**Corporate Finance**

**April 2023 Examination**

**Q1. Calculate WACC with the following information. Which source of funding is most desirable and why? (10 Marks)**

**PQR Ltd. is coming out with a new equity issue of Rs. 10 lacs par value Rs. 100/share. The cost of issuing external equity is around 5%. Shareholders expect a return of 16% p.a. for the risk involved in parking their funds in PQR Ltd.**

**PQR Ltd. also has retained earnings of Rs. 8 lacs as on date.**

**It has a long term debt of Rs. 5 lacs taken at 8% p.a. Tax rate is @ 30%**

**Preference shares capital of par value Rs. 6 lacs (Rs. 100 each), yield a return of 10% p.a. Market value of each equity share is Rs. 105 per share and that of Preference shares is Rs. 125/share.**

**Ans 1.**

**Introduction**

WACC, also weighted ordinary cost of capital, represents a company's traditional after-tax value of money from all sources, including preferred stock, commonplace stock, different types of debt, and bonds. WACC may be defined because of the typical fee a company expects to pay to finance its assets.

WACC is a traditional manner of deciding the specified price of return (RRR) as it expresses, in one range, the go-back that each shareholder and bondholders call for to provide the firm with the capital. A company's WACC is better if its debt is seen as risky or if its stock is

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**Q2. What is a Cash Cycle? Explain. Calculate using the following information. (Assume 360 days in a year). (10 Marks)**

|  |  |
| --- | --- |
| **Opening Balances** |  |
| **Raw Material** | **1,00,000** |
| **WIP** | **45,000** |
| **Finishes Goods** | **1,35,000** |
| **Debtors** | **6,00,000** |
| **Creditors** | **8,60,000** |
|  |  |
| **Closing Balances** |  |
| **Raw Material** | **2,00,000** |
| **WIP** | **65,000** |
| **Finishes Goods** | **1,25,000** |
| **Debtors** | **5,45,000** |
| **Creditors** | **9,75,000** |
|  |  |
| **Costs Incurred during the year** |
| **Manufacturing Costs** | **11,60,000** |
| **Excise Duty** | **18,80,000** |
| **Selling and Distribution Expenses** | **6,20,000** |
| **Admin. Overheads** | **2,00,000** |
|  |  |
| **Total Sales** | **2,01,96,800** |
| **Total Purchases** | **1,46,00,000** |

**40% of sales are on credit and 70% of purchases are on credit**

**Ans 2.**

**Introduction**

CCC stands for cash conversion cycle, also called the coins cycle- a metric stating the number of days it takes a firm to convert the cash it spends on raw materials again into coins through selling its goods. The shorter a firm's CCC, the less time it has cash connected up in inventory and accounts receivable.

The cash cycle is an essential running capital metric for all firms that buy and manipulate raw materials or stock. It indicates operational effectiveness, everyday monetary fitness, and

**Q3a. What is Net Working Capital? Explain each element briefly. Look at the following Balance sheet extract and identify each element of the working capital and calculate NWC. (5 Marks)**





**Ans 3a.**

**Introduction**

Net working capital is the difference between a company's current liabilities and assets on its balance sheet. It is a measure of a firm's liquidity and capability to meet short-term duties in addition to funding the company's operations. The proper position is to have fewer current liabilities than present-day assets and thus have positive internet working capital stability.

**Q3.b. With the following data, calculate DSO and Debtor Turnover Ratio. Explain the importance of each and make inferences. (5 Marks)**

**Rs. In Crores**

|  |  |  |
| --- | --- | --- |
|  | **FY 2021-22** | **FY 2020-21** |
| **Sales** | **1,01,000** | **87,255** |
| **Receivables** | **36,347** | **33,331** |
| **0% of the sales are on credit basis** |  |  |

**Ans 3b.**

**Introduction**

Income great day, DSO measures the standard number of days a business takes to collect income payment. DSO is usually determined on an annual, quarterly, and monthly basis.2

To calculate DSO, divide the average accounts receivable throughout the required duration using the absolute value of income in credit during the exact length. Then multiply the