Karunya University
(Karunya Institute of Technology and Sciences)
(Declared as Deemed to be University under Sec.3 of the UGC Act, 1965)

End Semester Examinations - 2015-16 MBA Trimester - May 2016

15MS3013 Corporate Finance

Set A

Time : 3 hrs
Total Marks: 100

1. Merger and Acquisition decisions are viewed as corporate restructuring decision, strategic decision, and investment decision? Elaborate. (10 marks)

   The direction, scale, and sectors of M&A deals involving Indian firms have undergone significant change over the years. Analyse the statement and discuss the key reasons responsible for the increasing scale of M&A activities involving Indian firms. (10 marks)

OR

2. Two companies A and B decide to merge. The relevant financials of the two firms are as follows: (20 marks)

	Firm A	**Firm B**
Total Earnings, E (Rs. Lakh)	210	60
No. of shares outstanding, S (in lakh)	20.5	8
Earnings per share, EPS (Rs,)	10.24	7.50
Price earnings ratio, P/E (times)	10	7
Market price per share	40	14

   Determine the exchange ratio for Firm A and Firm B using LG model.

3. The Managing Director of AB Ltd also stated 'When it comes to choosing between two technologies, it is always advisable to choose the more expensive and longer lasting technology as compared to the cheaper equipment with lesser useful life because expensive technology is always priced so as to outperform the economic benefits of the cheaper machine. As such there is no need to evaluate the two competing technologies.' Comment on the statement made by the Managing Director. (20 marks)

OR

4. Certainty Enterprises are considering two projects A and B with initial outlays of Rs 50 lakh and Rs 60 lakh. The inflows of the projects are sensitive to the economic conditions that are expected to prevail over 10 years; the life of each of the project. The cash flows for the 4 different economic conditions of Excellent, Good, Average and Poor with their respective probabilities are as below:

		Cash Flows ((Rs. Lakh)	
	Probability	**A**	**B**
Initial Cost	Certain	-50.00	-60
Excellent	0.30	15.00	18.00
Good	0.20	12.00	14.00
Average	0.30	10.00	12.00
Poor	0.20	8.00	7.00

   What is the net present value of the projects under the different economic conditions?

   What NPV You expect for each of the project?

   What are the risk associated with each of the projects in terms of standard deviation and co-efficient of variation?

   Which of the two projects would you choose? (20 marks)

5. What is Modified Internal Rate of Return (MIRR) and how it is calculated? Discuss the rationale behind its calculation. (20 marks)

OR

6. **A firm in the business of manufacture of automobile components is considering two mutually exclusive technologies for manufacture of hydraulic brakes. These two technologies are designated as Option A and Option B with project cost of Rs. 1600 lakh and Rs. 1850 lakh. Depending upon various features of the product obtainable from the two technologies the firm has developed a forecast of cash flows for 5 years. i.e., the life of each project. These cash flows are as below:**

(Rs. Lakh)		
Year	Option A	Option B
1	350.00	675.00
2	475.00	575.00
3	625.00	725.00
4	575.00	350.00
5	350.00	400.00

Option A is a familiar technology and therefore the firm feels that the current cost of capital of 13% is the appropriate discount rate. However, Option B is considered riskier than the Option A and therefore firm would like to use a discount rate of 15%, some what higher than the current cost of capital.
(20 marks)

Find out the following:

NPVs of the Options A and B

IRR of the Options A and B

Which option would you consider with NPV rule and the IRR rule.

Firm believes that under most probable circumstances it would be able to re-invest the internally generated cash flows of the project at 14%. What would be your decision if that be the case?

7. Describe the adjusted balance sheet approach to valuation. What are the limitations of such a valuation? (20 marks)

OR

8. Innovative Bridges Limited (IBL) is planning to buy a specialized crane for use in various projects. The manufacturer of the crane has offered it on lease for a period of 4 years at a lease rent of Rs. 20 lakh per annum payable in advance. The lease rent includes cost of operator, maintenance, and insurance. Alternatively, IBL can buy the crane outright at Rs. 50 lakh, but will have to bear the cost of operator, estimated at Rs. 5 lakh per annum with an annual increase of 10%, and maintenance cost, estimated at Rs. 6 lakh for the first year, with 20% annual increase. If the crane is bought outright the manufacturer has indicated willingness to take back the crane for furbishing at Rs. 15 lakh. Cranes are grouped under items eligible for 35% depreciation on WDV basis. IBL can arrange a loan at 10%, while WACC is placed at 12%. IBL pays tax of 40%. Find whether the firm should lease the crane or buy it. (20 marks)

9. **CASE STUDY: (Compulsory)** **(20 marks)**

Amusement Parks Limited owns an entertainment park and contemplating an expansion by adding few more rides in the park. Their current balance sheet on book values and market values is given:

Balance Sheet (Rs crore)	**Book value**	**Market Value**
Fixed Assets	110.00	149.17
Net Current Assets	7.50	7.50
Total	**117.50**	**156.67**
Equity Capital	94.00	133.17
Debt	23.50	23.50
Total	**117.50**	**156.67**

Based on market weights the firm has a debt ratio of 15% and beta of its equity is 1.20. The risk free rate is 6% while market risk premium is 8%. Corporate tax applicable is 35% and post-tax cost of its debt is 9%. The depreciation charged by the firm is 5.5% of the net fixed assets. The capital expenditure plan aggregating Rs. 135 crore spanning next 4 years is as below:

Year	1	2	3	4
Addition during the year (Rs. Crore)	20.00	30.00	35.00	50.00

Besides capital expenditure the firm would have nominal working capital at 5% of the total revenue.

The park earns its revenues from entry fee, tickets for rides, rentals from the few kiosks in the park, and the catering. The growth rates and the first year projections net of entertainment tax are projected as below:

Assumptions	**Growth % for next 4 years**	**First year projection (Rs. In crore)**
Revenue		
Gate Money	10%	5.00
Fee from the Rides	30%	60.00
Rentals from Kiosk owners	2%	3.00
Food (% of fee from ride)	65%	39.00
Cash Expenses	60%*	
*(of revenue and to decline by 2% every year till the 4th year)		

After four years the free cash flow to the firm are expected to grow at 6% annually forever. Find out the value of the firm and its equity.

Wishing you All the Best
