bases: cost leadership, differentiation, and focus. Porter called these base generic strategies.

XXP India Ltd. has planned for Differentiation Strategy. The company is planning to launch various innovative product designs and offer loyalty programmes to lure customers.

Differentiation strategy should be pursued only after a careful study of buyers' needs and preferences to determine the feasibility of incorporating one or more differentiating features into a unique product that features the desired attributes. A successful differentiation strategy allows a firm to charge a higher price for its product and to gain customer loyalty, because consumers may become strongly attached to the differentiated features.

Advantages of Differentiation Strategy

A differentiation strategy may help an organisation to remain profitable even with rivalry, new entrants, suppliers' power, substitute products, and buyers' power.

1. **Rivalry** - Brand loyalty acts as a safeguard against competitors. It means that customers will be less sensitive to price increases, as long as the firm can satisfy the needs of its customers.
2. **Buyers** – They do not negotiate for price as they get special features, and they have fewer options in the market.

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3. **Suppliers** – Because differentiators charge a premium price, they can afford to absorb higher costs of supplies as the customers are willing to pay extra too.

4. **Entrants** – Innovative features are an expensive offer. So, new entrants generally avoid these features because it is tough for them to provide the same product with special features at a comparable price.

5. **Substitutes** – Substitute products can't replace differentiated products which have high brand value and enjoy customer loyalty.

12. Mendelow's Matrix can be used effectively to analyze and manage stakeholders through a grid-based approach by the following steps:

1. **Identify Stakeholders:** Begin by identifying all relevant stakeholders for your project or organization. This includes individuals, groups, or organizations that may be impacted by or have an impact on your activities.

2. **Assess Power and Interest:** For each stakeholder, assess their power to influence your project or organization and their level of interest in its success. Power can be assessed based on factors such as authority, resources, and expertise, while interest can be gauged by their level of involvement, expectations, and potential benefits or risks.

3. **Plot Stakeholders on the Grid:** Create a grid with Power on one axis and Interest on the other. Plot each stakeholder on the grid based on your assessment. Stakeholders with high power and high interest are placed in the "Key Players" quadrant, those with high power but low interest are in the "Keep Satisfied" quadrant, those with low power but high interest are in the "Keep Informed" quadrant, and those with low power and low interest are in the "Low Priority" quadrant.

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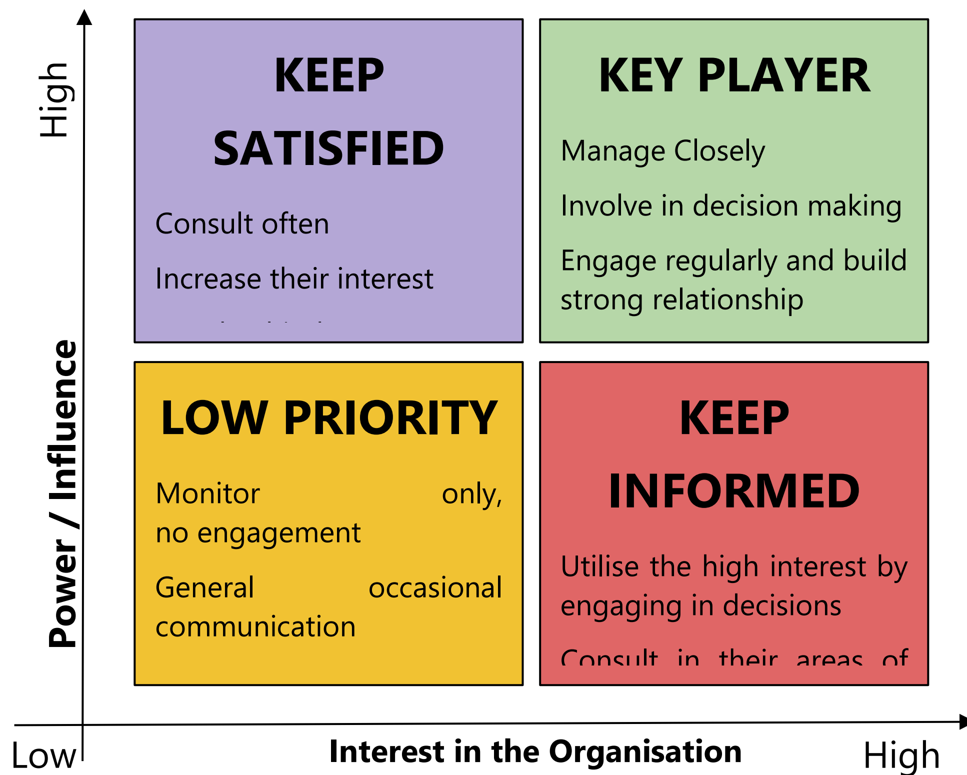

4. **Develop Strategies for each Quadrant:** Based on the placement of stakeholders in the grid, develop specific strategies for managing each quadrant:

   - **Key Players:** Fully engage with these stakeholders, seek their input, and keep them informed. They are crucial for the success of your project, so their needs and expectations should be a top priority.

   - **Keep Satisfied:** These stakeholders have significant power but may not be as interested in your project. Keep them satisfied by providing regular updates and addressing any concerns they may have to prevent them from becoming detractors.

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- **Keep Informed:** While these stakeholders may not have much power, they are highly interested in your project. Keep them informed to ensure they remain supportive and to leverage their insights and feedback.
- **Low Priority:** These stakeholders have low power and interest. Monitor them for any changes but allocate minimal resources to managing their expectations.

5. **Monitor and Adapt:** Continuously monitor the power and interest of stakeholders and adjust your strategies accordingly. Stakeholders may move between quadrants based on changing circumstances, so it's important to remain flexible and responsive.

   By using Mendelow's Matrix as a grid-based tool, you can effectively analyze and manage stakeholders by tailoring your engagement strategies to their specific needs and expectations, ultimately increasing the likelihood of project success.

13. Pizza Chain may choose to have turnaround strategy if there are:

- Persistent negative cash flow from business.
- Uncompetitive products or services.
- Declining market share.
- Deterioration in physical facilities.
- Over-staffing, high turnover of employees, and low morale.
- Mismanagement.

For turnaround strategies to be successful, it is imperative to focus on the short and long-term financing needs as well as on strategic issues. The chain may attempt to leverage the potential Indian market by engaging a new logistics partner. It may bring innovation in food items, as well as quality and improvements in the overall dine-in and delivery experience. During the turnaround, the "product mix" may be changed, requiring the organization to do some repositioning.

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A workable action plan for turnaround would involve:

Stage One – Assessment of current problems: The first step is to assess the current problems and get to the root causes and the extent of damage the problem has caused.

Stage Two – Analyze the situation and develop a strategic plan: Before making any major changes; determine the chances of the business's survival. Identify appropriate strategies and develop a preliminary action plan.

Stage Three – Implementing an emergency action plan: If the organization is in a critical stage, an appropriate action plan must be developed to stop the bleeding and enable the organization to survive. A positive operating cash flow must be established as quickly as possible and enough funds to implement the turnaround strategies must be raised.

Stage Four – Restructuring the business: The financial state of the organization's core business is particularly important. If the core business is irreparably damaged, then the outlook for the entire organization may be bleak. Efforts to be made to position the organization for rapid improvement.

Stage Five – Returning to normal: In the final stage of turnaround strategy process, the organization should begin to show signs of profitability, return on investments and enhancing economic value-added. Emphasis is placed on a number of strategic efforts such as carefully adding new products and improving customer service, creating alliances with other organizations, increasing the market share, etc.

14. The following are the principal points of distinction between concentric diversification and conglomerate diversification:

(i) Concentric diversification occurs when a firm adds related products or markets. On the other hand, conglomerate diversification occurs when a firm diversifies into areas that are unrelated to its current line of business.

(ii) In concentric diversification, the new business is linked to the existing businesses through process, technology or marketing. In

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conglomerate diversification, no such linkages exist; the new business/product is disjointed from the existing businesses/ products.

(iii) The most common reasons for pursuing concentric diversification are that opportunities in a firm's existing line of business are available. However, common reasons for pursuing a conglomerate growth strategy are that opportunities in a firm's current line of business are limited or opportunities outside are highly lucrative.

15. PQR Ltd. has planned to implement the Strategic Business Unit (SBU) structure. Very large organisations, particularly those running into several products, or operating at distant geographical locations that are extremely diverse in terms of environmental factors, can be better managed by creating strategic business units. SBU structure becomes imperative in an organisation with increase in number, size and diversity.

The attributes of an SBU and the benefits a firm may derive by using the SBU Structure are as follows:

- ♦ A scientific method of grouping the businesses of a multi – business corporation which helps the firm in strategic planning.
- ♦ An improvement over the territorial grouping of businesses and strategic planning based on territorial units.
- ♦ Strategic planning for SBU is distinct from rest of businesses. Products/ businesses within an SBU receive same strategic planning treatment and priorities.
- ♦ Each SBU will have its own distinct set of competitors and its own distinct strategy.
- ♦ The CEO of SBU will be responsible for strategic planning for SBU and its profit performance.
- ♦ Products/businesses that are related from the standpoint of function are assembled together as a distinct SBU.
- ♦ Unrelated products/ businesses in any group are separated into separate SBUs.

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- Grouping the businesses on SBU lines helps in strategic planning by removing the vagueness and confusion.
- Each SBU is a separate business and will be distinct from one another on the basis of mission, objectives etc.

16. Strategic performance measures are essential for organizations for several reasons:

- **Goal Alignment:** Strategic performance measures help organizations align their strategies with their goals and objectives, ensuring that they are on track to achieve their desired outcomes.
- **Resource Allocation:** Strategic performance measures provide organizations with the information they need to make informed decisions about resource allocation, enabling them to prioritize their efforts and allocate resources to the areas that will have the greatest impact on their performance.
- **Continuous Improvement:** Strategic performance measures provide organizations with a framework for continuous improvement, enabling them to track their progress and make adjustments to improve their performance over time.
- **External Accountability:** Strategic performance measures help organizations demonstrate accountability to stakeholders, including shareholders, customers, and regulatory bodies, by providing a clear and transparent picture of their performance.

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PAPER – 6: FINANCIAL MANAGEMENT AND STRATEGIC MANAGEMENT

6A: FINANCIAL MANAGEMENT

QUESTIONS

Division A: Case Scenarios

Integrated Case Scenario

1. Samvar Ltd, a leading **FMCG** company having its current presence in more than 150 Tier I and Tier II cities in India. The stores are operating in the brand name of **GoMART** competing with Reliance fresh, Walmart, BigBazaar and other chains. Owing to the increase in demand from Tier III cities and rural areas, it is planning for massive expansion and is contemplating to open up additional 50 stores which will have variety of FMCG products.

   The CFO and his team estimate that the funds needed for massive expansion would be ₹ 200 lakhs per store. Such funds would be utilized for buying out a space and setting up a store, buying the other required fixed assets, etc. Central government will provide a revenue subsidy of 15% on Gross profit if the overall cost of capital doesn't exceed 10%

   Apart from above, CFO and his team require an estimate on the additional capital needed based for the smooth running of fixed assets and its daily operations. Based on their market research, they have collected the other information for each store which is as follows-

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Average Sales would be ₹ 120 lakhs p.a. with a GP margin of 18%. Customers pay through different digital modes and channels including POS systems (Debit and credit cards) which generally takes approx. 9 days for the funds to get credited in the bank account. 15% of the customers use debit and credit cards to make the payment. Installing a POS system comes with a fee of 2% of total sales through POS.

Being a FMCG outlet, inventories of multiple products need to be kept. Different products have different storage period. However primarily, products are classified into three broad categories, Durable, Semi Durable & Perishable. Perishable products comprise 60% of sales, whereas semi-durable is 25% and balance is for durable products. Inventory storage period for perishable, semi-durable & durable products are 10 days, 30 days & 60 days respectively. Suppliers of these products provide a credit period of average 30 days.

Each store will employ around 20 personnel of a different hierarchy and monthly average salaries to staff for each store is estimated at ₹ 4 lakhs per month. Company will pay employees' dues on the 1st of next month.

Samvar Ltd plans to keep optimum cash balance in hand as suggested by Baumol's model. Excess cash balance if any, will be invested in the marketable securities which will generate a return of 12% p.a. The total disbursement for the year is estimated at ₹ 1.50 lakhs per month with the transaction cost of ₹ 20 per transfer to the disbursement account.

The optimum capital structure with debt equity of 2:1 has been proven ideal for raising the finance and company wishes to follow the same pattern for the additional funds required for each store. Trade credit can also be utilized for financing the expansion needs.

The cost of raising debt and equity for each store is as per the slabs as under:

Project Cost *	**Cost of Debt**	**Minimum rate expected by equity share holders**
Upto 80 lakhs	10%	12.5%
Above 80 lakhs but upto 150 Lakhs	11.5%	13.5%

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Above 150 lakhs & Upto 250 lakhs	12%	14%
Above 250 lakhs	13.5%	15%

*It means that upto 80 lakhs of project cost company can raise debt at 10% and equity at 12.5% and so on.

Tax rate applicable to the corporate is 25%

Based on the above details, calculate the following for each store:

i. The optimum Cash balance is

(A) ₹ 7,071

(B) ₹ 26,500

(C) ₹ 7,150

(D) ₹ 24,495

ii. The Gross and Net Working Capital for the next year would be

(A) ₹ 6.7730 L, (5.9396 L)

(B) ₹ 6.7730 L, 12.7125 L

(C) ₹ 200 L, (5.9396L)

(D) ₹ (5.9396 L), 6.7730 L

iii. The amount of total funds needed to setup a store is

(A) ₹ 194.0605 L

(B) ₹ 200 L

(C) ₹ 6.7730 L

(D) ₹ 206.7730 L

iv. The overall cost of capital for raising additional funds for setting up of each store is

(A) 10.01%

(B) 10.65%

(C) 9.90%

(D) 8.91%

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v. The amount of revenue subsidy granted by the central govt is

(A) ₹ 3 L

(B) ₹ 3.24 L

(C) Nil

(D) ₹ 2.25 L

Dividend Decision

2. The cost of capital of a firm is 12% & its expected earning per share at the end of the year is ₹ 20. its existing payout ratio is 25%. the company is planning to increase its payout ratio to 50% what will be the effect of this change on the market price of equity share (MPS) of the company as per Gordon model, if the reinvestment rate of the company is 15%?

(A) It will increase by ₹ 444.45

(B) It will decrease by ₹ 444.45

(C) It will increase by ₹ 222.22

(D) It will decrease by ₹ 222.22

Financing Decision - Cost of Capital

3. Abhi Ltd is an all equity financed company. It is considering replacing ₹ 275 lakhs equity shares with 15% debentures of the same amount. Current Market value of the company is 1750 lakhs with cost of capital at 20%. Future EBITs are going to be constant and entire earnings are going to be distributed. Corporate Tax Rate can be assumed to be 30%. What will be the new cost of equity of the firm?

(A) 19.11%

(B) 17.53%

(C) 10.50%

(D) 20.62%

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Division B: Descriptive Questions

Financial Analysis & Planning – Ratio Analysis

4. Vardhaman Limited gives you the following information related for the year ending 31st March, 2024:

Particulars	Amount (₹)
Current Ratio	3:1
Loan funds to Owned Funds Ratio	1:3
Gross Profit Ratio	25%
Stock Turnover Ratio	10
Net Working Capital	₹ 5,00,000
Return on Total Assets (pre-tax)	15%
MPS	₹ 20
Total Assets Turnover Ratio	2.5
Opening stock	₹ 6,50,500
Fixed Assets	₹ 15,00,000
75,000 equity shares of	₹ 10 each
25,000, 12% Pref. Shares of	₹ 10 each
Depreciation	₹ 50,000
Interest on Debt	9%
Future Instalments	₹ 2,00,000

Tax rate applicable to the company is 25%

You are required to CALCULATE:

(i) Quick Ratio

(ii) Fixed Assets Turnover Ratio

(iii) Debt Service Coverage

(iv) Earnings per Share

(v) Price Earnings Ratio

Financing Decision - Cost of Capital

5. The Capital Structure of Samyaktva Limited is as follows:

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	Amount (in ₹)
12% Debentures	3,50,000
14% Pref. Shares	4,50,000
Equity shares (Face value of ₹ 10 each)	8,50,000
	16,50,000

Additional Information:

1. ₹ 100 per debentures redeemable at premium of 6% with floatation cost of 5% & 5 years of maturity. The current market price of the debenture is ₹ 115
2. ₹ 100 per preference shares redeemable at a premium of 10%, issued at discount of 2% with a floatation cost of 5% on the issue price. The current market price per preference share is ₹ 108. It has maturity of 10 years
3. An equity share has a floatation cost of ₹ 5 with a market price per share currently quoted at ₹ 30. Samyaktva Limited paid a last dividend of ₹ 4 and the company is expected to give an annual growth rate of 9% on the dividends. The company has a practice of paying all the earnings in the form of dividends.
4. Corporate Taxation rate is at 25%

CALCULATE WACC using market value weights

Financing Decision - Capital Structure

6. Ritu Limited in the expansion stage and it provides you the following information:

	(₹)
Profit (EBIT)	5,00,000
Less: Interest on Debenture @ 10%	(1,00,000)
EBT	4,00,000
Less Income Tax @ 30%	(1,20,000)
	2,80,000
No. of Equity Shares (₹ 10 each)	50,000

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Earnings per share (EPS)	5.6
Price /EPS (PE) Ratio	10

The company has reserves and surplus of ₹ 10,00,000 and required ₹ 5,00,000 further for modernisation. Return on Capital Employed (ROCE) is constant. Debt (Debt/ Equity) Ratio lesser than 2 will raise the P/E Ratio to 12. Interest rate on additional debts is 12%. You are required to ASCERTAIN the probable price of the share.

(i) If the additional capital are raised as debt; and

(ii) If the amount is raised by issuing equity shares at ruling market price.

Financing Decision – Leverages

7. From the following financial data of Company X and Company Y:

(i) PREPARE their Income Statements.

(ii) CALCULATE Margin of Safety for both the Companies

(iii) CALCULATE Percentage change in EPS for both the companies, if percentage change in sales is 25%

(in ₹)

	Company X	**Company Y**
Variable Cost	72,000	65% of Sales
Fixed Cost	35,000	-
Interest Expenses	12,000	6,000
Financial Leverage	4:1	-
Operating Leverage	-	5:1
Income Tax Rate	30%	30%
Sales	-	1,45,000

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Dividend Decisions

8. The following information is supplied to you:

Particulars	Amount (₹)
Total Earnings	4,50,000
No of Equity Shares (of ₹ 100 each)	25,000 shares
Retention ratio	40%
MPS	198

Applying Walter's Model:

(i) ANALYSE whether the company is following an optimal dividend policy.

(ii) COMPUTE P/E ratio at which the dividend policy will have no effect on the value of the share. Also calculate the MPS at such P/E ratio

(iii) Will your decision change if the P/E ratio is 4.5? ANALYSE.

Investment Decisions – Capital Budgeting

9. A company is considering the proposal to take up a new project which requires investment of ₹ 850 lakhs in plant & machinery and ₹ 150 lakhs in working capital. The project is expected to yield the following Cash flows before tax and depreciation over the next five years:

Year	Amount (₹ in Lakhs)
1	290
2	320
3	360
4	390
5	270

The desired rate of return from the project is 14% and assets must be depreciated at 20% on a written down value basis. The scrap value at the end of the five-year period may be taken as ₹ 140 lakhs. The income tax

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applicable to the company is 20%. This is the only asset in the entire block. Capital gains tax is at 15% (for capital loss as well)

You are required to CALCULATE the net present value of the project and advise the management to take appropriate decisions. Also calculate the Internal Rate of Return and Desirability factor of the Project.

Note: Present values of Re. 1 at different rates of interest are as follows:

Year	14%	16%	20%
1	0.88	0.86	0.83
2	0.77	0.74	0.69
3	0.67	0.64	0.58
4	0.59	0.55	0.48
5	0.52	0.48	0.40

Management of Working Capital

10. Nirmoh Limited wants to avail short-term loan from the bank. However, bank grants short term loan by keeping the collateral in the form of accounts receivable. A bank is analyzing the receivables of Nirmoh Limited to identify acceptable collateral for a short-term loan.

The current policy of the company is 3/10 net 40. Bank will lend only to the extent of 90% of acceptable receivables at an interest rate of 12% only if both the conditions mentioned below are fulfilled. Bank will keep a reserve of 5% for cash discount & returns

(a) Customers are not currently overdue for more than 5 days to the net period

(b) Average aging (payment period) of the customer should not exceed 15 days past the net period.

If any of the above conditions are not fulfilled, the bank will lend 65% of the receivables subject to a reserve of 15% and the interest rate will be charged at 15% on such accounts. The corporate tax rate applicable is 25%.

On the scrutiny of all the receivables, following are the acceptable receivables considered for lending-

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Accounts	Amount (₹)	Outstanding in Days since invoiced	Average Aging (payment period) in Days
DR 01	50,000	37	40
DR 02	25,000	25	48
DR 03	1,20,000	47	49
DR 04	72,000	10	56
DR 05	45,000	30	30
DR 06	1,75,000	39	50
DR 07	19,000	55	25
DR 08	54,000	44	54
DR 09	1,05,000	15	25
DR 10	37,000	22	75

You are required to CALCULATE:

(a) Total amount lend by the bank

(b) Effective Interest cost (%) to the company

11. (a) LIST the emerging issues (any four) affecting the future role of CFO.

(b) EXPLAIN any four Methods for Computation of Cost of Equity Capital.

(c) Do the profitability index and the NPV criterion of evaluating investment proposals lead to the same acceptance-rejection and ranking decisions? In what SITUATIONS will they give conflicting results?

SUGGESTED ANSWERS/HINTS

1. i. (D) ₹ 24,495

As per William J Baumol,

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optimum cash balance = $\sqrt{\frac{2AT}{O}}$

A = Annual Cash disbursement

T = Cost per transfer

O = Opportunity cost

$= \sqrt{\frac{2 \times 18,00,000 \times 20}{0.12}}$ = **₹ 24,495/-**

ii. (A) ₹6.7730 L, (5.9396 L)

Gross working capital is sum of total current assets and net working capital is Gross working capital less current liabilities.

Estimation of Working Capital Statement

	Amount (₹)	Amount (₹)
A) CURRENT ASSETS / GROSS W.C		
1. FG Inventory **WN - 1** 2. Trade receivables **WN - 2** 3. Cash/ bank balance **(Calculated in Solution 1)**	6,15,000 37,800 24,495	**6,77,295**
B) CURRENT LIABILTIES		
1. Trade payables **WN - 3** 2. Outstanding salaries **WN - 4**	8,71,250 4,00,000	**12,71,250**
NET WORKING CAPITAL (A) - (B)		**(5,93,955)**

WN – 1 Calculation of FG Inventory

FG Inventory = COGS x $\frac{\text{FG STORAGE PERIOD (DAYS)}}{360}$

COGS = 120 Lakhs x 82% = 98.40 Lakhs

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Perishable = 98.40 x 60% x 10 /360 = 1.64 Lakhs

Semi Durable = 98.40 X 25% X 30 /360 = 2.05 Lakhs

Durable = 98.40 X 15% X 60 /360 = 2.46 Lakhs

Total = **₹ 6.15 lakhs**

WN – 2 Calculation of Trade Receivables

Since, company is into FMCG industry, sales are always on cash basis as no credit is given to any of the custome₹ However, as mentioned in the case study, company will get the credit in the bank account only after 9 days for those customers that pay through POS (debit and credit cards). It means companies funds' get blocked for 9 days.

Company's trade receivable would only comprise of 15% of total sales as rest are through cash basis

Trade Receivables = Cost of Sales x Days Blocked / 360

= 15.12 L x 9 / 360

= **0.378 Lakhs**

Cost of Sales = COGS + POS Transaction fees

= (98.40 L x 0.15) + (120 L x 0.15 x 2%)

= 15.12 Lakhs

WN – 3 Calculation of Trade Payables

$$\text{Trade Payables} = \text{Purchases} \times \frac{\text{Average Credit period in days}}{360}$$

= 104.55 x 30 /360

= **8.7125 Lakhs**

Purchases = COGS (+) Closing Stock (-) Opening Stock

Since, company is planning to open up new store, its opening stock would be NIL but there would be definitely a closing FG stock which is calculated in WN -1

Therefore, Purchases = 98.40 L + 6.15 L - 0 = **104.55 Lakhs**

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WN – 4 Calculation of Outstanding salaries

Salaries are paid on 1st of next month, thereby meaning it has been outstanding for a period of 30 days assuming salaries accruing evenly throughout.

Outstanding salaries = 48,00,000 x 30 / 360

= **4,00,000**

iii. (A) ₹ 194.0605 L

Total Capital needed = Total capital needs (Fixed assets) + Working Capital needs

= 200 L + (5,93,955)

= ₹ 194.0605 L

iv. (C) 9.90%

Samvar Ltd would require financing of ₹ 194.0605 lakhs from debt and equity and not ₹ 200 lakhs as trade credit is also considered to be a source of finance as mentioned in the case study.

Furthermore, the overall cost of raising this additional fund for each store of ₹ 194.0605 needs to be calculated slab wise

Project Cost	Weights (W)	Cost (K)	W X K	Total cost (₹)
Upto 80 Lakhs	Debt = 0.67 Equity = 0.33	Kd = 10 (1 - 0.25) = 7.5 Ke = 12.5	Ko = 9.167%	= 80L x 9.167% **= 7.334 Lakhs**
Above 80 L upto 150 L	Debt = 0.67 Equity = 0.33	Kd = 11.5(1-0.25) = 8.625 Ke = 13.5	Ko = 10.25%	= 70L x 10.25% **= 7.175 Lakhs**
Above 150 L upto 250 L	Debt = 0.67 Equity = 0.33	K = 12 (1-0.25) = 9 Ke = 14	Ko = 10.667%	=44.0605L x 10.667% **= 4.7Lakhs**

Total Funds = 194.0605 L

Total Cost (₹) = 7.334 L + 7.175 L + 4.700 L = 19.209 L

Ko = Total Cost (₹) / Total Funds

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= 19.209 / 194.0605

= 9.90%

v. (B) **₹ 3.24 L**

Since the Overall Cost of Capital is below 10%, Samvar Ltd is eligible for revenue subsidy

Revenue Subsidy = GP x 15%

= 21.6 L x 15%

= **₹ 3.24 Lakhs**

2. (B) **It will decrease by ₹ 444.45**

Current D1 = 20 x 25% = 5

Current g = 0.75 x 0.15 = 11.25%

Current MPS = 5/(0.12 - 0.1125) = 666.67

Proposed D1 = 20 x 50% = 10

proposed g = 0.5 x 0.15 = 0.075,

Proposed MPS = 10/(0.12 - 0.075) = 222.22

Change in MPS = 666.67 - 222.22 = **₹444.45**

3. (D) **20.62%**

Current PAT	= 1750 x 20%	= 350
Current PBT	= Future EBIT	= 350/0.7 = 500
Future PBT	= 500 - 275x15%	= 458.75
Future PAT	= 458.75 x 70%	= 321.125
Value (L)	= Value (UL) + Debt x t	= 1750+275 x 30% = 1832.5
Value of Equity	= 1832.5-275	= 1557.5
Ke	= 321.125/1557.5	**= 20.62%**

4. **WN 1: Calculation of Current Assets & Current Liabilities**

Current Ratio = CA / CL = 3:1

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Therefore, CA = 3CL

Net Working Capital = CA - CL = 5,00,000

= 3CL (-) CL = 5,00,000

Therefore, CL = 2,50,000,

CA = 7,50,000

WN 2: Calculation of Average Stock Value & Closing Stock

Total Assets = Fixed Assets + Current Assets

= 15 L + 7.5 L = **22.50 lakhs**

Total Assets Turnover Ratio = Sales / Total Assets = 2.5 (given)

Therefore Sales = 22.5 lakhs X 2.5

Sales = **56,25,000**

GP Margin = 25%, therefore COGS = 75% of Sales

COGS = 56.25 x 75% = **42,18,750**

Stock Turnover Ratio = COGS / Average Stock = 10 (given)

Average Stock = 42,18,750 / 10 = **4,21,875**

Average Stock = Op. Stock + Cl. Stock / 2

4,21,875 = 6,50,500 + Cl. Stock / 2

Cl Stock = 1,93,250

WN 3: Calculation of Cash Profit before Interest & Tax

Return on Total Assets (pre-tax) = (EBIT / Total Assets)

0.15 = EBIT / 22.50 lakhs

Therefore, EBIT = **3,37,500**

Cash Profit before Int & Tax = EBIT + Depreciation

= 337500 + 50000

Cash Profit before Int & Tax = **3,87,500**

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WN 4 : Calculation of Loan Funds (Debt) & Owned Funds (Equity)

Debt to Equity = 1 : 3, which means 3 times Debt = Equity (Owned Funds)

As per the Accounting equation,

Equity + Debt + Current Liab.	**=**	**Fixed Assets + Current Assets**
3 Debt + Debt + 2,50,000	=	15,00,000 + 7,50,000
4 Debt	=	20,00,000
Therefor Debt (Loan Funds)	=	**5,00,000**
Equity (Owned Funds)	=	**15,00,000**

WN 5: Calculation of Earnings Available to Eq. Share holders

Particulars	Amount (₹)
EBIT	3,37,500
(-) Int (5 lakhs x 9%)	(45,000)
EBT	2,92,500
(-) Tax @ 0.25	(73,125)
EAT	2,19,375
(-) Pref Div. (250000 x 12%)	(30,000)
Earnings For Eq. Sh Holders	1,89,375

1. Quick Ratio = {CA - Cl Stock}/CL

   = 7,50,000 – 1,93,250 / 2,50,000

   Quick Ratio = 2.23 : 1

2. Fixed Assets Turnover Ratio = Sales / Total Fixed Assets

   = 56,25,000 / 15,00,000

   Fixed Assets Turnover Ratio = 3.75 times

3. Debt Service Coverage Ratio = Cash profit before Int & Tax / Int + Instalments

   = 3,87,500 / (45,000+2,00,000)

   Debt Service Coverage Ratio = 1.58 times.

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4. **EPS = Earnings for Eq. Shareholders / No of Eq. Shareholders**

= 1,89,375/75,000

EPS = ₹ 2.53

5. Price to Earnings Ratio = MPS / EPS

= 20 / 2.53

Price to Earnings Ratio = 7.91 times

5. WN 1: Calculation of Cost of Debt

$$Kd = \frac{I(1-t)+\frac{(RV-NP)}{n}}{\frac{(RV+NP)}{2}}$$

RV = 100 + 6% = 106

n = term = 5 years

t = tax = 0.25

NP = Issue Price – Floatation cost

= 115 – 5% (Issue price will be at Market price and no Face Value)

= 109.25

$$Kd = \frac{12(1-0.25)+\frac{(106-109.25)}{5}}{\frac{(106+109.25)}{2}}$$

Therefore **Kd = 7.76%**

WN 2: Calculation of Cost of Preference Shares

$$Kp = \frac{PD+\frac{(RV-NP)}{n}}{\frac{(RV+NP)}{2}}$$

RV = 100 + 10% = 110

n = term = 10 years

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NP = Issue Price – Floatation cost

Issue Price = (108 – 2%) = 105.84

Net Proceeds = 105.84 (-) 5% = 100.55

$$Kp = \frac{14 + \frac{(110 - 100.55)}{10}}{\frac{(110 + 100.55)}{2}}$$

Therefore **Kp = 14.19%**

WN 3: Calculation of Cost of Equity

Since growth rate is given, Ke is to be calculated by using Gordon's formula

As per Gordon,

$$Ke = \frac{D_1}{P_0} + g$$

Where, D1 = Expected dividend at the end of Year 1

Po = Current Market Price (–) Floatation cost

G = growth rate in dividends

$$Ke = \frac{4 + 9\% \times 4}{30 - 5} + 0.09$$

Ke = 26.44%

Calculation of WACC using Market Value Weights

Sources	Amount of Capital (₹)	Weights (W)	Cost (K)	W X K
Debentures	4,02,500 (3,500 x 115)	0.1171	7.76 (WN 1)	0.9087
Preference shares	4,86,000 (4,500 x 108)	0.1413	14.19 (WN 2)	2.00
Equity shares	25,50,000 (85,000 x 30)	0.7416	26.44 (WN 3)	19.6079
	34,38,500			Ko = 22.52%

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6. Ascertainment of probable price of shares of Akash limited

Particulars	Plan-I If ₹ 5,00,000 is raised as debt (₹)	Plan-II If ₹ 5,00,000 is raised by issuing equity shares (₹)
Earnings Before Interest and Tax (EBIT) {20% of new capital i.e. 20% of (₹ 25,00,000 + ₹ 5,00,000)} (Refer working note1)	6,00,000	6,00,000
Less: Interest on old debentures (10% of ₹ 10,00,000)	(1,00,000)	(1,00,000)
Less: Interest on new debt (12% of ₹ 5,00,000)	(60,000)	--
Earnings Before Tax (EBT)	4,40,000	5,00,000
Less: Tax @ 30%	(1,32,000)	(1,50,000)
Earnings for equity shareholders (EAT)	3,08,000	3,50,000
No. of Equity Shares (refer working note 2)	50,000	58,929
Earnings per Share (EPS)	₹ 6.16	₹ 5.94
Price/ Earnings (P/E) Ratio (refer working note 3)	12	10
Probable Price Per Share (PE Ratio × EPS)	₹ 73.92	₹ 59.40

Working Notes:

1. Calculation of existing Return of Capital Employed (ROCE):

	(₹)
Equity Share capital (50,000 shares × ₹ 10)	5,00,000

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10% Debentures $\left(₹1,00,000 \times \frac{100}{10}\right)$	10,00,000
Reserves and Surplus	10,00,000
Total Capital Employed	25,00,000
Earnings before interest and tax (EBIT) (given)	5,00,000
ROCE $= \frac{₹\,5,000,000}{₹\,25,00,000} \times 100$	20%

2. Number of Equity Shares to be issued in Plan-II:

$$= \frac{₹5,00,000}{₹56} = 8,929 \text{shares}$$

Thus, after the issue total number of shares = 50,000+ 8,929 = 58,929 shares

3. Debt/Equity Ratio if ₹ 5,00,000 is raised as debt:

$$= \frac{₹15,00,000}{₹15,00,000} = 1$$

As the debt equity ratio is less than 2 the P/E ratio will be increase to 12 in Plan-I

7. (i) Income Statement

Particulars	**Co. X (₹)**	**Co. Y (₹)**
Sales	1,23,000 **(WN 2)**	1,45,000
(-) Variable Cost	(72,000)	(94,250) (65% on sales)
Contribution	51,000 **(WN 2)**	50,750
(-) Fixed Cost	(35,000)	(40,600)
EBIT	16,000 **(WN 1)**	10,150 **(WN 3)**
(-) Interest	(12,000)	(6,000)

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EBT	4,000	4,150
(-) Tax @ 30%	(1,200)	(1,245)
EAT	**2,800**	**2,905**

WN 1: Calculation of EBIT for Co. X using Financial Leverage

$$FL = \frac{EBIT}{EBT} \text{ or } \frac{EBIT}{EBIT - Interest}$$

$$4 = \frac{EBIT}{EBIT - 12{,}000}$$

EBIT = ₹ 16,000

EBT = ₹ 16,000 – ₹ 12,000 = ₹ 4,000

WN 2: Calculation of Contribution and Sales using reverse mechanism

Contribution = EBIT + Fixed Cost

= ₹ 16,000 + ₹ 35,000

Contribution = ₹ 51,000

Sales = Contribution + Variable Cost

Sales = ₹1,23,000

WN 3: Calculation of EBIT for Co. Y using Operating leverage

OL = Contribution / EBIT

$$5 = \frac{50{,}750}{EBIT}$$

EBIT = ₹ 10,150

(ii) Margin of Safety (MOS) is inversely proportionate to the Operating Leverage as higher the safety margin lower would be the business risk

$$MOS = \frac{1}{OL}$$

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Operating Leverage (Co. X) = $\frac{51,000}{16,000}$

Operating Leverage (Co. X) = 3.1875 : 1

Therefore, MOS for Co. X = 1 / 3.1875

MOS for Co. X = 31.37%

Operating Leverage (Co. Y) = 5 : 1

Therefore, MOS for Co. X = $\frac{1}{5}$

MOS for Co. Y = 20%

(iii) Combined leverage measures the percentage change in EPS due to percentage change in sales

Combined Leverage = $\frac{\text{Contribution}}{\text{EBT}}$

Combined Leverage (Co. X) = $\frac{51,000}{4,000}$

= 12.75

Combined Leverage = $\frac{\text{\% change in EPS}}{\text{\% change in sales}}$

12.75 = $\frac{\text{\% change in EPS}}{25\%}$

% change in EPS (Co. X) = 318.75%

Combined Leverage (Co. Y) = $\frac{50,750}{4,150}$

= 12.23

12.23 = $\frac{\text{\% change in EPS}}{25\%}$

% change in EPS (Co. Y) = 305.75%

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8. (i) As per Walter,

If ROI > Ke, firm should retain everything and distribute nothing to maximize the share price. On the contrary, if ROI < Ke, firm should distribute everything and retain nothing to maximize the wealth of the equity owners.

ROI = Total Earnings / Equity Share capital

= 4,50,000 / 25,00,000

ROI = 18%

Ke = $\frac{1}{PE}$

P.E Ratio = MPS / EPS = 198 /18 = 11

Therefor Ke = 1/11 = 9.091%

Since ROI > Ke, optimal dividend policy of the firm should be to retain everything and distribute nothing. However, the firm has retained 40% and distributed 60%, hence it is not having an optimal dividend policy as per Walter's model.

(ii) When ROI = Ke, dividend policy of the company will have no effect on the value of the share as per Walter's model

Therefore, in that case, Ke should be equal to 18%

P.E Ratio = $\frac{1}{Ke} = \frac{1}{0.18}$

P.E Ratio = 5.56 times

MPS at the above P.E Ratio = 18 x 5.56 = ₹ 100.08

(iii) If P.E Ratio is 4.5,

Ke = $\frac{1}{4.5}$ = 22.22%

Since, ROI < Ke, optimal dividend policy of the firm should be to distribute everything and retain nothing, as the value of share would be maximum at that point thereby maximizing the wealth of the shareholder

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9. (A) Calculation of NPV

WN 1 : Calculation of Present Value of Cash Outflow (PV CO)

(i) Initial Investment = ₹ 850 lakhs

(ii) Working capital outlay = ₹ 150 lakhs

Therefore, total PV CO = ₹ 1000 lakhs

WN 2 : Calculation of Present Value of Cash Inflows (PV CI)

Cash flows before tax are given i.e. nothing but NPBDT

Amount (₹ in lakhs)

Year	**1**	**2**	**3**	**4**	**5**
NPBDT	290.00	320.00	360.00	390.00	270.00
(-) Dep	170.00	136.00	108.80	87.04	69.63
NPBT	120.00	184.00	251.20	302.96	200.37
(-) Tax	24.00	36.80	50.24	60.59	40.07
NPAT	96.00	147.20	200.96	242.37	160.29
(+) Dep	170.00	136.00	108.80	87.04	69.63
CFAT	266.00	283.20	309.76	329.41	229.93
(+) Working Capital Release					150.00
(+) Scrap					140.00
PV Factor @ 14%	0.88	0.77	0.67	0.59	0.52
PV CI	**234.08**	**218.06**	**207.54**	**194.35**	**270.36**

(i) Total PV CI = ₹ 1124.40 Lakhs

WN 3 : Calculation of Present Value of tax savings on short term Capital loss

	₹ in Lakhs
WDV at end of 5th year	278.53
(-) Sale value	140.00

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Loss on sale	138.53
Tax savings on above @ 15%	20.78

PV of tax savings on short term capital loss (STCL) = Tax saving x PV factor (14%, 5th year)

= 20.78 x 0.52

= ₹ 10.81 lakhs

NPV = PV CI + PV of tax savings on STCL - PV CO

= 1124.40 + 10.81 - 1000

NPV = ₹ 135.20 lakhs

Advise: Since the NPV of the project is positive, project should be accepted

(B) Calculation of IRR

IRR is that discounting rate where NPV = 0 (point where PV of all CI = PV Co)

We know that @ 14%, NPV is ₹ 135.20, so by trial-and-error method we need to calculate that rate where NPV equals 0.

When Discounting rate is 16%

	1	**2**	**3**	**4**	**5**
CFAT	266.00	283.20	309.76	329.41	229.93
(+) Working Capital Release					150.00
(+) Scrap					140.00
PV Factor @ 14%	0.86	0.74	0.64	0.55	0.48
PV CI	**228.76**	**209.57**	**198.25**	**181.17**	**249.56**

PV CI = 1067.31

(+) PV of tax savings on STCL = 9.97 {20.78 x 0.48}

(-) PV CO = (1000)

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NPV = ₹ 77.29

Since NPV is positive at 16% as well, we need to go for Trial II at 20%

When Discounting rate is 20%

	1	2	3	4	5
CFAT	266.00	283.20	309.76	329.41	229.93
(+) Working Capital Release					150.00
(+) Scrap					140.00
PV Factor @ 14%	0.83	0.69	0.58	0.48	0.4
PV CI	220.78	195.41	179.66	158.12	207.97

PV CI = 961.94

(+) PV of tax savings on STCL = 8.31 {20.78 x 0.40}

(-) PV CO = (1000)

NPV = ₹ (29.75)

Since NPV is negative at 20%, IRR lies somewhere between 16% and 20%

IRR = $LR + \frac{\text{NPV at LR}}{\text{NPV at LR - NPV at HR}} \times (HR - LR)$

LR = Lower Rate (16% here) HR = Higher Rate (20% here)

IRR = $16 + \frac{77.29}{77.29 - (-29.75)} \times (20 - 16)$

IRR = 18.89%

(C) Calculation of Desirability Factory (Profitability Index)

PI = TOTAL PV CI / PV CO

PI = 1135.21 / 1000

PI = 1.13521

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10. (A) **Condition (a)** says that accounts shouldn't be overdue for more than 5 days to the net period. In other words, it means those accounts who are overdue by 45 days (40 days + 5 additional days), will not fulfill condition a) and thus will not be eligible for 90% lending.

Therefore, from the above, we can see that **Accounts DR 03 & DR 07** are overdue for more than 45 days and hence will not be eligible for 90% lending.

Condition (b) says that average receivables ageing (payment period) should not exceed 15 days to the net period i.e. it should not exceed 55 days (40 days + 15 days = 55 days). Therefore, from the above, we can see that **Accounts DR 04 & DR 10** has an ageing of more than 55 days. Hence, they would also not be eligible for 90% lending.

Amount of Bank Lending:

Accounts	Bank Lending at 90%	Bank Lending at 65%
DR 01	50,000	-
DR 02	25,000	-
DR 03	-	1,20,000
DR 04	-	72,000
DR 05	45,000	-
DR 06	1,75,000	-
DR 07	-	19,000
DR 08	54,000	-
DR 09	1,05,000	-
DR 10	-	37,000
Total	**4,54,000**	**2,48,000**
(-) Reserve	22,700 {4,54,000 x 5%}	37,200 {2,48,000 x 15%}
Net	**4,31,300**	**2,10,800**
Loan	**3,88,170**	**1,37,020**

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Total short-term loan granted by the bank = ₹ 5,25,190

(B) Calculation of the Effective Interest Cost

Interest at 12% (On 90% lending) = 3,88,170 x 0.12 = 46,580.4

Interest at 15% (On 65% lending) = 1,37,020 x 0.15 = 20,553

Total Interest = ₹ 67,133.4

Effective Interest Cost (%) = Interest (1-t) / Total Short-term Loan

= 67,133.4 (1-0.25) / 5,25,190

Effective Interest Cost (%) = 9.59%

11. (a) Emerging Issues/Priorities Affecting the Future Role of Chief Financial Officer (CFO)

(i) **Regulation**: Regulation requirements are increasing and CFOs have an increasingly personal stake in regulatory adherence.

(ii) **Globalisation:** The challenges of globalisation are creating a need for finance leaders to develop a finance function that works effectively on the global stage and that embraces diversity.

(iii) **Technology:** Technology is evolving very quickly, providing the potential for CFOs to reconfigure finance processes and drive business insight through 'big data' and analytics.

(iv) **Risk:** The nature of the risks that organisations face are changing, requiring more effective risk management approaches and increasingly CFOs have a role to play in ensuring an appropriate corporate ethos.

(v) **Transformation:** There will be more pressure on CFOs to transform their finance functions to drive a better service to the business at zero cost impact.

(vi) **Stakeholder Management:** Stakeholder management and relationships will become important as increasingly CFOs become the face of the corporate brand.

(vii) **Strategy:** There will be a greater role to play in strategy

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validation and execution, because the environment is more complex and quick changing, calling on the analytical skills CFOs can bring.

(viii) Reporting: Reporting requirements will broaden and continue to be burdensome for CFOs.

(ix) Talent and Capability: A brighter spotlight will shine on talent, capability and behaviours in the top finance role.

(b) Cost of equity capital is the rate of return which equates the present value of expected dividends with the market share price.

Methods for Computation of Cost of Equity Capital

- **Dividend Price Approach (:** Here, cost of equity capital is computed by dividing the expected dividend by market price per share.

  $$K_e = \frac{D_1}{P_o}$$

- **Earning/ Price Approach:** The advocates of this approach co-relate the earnings of the company with the market price of its share.

  $$K_e = \frac{E}{P}$$

- **Realized Yield Approach:** According to this approach, the average rate of return realized in the past few years is historically regarded as 'expected return' in the future. The yield of equity for the year is:

  $$Y_t = \frac{D_t + P_t}{P_{t-1}}$$

- **Capital Asset Pricing Model Approach (CAPM):** CAPM model describes the risk-return trade-off for securities. It describes the linear relationship between risk and return for securities.

  $K_e = R_f + ß\ (R_m - R_f)$

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(c) In the most of the situations the Net Present Value Method (NPV) and Profitability Index (PI) yield same accept or reject decision. In general items, under PI method a project is acceptable if profitability index value is greater than 1 and rejected if it less than 1. Under NPV method a project is acceptable if Net present value of a project is positive and rejected if it is negative. Clearly a project offering a profitability index greater than 1 must also offer a net present value which is positive. But a conflict may arise between two methods if a choice between mutually exclusive projects has to be made. Consider the following example:

	Project A	**Project B**
PV of Cash inflows	3,00,000	1,60,000
Initial cash outflows	1,00,000	40,000
Net present value	2,00,000	1,20,000
P.I	$\frac{3,00,000}{1,00,000} = 3$	$\frac{1,60,000}{40,000} = 4$

According to NPV method, project A would be preferred, whereas according to profitability index method project B would be preferred.

This is because Net present value gives ranking on the basis of absolute value of rupees, whereas, profitability index gives ranking on the basis of ratio. Although PI method is based on NPV, it is a better evaluation technique than NPV in a situation of capital rationing.

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6B: STRATEGIC MANAGEMENT

QUESTIONS

Multiple Choice Questions

1. In the ever-growing consumer electronics industry, Horizon Technologies found itself at a crossroads in 2018. The company, founded a decade earlier, had established itself as a key player in the global market for smartphones and other electronics. However, the pressure to stay relevant, meet customer demands, and fend off competitors was mounting. This is the story of how Horizon Technologies navigated its challenges, leveraging key business strategies and analyses to achieve remarkable success.

   Horizon Technologies recognized the need to divide its operations to find areas for improvement. They conducted a comprehensive value chain analysis, identifying both primary and support activities. By streamlining processes and eliminating redundancies, the company reduced production costs and enhanced product quality. This allowed them to offer more competitive prices, thus gaining a strategic edge in the market.

   The company's CEO, Mr. Jonathan Mercer, was known for his authoritative management style. His challenge was to transform his leadership approach to one that encouraged creativity and teamwork within the SBUs. Mr. Mercer invested in leadership development programs for middle and senior managers to enhance their interpersonal and communication skills. The transition wasn't easy, but it fostered a more collaborative and dynamic work environment.

   They did not stop there, Horizon Technologies adopted a Strategic Business Unit (SBU) structure, dividing the company into smaller, more manageable units. Each SBU was tasked with focusing on specific product lines. This decentralization empowered individual units to make

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strategic decisions autonomously, leading to quicker market response and a deeper understanding of customer needs. It was the catalyst for innovation and improved customer satisfaction.

Post organizational changes, Horizon Technologies strategized to embrace a cost leadership strategy, positioning itself as the go-to brand for affordable yet high-quality electronics. By optimizing production processes and supply chain management, the company achieved cost efficiencies that competitors struggled to match. This not only attracted cost-conscious consumers but also enabled the company to maintain healthy profit margins.

As Horizon Technologies expanded into new international markets, the management recognized the importance of adapting to the local environment. Conducting a thorough PESTLE analysis (Political, Economic, Social, Technological, Legal, and Environmental) proved pivotal for navigating complex market dynamics. This analysis highlighted specific challenges, especially in understanding socio-cultural trends and regulatory differences across regions. By leveraging these insights, Horizon Technologies was able to overcome these obstacles, customizing its products, marketing strategies, and operations to align more effectively with local preferences and regulations, ultimately contributing to their success.

Through these strategic moves, Horizon Technologies experienced a remarkable transformation. Within two years, their market share had significantly grown in local markets, whereas the cost leadership strategy resonated strongly. Their annual revenue skyrocketed by 35%, and the company saw a 20% increase in its stock price. The business case for Horizon Technologies serves as an inspiration for companies navigating competitive and dynamic industries.

Based on the above Case Scenario, answer the Multiple Choice Questions.

(i) In Horizon Technologies' journey towards globalization, PESTLE analysis played a pivotal role in navigating diverse international markets. Which aspect of PESTLE analysis proved to be the most challenging for Horizon Technologies?

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(a) Socio-cultural factors, as they struggled to keep up with changing trends and cultural preferences.

(b) Legal factors, given the complex regulatory landscape in foreign markets.

(c) Environmental factors, with the need to adhere to varying sustainability standards.

(d) Technological factors, due to rapid changes in local technology preferences.

(ii) Horizon Technologies implemented a Strategic Business Unit (SBU) structure to improve its responsiveness and innovation. How did the SBU structure differ from the company's previous organizational model, and what benefits did this new structure bring?

(a) The SBU structure replaced a functional structure and empowered units to make strategic decisions. It led to quicker market response and enhanced customer satisfaction.

(b) The SBU structure replaced a matrix structure, improving vertical communication and reducing operational silos.

(c) The SBU structure maintained the existing functional structure but focused solely on cost-cutting measures.

(d) The SBU structure introduced a more centralized approach, ensuring consistent decision-making across units.

(iii) Horizon Technologies faced internal challenges, including leadership struggles with an authoritative CEO. How did Mr. Jonathan Mercer transform his leadership style to foster a more collaborative work environment, and what were the key outcomes of this transformation?

(a) Mr. Mercer increased his authoritative approach to drive quicker decision-making and efficiency.

(b) He introduced a strict top-down hierarchy to enhance discipline and order within the organization.

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(c) Mr. Mercer invested in leadership development programs, enhancing interpersonal and communication skills, which resulted in a more collaborative and dynamic work environment.

(d) He delegated most of his responsibilities to middle managers, reducing his involvement in the company's daily operations.

(iv) While implementing a cost leadership strategy, Horizon Technologies went beyond just streamlining their production processes. What other factors did they consider achieving cost efficiencies, and how did this contribute to their success?

(a) They solely focused on reducing labor costs, resulting in job cuts and employee dissatisfaction.

(b) Horizon Technologies invested heavily in extravagant marketing campaigns to attract a premium customer base.

(c) They optimized supply chain management and invested in research and development, leading to enhanced product quality and reduced production costs.

(d) The company acquired competitors to eliminate competition and establish a monopoly in the market.

(v) The primary factor contributing to Horizon Technologies' remarkable transformation was their commitment to systematic analysis. What role did value chain analysis play in this transformation, and how did it drive their success in both local and global markets?

(a) Value chain analysis revealed opportunities for diversification, enabling them to cater to various market segments.

(b) It allowed the company to identify and eliminate inefficiencies in their operations, resulting in cost reductions and improved product quality.

(c) Value chain analysis highlighted the need for excessive vertical integration, helping them control the entire supply chain.

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(d) Horizon Technologies used value chain analysis primarily for financial forecasting and budgeting.

2. In a recent strategy meeting, the leadership team of TechNova, a growing software development firm, emphasized the importance of defining the core purpose of the organization. They aimed to outline the primary reason for the company's existence and to guide their decision-making processes during challenging times. They noted that this central guiding declaration would help align the team's efforts and communicate to stakeholders what the company stands for. What term best describes the central guiding declaration that communicates the purpose and values of TechNova?

   (a) Vision

   (b) Mission

   (c) Objectives

   (d) Goals

3. A company's flagship product has experienced a plateau in sales despite heavy promotions and marketing. What phase of the Product Life Cycle are they likely in, and what is the best strategic option to consider?

   (a) Introduction; increase prices

   (b) Growth; diversify product range

   (c) Maturity; seek product differentiation

   (d) Decline; invest in new technology

4. A multinational corporation is planning a merger with a local firm in a developing country. The local firm's community has high stakes in maintaining local employment and environmental standards but possesses low power in formal negotiations. How should the corporation categorize this stakeholder?

   (a) High power, low interest

   (b) Low power, high interest

   (c) High power, high interest

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(d) Low power, low interest

5. EcoGreen, a company specializing in sustainable home products, has decided to enter the energy sector by developing and marketing solar panels and home energy storage solutions. This new direction involves creating a completely new product line that extends beyond their traditional home goods, thereby entering an industry with their current brand. What strategy is EcoGreen using to enter the energy sector?

   (a) Market penetration

   (b) Product development

   (c) Market development

   (d) Diversification

6. Alpha Corp is undergoing a shift to foster a culture that encourages innovative thinking and team collaboration. To achieve this, the company is focusing on how leaders interact with their teams and set examples for behavior, aiming to align leadership practices with desired cultural outcomes. Which aspect of AlphaCorp is being adjusted to foster a culture of innovation and collaboration?

   (a) Structure

   (b) Systems

   (c) Skills

   (d) Style

Descriptive Questions

Chapter 1-Introduction to Strategic Management

7. XYZ Enterprises operates in various sectors, including renewable energy solutions, organic skincare products, eco-friendly packaging, and smart home technologies. The organization is currently in the process of recruiting a Chief Executive Officer. In this scenario, imagine yourself as an HR consultant for XYZ Enterprises. Identify the strategic level that encompasses this role within XYZ Enterprises. Provide an overview of the key duties and responsibilities falling under the Chief Executive Officer's scope.

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8. 'A company's mission statement is typically focused on its present business scope.' Explain the significance of a mission statement.

Chapter 2-Strategic Analysis: External Environment

9. Mr. Arun Kumar has built a successful business in the handmade ceramic products industry in Gujarat. His company, CeramiCrafts, is renowned for crafting distinctive, high-quality ceramic home décor items that have gained a strong foothold in the market. However, recent market shifts and rising competition have impacted sales. Seeking professional guidance, Mr. Kumar consults a strategic advisor who recommends an in-depth analysis of the competitive landscape. To comprehend the competitive landscape, what steps should Mr. Kumar follow?

10. According to Michael Porter, what are the five competitive forces that exist within an industry?

Chapter 3-Strategic Analysis: Internal Environment

11. ABC Corporation, a leading manufacturer of consumer electronics, is considering launching a new line of smart home devices. As a strategic manager, conduct a SWOT analysis for ABC Corporation to assess the feasibility and potential success of this new venture. Consider both internal and external factors that could impact on the success of the new product line.

12. What are channels? Why is channel analysis important? Explain the different types of channels?

Chapter 4-Strategic Choices

13. InnovaTech, a technology company with a range of business units, is assessing its investment opportunities. To allocate resources effectively, InnovaTech uses a matrix that evaluates each business unit based on two key factors: **industry attractiveness** and **business unit strength**. For example, the AI solutions division, positioned in a highly attractive industry with a strong competitive edge, receives a "go ahead" for further investment. In contrast, its legacy software division, operating in a less attractive industry with a weaker position, receives a "be careful" rating, suggesting limited investment. Identify and explain which analytical tool InnovaTech is using for this evaluation.

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14. What do you understand by Strategic Alliance? Discuss its advantages.

Chapter 5-Strategy Implementation and Evaluation

15. EcoTec, a company specializing in sustainable technology solutions, is facing challenges due to shifts in environmental regulations and market preferences. To manage these uncertainties, they regularly review and update their business assumptions and strategic plans based on changing regulatory environments and consumer trends. This proactive approach helps them stay aligned with evolving market conditions and maintain a competitive edge. Explain which approach is EcoTech to adapt to changes in regulations and market conditions?

16. **GloWare Ltd.**, an apparel manufacturer, has been in the market for over a decade. Until 2023, it operated on the founding principles of its CEO, focusing on a limited regional market. With new growth opportunities arising, GloWare is now interested in developing new competencies in areas such as digital marketing, product innovation, sustainable materials, and financial management. Recognizing that changing one area may impact others, the company wants a comprehensive understanding of the interconnected elements that contribute to its operational effectiveness.

    As a strategist, you are tasked with creating a questionnaire to analyze both the "hard" and "soft" elements of the organization. This assessment will enable GloWare to understand the factors that influence its effectiveness and to strategically align its structure, skills, and culture with its growth ambitions.

SUGGESTED ANSWERS/HINTS

MCQ No.	Answer	
1.	(i)	(a)
	(ii)	(a)
	(iii)	(c)
	(iv)	(c)
	(v)	(b)

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2.		**(b)**
3.		**(c)**
4.		**(b)**
5.		**(d)**
6.		**(d)**

7. The Chief Executive Officer (CEO) position within XYZ Enterprises operates at the **Corporate Level.** This executive level is key in leading the overall direction, performance, and success of the entire organization. The CEO assumes a central role in shaping the company's strategic vision, overseeing diverse business sectors, and ensuring alignment with organizational goals.

Key Duties and Responsibilities of the CEO:

The CEO's role encompasses various strategic responsibilities at the Corporate Level, involving:

1. **oversee the development** of strategies for the whole organization;
2. **defining the mission and goals** of the organization;
3. **determining what businesses**, it should be in;
4. **allocating resources** among the different businesses;
5. **formulating, and implementing** strategies that span individual businesses;
6. **providing leadership** for the organization;
7. ensuring that the corporate and business level strategies which company pursues are consistent with **maximizing shareholders wealth**; and
8. managing the **divestment and acquisition** process.

Given the diverse nature of XYZ Enterprises, including renewable energy solutions, organic skincare products, eco-friendly packaging, and smart home technologies, the CEO's responsibilities are tailored to navigate the unique challenges and opportunities presented by each sector. In conclusion, the CEO at the Corporate Level plays a critical role in guiding

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XYZ Enterprises strategically, ensuring cohesive leadership, and driving sustainable success across its diverse business domains.

8. A company's mission statement is typically focused on its present business scope, **who we are and what we do**. Mission statements broadly describe an organization's present capability, customer focus, activities, and business make up. Mission for an organization is significant for the following reasons:

- It ensures **unanimity of purpose** within the organization.
- It develops a basis, or standard, for **allocating organizational resources.**
- It provides a basis for **innovating the use of the organisation's resources**
- It **establishes** a general tone or **organizational climate**, to suggest a business-like operation.
- It serves as a **focal point** for those who can identify with the **organisation's purpose and direction**.
- It facilitates the **translation of objectives and goals into a work structure** involving the assignment of tasks to responsible elements within the organization.
- It specifies organizational purposes and the **translation of these purposes into goals** in such a way that cost, time, and performance parameters can be assessed and controlled.

9. Understanding the competitive landscape is crucial for Mr. Arun Kumar to navigate the handmade ceramic products industry in Gujarat successfully. This involves identifying both direct and indirect competitors while gaining insights into their vision, mission, core values, niche markets, and strengths and weaknesses. Here are the structured steps Mr. Kumar should follow to comprehend the competitive landscape and bolster his strategic position:

(i) **Identify the competitor:** The first step to understanding the competitive landscape is to identify the competitors in the

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handmade ceramic products industry. Mr. Kumar should gather actual data on the market share and positioning of competitors within the industry.

(ii) Understand the competitors: Once the competitors have been identified, Mr. Kumar can use market research reports, the internet, newspapers, social media, industry reports, and various other sources to understand the products and services offered by competitors. This will help him comprehend how they position themselves in different markets and their unique selling propositions.

(iii) Determine the strengths of the competitors: Mr. Kumar should assess what the competitors excel at. Do they offer superior product quality? Are they using marketing strategies that reach a wider customer base? Why do consumers choose them over others? Understanding these strengths will help Mr. Kumar identify areas where his company, CeramiCrafts, can enhance its offerings.

(iv) Determine the weaknesses of the competitors: Weaknesses of competitors can be identified by reviewing customer feedback, consumer reports, and reviews. Consumers often share their experiences, especially when products or services are either exceptional or subpar. By examining these weaknesses, Mr. Kumar can find opportunities to position CeramiCrafts as a better alternative.

(v) Put all of the information together: At this stage, Mr. Kumar should consolidate all the information gathered about competitors. This will help him identify gaps in the market that his company can fill, as well as areas where CeramiCrafts needs to improve. By understanding the competition thoroughly, he can devise strategies that strengthen his market position.

By following these steps, Mr. Kumar can gain a comprehensive understanding of the competitive landscape, enabling him to make informed strategic decisions for CeramiCrafts. This tailored approach ensures that the insights gained are directly applicable to the handmade ceramic products industry in Gujarat.

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10. Michael Porter's Five Forces model is a widely utilized tool for systematically analyzing the competitive forces within an industry. The model identifies five competitive forces that shape the overall competitive landscape:

- **Threat of New Entrants:** New entrants bring added capacity and product variety, intensifying competition and impacting prices. The size of new entrants magnifies their competitive influence, placing constraints on prices and affecting existing players' profitability.
- **Bargaining power of Buyers:** The ability of buyers to form groups or cartels influences their bargaining power. This force, particularly in industrial products, impacts pricing and often leads to demand for better services, influencing costs and investments for producers.
- **Bargaining power of Suppliers:** Suppliers with specialized offerings exert significant bargaining power, especially when limited in number. Supplier bargaining power determines raw material costs, affecting industry attractiveness and profitability.
- **Rivalry among Current Players:** Existing players engage in competition, influencing strategic decisions across various levels. This rivalry is evident in pricing, advertising, cost pressures, and product strategies, impacting the overall competitive landscape.
- **Threats from Substitutes:** Substitute products can alter an industry's competitive dynamics, offering price advantages or performance improvements. Substitutes limit prices and profits, and industries with substantial R&D investments are particularly susceptible to threats from substitute products.

These forces collectively determine industry’s attractiveness and profitability by influencing factors such as costs and investments required for industry participation. The strength of these forces varies across industries, ultimately shaping the potential for earning attractive profits.

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11. SWOT Analysis for ABC Corporation's New Smart Home Devices Venture:

Strengths	Weaknesses
• Strong brand reputation in consumer electronics.	• Limited experience in the smart home devices market.
• Established distribution network.	• May require additional investments in research and development.
• Access to technological expertise for product development.	• Potential challenges in integrating a new product line with existing offerings.
• Financial resources to support product launch and marketing.	• Lack of established customer base for smart home devices.
Opportunities	**Threats**
• Growing market for smart home devices due to increasing consumer interest in home automation.	• Intense competition from established players in the smart home devices market.
• The possibility of partnering with existing smart home platform providers.	• Rapid technological advancements lead to short product life cycles.
• Potential to leverage brand loyalty from existing customers.	• Potential for cybersecurity threats in connected devices.
• Ability to differentiate through innovative features and design.	• Economic factors impacting consumer spending on discretionary items.

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The SWOT analysis highlights that while ABC Corporation has several strengths that can support the launch of a new smart home devices line, there are also significant weaknesses and threats to consider. To maximize the chances of success, ABC Corporation should focus on leveraging its brand reputation and distribution network while carefully addressing the weaknesses and threats identified. Additionally, being informed about technological developments and consumer trends will be essential for maintaining competitiveness in the dynamic smart home devices market.

12. Channels represent the **distribution system** through which organizations distribute their products or provide services to customers. They play a pivotal role in reaching target markets, maximizing sales, and establishing competitive advantages.

Channel analysis is important when the business strategy is to scale up and expand beyond the current geographies and markets. When a business plans to grow to newer markets, they need to develop or leverage existing channels to get to new customers. Thus, analysis of channels that suit one's products and customers is of utmost importance.

There are typically three channels that should be considered: sales channel, product channel and service channel.

- **The sales channel** - These are the intermediaries involved in selling the product through each channel and ultimately to the end user. The key question is: Who needs to sell to whom for your product to be sold to your end user? **For example**, many fashion designers use agencies to sell their products to retail organizations, so that consumers can access them.
- **The product channel** - The product channel focuses on the series of intermediaries who physically handle the product on its path from its producer to the end user. This is true of Australia Post, who delivers and distributes many online purchases between the seller and purchaser when using eBay and other online stores.

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- **The service channel** - The service channel refers to the entities that provide necessary services to support the product, as it moves through the sales channel and after purchase by the end user. The service channel is an important consideration for products that are complex in terms of installation or customer assistance. **For example**, a Bosch dishwasher may be sold in a Bosch showroom, and then once sold it is installed by a Bosch contracted plumber.

13. InnovaTech is using the **GE Matrix**, a strategic tool designed to assess the resource allocation needs of different business units based on two factors: **industry attractiveness** and **business unit strength**. This matrix is a nine-cell grid that helps companies prioritize investments by categorizing units into "grow," "hold," or "harvest" zones, depending on their positions within the matrix.

For InnovaTech, the **AI solutions division**, which operates in a highly attractive industry with a strong competitive position, falls into the "grow" category, meriting further investment. Meanwhile, the **legacy software division** operates in a less attractive industry with weaker positioning, likely placing it in the "harvest" or "hold" category, where investments are minimized.

The GE Matrix enables companies like InnovaTech to systematically evaluate each business unit's potential, optimize resource allocation, and focus on divisions that align with long-term growth and profitability goals.

14. A strategic alliance is a relationship between two or more businesses that enables each to achieve certain strategic objectives which neither would be able to achieve on its own. The strategic partners maintain their status as independent and separate entities, share the benefits and control over the partnership, and continue to make contributions to the alliance until it is terminated. The advantages of strategic alliance can be broadly categorised as follows:

(a) **Organizational:** Strategic alliance helps to learn necessary skills and obtain certain capabilities from strategic partners. Strategic

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partners may also help to enhance productive capacity, provide a distribution system, or extend supply chain.

(b) **Economic:** There can be reduction in costs and risks by distributing them across the members of the alliance. Greater economies of scale can be obtained in an alliance, as production volume can increase, causing the cost per unit to decline. The partners can also take advantage of co-specialization, creating additional value.

(c) **Strategic:** Rivals can join together to cooperate instead of competing. Strategic alliances may also be useful to create a competitive advantage by the pooling of resources and skills. This may also help with future business opportunities and the development of new products and technologies. Strategic alliances may also be used to get access to new technologies or to pursue joint research and development.

(d) **Political:** Sometimes strategic alliances are formed with a local foreign business to gain entry into a foreign market either because of local prejudices or legal barriers to entry.

15. EcoTech is using **Premise Control** to adapt to changes in regulations and market conditions. Premise Control is a strategic management approach focused on continuously monitoring and reviewing the underlying assumptions that form the basis of an organization's strategy. By regularly assessing these assumptions—such as environmental regulations and consumer preferences, EcoTech ensures that its strategic plans remain relevant and responsive to external changes. This proactive process helps the company make timely adjustments to its strategies, allowing it to stay competitive and aligned with the evolving market environment.

16. In addressing the strategic needs of **GloWare Ltd.**, the **McKinsey 7-S Model** serves as a valuable tool. This model examines how various "hard" and "soft" elements within the organization interact, with the understanding that modifying one aspect can create a ripple effect on other elements, helping to maintain a balanced and effective organizational structure. By analyzing these elements, **GloWare** can gain

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insights into its organizational design and make strategic adjustments to improve performance.

The McKinsey 7-S Model categorizes elements into **hard** and **soft** components:

Hard Elements (directly managed by the company):

1. **Strategy**: The organization's direction and competitive approach, designed to leverage core competencies and achieve industry leadership.
2. **Structure**: The chosen organizational setup, shaped by resource availability and the degree of centralization or decentralization desired by management.
3. **Systems**: The daily operations, processes, and teams that execute objectives in an efficient and effective manner.

Soft Elements (influenced by organizational culture and more challenging to define):

1. **Shared Values**: Core beliefs that shape the culture and ethical code within the organization.
2. **Style**: Leadership style and its impact on decision-making, employee motivation, and goal delivery.
3. **Staff**: The talent pool and workforce capabilities.
4. **Skills**: The key competencies of employees that contribute to organizational success.

While the McKinsey 7-S Model provides a structured approach to analyzing organizational effectiveness, it has certain limitations:

1. **Limited Focus on External Environment**: The model focuses only on internal elements, potentially overlooking external factors impacting the organization.
2. **Undefined Organizational Effectiveness**: It does not clearly explain how to measure or achieve organizational effectiveness.

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3. **Static Nature**: The model is considered more static and may lack flexibility in dynamic decision-making situations.

4. **Potential Gaps in Strategy Execution**: It may not fully capture gaps between strategy development and execution.

By applying the McKinsey 7-S Model, **GloWare Ltd.** can gain a comprehensive understanding of the interconnected elements within its organization and how they impact overall performance. Insights gathered from a questionnaire based on this model can inform strategic decisions, allowing **GloWare** to enhance growth, operational efficiency, and competitiveness in a changing market.

PAPER – 6: FINANCIAL MANAGEMENT AND STRATEGIC MANAGEMENT

SECTION A: FINANCIAL MANAGEMENT

Question No. ***1*** *is compulsory.*

Attempt any ***two*** *questions out of the remaining* ***three*** *questions.*

In case, any candidate answers extra question(s)/ sub-question(s) over and above the required number, then only the requisite number of questions first answered in the answer book shall be valued and subsequent extra question(s) answered shall be ignored.

Working notes should form part of the answer.

Question 1

(a) Theme Ltd provides you the following information:

12.5 % Debt	*₹ 45,00,000*
Debt to Equity ratio	*1.5 : 1*
Return on Shareholder's fund	*54%*
Operating Ratio	*85%*
Ratio of operating expenses to Cost of Goods sold	*2 : 6*
Tax rate	*25%*
Fixed Assets	*₹ 39,00,000*
Current Ratio	*1.8 : 1*

You are required to calculate:

(i) Interest Coverage Ratio

(ii) Gross Profit Ratio

(iii) Current Assets

(b) *Alpha Limited has provided following information:*

Equity Share Capital	*25,000 Shares @ ₹ 100 per Share*
15% Debentures	*10,000 Debentures@ ₹ 750/- per Debenture*
Sales	*50 Lakhs units@ ₹ 20 per unit*
Variable Cost	*₹ 12.50 per unit*
Fixed Costs	*₹ 175.00 Lakhs*

Due to recent policy changes and entry of foreign competitors in the sector, Alpha Limited expects the sales may decline by 15-20%, However, selling price and other costs will remain the same. Corporate Taxes will continue@20%.

You are required to calculate the decrease in Earnings per share, Degree of Operating Leverage and Financial Leverage separately if sales are declined by (i) 15%; and (ii) 20%;

(c) *Following is the sales information in respect of Bright Ltd:*

Annual Sales (90 % on credit)	*₹ 7,50,00,000*
Credit period	*45 days*
Average Collection period	*70 days*
Bad debts	*0.75%*
Credit administration cost (out of which 2/5th is avoidable)	*₹ 18,60,000*

A factor firm has offered to manage the company's debtors on a non-recourse basis at a service charge of 2%. Factor agrees to grant advance against debtors at in interest rate of 14% after withholding 20% as reserve. Payment period guaranteed by factor is 45 days. The cost of capital of the company is 12.5%. One time redundancy payment of ₹ 50,000 is required to be made to factor.

Calculate the effective cost of factoring to the company. (Assume 360 days in a year)

Answer

(a) Working Notes:

Debt = ₹ 45,00,000

Interest = ₹ 45,00,000 x 12.5%= 5,62,500

Debt to Equity = 1.5:1 = $\frac{\text{Total Debt}}{\text{Shareholders' Equity}}$

Equity = ₹ 30,00,000

Return of Shareholder's funds = 54% = $\frac{\text{Net Profit after taxes}}{\text{Equity shareholders' fund}} \times 100$

Profit after tax (PAT) = 54% x Equity = ₹16,20,000

Profit before tax (PBT)(1-25%) = Profit after tax

= ₹16,20,000/75% = ₹21,60,000

Earning before interest and tax (EBIT) = PBT + Interest

= ₹21,60,000 + ₹ 5,62,500

= ₹27,22,500

(i) Interest Coverage Ratio = EBIT/Interest

= ₹27,22,500/₹5,62,500

= 4.84 Times

(ii) Operating Profit Ratio = 1 - Operating Ratio

= 1 – 0.85 = 0.15 or 15%

0.15 = $\frac{\text{Operating Profit}}{\text{Sales}} \times 100$

Sales = EBIT or Operating Profit /0.15

= ₹ 27,22,500 / 0.15

= ₹ 1,81,50,000

Operating ratio = $\frac{\text{Operating expenses}}{\text{Cost of goods sold (COGS)}}$ = 2 : 6 = 1 : 3

Operating expenses = 1/3COGS

Operating cost = Sales – Operating profit

= ₹ 1,81,50,000 - ₹ 27,22,500

= ₹ 1,54,27,500

₹ 1,54,27,500 = COGS + Operating expenses

₹ 1,54,27,500 = COGS + 1/3COGS

COGS = ₹ 1,15,70,625

Gross profit = Sales – COGS

= 1,81,50,000 – 1,15,70,625

= ₹ 65,79,375

Gross Profit ratio $= \frac{\text{Gross Profit}}{\text{Sales}} \times 100$

= 65,79,375/1,81,50,000

= 0.3625 or 36.25%

Gross profit and sales can be calculated in alternative way also. However, there will be no change in GP ratio i.e 36.25%

(iii) Current Ratio $= \frac{\text{Current Assets}}{\text{Current Liabilities}}$

= 1.8

Current Assets = 1.8 Current Liabilities

Total of Balance sheet liability = Equity + Debt + Current Liabilities

=30,00,000+45,00,000+CL ....(2)

Total Balance sheet asset = Fixed Assets + Current Assets

= 39 lakhs + CA= 39 + 1.8CL.......(3)

Equating 2 and 3,

75,00,000 + CL = 39,00,000 + 1.8CL

0.8CL = 36,00,000

CL =₹ 45,00,000

Current Assets = 1.8 CL **=** 1.8 x 45 lakhs= ₹ **81,00,000**

(b) Income Statement with required calculations

Particulars	**(₹)**	**(₹)**	**(₹)**
	Existing	**Sales declined by 15%**	**Sales declined by 20%**
Sales in units	50,00,000	42,50,000	40,00,000
Sales price per unit	20	20	20
Variable Cost per unit	(12.50)	(12.50)	(12.50)
Contribution per unit	7.5	7.5	7.5
Contribution	3,75,00,000	3,18,75,000	3,00,00,000
Fixed expenses	(1,75,00,000)	(1,75,00,000)	(1,75,00,000)
EBIT	2,00,00,000	1,43,75,000	1,25,00,000
Debenture Interest	(11,25,000)	(11,25,000)	(11,25,000)
EBT	1,88,75,000	1,32,50,000	1,13,75,000
Tax @ 20%	(37,75,000)	(26,50,000)	(22,75,000)
Profit after tax (PAT)	1,51,00,000	1,06,00,000	91,00,000
No. of shares	25,000	25,000	25,000
Earnings per share (EPS) $= \frac{\text{PAT}}{\text{No. of shares}}$	$\frac{₹1,51,00,000}{25,000}$ = ₹ 604	$\frac{₹1,06,00,000}{25,000}$ = ₹424	$\frac{₹91,00,000}{25,000}$ = ₹364
(i) Decrease in EPS		= ₹180 **Or** % Decrease in EPS $= \frac{180}{604} \times 100$ **= 29.80%**	= ₹240 **Or** % Decrease in EPS $= \frac{240}{604} \times 100$ **= 39.73%**
(ii) Operating leverage $= \frac{\text{Contribution}}{\text{EBIT}}$ Or		$= \frac{₹3,18,75,000}{₹1,43,75,000}$ **= 2.22** **Or** 28.125/15 =	$= \frac{₹3,00,00,000}{₹1,25,00,000}$ **= 2.40** **Or** 37.50/20 **1.875**

Degree of Operating leverage $= \frac{\text{Percentage change in EBIT}}{\text{Percentage change in sales}}$		**1.875**	
(iii) Financial Leverage $= \frac{\text{EBIT}}{\text{EBT}}$ Or Degree of Financial Leverage $= \frac{\text{Percentage change in EPS}}{\text{Percentage change in EBIT}}$		$= \frac{₹1,43,75,000}{₹1,32,50,000}$ **= 1.08** **Or** 29.80/28.125 **= 1.06**	$= \frac{₹1,25,00,000}{₹1,13,75,000}$ **= 1.10** **Or** 39.735/37.50 **= 1.06**

(c) Evaluation of Factoring Proposal

	Particulars	**₹**	**₹**
A.	**Savings due to factoring**		
	Bad Debts saved	0.75% x 7.5 crores x 90%	₹ 5,06,250
	Administration cost saved	18.6 lakhs x 2/5	₹ 7,44,000
	Interest saved due to reduction in average collection period	7.5 crores x 90% x (70-45)/ 360 x 12.5%	₹ 5,85,937.5
	Total		**₹ 18,36,187.5**
B.	**Costs of factoring:**		
	Service charge	7.5 crores x 90% x 2%	₹ 13,50,000
	Interest cost	₹ 1,15,171.875 x 360/45	₹ 9,21,375
	Redundancy Payment		₹ 50,000
	Total		**₹ 23.21,375**
C.	**Net Annual cost to the Firm: (A-B)**		**₹ 4,85,187.5**
	Rate of effective cost of factoring	₹ 4,85,187.5/ ₹ 64,66,078.125 x 100	**7.504%**

Advice: Since the rate of effective cost of factoring is less than the existing cost of capital, therefore, the proposal is acceptable.

Credit Sales = ₹ 7.5 crores x 90%	= ₹ 6,75,00,000
Average level of receivables = ₹ 6.75 crores x 45/360	= ₹ 84,37,500
Service charge = 2% of ₹ 84,37,500	₹ 1,68,750
Reserve = 20% of ₹ 84,37,500	₹ 16,87,500
Total (i)	₹ 18,56,250
Thus, the amount available for advance is	
Average level of receivables	₹ 84,37,500
Less: Total (i) from above	₹ 18,56,250
(ii)	₹ 65,81,250
Less: Interest @ 14% p.a. for 45 days	₹ 1,15,171.875
Net Amount of Advance available.	₹ 64,66,078.125

Note: Alternatively, if redundancy cost is taken as irrelevant for decision making, then Net Annual cost to the Firm will be ₹ 4,35,187.5 and Rate of effective cost of factoring will be ₹ 4,35,187.5/₹ 64,66,078.125 x 100 = 6.730%

If average level of receivables is considered for 70 days then the calculation can be done in following way:

Evaluation of Factoring Proposal

Credit Sales = ₹ 7.5 crores X 90%	= ₹ 6,75,00,000
Average level of receivables = ₹ 6.75 crores x 70/360	= ₹ 1,31,25,000
Service charge = 2% of ₹ 1,31,25,000	₹ 2,62,500
Reserve = 20% of ₹ 1,31,25,000	₹ 26,25,000
Total (i)	₹ 28,87,500
Thus, the amount available for advance is	
Average level of receivables	₹ 1,31,25,000
Less: Total (i) from above	₹ 28,87,500

(ii)	₹ 1,02,37,500
Less: Interest @ 14% p.a. for 45 days	₹ 1,79,156.25
Net Amount of Advance available.	₹ 1,00,58,343.75

Note 1: Accordingly, interest cost will be ₹ 14,33,250 cost of factoring will be ₹ 28,33,250. Therefore, Rate of effective cost of factoring is 9.913%

Note 2: Alternatively, if redundancy cost is taken as irrelevant for decision making, then Net Annual cost to the Firm will be ₹ 9,47,062.5 and Rate of effective cost of factoring will be ₹ 9,47,062.5/ ₹ 1,00,58,343.75 x 100 = 9.416%.

Advice: Since the rate of effective cost of factoring is less than the existing cost of capital, therefore, the proposal is acceptable.

Question 2

(a) The capital structure of Shine Ltd. as on 31.03.2024 is as under:

Particulars	***Amount (₹)***
Equity share capital off 10 each	*45,00,000*
15% Preference share capital of f 100 each	*36,00,000*
Retained earnings	*32,00,000*
13% Convertible Debenture off 100 each	*67,00,000*
11% Term Loan	*20,00,000*
Total	*2,00,00,000*

Additional information:

(A) Company issued 13% Convertible Debentures of ₹ 100 each on 01.04.2023 with a maturity period of 6 years. At maturity, the debenture holders will have an option to convert the debentures into equity shares of the company in the ratio of 1 : 4 (4 shares for each debenture). The market price of the equity share is ₹ 25 each as on 31.03.2024 and the growth rate of the share is 6% per annum.

(B) Preference stock, redeemable after eight years, is currently selling at ₹ 150 per share.

(C) The prevailing default-risk free interest rate on 10-year GOI treasury bonds is 6%. The average market risk premium is 8% and the Beta (β) of the company is 1.54.

Corporate tax rate is 25% and rate of personal income tax is 20%.

You are required to calculate the cost of:

(i) Equity Share Capital

(ii) Preference Share Capital

(iii) Convertible Debenture

(iv) Retained Earnings

(v) Term Loan

(b) Following data is available in respect of Levered and Unlevered companies having same business risk:

Capital employed = ₹ 2,00,000, EBIT = ₹ 25,000 and Ke = 12.5%

Sources	***Levered Company (₹)***	***Unlevered Company (₹)***
Debt (@8%)	*75,000*	*Nil*
Equity	*1,25,000*	*2,00,000*

An investor is holding 12% shares in levered company. Calculate the increase in annual earnings of investor if he switches over his holding from Levered to Unlevered company.

Answer

(a) (i) Cost of Equity Share capital

As per CAPM Model $K_e = R_f + ß (R_m - R_f)$

Rf = 6%

B = 1.54

Rm-Rf = 8%

Ke = 6% + 1.54(8%)

Ke = **18.32%**

(ii) Cost of Preference Share capital

n = 8

Net Proceeds (NP) = 150

Redemption Value (RV) = 100

Preference Dividend (PD) = 15

$$K_p = \frac{PD + \frac{(RV - NP)}{n}}{\frac{(RV + NP)}{2}}$$

$$K_p = \frac{15 + \left(\frac{100 - 150}{8}\right)}{\left(\frac{100 + 150}{2}\right)}$$

K_p = **7%**

Alternatively, if we take NP as 100 and RV as 100, then solution can be done in the following way:

Cost of Preference Share capital

n = 8

Net Proceeds (NP) = 100

Redemption Value (RV) = 150

Preference Dividend (PD) = 15

$$K_p = \frac{PD + \frac{(RV - NP)}{n}}{\frac{(RV + NP)}{2}}$$

$$K_p = \frac{15 + \left(\frac{150 - 100}{8}\right)}{\left(\frac{150 + 100}{2}\right)}$$

K_p = **17%**

(iii) Cost of convertible debenture

Cash Redemption Value (RV) = 100

Share Redemption Value (RV):

Value of share after 5 years = 25 x $(1.06)^5$ = 33.46

Share Redemption Value (RV) = 33.46 X 4=133.82

Therefore, investor will choose share redemption.

Redemption Value (RV) = 133.82

Net Proceeds (NP) = 100

n = 5

Interest (I) = 13

Tax (t) = 25%

$$K_d = \frac{I(1-t)+\frac{(RV-NP)}{n}}{\frac{(RV+NP)}{2}}$$

$$= \frac{13(1-0.25)+\frac{(133.82-100)}{5}}{\frac{(133.82+100)}{2}}$$

K_d = **14.13%**

(iv) Cost of Retained Earnings

$K_r = K_e (1-t_p)$ = 18.32 % x (1-0.20) = **14.66%**

We can also take cost of equity as cost of retained earnings,

Accordingly, $K_r = K_e$ = **18.32%**

(v) Cost of Term Loan

= 11% x (1-0.25) = **8.25%**

(b) 1. Valuation of firms

Particulars	**Levered Firm (₹)**	**Unlevered Firm (₹)**
EBIT	25,000	25,000
Less: Interest on debt (8% × ₹ 75,000)	6,000	Nil
Earnings available to Equity shareholders	19,000	25,000
K_e	12.5%	12.5%
Value of Equity (S) (Earnings available to Equity shareholders/ K_e)	1,52,000	2,00,000
Debt (D)	75,000	Nil
Value of Firm (V) = S + D	2,27,000	2,00,000

Value of Levered company is more than that of unlevered company. Therefore, investor will sell his shares in levered company and buy shares in unlevered company. To maintain the level of risk he will borrow proportionate amount and invest that amount also in shares of unlevered company.

2. Investment & Borrowings

	₹
Sell shares in Levered company (₹ 1,52,000 x 12%)	18,240
Borrow money (₹ 75,000 x 12%)	9,000
Buy shares in Unlevered company	27,240

3. Change in Return

	₹
Income from shares in Unlevered company	
(₹ 27,240 x 12.5%)	3,405
Less: Interest on loan (₹ 9,000 x 8%)	720
Net Income from unlevered firm	2,685
Less: Income from Levered firm (₹ 18,240 x 12.5%)	2,280
Incremental Income due to arbitrage	405

Solution can also be done in the following way:

Valuation of firms

Particulars	**Levered Firm (₹)**	**Unlevered Firm (₹)**
EBIT	25,000	25,000
Less: Interest on debt (8% × ₹ 75,000)	6,000	Nil
Earnings available to Equity shareholders	19,000	25,000
K_e	12.5%	12.5%
Value of Equity (S) (Earnings available to Equity shareholders/ K_e)	1,52,000	2,00,000
Debt (D)	75,000	Nil
Value of Firm (V) = S + D	2,27,000	2,00,000

Value of Levered company is more than that of unlevered company. Therefore, investor will sell his shares in levered company and buy shares in unlevered company.

Arbitrage Process:

If investor have 12% shares of levered company, value of investment in equity shares is 12% of ₹ 1,52,000 i.e. ₹ 18,240 and return will be 12% of ₹19,000 = ₹ 2,280.

Alternate Strategy will be:

Sell 12% shares of levered firm for ₹ 18,240 and borrow 12% of levered firm's debt i.e. ₹ 9,000 (12% of ₹ 75,000) and invest the money i.e. 12% in unlevered firm's stock:

Total resources /Money investor have = ₹ 18,240 + ₹ 9,000 = ₹ 27,240 and investor invest 12% of ₹ 2,00,000 = ₹ 24,000

Surplus cash available with investor is = ₹ 27,240 – ₹ 24,000 = ₹ 3,240

Investor return = 12% EBIT of unlevered firm – Interest to be paid on borrowed funds

i.e. = 12% of ₹ 25,000 – 8% of ₹ 9,000 = ₹ 3,000 – ₹ 720 = ₹ 2,280

Now, return remains the same i.e. ₹ 2,280 which investor is getting from levered company before investing in unlevered company but still have ₹ 3,240 excess money available with investor. Hence, investor is better off by doing arbitrage.

Question 3

(a) *HCP Ltd. is a leading manufacturer of railway parts for passenger coaches and freight wagons. Due to high wastage of material and quality issues in production, the General Manager of the company is considering the replacement of machine A with a new CNC machine B. Machine A has a book value of ₹ 4,80,000 and remaining economic life is 6 years. It could be sold now at ₹ 1,80,000 and zero salvage value at the end of sixth year. The purchase price of Machine B is ₹ 24,00,000 with economic life of 6 years. It will require ₹ 1,40,000 for installation and ₹ 60,000 for testing. Subsidy of 15% on the purchase price of the machine B will be received from Government at the end of 1st year. Salvage value at the end of sixth year will be ₹ 3,20,000.*

The General manager estimates that the annual savings due to installation of machine B include a reduction of three skilled workers with annual salaries of ₹ 1,68,000 each, ₹ 4,80,000 from reduced wastage of materials and defectives and ₹ 3,50,000 from loss in sales due to delay in execution of purchase orders. Operation of Machine B will require the services of a trained technician with annual salary of t 3,90,000 and annual operation and maintenance cost will increase by ₹ 1,54,000. The company's tax rate is 30% and it's required rate of return is 14%. The company follows straight line method of depreciation. Ignore tax savings on loss due to sale of existing machine.

The present value factors at 14% are:

Years	***0***	***1***	***2***	***3***	***4***	***5***	***6***
PV Factor	*1*	*0.877*	*0.769*	*0.675*	*0.592*	*0.519*	*0.456*

Required:

(i) *Calculate the Net Present Value and Profitability Index and advise the company for replacement decision.*

(ii) *Also calculate the discounted pay-back period.*

(b) *Vista Limited's retained earnings per share for the year ending 31.03.2023 being 40% is ₹3.60 per share. Company is foreseeing a growth rate of 10% per annum in the next two years. After that the growth rate is expected to stabilize at 8% per annum. Company will maintain its existing pay-out ratio. If the investor's required rate of return is 15%, Calculate the intrinsic value per share as of date using Dividend Discount model.*

Answer

(a) Calculation of Net Initial Cash Outflows:

Particulars	**₹**
Cost of new machine	24,00,000
Less: Sale proceeds of existing machine	(1,80,000)
Add: Installation	1,40,000
Add: Testing	60,000
Less: Subsidy from government (15% of 24,00,000) x 0.877	**(3,15,720)**
Net initial cash outflows	**21,04,280**

Calculation of Incremental Depreciation

Particulars	**₹**
Depreciation on existing machine (4,80,000/6) **(i)**	80,000
Depreciation base of New Machine	
Cost of new machine	24,00,000
Add: Installation	1,40,000
Add: Testing	60,000
Less: Subsidy from government	(3,60,000)
Less: Salvage value at the end of 6th year	(3,20,000)
Depreciation base of New Machine	**19,20,000**
Depreciation on New Machine (19,20,000/6) **(ii)**	3,20,000
Incremental depreciation [(ii) – (i)]	2,40,000

Computation of Annual Operating Cash flow after tax (CFAT)

Particulars	Amount (₹)	Amount (₹)
Savings in cost		
Cost of 3 skilled workers (₹1,68,000 x 3)	5,04,000	
Reduced wastage of material	4,80,000	
Saving in loss of sales	3,50,000	
Total		13,34,000
Less: Increase in cost		
Salary to trained technician	3,90,000	
Increase in annual operation and maintenance cost	1,54,000	
Total		(5,44,000)
Incremental Saving before tax and depreciation		7,90,000
Less: Incremental Depreciation		(2,40,000)
Incremental PBT		5,50,000
Less: Tax @30%		(1,65,000)
PAT		3,85,000
Add: Depreciation		2,40,000
Incremental CFAT		6,25,000

Calculation of NPV

Particulars	Year	Net Cashflow (₹)	PVF @ 14%	PV (₹)
Net initial cash outflows	0	(24,20,000)	1	(21,04,280)
Incremental CFAT	1 to 6	6,25,000	3.888	24,30,000
Salvage Value of New Machine	6	3,20,000	0.456	1,45,920

PV of inflows				25,75,920
Net Present Value				**4,71,640**

$$\text{Profitability Index} = \frac{\text{Sum of discounted cash inflows}}{\text{Initial cash outlay or Total discounted cash outflow (as the case may)}}$$

= 25,75,920/21,04,280= **1.224**

Advise: Since the NPV is positive and PI is greater than 1, the company should replace the machine

Computation of Discounted Payback Period

Year	Cashflow	PVF @ 14%	PV of CFs (₹)	Cumulative PV (₹)
1	6,25,000	0.877	5,48,125	5,48,125
2	6,25,000	0.769	4,80,625	10,28,750
3	6,25,000	0.675	4,21,875	14,50,625
4	6,25,000	0.592	3,70,000	18,20,625
5	6,25,000	0.519	3,24,375	21,45,000
6	9,45,000	0.456	4,30,920	25,75,920

Discounted Payback Period

$$= 4 + \frac{21,04,280 - 18,20,625}{3,24,375}$$

= 4.87 years

If we take subsidy in cash inflow of 1st year, then solution can also be done in the following way:

Calculation of Net Initial Cash Outflows:

Particulars	₹
Cost of new machine	24,00,000
Less: Sale proceeds of existing machine	(1,80,000)
Add: Installation	1,40,000
Add: Testing	60,000
Net initial cash outflows	**24,20,000**

Note: However, Incremental Depreciation and CFAT will remain same.

Calculation of NPV

Particulars	Year	Net Cashflow (₹)	PVF @ 14%	PV (₹)
Net initial cash outflows	0	(24,20,000)	1	(24,20,000)
Subsidy	1	3,60,000	0.877	3,15,720
Incremental CFAT	1 to 6	6,25,000	3.888	24,30,000
Salvage Value of New Machine	6	3,20,000	0.456	1,45,920
PV of inflows				28,91,640
Net Present Value				**4,71,640**

$$\text{Profitability Index} = \frac{\text{Sum of discounted cash in flows}}{\text{Initial cash outlay or Total discounted cash outflow (as the case may)}}$$

= 28,91,640 /24,20,000 = **1.195**

Advise: Since the NPV is positive and PI is greater than 1, the company should replace the machine

Computation of Discounted Payback Period

Year	Cashflow	PVF @ 14%	PV of CFs (₹)	Cumulative PV (₹)
1	9,85,000	0.877	8,63,845	8,63,845
2	6,25,000	0.769	4,80,625	13,44,470
3	6,25,000	0.675	4,21,875	17,66,345
4	6,25,000	0.592	3,70,000	21,36,345
5	6,25,000	0.519	3,24,375	24,60,720
6	9,45,000	0.456	4,30,920	28,91,640

Discounted Payback Period

$$= 4 + \frac{24,20,000 - 21,36,345}{3,24,375}$$

= 4.87 years

(b) As per Dividend discount model, the price of share is calculated as follows:

Retained earning per share = ₹ 3.60

Dividend per share, $D_0 = \frac{₹\ 3.60}{40\%} \times 60\% = ₹5.40$

$$P = \frac{D_1}{(1+K_e)^1} + \frac{D_2}{(1+K_e)^2} + \frac{D_3}{(K_e-g)} \times \frac{1}{(1+K_e)^2}$$

Where,

P = Price per share

K_e = Required rate of return on equity

g = Growth rate

$$P = \frac{5.4x1.1}{(1+0.15)^1} + \frac{5.94x1.1}{(1+0.15)^2} + \frac{6.534x1.08}{(0.15-0.08)} \times \frac{1}{(1+0.15)^2}$$

P= 5.17 + 4.94 + 76.23 = ₹86.33

Intrinsic value of share is ₹ 86.33

Question 4

(a) State with brief reasons whether the following statements are true or false:

(i) Maximising Market Price Per Share (MPS) as the financial objective which maximises the wealth of shareholders.

(ii) A combination of lower risk and higher return is known as risk return trade off and at this level of risk-return, profit is maximum.

(iii) Financial distress is a position when accounting profits of a firm are sufficient to meet its long-term obligations.

(iv) Angel investor is one who provides funds for start-up m exchange for an ownership/equity.

(b) ABC Ltd. is approaching the banks for financing its business activity. You are required to describe any four forms of bank credit for the consideration of the company.

(c) Discuss the relevance of Payback reciprocal in capital budgeting decisions.

OR

(c) Explain the features of crowd funding.

Answer

(a)

Statement	**True or False**	**Reason**
Maximising Market Price Per Share (MPS) as the financial objective which maximises the wealth of shareholders.	**True**	Maximizing MPS or Market value as the financial objective will ensure the maximizing shareholder's wealth.
A combination of lower risk and higher return is known as risk-return trade off and at this level of risk-return, profit is maximum.	**False**	There is a direct relationship between risk and profit. Higher the risk, higher is the possibility of profits. Stockholders expect greater returns from investments of higher risk and vice-versa.
Financial distress is a position when accounting profits of a firm are sufficient to meet its long-term obligations.	**False**	Financial distress is a position where Cash inflows of a firm are inadequate to meet all its current obligations.
Angel investor is one who provides funds for start-up in exchange for an ownership/equity.	**True**	Angel Financing is a form of an equity-financing where an angel investor provides capital for start-up or expansion, in exchange for an ownership/equity in the company.

(b) Some of the forms of bank credit are:

(i) Cash Credit: This facility will be given by the banker to the customers by giving certain amount of credit facility on continuous basis. The borrower will not be allowed to exceed the limits sanctioned by the bank.

(ii) Bank Overdraft: It is a short-term borrowing facility made available to the companies in case of urgent need of funds. The banks will impose limits on the amount they can lend. When the borrowed funds are no longer required they can quickly and easily be repaid. The banks issue overdrafts with a right to call them in at short notice.

(iii) Bills Discounting: The Company which sells goods on credit will normally draw a bill on the buyer who will accept it and sends it to the seller of goods. The seller, in turn discounts the bill with his banker. The banker will generally earmark the discounting bill limit.

(iv) Bills Acceptance: To obtain finance under this type of arrangement a company draws a bill of exchange on bank. The bank accepts the bill thereby promising to pay out the amount of the bill at some specified future date.

(v) Line of Credit: Line of Credit is a commitment by a bank to lend a certain amount of funds on demand specifying the maximum amount.

(vi) Letter of Credit: It is an arrangement by which the issuing bank on the instructions of a customer or on its own behalf undertakes to pay or accept or negotiate or authorizes another bank to do so against stipulated documents subject to compliance with specified terms and conditions.

(vii) Bank Guarantees: Bank guarantee is one of the facilities that the commercial banks extend on behalf of their clients in favour of third parties who will be the beneficiaries of the guarantees.

(viii) Short Term Loans: In a loan account, the entire advance is disbursed at one time either in cash or by transfer to the current account of the borrower. It is a single advance and given against securities like shares, government securities, life insurance policies and fixed deposit receipts, etc.

(ix) **Clean Overdrafts**: Request for clean advances are entertained only from parties which are financially sound and reputed for their integrity. The bank has to rely upon the personal security of the borrowers.

(x) **Advances against goods:** Goods are charged to the bank either by way of pledge or by way of hypothecation. Goods include all forms of movables which are offered to the bank as security.

(xi) Usance bills maturing at a future date or sight are discounted by the banks for approved parties. The borrower is paid the present worth and the bank collects the full amount on maturity.

(xii) **Advance against documents of title to goods**: A document becomes a document of title to goods when its possession is recognised by law or business custom as possession of the goods like bill of lading, dock warehouse keeper's certificate, railway receipt, etc. An advance against the pledge of such documents is an advance against the pledge of goods themselves.

(xiii) **Advance against supply of bills**: Advances against bills for supply of goods to government or semi-government departments against firm orders after acceptance of tender fall under this category. It is this debt that is assigned to the bank by endorsement of supply bills and executing irrevocable power of attorney in favour of the banks for receiving the amount of supply bills from the Government departments.

(c) Reciprocal of the payback would be a close approximation of the Internal Rate of Return if the life of the project is at least twice the payback period and the project generates equal amount of the annual cash inflows.

The payback reciprocal is a helpful tool for quick estimation of rate of return of a project provided its life is at least twice the payback period.

It may be calculated as follows:

Payback Reciprocal = Average annual cash flows/initial Investment

Or

Payback Reciprocal = 1 / payback period

OR

(c) Crowd funding: crowdfunding means raising money for an individual or organisation from a group of people to fund a project, typically via internet (social media and crowdfunding websites). It generally involves collecting funds from family, friends, strangers, corporates and many more in exchange of equity (known as Equity funding), loans (known as P2P lending) or nothing at all (i.e. donation). This source of funding also helps start-up to substantiate demand for their product before entering into production.

In the crowdfunding process, three parties are involved i.e. fund raiser, mediator and fund investor. The platforms (mediator) may also charge certain fees in the form of processing fee, transaction fee, etc. either as a fixed amount or a percentage or in combination of both.

SECTION – B: STRATEGIC MANAGEMENT

*Question paper comprises of **4** questions, Answer Question No. **5** which is compulsory and any **2** out of the remaining **3** questions.*

Question 5

(a) *BOYA Ltd. is a venture in the market present for a decade. Till, 2023, it was working on the values and vision of its founder while operating in limited area of operations.*

Growth opportunities exist for BOYA Ltd. Considering the changing environment, company is interested to leverage new skills in marketing, technology, product development and financial management. As a known fact, modifying one aspect might have a ripple effect on other elements. The company wants to understand various hard and soft elements interrelated with each other in the company and having a bearing on effective operational results.

As a strategist, you intend to prepare a questionnaire based on both types of elements by analyzing the organizational design. The response to the same will help in finding an answer to ensure effectiveness through the interaction of such elements.

Briefly discuss the strategic model you will use in the given situation. State the limitations of the model as well. ***(2 +3 = 5 Marks)***

(b) *Elvis Global is a famous OTT platform facing fierce competition from its competitors amid changing consumer preferences. This has made it difficult to retain customers as the existing television channels are also launching their own platforms. The company has appointed Raghav to lead the company forward as the sales & marketing manager. Raghav needs to design creative and innovative advertising campaigns to gain a competitive edge, engage the public and capture the market.*

Identify the strategic level that represents Raghav's role at Elvis Global. As a strategic advisor, highlight the various benefits of strategic management in overcoming different challenges to Raghav. ***(1 +4 = 5 Marks)***

(c) *Yash is planning to launch his new tech start-up. He is exploring different locations across the country to establish his company in the right business environment. One option is the city of Bengaluru, the silicon valley of India,*

with an engaging network of entrepreneurs, investors, advisors and mentors. Coupled with various subsidies for new ventures and tax benefits, Bengaluru might be an ideal choice for Yash to establish his company and increase the chances of success.

Define the term Business Environment with respect to the above scenario. Explain the different ways in which the interaction of a business with its environment can be helpful in developing a successful strategy.

(1 +4 = 5 Marks)

Answer

(a) In addressing the strategic needs of BOYA Ltd., the **McKinsey 7S Model** is an effective tool to consider. This model focuses on the interaction of hard and soft elements within an organization, suggesting that modifying one aspect might have a ripple effect on the other elements to maintain an effective balance. The McKinsey 7S Model helps analyze the company's organizational design to achieve effectiveness through these interactions. The model categorizes the elements into 'hard' and 'soft' components:

The **Hard elements** are directly **controlled by the management.** The following elements are the hard elements in an organization.

- **Strategy:** the direction of the organization, a blueprint to build on a core competency and achieve competitive advantage to drive margins and lead the industry.
- **Structure:** depending on the availability of resources and the degree of centralisation or decentralization that the management desires, it choses from the available alternatives of organizational structures.
- **Systems:** the development of daily tasks, operations and teams to execute the goals and objectives in the most efficient and effective manner.

The **Soft elements** are difficult to define as they are more **governed by culture.** But these soft elements are equally important in determining an organization’s success as well as growth in the industry. The following are the soft elements in this model.

- **Shared Values:** The core values which get reflected within the organizational culture or influence the code of ethics of the management.
- **Style:** This depicts the leadership style and how it influences the strategic decisions of the organisation. It also revolves around people motivation and organizational delivery of goals.
- **Staff:** The talent pool of the organisation.
- **Skills:** The core competencies or the key skills of the employees play a vital role in defining the organizational success.

While the McKinsey 7S Model provides a structured approach to analysing organizational effectiveness, it has certain limitations:

- It ignores the importance of the external environment and depicts only the most crucial elements within the organization.
- The model does not clearly explain the concept of organizational effectiveness or performance.
- The model is considered to be more static and less flexible for decision making.
- It is generally criticized for missing out the real gaps in conceptualization and execution of strategy.

By applying the McKinsey 7S Model, BOYA Ltd. can gain a comprehensive understanding of how different elements within the organization interact and influence overall performance. The insights gathered from the questionnaire can guide strategic decisions to enhance growth and operational effectiveness.

(b) Raghav's role at Elvis Global represents the **Functional level** of strategy. As the sales and marketing manager, his responsibilities are focused on specific areas within the company, particularly on crafting and executing marketing and sales strategies that drive customer engagement and competitive positioning.

Benefits of Strategic Management for Raghav at Elvis Global

Strategic management can provide several benefits to Raghav in addressing the competitive and consumer challenges faced by Elvis Global:

- Strategic management helps Elvis Global define its goals and mission, providing clear **direction for future initiatives**. This ensures that all marketing efforts are aligned with the company's overall vision. It allows Raghav to **set realistic** and achievable **objectives** that support the company's **long-term goals**, ensuring that marketing strategies are both ambitious and attainable.

- Through strategic management, Raghav can **proactively shape the future** of Elvis Global rather than merely reacting to market changes. This allows the company to **anticipate trends and act accordingly**. A proactive approach enables Elvis Global to better manage environmental uncertainties and stay ahead of competitors, ensuring a more controlled and predictable business environment.

- Strategic management provides a robust **framework for making critical decisions** regarding marketing strategies, target markets, and resource allocation. This ensures that all major decisions are well-informed and strategically sound. It ensures **coherence and consistency in decision-making** across the organization, aligning marketing strategies with overall business objectives.

- Strategic management helps **identify and exploit new business opportunities**, allowing Raghav to craft **campaigns** that resonate **with** emerging **consumer preferences and market trends**. By recognizing and capitalizing on these opportunities, Elvis Global can differentiate itself from competitors and capture a larger market share.

- Strategic management **acts as a defence mechanism** against potential mistakes and pitfalls, helping Raghav avoid costly errors in marketing decisions and campaign execution. It provides a structured approach to identifying and mitigating risks, ensuring **more informed and safer decision-making.**

- Strategic management **enhances the longevity and sustainability** of Elvis Global by ensuring that marketing strategies are adaptable and

resilient in a dynamic market. It helps the company **establish a clear and deliberate position** within the industry, ensuring sustained relevance and competitiveness.

- Strategic management enables the **development of core competencies** and competitive advantages that are crucial for the company's success. This includes building strong brand identity, innovative content offerings, and superior customer service. By focusing on these strengths, Raghav can ensure that **Elvis Global achieves sustainable growth** and **maintains its competitive edge** in the OTT market.

Through strategic management, Raghav can effectively navigate the competitive challenges faced by Elvis Global. By providing clear direction, encouragement a proactive approach, guiding critical decisions, identifying new opportunities, defending against pitfalls, ensuring longevity, and developing core competencies, strategic management enables the company to achieve and sustain a competitive edge. This comprehensive approach will allow Raghav to design innovative advertising campaigns that engage the public, capture the market, and drive the company forward.

(c) Business Environment refers to all **external factors**, influences, or situations **that affect business decisions**, plans, and operations. In Yash's case, these factors include the dynamic and evolving conditions in Bengaluru, which impact the strategic decisions for his tech start-up.

Benefits of Interaction with the Business Environment

- **Determine Opportunities and Threats:** Interaction with the environment helps Yash **identify new consumer needs, emerging trends, and potential market opportunities.** This insight can guide the development of innovative products and services that meet market demands. Understanding changes in laws, social behaviors, and competitor actions enables Yash to anticipate and mitigate potential threats, ensuring the start-up remains resilient and adaptive.
- **Give Direction for Growth:** By analyzing the external environment, Yash can pinpoint areas for expansion and growth. Recognizing market trends and technological advancements allows him to **strategize effectively, ensuring the start-up scales successfully.**

Awareness of the changes around the business environment facilitates better planning and strategic decisions, aligning the start-up's goals with the market dynamics.

- **Continuous Learning:** Continuous interaction with the environment motivates Yash and his team to update their knowledge, understanding, and skills. Staying **informed about industry trends and advancements ensures the start-up remains competitive.** This ongoing learning process enhances the start-up's ability to adapt to changes, promoting innovation and responsiveness to market shifts.
- **Image Building:** Understanding and responding to environmental needs help the start-up build a positive image. For instance, adopting sustainable practices or **contributing to local initiatives can enhance the company's reputation.** Demonstrating sensitivity to the business environment shows that the start-up is responsible and community-focused, attracting customers and partners who value corporate social responsibility.
- **Meeting Competition:** Interaction with the environment allows Yash to analyze competitors' strategies and adapt accordingly. **Understanding competitors' strengths and weaknesses helps in crafting strategies that provide a competitive edge**. By leveraging insights from the environment, the start-up can position itself uniquely in the market, differentiating its offerings from those of competitors.

Question 6

(a) *'Innovation leads to unnecessary expenses that do not give as many returns.' Do you agree with the statement? Give reasons in support of your answer.* ***(1 + 4 = 5 Marks)***

(b) *Explain how organizations can effectively manage strategic uncertainties in a rapidly changing business environment.* ***(5 Marks)***

Answer

(a) The statement "Innovation leads to unnecessary expenses that do not give as many returns" is often debated, but evidence strongly suggests

that innovation is crucial for long-term business growth and success. I **disagree** with the statement for several reasons:

Innovation offers the following for a business to grow long term:

Helps to solve complex problems: A business strives to find opportunities in existing problems of the society, and it does so through planned innovation in areas of expertise. This guided innovation helps solve complex problems by developing customer centric sustainable solutions.

Increases productivity: Innovation leads to simplification and in most cases automation of existing tasks. Companies are willing to spend millions on increasing their productivity. Innovation, by automating repetitive tasks and simplifying the long chain of processes, adds to productivity of teams and thereby the organization as a whole.

Gives competitive advantage: Being ahead of competition is a need and businesses spend majority of their strategic time building solutions to achieve this advantage. The faster a business innovates, the farther it goes from its competitors reach. Innovative products need less marketing as they aim to provide added satisfaction to consumers, thus, creating a competitive advantage. Innovation not only helps retain its existing customers but helps acquire new ones with ease too.

(b) In managing strategic uncertainties in a rapidly changing business environment, organizations need to adopt proactive strategies to navigate unpredictability effectively. Here are several key approaches:

Flexibility: Organizations should build flexibility into their strategies to enable quick adaptation to change in the environment.

Diversification: Diversifying the organization's product portfolio, markets, and customer base can help reduce the impact of strategic uncertainty.

Monitoring and Scenario Planning: Regularly monitoring key indicators of change and conducting scenario planning exercises can help organizations anticipate and prepare for different future scenarios.

Building Resilience: Investing in building internal resilience is essential for weathering uncertainty. This includes strengthening operational

processes, increasing financial flexibility, and improving risk management capabilities.

Collaboration and Partnerships: Collaborating with other organizations, suppliers, customers, and partners can provide access to additional resources, expertise, and market opportunities. Strategic partnerships enable organizations to pool resources, share risk, and leverage each other's strengths to navigate uncertainty more effectively.

Question 7

(a) What are the key characteristics of business products that contribute to the overall competitiveness and dynamics of the market? ***(5 Marks)***

(b) 'A company's mission statement is typically focused on its present business scope.' Explain the significance of a mission statement. ***(5 Marks)***

Answer

(a) Businesses sell products. A product can be either a good or a service. It might be physical good or a service, an experience.

Following are the key characteristics of business products:

1. **Products are either tangible or intangible.** A tangible product can be handled, seen, and physically felt, such as a car, book, pen, table, mobile handset and so on. Alternatively, an intangible product is not a physical good, such as telecom services, banking, insurance, or repair services.

2. **Product has a price**. Businesses determine the cost of their products and charge a price for them. The dynamics of supply and demand influence the market price of an item or service. The market price is the price at which quantity provided equals quantity desired. The price that may be paid is determined by the market, the quality, the marketing, and the targeted group. In the present competitive world price is often given by the market and businesses have to work on costs to maintain profitability.

3. **Products have certain features that deliver satisfaction**. A product feature is a component of a product that satisfies a consumer need. Features determine product pricing, and businesses alter features

during the development process to optimize the user experience. Products should be able to provide value satisfaction to the customers for whom they are meant. Features of the product will distinguish it in terms of its function, design, quality and experience A customer's cumulative experience with a product from its purchase to the end of its useful life is an important component of a product feature.

4. **Product is pivotal for business**. The product is at the centre of business around which all strategic activities revolve. The product enables production, quality, sales, marketing, logistics and other business processes. Product is the driving force behind business activities.

5. **A product has a useful life**. Every product has a usable life after which it must be replaced, as well as a life cycle after which it is to be reinvented or may cease to exist. We have observed that fixed line telephone instruments have largely been replaced by mobile phones.

(b) A company's mission statement is typically focused on its present business scope **who we are and what we do**. Mission statements broadly describe an organization's present capability, customer focus, activities, and business make up. Mission for an organization is significant for the following reasons:

- It ensures **unanimity of purpose** within the organization.
- It develops a basis, or standard, for **allocating organizational resources.**
- It provides a basis for **innovating the use of the organisation's resources**
- It **establishes** a general tone or **organizational climate**, to suggest a business like operation.
- It serves as a **focal point** for those who can identify with the **organisation's purpose and direction**.
- It facilitates the **translation of objectives and goals into a work structure** involving the assignment of tasks to responsible elements within the organization.

- It specifies organizational purposes and the **translation of these purposes into goals** in such a way that cost, time, and performance parameters can be assessed and controlled.

Question 8

(a) *What are channels? Why is channel analysis important? Explain the different types of channels?* ***(1 + 1 + 3 = 5 Marks)***

(b) *Explain the concept of vertically integrated diversification. How is forward integration different from backward integration?* ***(5 Marks)***

OR

(b) *Recommend a tool to analyze the competitive position of various rival companies in the market and outline the step by step procedure for using the identified tool.* ***(5 Marks)***

Answer

(a) Channels represent the **distribution system** through which organizations distribute their products or provide services to customers. They play a pivotal role in reaching target markets, maximizing sales, and establishing competitive advantages.

Channel analysis is important when the business strategy is to scale up and expand beyond the current geographies and markets. When a business plans to grow to newer markets, they need to develop or leverage existing channels to get to new customers. Thus, analysis of channels that suit one's products and customers is of utmost importance.

There are typically three channels that should be considered: sales channel, product channel and service channel.

- **The sales channel** - These are the intermediaries involved in selling the product through each channel and ultimately to the end user. The key question is: Who needs to sell to whom for your product to be sold to your end user? **For example**, many fashion designers use agencies to sell their products to retail organizations, so that consumers can access them.
- **The product channel** - The product channel focuses on the series of intermediaries who physically handle the product on its path from its

producer to the end user. This is true of Australia Post, who delivers and distributes many online purchases between the seller and purchaser when using eBay and other online stores.

- **The service channel** - The service channel refers to the entities that provide necessary services to support the product, as it moves through the sales channel and after purchase by the end user. The service channel is an important consideration for products that are complex in terms of installation or customer assistance. **For example**, a Bosch dishwasher may be sold in a Bosch showroom, and then once sold it is installed by a Bosch contracted plumber.

(b) Vertically integrated diversification is a strategic approach in which a company expands its business operations into different stages of the production or distribution process within the same industry. This involves either forward integration or backward integration.

The key difference between forward and backward integration lies in the direction of expansion within the supply chain. **Forward integration moves towards the end consumer,** while **backward integration moves towards the source of raw materials or components.**

Forward integration allows companies to have **more control over distribution channels,** improve customer relationships, and capture a larger share of the value chain. In contrast, **backward integration helps** companies **secure a stable supply of inputs,** reduce dependency on suppliers, and potentially lower production costs.

Forward integration is often associated with activities such as retailing, marketing, and after-sales services, while backward integration is associated with activities such as manufacturing, sourcing, and procurement.

Both types of integration offer strategic advantages such as increased market power, cost efficiencies, and greater control over critical business processes. However, the decision to pursue forward or backward integration depends on factors such as industry dynamics, competitive landscape, and the company's core competencies and resources.

Or

A tool to identify the market positions of rival companies by grouping them into like positions is **Strategic Group Mapping.** A strategic group consists of those rival firms which have similar competitive approaches and positions in the market.

The procedure for constructing a strategic group map and deciding which firms belong in which strategic group are as follows:

1. Identify the competitive characteristics that differentiate firms in the industry typical variables that are price/quality range (high, medium, low); geographic coverage (local, regional, national, global); degree of vertical integration (none, partial, full); product-line breadth (wide, narrow); use of distribution channels (one, some, all); and degree of service offered (no-frills, limited, full).
2. Plot the firms on a two-variable map using pairs of these differentiating characteristics.
3. Assign firms that fall in about the same strategy space to the same strategic group.
4. Draw circles around each strategic group making the circles proportional to the size of the group's respective share of total industry sales revenues.

PAPER – 6: FINANCIAL MANAGEMENT AND STRATEGIC MANAGEMENT

SECTION A: FINANCIAL MANAGEMENT

PART - I

Case Scenario 1

RS Limited is manufacturing selling soft drinks in India. The production process involves one important process which increases the shelf life of the soft drinks. Presently, the machine used for this purpose is an old one, in which wastage due to breakage of glass bottles is considerably high and due to its limited capacity, the company is not in a position to increase its production.

The production manager has approached the CEO of RS Limited for purchasing an automated machine, which will drastically reduce the wastage due to breakage during the process of increasing shelf life of soft drinks. The automated machine will support increase in production. The production manager is confident that acquisition of the automated machine will be beneficial for the company.

Other information is as under :

- *With the introduction of automated machine, additional sales and related costs over the next five years would be as follows:*

Year	Additional Sales Unit	Selling price per unit (₹)	Variable Manufacturing, Selling and Distribution cost per unit (₹)	Additional fixed Selling & Distribution Cost (₹)
1	20,000	30	20	25,000
2	25,000	30	20	30,000
3	30,000	35	20	30,000
4	32,000	35	22	35,000
5	28,000	35	22	35,000

- *Cost of acquisition of automated machine is ₹ 5,00,000. Residual value of the automated machine at the end of its life of 5 years will be ₹ 50,000. Depreciation on automated machine will be under Straight line method.*

  Depreciation is not included in the cost stated above.

- *The Production Manager has estimated the cost savings (before tax) due to reduction in breakages as under:*

	Year 1	Year 2	Year 3	Year 4	Year 5
Savings Cost due reduction in breakages	₹ 15,000	₹ 15,000	₹ 20,000	₹ 20,000	₹ 20,000

- *The machine which is being used at present has zero written down value and if sold, would fetch an amount of ₹ 10,000 only.*

- *The cost of capital of the company is 10%. The tax rate applicable for the company is 30%. Ignore capital gain taxes.*

  P.V Factors of ₹ 1 at year end at 10%:

	Year 1	**Year 2**	**Year 3**	**Year 4**	**Year 5**
P.V Factor of ₹ 1	0.909	0.826	0.751	0.683	0.621

You are required to answer the following Questions 1 to 5 :

1. *What is the Profit before Taxes for the Year 2, Year 3 and Year 4 of the investment proposal ?*

   (A) ₹ 2,35,000, ₹ 4,40,000, ₹ 4,01,000

   (B) ₹ 1,45,000, ₹ 3,50,000, ₹ 3,11,000

   (C) ₹ 2,05,000, ₹ 4,10,000, ₹ 3,66,000

   (D) ₹ 1,40,000, ₹ 3,60,000, ₹ 3,31,000

2. *What is the Cash Inflow after Taxes for the Year 1, Year 2 and Year 3 of the investment proposal ?*

   (A) ₹ 1,50,000, ₹ 1,85,000, ₹ 3,45,000

   (B) ₹1,65,000, ₹ 1,95,500, ₹ 3,55,000

   (C) ₹ 1,60,000, ₹ 1,91,500, ₹ 3,35,000

(D) ₹ 1,70,000, ₹ 1,90,000, ₹ 3,40,000

3. *What is the Discounted Cash Inflow after Taxes for the Year 1, Year 2 and Year 3 of the investment proposal ?*

   (A) ₹ 1,49,985, ₹ 1,61,483, ₹ 2,66,605

   (B) ₹ 1,36,350, ₹ 1,52,810, ₹ 2,59,095

   (C) ₹ 1,54,530, ₹ 1,56,940, ₹ 2,55,340

   (D) ₹ 1,45,440, ₹ 1,58,179, ₹ 2,51,585

4. *What is the Net Present Value of the investment proposal?*

   (A) ₹ 3,78,990.30

   (B) ₹ 4,54,980.60

   (C) ₹ 4,74,890.40

   (D) ₹ 3,89,260.70

5. *What is the Discounted Payback period of the investment proposal ?*

   (A) 2.74 years

   (B) 2.87 years

   (C) 2.38 years

   (D) 2.48 years

6. *A company has sales of ₹ 6,00,000, variable cost of ₹ 2,40,000, fixed operating cost of ₹ 2,70,000. The financial leverage is 2.5. The company wants to double its EBIT. The percentage change in ales required in order to double its EBIT will be :*

   (A) 50%

   (B) 25%

   (C) 40%

   (D) 80%

7. *The capital structure of KPS Limited includes 5,00,000 equity shares of ₹ 10 each. The market price of equity share (cum-dividend) is ₹ 75 per share. The company has declared to pay dividend on equity shares @ ₹ 6 per share*

which will be paid within next three days. The company has a history of consistent growth in its dividends. It has been predicted that in the next year KPS Limited will pay dividend on its equity shares@ ₹ 7.59 per share. The rate of dividend growth will be maintained in foreseeable future. The cost of equity is calculated as:

(A) 36.5%

(B) 34.5%

(C) 37.5%

(D) 38.5%

8. *ZX Limited has total assets of ₹ 7,20,000 and its Shareholders' equity is ₹ 4,50,000. The net profit margin of ZX Limited is 12.5% and asset turnover ratio is 1.5. Using the DuPont model, the return on equity of ZX Limited is calculated as :*

(A) 7.03%

(B) 50%

(C) 11.72%

(D) 30%

Answer Key

Question No.	Answer
1.	(B)
2.	(C)
3.	(D)
4.	(C)
5.	(A)
6.	(B)
7.	(C)
8.	(D)

SECTION – B: STRATEGIC MANAGEMENT

PART - I

Case Scenario 2

Quick N Safe Logistics is one of the prominent transporters of goods for more than two decades. It has its own fleets and also has business arrangement with Railways.

Competition with existing players and threat from new entrants are increasing regularly. Customer preferences and expectations are also changing. Need for considering new and improved means of transportation seems inevitable.

Current philosophy of the company is 'to bring the best user experience to its customers through timely and safe delivery of goods'. While keeping this philosophy in mind, it desires to keep ahead and reap the benefits of first mover advantages in the industry. In order to achieve its growth target, company is exploring available other options so as to have a strong presence in supply chain management.

The company is of a considered view that 'we learn as we grow'. It knows that the overall per mile operating cost decreases due to increase in efficiency and cumulative volume of services. Since the company will have a cost advantage over the competitors due to reduced cost of services, it can develop and adopt a penetrative pricing strategy by setting a low price to attract more customers.

It is also observed that arrangement of transportation through railways is becoming a concern. Growth rate is slow and market for areas being covered by this means of transport is by and large stabilized. Profit margin is coming down due to stiff competition. Company has to work out an action plan to maintain the stability.

On the other side, one of the customer segments is looking for fast delivery of its goods in major cities all across the country. The prime consideration of such customers is quick and safe delivery of their products, irrespective of cost for the same. The target market of such services is very large and also increasing very fast. In view of the same, the company wants to reform its operation, by engaging a dedicated team to perform with a niche marketing strategy for transporting such goods through airways on an assurance of 'delivery by next day'.

In view of the given case scenario, answer MCQs from 9 to 13 with correct option.

9. *The strategy in which the company wants to keep ahead and reap the first mover advantages in the industry, is known as:*

   (A) Adaptive strategy

   (B) Reactive strategy

   (C) Proactive strategy

   (D) Responsive strategy

10. *In context to service in transportation through railways, the company is analyzing a relationship between volume of business on one axis with respect to time on another axis. As per Product Life Cycle (PLC), which stage this service is passing through:*

    (A) Introduction

    (B) Maturity

    (C) Growth

    (D) Decline

11. *In Strategic Management, the concept of decrease in the overall per mile operating cost due to increase in efficiency and cumulative volume of services is depicted as:*

    (A) Experience curve

    (B) Ansoff's growth matrix

    (C) Strategic surveillance

    (D) Value chain analysis

12. *As per strategies propagated by Michael Porter, niche marketing strategy for transporting goods through airways for a large customer segment on an assurance of 'delivery by next day', is known as:*

    (A) Cost leadership strategy

    (B) Differentiation strategy

    (C) Focus differentiation strategy

(D) *Focus cost leadership strategy*

13. *The philosophy of the company stated as, 'to bring the best user experience to its customers through timely and safe delivery of goods', is indicating towards:*

(A) *Vision statement*

(B) *Mission statement*

(C) *Goals of the company*

(D) *Objectives of the company*

14. *Super Products Ltd. is having four divisions, i.e. Alpha, Beta, Cos and Theta. All the divisions are independent product center and are also integral part of product Gama of the company. Each division contains its own set of activities under the control of respective general manager. Each general manager is responsible for his respective product line and its profitability. While having own set of competitors, each center has its own competitive advantages with the resources and capabilities they develop. Such structure is known as:*

(A) *Network structure*

(B) *Divisional structure*

(C) *Multi divisional structure*

(D) *Strategic business unit*

15. *Always Ahead Ltd. is an established player in FMCG, Herbs, Health care and White goods. Company has classified its portfolio on investments in different businesses in four quadrants as suggested by Boston Consulting Group. On further analysis of relationship between market growth rate and relative market share for White goods business, it is found that opportunities to increase its market share are there. Emphasis need to be given to make a strong future with large market share even by foregoing short-term earnings for this business. Which strategy is being pursued by the company for White goods segment:*

(A) *Build*

(B) *Hold*

(C) *Harvest*

(D) Divest

16. *The correct sequence of the stages as per Kurt Lewin's model of change is:*

(A) Changing to the new situation, Unfreezing the situation and Refreezing

(B) Unfreezing the situation, Refreezing and Changing to the new situation

(C) Refreezing, Unfreezing the situation and Changing to the new situation

(D) Unfreezing the situation, Changing to the new situation and Refreezing

Answer Key

Question No.	Answer
9.	**(C)**
10.	**(B)**
11.	**(A)**
12.	**(C)**
13.	**(B)**
14.	**(D)**
15.	**(A)**
16.	**(D)**

PAPER – 6: FINANCIAL MANAGEMENT AND STRATEGIC MANAGEMENT

SECTION A: FINANCIAL MANAGEMENT

Part II

*Question No. **1** is compulsory.*

*Attempt any **two** questions out of the remaining **three** questions.*

In case, any candidate answers extra question(s)/ sub-question(s) over and above the required number, then only the requisite number of questions first answered in the answer book shall be valued and subsequent extra question(s) answered shall be ignored.

Working notes should form part of the answer.

Question 1

(a) Financial information for the year 2023-24 of two companies, N Limited and C Limited are as under:

Details	*N Limited*	*C Limited*
Equity share capital (₹ 100 each)	*₹ 10,00,000*	*₹ 8,00,000*
Debt	*₹ 5,00,000@10%*	*₹ 7,00,000@8%*
Fixed Cost	*3,00,000*	*3,36,000*
Combined Leverage	*8*	*4.5*
Financial Leverage	*2*	*1.5*

You are required to calculate:

(i) Contribution for N Ltd. and C Ltd.

(ii) Margin of safety in % for N Ltd. and C. Ltd.

(iii) Sales of C Ltd. ***(5 Marks)***

(b) *The following information is available for SK Limited for the year ended on 31st March,2024:*

Particulars	₹
Cost of production	15,48,000
Cost of goods sold	14,61,000
Average stock of work-in-progress	94,600
Average stock of finished goods	2,43,500
Administration and Selling expenses	4,14,000
Receivables collection period	36 days
Raw Material Storage period	65 days
Creditors payment period	63 days

You are required to calculate the working capital requirement by operating cycle method. Assume a 360 days year. ***(5 Marks)***

(c) *Following information relates to MNP Limited for the year ended on 31sMarch, 2024:*

Inventory turnover ratio (based on cost of goods sold)	7.5 times
Total assets turnover ratio	2.5 times
Long term debt to Shareholders' fund	0.6:1
Debtors collection period	30 days
Gross profit ratio	25% on sales
Current Ratio	2.9:1

Balance Sheet as on 31st March,2024

Liabilities	₹	Assets	₹
Equity share capital	6,00,000	Fixed Assets	?
Reserves & Surplus	3,00,000	Inventories	?
Long term debt	?	Debtors	?
Creditors	3,00,000	Cash	?
Total		Total	

You are required to complete the Balance Sheet of MNP Limited as on 31st March,2024. Assume a 360 days year and all sales are credit sales.

(5 Marks)

Answer

(a) (i) Calculation of Contribution

N Limited	C Limited
Financial Leverage (FL) $= \frac{EBIT}{EBT}$ or $\frac{EBIT}{EBIT - Interest}$	
$2 = \frac{EBIT}{EBIT - 50{,}000}$	$1.5 = \frac{EBIT}{EBIT - 56{,}000}$
2 EBIT – 1,00,000 = EBIT	1.5 EBIT – 84,000 = EBIT
EBIT = ₹ 1,00,000	**EBIT = ₹ 1,68,000**
EBT = ₹ 50,000	EBT = ₹ 1,12,000
Combined Leverage (CL) $= \frac{Contribution}{EBT}$	
8 = Contribution / 50,000	4.5 = Contribution / 1,12,000
Contribution= ₹ 4,00,000	**Contribution= ₹ 5,04,000**

(ii) Calculation of Margin of safety (MOS) in %

$$MOS = \frac{\text{Contribution - Fixed Cost}}{\text{Contribution}} = \frac{EBIT}{\text{Contribution}}$$

N Limited	C Limited
MOS = 1,00,000/4,00,000 **= 25%**	MOS = 1,68,000/5,04,000 **= 33.33%**

Part (ii) can also be presented in following way:

Calculation of Margin of safety (MOS) in %

MOS = 1/operating leverage (OL)

OL = CL/FL

N Limited	C Limited
OL = 8/2 = 4	OL = 4.5/1.5 = 3
MOS = 1/4 **= 25%**	MOS = 1/3 **= 33.33%**

(iii) Sales of C Limited

Let assume that PV ratio is 40%

$$\textbf{PV Ratio} = \frac{\text{Contribution}}{\text{Sales}} \text{ OR Sales} = \frac{\text{Contribution}}{\text{PV Ratio}}$$

$$\textbf{Sales} = \frac{5,04,000}{0.40} = \textbf{₹ 12,60,000}$$

Part (iii) of the solution can be solved by any alternative assumption.

(b) Operating Cycle = R + W + F + D – C

Where,

R = Raw material storage period = 65 days

W = Work-in-progress inventory* holding period

F = Finished goods storage period

D = Receivables (Debtors) collection period = 36 days

C = Credit period allowed by suppliers (Creditors) = 63 days

Work-in-progress inventory holding period (W)

$$= \frac{\text{Average Work-in-progress inventory}}{\text{Average Cost of Production per day}}$$

$$= \frac{₹\ 94,600}{₹\ 15,48,000 \div 360 \text{ days}} = \textbf{22 days}$$

Finished Goods storage period (F)

$$= \frac{\text{Average stock of finished goods}}{\text{Average Cost of Goods Sold per day}}$$

$$= \frac{₹2,43,500}{₹14,61,000 \div 360 \text{ days}} = \textbf{60 days}$$

Net Operating Cycle = 65+22+60+36-63 = **120 days**

Number of Operating Cycles in a year

$$= \frac{\text{No. of days in a year}}{\text{Operating Cycle period}}$$

$$= \frac{360\text{ days}}{120\text{ days}} = \textbf{3 times}$$

Amount of Working Capital Required

$$= \frac{\text{Annual Operating Cost}}{\text{Number of Operating Cycles}} = \frac{₹\,14,61,000 + ₹\,4,14,000}{3} = ₹\ 6,25,000$$

(c) Working Notes:

Long term debt to Shareholder's fund = 0.6:1

Long term debt = 0.6 x ₹ 9,00,000 = ₹ 5,40,000

Total Assets = ₹ 17,40,000

Total Asset turnover ratio $= \frac{\text{Sales}}{\text{Total Assets}}$ = 2.5 times

Sales = 2.5 x ₹ 17,40,000 = ₹ 43,50,000

Current ratio $= \frac{\text{Current Assets}}{\text{Current Liabilities}}$ = 2.9:1

Current Assets = 2.9 x ₹ 3,00,000 = ₹ 8,70,000

Fixed Assets = Total Assets - Current Assets

= ₹ 17,40,000 – ₹ 8,70,000 = ₹ 8,70,000

Gross profit ratio = 25% on sales

Gross Profit (GP) = ₹ 43,50,000 x 0.25 = ₹ 10,87,500

Cost of Good Sold (COGS) = Sales – GP

= ₹ 43,50,000 - ₹ 10,87,500

= ₹ 32,62,500

Inventory Turnover Ratio $= \frac{\text{Cost of Goods Sold}}{\text{Average Inventory}}$ = 7.5 times

Inventory = ₹ 32,62,500/7.5 = ₹ 4,35,000

Debtor Collection Period $= \frac{\text{Average Accounts Receivables}}{\text{Average Daily Credit Sales}}$ = 30 days

Receivables = 30 days x ₹ 43,50,000/360 days = ₹ 3,62,500

Balance Sheet as on 31st March 2024

Liabilities	(₹)	Assets	(₹)
Share Capital	6,00,000	Fixed Assets	8,70,000
Reserve and Surplus	3,00,000	Inventories	4,35,000
Long-term loan	5,40,000	Debtors	3,62,500
Creditors	3,00,000	Cash (Balancing Figure)	**72,500**
	17,40,000		17,40,000

Question 2

(a) *Capital structure of T Limited as on 1st April,2024 is as under:*

	₹
Equity Share Capital (₹ 10 per share)	*50,00,000*
10% Debentures (₹ 100 per Debenture)	*40,00,000*
12% Preference Share Capital (10,000 shares of ₹ 100 each)	*10,00,000*

Additional Information:

(1) *The risk free rate of return is 10%. The Beta of T Ltd. is 1.75 and the return on market portfolio is 12%. The Equity shares have a current market price of ₹ 70 per share.*

(2) *The debentures are trading at a market price of ₹ 80 per debenture. The Debentures are to be redeemed after 5 years at par.*

(3) *Preference shares are redeemable after 5 years at a premium of 5%, presently selling at ₹ 104 per share.*

(4) *The Company pays tax at a rate of 30%.*

(5) *The Cost of Debentures are to be calculated on Yield to Maturity approach.*

(6) The present value factors at 10% and 14% are:

Year	***1***	***2***	***3***	***4***	***5***
$\boldsymbol{PVIF_{0.10,t}}$	*0.909*	*0.826*	*0.751*	*0.683*	*0.621*
$\boldsymbol{PVIF_{0.14,t}}$	*0.877*	*0.769*	*0.675*	*0.592*	*0.519*

You are required to calculate Weighted Average Cost of Capital (after tax) of T Limited using Market value weights. ***(8 Marks)***

(b) Explain Angel Financing. ***(2 Marks)***

Answer

(a) Cost of Equity Share Capital using Capital Asset Pricing Model (CAPM) Approach

$K_e = R_f + ß (R_m - R_f)$

$K_e = 0.10 + 1.75 (0.12 – 0.10)$

$= 0.10 + 1.75 (0.02) = 0.135$ or **13.5%**

Cost of Redeemable Debentures using Yield to Maturity (YTM) Approach

Step-1: Identification of relevant cash flows

Year	Cash flows
0	Current market price (P_0) = ₹ 80
1 to 5	Interest net of tax [I(1-t)] = 10% of ₹ 100 (1-0.30) = ₹ 7
5	Redemption value (RV) = Face value i.e. ₹ 100

Step- 2: Calculation of NPVs at two discount rates

Year	**Cash flows (₹)**	**Discount factor @ 10% (L)**	**Present Value (₹)**	**Discount factor @ 14% (H)**	**Present Value (₹)**
0	80	1.000	(80.000)	1.000	(80.000)
1 to 5	7	3.790	26.530	3.432	24.024
5	100	0.621	62.100	0.519	51.900
NPV			**+8.630**		**-4.076**

Step- 3: Calculation of Cost of Debentures (Kd)

$$Kd = L + \frac{NPVL}{NPVL\text{-}NPVH}(H\text{-}L) = 10\% + \frac{₹\ 8.630}{₹\ 8.630 - (₹\text{-}4.076)}(14\%\text{-}10\%) = \mathbf{12.72\%}$$

Cost of Redeemable Preference Share Capital using approximation method

$$K_p = \frac{PD + \frac{(RV\text{-}NP)}{n}}{\frac{(RV+NP)}{2}}$$

$$K_p = \frac{12 + \left(\frac{105 - 104}{5}\right)}{\left(\frac{105 + 104}{2}\right)}$$

$$= \mathbf{11.67\%}$$

Calculation of WACC using market value weights

Source of Capital	Market Value	Weights	After tax cost of capital	WACC (K_o)
	(₹)	(a)	(b)	(c) = (a)×(b)
Equity Share Capital (₹ 70 x 5,00,000 equity shares)	3,50,00,000	0.8919	0.1350	**0.1204**
10% Debentures (₹ 80 × 40,000)	32,00,000	0.0816	0.1272	**0.0104**
12% Preference Share Capital (₹ 104 × 10,000 shares)	10,40,000	0.0265	0.1167	**0.0031**
	3,92,40,000	1.000		**0.1339**

WACC (K_o) = 0.1339 or 13.39%

(b) Angel Financing is a form of an equity-financing in which individual or a group of individuals provides capital to entrepreneurs and early-stage businesses, or start-ups, in exchange for an ownership/equity in the company.

They may provide a one-time investment or an ongoing capital injection via a series of investments, Angel investors are looking for a higher rate of return than what is given by traditional investment

Question 3

(a) *AB Enterprises deals in hardware materials having current turnover ₹ 30 Lakhs per annum. All sales are on credit and average collection period is 30 days with zero bad debts. The customers are requesting to increase the credit period. As a result of increase in credit period sales will also increase. Other information is as under:*

Credit policy	***Increase in collection period (days)***	***Increase in sales (₹)***	***Bad debts anticipated***
A	*15*	*3,00,000*	*1%*
B	*30*	*5,00,000*	*3.5%*

The Selling price is ₹ 100/- per unit. Variable cost per unit is ₹ 50/- and fixed cost is ₹ 5,00,000. Required rate of return on additional investment is 20%. Creditors for variable cost are ready to give 15 days extra credit for the additional cost incurred. Assume a 360 days year.

You are required to analyse the present and proposed credit policies using the "Total Approach" method and recommend the credit policy to be adopted.

(5 Marks)

(b) *ER Private Limited has a paid-up capital ₹ 2,50,000 consisting of 25,000 Equity shares of ₹ 10 each. The Market price per share is ₹ 24 with PE ratio of 8. The company is planning to purchase a plant which will cost ₹ 5,00,000. This plant is expected to yield earnings before interest and taxes of ₹ 2,00,000 per annum. It has two alternatives to finance the plant:*

Alternatives	*Equity*	*Debt*
A	*100%*	*-*
B	*50%*	*50%*

Other information is as under:

(i) Cost of debt is 12%.

(ii) Equity shares of face value of ₹ 10 each will be issued at a premium of ₹ 10 per share.

(iii) PE ratio of Leveraged company will be 7.

(iv) Tax rate -40%.

Advise which alternative is the most suitable to raise the funds for additional capital, keeping in mind to maximize the benefit to its Shareholders.

(5 Marks)

Answer

(a) A. Statement showing the Evaluation of Credit Policies (Total Approach)

	Particulars	**Present Credit Policy**	**Proposed Credit Policy**	
			A	**B**
	Credit Period (in days)	30	45	60
	Units sold	30,000	33,000	35,000
		₹	₹	₹
A	**Expected Profit:**			
	(a) Credit Sales @ ₹ 100 per unit	30,00,000	33,00,000	35,00,000
	(b) Total Cost other than Bad Debts			
	(i) Variable Costs @ ₹ 50 per unit	15,00,000	16,50,000	17,50,000
	(ii) Fixed Costs	5,00,000	5,00,000	5,00,000
		20,00,000	21,50,000	22,50,000
	(c) Bad Debts	-	33,000	1,22,500
	(d) Expected Profit [(a) – (b) – (c)]	**10,00,000**	**11,17,000**	**11,27,500**

B	**Opportunity Cost of Investments in Receivables (i)-(ii)**	**33,333**	**52,500**	**72,917**
C	**Net Benefits (A – B)**	**9,66,667**	**10,64,500**	**10,54,583**

Recommendation: The Proposed Policy A (i.e. increase in collection period by 15 days or total 45 days) should be adopted since the net benefits under this policy are higher as compared to other policies.

Working Notes:

(i) Calculation of Opportunity Cost of Average Investment in Receivables

	Particulars	**Present Credit Policy**	**Proposed Credit Policy**	
			A	**B**
	Credit Period (in days)	30	45	60
		₹	₹	₹
(a)	Cost of Sales (Variable Cost + Fixed Cost)	20,00,000	21,50,000	22,50,000
(b)	Average Debtors = Cost of Sales × (Credit period) / 360	1,66,667	2,68,750	3,75,000
(c)	Average Creditors for extra variable cost [(Variable Cost) x 15/360]	-	6,250	10,417
(d)	**Average Investment in Receivables or Net Working Capital = (b) – (c)**	1,66,667	2,62,500	3,64,583
(e)	**Opportunity Cost @20% of average Investments in Receivables**	33,333	52,500	72,917

(b) Calculation of No. of Equity Shares and Existing Earnings before Interest and Taxes

Particulars	**Existing**	**Alternative A: Issue Equity shares only**	**Alternative B: Issue Equity Shares and 12% Debentures of equal amount**
Number of Equity Shares			
- Existing	25,000	25,000	25,000
- Newly issued		25,000 $\left(\frac{₹\ 5,00,000}{₹\ (10+10)}\right)$	12,500 $\left(\frac{₹\ 2,50,000}{₹(10+10)}\right)$
Total no. of Equity Shares	25,000	50,000	37,500
Calculation of Existing Earnings before Interest and Taxes (EBIT)			
Market Price per share (MPS)	₹ 24		
Price-Earnings Ratio (PE Ratio)	8 times	8 times	7 times
Earning per share (EPS) = MPS/PE Ratio	3		
Earnings after Tax (EAT) = EPS x No. of Equity shares	**75,000**		
Earning before Tax (EBT) = EAT/0.6 (or EBIT as Interest nil)	1,25,000		

Calculation of EPS and MPS under two financial alternatives

Particulars	Existing	Alternative A	Alternative B
Earnings before Interest and Tax: - Existing EBIT - From New Project	1,25,000	1,25,000 2,00,000	1,25,000 2,00,000
	1,25,000	3,25,000	3,25,000
Less: Interest on 12% Debentures	-	-	30,000
Earnings before Tax (EBT)	1,25,000	3,25,000	2,95,000
Less: Tax @ 40%	50,000	1,30,000	1,18,000
Earnings after Tax (EAT)	**75,000**	**1,95,000**	**1,77,000**
EPS = EAT/ No. of Equity Shares	**3.00**	**3.90**	**4.72**
Market Price per share (MPS) = EPS x Price-Earning Ratio	**24.00**	**31.20**	**33.04**

Advise: Alternative B i.e., issue of 12% Debentures is most suitable to maximize the market price per share.

Alternatively, Solution can also be presented in following way:

Calculation of EPS and MPS under two financial alternatives

Particulars	Existing	Alternative A	Alternative B
Earnings before Interest and Tax:		2,00,000	2,00,000
- From New Project		2,00,000	2,00,000
Less: Interest on 12% Debentures	-	-	30,000
Earnings before Tax (EBT)		2,00,000	1,70,000
Less: Tax @ 40%		80,000	68,000
Earnings after Tax (EAT) from new project		1,20,000	1,02,000

Earnings from Existing (PAT)	75,000	75,000	75,000
Total Earnings After Tax (EAT)	75,000	1,95,000	1,77,000
Number of Shares	25,000	50,000	37,500
EPS = EAT/ No. of Equity Shares	**3.00**	**3.90**	**4.72**
Market Price per share (MPS) = EPS x Price-Earning Ratio	**24.00**	**31.20**	**33.04**

Advise: Alternative B i.e., issue of 12% Debentures is most suitable to maximize the market price per share.

Question 4

Answer the following:

(a) *Discuss any 2 advantages and 2 disadvantages of raising finance by issue of debentures.* ***(4 Marks)***

(b) *List any four assumptions of Gorden's Model.* ***(4 Marks)***

(c) *What is Leveraged Lease? Explain.* ***(2 Marks)***

OR

(d) *What are the remedies for over-capitalisation?* ***(2 Marks)***

Answer

(a) Advantages of raising finance by issue of debentures are:

(i) The cost of debentures is much lower than the cost of preference or equity capital as the interest is tax-deductible. Also, investors consider debenture investment safer than equity or preferred investment and, hence, may require a lower return on debenture investment.

(ii) Debenture financing does not result in dilution of control.

(iii) In a period of rising prices, debenture issue is advantageous. The fixed monetary outgo decreases in real terms as the price level increases. In other words, the company has to pay a fixed rate of interest.

Disadvantages of debenture financing are:

(i) Debenture interest and the repayment of its principal amount is an obligatory payment.

(ii) The protective covenants associated with a debenture issue may be restrictive.

(iii) Debenture financing enhances the financial risk associated with the firm because of the reasons given in point (i).

(i) Since debentures need to be paid at the time of maturity, a large amount of cash outflow is needed at that time.

(b) Gordon's model is based on the following assumptions:

- Firm is an all equity firm i.e. no debt.
- IRR will remain constant, because change in IRR will change the growth rate and consequently the value will be affected. Hence this assumption is necessary.
- K_e will remain constant, because change in discount rate will affect the present value.
- Retention ratio (b), once decide upon, is constant i.e. constant dividend payout ratio will be followed.
- Growth rate (g = br) is also constant, since retention ratio and IRR will remain unchanged and growth, which is the function of these two variable will remain unaffected.
- $K_e > g$, this assumption is necessary and based on the principles of series of sum of geometric progression for 'n' number of years.
- All investment proposals of the firm are to be financed through retained earnings only.

(c) **Leveraged Lease:** Under this lease, a third party is involved besides lessor and the lessee. The lessor borrows a part of the purchase cost (say 80%) of the asset from the third party i.e., lender and asset so purchased is held as security against the loan. The lender is paid off from the lease rentals directly by the lessee and the surplus after meeting the claims of the lender goes to the lessor. The lessor is entitled to claim depreciation allowance.

OR

(c) Following steps may be adopted to avoid the negative consequences of over-capitalisation:

(i) Company should go for thorough reorganization.

(ii) Buyback of shares.

(iii) Reduction in claims of debenture-holders and creditors.

(iv) Value of shares may also be reduced. This will result in sufficient funds for the company to carry out replacement of assets.

SECTION – B: STRATEGIC MANAGEMENT

Part II

*Question paper comprises of **4** questions, Answer Question No. **5** which is compulsory and any **2** out of the remaining **3** questions.*

Question 5

(a) *M/s. MTS Ltd, is one of the mobile telephone service providers in India. It has its own mobile network, towers and distribution channels. It operates through its team of network operation, technicians, marketing, sales and after sales services. Currently all the team members are on its roll.*

Company knows that market is densely competitive. The environment is quite unstable and likely to remain so. Customer's taste and preferences are changing very fast. There is a strong need for innovation and quick response. While eliminating in-house business functions, company is considering outsourcing major activities and focusing on its core competencies.

In the given situation identify the organizational structure suitable for the company. Also outline the merits and demerits in going for the identified structure. ***(5 Marks)***

(b) *Symergy Ltd. is manufacturing a product since year 2010. The company was doing well till year 2022. After that its market share started declining. Accumulated losses started mounting and in turn carried a persistent negative impact on its cash flow. As a result morale of the employees was not up to mark.*

The Board of Directors (BoD) of the company thought it proper to continue in business by placing emphasis on improvement in internal efficiency. In view of the same, the BoD is evolving a workable action plan with intent to ensure a radical change in direction in strategy which includes revamping in top management.

Which retrenchment strategy company should adopt in the given situation? Also state the stages in the action plan for the strategy. ***(5 Marks)***

(c) *Market for baby care, readymade garments for new born, toys and strollers meant for babies are there. M/s. Maa ki Pasand is desirous to introduce new*

products for existing customers and new customers as well. The market for such products is narrow. On one side there are customers who are price conscious and on the other side there are customers who are ready to pay premium charges for an upscale product. The company wants to charge low price, relative to other firms that compete within the target market for customers who are price sensitive and also wants to charge premium based on uniqueness for rest of its products.

Which of the strategy is being considered by the company, out of strategies as suggested by Michael Porter at business level. Also outline the advantages and disadvantages using such strategy. ***(5 Marks)***

Answer

(a) The suitable organizational structure for **MTS Ltd** is the **Network Organizational Structure**. A company with such a structure is often called a **Virtual Organization.**

Merits of the Network Structure:

1. **Flexibility and Adaptability**: The structure allows for rapid technological changes and shifting competition patterns. This enables the company to adapt quickly to the unstable environment and changing customer preferences.
2. **Focus on Core Competencies**: The company can concentrate on its distinctive competencies while outsourcing non-core functions to specialized firms, which can perform them more efficiently.
3. **Cost Efficiency**: Through subcontracting and outsourcing, MTS Ltd can reduce the costs associated with maintaining in-house teams.
4. **Decentralized Operations**: The network structure scatters business functions across various geographical locations, reducing the need for a large central headquarters and ensuring responsiveness in different regions.

Demerits of the Network Structure:

1. **Loss of Synergies**: Contracting out functions may prevent MTS Ltd from discovering synergies that could emerge from combining internal activities.

2. **Over-Specialization Risk**: By focusing on only a few functions, the company may risk choosing the wrong functions, leading to a loss of competitiveness.

3. **Stress and Learning Challenges**: The flatter structure and increased need for personal interactions may create stress for employees, especially those who lack the confidence for active participation in organization-sponsored learning programs.

(b) In the given situation, the suitable retrenchment strategy for **Symergy Ltd.** is the **Turnaround Strategy**. This strategy is designed to reverse the company's decline and restore it to profitability, particularly when the company is facing challenges such as declining market share, negative cash flows, and low employee morale.

Stages in the Action Plan for Turnaround Strategy:

- **Stage One - Assessment of Current Problems**: The first step is to assess and diagnose the root causes of the company's decline, such as uncompetitive products, poor cash flow, or internal inefficiencies. This stage involves determining the extent of the damage caused by these problems.

- **Stage Two - Analyze the Situation and Develop a Strategic Plan**: Evaluate the chances of the company's survival and develop a strategic plan that outlines the corrective actions to be taken. This includes identifying appropriate strategies to address internal inefficiencies, improve competitiveness, and enhance employee morale.

- **Stage Three - Implementing an Emergency Action Plan**: If the situation is critical, an immediate action plan must be executed to stabilize the business. This may involve cutting costs, ensuring positive cash flow, raising necessary funds, and addressing short-term operational issues.

- **Stage Four - Restructuring the Business**: Focus on restructuring the company's core business operations, especially if they have been significantly affected. This stage involves efforts to improve efficiency, restructure finances, and position the company for long-term recovery and growth.

- **Stage Five - Returning to Normal**: In the final stage, the company should begin showing signs of profitability and improving financial performance. Strategic efforts such as introducing new products, improving customer service, and forming alliances should be emphasized to restore market share and build long-term sustainability.

  By following these stages, **Symergy Ltd.** can develop a comprehensive turnaround plan to regain its financial stability, improve operational efficiency, and rebuild its competitive position in the market.

(c) The company, M/s. Maa ki Pasand, is adopting a **focus strategy** that incorporates both **focused cost leadership** and **focused differentiation** strategies. In the given case, M/s. Maa ki Pasand aims to target price-conscious customers by charging low prices relative to other firms within the narrow market of baby care products. This aligns with **focused cost leadership**, where the firm competes based on price within a targeted niche.

For the segment of customers willing to pay more for premium, unique products, the company follows a **focused differentiation strategy**. It caters to this specific niche by offering high-end, differentiated products, which is a key feature of focused differentiation.

Advantages of using a Focus Strategy:

1. **Premium prices**: For the differentiated segment, the company can charge higher prices for its upscale products.
2. **Expertise in niche markets**: M/s. Maa ki Pasand can develop expertise in both price-sensitive and premium segments, making it difficult for rivals to compete effectively.

Disadvantages of Using a Focus Strategy:

1. **Distinctive competencies required**: The firm needs to have strong competencies in both cost control and product differentiation to succeed. Otherwise, it may struggle to pursue the focus strategy effectively.
2. **High costs**: Serving a narrow market can lead to higher costs due to limited demand, which could pose challenges in maintaining profitability, especially in the premium segment.

3. **Disappearance in long run**: In the long run, the niche goods can disappear or be taken over by large competitors by acquiring the same distinctive competencies.

   In conclusion, M/s. Maa ki Pasand is adopting a **focus strategy** by targeting specific customer niches with both cost leadership and differentiation. While this strategy offers opportunities for premium pricing and market expertise, it also comes with challenges related to cost control and distinctive competencies.

Question 6

(a) Explain in brief the term 'objectives' as part of strategic intent. Also outline the characteristics, the objectives of a company must possess to be meaningful and to serve the intended role. ***(5 Marks)***

(b) Value Chain Analysis consist two activities: Primary activities and Support activities. As per Michael Porter both the activities are intertwined. Do you agree with the statement? Also delineate the main areas in which primary activities of any organization are grouped. ***(5 Marks)***

Answer

(a) Objectives are an **organization's performance targets** – the results and outcomes it wants to achieve. They **function as yardstick** for tracking an organization's performance and progress. Objectives with strategic focus relate to outcomes that strengthen an organization's overall business position and competitive vitality.

Objectives, to be meaningful to serve the intended role, must possess the following characteristics:

- Objectives should define the organisation's relationship with its environment.
- They should be facilitative towards achievement of mission and purpose.
- They should provide the basis for strategic decision-making.
- They should provide standards for performance appraisal.
- They should be concrete and specific.

- They should be related to a time frame.
- They should be measurable and controllable.
- They should be challenging.
- Different objectives should correlate with each other.
- Objectives should be set within the constraints of organisational resources and external environment.

(b) **Yes, I agree with the statement** that Value Chain Analysis consist of two activities: Primary activities and Support activities. As per Michael Porter both the activities are intertwined. It is a tool used to examine the activities that create value in an organization, helping to enhance efficiency and build competitive advantage. It breaks down a business's operations to identify areas for improvement in value creation.

The **primary activities** of an organization are categorized into five areas:

1. **Inbound logistics**: Activities related to receiving, storing, and distributing inputs (e.g., materials handling, stock control, and transport).
2. **Operations**: Transforming inputs into final products or services (e.g., machining, packaging, assembly).
3. **Outbound logistics**: Collecting, storing, and delivering products to customers (e.g., warehousing, transport).
4. **Marketing and sales**: Promoting and selling the product or service, including advertising and sales administration.
5. **Service**: Enhancing or maintaining product value (e.g., installation, repair, training).

Question 7

(a) Explain the four specific criteria of sustainable competitive advantages that a company can use to determine the capabilities that are core competencies. ***(5 Marks)***

(b) Start-ups rarely aim for stability strategy. While agreeing with the statement or otherwise, support your point of view by briefly stating as to when the stability strategy is meaningful. State the major reasons for

considering stability strategy as one of the corporate strategies by a company. ***(5 Marks)***

Answer

(a) Four specific criteria of sustainable competitive advantage that firms can use to determine those capabilities that are core competencies. Capabilities that are valuable, rare, costly to imitate, and non-substitutable are core competencies.

i. **Valuable:** Valuable capabilities are the ones that allow the firm to exploit opportunities or avert the threats in its external environment. A firm created value for customers by effectively using capabilities to exploit opportunities. Finance companies build a valuable competence in financial services. In addition, to make such competencies as financial services highly successful require placing the right people in the right jobs. Human capital is important in creating value for customers.

ii. **Rare:** Core competencies are very rare capabilities and very few of the competitors possess this. Capabilities possessed by many rivals are unlikely to be sources of competitive advantage for any one of them. Competitive advantage results only when firms develop and exploit valuable capabilities that differ from those shared with competitors.

iii. **Costly to imitate:** Costly to imitate means such capabilities that competing firms are unable to develop easily.

iv. **Non-substitutable:** Capabilities that do not have strategic equivalents are called non-substitutable capabilities. This final criterion for a capability to be a source of competitive advantage is that there must be no strategically equivalent valuable resources that are themselves either not rare or imitable.

(b) **Agree with the given statement.** Start-ups rarely aim for a stability strategy because they are in the **early stages of ideation and development**, where **speed and agility** are critical. Stability strategy is more relevant for businesses that have reached maturity, where maintaining current operations and market share becomes a priority. Start-ups, however, focus on rapid growth and market penetration, and

stability is usually considered when a business has expanded to full capacity.

A stability strategy is meaningful in the following scenarios:

- When a firm continues serving the same markets with the same products and services.
- Firms whose products are in the maturity stage of the product life cycle or who have a substantial market share may opt for stability to retain their position.
- Stability helps consolidate gains after rapid expansion, optimize returns on committed resources, and enhance functional efficiencies.

Major reasons for choosing a stability strategy include:

- Maturity of products in the life cycle.
- Comfort of staff with fewer changes and risks.
- Stable external environment.
- A need to consolidate after rapid growth or expansion.
- Where it is not advisable to expand as it may be perceived as threatening.

Question 8

(a) In light of the five forces as propagated by Michael Porter, explain the common barriers which may cause restrain for the keenness of new entrepreneurs. ***(5 Marks)***

(b) Strategic performance measures are key indicators that organizations use to track the effectiveness of their strategies and make informed decisions about resource allocation. In light of the statement, state various types of Strategic performance measures. ***(5 Marks)***

OR

(b) Explain the pointers for navigating change during digital transformation.

(5 Marks)

Answer

(a) In light of Michael Porter's Five Forces, new entrepreneurs often face significant barriers that restrain their keenness to enter an industry. These barriers increase the competitiveness of existing firms and discourage new entrants, impacting industry profitability.

Common barriers that may restrain new entrepreneurs include:

(i) Capital Requirements: When a large amount of capital is required to enter an industry, firms lacking funds are effectively barred from the industry, thus enhancing the profitability of existing firms in the industry.

(ii) Economies of Scale: Many industries are characterized by economic activities driven by economies of scale. Economies of scale refer to the decline in the per-unit cost of production (or other activity) as volume grows.

(iii) Product Differentiation: Product differentiation refers to the physical or perceptual differences, or enhancements, that make a product special or unique in the eyes of customers.

(iv) Switching Costs: To succeed in an industry, new entrant must be able to persuade existing customers of other companies to switch to its products. When such switching costs are high, buyers are often reluctant to change.

(v) Brand Identity: The brand identity of products or services offered by existing firms can serve as another entry barrier. Brand identity is particularly important for infrequently purchased products that carry a high unit cost to the buyer.

(vi) Access to Distribution Channels: The unavailability of distribution channels for new entrants poses another significant entry barrier. Despite the growing power of the internet, many firms may continue to rely on their control of physical distribution channels to sustain a barrier to entry to rivals.

(vii) Possibility of Aggressive Retaliation: Sometimes the mere threat of aggressive retaliation by incumbents can deter entry by other firms into an existing industry.

(b) Strategic performance measures are key indicators used by organizations to track the effectiveness of their strategies and make informed decisions about resource allocation. These measures provide a snapshot of performance, enabling leaders to assess whether their strategies align with organizational goals and make necessary adjustments for improvement.

Types of strategic performance measures include:

1. **Financial Measures**: These include revenue growth, return on investment (ROI), and profit margins, which help in understanding the financial performance and profitability of the organization.
2. **Customer Satisfaction Measures**: Metrics like customer satisfaction, retention, and loyalty give insights into how well the organization meets customer needs and the quality of its products and services.
3. **Market Measures**: Market share, customer acquisition, and referrals indicate the organization's competitiveness and ability to attract and retain customers in the marketplace.
4. **Employee Measures**: Employee satisfaction, turnover rate, and engagement provide insights into the organization's ability to create a positive work environment and retain talent.
5. **Innovation Measures**: These include R&D spending, patent applications, and new product launches, reflecting the organization's capacity to innovate and meet evolving customer demands.
6. **Environmental Measures**: Environmental measures such as energy consumption, waste reduction, and carbon emissions offer insights into the organization's impact on the environment. These measures help track sustainability efforts and ensure that the organization is operating in an eco-friendly and socially responsible manner.

   These measures help organizations ensure their strategies are effectively executed, aligned with their objectives, and adaptable to changes in both market and environmental contexts.

Or

Any organisation may find the work of digital transformation challenging and overwhelming. To ensure that a digital transition is effective, change

management is essential. Here are some pointers for navigating change during the digital transformation:

1. **Specify the digital transformation's aims and objectives:** What is the intended outcome? What are the precise objectives that must be accomplished? It will be easier to make sure that everyone is on the same page and pursuing the same aims if everyone has a clear grasp of the goals.
2. **Always, always, always communicate:** It might be challenging for people to accept change and adjust to it. Ensure that you routinely and honestly discuss the objectives of the digital transformation and how they will affect stakeholders, including employees, clients, and other parties.
3. **Be ready for resistance:** Even when a change is for the better, it can be challenging for people to embrace it. Have a strategy in place for dealing with any resistance that may arise.
4. **Implement changes gradually:** Changes should ideally be implemented gradually rather than all at once. In order to avoid overwhelming individuals with too much change at once, this will give people time to become used to the new way of doing things.
5. **Offer assistance and training:** Workers will need guidance in the new procedures, software applications, etc.

In conclusion, effective completion of the massive project known as digital transformation depends on meticulous planning and change management. Digital transformation efforts are more likely to fail without change management. Organizations can successfully integrate a new digital system by planning for and managing the changes that must take place. Any project involving digital transformation must include it.

INTERMEDIATE EXAM
PAPER-6
FINANCIAL MANAGEMENT &
STRATEGIC MANAGEMENT

EUM2(H)

17 MAY 2024

Roll No. ....

17/05/2024
05:10 PM

Total No. of Questions – **8**

Total No. of Printed Pages – **16**

Maximum Marks – **70**

GENERAL INSTRUCTIONS TO CANDIDATES

1. The question paper comprises two parts, Part I and Part II.
2. Part I comprises Multiple Choice Questions (MCQs).
3. Part II comprises questions which require descriptive type answers.
4. Ensure that you receive the question paper relating to both the parts. If you have not received both, bring it to the notice of the invigilator.
5. Answers to MCQs in Part I are to be marked on the OMR answer sheet as given on the cover page of descriptive answer book of Section – A only. Answers to questions in Part II are to be written in the same descriptive answer book. Answers to MCQs, if written inside the descriptive answer book or on Part-II Question paper will not be evaluated.
6. OMR answer sheet given on the cover page of descriptive answer book will be in English only for all candidates, including for Hindi medium candidates.
7. The bar coded sticker provided in the attendance register, is to be affixed only on the descriptive answer book.
8. You will be allowed to leave the examination hall only after the conclusion of the exam. If you have completed the paper before time, remain in your seat till the conclusion of the exam.
9. Duration of the examination is 3 hours. You will be required to submit (a) Part I of the question paper containing MCQs, and (b) the answer book in respect of descriptive answer book with OMR cover page to the invigilator before leaving the exam hall, after the conclusion of the exam.
10. The invigilator will give you acknowledgement on Page 2 of the admit card, upon receipt of the above-mentioned items.
11. Candidate found copying or receiving or giving any help or defying instructions of the invigilators will be expelled from the examination and will also be liable for further punitive action.

PART – II

70 Marks

1. **Section-A :** Question paper comprises **4** questions (1 to 4). Answer Question No. **1** which is compulsory and any **2** out of the remaining **3** questions.
2. **Section-B :** Question paper comprises **4** questions (5 to 8). Answer Question No. **5** which is compulsory and any **2** out of the remaining **3** questions.
3. Answers to the questions are to be given only in English except in the case of candidates who have opted for Hindi Medium. If a candidate has not opted for Hindi Medium, his/her answers in Hindi will not be evaluated.
4. Working note should be part of the respective answers.

PART – II

Section-A

1. (a) Theme Ltd provides you the following information : **5**

12.5 % Debt	₹ 45,00,000
Debt to Equity ratio	1.5 : 1
Return on Shareholder's fund	54%
Operating Ratio	85%
Ratio of operating expenses to Cost of Goods sold	2 : 6
Tax rate	25%
Fixed Assets	₹ 39,00,000
Current Ratio	1.8 : 1

You are required to calculate :

(i) Interest Coverage Ratio

(ii) Gross Profit Ratio

(iii) Current Assets

(b) Alpha Limited has provided following information : **5**

Equity Share Capital	25,000 Shares @ ₹ 100 per Share
15% Debentures	10,000 Debentures @ ₹ 750/- per Debenture
Sales	50 Lakhs units @ ₹ 20 per unit
Variable Cost	₹ 12.50 per unit
Fixed Costs	₹ 175.00 Lakhs

Due to recent policy changes and entry of foreign competitors in the sector, Alpha Limited expects the sales may decline by 15-20%, However, selling price and other costs will remain the same. Corporate Taxes will continue @ 20%.

You are required to calculate the decrease in Earnings per share, Degree of Operating Leverage and Financial Leverage separately if sales are declined by (i) 15%; and (ii) 20%.

(c) Following is the sales information in respect of Bright Ltd : 5

Annual Sales (90 % on credit)	₹ 7,50,00,000
Credit period	45 days
Average Collection period	70 days
Bad debts	0.75%
Credit administration cost (out of which 2/5th is avoidable)	₹ 18,60,000

A factor firm has offered to manage the company's debtors on a non-recourse basis at a service charge of 2%. Factor agrees to grant advance against debtors at an interest rate of 14% after withholding 20% as reserve. Payment period guaranteed by factor is 45 days. The cost of capital of the company is 12.5%. One time redundancy payment of ₹ 50,000 is required to be made to factor.

Calculate the effective cost of factoring to the company.

(Assume 360 days in a year)

2. (a) The capital structure of Shine Ltd. as on 31.03.2024 is as under : 6

Particulars	Amount (₹)
Equity share capital of ₹ 10 each	45,00,000
15% Preference share capital of ₹ 100 each	36,00,000
Retained earnings	32,00,000
13% Convertible Debenture of ₹ 100 each	67,00,000
11% Term Loan	20,00,000
Total	**2,00,00,000**

Additional information :

(A) Company issued 13% Convertible Debentures of ₹ 100 each on 01.04.2023 with a maturity period of 6 years. At maturity, the debenture holders will have an option to convert the debentures into equity shares of the company in the ratio of 1 : 4 (4 shares for each debenture). The market price of the equity share is ₹ 25 each as on 31.03.2024 and the growth rate of the share is 6% per annum.

(B) Preference stock, redeemable after eight years, is currently selling at ₹ 150 per share.

(C) The prevailing default- risk free interest rate on 10-year GOI treasury bonds is 6%. The average market risk premium is 8% and the Beta (β) of the company is 1.54.

Corporate tax rate is 25% and rate of personal income tax is 20%.

You are required to calculate the cost of :

(i) Equity Share Capital
(ii) Preference Share Capital
(iii) Convertible Debenture
(iv) Retained Earnings
(v) Term Loan

(b) Following data is available in respect of Levered and Unlevered companies having same business risk : **4**

Capital employed = ₹ 2,00,000, EBIT = ₹ 25,000 and K_e = 12.5%

Sources	Levered Company (₹)	Unlevered Company (₹)
Debt (@ 8 %)	75,000	Nil
Equity	1,25,000	2,00,000

An investor is holding 12% shares in levered company. Calculate the increase in annual earnings of investor if he switches over his holding from Levered to Unlevered company.

3. (a) HCP Ltd. is a leading manufacturer of railway parts for passenger coaches and freight wagons. Due to high wastage of material and quality issues in production, the General Manager of the company is considering the replacement of machine A with a new CNC machine B. Machine A has a book value of ₹ 4,80,000 and remaining economic life is 6 years. It could be sold now at ₹ 1,80,000 and zero salvage value at the end of sixth year. The purchase price of Machine B is ₹ 24,00,000 with economic life of 6 years. It will require ₹ 1,40,000 for installation and ₹ 60,000 for testing. Subsidy of 15% on the purchase price of the machine B will be received from Government at the end of 1st year. Salvage value at the end of sixth year will be ₹ 3,20,000. **7**

The General manager estimates that the annual savings due to installation of machine B include a reduction of three skilled workers with annual salaries of ₹ 1,68,000 each, ₹ 4,80,000 from reduced wastage of materials and defectives and ₹ 3,50,000 from loss in sales due to delay in execution of purchase orders. Operation of Machine B will require the services of a trained technician with annual salary of ₹ 3,90,000 and annual operation and maintenance cost will increase by ₹ 1,54,000. The company's tax rate is 30% and it's required rate of return is 14%. The company follows straight line method of depreciation. Ignore tax savings on loss due to sale of existing machine.

The present value factors at 14% are :

Years	0	1	2	3	4	5	6
PV Factor	1	0.877	0.769	0.675	0.592	0.519	0.456

Required :

(i) Calculate the Net Present Value and Profitability Index and advise the company for replacement decision.

(ii) Also calculate the discounted pay-back period.

(b) Vista Limited's retained earnings per share for the year ending 31.03.2023 being 40% is ₹ 3.60 per share. Company is foreseeing a growth rate of 10% per annum in the next two years. After that the growth rate is expected to stabilize at 8% per annum. Company will maintain its existing pay-out ratio. If the investor's required rate of return is 15%, Calculate the intrinsic value per share as of date using Dividend Discount model. **3**

4. (a) State with brief reasons whether the following statements are true or false : **4**

   (i) Maximising Market Price Per Share (MPS) as the financial objective which maximises the wealth of shareholders.

   (ii) A combination of lower risk and higher return is known as risk-return trade off and at this level of risk-return, profit is maximum.

   (iii) Financial distress is a position when accounting profits of a firm are sufficient to meet its long-term obligations.

   (iv) Angel investor is one who provides funds for start-up in exchange for an ownership/equity.

(b) ABC Ltd. is approaching the banks for financing its business activity. You are required to describe any four forms of bank credit for the consideration of the company. **4**

(c) Discuss the relevance of Payback reciprocal in capital budgeting decisions. **2**

OR

(c) Explain the features of crowd funding. **2**

Section-B

5. (a) BOYA Ltd. is a venture in the market present for a decade. Till, 2023, it was working on the values and vision of its founder while operating in limited area of operations. **2+3 =5**

Growth opportunities exist for BOYA Ltd. Considering the changing environment, company is interested to leverage new skills in marketing, technology, product development and financial management. As a known fact, modifying one aspect might have a ripple effect on other elements. The company wants to understand various hard and soft elements interrelated with each other in the company and having a bearing on effective operational results.

As a strategist, you intend to prepare a questionnaire based on both types of elements by analyzing the organizational design. The response to the same will help in finding an answer to ensure effectiveness through the interaction of such elements.

Briefly discuss the strategic model you will use in the given situation. State the limitations of the model as well.

(b) Elvis Global is a famous OTT platform facing fierce competition from its competitors amid changing consumer preferences. This has made it difficult to retain customers as the existing television channels are also launching their own platforms. The company has appointed Raghav to lead the company forward as the sales & marketing manager. Raghav needs to design creative and innovative advertising campaigns to gain a competitive edge, engage the public and capture the market. **1+4 =5**

Identify the strategic level that represents Raghav's role at Elvis Global. As a strategic advisor, highlight the various benefits of strategic management in overcoming different challenges to Raghav.

P.T.O.

(c) Yash is planning to launch his new tech start-up. He is exploring different locations across the country to establish his company in the right business environment. One option is the city of Bengaluru, the silicon valley of India, with an engaging network of entrepreneurs, investors, advisors and mentors. Coupled with various subsidies for new ventures and tax benefits, Bengaluru might be an ideal choice for Yash to establish his company and increase the chances of success. Define the term Business Environment with respect to the above scenario. Explain the different ways in which the interaction of a business with its environment can be helpful in developing a successful strategy. **1+4=5**

6. (a) 'Innovation leads to unnecessary expenses that do not give as many returns.' Do you agree with the statement ? Give reasons in support of your answer. **1+4=5**

(b) Explain how organizations can effectively manage strategic uncertainties in a rapidly changing business environment. **5**

7. (a) What are the key characteristics of business products that contribute to the overall competitiveness and dynamics of the market ? **5**

(b) 'A company's mission statement is typically focused on its present business scope.' Explain the significance of a mission statement. **5**

8. (a) What are channels ? Why is channel analysis important ? Explain the different types of channels ? **1+1+3=5**

(b) Explain the concept of vertically integrated diversification. How is forward integration different from backward integration ? **5**

OR

(b) Recommend a tool to analyze the competitive position of various rival companies in the market and outline the step by step procedure for using the identified tool. **5**

PART – II

(Hindi Version)

Section – A

1. (a) Theme लि. ने निम्नलिखित सूचना प्रदान की है **5**

12.5% ऋण	₹ 45,00,000
ऋण समता अनुपात	1.5 : 1
अंशधारियों की निधि पर प्रत्याय	54%
परिचालन अनुपात	85%
परिचालन व्ययों का विक्रित सामग्री की लागत से अनुपात	2 : 6
कर की दर	25%
स्थायी सम्पत्तियाँ	₹ 39,00,000
चालू अनुपात	1.8 : 1

आपसे अपेक्षित है कि गणना कीजिए :

(i) ब्याज आवरण अनुपात

(ii) सकल लाभ अनुपात

(iii) चालू सम्पत्तियाँ

(b) Alpha लि. ने निम्नलिखित सूचनायें प्रदान की हैं : **5**

समता अंश पूँजी	25,000 अंश ₹ 100 प्रत्येक अंश के
15% ऋण पत्र	10,000 ऋण पत्र ₹ 750/- प्रत्येक ऋण पत्र के
विक्रय	50 लाख इकाइयाँ प्रति इकाई ₹ 20
परिवर्तनशील लागत	₹ 12.50 प्रति इकाई
स्थिर लागत	₹ 175.00 लाख

हाल में हुये नीतिगत परिवर्तनों तथा इस क्षेत्र में विदेशी प्रतिस्पर्धियों के प्रवेश के कारण Alpha लि. की प्रत्याशा है कि विक्रय 15-20% तक गिर सकती है । यद्यपि विक्रय कीमत तथा अन्य लागतें समान रहेंगी । निगम कर भी 20% की दर पर होगा ।

आपसे अपेक्षित है कि प्रति अंश आय में कमी, परिचालन प्रभावन क्षमता तथा वित्तीय प्रभावन क्षमता की डिग्री की गणना अलग-अलग कीजिए जब विक्रय में (i) 15% तथा (ii) 20% की कमी हो जाए ।

(c) ब्राइट लि. की विक्रय सम्बन्धी सूचनायें निम्नलिखित हैं : 5

वार्षिक विक्रय (90% साख पर)	₹ 7,50,00,000
साख अवधि	45 दिन
औसत संग्रहण अवधि	70 दिन
अशोध्य ऋण	0.75%
साख प्रशासन लागत (जिसका 2/5 एवॉइडेबल है)	₹ 18,60,000

एक फैक्टर फ़र्म ने कम्पनी के देनदारों को 2% के सेवा प्रभार की दर से नॉन–रिकोर्स आधार पर प्रबन्धन करने का प्रस्ताव दिया है । फैक्टर सहमत है कि 20% संचय के रूप में रोकने के उपरान्त देनदारों पर 14% ब्याज दर से अग्रिम भुगतान कर देगा । भुगतान अवधि 45 दिन फैक्टर द्वारा गारण्टेड है । कम्पनी की पूँजी की लागत 12.5% है । फैक्टर के एक बार रिडन्डेन्सी भुगतान ₹ 50,000 अपेक्षित है ।

कम्पनी के लिए फैक्टरिंग की प्रभावी लागत की गणना कीजिए ।

(वर्ष में 360 दिन परिकल्पित कीजिए ।)

2. (a) 31.03.2024 को Shine लि. की पूँजी संरचना निम्नवत् है : 6

विवरण	धनराशि (₹)
समता अंश पूँजी प्रत्येक ₹ 10 के	45,00,000
15% पूर्वाधिकार अंश पूँजी प्रत्येक ₹ 100 के	36,00,000
धारित आय	32,00,000
13% परिवर्तनीय ऋण पत्र प्रत्येक ₹ 100 के	67,00,000
11% दीर्घकालीन ऋण	20,00,000
कुल	**2,00,00,000**

अतिरिक्त सूचनायें :

(A) कम्पनी ने 01.04.2023 को प्रत्येक ₹ 100 के 13% परिवर्तनीय ऋण पत्र 6 वर्षों की परिपक्वता अवधि के लिये निर्गमित किए । परिपक्वता पर ऋण पत्र धारकों को यह विकल्प होगा कि वे 1:4 (एक ऋण पत्र के बदले चार अंश) के अनुपात में ऋण पत्रों का अंशों में परिवर्तन कर सकेंगे । समता अंशों का बाज़ार मूल्य 31.03.2024 को ₹ 25 प्रति अंश है तथा अंशों का विकास दर 6% प्रतिवर्ष है ।

(B) पूर्वाधिकार स्टॉक, जो 8 वर्षों बाद शोधनीय हैं, वर्तमान में ₹ 150 प्रति अंश पर बेचे जा रहे हैं ।

(C) वर्तमान में डिफाल्ट जोखिम रहित ब्याज दर 10 वर्षीय GOI ट्रेजरी बॉण्ड पर 6% है । औसत बाज़ार जोखिम प्रत्याय 8% है तथा कम्पनी का वीटा (β) 1.54 है । निगम कर की दर 25% तथा व्यक्तिगत आयकर की दर 20% है ।

आपसे अपेक्षित है कि निम्न के लागत की गणना कीजिए :

(i) समता अंश पूँजी

(ii) पूर्वाधिकार अंश पूँजी

(iii) परिवर्तनीय ऋण पत्र

(iv) प्रतिधारित उपार्जन

(v) दीर्घकालीन ऋण

(b) एक समान व्यावसायिक जोखिम वाली लीवर्ड तथा अनलीवर्ड कम्पनियों के सम्बन्ध में निम्नलिखित आँकड़े उपलब्ध हैं : **4**

विनियोजित पूँजी = ₹ 2,00,000, ब्याज एवं कर पूर्ण आय = ₹ 25,000 तथा K_e = 12.5%

स्रोत	लीवर्ड कम्पनी (₹)	अनलीवर्ड कम्पनी (₹)
ऋण दर 8%	75,000	Nil
समता	1,25,000	2,00,000

एक विनियोक्ता के लीवर्ड कम्पनी में 12% अंश हैं । विनियोक्ता की वार्षिक आय में वृद्धि की गणना कीजिये यदि वह अपनी होल्डिंग लीवर्ड कम्पनी से अनलीवर्ड कम्पनी में हस्तान्तरित कर दे ।

3. (a) HCP लि. पैसेन्जर कोच तथा वैगनों के अग्रणी पार्ट्स उत्पादक हैं । सामग्री के अत्याधिक क्षय तथा उत्पादन में गुणवत्ता समस्या के कारण कम्पनी के महाप्रबन्धक मशीन A को नयी CNC मशीन B से प्रतिस्थापित करने पर विचार कर रहे हैं । मशीन A का पुस्तकीय मूल्य ₹ 4,80,000 तथा शेष आर्थिक जीवन 6 वर्ष है । यह इस समय ₹ 1,80,000 में बेची जा सकती है तथा छठें वर्ष के अन्त में शून्य साल्वेज वैल्यू रहेगी । मशीन B का क्रय मूल्य ₹ 24,00,000 तथा आर्थिक जीवन 6 वर्ष है । इस पर ₹ 1,40,000 स्थापन व्यय तथा ₹ 60,000 टेस्टिंग के खर्चे करने पड़ेंगे । प्रथम वर्ष के उपरान्त मशीन B के क्रय मूल्य पर 15% का अनुदान सरकार से प्राप्त किया जायेगा । छठे वर्ष के अन्त में साल्वेज वैल्यू ₹ 3,20,000 होगी । 7

महाप्रबन्धक का अनुमान है कि मशीन B की स्थापना से वार्षिक बचतों में तीन स्किल्ड श्रमिकों का वार्षिक वेतन प्रत्येक के ₹ 1,68,000, ₹ 4,80,000 सामग्री एवं दोषपूर्ण क्षय में कमी से तथा ₹ 3,50,000 क्रय आदेशों की आपूर्ति में देरी होने से विक्रय में कमी से शामिल होगी । मशीन B का परिचालन के लिये एक प्रशिक्षित टेक्नीशियन चाहिए जिसका वार्षिक वेतन ₹ 3,90,000 होगा तथा वार्षिक परिचालन तथा रख–रखाव की लागत में ₹ 1,54,000 की बढ़ोत्तरी हो जायेगी । कम्पनी के कर की दर 30% है तथा अपेक्षित प्रत्याय दर 14% है । कम्पनी ह्रास की सीधी रेखा विधि का अनुसरण करती है । वर्तमान मशीन के विक्रय पर हानि के कारण कर बचत की उपेक्षा कीजिए ।

14% की दर पर वर्तमान मूल्य फैक्टर निम्नवत् है :

वर्ष	0	1	2	3	4	5	6
वर्तमान मूल्य घटक	1	0.877	0.769	0.675	0.592	0.519	0.456

अपेक्षित :

(i) शुद्ध वर्तमान मूल्य तथा लाभदायकता इन्डेक्स की गणना कीजिए तथा कम्पनी को प्रतिस्थापन निर्णय पर सलाह दीजिए ।

(ii) डिस्काउण्टेड पे–बैक पीरियड की गणना कीजिए ।

(b) Vista लि. की प्रतिधारित उपार्जन प्रति अंश 31.03.2023 को समाप्त हुए वर्ष के लिए ₹ 3.60 (40%) है । कम्पनी अगले दो वर्षों के लिए विकास दर 10% की कल्पना कर रही है । तत्पश्चात् विकास दर 8% पर स्थिर होने की प्रत्याशा है । कम्पनी अपने वर्तमान प्रतिदाय अनुपात को कायम रखेगी । यदि विनियोक्ता की अपेक्षित प्रत्याय दर 15% है, लाभांश बट्टा मॉडल (Dividend Discount model) का प्रयोग करते हुए उक्त तिथि पर अंशों के विहित मूल्य (Intrinsic value of share) की गणना कीजिए । **3**

4\. (a) संक्षिप्त कारणों का वर्णन करते हुए स्पष्ट कीजिए कि निम्नलिखित विवरण सत्य हैं या असत्य : **4**

(i) वित्तीय उद्देश्य के रूप में बाज़ार मूल्य प्रति अंश को अधिकतम करना अंशधारियों की सम्पदा को अधिकतम करता है ।

(ii) कम जोखिम और अधिक प्रत्याय को जोखिम-प्रत्याय ट्रेड ऑफ कहते हैं । तथा जोखिम – प्रत्याय के इस स्तर पर लाभ अधिकतम होता है ।

(iii) वित्तीय संकट वह स्थिति है जब किसी फ़र्म के लेखांकन लाभ दीर्घकालीन दायित्वों को सम्पादित करने के लिए पर्याप्त हों ।

(iv) एन्जिल विनियोक्ता वह है जो स्टार्टअप को फण्ड स्वामित्व / समता के विनिमय में देता है ।

(b) ABC लि. अपने व्यावसायिक क्रियाओं के वित्तीयन के लिए बैंकों को एप्रोच कर रही है । कम्पनी के विचार के लिए आप से अपेक्षित है कि बैंक क्रेडिट के किन्हीं चार प्रकारों का वर्णन कीजिए । **4**

(c) पूँजी बजटिंग निर्णयों में पे-बैक रेसीप्रोकल की उपादेयता की विवेचना कीजिए । **2**

अथवा

(c) क्राउड फण्डिंग के लक्षणों की व्याख्या कीजए । **2**

Section – B

5. (a) बोया लि. (Boya Ltd.,) दशकों से बाज़ार में स्थापित है । 2023 तक वह अपने संस्थापक के उद्देश्य एवं नैतिक मूल्यों के अनुसार काम करती है अपने व्यापार के संचालन के सीमित क्षेत्र में । बदलते हुए वातावरण को ध्यान में रखते हुए एवं उपलब्ध विस्तार चुनौतियों के साथ कंपनी विपणन, तकनीक, उत्पाद विकास एवं वित्तीय प्रबन्धन के क्षेत्र में नये हुनर को आगे बढ़ाना चाहती है । यह जानते हुए कि अगर एक चीज को बदलते हैं तो उसका कुछ प्रभाव दूसरे तथ्यों पर भी पड़ता है, कंपनी यह जानना चाहती है कि विभिन्न प्रकार के हलके एवं सख़्त तत्त्व एक दूसरे से कंपनी से जुड़े हुए हैं और उनका बर्ताव परिणामकारी संचालन के परिणाम में शामिल है । **2+3 =5**

एक रणनीतिक की तरह आपको व्यापारिक डिजाइन का विश्लेषण करते हुए दोनों प्रकार के तत्त्वों (elements) के अनुसार एक प्रश्नावली तैयार करनी है । इस प्रतिक्रिया से उन उत्तरों को जानने में आसानी होगी जिससे इस प्रकार के तत्त्वों को मिलाकर काम करना बहुत प्रभावी सिद्ध होता है ।

संक्षेप में चर्चा करें कि किस प्रकार का रणनीतिक नमूना (strategic module) आप इस स्थिति में उपयोग करेंगे । इसके साथ उस नमूने की सीमाओं (limitation) को भी बताइये ।

(b) Elvis Global एक जाना माना OTT प्लेटफॉर्म (Platform) है जिसको अपने प्रतिद्वन्द्वियों से तीव्र प्रतिस्पर्धा का सामना करना पड़ रहा है । ग्राहकों के बदलते चयन को देखते हुए, अपने दर्शकों को अपने साथ बनाए रहने के लिए उन्हें बहुत कठिनाई हो रही है क्योंकि मौजूदा TV Channel भी अपने OTT Platform चालू कर रहे हैं । कंपनी ने राघव को नियुक्त किया है जिससे वह कंपनी को बिक्री एवं विज्ञापन प्रबन्धक के रूप में आगे की ओर ले जाये । **1+4 =5**

राघव को सृजनात्मक एवं नये प्रकार की विज्ञापन गतिविधि को बनाना है जिससे प्रतिस्पर्धात्मक तीव्रता का लाभ ले सके और लोगों को अपनी ओर आकर्षित कर सके जिससे पूरे बाज़ार पर उनका कब्जा हो जाये ।

Elvis Global में राघव के रणनीतिक स्तर को पहचानिये । एक रणनीतिक सलाहकार के रूप में राघव के सामने आने वाली विभिन्न चुनौतियों को पार करने में रणनीतिक प्रबंधन के विविध लाभ को उजागर कीजिए ।

(c) यश तकनीकी व्यापार में अपना उद्यम शुरू करने के बारे में सोच रहा है वह पूरे देश के विभिन्न स्थानों के बारे में शोध कर रहा है, जिससे उसकी कंपनी एक सही व्यापारिक परिस्थिति में विकसित हो सके। एक विकल्प है बैंगलुरु जो कि भारत की सिलिकोन वैली (Silicon Valley) है अपने उद्यम कर्ता, निवेशक, सलाहकार और अनुमती परामर्शदाता के व्यस्त नेटवर्क के साथ है। **1+4 =5**

नये उद्यम के लिए आर्थिक सहायता एवं कर में छूट के साथ बैंगलुरु एक अच्छा विकल्प है यहाँ पर कंपनी को स्थापित करने के लिए, जिससे सफलता के अवसर बढ़ सकें।

* उपर्युक्त कथनों के अनुसार व्यावसायिक परिस्थिति को परिभाषित कीजिए।
* मेल-जोल के द्वारा व्यावसायिक परिस्थिति को सफल रणनीति बनाने के लिए विभिन्न प्रकारों को समझाइये।

6. (a) 'नवप्रवर्तन से अनावश्यक खर्च होता है जो उतना रिटर्न नहीं देता।' क्या आप इस कथन से सहमत हैं ? अपने उत्तर के साथ कारण बताइए। **1+4 =5**

(b) किस प्रकार से संगठन शीघ्र बदलने वाले व्यापारिक वातावरण की रणनीतिक अनिश्चितताओं से निपटता है ? उनको समझाइए। **5**

7. (a) व्यापार उत्पाद की मुख्य विशेषताओं को बताइए जो कि बाज़ार की पूर्ण प्रतिस्पर्धा एवं गति (dynamics) के लिए सहायक हैं ? **5**

(b) 'किसी कम्पनी का मिशन वक्तव्य सामान्य तौर पर उसके वर्तमान व्यावसायिक दायरे पर केन्द्रित होता है।' मिशन वक्तव्य की ज़रूरत को समझाइए। **5**

8. (a) चैनल (Channels) क्या हैं ? चैनल का विश्लेषण क्यों आवश्यक है। विभिन्न प्रकार के चैनलों को समझाइए। **1+1+ 3=5**

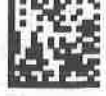
(b) ऊर्ध्वाधर एकीकृत विविधीकरण की अवधारणा को समझाइए। किस प्रकार से आगे की ओर एकीकरण पीछे की ओर एकीकरण से भिन्न है ? **5**

अथवा

(b) उचित साधनों को प्रस्तावित कीजिए जिससे प्रतिद्वन्द्वी कंपनियों की प्रतिस्पर्धी स्थिति को जाना जा सकें तथा पहचाने हुए साधन को किस प्रकार उपयोग करेंगे यह क्रमानुसार बताइए। **5**

EUM2(H)

रोल नं. ....



कुल प्रश्नों की संख्या – 8

कुल पृष्ठ – 16

अधिकतम अंक – 70

अभ्यर्थियों के लिए सामान्य निर्देश

1. प्रश्न-पत्र के दो भाग हैं, Part-I और Part-II.
2. Part-I में बहुविकल्पीय प्रश्न (MCQs) हैं ।
3. Part-II में वर्णनात्मक प्रकार के उत्तर की अपेक्षा वाले प्रश्न हैं ।
4. सुनिश्चित करें कि दोनों भागों से संबंधित प्रश्न-पत्र आपने प्राप्त किया है । यदि आपने दोनों भाग प्राप्त नहीं किये हैं तो निरीक्षक के ध्यान में लावें।
5. Part-I के प्रश्नों के उत्तर केवल OMR उत्तर-पत्र पर चिह्नित करने हैं जो कि वर्णनात्मक उत्तर-पुस्तिका (Section-A) के मुख्य पृष्ठ पर दिया गया है । Part-II के प्रश्नों के उत्तर वर्णनात्मक उत्तर-पुस्तिका में लिखना है । बहुविकल्पीय प्रश्नों के उत्तर वर्णनात्मक उत्तर-पुस्तिका के भीतर या Part-I बहुविकल्पीय प्रश्न-पुस्तिका में लिखने पर उनका मूल्यांकन नहीं होगा ।
6. OMR उत्तर-पत्र, जो कि वर्णनात्मक उत्तर-पुस्तिका के मुख्य पृष्ठ पर दिया गया है । सभी अभ्यर्थियों के लिए, हिंदी माध्यम के अभ्यर्थियों सहित, केवल अंग्रेजी में होगा ।
7. उपस्थिति पंजीयक में दिया बार कोड स्टीकर वर्णनात्मक प्रकार उत्तर-पुस्तिका पर लगाया जाएगा ।
8. परीक्षा की समाप्ति के पश्चात् ही आपको परीक्षा कक्ष छोड़ने की अनुमति होगी । यदि आपने समय से पूर्व पेपर पूर्ण कर लिया है तो भी आपको अपनी सीट पर ही बैठना होगा ।
9. परीक्षा की अवधि 3 घंटे है । आपको परीक्षा की समाप्ति के पश्चात् परीक्षा कक्ष छोड़ने के पूर्व निरीक्षक को (a) बहुविकल्पीय प्रश्नों वाले प्रश्न-पत्र का Part-I और (b) वर्णनात्मक उत्तरों वाली उत्तर-पुस्तिका मुख्य पृष्ठ सहित जमा कराना आवश्यक है ।
10. उपर्युक्त दर्शित सामग्री की प्राप्ति पर, निरीक्षक प्रवेश-पत्र के पृष्ठ 2 पर अभिस्वीकृति प्रदान करेगा ।
11. अभ्यर्थी नकल करते या किसी प्रकार की सहायता देते या प्राप्त करते या निरीक्षक के निर्देशों की अवज्ञा करते पाया गया, तो परीक्षा से निष्कासित कर दिया जाएगा और इसके अतिरिक्त दंडात्मक कार्यवाही के लिए भी उत्तरदायी होगा ।

भाग – II — 70 अंक

1. Section-A में 1-4 तक प्रश्न हैं । प्रश्न संख्या 1 अनिवार्य है तथा शेष 3 प्रश्नों में से किन्हीं 2 का उत्तर देना है ।
2. Section-B में 5-8 तक प्रश्न हैं । प्रश्न संख्या 5 अनिवार्य है तथा शेष 3 प्रश्नों में से किन्हीं 2 का उत्तर देना है ।
3. उन परीक्षार्थियों को छोड़कर जिन्होंने हिन्दी माध्यम चुना है, प्रश्नों के उत्तर केवल अंग्रेजी में ही देने हैं । वह परीक्षार्थी जिसने हिन्दी माध्यम नहीं चुना है, यदि हिन्दी में उत्तर देता है, तो उसके हिन्दी में दिये गये उत्तरों का मूल्यांकन नहीं होगा ।
4. कार्यशील टिप्पणियाँ उत्तर का भाग मानी जायेगी ।