**STRATEGIC FINANCIAL MANAGEMENT**

**April 2024**

# QUESTION 1

# Alpha Ltd is contemplating an investment in a new piece of machinery. Based on the details given below calculate the cash flows and perform the capital budgeting analysis. Would you go ahead with the investment?

**Initial Investment Cost: Rs.100,000**

**Useful Life of Machinery: 5 years**

**Annual Revenue: Rs. 40,000**

**Annual Operating Costs: Rs. 10,000**

**Annual Depreciation (Straight-line method): Rs. 20,000**

**Tax Rate: 30%**

**Discount Rate: 10%**

# Answer:

|  |  |
| --- | --- |
| **ALPHA LTD:** |  |
| **CALCULATIONS:** |  |
| Initial Investment Cost | 100,000 |
| Useful Life of Machinery | 5 |
| Annual Revenue | 40,000 |
| Annual Operating Costs | 10,000 |
| Annual Depreciation (Straight-line method) | 20,000 |
| Tax Rate | 30% |
| Discount Rate | 10% |
| Annual Cash Flows | 10,000 |
| Depreciation Expense | 20000 |

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**QUESTION 2**

**The current stock price of XYZ Inc is Rs. 100 per share. Based on the information given below calculate the total profit or loss for an investor who buys one call option contract (representing 100 shares) and exercises it at expiration, depending on different scenarios of the stock price at expiration.**

**Option Type: Call Option**

**Strike Price: Rs.105 per share**

**Premium (Cost of the Option): Rs.5 per share**

**Expiration Date: 30 days from now**

**Answer:**

|  |  |
| --- | --- |
| **XYZ INC:** |  |
| **CALCULATIONS:** |  |
| Current stock price | 100 |
| Option type | Call Option |
| Strike price | 105 |
| Premium (Cost of the Option) | 5 |
| Expiration date | 30 |

# QUESTION 3(A)

# Maurya Ltd issues bonds with a face value of INR 1000, coupon rate 6% (annual coupon payment) with time to maturity as 5 years. Compute the Yield to Maturity (YTM) assuming the current market price of the bond is INR 950.

**Answer:**

|  |  |
| --- | --- |
| **MAURYA LTD:** |  |
| **CALCULATIONS:** |  |
| Face value of the bond (FV) | 1000 |
| Coupon rate © | 6% |
| Time to maturity (N) | 5 |

# QUESTION 3(B)

**Micro Ltd considering its dividend policy. The current earnings per share (EPS) are Rs. 5. The shared holders of Micro Ltd expect a return (ke) of 10%. Assuming the retention ratio (b) is 60%, what would be the optimal dividend payout ratio as per Walter’s Model?**

**Answer**

Mikro Ltd. has to choose how it will give out dividends. How happy shareholders are and how much the company is worth in the long run will depend on this choice. To find the right dividend distribution ratio, the company needs to use Walter's Model and the preferences of its shareholders. Its EPS is Rs. 5. People who own shares in Micro Ltd. expect a 10% return, or Ke,