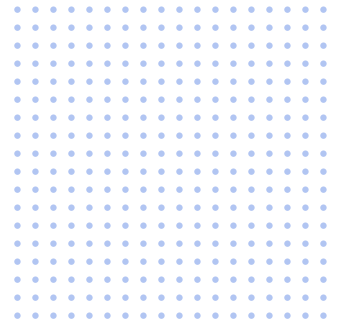




FOR CA FINAL EXAM PREPARATION

# CA Final 2024 Question Paper · Paper 2 Advanced Financial Management

EXAM

CA Final

YEAR

2024

TYPE

Question Paper

SUBJECT

Paper 2 Advanced Financial Management

DATE

November 2024

FINAL EXAM  
PAPER - 2  
Advanced Financial Management

BQK2

05 NOV 2024

Roll No. ....

Total No. of Questions : 6

Total No. of Printed Pages : 8

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 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 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 I 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 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 or having/using mobile phone or smart watch will be expelled from the examination and will also be liable for further punitive action.

## PART - II

70 Marks

1. Question paper comprises 6 questions. Answer Question No. 1 which is compulsory and any 4 out of the remaining 5 questions.
2. Working notes should form part of the answer.
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.

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( 2 )

**BQK2****PART II**

1. (a) Following is the data regarding Three Securities.

| Stock                 | Expected Return (%) | Std. deviation | Correlation with the Market return |
|-----------------------|---------------------|----------------|------------------------------------|
| A                     | 19%                 | 2.50           | 0.840                              |
| B                     | 13.50%              | 2.00           | 0.540                              |
| C                     | 11.00%              | 0.80           | 0.975                              |
| Market risk           | —                   | 1.20           | —                                  |
| Market rate of return | 14.00%              | —              | —                                  |
| Risk free rate        | 9.00%               | —              | —                                  |

- (i) Advise which of the above stocks are over, under or correctly valued in the market?
- (ii) What will be strategy you would like to recommend? (6 Marks)
- (b) A firm is considering a proposal to set up a cement manufacturing plant with an initial investment of ₹ 150 crore. The firm has the option to abandon the project after one year by selling it to a competitor for ₹ 100 crore if the market conditions are unfavorable and the demand is low, the project's value will decline by 60%. However, if the market conditions turn out to be favorable and the demand for cement is high, the value of the project at the end of year 1 will increase by 50%.
- Given that the risk free rate of interest as 8%, what will be the value of the abandonment option and the value of the project with abandonment option? (4 Marks)
- (c) This decision determines the division of earnings between payments to shareholders and reinvestment in the company. What this decision is called? What are other decisions falling in this strategy? Briefly explain. (4 Marks)

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2. (a) Mr X invested ₹ 1,00,000 at a face value of ₹ 10 per unit in a dividend reinvestment plan in a mutual fund during its initial public offering on 1<sup>st</sup> July, 2022. On 31<sup>st</sup> March, 2023, the mutual fund declared a dividend of 10%. At that time Mr X calculated his holding period return to be 115%.

On 31<sup>st</sup> March, 2024 the mutual fund declared a dividend of 20% and Mr. X redeemed all his investment and calculated his holding period return to be 193.134%.

You are required to calculate

(i) The NAVs as on 31.03.2023 and 31.03.2024.

(ii) Calculate the total units redeemed. (6 Marks)

- (b) PQ Ltd. expects sales of ₹ 100 lakhs in the year 1. The same will increase by ₹ 20 lakhs per year over the next four years. At the end of 5 years the project would be wound up. The Depreciation will be charged at 20% p.a. on straight line method. The expenses excluding the depreciation will be 40% of the sales. There will be no salvage value of the plant. PQ Ltd. proposes to invest in the plant an amount where the Net Present Value will be Zero.

Corporate Tax rate is 30%.

You are required to calculate the investment which can be made in the plant.

(8 Marks)

3. (a) XY Ltd. is planning to expand its operations in view of growing demand for its products. For this purpose, it is considering to borrow an amount of ₹ 100 crores for a period of 3 months in the coming 6 months' time from now. The current rate of interest is 8% per annum but due to inflation it may go up in 6 months' time. The company wants to hedge itself against the likely increase in interest rate.

The company's Bankers quoted an FRA (Forward Rate Agreement) at 8.20% per annum.

You are required to calculate due to FRA:

(i) The actual interest rate if the Banker pays to XY Ltd. an amount of ₹ 9,78,952.52

(ii) The actual interest rate if XY Ltd. will pay to the Banker a sum of ₹ 9,80,872.98 (6 Marks)

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- (b) On 20.10.2024, the balance in NOSTRO account with XYZ Bank in London was GBP 80000 and the balance in overbought was GBP 50000. During the day the following transactions have taken place.

| <u>Events</u>                        | <u>Amount (GBP)</u> |
|--------------------------------------|---------------------|
| DD Purchased                         | 25,000              |
| Purchased a bill on London           | 75,000              |
| Sold forward TT                      | 50,000              |
| Forward purchased contract cancelled | 25,000              |
| Remitted by TT                       | 42,500              |
| Draft in London cancelled            | 20,000              |

What steps would you take, if you are required to maintain a credit balance of GBP 10,000 in the NOSTRO account and keep as overbought position on GBP 32,500?  
(8 Marks)

4. (a) On January 1, 2023 an investor has a portfolio of 5 securities as given below:

| Security | Price (Rs.) | No. of shares | Beta |
|----------|-------------|---------------|------|
| A        | 612.65      | 3000          | ?    |
| B        | 334.20      | 5000          | 1.15 |
| C        | 454.45      | 6000          | 0.40 |
| D        | 775.10      | 10000         | 0.95 |
| E        | 781.05      | 3000          | 0.85 |

Portfolio beta is 0.859.

The cost of capital to the investor is 10.5% p.a.

You are required to calculate:

- The beta of Security A.
- The theoretical value of the Nifty futures for February, 2023. Current value of Nifty 6500.
- The number of contract of Nifty the investor needs to sell to get a full hedge until February, for his portfolio, if the current value of Nifty is 6500 and Nifty futures have a minimum trade lot requirement of 200 units. Assume that the Futures are trading at their fair value.
- What will be new beta if 4 Future contracts are sold to the investors?

No. of days in a year be traded as 365 days

Given:  $\ln(1.105) = 0.0998$ ,  $e^{0.015858} = 1.01598$  and  $e^{0.01668} = 1.01682$  (6 Marks)

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- (b) Economic Value Added (EVA) of ABC Ltd was ₹ 31,10,000.

Following is the capital structure of ABC Ltd. at the end of current financial year:

Equity (Share Capital + Reserves & Surplus) ₹ 170 lakhs

Debt (Coupon Rate 10%) ₹ 80 lakhs

Invested Capital ₹ 250 lakhs

Following data is given to estimate the cost of equity capital :

Beta of ABC Ltd. 0.90

Risk-free rate (i.e. current yield on Govt. Bonds) 8%

Average market risk premium 10%

Economic Value Added (EVA) of ABC Ltd was ₹ 31,10,000.

The applicable corporate income tax rate is 30%.

You are required to calculate the Profit After Tax of ABC Ltd. (4 Marks)

- (c) Succession planning is a good way for companies to ensure that businesses are fully prepared to promote and advance all employees—not just those who are at the management or executive levels. (4 Marks)

Do you agree? Justify.

**OR**

- (c) MN Bank entered into a plain Vanilla Swap through an OIS (Overnight Index Swap) on a principal of ₹ 5 crores and agreed to receive MIBOR overnight floating rates for a fixed payment on the principal. The swap was entered into on Monday 2<sup>nd</sup> August and was to commence on 3<sup>rd</sup> August and run for a period of 7 days.

Respective MIBOR rates for Tuesday to Monday were

8.00%, 8.25%, 8.15%, 7.90%, 7.95%, 8.15%.

MN Bank received ₹ 275 net of settlement.

Working is to be rounded off. Bank does not accept decimal values.

You are required to calculate the fixed rate and Interest under both legs where Sunday is holiday.

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5. (a) PQR Ltd. is considering a project in US, which involve an initial investment of ₹ 124.50 Crore. The project will have useful life of 5 years. Current spot exchange rate is INR/USD is 83. The risk free rate in US is 4.186 % and the same in India is 6.9768%. Cash inflows in USD from the project are as follows

| Year        | 1         | 2         | 3         | 4         | 5         |
|-------------|-----------|-----------|-----------|-----------|-----------|
| Cash inflow | 30,00,000 | 40,00,000 | 50,00,000 | 60,00,000 | 70,00,000 |

PQR Ltd. is expecting net surplus of ₹ 1858.08 lakh to be received after closure of the project. There is no salvage value. PQR Ltd. want to take a forward cover to protect itself from exchange rate fluctuations.

| n               | 1     | 2     | 3     | 4     | 5     |
|-----------------|-------|-------|-------|-------|-------|
| PVIF(6.976%, n) | 0.935 | 0.874 | 0.817 | 0.764 | 0.714 |
| PVIF(4.186%,n)  | 0.959 | 0.921 | 0.884 | 0.849 | 0.815 |
| PVIF(12%, n)    | 0.893 | 0.797 | 0.712 | 0.636 | 0.567 |
| PVIF(15%, n)    | 0.870 | 0.756 | 0.658 | 0.572 | 0.497 |

You are required to recommend the INR/USD rate for the forward cover? (6 Marks)

- (b) AMN Ltd. has surplus cash of ₹ 200 lakhs and wants to distribute 30% of it to the shareholders. The company decides to buy back shares. The Finance officer of the company estimates that it share price after repurchase is likely to be 15% above the buyback price if the buyback route is taken. The number of shares outstanding at present is 15 lakhs and the current EPS is ₹ 3.00.

Bought Back price is to be rounded off to one decimal point.

You are required to determine.

- The price at which the shares can be repurchased, if the market capitalisation of the company should be ₹ 250 lakhs after buyback.
- The number of shares that can be repurchased.
- The impact of share repurchase on the EPS, assuming that net income is the same.

(4 Marks)

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**BQK2**

- (c) Mohan buys 10,000 shares of X Ltd. @ ₹ 25 per share whose beta value is 1.5 and sells 5,000 shares of A Ltd. @ ₹ 40 per share having a beta value of 2. He obtains a complete hedge by buying 25 Nifty Futures. He closes out his position at the closing price of the next day when the share of X Ltd. has fallen by 4% and Nifty Futures has dropped by 2.50%. In the process he suffered a loss of ₹ 16625.

You are required to determine

- (i) The value of the Nifty future
- (ii) Initial cash outlay
- (iii) Cash inflow at the close out
- (iv) Percentage Gain/ loss to Shares of A Ltd. at the time of closure (4 Marks)

6. (a) A Portfolio Manager (PM) has three mutual funds in his portfolio. Following are the details of these three mutual funds :

| Particulars        | Growth fund | Balanced fund | Regular fund | Market |
|--------------------|-------------|---------------|--------------|--------|
| Average Return (%) | 7.5         | 6.3           | 5.4          |        |
| Variance           |             |               |              | 50.41  |
| Sharpe Ratio       | -0.15       | -0.36         | -0.48        |        |
| Treynor's Ratio    | -2          | -3            | -4.80        |        |

The yield on 182 days Treasury bill is 9 per cent per annum.

You are required to calculate

- (i) Variance of the Funds
  - (ii) Coefficient of Determination of the Funds (8 Marks)
- (b) True Life Inc., a US based company, has won a contract to implement a project in India. The project will require an initial investment of ₹ 8000 million. The whole project along with the equipment will be sold to the Indian Government for ₹ 9600 million in one-year time. Since the Indian Government will pay for the amount in Indian Rupee (₹), the company is worried about exposure due to exchange rate volatility.
- (i) Construct a swap that will help the True Life Inc. to reduce the exchange rate risk.
  - (ii) Assume that the Indian Government offers a swap at spot rate which is INR/USD 80 in one year. The spot rate after one year is expected to be INR/USD 84. Further, you may also assume that the True Life Inc. can also take a USD loan at 6% per annum. **ADVISE** whether the company should opt for this option or just do nothing. (6 Marks)

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**SPACE FOR ROUGH WORK**

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