



BUSINESS STUDIES

BOOKS - ARIHANT BUSINESS STUDIES (HINGLISH)

Financial Management

Check Point 1

1. State two purposes of business finance.



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2. List two functions of a finance manager.



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3. State two derivative objectives of financial management.



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4. Give one example of long-term investment



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Check Point 2

1. what does investment criteria involve ?



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2. When is the fixed operating burden of a company less ?



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3. How does the terms of loan agreement affect dividend decision ?



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4. State one major objective of financial planning ?



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5. What are long-term plans ?



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Check Point 3

1. what does owen's fund consist of ?



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2. What does debt consist of ?



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3. What is optimal capital structure ?



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4. When is Trading on Equity unfavourable ?



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5. What is DSCR ?



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Check Point 4

1. How are capital budgeting decisions irreversible ?



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2. How is fixed capital affected by choice of technique of production ?



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3. State two examples each of current assets and current liabilities.



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4. Define operating cycle.



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1. The Cheapest source of finance is

- A. debenture
- B. equity share capital
- C. Preference share
- D. retained earnings

Answer: D



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2. A decision to acquire a new and modern plant to ungrade an old one is a

- A. financing decision
- B. working capital decision
- C. investment decision
- D. None of the above

Answer: C



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3. Other things remaining the same, an increase in the tax rate on corporate profits will

- A. make the debt relatively cheaper
- B. make the debt relatively the deareer
- C. have no impact on the cost of debt
- D. we can't say

Answer: A



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4. Companies with a higher growth pattern are likely to

A. pay lower dividends

B. pay higher dividends

C. dividends are not affected by growth considerations

D. None of the above

Answer: A



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5. Financial leverage is called favourable if

A. Return on investment is lower than the cost of debt

B. RoI is higher than the cost of debt

C. Debt is easily available

D. If the degree of existing financial leverage is low

Answer: B



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6. Higher debt- equity ratio results in

- A. lower financial risk
- B. higher degree of operating risk
- C. higher degree of financial risk
- D. higher EPS

Answer: C



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7. Higher working capital usually results in

A. Higher current ratio, higher risk and higher profits

B. lower current ratio, higher risk and profits

C. higher equity, lower risk and lower profits

D. lower equity, lower risk and higher profits.

Answer: A



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8. Current assets are those assets which get converted into cash

- A. Within six months
- B. within one year
- C. between one and three years
- D. between three and five years

Answer: B



9. Financial planning arrives at

A. minimising the external borrowing by resorting to equity issues

B. entering that the firm always have singinificantly more fund than required so that there is not paucity of founds.

C. ensuring that the firm faces neither a shortage nor a glut of unusable funds

D. doing only what is possible with the funds that the firms has at disposal

Answer: C



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10. Higher dividend per share is associated with

A. high earnings , high cash flows, unstable earnings and higher growth

opportunities.

B. higher earnings, high cash flows, stable earnings and higher growth opportunities

C. high earnings , high cash flows, stable earnings and lower growth opportunities

D. high earnings , low cash flows, stable earnings and lower growth opportunities.

Answer: C



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11. A fixed asset should be financed through

- A. a long -term liability
- B. a short -term liability
- C. a mix of long and short -term liabilities
- D. None of the above

Answer: A



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12. Current assests of a business firm should be financed through

A. current liability only

B. long -term liability only

C. both types (i.e long and short -term liabilities)

D. None of the above

Answer: C



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Ncert Folder Short Answer Type

1. What is meant by capital structure ?

or

Define capital structure.



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2. Discuss the two objectives of financial planning .

or

What is meant by 'financial planning '? State its objectives.

or

'Financial planning is a financial blueprint of an organisation's future operations .Explain the twin objectives of financial planning in the light of this statement



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3. What is financial risk ? Why does it arise ?



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4. Define a current asset. Give four examples to such assets.



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5. Financial management is based on three broad decisions. What are these ?

or

Every manager has to take three major

decisions while performing the finance functions . Explain them .



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6. What are the main objectives of financial management ? Briefly explain.



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7. How does working capital affect both the liquidity as well as profitability of a business ?



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Ncert Folder Long Answer Type Questions

1. what is working captial ? How is it calculated
? Discuss five important determinats of
working capital requirement .



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2. Explain any four factors affecting the 'working capital requirement' of a company.



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3. You are the financial manager of a newly established company. The directors have asked you determine the amount of working capital requirement for the company. Explain any four factors that you will consider while

determining the working capital requirement for the company .



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4. Capital structure decision is essentially optimisation of risk-return relationship comment .



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5. A capital budgeting decision is capable of changing the financial of a business. Do you agree? Why or why not ?



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6. Discuss in brief the concept of investment decision and why capital budgeting decisions are crucial in nature ?



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7. Explain the factors affecting the dividend decision.



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8. Explain the following as factors affecting 'dividend decision.

(i) Stability of dividend

(ii) Shareholders' preference

(iii) Legal constraints

Access to capital market



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9. Explain the following as factors affecting dividend decision

- (i) Stability of earnings
- (ii) Growth opportunities
- (iii) Cash flow position
- (iv) Taxation policy



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10. Identify the financial decision which determines the amount of profits earned to be distributed and to be retained in the business. Explain four factors affecting this decision.



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11. You are the finance manager of a company your board of directors have asked you to decide the dividend policy of a company .

Explain the factors which you will consider while determining the dividend policy.



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12. Explain and four factors of ' dividend decision of a company.



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13. Explain the term ' trading on equity' why. When and how can it be used by a business

organisation ?



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14. How does 'trading on equity, affect the choice of capital structure of a company ?

Explain with the help of suitable example.



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15. How are the shareholders likely to gain with loan components in capital employed ?

Explain with suitable example.



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Ncert Folder Case Problems

1. What is the role and objectives of financial management for this company ?



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2. Explain the importance of having a financial plan for this company . Give an imaginary plan to support your answer.



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3. What are the factors which will affect the capital structure of this company ?



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4. Keeping in mind that it is a highly capital intensive sector, what factors will affect the fixed and working capital ? Given reasons with regard to both in support of your answer.



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Chapter Practice Mcq

1. Financial management helps in

A. reducing the cost of funds

B. keeping the risks under control

C. achieving effective deployment of funds

D. All of the above

Answer: D



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2. In financial management , the procurement of funds is done for

A. long- term needs only

B. short-term needs only

C. Both (a) and(b)

D. maximising risks

Answer: C



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3. Decisions related to investment in fixed assets are popularly known as

A. business finance decisions

B. financial management

C. capital budgeting decisions

D. None of the above

Answer: C



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4. To maximise the wealth of owners (i.e shareholders) means

A. to minimise the risk of the shareholders

B. to maximise the shares of shareholders

C. to maximise the current price of equity
shares of the company

D. to minimise the tax in the hands of
shareholders

Answer: C



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5. Financial decisions impacts which of the following items of profit and loss account ?

A. interest

B. profit

C. Tax

D. All of the above

Answer: D



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6. Dividend is that portion of profit, which is distributed to the shareholders and undistributed profit which remains in the business is known as

A. earning

B. equity

C. retained earning

D. interest

Answer: C



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7. Debt is considered to be cheaper than equity because for borrowers, interest on debentures is a while dividend on equity is not.

- A. exempt from tax
- B. deductible expenditure
- C. non-deductible espenditure
- D. None of the above

Answer: B



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8. The risk of default on payment of borrowed funds is known as

A. operating risk

B. financial risk

C. business risk

D. None of these

Answer: B



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9. Though the dividends are free of tax in the hands of shareholders, which tax is levied on companies for the dividend ?

- A. Dividend payout tax
- B. Dividend allocation tax
- C. Dividend distribution tax
- D. None of the above

Answer: C



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10. In which case, a company should go to opt for equity rather than debt ?

- A. if the stock market is rising
- B. if the firm has higher operating cost
- C. if cash flow position is stronger
- D. both (a) and (b)

Answer: D



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11. Financial planning helps in

- A. running the business smoothly
- foreceasing
- B. avoiding business shocks and surprise
- C. coordinating various business function
- D. All of the above

Answer: D



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12. The objective of financial planning is

- A. to ensure timely availability of funds
- B. to avoid idle funds
- C. both (a) and (b)
- D. to maximise financial costs

Answer: C



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13. Short-term plans are also known as..... And are made for a period of

A. capital budgeting programs , two years

B. captials budgeting programs, one year
or less

C. budgets, two years

D. budgets, one year or less

Answer: D



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14. Long -term financial planning is done ofr

- A. zero to one year
- B. more than one year
- C. ten to twenty years
- D. twenty to thirty years.

Answer: B



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15. The process of estimating the financial requirements of an organisation specifying the sources of funds and ensuring that enough funds are available at the right time is called

A. financial management

B. financial planning

C. financial decision

D. business finance

Answer: B



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16. Higher working capital usually results in

A. higher current ratio, higher risk and higher profits

B. lower current ratio, higher risk and profits

C. higher equity, lower risk and higher profits

D. Lower equity, lower risk higher profits.

Answer: A



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17. Which of the following statement is incorrect ?

A. Current assests are usually more liquid
than fixed asserts

B. Current assets contribute less to the
profits than fixed assets

C. B/R, debtors, stock, etc, are fixed assets

D. fixed assets are financed through long-term liabilities

Answer: C



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18. Company 'A' has profit after tax, ₹1,50,000 and its number of equity shares is 10,000. Company 'B' has profits after tax, ₹1,20,000.

and its numgber of shares is 12,000. which company has better EPS and how much ?

A. Company 'A' ₹ 10

B. Compnay 'A' ₹ 15

C. Company 'B' ₹ 10

D. Company 'B' ₹ 12

Answer: B



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19. Calculate the profits before interest and tax from the following information

Profit after tax= ₹ 1,50,000. Interest.

A. ₹ 3,60,000

B. ₹ 3,00,000

C. ₹ 45,000

D. ₹1,05,000

Answer: A



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20. Calculate the net working capital from the following information

Sundry Creditors = ₹ 30,000 , Cash = ₹ 25,000 ,
prepaid expenses = ₹5,000

Sundry Creditors = ₹ 17,000 , Outstanding
expenses = ₹ 3,000 , Bills payable = ₹ 8,000.

A. ₹32,000

B. ₹ 30 ,000

C. ₹ 88,000

D. ₹ 60,000

Answer: A



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Chapter Practice Very Short Answer

1. What is meant by ' financial management ' ?



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2. Define financial management





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3. What is the primary objective of 'financial management ?



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4. State the objective of financial management

.



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5. What is business finance ?



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6. How is the overall financial health of business determined ?



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7. Wealth maximisation objective of financial management leads to achievements of other objectives too. List any two such objectives .



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8. The primary aim of financial management is to maximise shareholders' wealth of Beta Constructions Pvt Ltd. Identify any two aims that would help the company to achieve its objectives.



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9. There are three major decisions which an organisation has to take in respect of financial management . State these decisions.



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10. What do you mean by investment decision ?



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11. What is the other name used for long -term investment decision ?



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12. What do you mean by financing decision ?



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13. What is dividend ?



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14. What do you mean by divided decision ?



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15. What do you understena by flatation cost ?



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16. According to you, which is the cheapest source of finance ?



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17. Which is the riskless source of finance ?



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18. which company is in a position to declare high dividends ?



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19. Define financial planning .



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20. What are borrowed funds ?



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21. Even though, cost of debt, is lower than the 'cost of equity share capital. Give reasons,

even then a company cannot work only with debt.



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22. What is an important determinant of company's ability of trading on equity ?



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23. What does higher business risk indicate ?



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24. Define fixed assests.



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25. What is operating cycle ?



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26. Name any two essential ingredients of sound working capital management . \



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27. What is business cycle ?



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28. Name and state the aspect of financial management that enables to foresee the fund requirements both in terms of the quantum and the timings.



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29. Name and state the aspect of financial management that provides a link between investment and financing decisions.



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30. What provides a link between investment and financing decisions on a continuous basis ?



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31. It is essentially a blueprint of an organisations future operations related to finance . Identify it.



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32. The finance manager of Aerial Automobiles has made a detailed plan analysing the minutest financial needs of the firm in the coming six months. He also analyses the sources from where such fund requirement

will get met. Name the process the finance manager is involved in.



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33. Which component of capital structure determines the overall financial risk in an organisation ?



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34. Name the concept which increases the return on equity shares with a change in the capital structure of a company.



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35. The size of assets, the profitability and competitiveness are affected by one of the financial decisions. Name and state the decision.



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36. If a finance manager has taken the decision to invest in a long-term project, what is this decision called ?



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37. A company wants to establish a new unit and purchases a machinery of worth ₹10 lakh. Identify the type of decision involved.



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38. Which decision is involved in launching a new product line or opening a new branch ?



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39. State, why the need of working capital for a service industry, is different from that of a manufacturing industry ?



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40. Radhika and Vani who are young fashion designers left their job with a famous fashion designer chain to set-up a company 'Fashionate Pvt.Ltd. ' They decided to run a boutique during the day and coaching classes for entrance examination of National Institute of Fashion Designing in the evening. For the coaching centre they hired the first floor of a nearby building. Their major expense was money spent on photocopying of notes for their students. They thought of buying a photocopier knowing fully that their scale of

operations was not sufficient to make full use of the photocopier.

In the basement of the building of Fashionate Pvt. Ltd.' Praveen and Ramesh were carrying on a printing and stationery business in the name of 'Neo Prints Pvt.Ltd'. Radhika approached Praveen with the proposal to buy a photocopier jointly which could be used by both of them without making separate investment ,Praveen agreed to this.

Identify the factor affecting fixed capital requirements of 'Fashionate Pvt. Ltd.'



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41. Best Bulbs Pvt Ltd was manufacturing good quality LED bulbs and carting to local market. The current production of the company is 800 bulbs a day. Sumit , the marketing manager of the company surveyed the market and decided to supply the bulbs to five-star-hotels also. He anticipated higher demand in future and decided to buy a sophisticated machine to further improve the quality and quantity of the bulbs produced.

Identify the factor affecting fixed capital requirements of the company



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42. Rizul Bhattacharya after leaving his job wanted to start a Private Limited Company with his son. His son was keen that the company may start manufacturing of Mobile-phones with some unique features. Rizal Bhattacharya felt that the mobile-phones are prone to quick obsolescence and a heavy fixed

capital investment would be required regularly in this business. Therefore, he convinced his son to start a furniture business.

Identify the factor affecting fixed capital requirements which made Rizul Bhattacharya to choose furniture business over mobile - phones.



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43. In the paint industry, various raw materials are mixed in different proportions with

petroleum for manufacturing different kinds of paints. One specific raw material is not readily and regularly available to the paint manufacturing companies. Bonler paints company is also facing this problem and because of this there is a time lag between placing the order and the actual receipt of the material. But, once it receives the raw materials, it takes less time in converting it into finished goods.

Identify the factor affecting the working capital requirements of this industry.



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Chapter Practice Short Answer Type Questions

1. What does good financial management imply ?



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2. Sound financial management is the key to prosperity of business. Explain why ?



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3. what is meant by financial management ?

State the primary objective of financial management .



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4. State the objective of financial management

.



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5. Discuss in brief the importance of financial management .



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6. What is meant by 'long-term investment decision ? State any three factors which affect the long-term investment decision.



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7. Investment decision can be long-term or short-term. Explain long-term investment decision and state any two factors affecting this decision.



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8. Explain any four points that highlight the importance of financial planning.



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9. Financial planning tries to link the present with the future. Explain the importance of financial planning in the light of this statement.



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10. what do you understand by the term 'trading on equity. ?



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11. Though Angel Pharma is making huge profits every year on a regular basis, it is not able to provide sufficient dividend to its shareholders. As a result, EPS remains low. Identify and explain the concept that can help to resolve the problem.



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12. When can a capital structure be considered optimum and what kind of capital structure is best for a firm ?



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13. What is fixed capital ? Enumerate any two of the factors determining the fixed capital requirements of an enterprise.



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14. What is meant by working capital ?



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15. What does 'management of fixed capital, imply ? Explain briefly any three factors determining the amount of fixed capital.



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16. You are a financial expert and your company startys a busineess of manufacturing baby toys. Suggest the working capital requirement and phases of operating cycle.



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17. The overall financial health of a business is determined by the quality of its financial management '. In the light of above statement , discuss some of the aspects which affect the financial health of a business.



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18. How is shareholder's wealth maximisation linked with the market price of the shares of the company ?





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19. Why does a financial manager consider wealth maximisation as the foremost objective ?



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20. Investment criteria is one of the factors, which affect capital budgeting decision, Comment .



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21. State whether the working capital requirement of business manufacturing the following items are big or small. Justify your answer:

(i) Bread

(ii) Coolers

(iii) Sugar

(iv) Furniture

(v) Motor car

(vi) Locomotives



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22. Distinguish between fixed capital and working capital .



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23. The Return on Investment (RoI) of a company ranges between 10-12% for the past three years. To finance its future fixed capital needs, it has the following options for borrowing debt.

Option 'A': Rate of interest 9%

Option 'B': Rate of interest 13 %

Which source of debt : OPTion A or Option B is better ? Give reason in support of your answer.

Also state the concept being used in taking the decision.



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Chapter Practice Long Answer Type

1. Explain the term ' Financial management

Breifly explain any two of its objectives.



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2. Explain the concept and the objectives of financial management .



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3. Explain the following , as factors affecting financing decision.

(i) Cost

(ii) Cash flow position.

(iii) Level of fixed operating cost

(iv) Control considerations.



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4. Name the descision, a finanical manager takes keeping in view the overall objective of

maximising shareholders' wealth.

Explain any two factors affecting the decision.



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5. What is meant by financing decision ?

State any four factors affecting the financing decision.



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6. Given the meaning of investment and financing decision of financial management .



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7. Discuss the importance of financial planning in financial management .



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8. Sound financial planning is essential for the success of any business enterprise. Explain the statement by giving any six reasons.



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9. What is meant by financial planning ?
State any three points of its importance.



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10. Explain briefly any four factors which affect the choice of capital structure of a company.



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11. Explain the followings as factors affecting the choice of capital structure.

- (i) Nature of business
- (ii) Scale of operations
- (iii) Seasonal factors
- (iv) Production cycle.





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12. Explain the following as factors affecting the requirements of working capital.

(i) Business cycle

(ii) Level of competition

(iii) Availability of raw material

(iv) Operating efficiency



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13. Explain briefly any four factors affecting the fixed capital , requirement of an organisation.



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14. Explain the following as factors affecting the requirements of fixed capital..

(i) Scale of operations

(ii) Choice of technique

(iii) Technology upgradation

(iv) Financing alternatives \



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15. Explain the following as factors affecting the requirements as factors affecting the requirements of fixed capital.

(i) Nature of business

(ii) Growth prospects

(iii) Divesification

(iv) Level of collaboration



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16. Neelabh is engaged in transport business, and transports fruits and vegetables to different states. Stating the reason in support of your answer, identify the working capital requirements of Neelabh, Neelabh also wants to expand and diversify his transport business, explain any two factors that will affect his fixed capital requirements.



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17. Financial management is concerned with inflow and outflow of money. Do you agree ? If yes, How ?



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18. KAY Ltd is a company manufacturing textiles. It has a share capital of ₹60 lakh in the previous year its earning per share was ₹0.05. For diversification, the company required additional capital of ₹ 40 lakh. The company raised funds by issuing 10 % Debentures for

the same. During the year the company earned profit of ₹8 lakh on capital employed. It paid tax @40%.

- (i) State whether the shareholders gained or lost, in respect of earning per share on diversification. show your calculations clearly.
- (ii) Also, state any three factors that favour the issue of debentures by the company as part of its capital structure.



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1. Tata Steel Acquires Corus.

Tata Steel, biggest steel producer in the Indian private sector has acquired Corus, (formerly known as British steel) in a deal worth ₹8.6 billion. This makes Tata Steel the fifth largest steel producer in the world. A financial decision of this magnitude has significant implications for both Tata Steel and Corus as well as their employees and Shareholders. To mention some of them:

Tata Steel will become the fifth largest producer

of steel in the world.

Tata steel will raise a debt of over ₹8 billion to finance the transaction. The deal will be paid for by Tata steel UK. a Special purpose Vehicle (SPV) set up for the purpose. This SPV will get funds from Tata Steel route through a Singapore subsidiary. Another company of the Tata Group, Tata Sons Ltd., Will invest ₹1 billion dollars for preference shares along with Tata steel which will invest an equal amount. Tata steel acquirer company , shall have to arrange about 36,500 crore of rupees to finance the take-over.

Tata - Steel will have to raise this amount through debt or equity or a combination of both. Some amount may come from internal accruals also. This financing decision will affect the capital structure of Tata Steel.

Tata Steel hopes to increase the production to 40 million tonnes and revenue to 32 billion US dollars by 2012.

It may affect the competitiveness of Tata Steel because the cost of production of steel in all probability, will change.

The dividend paying capacity of Tata steel may be affected because of this huge cash outflow

and because of a significantly higher debt which would need to be serviced before paying any dividends to shareholders.

The degree of risk shall also be affected. Needless to emphasise, decisions like this affect the future of the organisation. These decisions are almost irrevocable after they have been formalised.

Name the financial decision discussed in the above case.



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2. Tata steel Acquires Corus.

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Explain the factors that affect this decision..



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3. India Inc., Issue bonus Shares and Dividends

Corpotate india has opens its purse stings to

shareholders with interim dividends and bonus share. At least 60 companies have declared interim dividend or announced plans to do so in the companies have announced bonus share issues this month, about three times more than January 2006.

There are range of things that a company can do for maximising shareholder value and dividends is companies need to balance it up between paying cash and building value of the stock for total shareholder returns.

This trend of dividends and bonuses is in synchronisation with the good profits being

posted A number of companies have also announced plans of bonus shares for their shareholders. Most of the or announced that they would be taking it up in their next board meeting are small or mid-sized companies

Identify the financial decision involved in this case. Explain.



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What factors are considered while taking this decision ?



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5. Rising dividends can support valuations Over the next few years, companies cannot afford

to ignore dividends, Investors are looking for higher payouts and need the assurance of a stated dividend payouts and need the assurance of a stated dividends policy. In India , though there are few companies that are as consistent in dividend payments , even over the past five years.

The dividend yield, though has steadily declined and is now at an average of 1.1 per cent of a set of 800 companies. These companies form part of the various BSE and NSE indices. Not only has the dividend yield gone down , there is not one company in this

list that has increased dividends in line with profit growth in each of the past five years.

Among companies in the set, those that have steadily increased the payout over their years include a number of multinational companies such as a high return on net worth. Companies such as AstraZeneca Pharma, Nestle India, Hindustan Lever, Clariant, Pfizer, GlaxoSmithKline Consumer and Cummins India have enhanced dividends to deliver value to shareholders. These companies do not seem to be constrained for growth, either. Some Indian companies that have also shown the

way forward include Automative Axles, Ranbaxy LABs, Hero Honda Motors, Asian Paints. Theremax and a number of banking and non-banking finance companies. These companies , too, are growing fast, and the declaration of dividends has not dampened prospects.

Companies that have held on to profits and not declared dividends include e-serve, Cranes Software, Sesa Goa, Tata motors, Moser Baer, AVV ,MICO, Aztec Software, Havells Indian, Amtek Indai nad Sterlite Industries. This is only an indicative list and includes many more. The

dividend payout ratio in the case of the indicated companies is less than 20 per cent. Investors, however, need dividends to risk and they also need a stated dividend policy. The earnings yield (inverse of PE ratio) is now at about 6 per cent. if the payout ratio were stepped up to 40 per cent then the dividend yield would rise to about 2.5 per cent.

Which factor affecting dividend decision is indicated in the first paragraph of the given case ?



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Explain any three other factors affecting this decision.



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7. Cutting businesses have debt, but how much is too much? Learning how to manage how to manager debt is what can put you ahead.

Taking on the right amount of debt can mean the difference between a business struggling to survive and one that can respond nimbly to changin economic or market conditions. A number of circumstances may justigy acquiring debt. As a general rule , borrowing

makes the most sense when you need to bolster cash flow or finance growth on expansion. But while debt can provide the leverage you need to grow, too much debt can strangle your business. So the question is: How much debt is too much ?

The answer, experts say, lies in a careful analysis of your cash flow as well as your industry. A business that doesn't grow dies. you've got to grow, but you've got to grow within the financial constraints of your business. What is the ideal capital structure a business needs in its industry to remain viable ?

The higher the volatility (in your industry) , the less debt your should have. The smaller the volatility , the more debt your can afford.

Although banks and other fiancial institutions look for a satisfactory debt- to equity ratio before agreeing to make a loan, don't assume a creditor's willingness to extend funds is evidence that your business is in a strong debt position. Some financial institutions are or hold on to promising business customer. The bank may be looking more at collateral than whether the (business's) earnings are going to come in to justfy the debt service.

To avoid these and other credit pitfalls, it's up to you to get the financial facts on your business and make sound borrowing decisions. Unfortunately, many entrepreneurs fail to recognise how important financial analysis is to running a successful business. Even business owners who receive detailed financial statements from their accountants often do not take advantage of the valuable information contained in the documents.

Which decision relates to the amount of debt employed in the capital of a company ? Explain.



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What factors are considered while taking this decision ?



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Company X Ltd.

Total Funds used ₹	30 Lakh
Interest rate	10% p.a.
Tax rate	30%
EBIT	₹ 4 Lakh
Debt	
Situation I	Nil
Situation II	₹ 10 Lakh
Situation III	₹ 20 Lakh

EBIT-EPS Analysis

	<i>Situation I</i>	<i>Situation II</i>	<i>Situation III</i>
EBIT	4,00,000	4,00,000	4,00,000
Interest	NIL	1,00,000	2,00,000
EBT	4,00,000	3,00,000	2,00,000
(Earnings before taxes)			
Tax	1,20,000	90,000	60,000
EAT	2,80,000	2,10,000	1,40,000
(Earnings after taxes)			
No. of shares of ₹10	3,00,000	2,00,000	1,00,000
EPS	0.93	1.05	1.40
(Earnings per share)			

9.

Which concept is responsible for increase in

EPS with increased used of debt in the capital structure ?



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10.

When is it favorable ?



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11. Who funds Indian Industry, Why it matters ?

Using data on listed Indian firms from the mid-1980s to the 1990s, several issues relating to Indian industry were investigated. One aspect then was the extremely limited extent to which promoters and entrepreneurs actually owned shares in the various companies they had control of .

Proportions of the total capital of the firm	
	Percentage Share
Where did the borrowing come from?	
Borrowing from Commercial Bank	26.69
Borrowings from Financial Institutions	19.89
Debentures	7.78
Fixed deposits	3.86
Other borrowings	8.78
Who owned the shares?	
Shares held by the public at large	10.88
Foreign shareholding	3.54
Government shareholding	5.49
Institutional shareholding	8.44
Directors' shareholding	2.81
Top 50 shareholders shareholding	1.85
Total Debt and Equity Capital of a Company	100

Nevertheless in spite of the relative lack of ownership, the majority of listed entities , mostly private sector companies , were managed by these founders, their successive family members and other promoters as if they were fiefdoms.

By and large, Indian companies were

essentially financed by debt. This was unlike in the West. If the total debt plus nominal equity capital in the average Indian company was 100, then 67 per cent of that amount came in the form of debt capital while equity capital contributed only 33 per cent.

If the share of government ownership in corporate equity and the share of financial institutions, equity was added, then over 60 per cent $(26.69 + 19.89 + 5.49 + 8.44)$ of firms' finances were funded by the state in one form or another.

Foreign shareholder, in spite of a lot of clamour

about their role in India's corporate economy, hardly owned more than 4 per cent (3.54) of the shares in India's listed companies. While the public at large provided about 11 per cent of the finances of an average Indian listed company, the share of the Top 50 shareholders was less than 2 (1.85) per cent. It is within this particular shareholding category that promoters, entrepreneurs and the other large shareholder's equity stakes fall under for the purposes of classification.

The public at large provides five times as much money for the company as the entrepreneurs.

Yetm a group of induviduals, whose fiancial contributions towards a company are exceedingly small in magnitude, effectively control the company.

Which decision relates to the amount of debt and equity to finace the capital fo a company ?



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The public at large provides five times as much money for the company as the entrepreneurs.

Yet, a group of individuals, whose financial contributions towards a company are exceedingly small in magnitude, effectively control the company.

Explain few factors affecting this decision.



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13. Working capital position

It's been a rather glamorous 18 months, with sales just huge, says, CFO of PT Astra International, the US \$4 billion in sales Indonesian automaker. Indonesia is on the growth path again, and a new breed of consumer is eager for a first vehicle - motorcycles - as well as Astra's more premium brands of Hondas and Toyotas. And one of the most beautiful parts of the proposition is that working capital management seems to be taking care of itself. Depending on the business, and counting trade receivables, only

we have between eight and 19 days working capital . which is manageable given the company's steady growth. One of the reasons that working capital has not expanded at the rate of the business is inventory, or rather the dearth of it . We're in a market that responds very strongly to new products says the manager and the sales of products are very high. We have advanced orders from four to six months. With deposits paid, and this helps our cash position, Best of all as soon as a vehicle is off the assembly line, it's out the dealer. We have low inventory costs and the product lines are

very easy to move. The salutary role of banks in working capital management is one reason that cashflow has improved in his business. Better management is a result of baking competition that has allowed the company to move from traditional bakers. the ste-owned Inidan institutions , to mroe competitive private institutions and the foreign banks that partner with them. These banks have invested in technology, allowing a visibillity over cashflow unheard of five years ago.

Explain the concept of working capital.



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cashflow unheard of five years ago.

State few factors affecting working capital requirement of a business.



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15. There are two companies B and D. Total contribution of capital is ₹40 lakh each. The ratio of equity to total capital in company B is ₹10 lakh and debt is ₹30 lakh while in company D, the total equity capital is ₹ 40 lakh, sourced through equity. EBIT is ₹ 8 lakh , the interest

rate on debt is @10% and the tax rate is 30%.

Identify, which concept is related to the above case.



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17. A newly appointed finance manager has been assigned the task of procuring funds for an upcoming project . After procurement, he has to decide upon the assets in which investment is to be made.

Identify the financial decisions that he has to take.



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18. A newly appointed finance manager has been assigned the task of procuring funds for an upcoming project . After procurement, he has to decide upon the assets in which investment is to be made.

Explain the various factors that the manager would consider in taking the above decisions.



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19. While taking the financing decision, which two major sources will be considered by the manager.



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20. Ramnath Ltd, is dealing in import of organic food items in bulk. The company sells the items in smaller quantities in attractive packages. Performances of the company has

been up to the expectations in the past. Keeping up with the later packaging technology, the company decide to upgrade its machinery. For this the finance Manager of the company, Mr. Vikrant Dhull, estimated the amount of funds required and the timings. This will help the company in linking the investment and the financing decisions on a continuous basis.

Therefore, Mr Vikrant Dhull began with the preparation of a sales forecast for the next four years. He also collected the relevant data about the profit estimates in the coming

years. By doing this, he wanted to be sure about the availability of funds from the internal sources. For the remaining funds he is trying to find out alternative sources.

Identify the financial concept discussed in the above paragraph. Also state any two point of importance of the financial concept, so identified.



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Self Assessment Mcq

1. Which of the following is not an example of fixed capital decision ?

A. Launching of a new product line

B. Investing in advanced techniques of production

C. expenditure on Research and Development programs

D. Purchase of raw materials

Answer: d



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2. Name the type of dividend policy that should be followed by a company having growth opportunities.

A. Conservative dividend policy

B. Regular dividend policy

C. Stable dividend policy

D. None of the above

Answer: a



3. Investment decision include

A. capital budgeting decision and working capital decision

B. debt and equity decisions

C. retained earnings and dividends decisions

D. None of the above

Answer: a



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4. Use of debt alongwith equity increaes EPS,
this concept is also known as

- A. trading of debt
- B. trading on equity
- C. trading EPS
- D. None of these

Answer: b



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Self Assessment Very Short Answer

1. How does effective working capital management increase efficiency ?



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2. What do you understand by wealth maximisation concept



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3. What do you understand by term 'financial risk'?



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4. Define financial leverage.



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Self Assessment Short Answer Type

1. How does operating cycle affect working capital ?



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2. What does financial management aim at ?



[View Text Solution](#)

3. How is debt differnece from equity on the basis of cost and risk



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Self Assessment Short Answer Type Ii

1. Explain any four factors affecting dividend deccsion.



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2. Financial management is based on three financial decisions. What are they?



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3. Explain the two objectives of financial planning.



View Text Solution

1. Discuss the importance of financial planning

.



View Text Solution

2. How can shareholders benefit with the use of debt in the capital structure of the company ? Explain with an example.



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1. As a finance manager, you have to design the capital structure for your company . Enumerate the factors that you would consider for taking the decision.



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Cbse Examination Archive Very Short

1. In the paint industry, various raw materials are mixed in different proportions with

petroleum for manufacturing different kinds of paints. One specific raw material is not readily and regularly available to the paint manufacturing companies. Bonler paint company is also facing this problem and because of this there is a time lag between placing the order and the actual receipt of the material. But, once it receives the raw materials, it takes less time in converting it into finished goods.

Identify the factor affecting the working capital requirements of this industry.



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2. what is meant by ' financial management ?



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3. What is the primary objective of financial management ?



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4. State the objective of financial management



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5. What company is in a position to declare high dividends ?



View Text Solution

6. Define financial management .



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7. Cost of debt is lower than the cost of equity share capital. Give reason why even then a company cannot work only with the debt ?



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8. Which is the riskless source of finance ?



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9. Name any two essential ingredients of sound working capital management?



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10. Define fixed capital.



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11. what is working capital ?



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Cbse Examination Archive Short Answer

1. The Return on Investment (RoI) of a company ranges between 10-12% for the past three years. To finance its future fixed capital needs, it has the following options for borrowing debt.

Option 'A': Rate of interest 9%

Option 'B': Rate of interest 13 %

Which source of debt : Option A or Option B is better ? Give reason in support of your answer.

Also state the concept being used in taking the decision.



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2. Define capital structure.



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3. Explain the concept and the objective of financial management .



View Text Solution

4. What is meant by 'financial planning? State any three points of its importance .



View Text Solution

5. Explain any four factors which affect the working capital requirement of a company.



View Text Solution

6. What is meant by 'long -term investment decision.



View Text Solution

7. Investement decision can be long-term or short - term Explain long -term. Explain long - term investment decision and state any two factors affect this decision.



View Text Solution

8. What is meant by ' investment decision ?

State any three factors which affect the investment decision



View Text Solution

9. Explain any four factors which affect the 'fixed capital ' requirement of a company.



View Text Solution

10. What is meant by financial management ?

State the primary objective management.



View Text Solution

11. what is meant by financial planning ? State any two points of importance of financial planning ?



View Text Solution

12. Financial planning tries to link the present with the future. Explain the importance of financial planning in the light of this statement ?



View Text Solution

13. Explain the following factors affecting financing decision

(a) Cost

(b) Cash flow position of the business

© Control considerations

(d) Floatation cost



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14. Neelabh is engaged in transport business, and transports fruits and vegetables to different states. Stating the reason in support of your answer, identify the working capital requirements of Neelabh, Neelabh also wants to expand and diversify his transport business,

explain any two factors that will affect his fixed capital requirements.



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15. Pranav is engaged in transport business. Identify the working capital requirements of Pranav stating the reason in support of your answer. Pranav wants to expand and diversify his transport business. Explain any two factors that will affect his fixed capital requirements.



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16. Determining the relative proportion of various types of funds depends upon various factors. Explain any five such factors



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17. Determining the overall cost of capital and the financial risk of the enterprise depends upon various factors.
Explain any five factors.



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18. Name the decision taken by a financial manager which determines the overall cost of capital and the financial risk of the enterprise. Explain any two factors which affect any decision .



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19. Financial planning is a financial blue print of an organisation's future operations. Explain

the twin objectives of financial planning in the light of this statement.



View Text Solution

20. Explain how the

(a) cost of debt and

(b) Cost of equity affect the choice of capital structure ?



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1. Explain briefly any four factors affecting the fixed capital requirements of an organisation.



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2. Explain the following as factors affecting the requirements of fixed capital.

(i) Scale of operations

(ii) Choice of technique

(iii) Technology upgradation

(iv) Financing alternatives



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3. Explain the following as factors affecting the requirements of fixed capital.

(i) Nature of business

(ii) Growth prospects

(iii) Diversification

(iv) Level of collaboration



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4. Explain briefly any four factors that affect the choice of capital structure of a company.



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5. Explain the following as factors affecting dividend decision.

- (i) Stability of dividend
- (ii) shareholders preference
- (iii) Legal constraints
- (iv) Access to capital market



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6. Explain the following ad factors affecting dividend decision.

- (i) Stability of earnings
- (ii) Growth opportunities
- (iii) Cash flow position
- (iv) Taxation policy



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7. Explain the following as factors affecting the choice of capital structure.

(i) cash flow position (ii) Cost of equity

(iii) Floatation costs

(iv) Stock market conditions



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8. Explain the following as factors affecting the requirements of working capital.

(i) Nature of business

(ii) Scale of operations

(iii) Seasonal factors

(iv) Production cycle



View Text Solution

9. Explain the following as factors affecting the requirements of working capital.

(i) Business cycles

(ii) Level of competition

(iv) Operating efficiency



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10. Explain any four which affect the dividend decision of a company.



View Text Solution

11. what is meant by dividend decision ?
Explain any four factors which affect the dividend decision of a company.



View Text Solution

12. What is meant by dividend decision ? State any four factors affecting the dividend decision.



View Text Solution

13. Sound financial planning is essential for the success of any business enterprise. Explain the statement by giving any six reasons.



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14. Explain the term ' financial planning, and four points of its importance in financial management



View Text Solution

15. Explain any four factors which determine the choice of the capital stucture of a company.



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16. You are a finance manager of a newly established company. The directors have asked you to determine the amount of fixed capital requirement for the company. Explain any four factors that you will consider while determining the fixed capital requirement of the company.



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