

# **QUESTION BANK**

**MBA**

**SEMESTER 2**

**Vol. I**

**FOR PRIVATE CIRCULATION**

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# **QUESTION BANK**

## **MANAGEMENT OF TECHNOLOGY INNOVATION & CHANGE**

**MS -102**

**QUESTION BANK**  
**MANAGEMENT OF TECHNOLOGY INNOVATION & CHANGE – MS 102**  
**MBA II**

**UNIT - I**

**I Test Your Skills:**

**(a) State Whether the Following Statements are True or False:**

1. Technology development provides specific advantages to a business firm, which is known as firm specific advantages.
2. Technology is restricted to hardware and it does not include know – how and software.
3. Hybrid technology support R&D, and manufacturing and marketing functions in the industry.
4. The basic features of fourth stage of Technology Life Cycle are Technology Applications + rise in product sales.
5. Time of forecast means it is the future date when forecast is realized.
6. Committee is a qualitative forecasting technique in which a group of experts are involved; this helps in avoiding individual biases.
7. Technology is the practical implementation of learning & knowledge by individuals and organizations to aid human endeavor.
8. Lead time from idea to market is being reduced by the emergence of new or altered technologies
9. Software refers to particular physical structure of components and also their logical layout which are subject matter of absorption
10. Brainware is the application and justification of hardware, software development, knowwhat and know-why of technology
11. Technology Adoption means technology being absorbed without changing the parameters of acquired technology.

**Ans.** (1)(T), (2),(F), (3)(F), (4), (T), (5)(T), (6)(T) (7)(T) (8)(T) (9)(F) (10)(T) (11)(T)

**(b) Multiple Choice Questions:**

- 1 Technology forecast techniques which is based on historical date is:
  - (a) Committee
  - (b) Delphi
  - (c) Normative forecast
- 2 Technology absorbed by changing the parameters of acquired technology is called:

- (a) Technology Adaptation
  - (b) Technology Adoption
  - (c) Technology Acquisition
- 3 Mode of payment for technology transfer is:
- (a) Cross – licensing agreement
  - (b) Lump – sum payment or periodical installments
  - (c) Royalties as a percentage of sales over the next few years
- 4 Ministry of international trade and industry adopted the technology policy in Japan in ----  
-----
- (a) 1975
  - (b) 1980
  - (c) 1982
  - (d) 1985
- 5 Technology is the \_\_\_\_\_ tool available to humanity which can effect fundamental changes in the ground rules of economic competitiveness.
- (a) linear
  - (b) non linear
  - (c) static
- 6 Technological advancement in domestic market leads to growth of national -----  
- (a) wealth
- (b) income
  - (c) employment
- 7 Lead time has\_\_\_\_\_ sharply due to information technology and communication revolution. (a) increased
- (b) fallen
  - (c) both
- 8 According to a UN report, -----are engines of growth.
- (a) TNCs
  - (b) MNCs
  - (c) Both
- 9 Tick the odd method of technology acquisition
- (a) Internal R&D

- (b) Joint ventures
  - (c) Contracting out for R&D
  - (d) Licensing
  - (e) Purchasing
  - (f) Relative standing
10. A company that owns certain technology should include \_\_\_\_\_ as an essential component of its technology strategy
- (a) Technology Acquisition
  - (b) Technology Exploitation
  - (c) Technology Assimilation
  - (d) Technology Absorption
11. Ministry of international trade and industry adopted the technology policy in Japan in ----- (a) 1975
- (b) 1980
  - (c) 1982
  - (d) 1985
12. Technology is the \_\_\_\_\_ tool available to humanity which can effect fundamental changes in the ground rules of economic competitiveness.
- (a) linear
  - (b) non linear
  - (c) static
  - (d) non static
13. Technological advancement in domestic market leads to growth of national -----
- (a) wealth
  - (b) income
  - (c) employment
  - (d) debts
14. Lead time has \_\_\_\_\_ sharply due to information technology and communication revolution.
- (a) increased
  - (b) fallen
  - (c) both
  - (d) none
15. According to a UN report, -----are engines of growth.

- (a) TNCs
  - (b) MNCs
  - (c) Both
  - (d) none
16. Technology is the purposive -----of scientific knowledge for practical purposes.
- (a) Implementation
  - (b) Qualification
  - (c) Application
  - (d) Extension
17. \_\_\_\_\_ is commemorated as Technology Day in India.
- (a) May 11
  - (b) June 21
  - (c) May 1
  - (d) May 10
18. Science deals with natural world, whereas technology deals with \_\_\_\_\_ world.
- (a) man made
  - (b) space
  - (c) Imaginary
  - (d) natural
19. Technology is not only restricted to hardware but also includes \_\_\_\_\_ and \_\_\_\_\_
- (a) know – how
  - (b) software
  - (c) both
  - (d) none
20. Technology resides in the company's \_\_\_\_\_ and its technological systems.
- (a) people
  - (b) processes
  - (c) policy
  - (d) infrastructure
21. Technology is generally user friendly & aims at minimizing ----- (a)  
Revenues

- (b) Profits
  - (c) Costs
  - (d) Income
22. Nano-technology is an-----technology
- (a) infra
  - (b) hybrid
  - (c) emerging
  - (d) basic
23. A number of technologies are embodied & encapsulated in ----- (a)
- Technology Portfolio
  - (b) Disembodied Technology
  - (c) Basic Technology
24. The National Technology Portfolio should aim at----- (a)
- Competitiveness
  - (b) Cost-effective ness
  - (c) Efficiency
  - (d) All
25. ----- -is created on the basis of technology, production and smart work
- (a) Income of nation
  - (b) Wealth of nation
  - (c) Image of nation
  - (d) All
26. Technology development is many times guided by ----- analysis.
- (a) cost/benefit
  - (b) input/output
  - (c) demand/supply
  - (d) cause/ effect
27. An appropriate & effective use of technology creates ----- (a)
- Income of nation
  - (b) Wealth of nation
  - (c) Image of nation
  - (d) Debt of nation
28. Speed & magnitude of technological change around the world has been remarkably noticed after the year----- (a) 1780



- (b) 1880
  - (c) 1980
  - (d) 1990
29. Multitude of types & variation of the same tool causes high degree of-----in technology.
- (a) valence
  - (b) Flexibility
  - (c) Complexity
  - (d) creativity
30. Atlas of technology combines-----
- (a) Techno ware
  - (b) Human ware
  - (c) Info ware
  - (d) Orgaware
  - (e) Above all
31. When firms join hands to make their rivals their friends, it is called:
- (a) Co-option
  - (b) Merger
  - (c) Joint venture
  - (d) Strategic alliance
32. HDFC recently took over \_\_\_\_\_ bank which gave it access to ready next:
- (a) Centurion Bank of Punjab
  - (b) Centurion Bank
  - (c) Axis Bank
  - (d) Karur Vyasa
33. Hardware, Software, Brain ware and support net are the four basic components of:
- (a) Technology Transfer
  - (b) Technology absorption
  - (c) Technology Diffusion
  - (d) Technology Dependence
34. Technology Diffusion is also known as:
- (a) Diffusion of Innovation

- (b) Innovation Diffusion
  - (c) Diffusion of technology
  - (d) Technology Dissemination
35. \_\_\_\_\_ usually occurs when technology developed by one enterprise in one technical area and usually for one purpose is applied and used for a different technical area, for different purpose other than those foreseen at the time when R&D was initiated:
- (a) Scientific knowledge transfer
  - (b) Spin Off technology transfer
  - (c) Direct technology transfer
  - (d) outsourcing technology
36. Intellectual property risk is a limitation of:
- (a) Franchising
  - (b) Licensing
  - (c) Joint Venture
  - (d) Turnkey Contract
37. Technology absorbed without changing the parameters of acquired technology is Called \_\_\_\_\_
- (a) Technology absorption
  - (b) Technology adaptation
  - (c) Technology adoption
  - (d) Technology acquisition
38. \_\_\_\_\_ is any commercial formula, device, pattern or information that provides an enterprise with competitive edge over others who do not know it.
- (a) Trade secret
  - (b) Know-how
  - (c) Trademark
  - (d) Copyright
39. \_\_\_\_\_ usually has legal boundaries attached to it.
- (a) Technology acquisition
  - (b) Technology diffusion
  - (c) Technology transfer
  - (d) Technology Borrowing
40. What is the full form of “EHTP?”
- (a) Electronic Hardware Technology Park

- (b) Electronic Hardware Technology Protocol
  - (c) Economic Hardware Technology Park
  - (d) Economic Hardware Technology Protocol
41. At the level of an individual firm, technical change may be described as a process of problem solving. What two stages in the process of problem solving include strong judgmental input?
- (a) Solution development and technology choice
  - (b) Problem recognition and solution development
  - (c) Problem recognition and technology choice
  - (d) Commercialization and technology choice
42. The processes by which firms arrive at a feasible solution to customer wants is known as
- (a) Diffusion.
  - (b) Innovation.
  - (c) T-M matrix.
  - (d) Invention.
43. Which component of the output of the process of innovation is the major facet of the marketing strategy of a firm?
- (a) The hardware component
  - (b) The evaluation information component
  - (c) The dominant component
  - (d) The software component
44. The development of the computer is an example of which of the following innovations?
- (a) Autonomous
  - (b) Market
  - (c) Political
  - (d) Environmental
45. Technology push innovations tend to be driven by which of the following?
- (a) Consumers
  - (b) Political factors
  - (c) Research
  - (d) Manufacturers

46. An innovation that uses existing organizational practices and technologies but reconfigures them in new or different ways is known as (a) Architectural innovation.
- (b) Modular innovation.
  - (c) Incremental innovation.
  - (d) Radical innovation.
47. The process by which new technologies emerge to obsolete existing technologies is known as
- (a) Technology limit.
  - (b) Learning curve.
  - (c) S-curve of technology development.
  - (d) Technology progression.
48. What principle suggests that a characteristic feature of technical know-how is not easily transmitted?
- (a) Technological insularity
  - (b) Temporal clustering
  - (c) Spatial clustering
  - (d) Managed innovation
49. The competitive impact of specific technologies varies over competitive domains, and there is a progression over time from the first to the fourth stage listed below. Which arena would one find most critical to competitive success?
- (a) Pacing technology (b) Base technology
  - (c) Key technology
  - (d) Radical technology
50. Relative technological competitive strength is a measure of the degree to which a firm has mastery in a specific set of technologies relative to its competitors. The variance follows a continuum. Which level has the firm able to express independent technical actions and set new directions?
- (a) Tenable
  - (b) Favorable
  - (c) Strong
  - (d) Dominant

51. Which of the following is not a forecasting technique?
- (a) Judgemental
  - (b) Time series
  - (c) Time Horizon
  - (d) Associative
52. A personnel plan requires forecast of
- (a) personnel needs
  - (b) supply of inside candidates
  - (c) supply of outside candidates
  - (d) all of above
53. Process which consists how and what positions are to be filled is called
- (a) Employment planning
  - (b) Human resource planning
  - (c) Succession planning
  - (d) all of above
54. Design strategy of business includes
- (a) marketing strategy
  - (b) technology strategy
  - (c) sourcing strategy
  - (d) all of above
55. First phase of value creation in sequence is
- (a) choosing value
  - (b) providing value
  - (c) communicating value
  - (d) making superior product
56. Plausible representation of possible future based on assumptions is called
- (a) scenario analysis
  - (b) market analysis
  - (c) segmentation analysis
  - (d) targeted factors
57. When amalgamation is in the nature of merger, the accounting method to be followed is :
- (a) Equity method
  - (b) Purchase Method

- (c) Pooling of interest method
  - (d) Consolidated method
58. When amalgamation is in the nature of Purchase, the accounting method to be followed is :
- (a) Equity method
  - (b) Purchase Method
  - (c) Pooling of interest method
  - (d) Consolidated method
59. Under pooling of interest the difference between purchase considered and share capital of transferee company should be adjusted to:
- (a) General Reserve
  - (b) Amalgamation of adjustment account
  - (c) Goodwill or Capital Reserve
  - (d) None of the above
60. Under purchase method the difference between purchase considered and share capital of transferee company should be adjusted to:
- (a) General Reserve
  - (b) Amalgamation of adjustment account
  - (c) Goodwill or Capital Reserve
  - (d) None of the above

**Ans.** (1)(c), (2)(a), (3)(d), (4)(b), (5)(b) ,(6)(a), (7)(b), (8)(c),(9)(f),(10)(b), 11(b) 12(b) 13(a)14(b)15(c)16(c)17(a)18(a)19(c)20(a)21(c)22(c)23(a)24(a)25(b)26(a)27(b)28(c) 29 (a)30(e), (31)(a), (32)(b), (33)(b) ,(34)(a), (35)(b) ,(36)(c) ,(37)(c), (38)(a), (39)(a), (40)(a), (41)(c), (42)(b), (43)(b), (44)(a), (45)(d), (46)(a), (47)(d), (48)(a), (49)(c), (50)(c) 51(c), 52(d), 53(d), 54(d), 55(a), 56(a), 57(c), 58(b), 59(a), 60(c)

**(c) Fill in the Blanks:**

1. Technological advancement in domestic market leads to growth of \_\_\_\_\_.
2. Proper change management reduces \_\_\_\_\_.
3. Science deals with natural world, whereas technology deals with \_\_\_\_\_ world.
4. The third stage in the Technology Life Cycle is \_\_\_\_\_.
5. A normative forecast starts with \_\_\_\_\_ and identifies the technological performance necessary to meet these required needs.
6. An exploratory forecast is based on \_\_\_\_\_ and is opportunity oriented.

7. Technology of forecasting involving a group of experts are \_\_\_\_\_ and \_\_\_\_\_.
8. \_\_\_\_\_ and \_\_\_\_\_ are the two important factors that affect technology acquisition.
9. Internal technology transfer refers to the technology transfer where control of ownership resides with the \_\_\_\_\_.
10. In external technology transfer the control of ownership resides with the \_\_\_\_\_. 11 \_\_\_\_\_ and \_\_\_\_\_ are advantages of technology absorption in a country like India.
- 12 Modern technologies can be created through \_\_\_\_\_
- 13 Technology lifecycle position; commitment involved; urgency of acquisitions and company's relative standing are \_\_\_\_\_ factor
- 14 Technology should be marketed widely to get good \_\_\_\_\_ that increases the market share
- 15 Relative standing of the company; urgency of exploitation; need for support technologies; commitment involved and technology life cycle are \_\_\_\_\_

**Ans.** (1)(National Wealth), (2)(Staff Dissatisfaction), (3)(Human – made), (4)(Application Launch), (5)(Future Needs), (6)(Technology Push), (7)(Committees, Delphi), (8)(Level of economic development of a nation, State of technology), (9)(Transferor), (10)(Recipient), (11)(Employment generation and Capability to fight foreign competition) (12) R&D and scientific approach (13) Absorption Decisions (14) Market Penetration (15) Exploitation decision factors

## **II Short Answer Type Questions:**

1. Explain how technology is associated with the wealth of nations.
2. What is technology life cycle? Discuss its various stages.
3. Differentiate between Science and Technology.
4. Define technology in all its dimensions.
5. Write short note on Globalization of Technology.
6. Discuss the role of technology development in the economic growth of a nation.
7. Explain the role of innovation in the survival and growth of a nation and its business firms.
8. What is Technological Forecast? What are its essential elements? List its benefits/importance to organizations.
9. Briefly discuss the concept of Technology Forecast and Strategic Planning.
10. 'Science and technology carry the same meaning,. Do you agree with this statement? If yes, why? If not, why not? Justify your answer.
11. Distinguish between Discovery, Invention and Innovation.

12. What do you understand by firm's specific knowledge?
13. What is joint venture abroad? Why do we need them? Explain using an example.
14. Distinguish between Cooperative research and Contract research.
15. What is technology life cycle? Explain the various stages of TLC?
16. Distinguish between: Technology Adoption, Adaption, Absorption, Optimization, and Up gradation.
17. Discuss the importance of technology Management in economic prosperity of a nation.
18. The growth of technology follows a 'S' shaped curve. Explain.
19. Name and explain briefly the various approaches to technology Development
20. Explain the terms
  - (a) Technology Adoption
  - (b) Technology Adaptation
  - (c) Joint Venture
21. Why do home countries oppose export of technology?
22. How does the 'Export Control Organization' control electronic transfers?
23. What does 'in the public domain' mean?
24. Discuss various noticeable developments in modern economies as an outcome of globalization of technology.
25. Explain various factors leading to fast globalization of technology & communication revolution.
26. What do you mean by technology management aspects of non conventional sources of energy?
27. Growth of technology follows an 'S' shaped curve. Explain using an appropriate example.
28. Difference between collaboration, licensing and joint venture
29. Coin the terms -Science, Discovery, Invention and Innovation
30. Technology is important for the economic prosperity of a nation. Discuss.
31. Comment on Science –Technology push.
32. Why a firm should sell or purchase technology? List at least two examples where sale or purchase of technology has taken place.
33. Distinguish between the following- (a) Discovery, Invention & Innovation
  - (b) Cooperative Research & Contract Research
  - (c) Technology Adoption, Adaptation & Absorption
  - (d) Mass Production & Mass Customization
34. Write a short note on Technology and Society.
35. Distinguish between Embodied Technology and Disembodied Technology
36. What do you mean by globalization of technology? Give examples in support of your answer.
37. Write a short note on:



- (a) Technology Development
  - (b) Technology application
  - (c) Technological Maturity
  - (d) Degraded Technology
  - (e) Strategic Management of Technology
38. Explain the term Technological dependence in brief.
  39. Differentiate between Technology Transfer and Technology Acquisition.
  40. The growth of technology follows “S” shaped curve. Explain using an appropriate example.
  41. Discuss the various technology joint ventures in India and China
  42. Write short note on Technology Diffusion
  43. Discuss the various techniques of Technology Forecasting.
  44. What do you understand by Technology strategy of a corporate? What factors influence it?
  45. What is creativity? Explain the role of creativity in organizational growth with the help of suitable examples.
  46. What is Technology Transfer? What are the various types?
  47. Write a short note on Technology Acquisition.
  48. What governance structure model should be selected for the JV?
  49. How will the functional activities of the JV be conducted and managed?
  50. How should you structure a forecasting problem?
  51. What methods are commonly used for forecasting?
  52. Why a firm should sell or purchase technology? Give reasons.

### **III Long Answer Type Questions:**

1. Discuss in detail the benefits of proper change management to a nation and its business enterprises.
2. “Technology development creates firm – specific advantages’. Elaborate.
3. Demonstrate the role of firm – specific knowledge in sustaining competitive advantage by taking examples of two firms in the relevant industry.
4. What do you understand by term technology? What are its features? Explain various types of technologies with the help of examples.
5. Explain the concept of technology life cycle with the help of an example from an industry.
6. ‘Technology and its related products, services and processes pass through stages similar to human life cycle like birth, growth, maturity and death’. Elaborate the statement with the help of examples.
7. Technology development influences economic progress and wealth of nations and its business firms’. Elaborate.

8. What is Technology Forecasting? Explain briefly the techniques for forecasting changes in markets and in competitive conditions as a result of technological innovation.
9. What is technology forecasting? How it is useful to an organization? List the steps involved in any one of the forecasting technique you are aware of.
10. Write notes on the following:
  - (a) Committee
  - (b) Delphi
  - (c) Exploratory Forecast
  - (d) Normative Forecast
11. What factors influence technology acquisition by a nation? How can a nation acquire technology?
12. Differentiate between technology transfer and technology acquisition.
13. What do you understand by technology acquisition? Explain various methods/routes of technology acquisition.
14. Which are leading firms in India in terms of technology exports?
15. What are barriers to scale – up technology exports from India? Give suggestions to reduce them.
16. Should the government allow free outflow/export of technology and setting up of Joint Venture and Wholly Owned Subsidiaries Abroad by Indian companies or should it regulate or restrict them? Give reasons in support of your answer.
17. ‘India is a big attraction to foreign partners’. Elaborate the statement.
18. Explain briefly the guidelines issued by the Government of India for foreign technology agreements (technology inflows).
19. Explain briefly the guidelines issued by the Government of India for export of technology (technology outflows) and setting up of Joint Venture and Wholly Owned Subsidiaries Abroad.
20. What is technology absorption? What are its advantages to business firms? How can they manage technology absorption?
21. What are benefits of technology absorption in a developing country? How does the Indian government encourage it?
22. Differentiate between:
  - (a) Technology Adoption and Technology Adaptation
  - (b) Technology Acquisition and Technology Absorption
23. Define the term ‘Technology’. List some characteristics of technology. Discuss the relationship between Technology and Economic prosperity of a nation citing examples.
24. Why a firm should buy or sell technology? Name various routes generally adopted for technology transfer?
25. How is technology forecasting useful to an organization? Differentiate between two basic approaches to technology Forecasting. Under what circumstances ‘delphi’ technique of forecasting preferred over ‘trend analysis’?

26. 'Technology has become an integral part of any business unit' keeping this statement in view discuss the role of technology in designing the business strategy of a firm.
27. Explain various routes of technology transfer. Discuss the merits & demerits of adopting a specific route by the organization for its product.
28. Explain the concept of linkages. Why are these essential for an organization having technology management group?
29. What are the major benefits an organization can have from effective absorption of technology? Explain.
30. Explain briefly various sources of procuring technical information. Discuss the advantages of any two of the information sources.
31. How technology capability building is related to flexibility & competitiveness?
32. Technological developments are also stimulated by Market Pull. Discuss the statement with an example.
33. The Science/Technology Push opens new vistas for industrial development & economic growth. Justify the statement.
34. What do you understand by the Diffusion-Communication-Channel relationship?
35. Comment upon the competition at different phases of Technology Life cycle. 36  
Identify the strategic importance of management of technology in industry.
37. "Technology is crucial for economic prosperity of a nation", Discuss the validity of this statement quoting suitable example.
38. What is the importance of technology forecast? Under what circumstances 'Delphi technique of forecasting preferred over 'trend analysis'?"
39. What is Technology Lifecycle? Discuss various stages of Technology Lifecycle of mobile phones.
40. Explain various types of technology along with the suitable examples. Which type of technology is most popular now days?
41. What are the leading firms in India in terms of Technology Exports? What are the barriers to scale up technology Exports from India?
42. Discuss the latest technology joint ventures in India.
43. How is technology related to creation of wealth of nations? Elucidate your answer by providing examples from Industry.
44. Science deals with natural world, whereas technology deals with man-made world. Elaborate the statement with suitable examples.
45. How has TIFAC as an organisation contributed to forecasting and planning in India?
46. 'Technology development influences economic progress and wealth of nations and its business firms.' Elaborate.
47. What is Technology Forecasting? Explain briefly the techniques for forecasting changes in markets and in competitive conditions as a result of technological innovation.
48. What is Technology Transfer? What problems are faced in Technology Transfers and how can they be overcome?

49. What does the field of forecasting encompass?
50. Is it possible to improve on forecasts by using expert knowledge about the situation? Explain.
51. Explain the terms giving examples: Discovery, Invention and Innovation
52. Technology helps in growth of nations and creating wealth. Discuss the validity of this statement giving suitable examples.
53. What is Technology Policy? Name the recently announced Technology Policy of India. Why a country should have a Technology Policy? Explain.

## UNIT - II

### I Test Your Skills:

#### (a) State whether the following statements are True or False:

1. Process Design refers to the complete specification of a product to be manufactured.
2. The last stage of Seven levels of Change Model is Doing Different - Doing things no one else is doing.
3. The degree to which a company can implement new initiatives to support changes in business strategy is known as Business Transformation.
4. Consolidation can be attained through increase in integration and senior management commitment.
5. The Power – Coercive strategy of Change Management explain people are social beings and will adhere to cultural norms and values.
6. Change takes place because of natural environment & business environment 7. Improving efficiency through organizational change includes low risk, less effort.
8. The role of leader in process of change can be to encourage competition.
9. A negative role played by leader can lead to more conflicts.
10. The change process involves unfolding, changing & stabilizing

**Ans.** (1)(T), (2)(F), (3)(F), (4)(T), (5)(F) (6)(T)(7)(T)(8)(F)(9)(T)(10)(T)

#### (b) Multiple Choice Questions:

- 1 Resistance to change can occur at:
  - (a) Individual Level

- (b) Group Level
  - (c) Organizational Level
  - (d) All of the above
- 2 Change management strategies can be:
- (a) Overt or Immediate
  - (b) Empirical – Rational
  - (c) Copying – Imitation
- 3 The changes which are introduced internally by management in a systematic manner are:
- (a) Unplanned Changes
  - (b) Fast Changes
  - (c) Planned Changes
- 4 Second Level in Seven Levels of Change Model is:
- (a) Increasing effectiveness – Doing the right things
  - (b) Enhancing – Doing Things Better
  - (c) Doing Different – Doing Things no one else is doing
- 5 Change Owner is a person who:
- (a) The person who initiates the request and ultimately will confirm its completion
  - (b) The person who gives business approval for change
- 6 The person who is allocated to a change and who manages it through to acceptance and closure. The three types of goals to be achieved in change problem are transformation, reduction and .... ?
- (a) Abstract
  - (b) Application
  - (c) Manage
  - (d) Control
- 7 Change problem can be treated as smaller problems having to do with..... of change?
- (a) When, what ,why
  - (b) What, when, how
  - (c) How, what, why
  - (d) When, where, what

- 8 The change process consists of ‘unfreezing, changing and .....’?
- (a) Applying
  - (b) Freezing
  - (c) Defrosting
  - (d) Refreezing
- 9 The importance of change can be all except:
- (a) It abandons negative cultural values.
  - (b) It raises motivation.
  - (c) It leads to satisfaction among employees.
  - (d) It makes organization monotonous.
- 10 Planned change is all except
- (a) Intentional
  - (b) Goal oriented
  - (c) Accidental
  - (d) Systematic
- 11 All are the external factors responsible for change except change in:
- (a) Government Policies
  - (b) Market scenario
  - (c) Technology
  - (d) Leadership
- 12 All are the internal factors responsible for change except :
- (a) Structural reorganization
  - (b) Decline in productivity
  - (c) Social pressure
  - (d) Productivity
- 13 Following are the parameters to assess organization capabilities to change except :
- (a) Vision for future
  - (b) Demographic culture
  - (c) Effective communication
  - (d) Commitment of top management
14. The three types of goals to be achieved in change problem are transformation, reduction and .... ?

- (a) Abstract
  - (b) Application
  - (c) Manage
  - (d) Control
15. Change problem can be treated as smaller problems having to do with..... of change?
- (a) When, what ,why
  - (b) What, when, how
  - (c) How, what, why
  - (d) When, where, what
16. The change process consists of ‘unfreezing, changing and?
- (a) Applying
  - (b) Freezing
  - (c) Defrosting
  - (d) Refreezing
17. The importance of change can be all except:
- (a) It abandons negative cultural values.
  - (b) It raises motivation.
  - (c) It leads to satisfaction among employees.
  - (d) It makes organization monotonous.
18. Planned change is all except
- (a) Intentional
  - (b) Goal oriented
  - (c) Accidental
  - (d) Systematic
19. All are the external factors responsible for change except change in:
- (a) Government Policies
  - (b) Market scenario
  - (c) Technology
  - (d) Leadership
20. All are the internal factors responsible for change except :
- (a) Structural reorganization
  - (b) Decline in productivity
  - (c) Social pressure

- (d) Productivity
21. Following are the parameters to assess organization capabilities to change except:
- (a) Vision for future
  - (b) Demographic culture
  - (c) Effective communication
  - (d) Commitment of top management
22. How many levels are there in change model?
- (a) 3
  - (b) 7
  - (c) 8
  - (d) 5
23. Following are the examples of overt or immediate resistance to change except :
- (a) Job dissatisfaction
  - (b) Slow down
  - (c) Threat to strike
  - (d) Holiday of worker
24. The individual change management model developed by Jeff Hiatt is known as:
- (a) SATCAR
  - (b) ADKAR
  - (c) DISHAK
  - (d) BASISCS
25. Which one are not the basic management strategies:
- (a) Empirical-rational
  - (b) Normative-reductive
  - (c) Power-coercive
  - (d) Societal-adaptive
26. Which one is not the one of the Eight steps to successful change by Kotler's
- (a) Increase urgency
  - (b) Get the vision right
  - (c) Focus on goal of worker
  - (d) Empower action
27. Following are the focus area of organizational change except changing :



- (a) Competitors
  - (b) People
  - (c) Physical setting
  - (d) Technology
28. Following is not the dimension of product design:
- (a) Core benefits
  - (b) Changing society
  - (c) Tangible specification
  - (d) Augmented features
29. In business transformation, changes in operational concept include all except :
- (a) Tactics
  - (b) Techniques
  - (c) Rules
  - (d) Procedures
30. Transformation is reflected in people mind by the way of all except :
- (a) Employee think
  - (b) Society changes
  - (c) Employees speak
  - (d) Employee act
31. Change management can be all expect:
- (a) Reactive & proactive'
  - (b) Internal & external
  - (c) Continuous & acc. To necessities
  - (d) Single disciplinary
32. Unplanned change is all below except:
- (a) Accidental
  - (b) Intentional
  - (c) Sudden
  - (d) Uninformed
33. Which of the following are not the characteristics of organizational change:
- (a) It makes things different
  - (b) It is inevitable
  - (c) It an ongoing activity
  - (d) It take place at single level of an organization

34. Change takes place because of all mentioned below except :
- (a) Natural environment
  - (b) Business environment
  - (c) Employee stress
  - (d) Economic environment
35. The rate of organizational change is influenced by all except :
- (a) Necessity
  - (b) Literacy level in employees
  - (c) Circumstances
  - (d) Management philosophy
36. Improving efficiency through organizational change includes :
- (a) Low risk , less effort
  - (b) High risk. Less effort
  - (c) Low risk, more effort
  - (d) High risk, more effort
37. The role of leader in process of change can be all below except :
- (a) Encourage collaboration
  - (b) Encourage training
  - (c) Encourage quality consciousness
  - (d) Encourage competition
38. A negative role played by leader can lead to all below except :
- (a) More conflicts
  - (b) Increase productivity
  - (c) Lack of commitment
  - (d) Decline in performance
39. The change process involves:
- (a) Unfreezing, changing & refreezing
  - (b) Unfolding, changing & refreezing
  - (c) Unfolding, changing & stabilizing
  - (d) Freezing, changing & refreezing
40. Resistance to change can be - (a) Overt or implicit
- (b) Immediate or deferred
  - (c) Individual or group

- (d) All above
41. Which of the following leadership style refers to strategic and operational actions that influence organizational and follower performance based on the leader's expert power?
- (a) Transformational leadership
  - (b) Transactional leadership
  - (c) Instrumental leadership
  - (d) Laissez-faire leadership
42. Which of the following is a disadvantage of narrow span of control?
- (a) Close control
  - (b) Close supervision
  - (c) High costs due to many levels
  - (d) Fast communication between subordinates and superiors
43. The statement of an organization's aspirations can be found in the organization's:
- (a) Mission statement
  - (b) Strategic objectives
  - (c) Actions
  - (d) Vision statement
44. Which of the following is an intangible design?
- (a) Control system
  - (b) Functional design
  - (c) Divisional design
  - (d) Matrix design
45. Identify a systematic variable which hampers execution of strategic change?
- (a) Misdirected reward and evaluation
  - (b) Too many hierarchical levels
  - (c) Overly narrow span of control
  - (d) Responsibility without authority
46. What does SOC stand for?
- (a) Systematic Organizational Change
  - (b) Strategic Organizational Change
  - (c) Successful Organization Change
  - (d) Stressful Organizational Change
47. Bounded rationality is one of the constraints in initiating the change, which is:

- (a) Internal to an organization
  - (b) External to an organization
  - (c) Inferior to an organization
  - (d) Exterior to an organization
48. There are different styles of managing strategic change. Which of the following are the potential benefits of "direction" as a change style?
- (a) Overcomes lack of information or misinformation
  - (b) Increases ownership of a decision or process
  - (c) Maintains control over the change process whilst also involving people in it
  - (d) Provides clarity and speed
49. Which of the following does NOT describe radical change?
- (a) It is multi-directional
  - (b) It is discontinuous
  - (c) It is long-term based
  - (d) It is based on constant learning
50. Which of the following is an intangible design?
- (a) Control system
  - (b) Functional design
  - (c) Divisional design
  - (d) Matrix design
51. The fundamental assumptions people share about organization's values, beliefs and norms \_\_\_\_\_ is referred to as \_\_\_\_\_.
- (a) Organizational behavior
  - (b) Organizational design
  - (c) Organizational culture
  - (d) Organizational structure
52. Which of the following were ranked in the top five organizational values?
- (a) Provide excellent service to customers.
  - (b) Operate in a highly ethical manner always.
  - (c) Staff the organization with high-caliber employees.
  - (d) All of the above.

53. The way in which new members of the organisation are indoctrinated in the expectations of the organisation and its cultural norms is termed:
- (a) Socialisation
  - (b) Orientation
  - (c) Realistic Job Preview (RJP)
  - (d) Internal locus of control
54. Which of the following most accurately describes the impact that a subculture can have on an organisation?
- (a) Promote an independence from the organisation, as commonly occurs among divisions of diversified firms.
  - (b) Serve to eradicate the dominant culture.
  - (c) Serve to provide leadership for the strategic direction of the firm.
  - (d) All of the above.
55. \_\_\_\_\_ are defined as temporal beliefs based on evaluative interpretations of current conditions.
- (a) Values
  - (b) Beliefs
  - (c) Attitudes
  - (d) None of the above.
56. When a set of core values are shared by the majority of organizational members, these core values become a:
- (a) Tradition-based value system.
  - (b) Organizational value system.
  - (c) Charismatic-based value system.
  - (d) Functional-based value system.
57. Values originating from a strong leader are:
- (a) Functional-traditional values.
  - (b) Functional values.
  - (c) Charismatic values.
  - (d) None of the above.
58. The \_\_\_\_\_ leadership style is an expression of the leader's trust in the abilities of his subordinates.
- (a) Participative
  - (b) Delegative
  - (c) Authoritarian

(d) All of the above

59. What is play to some people maybe to others.

- (a) Responsibility
- (b) Duty
- (c) Work
- (d) None of the above

60. Work attitudes can be reflected in an organization through

- (a) Job satisfaction
- (b) Organizational commitment
- (c) Both 'A' and 'B'
- (d) None of the above

**Ans.** (1)(d), (2)(b), (3)(c), (4)(a), (5)(c)(6)(b)(7)(c)(8)(d)(9)(d)(10)(c)(11)(d)(12)(c)(13)(b)  
14(b)15(c)16(d)17(d)18(c)19(d)20(c)21(b)22(b)23(a)24(b)25(d)26(c)27(a)28(b)29(c)  
30(d), 31(b),32(b),33(d), 34(c)35(b)36(a)37(d)38(b)39(a)40(d), (41)(c), (42)(c), (43)(d),  
(44)(a), (45)(a), (46)(b), (47)(b), (48)(d), (49)(d), (50)(c), 51(c), 52(d), 53(a), 54(a), 55(c),  
56(b), 57(c), 58(a), 59(c), 60(c)

**(c) Fill in the Blanks:**

1. \_\_\_\_\_ and \_\_\_\_\_ are the internal factors for organizational change.
2. \_\_\_\_\_ changes are sudden in nature as a result of some sudden development.
3. The process of change has been characterized as having three basic stages: \_\_\_\_\_, \_\_\_\_\_ and \_\_\_\_\_.
4. Managing change is seen as moving from one state to another, that is from \_\_\_\_\_ to \_\_\_\_\_.
5. \_\_\_\_\_, \_\_\_\_\_ and \_\_\_\_\_ involve ideas and ideas are about change.
6. Organizations live and operate in \_\_\_\_\_ environment, which keeps on changing continuously.
7. Change process can be used to raise \_\_\_\_\_ viz. by creating desire to support and participate in the change.
8. \_\_\_\_\_ refers to making of changes in a planned and managed, or systematic, fashion.
9. \_\_\_\_\_ is the Level 1 of Seven Levels of Change Model.
10. Change management is \_\_\_\_\_, in the case where management is responding to changes in the macro environment (external causes)

11. Technological change can be disastrous, if new technology is not successfully-----  
-
12. Higher level of change leads to ----- advances. \_\_\_\_\_ can dramatically boost innovation quickly & cheaply than starting from scratch.
13. Seeking support from people ----- the system is an important principle of change management.
14. It is -----Change management, when management is responding to changes in the macroeconomic environment.
15. \_\_\_\_\_ can dramatically boost innovation quickly & cheaply than starting from scratch.

**Ans.** (1)(Decline in profitability and Industrial relation problems), (2)(Unplanned), (3)(Unfreezing, changing and refreezing), (4)(Problem state to Solved state), (5)(Creativity, Innovation and Continuous Improvement), (6)(Dynamic), (7)(Motivation), (8)(Improving efficiency – Doing things right), (9)(Managing Change),(10)(Reactive)(11)(implemented)(12)(radical)(13)(within)(14)(re active)(15)(reverse engineering)

## **II Short Answer Type Questions:**

1. What is the role of organizational culture in smoothening the process of organizational change?
2. Explain the concept of change-strategy.
3. What do you understand by organizational change? What factors cause organizational changes?
4. What do you understand by technological change? What factors cause it?
5. Explain various types of changes which can be introduced by an organization.
6. Discuss the importance of Change in an organization.
7. Differentiate between technological change, technical change and technological progress.
8. What are the benefits of Organizational Change Management? How will you manage organizational change?
9. Discuss the characteristics of technological change.
10. What are the Thrust areas of Organizational Change? Discuss 11. How do external forces influence Organizational Change? Explain.
12. Contrast between Mass Production and Mass customization. Explain giving examples of each.
13. How the leadership in an organization can help in building a culture for change.
14. Explain any one of the technique for corporate transformation. State its limitations.

15. Develop a framework for diagnosing organizational capability for change.
16. Enumerate the various steps the leadership can adopt for building a culture for change.
17. What are the various forces of change from the
  - a. Individual Perspective
  - b. Organizational Perspective
18. Discuss the change management program in which you were a part giving rationale, mechanism and results.
19. Explain the meaning of change and whether all changes are beneficial.
20. Explain the internal and external forces that induce change in the organization
21. Describe the Process of Organisational change.
22. Discuss Lewin's model of change.
23. Discuss various prerequisites for change management.
24. State different ways to improve communication radically in the context of change.
25. How will you set realistic targets & priorities for change for an organization?
26. How can you help people to be positive about change?
27. How can you encourage the appropriate level of risk taking in an organization?
28. Comment upon 'team building for change management'.
29. What do you understand by diffusion of technology?
30. Contrast between Know how & Know why. Give examples for each.
31. What are the external forces of change? Give suitable examples.
32. Differentiate cooperative research & contract research.
33. Differentiate concurrent & sequential engineering
34. Differentiate BPR & TQM
35. What is the process of change as per Kurt Lewin Model?
36. Explain the role of organization structure in implementing change.
37. Explain how training can support implementing change in an organization?
38. Describe the various levels of change.
39. Describe the major sources of organizational resistance.
40. Explain the role of a leader in facilitating change.
41. How can people lever be harnessed for effective change management?
42. What do you understand by change in product design/product modification?
43. Explain the various change management strategies in brief.
44. Discuss 'Resistance to change' as a biggest challenge to change management.
45. In your opinion, what is the greatest technological invention? Why?
46. Can we engineer the climate?
47. How can countries help to create more inventors?
48. Give some examples of technology that have made the world worse.
49. How do you encourage "smart risk taking" and drive out fear of failure.



### III Long Answer Type Questions:

1. Explain the role of leader in facilitating organizational change.
2. “Change is the process of an organization” are inevitable in the light of innovation adoption.” Discuss in detail.
3. What do you understand by change in product design/product modification? Why does the necessity for changing product design arise?
4. What do you understand by change in process design? Explain the reasons necessitating changes in processes.
5. Explain various strategies/steps for overcoming resistance to organizational changes.
6. How can people lever (improvement of people) be harnessed for effective change management?
7. Discuss how a leader can nurture a culture for innovation and change in an organization.
8. Discuss the change management programme of which you were a part giving it rationale, mechanism and results. What would you do differently if you were to design the change management programme?
9. Discuss in detail Seven Levels of Change Model.
10. What are the steps involved in Change Management Process?
11. Discuss the John P Kotter’s – ‘Eight Steps to Successful Change’
12. Describe the four types of Change Management Strategies.
13. “Building culture for change is a time – consuming exercise and involves lot of efforts”. Explain.
14. “Before initiating the change process, it is very important to diagnose/assess the organizational capability to change”. Is it true? Discuss.
15. Discuss some of the Change Management principles.
16. “Change can bring both negative and positive effects in an organization”. Discuss.
17. What is change problem? Discuss in detail.
18. What do you mean by Business Transformation? How are transformations implemented in an organization?
19. Summarize key learning from biggest transformations in India. Evolve suggestions to transform Railways, if you were made a key member of the team leading the railway transformation.
20. Diagrammatically show the Time Frame of Change in Product and Process Design.
21. Give a diagrammatic representation of the ‘Change Process’. What are the various forces of change from the individual perspective and Organizational perspective?

22. Explain various external & internal forces for change in organizations.
23. Discuss the ways to encourage more openness from staff for listening & identifying the real problem in organizations.
24. Is there a stepwise approach to change? How can we deal with resistance to change?
25. How to manage communication down & up in an organization? Describe the cascade process.
26. Is it necessary to create a 'burning platform' in order to create awareness for the need to change? Discuss.
27. How does Kurt Lewin explain the process of change/ List its various phases & the activities in each phase
28. Explain any internal forces of change. Give suitable examples to support your answer.
29. What are the issues and challenges of Technology Acquisitions, Technology Absorption and Technology Transfer in a country like India?
30. Who do you think can build culture for change in an organization? Discuss various levels of changes in the organization.
31. Discuss various organizational and individual resistances to change. How can you overcome these resistances?
32. What are the issues involved in Technology Acquisition and Technology Absorption? How is India coping with these challenges?
33. What is change all about? How do OD interventions help in the change process?
34. Write notes on the following:-
  - a. Changing Technological Advancements
35. What do you understand by Technological Change? What factors cause organisational changes?
36. Discuss the change management programme of which you were a part giving it rationale, mechanism and results. What would you do differently if you were to design the change management programme?
37. Should access to scientific knowledge be totally free? Explain.
38. The fifth major issue to be tackled by our distinguished panel of innovation practitioners is innovation culture, specifically: How do you build and sustain a culture and climate for innovation and entrepreneurship, and how do you encourage "smart risk taking" and drive out fear of failure?
39. State the reasons why organizational culture change is difficult with the help of examples.
40. "Change your leaders to change your culture". Comment.
41. How does organization culture impact the change process? Explain.

## **UNIT - III**

### **I Test Your Skills:**

**(a) State Whether the Following Statements are True or False:**

- 1 Tools for Process Innovation are Developing assembly Charts, Developing Process Charts and Computer Aided Designing.
- 2 In the concurrent engineering approach, the product design and the process design do not go simultaneously.
- 3 When the product or service concept is frozen at early stage so as to minimize risk, in this the model is basically Traditional Phase Gate Model.
- 4 In Kaizen everybody from top to bottom is involved, whereas in Innovation selected few people are involved in multifunctional teams.
- 5 The term concurrent engineering refers to bringing engineering and manufacturing personnel together early in the design phase.
- 6 One difference between sequential and concurrent design is that concurrent design uses a “cost-plus” approach rather than “price minus” approach
- 7 Quality function deployment is a method of integrating the “voice of the customer” into the design process.
- 8 The concern for the environment during product design and manufacture is currently limited to the United States and has not yet become important in other countries.
- 9 Technical and strategic analysis is the first step in completing a feasibility study. 10 Maintainability refers to how long the product will perform its intended function.
- 11 Basic research, applied research and development are all part of the product life cycle.

**Ans.** (1)(T), (2)(F), (3)(T), (4)(T) (5)(T), (6)(F), (7)(T), (8)(F), (9)(F), (10)(F), (11)(F),

**(b) Multiple Choice Questions:**

1. In a competitive business, innovation is no longer
  - (a) Optional, but necessary
  - (b) Necessary, but optional
  - (c) Competitive
  - (d) None of the above
  
2. Innovation
  - (a) is invention plus creativity
  - (b) is invention plus commercialization
  - (c) is invention plus globalization
  - (d) none of the above

3. commoditization is the result of
  - (a) globalization
  - (b) innovation
  - (c) efficient logistics
  - (d) all of the above
  
4. The only innovations that are of interest to firms are those that
  - (a) Contribute to sales
  - (b) Contribute to profit
  - (c) Contribute to charity
  - (d) None of the above
  
5. The assumption reversals
  - (a) Are a sign of confusion
  - (b) are a result of weak management of innovation
  - (c) are a tool to gain a new and innovative perspective on a product, market or service
  - (d) are none of the above
  
6. The iPod and iTunes are
  - (a) Innovative products
  - (b) Creative products
  - (c) Complementary products
  - (d) Profitable products
  
7. Thomas Edison, working 150 years ago, would
  - (a) Not have been successful in the 21<sup>st</sup> century
  - (b) have been a poor manager in today's world
  - (c) not recognize innovation as we know it today
  - (d) none of the above
  
8. In Apple's iPod business model. Apple makes money
  - (a) From both iTunes and iPod
  - (b) With iTunes
  - (c) By selling iPods
  - (d) Somewhere else
  
9. Rates of return on successful innovations typically average
  - (a) Under 15%
  - (b) Around 25%

- (c) Over 40%
  - (d) Over 50%
10. Traditional business average rates of return in the range of
- (a) Around 30%
  - (b) Around 15%
  - (c) Around 10%
  - (d) Around 5%
11. US asset base today consists of intellectual assets (patents, copyrights and the like) that comprise what percent of total assets:
- (a) Around 1%
  - (b) Around 10%
  - (c) Around 40%
  - (d) Around 85%
12. Successful innovations are
- (a) style-conscious
  - (b) action-oriented
  - (c) smart and quick
  - (d) all of the above
13. innovations provide
- (a) the primary means for differentiating your product from your competitors'
  - (b) higher profit margins
  - (c) potential barriers to entry
  - (d) all of the above
14. Digital services benefit from innovation because
- (a) There is no shelf space to pay for
  - (b) no manufacturing costs
  - (c) low distribution fees
  - (d) all of the above
15. The most profitable 'Long Tail' companies are the ones that
- (a) offer the largest choice
  - (b) scale on database size, not factory output
  - (c) offer opportunities for transforming physical distribution into lower cost and scalable digital distribution

- (d) all of the above
- 
- 16. Successful innovation happens in four realms
    - (a) new products, new technologies, new markets, new ways of matching firm assets and competences
    - (b) commercialization, globalization, capitalization, commoditization
    - (c) Eeny, Meeny, Miney, Moe
    - (d) none of the above
  
  - 17. The core competences a firm need to acquire
    - (a) depend on the maturity of the underlying technology
    - (b) depend on their competitors
    - (c) should be purchased
    - (d) none of the above
  
  - 18. In the era of ferment
    - (a) well developed scientific theories provide the raw material for emerging technologies
    - (b) technology and standards are fluid, and do not necessarily perform well
    - (c) standards have been agreed upon, risk may be lowered sufficiently to warrant innovation
    - (d) all of the above
  
  - 19. Profitability of an innovation is determined by
    - (a) the nature of the innovation
    - (b) barriers to entry in imitating it
    - (c) understanding complements required to complete the innovation
    - (d) all of the above
  
  - 20. The majority of innovations
    - (a) are 'incremental' in that they make no demands for significant change in firm competences or markets
    - (b) are 'radical' in requiring a complete reengineering of their competences
    - (c) are 'progressive' in requiring management of market transitions
    - (d) none of the above
  
  - 21. The early automotive industry parallels other more recent technologies in the following way:

- (a) the automotive industry developed in a "knowledge cluster"
  - (b) the U.S. patent system was used to stifle creativity
  - (c) the most successful product did not possess better technology (d) all of the above
22. Ford succeeded because of
- (a) good marketing
  - (b) good technology
  - (c) sound production
  - (d) all of the above
23. Altering Innovations are also known as:
- (a) Incremental Innovation]
  - (b) Modular Innovation
  - (c) Radical Innovation
  - (d) Causal innovation
24. The model in which the consumer needs are regarded as the key driver of the innovation process is known as:
- (a) Market Pull
  - (b) Technology Push
  - (c) None of the above
  - (d) All of the above
25. Common causes of failure within the innovation process in most organization are as under:
- (a) Poor goal definition
  - (b) Poor communication and access to information
  - (c) Poor participation in teams
  - (d) Poor management
26. All of the above\_\_\_\_\_ is the process by which technology is disseminated.
- (a) Technology Transfer
  - (b) Technology Acquisition
  - (c) Technology Absorption
  - (d) Technology Diffusion
27. Direct technology transfer usually occurs through formal arrangement between any of the following:

i) enterprise to enterprise ii)  
government to enterprise iii)  
government to government

- (a) Only (i)
- (b) Only (iii)
- (c) Both (i) and (iii)
- (d) All the above

28 Acquisition of critical technical personnel is a method of:

- (a) informal technology transfer
- (b) formal technology transfer
- (c) outsourcing of technology
- (d) joint ventures

29 Under the internal technology transfer the control of ownership and usage of technology resides with the \_\_\_\_\_:

- (a) User
- (b) Recipient
- (c) Transferor
- (d) Transferee

30 \_\_\_\_\_ is a mechanism used under external technology transfer:

- i) Licensing ii)  
Contracting
- iii) Strategic alliance iv)  
Scientific meeting

- (a) Only (i)
- (b) only (iv)
- (c) (i) , (ii) and (iii)
- (d) All the above.

31. "Not-invented-here (NIH) syndrome," "I already known it (IAKI)," "Prove it to me

(PITM)," and "How on Earth could my firm possibly do that" are

- (a) legitimate reasons to maintain a conservative innovation policy
- (b) innovation's worst enemies (c) signs of weak management



- (d) none of the above
32. Core capabilities
- (a) consume your resources
  - (b) generate resources
  - (c) are generally outsourced
  - (d) none of the above
33. Innovations are responsible for
- (a) generating future resources to support the acquisition of future capabilities
  - (b) competing in a competitive marketplace
  - (c) taking competitive advantage of new technologies
  - (d) all of the above
34. The consumption chain
- (a) identifies the trigger events that precipitate customer movement from link to link
  - (b) defines the marketing channels for a potential innovation
  - (c) details the time sequence of the consumer experience for a potential innovation
  - (d) all of the above
35. Quiz to
- (a) assess needs that may not be met currently
  - (b) find a profitable niche in the competitive terrain
  - (c) understand and explore the consumer experience
  - (d) all of the above
36. Create an attribute-feature map for
- (a) each significant link in the Consumption Chain
  - (b) for the product in general
  - (c) to know what to manage to keep the customer consuming the innovation
  - (d) all of the above
37. When the competitive environment is moving fast (innovating)
- (a) complexity creates confusion and delay
  - (b) the ability to simplify means to eliminate the unnecessary so that the necessary may speak
  - (c) Any intelligent fool can make things bigger, more complex, and more violent. It takes a touch of genius - and a lot of courage - to move in the opposite direction.
  - (d) all of the above

38. Innovators order and manage complexity by
- (a) identifying generic business models
  - (b) identifying action strategies
  - (c) exercising their ability to capitalize on uncertainty and to take calculated risks
  - (d) all of the above
39. Innovation
- (a) requires crazy, out-of-the-box thinking
  - (b) is seldom radical and completely new
  - (c) never reconfigures existing services, business models and products
  - (d) all of above
40. Reconfiguration
- (a) breaks down technological, regulatory or organizational limits on the features you can offer
  - (b) changes the consumption chain
  - (c) changes the attribute map
  - (d) changes the business plan
41. Your '@Innovation Analysis Toolkit' consists of:
- (a) quizzing, and organization of resulting insights through Mind Maps
  - (b) the Consumption Chain
  - (c) the Attribute-Feature Map
  - (d) all of the above
42. Changing behaviour through unstructured group interaction is most accurately referred to As:
- (a) Sensitivity training
  - (b) Process consultation
  - (c) Team building
  - (d) Survey feedback
  - (e) Intergroup development
43. Which of the following situational factors is unlikely to facilitate cultural change
- (a) Leadership changes hands
  - (b) The organization is young and small
  - (c) The culture is strong
  - (d) The culture is weak

- (e) A dramatic crisis occur
44. An important characteristic of process reengineering is:
- (a) It works from bottom up in the organization
  - (b) It involves continually improving the quality of organizational activities that are basically ok
  - (c) It is initiated by top management
  - (d) It involves continuous, incremental changes
45. An example of an internal force for change is:
- (a) Technology
  - (b) Govt. laws and regulations
  - (c) Market place
  - (d) Work force
  - (e) Economic changes
46. Innovation is encouraged in an organization which:
- (a) has an organic structure, accepts ambiguity and has high job security
  - (b) has an organic structure, avoids ambiguity and has high job security
  - (c) has an bureaucratic structure, accepts ambiguity and has high job security
  - (d) has an organic structure, accepts ambiguity and has low job security
47. Which of the following is not an organizational development technique?
- (a) Process Consultation
  - (b) Affirmative action
  - (c) Sensitivity training
  - (d) Survey feedback
48. Which of the following is *not* an example of technological change?
- (a) Automation
  - (b) Improved tools or operating minds
  - (c) Renovation
  - (d) Computerization
49. The CEO plays an essential role in the change process by:
- (a) Showing strong leadership
  - (b) Giving his managers free reign
  - (c) Avoiding impacting on the employees values and perceptions

- (d) Setting the vision, and then allowing the organization to turn this into practice
50. The use of coercion as a change tactic:
- (a) Can be used as a basis of the change process
  - (b) Is an effective and efficient unpopular method
  - (c) Is unpopular, ineffective and can be illegal
  - (d) Is a standard practice in the early stages of change management?
51. Which of the following is not a factor in stimulating innovation within a nation?
- (a) There are strong support industries.
  - (b) Knowledgeable customers in the home market maintain pressure for improvement.
  - (c) Growing industries are protected from international competition.
  - (d) Firms and nations overcome shortages of scarce and specialized resources (e) Competition stimulates investment, cost reduction and general improvement.
52. 'Embedded in teams ... collective rules of thumb, hunches and skills'.
- (a) Tacit knowledge
  - (b) Tactical knowledge
  - (c) Explicit knowledge
  - (d) Organizational culture
  - (e) Creativity
  - (f) Inventiveness
53. According to Chaharbaghi and Newman, what roles are needed at different phases of the innovation process?
- (a) Inventors; incubators; consolidators
  - (b) Inventors; implementors; stabilisers
  - (c) Unfreezing agent; change agent; refreezing agent (d) Stormers; normers; performers (e) None of the above choices.
54. Why, according to the text, is it so difficult to select innovators?
- (a) A. Problems in observing innovativeness mean that psychometric tests cannot be calibrated.
  - (b) B. Biographical data is a good predictor but referees rarely refer to innovativeness.
  - (c) C. Successful responses to tests may depend more on leadership or lucidity than on innovativeness.

- (d) D.Candidates with good records of innovation may have been in favourable roles.
  - (e) A and C
  - (f) A, B and C
55. What reasons lie behind resistance to closer integration of R&D with other business functions?
- (a) Many managers are frustrated at the slow rate of progress in R&D.
  - (b) R&D managers show little understanding of the business world while other managers show little understanding of technology.
  - (c) Managers in different functions operate in dissimilar time frames.
  - (d) Different functions use incompatible methods of allocating and controlling budgets.
  - (e) Managers understand little of technology and there are differences in the personal backgrounds and organization of managers in other functions.
56. Which statement about innovative firms is untrue?
- (a) After an acquisition, the rate of innovation slows in both firms.
  - (b) If firms do not innovate, they are doomed.
  - (c) Firms that commit themselves to internal innovation tend to do better.
  - (d) When traded, innovative firms command higher prices.
  - (e) Innovative firms can gain income through granting licenses to others.
  - (f) In accounts, intellectual property cannot be counted as an asset.
57. What is the innovation gap?
- (a) An opening that can be exploited by an entrepreneur with a good idea
  - (b) The time that elapses between invention and innovation
  - (c) Restriction in the flow of new product ideas
  - (d) An opening that rivals might exploit
  - (e) Shortage of funds during the development phase
  - (f) A nation's lack of inventiveness
58. Which of the following shows the process of creating something new?
- (a) Business model
  - (b) Modeling
  - (c) Creative flexibility
  - (d) Innovation
59. Which one of the following is the next stage to the Concept Stage of Product Planning and Development Process?

- (a) Idea Stage
- (b) Product Planning Stage
- (c) Product Development Stage
- (d) Test Marketing Stage

60. Which one of the following is the most important characteristic of a successful business website?

- (a) Innovation
- (b) Speed
- (c) Graphics
- (d) Products

**Ans.** (1)(a), (2)(b), (3)(d) , (4)(b), (5)(c), (6)(c), (7)(d), (8)(c), (9)(d), (10)(b), (11)(c), (12)(b), (13)(d), (14)(d), (15)(d), (16)(a) (17)(a), (18)(b) (19)(d), (20)(a) (21)(d), (22)(d),(23)(c), (24)(a), (25)(d),(26)(a), (27)(d), (28)(a), (29)(c),(30)(c), (31)(b), (32)(a), (33)(a)(34)(d), (35)(d) (36)(d), (37)(b) (38)(c), (39)(d), (40)(a), (41)(d), 42(b) ,43(b), 44(a), 45(c), 46(b), 47(b), 48(c), 49(d), 50(c), 51(c), 52(a), 53(e), 54(e), 55(e), 56(f), 57(b), 58(d), 59(c), 60(b)

**(c) Fill in the Blanks:**

- 1 Innovation is primarily driven by the main goal of \_\_\_\_\_ and, consequently improving \_\_\_\_\_.
- 2 Ideas for innovation can come from \_\_\_\_\_, \_\_\_\_\_ and \_\_\_\_\_.
- 3 \_\_\_\_\_ refers to the organized efforts of the organization directed towards increasing scientific knowledge and product innovation.
- 4 The adoption of innovation means taking new product/processes/services from \_\_\_\_\_ to \_\_\_\_\_ and then to \_\_\_\_\_.
- 5 \_\_\_\_\_ is a Japanese concept of continuous improvement.
- 6 In \_\_\_\_\_ innovations there is high degree of flexibility to environmental feedback.
- 7 Innovation process needs support at three levels which are \_\_\_\_\_, \_\_\_\_\_ and \_\_\_\_\_.
- 8 \_\_\_\_\_ means long – term orientation/approach of the nation or organization towards innovation.
- 9 \_\_\_\_\_ means linking of engineering, science and management disciplines to plan, develop and implement technological capabilities to shape and accomplish the strategic and operational objectives of an organization.
- 10 \_\_\_\_\_ can be defined as the process by which new technological ideas are generated, developed and transformed into new business products, services and processes that are used to make profits and establish a marketplace advantage.

- 11 \_\_\_\_\_ Innovation is a change of product structure with no significant effect on component technologies.
- 12 Kaizen works well in \_\_\_\_\_ economy and has \_\_\_\_\_ effect on organizational system.
- 13 When a firm seeks to be the first to introduce innovation and aims at tapping fir mover advantages like increased reputation, early profits, the strategy in this case is known as \_\_\_\_\_
- 14 The purpose of \_\_\_\_\_ is to generate a large number of ideas.
- 15 The first idea reducing stage is \_\_\_\_\_ , which helps spot good ideas and drop poor ones as soon as possible.
- 16 A \_\_\_\_\_ is a detailed version of the idea stated in meaningful consumer terms.
- 17 A \_\_\_\_\_ is the way consumers perceive an actual or potential product.
- 18 An attractive idea must be developed into a \_\_\_\_\_.

**Ans.** (1)(Driving Growth and Improving Shareholder Value), (2)(Users (i.e. customers), Manufacturers (i.e. competitors) and Suppliers of raw materials(, (3)(Research and Development), (4)(R&D to manufacturing and then to markets), (5)(Kaizen), (6)(Open Innovation), (7)(Macro level, Enterprise Level and Individual Level), (8)(Innovision), (9)(Management of Innovation), (10)(Technovation), (11)(Architectural Innovation), (12)(Slow growth economy, Long Term effect), (13)(Innovation Leader)(14)(idea generation)(15)(idea screening)(16)( product concept)(17) (product image) (18)( product concept)

## **II Short Answer Type Questions:**

- 1 “Innovation is broader than R&D”. Elaborate the statement.
- 2 “Innovation is different from Kaizen”. Do you agree with this statement? If yes, why? If not, why not? Justify your answer.
- 3 Distinguish between incremental and radical innovation with the help of an example. Name some transformational tools used for the purpose.
- 4 Discuss briefly the radical and cyclic innovation processes.
- 5 Discuss some sources/ideas for Innovation?
- 6 What are the practical tools for process innovation?
- 7 How can you differentiate Disruptive Innovation from Sustaining Innovation?
- 8 What is innovation? What are its dynamics?
- 9 What do you understand by innovative organizations? What are their essential features? What are the different types of innovative organizations?
- 10 Explain any linear model of innovation in detail.
- 11 Differentiate between innovation and invention.

- 12 What are the key steps in becoming an innovative Organisation? 13 Compare TQM and BPR approaches to process Innovation.
- 14 Explain the 'Market Pull' and 'Technology push' Models of Innovation using Examples.
- 15 What is Innovision? What are its dynamics?
- 16 Explain any linear model of innovation in detail.
- 17 Distinguish between the following innovations with the help of an example:
- (a) Incremental
  - (b) Modular
  - (c) Architectural
  - (d) Radical
- 18 Differentiate between innovation and invention.
- 19 Why should innovations pose challenges?
- 20 What are the management functions that contribute to successful implementation of innovations in organizations?
- 21 How is innovation strategy in the context of services different from innovation strategy in the context of goods?
- 22 What factors favor innovation as a strategic activity?
- 23 How does implementation differ for product innovation and process innovation?
- 24 What are the key issues that should be addressed in implementing the innovation strategy?
- 25 The more the number of ideas being generated and reviewed, the more likely the firm will find a viable solution for its future. Comment.
- 26 Internal capabilities for innovative environment. Comment.
- 27 Role of leadership for change and innovation. Comment.
- 28 Discuss Innovation strategy of a firm while establishing the culture of innovation
- 29 Differentiate b/w modular and architectural innovation 30 What do you mean by BPR approach to process Innovation? 31 Differentiate b/w incremental & radical innovation
- 32 What is product innovation? Explain using examples.
- 33 What is process innovation? How value chain model is helpful in this?
- 34 Distinguish between Discovery, Invention and Innovation
- 35 Distinguish between Mass Production and Mass customization 36 Describe the various sources for generation of ideas 37 What is attribute-feature map?
- 38 Describe the Common causes of failure within the innovation process in most organizations.
- 39 What are the Major sources of organizational resistance?
- 40 Discuss how a leader can nurture the culture for innovation and change in an organization.
- 41 "Innovative firms have dissimilar cultures." Comment upon the statement. 42 How do you encourage innovation in an organization?



- 43 What is disruptive innovation?  
 44 How do you measure innovation results and outcomes?

### III Long Answer Type Questions:

- 1 Different R&D centers located at different places produce different technologies for achieving similar goals". Discuss the validity of statement.
- 2 What are the important factors for successful management of innovation process? Why do innovations fail?
- 3 Explain the concept of technology/technological innovation. What are the facilitating factors for technological innovation? What are the barriers to technological innovation?
- 4 Which industries in India are pioneering the technological innovation? Demonstrate giving examples of pioneering firms and their innovative performance.
- 5 'Changes in processes of an organization are inevitable in the light of innovation adoption'. Discuss in detail.
- 6 Describe the Traditional Gate Phase Model of Innovation in detail.
- 7 What is meant by Economics of Innovation? What are the various risks associated with Innovation?
- 8 What are the features/characteristics of Innovation? Mention few advantages of Innovation.
- 9 "Innovation brings changes in the organization". Discuss this statement with few live examples.
- 10 Discuss autonomous & induced inventions. What are the various learning experiences in the light of these inventions?
- 11 What are the important factors for successful management of innovation process? Why do innovations fail?
- 12 What is Process Innovation? What are the factors for Process Innovation?
- 13 What are the steps involved in Process Innovation? Discuss some tools for Process innovation.
- 14 On what factors does the Innovation Strategies depend? How does a firm change from one strategy to another?
- 15 Discuss the concept of Concurrent Engineering in detail.
- 16 "Innovation is the act of introducing something new or something newly introduced". Discuss.
- 17 "Invention is the creation of a new product, service or process". Explain 18 Explain the Flexible model of innovation 19 Write notes on the following:
  - (a) Product Innovation (b) Process Innovation
  - (c) Technovation
  - (d) Cyclic Innovation
  - (e) R&D

- (f) Innovision
- 20 Differentiate between the following:
- (a) Invention vs Innovation
  - (b) Process Innovation vs Innovation Process
  - (c) Technology Push vs Market Pull
- 21 What are the key challenges before a large firm and a small firm in terms of innovation management? Describe the characteristics of innovative firms
- 22 Name some important innovation models prevalent in organizations. Describe in details linear model of innovation.
- 23 What are the four key issues that should be addressed in implementing an innovation strategy? Briefly define and review the issues.
- 24 What factors favor innovation as a strategic activity? What are the possible hindrances to pursuing such strategy?
- 25 Discuss the difference between newness creation and process changes in the innovation arena. Which do you think is more difficult and why?
- 26 Why Concurrent Engineering approach is beneficial over the traditional approach to product design. What are the common bottlenecks in Concurrent Engineering approach?
- 27 What are the key challenges before a large firm and a small firm in terms of innovation management? Describe the characteristics of innovative firms.
- 28 Name some important innovation models prevalent in organizations. Describe in details linear model of innovation.
- 29 How can innovations be channelized involving people at work?
- 30 What are the common barriers to innovation? Explain with the help of suitable examples.
- 31 Which are the two most likely areas of a company to face challenges posed by innovations?
- 32 Kurt Lewin proposed the three stage model of the change process for moving the organization from the present position to the changed one. Discuss.
- 33 What are innovative firms? Explain the role of organizational climate in the making of an innovative firm. Do all innovative firms have similar culture?
- 34 What do you mean by innovative strategy of a firm? Explain various types of innovative strategies giving examples
- 35 What is process innovation? How Value Chain Model is helpful in this?
- 36 Discuss various organizational and individual resistances to change. How can you overcome these resistances?
37. What is “Process Innovation”? How do technology firms design these innovations.
38. Discuss Branscomb’s model of Innovation Management? What are its merits and Demerits.
39. What important role can leaders play in transforming organizations? Discuss in the light of the contributions made by Steve Jobs in APPLE?
40. Distinguish between the following innovations with the help of an example:
- Incremental

- Modular
  - Architectural
  - Radical
41. Discuss the major types on Innovation strategies generally adopted by organizations.
  42. What is innovation culture? Where does it come from? Why is innovation so important for an organization?
  43. Why is creativity and innovations so important for the entrepreneurs?
  44. What are the benefits of a culture that encourages creativity and innovation?

## **UNIT - IV**

### **I Test Your Skills:**

#### **(a) State whether the following statements are True or False:**

- 1 Lateral thinking is a substitute for linear thinking.
- 2 Problem solving usually involves application of logic for finding solution on the plane of existing knowledge.
- 3 Mere discovery of an already existing principle is known as Invention.
- 4 TLC is becoming longer due to fast technological changes or technological discontinuities.
- 5 Lateral thinking may be illogical and it forces the mind to look at other planes of knowledge. Creativity is about thinking something new and whatever this new idea is implemented it brings change.
- 6 Creativity is a one-time/isolated activity.
- 7 Creative thinking involves seeking answers to questions or problems.
- 8 Open-ended questions are very helpful for idea generation as these elicit a wide range of answers.
- 9 Creativity can play a significant role in the growth and long-term survival of an organization.
- 10 Autocratic Functioning of the top management, lack of respect for individual initiatives, intolerance for honest mistakes, etc. adversely affect the degree of creativity in the organization/enterprise.
- 11 At the individual level, one's own thought process, attitudes and approaches become a great barrier to individual creativity.
- 12 We become less creative as we gradually become older.
- 13 As we grow older, we stop asking discovery questions—what if, why not, how etc.
- 14 Our mind captures inputs according to the existing pattern of perceptions and the mind is generally not willing to go beyond a set pattern of perceptions.
- 15 High IQ of the individual may act as a barrier to creativity, as the person/thinker may be trapped in a particular way of thinking.

- 16 Creativity is a resource which has to be managed at the firm's level for obtaining continuous improvement and innovation.
- 17 Lateral thinking is a substitute for linear thinking
- 18 Lateral and linear thinking are complementary to each other 19 Creativity requires high degree of awareness.
- 20 Creativity involves pattern breaking.
- 21 Creativity can be stimulated only at individual level.
- 22 Creativity is about thinking something new and whatever this new idea is implemented it brings change.
- 23 Creativity is a one-time/isolated activity.
- 24 Creative thinking involves seeking answers to questions or problems.
- 25 Open-ended questions are very helpful for idea generation as these elicit a wide range of answers.

**Ans.** (1)(F), (2)(T), (3)(F), (4)(F), (5)(T) (6)( F), (7)(T), (8)(T), (9)(T),(10)(T) (11)(T), (12)(T), (13)(T), (14)(T) (15)(T) (16)(T) (17)(F) (18)(T)(19)(T),( 20)( T)(21)(F),(22)(T),(23)(F), (24)(T),(25)( T)

**(b) Multiple Choice Questions:**

- 1 The inventions which occur spontaneously rather than in response to environmental impulse is known as:
- (a) Autonomous Invention
  - (b) Induced Invention
  - (c) None of these
- 2 Morphological Analysis combines concepts of:
- (a) Fractionalization of problem into smaller parts and use of checklists.
  - (b) Slip Writing and Brainstorming
  - (c) Use of Metaphors and Analogies and Suspending Judgment
- 3 When a firm seeks to be the first to introduce technological changes; it is known as:
- (a) Technology Followership Strategy
  - (b) Technology Leadership Strategy
  - (c) None of these
- 4 Creativity helps in the growth of organization through:
- (a) Generation of ideas for new technologies, new products, new services
  - (b) Generation of ideas for converting process waste into useful byproducts
  - (c) Generation of ideas for improvement in human resources

- (d) All of the above
5. According to Porter, creativity has the following five elements (a) Fluency, flexibility, originality, awareness, drive  
(b) Flexibility, transparency, originality, awareness, drive  
(c) Adequacy, flexibility, originality, awareness, drive  
(d) Adaptability, flexibility, originality, awareness, drive
6. Which is not a characteristic of creativity  
(a) Creativity is not a product but a process  
(b) Creativity involves only conscious thinking  
(c) Can be both systematic and unsystematic  
(d) Can be stimulated at the individual as well as group level.
7. Creativity is a resource which has to be managed at the firm's level for obtaining continuous improvement and innovation Stimulating individual and group creativity  
(a) Providing right organizational support  
(b) Supporting inventive individuals by respecting individual initiatives  
(c) Setting an inventive environment by allowing room for failures and tolerance for honest mistakes  
(d) All the above
8. Techniques used for stimulating individual creativity are  
(a) encouraging lateral thinking  
(b) using check lists  
(c) morphological analysis  
(d) all the above
9. Role of creativity in organizational growth  
(a) Generation of ideas for new technologies, new products, new services  
(b) Generation of ideas for improvement in product/service and process design  
(c) Generation of ideas for improvement in human resources  
(d) Generation of ideas for improvement in productive capacity  
(e) All the above
10. Decreases in the Federal discount rate are examples of  
(a) Economic forces in the external environment that create change in organizations.

- (b) Forces internal to the organization that create change.
  - (c) Technological forces that create organizational change.
  - (d) Labor market fluctuations that create change in organizations
11. Job dissatisfaction, rising absenteeism, and labor strikes are forces for change that are
- (a) Created by governmental regulation.
  - (b) Internal to the organization.
  - (c) External to the organization.
  - (d) Impossible for management to overcome.
12. Lewin's model that describes a calm waters theory of organizational change
- (a) Requires unfreezing the status quo, introducing change, and then refreezing the change into a new state of equilibrium.
  - (b) Is more applicable to rapidly changing industries such as the software industry.
  - (c) Is more universally applicable to all industries.
  - (d) Is what most managers face today
13. Putting a project team structure in place and empowering employees at lower levels of the organization
- (a) Increases automation
  - (b) A structural response to changes in the environment
  - (c) Is a technological response to change
  - (d) Centralizes decision making and controls waste
14. Organizational development is a method of creating change in organizations that
- (a) Uses lower levels of employees to train top management.
  - (b) Would be useful in helping employees become more accepting of diversity in the workplace.
  - (c) Usually backfires
  - (d) Sends any employee requesting it to college.
15. A major reason why people resist change is that
- (a) They enjoying changing work habits and existing attitudes.
  - (b) They know they won't lose their jobs when there is a change in the organization.
  - (c) They dislike ambiguity and uncertainty.
  - (d) They prefer ambiguity and uncertainty.
16. One of the more commonly used means of reducing resistance to change and creating a positive attitude toward it

- (a) To simply give people the choice of “my way or the highway” and let them deal with it.
  - (b) To involve the employees the change will affect in planning for how it will occur.
  - (c) Is to spring it as a big surprise.
  - (d) To let the union make the change.
17. A favorable condition that facilitates cultural change in an organization
- (a) Is when top management doesn't follow new company policies. (b) A strong, well-entrenched and bureaucratic culture.
  - (c) Is a dramatic crisis such as the Enron scandal, because it shocks people into recognizing the need for a change toward more ethical values.
  - (d) Is when it is very large and has had success in the past doing it in an established way.
18. Stress is physical and psychological tension created when (a) Outcomes are both uncertain and important.
- (b) Outcomes are certain.
  - (c) People feel their lives are in balance.
  - (d) They really don't care what happens.
19. One way that managers can reduce employee stress is to
- (a) Make sure an employee's abilities match the job description.
  - (b) Reduce downward communication and let the grapevine take over.
  - (c) Change an employee's job description without telling the person first.
  - (d) Decrease challenges and increase workload
20. Managers in the organization who act as catalysts and take responsibility for the change process are called
- (a) Consultants
  - (b) Change Agents
  - (c) Team Members
  - (d) Creators
21. The calm waters metaphor for change as exemplified by Lewin's model proposes that change is (a) Constant
- (b) Rapid (c) None
  - (d) Both

22. Although some managers live in a calm waters environment, the number of managers facing the white-water model is rapidly
- (a) Increasing
  - (b) Decreasing
  - (c) Constant
  - (d) None of the above
23. An internal change that requires that employees to learn new skills is
- (a) Automation
  - (b) Creation
  - (c) Compulsion
  - (d) Confusion
24. Weak cultures are particularly ----- to change because employees have become so committed to them.
- (a) Resistant
  - (b) Acceptance
  - (c) No impact
  - (d) Agreement
25. Stress is not necessarily bad
- (a) True
  - (b) False
  - (c) Cannot be determined
26. Creativity is the ----- as innovation
- (a) Same
  - (b) Different
  - (c) Not related
  - (d) Opposite
27. Corporate level strategies are usually described as (a) Integrated, growth, or renewal.
- (b) Growth, stability, or renewal.
  - (c) Vertically and horizontally integrated
  - (d) Threats



28. At a time when an industry is involved in rapid change and great uncertainty, or when a company is already stretched to its limits, a strategy of \_\_\_\_\_ would be a wise choice.
- (a) The rule of three
  - (b) Growth
  - (c) Stretching beyond its limits
  - (d) Stability
29. Cost cutting and reorganization are necessary in
- (a) The BCG strategies
  - (b) Growth strategies
  - (c) Retrenchment and turnaround strategies
  - (d) All of Porter's strategies.
30. A strategically appropriate organization culture is important to an organization's success because
- (a) It is very strong.
  - (b) It fits the firm's chosen strategy.
  - (c) It is very weak
  - (d) It can be shared with other organizations.
31. Lateral thinking was coined by
- (a) Edward de Bono
  - (b) Porter
  - (c) William
  - (d) None of the above
32. In traditional type of thinking i.e. linear thinking, there is
- (a) Forward movement by taking a number of sequential steps
  - (b) Backward movement by taking a number of sequential steps
  - (c) Horizontal movement by taking a number of sequential steps
  - (d) Downward movement by taking a number of sequential steps
33. Problem solving usually involves application of logic and skills for finding solution on the plane of known/existing knowledge as.
- (a) Done by further investigations
  - (b) Done by improved skill capability
  - (c) Pursued path may be complex but it is still on the same plane.
  - (d) All the above

34. Techniques used for lateral thinking are
- (a) suspending judgment
  - (b) dismantling or fractionalization of problem into parts
  - (c) reversal of problem
  - (d) use of metaphors and analogies and random words
  - (e) all the above
35. Techniques used for stimulating group creativity
- (a) Slip writing
  - (b) Brainstorming
  - (c) In-basket
  - (d) All the above
36. Linear thinking is:
- (a) Logical
  - (b) illogical or intuitive
  - (c) does not force a mind to look at other planes of knowledge.
  - (d) All of the above
37. The forward movement can be in (a) Vertical direction
- (b) Horizontal direction
  - (c) both vertical as well as horizontal directions
  - (d) Any direction
38. Your products fall into several categories with very different production methods for each category. Because of this, you might consider departmentalizing by .
- (a) implementation
  - (b) method
  - (c) production
  - (d) process
39. The structure that combines functional and product departmentalization is the ....
- (a) matrix structure
  - (b) simple structure
  - (c) bureaucracy
  - (d) team structure
40. You have eliminated horizontal, vertical, and external barriers within your organization. You are operating as a ....

- (a) matrix organization
  - (b) virtual organization
  - (c) team structure
  - (d) boundaryless organization
- 41 Intuitive, affective or feeling, physical/sensing, and rational or reasoning are aspects of which of the following?
- 54. Gifted students
  - 55. Multiple intelligencies
  - 56. Learning styles
  - 57. Creativity
42. Keeping a group focused, offering compromises that are accepted by the group, being listened to and respected by group members, and eliciting agreement from others are attributes of which of the following?
- (a) Gifted students
  - (b) Multiple intelligencies
  - (c) Learning styles
  - (d) Creativity
43. There is growing concern about the number of students who are being misdiagnosed as having a specific learning disability or AD/HD when in fact they are
- (a) Mentally retarded
  - (b) Gifted
  - (c) Emotionally disturbed
  - (d) Dyslexic
44. Emotionally intelligent individuals are described as having specific characteristics associated with self-awareness, impulse control, persistence, self-motivation, empathy, hope, and.
- (a) Happiness
  - (b) Sensitivity
  - (c) Concern
  - (d) Optimism
- 45 Two challenges in evaluating a student for giftedness are the validity and reliability of the tests is questionable, and standardized tests
- (a) Are unfair
  - (b) Do not give good information
  - (c) Discriminate against some students

- (d) Produce anxiety

46 Providing opportunities for applying interests, acquiring advanced-level understanding of the content and process used within particular disciplines, developing authentic products, developing self-directed learning, and empowering students to control learning through organization and feelings of accomplishment are elements of which of the following?

- (e) Type I enrichment
- (f) Type II enrichment
- (g) Type III enrichment
- (h) Non specific enrichment

47 High general intellect; specific academic aptitude; creative, productive thinking; leadership ability; and visual and performing artistry are traits of which of the following?

- (a) Gifted students
- (b) Multiple intelligencies
- (c) Learning styles
- (d) Creativity

48 Instead of just presenting information in words through text or lectures, teachers who use multiple intelligences use physical and social experiences, music, and \_\_\_\_\_ the natural world.

- (a) Engagement with
- (b) Enrichment
- (c) Enhancement
- (d) Differentiated instruction

49. \_\_\_\_\_ refers to adding instruction on disciplines not found in the typical curriculum, using more challenging material, using an expanded range of instructional strategies, and teaching critical thinking and problem-solving skills.

- (a) Multiple intelligences
- (b) Enrichment
- (c) Enhancement
- (d) Differentiated instruction

50. \_\_\_\_\_ assists students in dealing with the socioeconomic issues that might accompany their giftedness.

- (a) Differentiated instruction
- (b) Curriculum extension
- (c) Cognitive taxonomy

- (d) The autonomous learning model
51. Who viewed that thinking is the organization and reorganization of current learning in the present circumstances?
- (a) G. W. Allport (1924)
  - (b) Vinacke (1968)
  - (c) L. F. Shaffer (1936)
  - (d) T.G.Andrews (1948)
  - (e) Hanfmann and Kasanin (1937)
52. “Peripheral theory of thinking” is otherwise known as:
- (a) Affective approach of Thinking
  - (b) Cognitive approach of Thinking
  - (c) Motor Theory of Thinking
  - (d) Stimulus Response Theory of Thinking
  - (e) None of the above
53. The “Central theory of thinking,” which holds that we think with our brain only, was advanced by the:
- (a) Behaviourists
  - (b) Structuralists
  - (c) Functionalists
  - (d) Gestalt Psychologists
  - (e) None of the above
54. In reasoning, the association begins with a problem and end with a/an:
- (a) Problem
  - (b) Solution
  - (c) Image
  - (d) Dream
  - (e) None of the above
55. Psychologists believe that people have ways of thinking in their peculiar and more or less in a fixed way. They call these as:
- (a) Thinking sets
  - (b) Concepts
  - (c) Images
  - (d) Fantasies
  - (e) None of the above

56. “Problem Solving” and “Creative Thinking” are two main forms of:
- (a) Autistic Thinking
  - (b) Directed Thinking
  - (c) Image
  - (d) Realistic Thinking
  - (e) None of the above
57. When we just start completely agreeing with some deduced results or principles and try to apply to particular cases, it is known as:
- (a) Deductive Reasoning
  - (b) Inductive Reasoning
  - (c) Divergent Thinking
  - (d) Convergent Thinking
  - (e) None of the above
58. When we make use of many experiences and examples for arriving at a generalized principle or conclusion, it is known as:
- (a) Deductive Reasoning
  - (b) Divergent Thinking
  - (c) Convergent Thinking
  - (d) Inductive Reasoning
  - (e) None of the above
59. The last stage of Creative Thinking is:
- (a) Verification
  - (b) Evaluation
  - (c) Incubation
  - (d) Preparation
  - (e) None of the above
60. The ideas which were interfering with the solution of the problem tend to fade in:
- (a) Evaluation Period
  - (b) Incubation Period
  - (c) Verification Period
  - (d) Preparation Period
  - (e) None of the above

**Ans.** (1)(a), (2)(a), (3)(b), (4)(d) (5)(a)(6)(b) (7)(e), (8)(d), (9)(e) ,(10)(A),(11)(B),(12)(A), (13)(B), (14)(B), (15)(C), (16)(B), (17)(C), (18)(A), (19)(A), (20)(B), (21)(C), (22)(A), (23)(A),(24)(B),(25)(A),(26)(B),(27)(A),(28)(D),(29)(C),(30)(B),(31)(A),(32)(A),(33)(D)

(34)(E),(35)(D),(36)(A), (37)(C), (38)(D),(39)(A),(40)(D),41(b), 42(b), 43(d)44(c), 45(d), 46(d), 47(d), 48(a), 49(d), 50(d) ), 51(b), 52(c), 53(d), 54(b), 55(a), 56(d), 57(a), 58(d), 59(a), 60(b)

**(c) Fill in the Blanks:**

- 1 \_\_\_\_\_ means to involve one's own thought or imagination to create something new as work of an art, an invention.
- 2 \_\_\_\_\_ thinking is logical and pursues a definite path.
- 3 In \_\_\_\_\_ member of a group are asked to respond to a central problem or theme.
- 4 \_\_\_\_\_ and \_\_\_\_\_ are the techniques used for stimulating individual creativity.
- 5 Induced Inventions are guided by the motive of \_\_\_\_\_.
- 6 For stimulating group creativity the techniques used are \_\_\_\_\_ and \_\_\_\_\_.
- 7 The elements of creativity are \_\_\_\_\_, \_\_\_\_\_, \_\_\_\_\_, \_\_\_\_\_ and \_\_\_\_\_.
- 8 \_\_\_\_\_ advantages influence enterprise's technology strategy.
- 9 Internalization Oriented Strategy aims at seeking technological development with an objective to become\_\_\_\_\_.
- 10 In Autonomous Inventions technology is transferred through \_\_\_\_\_.
- 11 The invention whose promotion depends upon the corporate investment and market requirement is \_\_\_\_\_ invention.
- 12 Many a times, we are too anxious to get the 'right' answer and, in the process, we----- our vision.
- 13 Sometimes, we are too willing to reject 'bad' ideas because of our ----- attitude

**Ans.** (1)(Creativity), (2)(Lateral), (3)(Brainstorming), (4)(Encouraging Lateral Thinking and Using Checklists), (5)(Economic Gain), (6)(Brainstorming and Slip Writing), (7)(Fluency, Flexibility, Originality, Awareness, Motivation), (8)(First Mover), (9)(Internally self reliant), (10)(Informal processes like exchange through scientific meeting), (11)(Induced)(12)( restrict)(13)( risk-averse)

**II Short Answer Type Questions:**

- 1 What is creativity? Explain the role of creativity in organizational growth with the help of suitable example.
- 2 What factors hinder creativity? Explain briefly how creativity can be stimulated by organizations.
- 3 What do you understand by lateral thinking? How it is different from linear thinking?

- 4 What are various techniques for encouraging lateral thinking?
- 5 Discuss autonomous and induced inventions.
- 6 What are the various learning experiences in the light of autonomous and induced inventions?
- 7 What are the characteristics of creativity?
- 8 What are the five elements of creativity? Discuss it.
- 9 Write a note on Management of Creativity.
- 10 What do you understand by term invention? Differentiate between autonomous and induced inventions.
- 11 List the prominent distinguishing characteristics of highly creative people.
- 12 What is creative problem-solving approach? Explain. 13 Discuss the five-stage process of thinking.
- 14 Explain the 'thinking hat' framework of thinking.
- 15 Write short note on creative problem-solving approach.
- 16 Distinguish between creative problem solving and lateral problem-solving approach.
- 17 Explain cooperation and competition for value creation.
- 18 Comment on customer as a source of knowledge.
- 19 In the context of innovations and change management, discuss the need of the ability to create options.
- 20 Comment on 'capability to move from one option to another'
- 21 Discuss the need of 'Empowerment to decide'.
- 22 What is creativity? How is it related to innovation?
- 23 What factors influence the Technology Strategy at enterprise level?
- 24 Justify the statement "Creativity is not a one – time activity"
- 25 "People are born creative". Do you agree with the statement? Discuss. 26  
Discuss common characteristics of creative people.
- 27 Elaborate on "Organizations can ensure creativity management amongst their employees" 28 Explain elements of creativity.
- 29 What jobs require creativity. Can creativity be trained?
- 30 Is creativity a strategic priority. Explain?
- 31 What are the different phases of critical thinking?
- 32 Determine the ways that enhance creative abilities?
- 33 What do you mean by open ended problem solving?

### **III Long Answer Type Questions:**

- 1 Write a detailed note on technological development in India.
- 2 Discuss recent technological changes which have took place in our country.



- 3 Mention various techniques used for stimulating individual creativity. Discuss them in detail.
- 4 “Do not go where a path may lead, go instead where there is no path and leave a trail”. Highlight the importance of creativity by keeping this statement in mind.
- 5 What are not inventions? Discuss some of them.
- 6 All inventions may not be commercialized/adopted. Elaborate.
- 7 Creativity requires high degree of awareness. Is it true? If yes, how? If not, why not?
- 8 Creativity is largely an individual activity, but its management is largely an organizational activity. Elaborate the statement with the help of example.
- 9 Creativity is not a one – time activity. Discuss.
- 10 Linear Thinking pursues a new path but lateral thinking may be illogical or intuitive. Discuss
- 11 Write a detailed note on Creative Problem Solving Approach.
- 12 Broadly discuss the two types of Invention in detail.
- 13 Technological changes have undergone sea change in nature since the advent of 1990s. Elaborate the statement. What are the reasons fro such a change in the nature of technological changes?
- 14 Discuss briefly various approaches fro technology development in a country.
- 15 What do you understand by technology strategy of a firm? What factors influence it?
- 16 What do you mean by technology development? Explain in detail. 17 How can technology be used to encourage creativity?
- 18 “Creativity involves both conscious and subconscious thinking. “Discuss”
- 19 Discuss various Technology Strategies at Enterprise Level. What factors influence the Technology Strategy at enterprise level?
- 20 Write notes on the following:
  - (a) Slip Writing
  - (b) Brainstorming
- 21 Explain the six thinking that framework for managing lateral thinking. What factors Push in or restrict creative thinking in organizations.
- 22 Distinguish between creative thinking and lateral thinking. “lateral thinking brings radical changes”. Comment.
- 23 What do you understand by ‘design for environment’ and ‘design for safety’? Give examples.
- 24 Explain the Six hat theory of innovation
- 25 Discuss the elements that are common to all creative people.
- 26 “People are born creative” Do you agree with the statement? Support your answer with examples.

27. Discuss various models of Innovation management. Do you think holistic model of innovation management is effective in modern times?
28. Compare Holistic Model of Innovation Management with Linear Model of Innovation Management
29. Discuss various steps in the creative thinking process. How can organizations ensure creativity management amongst their employees?
30. What are the steps involved in Problem Solving? How can we build the problem-solving skills in the manpower in an organization?
31. Write notes on the following:
  - a.) Changing technological advancements
  - b.) P.M. Narendra Modi's vision of "Make In India."
32. What do you mean by Blooms Taxonomy. Explain with the help of examples.
33. What do you mean by Socratic questions? Why it is called the heart of creative thinking?
34. Does innovation suffer because senior executives require "ironclad" assurances of success? Explain with the help of examples.
35. Which current management practice does the most to stifle or kill creativity and innovation within the organization?
36. What is the role of senior leadership and managers? Do managers think of themselves as innovators? If not, why not?

# QUESTION BANK

# FINANCIAL MANAGEMENT

## MS-104

### QUESTION BANK FINANCIAL MANAGEMENT - MS 104 MBA II

#### UNIT - I

##### I Test Your Skills:

##### (a) State Whether the Following Statements are true or false:

- 1 Capital budgeting is a responsibility of the Treasurer.
- 2 Cash management is a responsibility of the Controller.
- 3 The asset management decision involves determining the optimal firm size and the assets that should be acquired or eliminated.
- 4 The financing decision involves determining how the assets will be financed with regards to the type and mix as well as the best dividend policy.
- 5 The greater the ownership percentage of managers, then the more likely the managers will behave in a shareholder wealth maximizing behavior.
- 6 The present value interest factor of an (ordinary) annuity (PVIFA) is the reciprocal of the future value interest factor of an (ordinary) annuity (FVIFA).
- 7 All other things being equal, I'd rather have Rs.10,000 in 10 years than to receive Rs.10,000 today.
- 8 The rate of interest is used to express the time value of money.

- 9 The current ratio is never larger than the quick ratio.
- 10 A problem with a balance sheet based on historical costs is that in a period of inflation a company with old fixed assets will show a much better return on investment than a similar firm with new fixed assets.
- 11 A short average collection period assures us that accounts receivable are being efficiently managed.
- 12 A firm's operating cycle is equal to its inventory turnover in days (ITD) plus its receivable turnover in days (RTD).
- 13 A high inventory turnover would be more important to a dairy company than to a jewelry store.

**Ans.** (1)(T), (2)(F), (3)(F), (4)(T), (5)(T), (6)(F), (7)(F), (8)(T), (9)(F), (10)(T), (11)(F), (12)(T), (13)(T)

**(b) Multiple Choice Questions:**

- 1 Which of the following statements is correct regarding profit maximization as the primary goal of the firm?
- (a) Profit maximization will not lead to increasing short-term profits at the expense of lowering expected future profits
  - (b) Profit maximization is concerned more with maximizing net income than the stock price
- 2 Which of the following is not normally a responsibility of the treasurer of the modern corporation but rather the controller?
- (a) Financing management
  - (b) Budgets and forecasts
- 3 The \_\_\_\_\_ decision involves determining the appropriate make-up of the right-hand side of the balance sheet.
- (a) Capital Budgeting
  - (b) Financing
- 4 Which of the following is *not* normally a responsibility of the controller of the modern corporation?
- (a) Financial reporting to the IRS
  - (b) Asset management.

- 5 Which of the following statements is *not* correct regarding earnings per share (EPS) maximization as the primary goal of the firm?
- (a) EPS maximization is concerned with maximizing net income
  - (b) EPS maximization does not specify the timing or duration of expected EPS.
- 6 In 2 years you are to receive Rs.10, 000. If the interest rate were to suddenly decrease, the present value of that future amount to you would \_\_\_\_\_.
- (a) Rise
  - (b) Fall
- 7 To increase a given future value, the discount rate should be adjusted \_\_\_\_\_.
- (a) Upward
  - (b) Downward
- 8 Determine a firm's total asset turnover (TAT) if its net profit margin is 5 percent, assets are Rs.8 million, and ROI is 8 percent.
- (a) 1.60
  - (b) 2.05
  - (c) 2.50
  - (d) 4.00
- 9 Which of the following would not improve the current ratio?
- (a) Borrow short term to finance additional fixed assets
  - (b) Issue long-term debt to buy inventory
  - (c) Sell common stock to reduce current liabilities
  - (d) Sell fixed assets to reduce accounts payable
- 10 The gross profit margin is unchanged, but the net profit margin declined over the same period. This could have happened if \_\_\_\_\_. (a) cost of goods sold increased relative to sales
- (b) sales increased relative to expenses
  - (c) govt. increased the tax rate
  - (d) dividends were decreased
- 11 A company can improve (lower) its debt-to-total asset ratio by doing which of the following?
- (a) Borrow more
  - (b) Shift short-term to long-term debt

- (c) Shift long-term to short-term debt
  - (d) Sell common stock
- 12 Which of the following statements (in general) is correct?
- (a) A low receivables turnover is desirable
  - (b) The lower the total debt-to-equity ratio, the lower the financial risk for a firm
  - (c) An increase in net profit margin with no change in sales or assets means a weaker ROI
  - (d) The higher the tax rate for a firm, the lower the interest coverage ratio
- 13 Which of the following statements is the least likely to be correct?
- (a) A firm that has a high degree of business risk is less likely to want to incur financial risk
  - (b) There exists little or no negotiation with suppliers of capital regarding the financing needs of the firm
  - (c) Financial ratios are relevant for making internal comparisons
  - (d) It is important to make external comparisons of financial ratios
- 14 Which of the following statements is most accurate?
- (a) Coverage ratios also shed light on the "liquidity" of these current ratios
  - (b) Receivable- and inventory-based activity ratios also shed light on the "liquidity" of these current assets.
  - (c) Receivable- and inventory-based activity ratios also shed light on the firm's use of financial leverage.
  - (d) Liquidity ratios also shed light on the firm's use of financial leverage
- 15 The DuPont Approach breaks down the earning power on shareholders' book value (ROE) as follows:  $ROE = \underline{\hspace{2cm}}$ .
- (a) Net profit margin  $\times$  Total asset turnover  $\times$  Equity multiplier
  - (b) Total asset turnover  $\times$  Gross profit margin  $\times$  Debt ratio
  - (c) Total asset turnover  $\times$  Net profit margin
  - (d) Total asset turnover  $\times$  Gross profit margin  $\times$  Equity multiplier
- 16 Which group of ratios measures a firm's ability to meet short-term obligations? (a) Liquidity ratios (b) Debt ratios.
- (c) Coverage ratios
  - (d) Profitability ratios
  - (e) Activity ratios

- 17 Which group of ratios relate the financial charges of a firm to its ability to service them?  
(a) Liquidity ratios (b) Debt ratios.  
(c) Coverage ratios  
(d) Profitability ratios  
(e) Activity ratios
- 18 Which group of ratios measures how effectively the firm is using its assets? (a) Liquidity ratios (b) Debt ratios.  
(c) Coverage ratios  
(d) Profitability ratios  
(e) Activity ratios
- 19 According to the accounting profession, which of the following would be considered a cash-flow item from a "financing" activity? (a) A cash outflow to the government for taxes  
(b) A cash outflow to repurchase the firm's own common stock  
(c) A cash outflow to lenders as interest  
(d) A cash outflow to purchase bonds issued by another company
- 20 An examination of the sources and uses of funds is part of: (a) a forecasting technique (b) a funds flow analysis.  
(c) a ratio analysis  
(d) calculations for preparing the balance sheet
- 21 Which of the following is not a cash outflow for the firm?  
(a) Depreciation  
(b) Dividends  
(c) Interest payments  
(d) Taxes
22. The \_\_\_\_\_ decision involves determining the appropriate make-up of the right-hand side of the balance sheet.  
(a) asset management  
(b) financing  
(c) investment  
(d) capital budgeting
23. To whom does the Treasurer most likely report? (a) Chief Financial Officer.  
(b) Vice President of Operations.  
(c) Chief Executive Officer.

- (d) Board of Directors.
24. The \_\_\_\_\_ decision involves a determination of the total amount of assets needed, the composition of the assets, and whether any assets need to be reduced, eliminated, or replaced.
- (a) asset management
  - (b) financing
  - (c) investment
  - (d) accounting
25. How are earnings per share calculated?
- (a) Use the income statement to determine earnings after taxes (net income) and divide by the previous period's earnings after taxes. Then subtract 1 from the previously calculated value.
  - (b) Use the income statement to determine earnings after taxes (net income) and divide by the number of common shares outstanding.
  - (c) Use the income statement to determine earnings after taxes (net income) and divide by the number of common and preferred shares outstanding.
  - (d) Use the income statement to determine earnings after taxes (net income) and divide by the forecasted period's earnings after taxes. Then subtract 1 from the previously calculated value.
26. What is the most important of the three financial management decisions?
- (a) Asset management decision.
  - (b) Financing decision.
  - (c) Investment decision.
  - (d) Accounting decision.
27. The \_\_\_\_\_ decision involves efficiently managing the assets on the balance sheet on a day-to-day basis, especially current assets.
- (a) asset management
  - (b) financing
  - (c) investment
  - (d) accounting
28. Which of the following is not a perquisite (perk)?
- (a) Company-provided automobile.
  - (b) Expensive office.
  - (c) Salary.
  - (d) Country club membership.



29. Which of the following is not normally a responsibility of the controller of the modern corporation?

- (a) Budgets and forecasts.
- (b) Asset management.
- (c) Financial reporting to the IRS.
- (d) Cost accounting.

30. All constituencies with a stake in the fortunes of the company are known as \_\_\_\_\_.

- (a) shareholders

- (b) stakeholders
  - (c) creditors
  - (d) customers
31. Which of the following statements is not correct regarding earnings per share (EPS) maximization as the primary goal of the firm?
- (a) EPS maximization ignores the firm's risk level.
  - (b) EPS maximization does not specify the timing or duration of expected EPS.
  - (c) EPS maximization naturally requires all earnings to be retained.
  - (d) EPS maximization is concerned with maximizing net income.
32. \_\_\_\_\_ is concerned with the maximization of a firm's stock price.
- (a) Shareholder wealth maximization
  - (b) Profit maximization
  - (c) Stakeholder welfare maximization
  - (d) EPS maximization
33. The only viable goal of financial management is:
- (a) profit maximization
  - (b) wealth maximization
  - (c) assets maximization
  - (d) Sales maximization
34. The basic objective of financial management is:
- (a) maximization of profits
  - (b) maximization of shareholders' wealth
  - (c) ensuring financial discipline in the organization
  - (d) none of the above
35. Finance function involves:
- (a) Procurement of finance only
  - (b) Expenditure of funds only
  - (c) Safe custody of funds only
  - (d) Procurement and effective utilization of funds
- 
- (b)
  - (c)
  - (d)

36. The goal of wealth maximization takes into consideration:
- (a) Risk related to uncertainty of returns
  - Timing of expected returns
  - Amount of returns expected
  - All of the above
37. Financial management is mainly concerned with
- (a) Arrangement of funds
  - (b) All aspects of acquiring and utilizing means of financial resources for firm's activities
  - (c) Efficient management of every business
  - (d) None of the above
38. Time value of money explains that:
- (a) A unit of money received today is worth more than a unit received in future
  - (b) A unit of money received today is worth less than a unit received in future
  - (c) A unit of money received today and at some other time in future is equal
  - (d) None of them
39. Time value of money facilitates comparison of cash flows occurring at different time periods by:
- (a) Compounding all cash flows to a common point of time
  - (b) Discounting all cash flows to a common point of time
  - (c) Using either of a or b
  - (d) Neither a nor b
40. If the nominal rate of interest is 10% pa and frequency of compounding is 4 i.e. quarterly compounding, the effective rate of interest will be:
- (a) 10.25% pa
  - (b) 10.38% pa
  - (c) 10% pa
  - (d) None of them
41. Relationship between annual effective rate of interest and annual nominal rate of interest is, if frequency of compounding is more than 1,
- (a) Effective rate < nominal rate
  - (b)
  - (c)
  - (d)

- (b) Effective rate > nominal rate  
(c) Effective rate = nominal rate  
(d) None of these
42. Contribution per unit is Rs. 100. Fixed costs are Rs. 600000. Production and sales are 8000 units. When sales rise:
- (a) Total contribution rises by an amount greater than profit  
Total contribution rises by an amount smaller than profit  
Total contribution and profit rise by the same amount  
Contribution margin drops
43. Contribution per unit is Rs. 100. FC Rs. 600000. Production and sales are 8000 units. Total contribution is:
- (a) Rs. 600000  
(b) Rs. 400000  
(c) Rs. 800000  
(d) None of the above
44. What is the correct equation that calculates P (profit before tax)? Assume, selling price per unit = Rs. S, Variable cost per unit = Rs. V, Number of units sold = U units and Total fixed costs = Rs. F.
- (a)  $P = SV - F$   
(b)  $P = U(S - V) - F$   
(c)  $P = FS - V$   
(d)  $P = S(V - S)$
45. One of the following is not an assumption that underlies CVP analysis.
- (a) Fixed costs per unit will remain the same throughout the relevant range  
(b) Variable cost per unit will increase as sales increases  
(c) Variable costs have a linear relationship with sales  
(d) Selling price is constant throughout the relevant range
46. Which of the following helps analyzing return to equity Shareholders?
- (a) Return on Assets  
(b) Earnings Per Share (c) Net Profit Ratio  
(d) Return on Investment.
- (b)  
(c)  
(d)

47. Return on Assets and Return on Investment Ratios belong to:

- (a) Liquidity Ratios
- (b) Profitability Ratios
- (c) Solvency Ratios
- (d) Turnover

48. XYZ Ltd. has a Debt Equity Ratio of 1.5 as compared to 1.3 Industry average.

It means that the firm has:

- (a) Higher Liquidity  
Higher Financial Risk  
Higher Profitability  
Higher Capital Employed

- (b)
- (c)
- (d)

49. Ratio Analysis can be used to study liquidity, turnover, profitability, etc. of a firm. What does Debt-Equity Ratio help to study?
- (a) Solvency
  - (b) Liquidity
  - (c) Profitability
  - (d) Turnover
50. In Inventory Turnover calculation, what is taken in the numerator?
- (a) Sales
  - (b) Cost of Goods Sold (c) Opening Stock (d) Closing Stock.
51. Which of the following variables defines and explains the concept of finance?
- (a) Inflation
  - (b) Capital structure
  - (c) Risk- free rate of Interest
  - (d) Risk and return
52. Market value of the firm is a result of:
- (a) Investment decision
  - (b) Financing decision
  - (c) Working Capital Management
  - (d) Risk – Return Trade off
53. What is ignored in Principle of Profit Maximization?
- (a) Time Value of Money,
  - (b) Risk
  - (c) Wealth Creation
  - (d) All of the above
54. Discounting technique is used to find out:
- (a) Terminal Value
  - (b) Compounded Value
  - (c) Present Value
  - (d) Future Value
55. An investor wants to increase the Present Value. The rate of discount applied for should be:
- (a) Increased
  - (b) Decreased
  - (c) Any of (a) & (b)
  - (d) None of the above

56. Present Value can be calculated with the help of formula:
- (a)  $(1+r)^n$
  - (b)  $1/(1+r)^n$
  - (c)  $(1+r)^n / 1$
  - (d) None of the above
57. Four-times stock turnover ratio implies\_\_\_\_\_ months inventory holding period.
- (a) 3
  - (b) 2
  - (c) 4
  - (d) 5
58. A two-months debtor collection period implies that debtor turnover ratio is
- (a) 2 times
  - (b) 6 times
  - (c) 5 times
  - (d) 4 times
59. Increase in the amount of bills payable results in:
- (a) Increase in cash
  - (b) Decrease in cash
  - (c) No change in cash
  - (d) Cannot say
60. The preparation of Fund Flow Statement is governed by AS-3 (Revised). The statement is:
- (a) False
  - (b) True
  - (c) Partially True
  - (d) Cannot say
61. While calculating Gross Profit ratio
- (a) Closing stock is deducted from cost of goods sold
  - (b) Closing stock is added to cost of goods sold
  - (c) Closing stock is ignored
  - (d) None of the above
62. What will be the Gross Profit if, total sales are Rs 2,60,000 Cost of net goods sold is Rs 2,00,000 and Sales return is Rs 10,000?
- (a) 13%

- (b) 28%
- (c) 26%
- (d) 20%

63. Du Point Analysis deals with:

- (a) Analysis of Current Assets
- (b) Analysis of Profit
- (c) Capital Budgeting
- (d) Analysis of Fixed Assets

64. Cash Flow Statement is prepared from

- (a) Profit and loss account
- (b) Balance Sheet
- (c) Additional Information
- (d) All of the above

65. The only feasible purpose of financial management is

- (a) Wealth Maximization
- (b) Sales Maximization
- (c) Profit Maximization
- (d) Assets maximization

66. Given Net profit for the year Rs 2, 50,000 Transferred to general reserves Rs 40,000 and old machinery bought for Rs 50,000 was sold for Rs 20,000. Calculate funds from operations.

- (a) Rs 2, 80,000
- (b) Rs 2, 20,000
- (c) Rs 2, 90,000
- (d) Rs 3, 00,000

67. Time value of money indicates that

- (a) A unit of money obtained today is worth more than a unit of money obtained in future
- (b) A unit of money obtained today is worth less than a unit of money obtained in future
- (c) There is no difference in the value of money obtained today and tomorrow
- (d) None of the above

68. Time value of money supports the comparison of cash flows recorded at different time period by

- (a) Discounting all cash flows to a common point of time
- (b) Compounding all cash flows to a common point of time



- (c) Using either a or b
- (d) None of the above

69. Which of the following is the test of the long-term liquidity of a business?

- (a) Interest Coverage Ratio
- (b) Stock Turnover Ratio
- (c) Operating Ratio
- (d) Current Ratio

70. The satisfactory ratio between internal and external equity is \_\_\_\_

- (a) 1:1
- (b) 2:1
- (c) 3:1
- (d) 1.5:1

**Ans.** (1)(b), (2)(b), (3)(b), (4)(b), (5)(a), (6)(a), (7)(a), (8)(a) , (9)(a), (10)(c), (11)(d), (12)(b), (13)(b),(14)(b), (15)(a), (16)(a), (17)(c), (18)(e), (19)(b), (20)(b), (21)(a) 22(b),23(a),24(c), 25(b), 26(c), 27(a), 28(c), 29(b), 30 (b), 31(d), 32(a), (33)(b), (34)(b), (35)(d), (36)(d), (37)(b), (38)(a), (39)(c), (40)(b), (41)(b), (42)(c), (43)(c), (44)(b), (45)(b), (46)(b), (47)(b), (48)(b), (49)(a), (50)(b), (51)(d), (52)(d), (53)(d), 54(c), (55)(b), (56)(b), (57)(a), (58)(b), (59)(a), (60)(a), (61)(a), (62)(d), (63)(d), (64)(d), (65)(a), (66)(a), (67)(a), (68)(c), (69)(a), (70)(a)

**(c) Fill in the Blanks:**

1 \_\_\_\_\_ is concerned with the acquisition, financing, and management of assets with some overall goal in mind.

2 \_\_\_\_\_ is concerned with the maximization of a firm's earnings after taxes 3 \_\_\_\_\_ is the most appropriate goal of the firm.

4 \_\_\_\_\_ is concerned with the branch of economics relating the behavior of principals and their agents.

5 The Treasurer most likely reports to \_\_\_\_\_.

6 The \_\_\_\_\_ decision involves a determination of the total amount of assets needed, the composition of the assets, and whether any assets need to be reduced, eliminated, or replaced.

7 All constituencies with a stake in the fortunes of the company are known as \_\_\_\_\_.

8 \_\_\_\_\_ is concerned with the maximization of a firm's stock price.

9 Interest paid (earned) on only the original principal borrowed (lent) is often referred to as \_\_\_\_\_.

10 Interest paid (earned) on both the original principal borrowed (lent) and previous interest earned is often referred to as \_\_\_\_\_.

**Ans.** (1)(Financial management), (2)(Profit maximization), (3)(Shareholder wealth maximization), (4)(Agency theory), (5)(Chief Financial Officer), (6)(investment), (7)(stakeholders), (8)(Shareholder wealth maximization), (9)(simple interest), (10)(compound interest)

## **II Short Answer Type Questions:**

- 1 Discuss the objectives of the firm. Which of these goals is superior and why?
- 2 What are the major types of financial management decisions that business firms take? Discuss in brief.
- 3 Write short note on functions of a financial manager
- 4 Differentiate between finance and accounting
- 5 Explain the concept of wealth in the context of wealth maximization objective.
- 6 Write a short note on agency problem.
- 7 Discuss how agency problem can be resolved.
- 8 Differentiate between annuity and perpetuity.
- 9 Distinguish between present value and future value.
- 10 Discuss relevance of time value of money in financial decision making?
- 11 Distinguish between cash flow statement and funds flow statement.
- 12 Explain the significance of ratio analysis to an investor?
- 13 What is the objective of calculating profitability ratios?
- 14 What ratios do shareholders evaluate to judge the returns they are earning from a company?
- 15 Describe three broad areas of financial decision making?
- 16 Explain briefly effective rates of discount?
- 17 Explain in brief profitability ratios.
- 18 Explain liquidity ratios.
- 19 Write a short note on Du Pont analysis.
- 20 Briefly explain the concept and importance of common size statements.
- 21 State the methods of conducting financial statement analysis.
- 22 Explain the utility of time series in analyzing the wellbeing of the company.
- 23 What are the assumptions underlying financial statements?
- 24 Write short note on comparative financial statements.
- 25 What are trend ratios?
- 26 What is agency problem?
- 27 How do market forces act to prevent/ minimize the agency problem?
- 28 Explain the concept of continuous compounded rate of interest.

- 29 Write short note in DuPont equation.
- 30 Write short note on International Capital Budgeting decisions.
- 31 Evaluate Wealth-Maximization objective of Financial Management
- 32 What are the main functions of the modern Finance Manager? How do they differ from those of traditional Finance Manager?
- 33 Explain the concept of Time Value of Money
- 34 What do you mean by analysis of financial statements? What are the tools for analysis of financial statements? Explain any two of them.
- 35 Define break even analysis and outline its uses and applications
- 36 Explain the significance and objective of breakeven chart and state the factors which could cause the breakeven point to change.
- 37 What is the significance to financial management, of increase in output, fixed costs, variable cost and selling price?
- 38 Comment on the emerging role of the finance manager in India.
- 39 Discuss the use of financial ratios.
- 40 Write a note on Financial Forecasting.
- 41 Why should a company concentrate primarily on wealth maximization instead of profit maximization?
- 42 State the decisions involved in Financial management.
- 43 How does 'Interest coverage ratio' affects the capital structure.
- 44 M/Lakshmi Electrical Appliances furnish the following information - Calculate net cash flow from financing activities: -

Particulars	31.12.2007	31.12.2008
Equity share capital	2,00,000	4,50,000
10% debentures	1,00,000	.....
6% preference shares	.....	3,00,000

Additional information – (a) Interest paid on debentures Rs. 5,000/-. (b) Dividend paid on equity shares Rs. 40,000/-. (c) Bonus shares were issued to existing shareholders in the ratio of 4:1 during the year.

45. Give four examples of movement between cash and cash equivalents.

### III Long Answer Type Questions:

- 1 Explain the appropriate goal of the firm and why alternative goals are inappropriate.
- 2 “It has been traditionally argued that the objective of a firm is to earn profit, hence the objective of financial management is also profit making.” Comment.
- 3 Explain how the typical corporate firm is organized as it relates to the financial management function.

- 4 “Funds Flow statement presents a decision view of business”. Comment.
- 5 “Return on investments is a single comprehensive measure that contains everything happening within the organization.” Explain the statement.
- 6 Discuss the application of ratio analysis in the interpretation of financial statements and in financial analysis. What are its limitations?
- 7 What do you understand by inter-firm comparison? Explain how accounting ratios are meaningful in the inter-firm comparison.
- 8 Comment on emerging role of finance manager in India 9 What is EVA how is it used?
- 10 What are primary objectives of corporate management in India
- 11 Distinguish between Nominal Interest rates and Effective Interest Rates
- 12 Two companies have the same amount of working capital. The current debt paying ability of one company is much weaker than that of other. Explain how could it occur.
- 13 A uniform system of accounts, including identical forms for balance sheets and income statement is a pre-requisite of inter firm comparison.
- 14 Critically evaluate the goal of maximization of profit and maximization of return on equity.
- 15 Discuss the importance of Ratio Analysis as a tool for analysis and interpretation of financial statements. What are its limitations?
- 16 What are the Basic Financial Decisions? How do they involve risk return trade-off?
- 17 Explain the Limitations of Accounting Ratios?
- 18 Differentiate a Cash Flow Statement from a Funds Flow Statement.
- 19 “Depreciation is a non – cash expenses. Still it is an integral part of cash flows.” Explain.
- 20 Describe in brief the procedure of cash flow from operating activities as per indirect method AS-3. Take a appropriate example to illustrate your answer.
- 21 Two companies have the same amount of working capital. The current debt paying ability of one company is much weaker than the other. Explain how this could occur.
- 22 “The finance manager’s primary task is to plan for the acquisition and use of funds so as to maximize the value of the firm.” Do you agree with the statement? Comment.
- 23 “It is advantageous to decentralize accounting function while finance function should be centralised.’ Comment on the above statement.
- 24 Why is it inappropriate to seek profit maximization as the goal of financial decision making? How would you justify the adoption of present value maximization as an apt substitute for it?
- 25 How do depreciation allowances influence financial planning decisions?
- 26 Explain the relevance of time value of money in financing and investment decisions.
- 27 When can there arise a conflict between shareholders and managers goals? How does wealth maximisation goal take care of this conflict?
- 28 Should the titles of controller and treasurer be adopted under Indian context? Would you like to modify their functions in view of the company practices in India? Justify your opinion.

- 29 'Generally, individuals show a time preference for money.' Give reasons for such a preference.
- 30 Why is the consideration of time important in financial decision-making? How can time value be adjusted? Illustrate your answer.
- 31 Explain the mechanics of calculating the present value of cash flows.
- 32 What do you understand by Fund Flow Analysis? What is its importance? Explain the procedure of preparing: -
- Schedule of changes in working capital
  - Calculation of funds from operation
  - Fund Flows Statements
- 33 What do you mean by comparative financial statements? How are these prepared? Explain their utility.
- 34 What do you mean by common size financial statements? How are these prepared? Explain their utility.
- 35 Distinguish between (i) Fund flow statement and schedule of changes in working capital (ii) Net profit and fund from operation.
- 36 Distinguish between (i) Fund flow statement and cash flow statement. (ii) Cash flow statement and cash budget
- 37 What is the agency problem? How do market forces act to prevent/ minimize this problem? 38. Describe the relationship between finance and economics and explain why the finance manager should possess a basic knowledge of economics.
39. How would you analyse the financial position of a company from the point of view of (a) an investor (b) a creditor and (c) a financial executive of the company?
40. Discuss the limitations of financial ratios as a technique for appraising the financial position of a company.
41. Give the format of cash flow statement under direct method as per AS – 3 (Revised)
42. The managers in an enterprise are responsible for the proper utilization of the resources under their control. Since the resources are acquired in exchange for money, the decision of the managers will ultimately affect the financial condition of the organization. In this sense it can be said that the finance function interfaces with major functions of the enterprise as well as the top management. Briefly explain the interface function of the finance function with marketing and production function and the top management.
43. Explain the treatment of Interest (paid and received) and dividend (paid and received) in operating cash flows and financing cash flows in view of the AS-3 revised.
- 44 'Every Manager has to take three major decisions while performing the finance function' briefly explain them.
45. What is the need for financial analysis? How does the ratio analysis technique help in the financial analysis?
46. Explain the role of ratio analysis in the interpretation of financial statements. Examine the limitations of ratio analysis.

47. Explain the technique of preparing a cash flow statement with imaginary figures.  
 48. What do you mean by funds flow statements? How are they prepared? What are their uses?

**IV Practical Questions:**

- 1 The ABC bank pays 5.60%, compounded daily (based on 360 days), on a 9-month certificate of deposit. If you deposit Rs.20,000 you would expect to earn around \_\_\_\_\_ in interest.

**Ans. Rs.858**

- 2 With continuous compounding at 8 percent for 20 years, what is the approximate future value of a Rs.20,000 initial investment?

**Ans. Rs.99, 061 (Rs.20, 000[e<sup>(.08 × 20)</sup>] = Rs.20,000(4.9530324) = Rs.99,061)**

- 3 What is the present value of a Rs.1, 000 ordinary annuity that earns 8% annually for an infinite number of periods?

**Ans. 12,500**

- 4 PQR has an 8 percent return on total assets of Rs.300, 000 and a net profit margin of 5 percent. What are its sales?

**Ans. 4, 80,000**

- 5 A potential investor is considering the purchase of a bond that has the following characteristics: the bond pays 8% per year on its Rs. 1,000 principal, or face value. The bond will mature in 20 years. At maturity, the bondholder will receive interest for year 20 plus the Rs. 1,000 face value. What is the maximum purchase price that should be paid for this bond if the investor requires a 10% rate of return? **Ans. Rs. 830.12**

- 6 Following are the summarized Balance Sheets of S Ltd. as on 31<sup>st</sup> March, 2008 and 2009. Prepare Funds Flow Statement.

<b>Liabilities</b>	<b>2009</b>	<b>2008</b>	<b>Assets</b>	<b>2009</b>	<b>2008</b>
Share Capital	2,50,000	2,00,000	Land and Building	1,90,000	2,00,000
General Reserve	60,000	50,000	Machinery	1,69,000	1,50,000
P&L A/C	30,600	30,500	Stock	74,000	1,00,000
Debentures	-	70,000	Debtors	64,200	80,000
Creditors	1,35,200	1,50,000	Bank and cash	8,600	500
Provision for tax	35,000	30,000	Goodwill	5,000	-

	5,10,800	5,30,500		5,10,800	5,30,500
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During the year ended 31<sup>st</sup> March, 2009:

Dividend of Rs. 23,000 was paid.

Assets of another company were purchased for a consideration of Rs. 50,000 payable in shares:  
Stock Rs. 20,000, Machinery Rs. 25,000.

Depreciation written off machinery was Rs. 12,000.

Income tax provided during the year was Rs. 33,000.

Loss on sale of machine Rs. 200 was written off to General Reserve.

Machinery for Rs. 8,000 was purchased.

**Ans. Total of FFS: Rs. 1,29,000, Decrease in WC : Rs. 38,900, FFO: Rs. 78,300**

7 The following details relate to X Ltd.

Debtors' Velocity	3 Months
Stock Velocity	8 Times
Fixed Assets Turnover Ratio	8 Times
Creditors' Velocity	2 Months
Capital Turnover Ratio	2.5 times
Gross Profit Turnover Ratio	25%

Gross profit for the year amounted to Rs. 80,000. There is no long-term loan or overdraft. Reserves and Surplus amounted to Rs. 28,000; Liquid Assets are Rs. 97,333. Closing stock is Rs. 2,000 more than the opening stock. Bills receivable amounted to Rs. 5,000 and Bills payable are Rs. 2,000.

Find out:

- (a) Sales            (b) Sundry Debtors  
(c) Closing Stock    (d) Sundry Creditors  
(e) Fixed Assets      (f) Proprietor's Fund.

Also make out the Balance Sheet with as many details as possible.

**Ans. Sales: Rs. 3,20,000; Sundry Debtors: Rs. 75,000; closing stock: Rs. 31,000; creditors;: Rs. 38,333; fixed assets Rs. 40,000; Proprietor's fund: Total capital Rs. 1,28,000 inclusive of reserves of Rs. 28,000. Total of B/S Rs. 1,68,33**

8 Following is the Profit and Loss Account of a company for the year ending 31.3.09

**PROFIT AND LOSS ACCOUNT for the year ending 31.3.2009**

<i>Particulars</i>	<i>Rs.</i>	<i>Particulars</i>	<i>Rs.</i>
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To Opening Stock	1,00,000	By Sales	5,60,000
To Purchases	3,50,000	By Closing Stock	1,00,000
To Wages	9,000		
To Gross Profit c/ d	2,01,000		
	6,60,000		6,60,000
To Administrative Expenses	20,000	By Gross Profit b / d	2,01,000
To Selling Expenses	89,000	By Non-Trading Income	18,000
To Non-Trading Expenses	30,000		
To Net Profit	80,000		
	2,19,000		2,19,000

Calculate: GP Ratio [Ans. 35.89%]

Net Profit Ratio [Ans: 14.29%]

Operating Profit Ratio [Ans. 16.43%]

9 Balance Sheets of a firm as on 1st Jan 2008 and 31st December 2008 were as follows:

<i>Liabilities</i>	1.1.2008	31.12.2008	<i>Assets</i>	1.1.2008	31.12.2008
	<i>Rs.</i>	<i>Rs.</i>		<i>Rs.</i>	<i>Rs.</i>
Creditors	40,000	44,000	Cash	10,000	47,000
Loan from X	25,000	-	Debtors	30,000	50,000
Loan from Y	40,000	50,000	Stock	35,000	25,000
Capital	1,25,000	1,53,000	Machinery	80,000	55,000
			Land	40,000	10,000
			Building	35,000	60,000
	2,30,000	2,47,000		2,30,000	2,47,000

During the year a machine costing Rs.10,000 (accumulated depreciation Rs. 3,000) was sold for Rs. 5,000. The balance of provision for depreciation against machinery as on 1st January 2008 was Rs. 25,000 and on 31st December 2008 Rs. 40,000. Net profit for the year 2008 amounted to Rs.45,000. Prepare Cash Flow Statement.

**Ans. Cash Flow from operating activities: Rs. 59,000; Cash Flow from financing activities: Rs.-32,000; Cash Flow from investing activities: Rs. 10,000.**

10 X Ltd. supplies you the following, Balance Sheets for the year ending 31.12.2007 and 31.12.08.

<i>Liabilities</i>	31.12.07	31.12.08	<i>Assets</i>	31.12.07	31.12.08
Share Capital	70,000	74,000	Bank Balance	9,000	7,800
10% Bonds	12,000	6,000	Sundry Debtors	14,900	17,700
Sundry Creditors	10,360	11,840	Inventories	49,200	42,700
	700	800	Land	20,000	30,000



Provision for doubtful debts			Goodwill	10,000	5,000
P/LA/c	10,040	10,560			--
	1,03,100	1,03,200		1,03,100	1,03,200

Additional Information:

- (a) Dividend paid during 2008, was Rs. 3,500. (b) Land purchased for Rs. 10,000.  
(c) Goodwill written off Rs. 5,000  
(d) Bonds Rs. 6,000 redeemed during 2008.

Prepare Cash Flow Statement for the year-ended 31.12.08.

**Ans. Cash Flow from operating activities: Rs. 14,300; Cash Flow from investing activities: Rs. -10,000; Cash Flow from financing activities: Rs. -5,500**

- 11 The following is the summary of financial ratios of a company relating to its liquidity position

Particulars	Year 1	Year 2	Year 3
Current Ratio	2.00	2.13	2.28
Acid Test Ratio	1.20	1.10	.90
Debtors Turnover	10.00	8.00	7.00
Stock Turnover	6.00	5.00	4.00

The current ratio is increasing, while the acid test ratio is decreasing. Explain the contributing factors for this apparently divergent trend.

- 12 The directors of Precision Tools Ltd. are worried at deteriorating financial position of the company. The company has utilized full overdraft facility from the bank and is still not able to pay its creditors on due dates, although profits earned are satisfactory The following are the balance sheets as on March 31 for the recent 2 years.

	Previous Year		Current Year	
Share Capital: shares of Rs.10 each fully paid		10,00,000		10,00,000
P&L Appropriation A/c		60,000		80,000
Overdraft from Bank		1,60,000		6,00,000
Creditors		2,00,000		6,00,000
		<b>14,20,000</b>		<b>14,20,000</b>
Land and Building		3,00,000		5,00,000

Plant and Machinery <b>Less</b> Depreciation	5,00,000 <u>1,20,000</u>	3,80,000	6,00,000 <u>1,80,000</u>	4,20,000
Vehicles <b>Less</b> Depreciation	1,16,000 <u>56,000</u>	60,000	1,24,000 <u>84,000</u>	40,000
Stock		2,20,000		7,20,000
Debtors		4,60,000		6,00,000
		<b>14,20,000</b>		<b>22,80,000</b>

During the year ,a dividend of 10% was distributed to the shareholders. On 1<sup>st</sup> April of the current year, a motor car, which originally cost Rs.20,000,and showed a book value of Rs. 10,000 was sold for Rs. 16,000.

You are required to prepare a cash flow statement based on AS-3.

**Ans. Cash Flow from operating activities: Rs. 4,12,000; Cash Flow from investing activities: Rs. -3,12,000; Cash Flow from financing activities: Rs. -1,00,000**

13 The XYZ Ltd. financial statement contains the following information:  
Balance Sheet as n 31<sup>st</sup> march, current year

Particulars	Previous Year (in thousand)	Current Year (in thousand)
Cash	200	160
S.Debtors	320	400
Temporary Investments	200	320
Stock	1,840	2,160
Prepaid Expenses	28	12
Total Current Assets	2,088	3,052
Total Assets	5,600	6,400
Current Liabilities	640	800
15% Debentures	1,600	1,600
Eq.Share Capital	2,000	2,000
Retained Earnings	468	904

Statement of Profits year ended March 31, Current Year

Particulars	Rs.(in thousand)
Sales	4,000
<b>Less:</b> Cost of goods sold	2,800
<b>Less:</b> Interest	160
Net profit for current year	1,040
<b>Less:</b> Taxes	364
<b>EAT</b>	676

Dividend Declared on Eq. Shares	220
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From the above, appraise the financial position of the company from the point of view of (a) Liquidity (b) solvency (c) profitability (d) activity

**Ans. The company's position is sound from all the three aspects but the activity ratios do not seem to be adequate**

14 A person require Rs. 20,000 at the beginning of each year from 2010 to 2014. How much should he deposit at the end of each year from 2000 to 2005? The interest rate is 10 percent.

**Ans. Person should deposit Rs. 7069 at the end of each year from 2000 to 2006.**

15 Mr. Sourabh receives a provident fund amount of Rs. 1,00,000. He deposits it in a bank which pays 10 per cent interest. If he withdraws annually Rs. 20,000 how long can he do so?

**Ans. Mr. Sourabh can withdraw Rs. 20,000 annually for 7 years**

16 Balance Sheets of A Ltd. as on 1.1.2010 and 31.12.2010

Liabilities	1.1.2010 (Rs.)	31.12.2010 (Rs.)		1.1.2010 (Rs.)	31.12.2010 (Rs.)
Creditors	40,000	44,000	Assets	10,000	7,000
Mrs. A's Loan	20,000	-	Cash	30,000	50,000
Loan from Bank	40,000	50,000	Debtors	35,000	25,000
Capital	1,25,000	1,53,000	Stock	80,000	55,000
			Machinery	40,000	50,000
			Land	35,000	60,000
			Building		
	2,30,000	2,47,000		2,30,000	2,47,000

During the year a machine costing Rs. 10,000 (Accumulated depreciation Rs. 3,000) was sold for Rs. 5,000. The provision for depreciation against machinery as on 1.1.2010 was Rs. 25,000 and on 31.12.2010 Rs. 40,000. Net profit for the year 2010 amounted to Rs. 45,000.

You are required to prepare a Cash Flow Statement.

**Ans. Cash Flow from Operating Activities – 87,000/-**

**Cash Flow from Investing Activities – 52,000/-**

**Cash Flow from Financing Activities – 50,000/-**

17 Compute cash from operations from the following details:

	<b>31 Dec.2007</b>	<b>31 Dec. 2008</b>
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Debtors	50,000	47,000
Bills receivable	10,000	12,500
Creditors	20,000	25,000
Bills payable	8,000	6,000
Outstanding expenses	1,000	1,200
Prepaid expenses	800	700
Accrued expenses	600	750
Income received in advance	300	250
Profit made during the year	-	1,30,000

**Ans. CFO = 133700**

- 18 Mr. Ramesh will retire at the end of 10 years. Upon retirement, he is entitled to receive an annual end of year payment of Rs. 1,20,000 for 15 years. If he dies prior to the end of the 15 year period, his heirs would be entitled to the contractual payment. His employers, ABC Ltd. has to accumulate funds to provide a retirement annuity by making an equal annual year end deposits into an account earning 7% interest. When the 15 year payment period begins, the company would transfer the accumulated fund into an account earning a guaranteed 9%. At the end of the payment period, the account balance would be zero. (a) How much would the company accumulate by the end of 10<sup>th</sup> year.
- (b) What should be the company's equal annual end of year deposit into the account over the 10 year period to fund fully the retirement annuity.
- (c) How much would the company have to deposit annually during 10 year accumulation period, if it could earn 8%.
- (d) How much would the company have to deposit annually during the 10 year period of accumulation if the retirement annuity was perpetuity.
- 19 XYZ Ltd. is creating a sinking fund to redeem its preference capital of Rs. 5 lakhs issued on Jan. 1, 2002 and maturing on December 31, 2013. The annual investment will start on an. 1, 2002. The company will make equal investment and expects that the fund will earn 12% per year. How much will be the amount to sinking fund payment.

**Ans. Annuity amount = Rs. 18,500**

- 20 In setting up an education fund, a person agrees to make five annual payments of Rs. 5,000 each into a 'college fund programme.' The first payment is to be made 12 years from now and the 'college fund programme' wishes that upon making the last payment, the amount available should have grown to Rs. 30,000. What should be the minimum rate of return on this fund?

**Ans. Slightly higher than 9%. Annuity starting from 12 years from now is irrelevant.**

21 The following are the balance sheets of X Ltd. for the year 2009 and 2010. Prepare a funds flow statement for the year 2010.

<b>Balance Sheet</b>			<b>(Rs. In '000)</b>		
Liabilities	31.12.09	31.12.10	Assets	31.12.09	31.12.10
Share capital	200	320	Goodwill	100	80
8% preference share capital	100	40	Land and Building	200	170
General reserve	40	70	Plant and machinery	80	200
Profit and loss A/c	30	48	Debtors	150	250
Debentures	150	140	Stock	87	59
Sundry creditors	55	83	Debtors	150	250
Bills payable	20	16	Bills receivable	20	30
Proposed dividend	42	50	Preliminary expenses	15	10
Provision for tax	40	50			
<b>Total</b>	<b>677</b>	<b>817</b>		<b>677</b>	<b>817</b>

**Additional Information:**

1. An interim dividend of Rs. 20,000 has been paid in 2010.
2. Rs. 35,000 income tax was paid during the year.
3. Final dividend of Rs. 28,000 was paid during the year 2010.
4. During the year, assets of another company were purchased for a consideration of Rs. 50,000 payable in shares. The assets purchased were stock Rs. 20,000 and machinery Rs. 25,000.
5. Rs. 60,000, 8% preference share capital was redeemed at a premium of 5%.
6. A part of plant was sold for Rs. 20,000 (w.d.v.) Rs. 25,000). Depreciation on plant Rs. 20,000 fro the current year has been provided.
7. The company depreciates land and building by Rs. 10,000. Land costing rs. 20,000 was sold for Rs. 50,000.
8. Equity shares of Rs. 10,000 were issued as bonus shares.
9. Rs. 10,000, 10% debentures were redeemed by purchase in the open market @ Rs. 95.
10. The company also made a right issue of equity shares during the years.

**Ans. FFO: 1,96,500, Total of FFS: 3,26,500, Net increase in working capital: 31,000**

22 The balance sheet of R and Co. Pvt. Ltd. as at March 31, 2009 and 2010 are presented as follows:

	<b>2009</b>	<b>2010</b>

<b>Assets:</b>		
Fixed assets	70,000	88,000
Investment	40,000	40,000
Cash	6,000	8,000
Debtors	7,000	12,000
Prepaid rent	3,600	2,400
Stock	32,000	28,000
	<b>1,58,600</b>	<b>1,78,400</b>
<b>Liabilities:</b>		
Equity capital	50,000	60,000
Profit and loss account	26,400	20,900
Debentures	35,000	35,000
Accumulated depreciation	20,000	21,500
Creditors	7,200	9,000
Taxes payable	6,000	6,000
Bills payable	14,000	26,000
	<b>1,58,600</b>	<b>1,78,400</b>

Additional Information:

1. Purchased a new fixed asset costing Rs. 25,000, paid Rs. 13,000 cash and gave short term bills for the remainder.
2. Issued additional capital for cash.
3. Disposed off a fully depreciated asset having an original cost of Rs. 7,000 and no salvage value.
4. Net profit for the year amounted to Rs. 2,000 (after tax).

Prepare a statement of changes in financial position (cash basis) as per AS-3 (Revised).

- 23 As on 31<sup>st</sup> March, 2012, the paid up capital of Navroj Ltd. was Rs. 1,00,00,000. The ratios as on that date were as under:

Current debt to total debt	0.40
Total debt to equity	0.60
Fixed assets to equity	0.60
Total assets turnover (based on sales)	2 times
Inventory turnover (based on sales)	8 times

Draw the balance sheet of Navroj Ltd.

**Ans. Total of balance sheet :Rs. 1,60,00,000**

24 The capital of growfast co. ltd. is as follows:

10% preference shares of Rs. 10 each	50,00,000 Equity
shares of Rs. 100 each	<u>70,00,000</u>
	<u>1,20,00,000</u>

**Additional information:**

Profit after tax (at 50%)	15,00,000
Depreciation	6,00,000
Equity dividend paid	10%
Market price per equity share	Rs. 200

**Calculate the following:**

**Ans.**

- |                                       |                  |
|---------------------------------------|------------------|
| (i) Cover for the preference dividend | <b>3 times</b>   |
| (ii) Earnings per share               | <b>Rs. 14.29</b> |
| (iii) Price earnings ratio            | <b>14 times</b>  |
| (iv) Net funds flow                   | <b>21,00,000</b> |

25 (a) Deposit reinvestment scheme of Syndicate Bank is a scheme for a period from 1 to 10 years. In this case a small odd sum can be invested and certificate payable on maturity date for a denomination of Rs.10,000, Rs.50,000 and Rs.10,000 are issued. The rate of interest is 12% p.a. compounded quarterly. Find out the issue price of a certificate of Rs.10,000 to be received after 10 years.

**Ans:  $10,000 / 3.262 = \text{Rs. } 3,066$  [CVF<sub>(3%,40)</sub> = 3.262]**

(b) A loan of Rs.10,00,000 is to be repaid over 5 year in equated installments calculated on the basis of an effective rate of interest of 16% per annum. Find (i) equated annual installment, (ii) Capital repaid and interest paid in the first year and the final year.

**Ans: Annuity =  $PV / PVAF_{(16\%, 5\text{yrs})}$**   
**=  $10,00,000 / 3.274$  [PVAF<sub>(16%, 5yrs)</sub> = 3.274]**  
**=  $\text{Rs. } 3,05,436.77$**

26 A partial list of trend and common size percentage for ABC Ltd. For years 1 and 2 is given below:

Particulars	Year 2	Year 1
Trend percentage:		
Sales (Net)	120	100

Cost of goods sold	?	100
Gross profit on sales	?	100
Operating expenses & income taxes	?	100
Net income	?	100
Common size percentage:		
Sales (net)	100	100
Less: cost of goods sold	?	?
Gross profit on sales	40	?
Less: operating express & income taxes	20	25
Net income	20	10
		Rs.20,000

(a) Determine the missing trend and common-size percentage. Compute the net income for year 2

**Ans: COGS 110.77, Gross Profit 137.14, Operating Expenses 96.00, Net Income 240.00, Gross Profit 35.00**

27 A firm purchases a machinery for Rs. 8,00,000 by making a payment of Rs. 1,50,000 and the remainder in equal instalments of Rs. 1,50,000 for 6 years. What is the rate of interest to the firm.

**Ans: 10%**

28 The comparative Balance Sheet of Company A showed the following changes for 31<sup>st</sup> December 2012 and 2013:

Particulars	Amount	Increase/decrease
Working capital	1,27,500	Increase
Long term investment	45,000	Increase
Land	48,000	Increase
Machinery (Less accumulated depreciation)	90,000	Increase
15% Debentures	2,40,000	Increase
Share capital	60,000	Increase
Reserves and Surplus	10,500	Increase

The following additional information is provided:

- i) Net profit for the year was Rs. 1,57,500.
- ii) Accumulated depreciation for 2012 was Rs. 67,500 and for 2013 was 90,000.



- iii) A machine of Rs. 1,12,000 was purchased during the year. Depreciation expenses for the year were Rs. 22,500.
- iv) A bonus issue of shares of Rs. 60,000 was made during the year.
- v) A cash dividend of Rs. 87,000 was declared and paid during the year. Prepare a statement of changes in financial position for Company A.

29. With the following ratios and further information given below, prepare a Trading Account, Profit and Loss Account and a Balance Sheet of ShriNarain

Gross Profit Ratio	25%
Net Profit / Sales	20%
Stock Turnover Ratio	10
Net Profit / Capital	1 / 5
Capital to Total Liabilities	1 / 2
Fixed Assets / Capital	5 / 4
Fixed Assets / Total Current Assets	5 / 7
Fixed Assets	Rs.10,00,000

30. From the following Balance Sheets of ShriHari Synthetics Ltd. prepare a statement of sources and application of funds and as schedule of changes in working capital for 2014.

Liabilities	2006(Rs.)	2007(Rs.)	Assets	2006(Rs.)	2007(Rs.)
Share capital	2,00,000	2,50,000	Land& Building	2,00,000	1,90,000
General Reserve	50,000	60,000	Plant	1,50,000	1,74,000
P & L A/C	30,500	30,600	Stock	1,00,000	74,000
Bank loan(short term)	70,000	-	Debtors	80,000	64,200
Creditors	1,50,000	1,35,200	Cash	500	600
Provision for Taxation	30,000	35,000	Bank	-	8,000
	<u>5,30,500</u>	<u>5,10,800</u>		<u>5,30,500</u>	<u>5,10,800</u>

**Additional information:**

- a) Depreciation was written off plant Rs. 14,000 in 2007
- b) Dividend of Rs. 20,000 was paid during 2007.
- c) Income Tax provision made during the year was Rs. 25,000
- d) A piece of land has been sold during the year at cost.

31. Prepare a fund flow statement from the following Balance sheet:

(figures in thousands)

Liabilities	2007(Rs.)	2008(Rs.)	Assets	2007(Rs.)	2008(Rs.)
Share capital	1,400	1,740	Land	960	800
Reserves & Surplus	600	780	Plant	600	680
Debentures	880	880	Patents	40	36
Discount on Debentures	(80)	(72)	Closing Stock	600	688
Creditors	1,200	1,280	Debtors	400	740
Provision for Depreciation	200	112	Cash	1,600	1,776
	<u>4,200</u>	<u>4,720</u>		<u>4,200</u>	<u>4,720</u>

**Additional information:**

- (a) Net profit for the year Rs.4, 00,000.
- (b) Depreciation charged for the year Rs.4, 00,000.
- (c) Dividend Paid Rs. 80,000.
- (d) Shares issued for cash Rs.2, 00,000 and for bonus Rs. 1, 40,000.
- (e) A building was sold for Rs. 56,000 its cost and book-value being Rs. 1, 60,000 and Rs. 40,000.

32. The following is the summary of the financial ratios of a company relating to its liquidity position.

	Year 1	Year 2	Year 3
Current ratio	2	2.13	2.28
Acid test ratio	1.2	1.1	0.9
Debtors turnover	10	8	7
Stock turnover	6	5	4

The current ratio is increasing, while the acid test ratio is decreasing. Explain the contributing factors for this divergent trend.

33. Mr. X has Rs. 100000 to deposit in a bank account for 3 years. Assuming (i) annual compounding (ii) semi-annual compounding and (iii) quarterly compounding at a stated annual interest rate of 4%, compute (a) the amount he would have at the end of the third year, leaving all interest paid on deposits in the bank, (b), the effective rate of interest he would earn on each alternative, and (c) which plan should he choose?

**Ans.** (a)(i) 112500, (a)(ii) 112600, (a)(iii) 112700, (b)(i) 4%, (b)(ii) 4.04%, (b)(iii) 4.06%, (c)option(iii)

34. Mr. Ritesh is considering to take a life insurance policy of LIC for 20 years. The Insurance agent is advising him to take a money-back policy. The scheme offers money back at the end of 5<sup>th</sup>, 10<sup>th</sup>, 15<sup>th</sup> and 20<sup>th</sup> year to the extent of 25%, 25%, 25% and 50% of the insured amount. The premium he will have to pay is Rs. 62 annually for every Rs. 1000 insured. The insurance agent also informs him that he will get a minimum bonus to the extent of 40% at the end of the insurance term. Mr. Ritesh is of the opinion that the premium for the money back policy is on the higher side. If the banks are offering a rate of 100% on the long term deposits, calculate the effective return on the policy and advice Mr. Ritesh.

**Ans.** If  $i = 100\%$  then PV is -53.935, If  $i = 200\%$  then PV is -29.96. Mr. Ritesh should buy LIC Policy to have better return.

35. Mr. Suresh took a car Loan of Rs. 5,00,000 repayable in annual equal installments of 8 years at 11% rate of interest. Find out the amount of annual payable installment.

**Ans.** Installment = Rs. 97,160.

36. Prepare Cash Flow Statement of Suryan Ltd. from the following:

<b>Balance Sheets</b>					
<i>Liabilities</i>	<i>1.1.06 Rs.</i>	<i>31.12.06 Rs.</i>	<i>Assets</i>	<i>1.1.06 Rs.</i>	<i>31.12.06 Rs.</i>
Share Capital	1,00,000	4,00,000	Goodwill	—	20,000
8% Debentures	—	2,00,000	Machinery	1,25,000	4,75,000
Retained Earnings	60,000	90,000	Stock	20,000	80,000
Creditors	40,000	1,00,000	Debtors	30,000	1,00,000
Bills Payable	20,000	40,000	Cash at Bank	50,000	1,50,000
Provision for Tax	30,000	40,000	Cash in hand	25,000	45,000
	2,50,000	8,70,000		2,50,000	8,70,000

- (a) During 2006, the business of a sole trader was purchased by issuing shares for Rs. 2,00,000. The assets acquired from him were: Goodwill Rs. 20,000, Machinery Rs. 1,00,000, Stock Rs. 50,000 and Debtors Rs. 30,000.
- (b) Provision for tax charged in 2006 was Rs. 35,000.
- (c) The debentures were issued at a premium of 5% which is included in the retained earnings.
- (d) Depreciation charged on machinery was Rs. 30,000.

## UNIT- II

### I Test Your Skills:

#### (a) State Whether the Following Statements are True or False:

- 1 The term 'capital structure' includes also the financial structure.
- 2 The optimum capital structure is obtained when the market value per equity share is the maximum.
- 3 Net income approach and net operating income approach are synonymous terms.
- 4 According to MM Approach, the value of a firm is affected by the debt-equity mix.
- 5 The traditional approach is a mid-way approach between net income approach and net operating income approach.
- 6 The value of a levered firm is higher than that of an unlevered firm on account of corporate taxes.
- 7 The cost of capital is the minimum rate of return that will maintain the value of a firm's equity shares.
- 8 The implicit cost is the discount rate that equates the present value of the funds received by the firm with the present value of expected cash outflows.
- 9 For financial decision making, relevant costs are the historical costs.
- 10 Composite cost is inclusive of all cost of capital from all sources.
- 11 Marginal cost is the weighted average cost of the new funds raised by the firm.
- 12 According to MM Approach, cost of capital is affected by the firm's debt-equity mix. 13  
Retained earnings have no cost to the firm.
- 14 There is no need for calculating separate cost for retained earnings when cost of equity capital is calculated on the basis of the market value of equity shares.
- 15 Market value weights are theoretically consistent and sound as compared to book value weights.
- 16 Adjustment for income tax payable by the shareholder is required while calculating the cost of retained earnings for the company.
- 17 Operating leverage shows the effect on residual net income of long-term funds bearing fixed charges.
- 18 Dividend on preference share capital is ignored while calculating operating leverage. 19  
A high break-even point would indicate a high operating leverage.
- 20 If company A has an operating leverage of '2' and company B has operating leverage of '3' company B has less amount of risk.
- 21 It is risky to have a high operating leverage, since even a slight fall in sales would result in a disproportionately large fall in profits.
- 22 Composite leverage explains change in taxable income on account of change in sales.
- 23 The ideal situation is to have a high financial leverage and low operating leverage.

**Ans.** (1)(F), (2)(T), (3)(F), (4)(F), (5)(T), (6)(T), (7)(T), (8)(F), (9)(F), (10)(T), (11)(T), (12)(F), (13)(F), (14)(T), (15)(T), (16)(T), (17)(F), (18)(F), (19)(T), (20)(F), (21)(T), (22)(T), (23)(T)

(b) **Multiple Choice Questions:**

1. The discount rate used to determine the present value of a stream of expected future cash flows is referred to as the \_\_\_\_\_.
  - (a) net operating income
  - (b) capitalization rate
  - (c) capital structure
  - (d) yield on the company's market value of common equity
  
2. The traditional approach towards the valuation of a company assumes that \_\_\_\_\_.
  - (a) the cost of capital is independent of the capital structure of the firm
  - (b) the firm maintains constant risk regardless of the type of financing employed
  - (c) there exists no optimal capital structure
  - (d) that management can increase the total value of the firm through the judicious use of financial leverage
  
3. The presence of which one of the following costs is not used as a major argument against the M&M arbitrage process?
  - (a) Bankruptcy costs.
  - (b) Agency costs.
  - (c) Transactions costs.
  - (d) Insurance costs.
  
4. The term 'capital structure' also includes the financial structure.
  - (a) True
  - (b) False
  
5. The optimum capital structure is obtained when the market value per equity share is the maximum.
  - (a) True
  - (b) False
  
6. Which of the following statements regarding the net operating income approach is incorrect?
  - (a) The overall capitalization rate,  $k_O$ , is constant.
  - (b) The cost of debt funds,  $k_i$ , is constant.

- (c) The required return on equity,  $k_e$ , is constant.
- (d) The total value of the firm is unaffected by changes in financial leverage.
7. A high break even point would indicate high operating leverage.
- (a) True
- (b) False
8. Which of the following formulas represents a correct calculation of the degree of operating leverage
- (a)  $(Q - Q_{BE})/Q$
- (b)  $(EBIT) / (EBIT - FC)$
- (c)  $[Q(P-V) + FC] / [Q(P-V)]$
- (d)  $[Q(P-V)] / [Q(P-V) - FC]$
9. Composite leverage explains change in taxable income on account of change in sales.
- (a) True
- (b) False
10. Which of the following formulas represents the correct calculation of the degree of financial leverage?
- (a)  $[NI + T + I] / [NI - I - PD/(1-T)]$
- (b)  $EBIT / [EBIT - I - PD/(1-T)]$
- (c)  $EBIT / [NI - I - PD/(1-T)]$
- (d) All of the above are correct methods to calculate the degree of financial leverage (DFL).
11. A firm is considering three different financing alternatives -- debt, preferred stock, and common equity. The firm has created an EBIT-EPS chart that shows several indifference points. What does each indifference point show the firm?
- (a) The level of EBIT that generates identical EPS under two alternative financing plans.
- (b) The level of sales that generates identical EBIT and EPS figures.
- (c) It shows the level of EBIT and EPS at which DFL is identical under two alternative financing plans.
- (d) None of the above.
12. Which of the following statements is correct?
- (a) The coefficient of variation of EBIT,  $CVEBIT$ , is a measure of relative financial risk.

- (b) The coefficient of variation of EPS, CVEPS, is a measure of relative total firm risk.
  - (c) Total firm risk equals business risk times financial risk.
  - (d) A relative measure of relative business risk equals the difference, CVEPS - CVEBIT.
13. The ideal situation is to have a high financial leverage and low operating leverage.
- (a) True
  - (b) False
14. The maximum amount of debt (and other fixed-charge financing) that a firm can adequately service is referred to as the \_\_\_\_\_.
- (a) debt capacity
  - (b) debt-service burden
  - (c) adequacy capacity
  - (d) fixed-charge burden
15. The cash required during a specific period to meet interest expenses and principal payments is referred to as the:
- (a) debt capacity.
  - (b) debt-service burden.
  - (c) adequacy capacity.
  - (d) fixed-charge burden.
16. Which of the following costs would be considered a fixed cost?
- (a) Raw materials.
  - (b) Depreciation.
  - (c) Bad-debt losses.
  - (d) Production labor.
17. Composite cost is inclusive of all cost of capital from all sources.
- (a) True
  - (b) False
18. Marginal cost is the weighted average cost of the new funds raised by the firm.
- (a) True
  - (b) False
19. Retained earnings have no cost to the firm.
- (a) True
  - (b) False

20. Market value weights are theoretically consistent and sound as compared to book value weights.
- (a) True
  - (b) False
21. Cost of capital refers to:
- (a) Floatation costs
  - (b) dividend
  - (c) required rate of return
  - (d) none of the above
22. Which of the following sources of funds has an implicit cost of capital?
- (a) equity share capital
  - (b) preference share capital
  - (c) debentures
  - (d) retained earnings
23. Which of the following has the highest cost of capital?
- (a) equity shares
  - (b) loans
  - (c) bonds
  - (d) preference shares
24. Cost of capital for government securities is also known as:
- (a) risk free rate of interest
  - (b) maximum rate of return
  - (c) rate of interest on fixed deposits
  - (d) none of the above
25. Cost of capital for bonds and debentures is calculated on:
- (a) before tax basis
  - (b) after tax basis
  - (c) risk free rate of interest basis
  - (d) none of the above
26. Which is the correct order for the costs of the following sources of finance if the most expensive is placed first?
1. Debentures.
  2. Preference shares.
  3. Retained earnings.



4. Loan stock.
5. New issue of shares. (a) 1, 2, 3, 4, 5.  
(b) 5, 3, 2, 1, 4.  
(c) 3, 5, 4, 1, 2.  
(d) 5, 3, 4, 2, 1.  
(e) 5, 3, 2, 4, 1.
27. Which of these statements on the cost of different sources of finance is not correct?  
(a) Retained earnings are a cheaper way of raising equity finance than a new issue of shares.  
(b) Preference shares will have a lower cost compared to ordinary shares.  
(c) Convertible debt will have a lower cost of capital compared to ordinary debt.  
(d) The tax deductibility of interest payments reduces the cost of debt.  
(e) Debt finance is always cheaper than equity finance.
28. The overall (weighted average) cost of capital is composed of a weighted average of \_\_\_\_\_.  
(a) the cost of common equity and the cost of debt  
(b) the cost of common equity and the cost of preferred stock  
(c) the cost of preferred stock and the cost of debt  
(d) the cost of common equity, the cost of preferred stock, and the cost of debt
29. What is the overall (weighted average) cost of capital in the following situation? The firm has Rs.10 million in long-term debt, Rs.2 million in preferred stock, and Rs.8 million in common equity -- all at market values. The before-tax cost for debt, preferred stock, and common equity forms of capital are 8%, 9%, and 15%, respectively. Assume a 40% tax rate.  
(a) 6.40%  
(b) 6.54%  
(c) 9.30%  
(d) 10.90%
30. For which of the following costs is it generally necessary to apply a tax adjustment to a yield measure?  
(a) Cost of debt.  
(b) Cost of preferred stock.  
(c) Cost of common equity.  
(d) Cost of retained earnings.
31. Which of the following is not a recognized approach for determining the cost of equity?

- (a) Dividend discount model approach.
  - (b) Before-tax cost of preferred stock plus risk premium approach.
  - (c) Capital-asset pricing model approach.
  - (d) Before-tax cost of debt plus risk premium approach.
32. How is economic value added (EVA) calculated?
- (a) It is the difference between the market value of the firm and the book value of equity.
  - (b) It is the firm's net operating profit after tax (NOPAT) less a rupees cost of capital charge.
  - (c) It is the net income of the firm less a rupees cost that equals the weighted average cost of capital multiplied by the book value of liabilities and equities.
  - (d) None of the above are
33. What is the idea behind project-specific required rates of return for a firm or division?
- (a) Different projects should have different required rates of return because they are not alike with respect to risk.
  - (b) Each firm should have a different required rate of return because firms are not alike with respect to risk and have been created historically by projects taken that differ with regards to risk.
  - (c) A division of the firm will always have a required rate of return different from the firm's overall weighted average cost of capital because the risk of the division always differs from that of the firm.
  - (d) All of the above are
34. A single, overall cost of capital is often used to evaluate projects because:
- (a) it avoids the problem of computing the required rate of return for each investment proposal.
  - (b) it is the only way to measure a firm's required return.
  - (c) it acknowledges that most new investment projects have about the same degree of risk.
  - (d) it acknowledges that most new investment projects offer about the same expected return
35. The cost of equity capital is all of the following EXCEPT:
- (a) the minimum rate that a firm should earn on the equity-financed part of an investment.
  - (b) a return on the equity-financed portion of an investment that, at worst, leaves the market price of the stock unchanged.
  - (c) by far the most difficult component cost to estimate.

- (d) generally lower than the before-tax cost of debt.
36. What is the value of a levered firm L if it has the same EBIT as an unlevered firm U, (with value of Rs. 700 lakh), has a debt of Rs. 200 lakh, tax rate of 35 percent under MM approach? (a) Rs. 770 lakh  
(b) Rs 500 lakh  
(c) Rs. 630 lakh  
(d) Rs 900 lakh
37. According to the traditional approach, what is the effect of increase in degree of leverage on the valuation of the firm?  
(a) Increases  
(b) Decreases  
(c) Remains unaffected  
(d) Increases first and then decreases
38. According to the NOI Approach, with increase in debt/ equity ratio the financial risk of equityholders \_\_\_\_ (a) decreases  
(b) increases  
(c) no change  
(d) Depends on degree of leverage
39. The following is(are) the external source(s) of cash  
(a) Long terms loans  
(b) Short term borrowings  
(c) Issue of new shares  
(d) All of the above
40. DU PONT Analysis deals with:  
(a) Analysis of Current Assets  
(b) Analysis of Profit  
(c) Capital Budgeting  
(d) Analysis of Fixed Assets
41. Cost of Capital refers to:  
(a) Flotation Cost  
(b) Dividend  
(c) Required Rate of Return  
(d) None of the above

42. Which of the following sources of funds has an Implicit Cost of Capital?
- (a) Equity Share Capital
  - (b) Preference Share Capital
  - (c) Debentures
  - (d) Retained earnings
43. Which of the following has the highest cost of capital?
- (a) Equity shares
  - (b) Loans
  - (c) Bonds
  - (d) Preference shares
44. Cost of Capital for Government securities is also known as:
- (a) Risk-free Rate of Interest
  - (b) Maximum Rate of Return
  - (c) Rate of Interest on Fixed Deposits
  - (d) None of the above
45. Cost of Capital for Bonds and Debentures is calculated on:
- (a) Before Tax basis
  - (b) After Tax basis
  - (c) Risk-free Rate of Interest basis
  - (d) None of the above
46. Weighted Average Cost of Capital is generally denoted by:
- (a)  $k_A$ ,
  - (b)  $k_w$ ,
  - (c)  $k_0$ ,
  - (d)  $k_c$
47. Which of the following cost of capital require tax adjustment?
- (a) Cost of Equity Shares
  - (b) Cost of Preference Shares (c) Cost of Debentures (d) Cost of Retained Earnings.
48. Which is the most expensive source of funds?
- (a) New Equity Shares
  - (b) New Preference Shares
  - (c) New Debts

- (d) Retained Earnings
49. Marginal cost of capital is the cost of:
- (a) Additional Sales
  - (b) Additional Funds
  - (c) Additional Interests
  - (d) None of the above
50. In case the firm is all-equity financed, WACC would be equal to:
- (a) Cost of Debt
  - (b) Cost of Equity
  - (c) Neither (a) nor (b)
  - (d) Both (a) and (b)
51. Cost of capital for Bonds and Debentures is calculated on:
- (a) Before –Tax Basis
  - (b) After –Tax Basis
  - (c) Risk - free Rate of Interest basis,
  - (d) None of the above
52. In case of partially debt-financed firm,  $K_o$  is less than :
- (a)  $K_d$  (b)  $K_e$
  - (c) Both (a) & (b)
  - (d) None of the above
53. Advantage of Debt Financing is:
- (a) Interest is tax deductible,
  - (b) It reduces WACC,
  - (c) Does not dilute owners control,
  - (d) All of the above
54. Financial Leverage measures relationship between:
- (a) EBIT and PBT
  - (b) EBIT and EPS
  - (c) Sales and PBT
  - (d) Sales and EPS
55. Which of the following is correct?
- (a)  $CL = OL + FL$
  - (b)  $CL = OL - FL$

- (c)  $CL = OL * FL$
  - (d)  $CL = OL / FL$
56. At Indifference level of EBIT, different capital plans have:
- (a) Same EBIT
  - (b) Same EPS
  - (c) Same PAT
  - (d) Same PBT
57. In Pecking order theory, the first priority is given to:
- (a) Fresh Equity
  - (b) Fresh Loan
  - (c) Mix of Debt & Equity
  - (d) Retained Earnings
58. In MM Model with taxes, where 'r' is the interest rate, 'D' is the total debt and 't' is tax rate, then present value of tax-shields would be:
- (a)  $r * D * t$ ,
  - (b)  $r * D$ , (c)  $D * t$ ,
  - (d)  $(D * r) / (1 - t)$ .
59. 'Judicious use of leverage' is suggested by:
- (a) Net Income Approach
  - (b) Net Operating Income Approach
  - (c) Traditional Approach
  - (d) All of the above
60. In MM Model, irrelevance of capital structure is based on:
- (a) Cost of Debt and Equity
  - (b) Arbitrage Process
  - (c) Decreasing  $K_o$ ,
  - (d) All of the above
61. In weighted average cost of capital, a company can affect its capital cost through
- (a) policy of capital structure
  - (b) policy of dividends
  - (c) policy of investment
  - (d) All of above
62. A firm's degree of operating leverage (DOL) depends primarily upon its

- (a) sales variability
  - (b) level of fixed operating costs
  - (c) closeness to its operating break-even point.
  - (d) Debt to equity ratio
63. If a firm has a DOL of 5 at Q units, this tell us that: (a) if sales rise by 5%, EBIT will rise by 5%
- (b) if sales rise by 1%, EBIT will rise by 1%
  - (c) if sales rise by 5%, EBIT will fall by 25%
  - (d) if sales rise by 1%, EBIT will rise by 5%
64. A single, overall cost of capital is often used to evaluate projects because:
- (a) it avoids the problem of computing the required rate of return for each investment proposal.
  - (b) it is the only way to measure a firm's required return.
  - (c) it acknowledges that most new investment projects have about the same degree of risk.
  - (d) it acknowledges that most new investment projects offer about the same expected return
65. The cost of equity capital is all of the following **EXCEPT**:
- (a) the minimum rate that a firm should earn on the equity-financed part of an investment
  - (b) a return on the equity-financed portion of an investment that, at worst, leaves the market price of the stock unchanged.
  - (c) by far the most difficult component cost to estimate.
  - (d) generally lower than the before-tax cost of debt.
66. To compute the required rate of return for equity in a company using the CAPM, it is necessary to know all of the following **EXCEPT**:
- (a) the risk-free rate.
  - (b) the beta for the firm.
  - (c) the earnings for the next time period.
  - (d) the market return expected for the time period.
67. A critical assumption of the net operating income (NOI) approach to valuation is:
- (a) that debt and equity levels remain unchanged.
  - (b) that dividends increase at a constant rate.
  - (c) that  $k_o$  remains constant regardless of changes in leverage.
  - (d) that interest expense and taxes are included in the calculation.

68. Two firms that are virtually identical except for their capital structure are selling in the market at different values. According to M&M
- (a) one will be at greater risk of bankruptcy.
  - (b) the firm with greater financial leverage will have the higher value.
  - (c) this proves that markets cannot be efficient.
  - (d) this will not continue because arbitrage will eventually cause the firms to sell at the same value.
69. Which term would most likely be associated with the phrase "actions speak louder than words?"
- (a) Incentive signaling.
  - (b) Shareholder wealth maximization.
  - (c) Financial signaling.
  - (d) Optimal capital structure
70. Some projects that a firm accepts will undoubtedly result in zero or negative returns. In light of this fact, it is best if the firm.
- (a) adjusts its hurdle rate (i.e., cost of capital) upward to compensate for this fact.
  - (b) adjusts its hurdle rate (i.e., cost of capital) downward to compensate for this fact.
  - (c) does not adjust its hurdle rate up or down regardless of this fact
  - (d) raises its prices to compensate for this fact.

**Ans.** 1. (b), 2. (d), 3. (d), 4. (b), 5. (a), 6. (c), 7. (a), 8. (d), 9. (a), 10. (b), 11. (a), 12. (b), 13. (a), 14. (a), 15. (b), 16. (b), 17. (a), 18. (a), 19. (b), 20. (a), 21(c), 22(d), 23(a), 24(a), 25(b), 26. (e), 27. (c), 28. (d), 29. (c), 30. (a), 31. (b), 32. (b), 33. (a), 34. (a), 35. (d), (36)(a), (37)(d), (38)(b), (39)(d), (40)(b), (41)(c), (42)(d), (43)(a), (44)(a), (45)(b), (46)(c), (47)(c), (48)(a), (49)(b), (50)(b), (51)(b), (52)(b) (53)(d) (54)(b) (55)(c) (56)(b) (57)(d) (58)(c) (59)(c), (60)(b), (61)(d), (62)(c), (63)(d), (64)(a), (65)(d), (66)(c), (67)(c), (68)(d), (69)(c), (70)(c).

**(c) Fill in the Blanks:**

- 1 \_\_\_\_\_ refers to make-up of a firm's capitalization.
- 2 The arbitrage process is the behavioural foundation for the \_\_\_\_\_
- 3 Optimum leverage can be defined as that mixes of debt and equity which will \_\_\_\_\_ the market value of the firm.
- 4 MM Approach is similar to \_\_\_\_\_ approach.



- 5 \_\_\_\_\_refers to that EBIT level at which EPS remains the same irrespective of the debt-equity mix.
- 6 Cost of capital comprises both business and \_\_\_\_\_risks.
- 7 Cost of each component of capital is termed as \_\_\_\_\_ cost.
- 8 According to traditional approach cost of capital is affected by\_\_\_\_\_.
- 9 According to \_\_\_\_\_approach the investor arrives at the market price of an equity share by capitalizing the set of expected dividends payment.
- 10 According \_\_\_\_\_weights method, weights are assigned to each source of funds in proportion of financing inputs the firm intends to employ.
- 11 MM approach assumes that \_\_\_\_\_markets are perfect.
- 12 Cost of capital serves as \_\_\_\_\_rate of capital investment decisions.
- 13 It is risky to have both operating leverage and \_\_\_\_\_leverage at a high level.
- 14 Financial leverage indicates disproportionate change in taxable income as a result of change in \_\_\_\_\_.
- 15 An ideal situation would be to keep \_\_\_\_\_leverage low and \_\_\_\_\_leverage high.
- 16 A management would be considered too cautious if both operating leverage and financial leverage are kept\_\_\_\_\_.
- 17 The combined effect of operating leverage and financial leverage can be seen by \_\_\_\_\_of the two.
- 18 Trading on equity implies having a \_\_\_\_\_debt-equity ratio.
- 19 The Shareholders of a company's which has a high financial leverage stand to gain when the company's return on investment (ROI) is \_\_\_\_\_ as compared to \_\_\_\_\_ of debt.
- 20 The term trading on equity is generally used for \_\_\_\_\_ financial leverage.

**Ans.** (1)(Capital structure), (2)(MM Hypothesis), (3)(maximize), (4)(NOI), (5)(Point of indifference), (6)(Financial), (7)(Specific), (8)(Debt-equity Mix), (9)(Dividend Price), (10)(Marginal), (11)(Capital), (12)(Cut-off), (13)(Financial), (14)(Operating Income(EBIT), (15)(Operating, Financial), (16)(Low), (17)(Multiplication), (18)(High), (19)(Higher, Cost), (20) (Favourable)

## **II Short Answer Type Questions:**

- 1 Explain the term 'Point of Indifference'.
- 2 Differentiate 'Capitalisation' and 'Capital Structure'.
- 3 What is 'Optimum Capital Structure'?
- 4 Write a note on 'Arbitrage Process'.
- 5 What is meant by Financial Break-even point?

- 6 Explain EBIT-EPS approach for determining capital structure of a company. 7 Write short note on Modigliani-Miller Approach.
- 8 Explain the concept of Marginal Cost of Capital 9 Briefly discuss the rationale of Cost of Capital
- 10 Explain the rationale of using weighted cost of capital.
- 11 “Reserves and surpluses have no cost”. Do you agree? Give reasons for your answer.
- 12 Why is it that the ‘debt’ is the cheapest source of finance for a profit making company?
- 13 What is meant by the concept ‘financial risk’? What is the relationship between leverage and the cost of capital? Explain
- 14 Write notes on
  - (a) Arbitrage process
  - (b) NI and NOI Approaches
- 15 Explain implicit cost of capital.
- 16 What do you mean by target weights.
- 17 What is meant by the term “leverage”? What are its types? 18 What is the indifference point? And why is it called so?
- 19 How to calculate indifference point in the EBIT-EPS analysis?
- 20 Write a critical note on the traditional approach to capital structure.
- 22 What is meant by the concept of “financial risk?
23. Write Short note on Home Made Leverage.
24. Write Short note on Projected Cash Flow analysis.
25. What do you understand by capital structure? What are the major determinants of capital structure?
26. What are the characteristics of a balanced capital structure?
27. Define cost of capital and its importance.
28. Define leverage. What are different types of leverages?
29. Explain the causes of financial risk and operating risk. How can these two be measured?
30. The cost of preference capital is generally lower than cost of equity. State the reasons?

### III Long Answer Type Questions:

- 1 What do you understand by capital structure of a corporation. Discuss the qualities which a sound capital structure should possess.
- 2 Critically examine the Net Income and Net Operating Income approaches to capital structure. What is the traditional view on this question?
- 3 ‘An optimal combination of the decisions relating to investment, financing and dividends will maximize the value of the firm to its shareholders. Examine.
- 4 What do you understand by a Balanced Capital Structure? Why should a company aim at a balanced capital structure?

- 5 Explain the factors that determine the capital structure of a firm.
- 6 There is nothing like an optimal capital structure for a firm. Critically evaluate this statement.
- 7 Show that in the M-M hypothesis under corporate tax:  
$$v_l = v_u + td$$
  
i.e., Value of levered firm = Value of unlevered firm + Present value of tax shield.
- 8 What do you mean by an appropriate capital structure? What should generally be the features of an appropriate capital structure?
- 9 What do you mean by optimum capital structure? Make a list of factors determining optimum capital structure.
- 10 What do you understand by capital structure of a corporation? Discuss the qualities or features of a sound capital structure.
- 11 Explain “Arbitrage Process” under Modigliani/Miller Theorem.
- 12 Explain EBIT-EPS approach for determining capital structure of a company.
- 13 What factors must be considered by a manager when choosing between debt and equity?
- 14 What is the objective of the capital structure management? How might a firm go for determining its optimal capital structure?
- 15 What is Cost of Capital? What is meant by Explicit Cost and Real Cost of capital?
- 16 Define the concept of Cost of Capital. State how you would determine the weighted average cost of capital of a firm.
- 17 Explain the concept of Cost of Capital as a device for establishing a cut-off point of capital investment proposals.
- 18 What is meant by Cost of Capital for a firm and what relevance does it have in decisionmaking? How is it calculated with different types of sources of capital funds? Why is the cost of capital most appropriately measured on an after-tax basis?
- 19 What is Modigliani-Miller approach to the problem of capital structure. Under what assumptions do their conclusions hold good?
- 20 What is meant by Cost of Capital? What are the components of cost of capital?
- 21 What is business risk and is it the same as financial risk? How does the use of financial leverage affect the financial risk?
- 22 What do you understand by cost of capital? How it is ascertained?
- 23 Explain the concept of Cost of Capital. Also explain different types of costs.
- 24 What is cost of retained earnings? How is the cost of new equity issue determined?
- 25 (a) What is the relevance of cost of capital in corporate investment and financing decision?  
(b) Examine the problems in the determination of composite cost of capital.
- 26 Discuss briefly the different approaches to the computation of the cost of the equity capital.
- 27 How can you determine the cost of equity capital in a growth company?
- 28 Explain how the cost of retained earnings is determined where such retained earnings are proposed to be distributed as bonus shares or right shares to the existing shareholders.

- 29 State the limitation of M.M. Approach of capital structure.
- 30 Discuss the underlying logic of cost of capital.
- 31 Which combination of operating and financial leverages constitutes (i) risky situation and (ii) ideal situation.
- 32 What is cost of capital? Explain the significance of cost of capital.
- 33 Discuss the relationship between the cost of equity and financial leverage in accordance with MM Proposition II.
- 34 Define leverage. Explain its types. Discuss its significance.
- 35 ‘Operating leverage is determined by firm’s cost structure and financial leverage by the mix of debt-equity funds used to finance the firm’s fixed assets. These two leverages combined provide a risk profile of the firm’. Explain.
- 36 Operating leverages is determined by the firm’s cost structure and therefore by nature of business. Financial leverage on the other hand is determined by them of debt and equity funds used to finance the firm’s assets. Operating and financial leverages combined provide a risky profile of the firm, the variability of return to the equity shareholders arise from the business and financial risk. Explain.
- 37 What is meant by a concept of ‘Financial Risk’? Explain the relationship between leverage and cost of capital.
- 38 Explain the concept of Operating Leverage and Financial Leverage.
- 39 How does trading on equity relate to financial leverage?
- 40 Explain the types of leverages. State their significance.
- 41 Does financial leverage always increase the earning per share? Illustrate your example.
- 42 Discuss the relationship between leverage and cost of capital as per the net operating income approach? What are the assumptions made in this approach?
- 43 What is the objective of the Capital Structure Management? How might a firm go for determining its optimal capital structure?
- 44 Differentiate Net Income approach from Net Operating Income approach in capital structure decisions.
- 45 What is cost of capital? Differentiate between Explicit and Implicit Cost.
- 46 How do you determine cost of equity through NOI Approach?
- 47 Explain briefly the view of traditional writers on the relationship between capital structure and value of the firm.
- 48 What do you understand by “signaling hypothesis”. Explain briefly.
- 49 Why is cost of capital most appropriately measured on after tax basis? What effect does it have on specific cost of capital.
- 50 “As there is no explicit cost of retained earnings, these funds are free of cost.” Critically comment.
- 51 Examine the appropriateness of using market values and book values as weights for the calculation of WACC.

52. What is financial risk? Is it necessary to assume that firm's financial structure remain unchanged when evaluating the firm's cost of capital? Why is this assumption impractical?
53. Explain the CAPM. How SML is derived from CML? Do you think that CAPM is relevant in present context?
54. Explain the "Arbitrage Process" under Modigliani / Miller theory. 55. Differentiate between explicit and implicit cost of capital.
56. How will a firm go about determining its "optimal capital structure"?
57. Explain the "trade-off" theory of capital structure and how does it differ from MM proposition with taxes?
58. What is the meaning of "financial risk"? What is the relationship between leverage and the cost of capital? Explain.
59. Explain the view of traditional writers on the relationship between capital structure and the value of a firm.
60. "We should avoid borrowing in a currency that is likely to appreciate." True or False? Explain.
61. What are the merits of using market value weights in computing weighted average cost of capital?
62. What are various factors which affect business and financial risk of a firm? Differentiate between the two.
63. "Trading on equity is resorted with a view to decrease EPS". Comment.
64. "Capital Structure decision is essentially optimization of risk-return relationship". Comment.
65. Give a critical appraisal of the traditional approach and the Modigliani-Millers approach to the problem of capital structure.
66. Explain Operating Leverage. How is it computed? What does high/low operating leverage indicate?
67. Explain Financial Leverage. How is it calculated? What does high/ low financial leverage indicate?
68. Define the concept of cost of capital? State how you would determine the weighted average cost of capital of a firm?

#### **IV Practical Questions:**

1. Fitwell company is now capitalized with Rs. 50,00,000 consisting of 10,000 ordinary shares of Rs. 500 each. Additional finance of Rs. 50,00,000 is required for a major expansion programme launched by the company. Four possible financing plans are under consideration. These are:

- (i) Entirely through additional share capital, issuing 10,000 ordinary shares of Rs. 500 each.
- (ii) Rs. 25 lakhs through ordinary share capital and Rs. 25 lakhs through borrowings from term-lending institutions at 12 percent interest.
- (iii) Entirely through borrowings from the term-lending institutions at 13 percent interest.
- (iv) Rs. 25 lakhs through ordinary share capital and Rs. 25 lakhs through 10 percent preference shares, by issuing 5,000 preference shares of Rs. 500 each.

The company's existing earnings before interest and tax (EBIT) amounted to Rs. 6 lakhs. By virtue of the increase in capitalization, the earnings before interest and tax are expected to double the present level. Examine the impact of financial leverage of these four plans and calculate the earnings per share (EPS) for the shareholders, in each case. Assume 50 percent tax rate.

**Ans. EPS under Proposal (i) Rs. 30; (ii) Rs. 30; (iii) Rs. 27.50; (iv) Rs. 23.33. Proposals (i) and (ii) give the best and identical earnings per share of Rs. 30. Since the pre-tax return on ordinary share capital is 12 per cent, borrowings at 12 per cent rate is at a par of such rate but at 13 per cent it is more expensive than share capital.**

- 2 A Ltd. is capitalized with Rs. 10 lakhs divided into 10,000 shares of Rs. 100 each. The management desires to raise another Rs. 10 lakh to finance a major expansion programme. There are four possible financing plans : (i) all equity shares, (ii) Rs. 5 lakh in equity shares and Rs. 5 lakh in debentures carrying 5% interest, (iii) all debentures carrying 6% interest shares and (iv) Rs. 5 lakh in equity shares and Rs. 5 lakh in preference carrying 5% dividend.

The existing earning before interest and tax amount to Rs. 1,20,000 per annum.

- (a) You are required to calculate earnings per equity share under each of the above four financial plans.
- (b) Also calculate the earning per equity share if on account of expansion the level of *EBIT* is doubled.

**Ans. (a) (i) Rs. 3, (ii) Rs. 3.67, (iii) Rs. 3 and (iv) Rs. 2.33 (b) (i) Rs. 3, (ii) Rs. 3, (iii) Rs. 3 and (iv) Rs. 3**

- 3 Glorious Ltd. has a total capitalization of Rs. 10 lakhs consisting entirely of equity shares of Rs. 50 each. It wishes to raise another Rs. 5 lakhs for expansion through one of its two possible financial plans:

All equity shares of Rs. 50 each, and All debentures carrying 9% interest.

The present level of EBIT is Rs. 1,40,000 and Income Tax Rate is 50%.

You are required to calculate EBIT level at which earning per share would remain the same irrespective of raising of funds through equity shares or debentures.

**Ans. EBIT = Rs. 1,35,000, EPS at point of indifference Rs. 450**

- 4 Calculate the level of earnings before interest and tax (EBIT) at which the EPS Indifference point between the following financing alternatives will occur.  
Equity Share Capital of Rs. 6,00,000 and 12% debentures of Rs. 4,00,000.

OR

Equity Share Capital of Rs. 4,00,000, 14% Preference Share Capital of Rs. 2,00,000 and 12% Debentures of Rs. 4,00,000.

Assume the corporate tax rate is 35% and par value of equity share is Rs. 10 in each case.

**Ans. EPS Indifferences point Rs. 1,77,231**

- 5 A company needs Rs. 12,00,000 for the installation of a new factory which would yield an annual EBIT of Rs. 2,00,000. The company has the objective of maximizing the earnings per share. It is considering the possibility of issuing equity shares plus raising a debt of Rs. 2,00,000, Rs. 6,00,000 or Rs. 10,00,000. The current market price per share is Rs. 40 which is expected to drop to Rs. 25 per share if the market borrowings were to exceed Rs. 7,50,000. cost of borrowings are indicated as under:

UptoRs. 2,50,000	10% p.a.
Between Rs. 2,50,001 and Rs. 6,25,000	14% p.a.
Rs. 6,25,001 and Rs. 10,00,000	16% p.a.

Assuming the tax rate to be 50%, work the EPS and the Scheme which would meet the objective of the management.

**Ans. EPS under Schemes: I Rs. 3.60, II Rs. 4.20, III Rs. 3.91, Scheme II is the best since EPS is the highest.**

- 6 A company wishes to determine the optimum capital structure from the following selected information supplied to you. Determine the optimal capital structure of the capital:

	<i>Situations</i>	<i>Debt Amount</i>	<i>Equity amount</i>	<i>After tax cost Ke</i>
			<i>Rs.</i>	<i>of debt</i>
				<i>%</i>
1		4,00,000	1,00,000	9
2		2,50,000	2,50,000	6
3		1,00,000	4,00,000	5

**Ans. Situation 2**

7

ABC Corporation plans to expand assets by 50% to finance the expansion. It is choosing between a straight 12 percent debt issue and ordinary shares. Its balance sheet and profit and loss account are shown below:

**ABC Corporation**  
**BALANCE SHEET**  
**As on 31<sup>st</sup> December, 2008**

Liabilities	Rs.	Assets	Rs.
11% Debentures	40,00,000	Total Assets	2,00,00,000
Ordinary Share Capital (10,00,000 shares of Rs. 10 each)	1,00,00,000		
Retained Earnings	60,00,000		
	2,00,00,000		2,00,00,000

Sales	Rs. 6,00,00,000
Total Cost (excluding interest)	5,40,00,000
Net Income before Taxes (EBIT)	60,00,000
Interest on Debentures @ 11%	4,40,000
Income before Taxes	55,60,000
Taxes @ 50%	27,80,000
Profits after Tax	27,80,000
Earnings per Share Rs. 27,80,000/10,00,000	Rs. 2.78
Price/Earnings Ratio	7.5 times
Market price 7.5 x Rs. 2.78	Rs. 20.85

If ABC Corporation finances Rs. 1 crore expansion with debt, the rate of the incremental debt will be 12 percent and the price/earning ration of the ordinary shares will be 5 times. If the expansion is financed by equity, the new shares can be sold at Rs. 12 per share and the price earnings ratio will remain at 7.5 times.

- (a) Assuming that net income before interest and taxes (EBIT) is 10% of sales, calculate earnings per share at sales of Rs. 4 crores, Rs. 8 crores and Rs. 10 crores, when financing is with (i) ordinary shares, and (ii) debt.
- (b) At what level of earnings before interest and taxes (EBIT), after the new capital is acquired, would earnings per share (EPS) be the same whether new funds are raised by issuing ordinary shares or raising debt?



- (c) Also determine the level of EBIT at which uncommitted earnings per share (UEPS) would be the same if sinking fund obligations amount of Rs. 5 lakhs per year.
- (d) Using the P/E ratio, calculate the market value per share for each sales level for debt and the equity financing.

**Ans. (a)(i) Rs. 0.97, 2.06, 2.61; (ii) Rs. 1.18, 3.18, 4.18; (b) Rs. 30.806 lakhs; (c) Rs. 52.810 lakhs; (d) Debt Financing; Rs. 5.9, 15.9, 20.9; Equity Financing: Rs. 7.28, 15.46, 19.58**

- 8 From the following data, find out the value of each firm as per the Modigliani-Miller Approach:

	<i>Firm A</i>	<i>Firm B</i>	<i>Firm C</i>
EBIT	Rs. 13,00,000	13,00,000	13,00,000
Number of Shares	3,00,000	2,50,000	2,00,000
12% Debentures		9,00,000	10,00,000

Every firm expects 12% return on investment. **Ans.**

**Value of each firm :Rs. 1,08,33,33**

- 9 The values for two firms X and Y in accordance with the traditional theory are given below:

		X	Y
10	Expected Operating Income ( $x$ )	Rs. 50,000	Rs. 50,000
	Total Cost of Debt ( $kd \cdot D = R$ )	0	10,000
	Net Income ( $x - R$ )	50,000	40,000
	Cost of Equity( $ke$ )	0.10	0.11
	Market Value of Shares(S)	5,00,000	3,60,000
	Market Value of Debt ( $d$ )	0	2,00,000
	Total value of Firm ( $V = S + D$ )	5,00,000	5,60,000
	Average Cost of Capital( $ke$ )	0.10	0.09
	Debt-equity Ratio	0	0.556

**Ans. Value of Firms: X = Rs. 4,00,000; Y = Rs. 4,00,000**

A company with per annum net operating earnings of Rs. 3,00,000 is attempting to evaluate a number of possible capital structures, given below. Which of the capital structures will you recommend and why?

<i>Capital Structure</i>	<i>Debt in Capital Structure Rs.</i>	<i>Kd %</i>	<i>Ke %</i>
1	3,00,000	10.0	12.0
2	4,00,000	10.0	12.5
3	5,00,000	11.0	13.5
4	6,00,000	12.0	15.0
5	7,00,000	14.0	18.0

**Ans. Capital structure of Rs. 3,00,000 as debt is recommended.**

- 11 Determine the optimal capital structure of a company from the following information supplied to you, assuming 50% corporate tax rate:

<i>Kd</i>	<i>Ke</i>	<i>B/V*</i>
8.0	10.0	0.0
10.0	12.0	0.1
13.0	15.0	0.2
15.0	18.0	0.3
		0.4
		0.5
		0.6

\* Proportion of debt in total capital structure.

**Ans. Capital structure having debt of 10% is optimum.**

- 12 From the following selected data determine the value of the firms P and Q belonging to the homogeneous risk class under (a) the *NI* approach, and (b) the *NOI* approach:

	<i>Levered Firm</i>	<i>Unlevered Firm</i>
	<i>P</i>	<i>Q</i>
<i>EBIT</i>	Rs. 2,00,000	Rs. 2,00,000
Interest at 10%	50,000	-
Equity-capitalization Rate	15%	
Corporate Tax Rate	50%	

Which of the two firms has an optimal capital structure under the (i) *NI* approach, and (ii) *NOI* approach?

**Ans. Firm P has optimal capital structure both under NI and NOI approaches.**

- 13 The following are the equilibrium values of two firms belonging to the homogeneous risk class according to the *NOI* approach:

	<i>X</i>	<i>Y</i>
	<i>Rs.</i>	<i>Rs.</i>
Expected Net Operating Income ( <i>EBIT</i> )	25,000	25,000

<i>Less: Cost of Debt (I) = kd. B</i>	5,000	-
Net Income for Equity ( <i>EBIT-I</i> )	20,000	25,000
Equilibrium Cost of Capital ( <i>ko</i> )	0.125	0.125
Total Value of Company ( <i>V</i> ), i.e., <i>EBIT</i> <i>Ko</i>	2,00,000	2,00,000
Market Value of Debt ( <i>B</i> )	1,00,000	-
Market Value of Equity ( <i>ke</i> )	1,00,000	2,00,000
Cost of Equity ( <i>ke</i> )	20.0%	12.5%

Determine the values of the firms X and Y under the traditional approach assuming the *ke* for company Y as 11% and for X as 14%.

**Ans. V = Rs. 2,42,857 (Firm X) and Rs. 2,27,272 (Firm Y)**

- 14 A company's cost of capital was 15% in 2008. According to the management, this consisted of 8% due to risk less cost of money, 3% business risk premium and 4% financial risk premium. The company intends to issue new equity shares in 2009. You are required to determine the cost of equity capital in each of the following cases:

In 1992 the risk less cost of money goes up by 1%. Of course, the financial and business risks remain unchanged.

Besides increases in the risk less cost of money by 1%, the business risk increases by 50% on account of the company's undertaking a new line of production.

A competitor of the firm has 9% risk less cost of money, 3% business risk and only 1% as financial risk, since he has paid all long-term debts in 2007. **Ans. (a) 16%, (b) 17.50%, (c) 13%**

- 15 Mendex Ltd. issued 10% irredeemable preference shares. The nominal value of each share is Rs. 100. You are required to calculate the cost of (a) When issued at 5% discount, (b) When issued at 5% premium.

**Ans. (a) 10.53%, (b) 9.10%**

- 16 The current market price of the shares of A Ltd. is Rs. 95. The floatation costs are Rs. 5 per share. Dividend per share amounts to Rs. 4.50 and is expected to grow at a rate of 7%. You are required to calculate the cost of equity share capital.

**Ans. 12%**

- 17 The Xavier Corporation, a dynamic growth firm which pays no dividends, anticipates a long-run level of future earning of Rs. 7 per share. The current price of Xavier's shares is Rs. 55.45, floatation costs for the sale of equity shares would average about 10% of the price of the shares. What is the cost of new equity capital to Xavier?

**Ans. 7/49.90 or 14.03%**

- 18 Mahendrao is a shareholder in the Central India Ltd. Although earnings for the central have varied considerably. Mahendrao has determined that the long-run average dividends for the firm have been Rs. 2 per share. He expects a similar pattern to prevail in the future. Given the volatility of the central dividends, Mahendrao had decided that minimum rate of 20% should be earned on the share. What price would Mahendrao be willing to pay for the Central's Shares?

**Ans. Rs. 10**

- 19 ABC Ltd. has the following capital structure:

Equity (expected dividend 12%)	Rs. 10,00,000
10% Preference	Rs. 5,00,000
8% Loan	Rs. 15,00,000

You are required to calculate the weighted average cost of capital, assuming 50% as the rate of income tax, before and after tax.

**Ans. Before tax 9.66%, After tax 7.67%**

- 20 A company maintains debt equity ratio of 40:60. The desired rate of return after tax on debt is 4% and on equity is 10%. The company is intending for investing in a project which will cost Rs. 40,000. You are required to calculate the yield per annum on the project so that the market value of the equity shares remains consistent even after raising additional funds.

**Ans. 7.6%**

- 21 Following are the details regarding the capital structure of a company:

Type of Capital	Book Value	Market Specific Value	Cost
Debentures	40,000	38,000	5%
Preference Capital	10,000	11,000	8%
Equity Capital	60,000	1,20,000	13%
Retained earnings	20,000	-	9%
	<u>1,30,000</u>	<u>1,69,000</u>	

You are requested to determine the weighted average cost of capital using: (i) book value as weights, (ii) market value as weights. Do you think, there can be situation where weighted average cost of capital would be the same irrespective of the weights used.

**Ans. (i) 9.54%, (ii) 10.17%, Cost of capital would be the same irrespective of the weights in case the book value and the market value of retained earnings is Rs. 30,000 (i.e. 20,000 12/8) and equity capital Rs. 90,000 (i.e. 60,000 x 12/8)**

- 22 The capital structure of ABC Limited consists of equity share capital of Rs. 1,00,000 (10,000 shares of Rs. 10 each) and 8% debentures of Rs. 50,000. You are required to calculate and verify the degree of financial leverage on earning before interest and tax (EBIT) level of Rs. 20,000.

**Ans. Financial Leverage 1.25**

- 23 Calculate degree of (i) operating leverage, (ii) financial leverage and (iii) combined leverage from the following data:

Sales 1,00,000 units @ 2 per unit = Rs. 2,00,000

Variable Cost per unit @ Re. 0.70

Fixed Costs Rs. 1,00,000

Interest Charges Rs. 3,668

**Ans. (i) 4.33, (ii) 1.14, (iii) 4.9**

- 24 Calculate the Degree of Operating Leverage, Degree of Financial Leverage and the Degree of Combined Leverage for the following firms and interpret the results:

	<i>P</i>	<i>Q</i>	<i>R</i>
Output (Units)	3,00,000	75,000	5,00,000
Fixed Costs (Rs.)	3,50,000	7,00,000	75,000
Unit Variable Cost (Rs.)	1.00	7.50	0.10
Interest Expenses (Rs.)	25,000	40,000	Nil
Unit Selling Price (Rs.)	3.00	25.00	0.50

**Ans. Operating Leverage P = 2.40, Q = 2.14, R=1.60**  
**Financial Leverage P = 1.11, Q = 1.07, R=1.00**  
**Combined Leverage P = 2.67, Q = 2.29, R=1.60**

- 25 The following is the balance sheet of a company:

### BALANCE SHEET

Liabilities	Amount(Rs.)	Assets	Amount(Rs.)
Equity Capital (Rs. 10 per share)	60,000	Net Fixed Assets	1,50,000
10% Long-term debt	80,000	Current Assets	50,000
Retained earnings	20,000		
Current Liabilities	40,000		
	2,00,000		2,00,000

The company's total assets turnover ratio is 3.0, its fixed operating costs are Rs. 1,00,000 and its variable operating costs ratio is 40%. The income tax rate is 50%.

Calculate for the company all the three types of leverages.

Determine the likely level of EBIT if EPS is (a) Re. 1, (b) Rs. 3, and (c) Zero.

**Ans. (i) OL 1.385; FL 1.032, CL 1.429; (ii) (a) Rs. 20,000, (b) 44,000, (c) Rs. 8,000**

- 26 ABC Ltd. has EBIT of Rs. 1,60,000. Its capital structure consists of the following securities:

10% Debentures	Rs. 5,00,000
12% Preference Shares	1,00,000
Equity Shares for Rs. 100 each	4,00,000

The company is in the 55% tax bracket. You are required to determine the company's EPS;

the percentage change in EPS associated with 30% increase and 30% decrease in EBIT;  
and

the degree of financial leverage.

**Ans. (i) Rs. 9.375, (ii) 57.6%, (iii) 1.45**

- 27 Calculate the Operating Leverage, Financial Leverage and Combined Leverage from the following data under situations I and II and Financial Plans A and B:

Installed Capacity	4,000 units
Actual Production and Sales	75% of the Capacity
Selling Price	Rs. 30 per unit
Variable Cost	Rs. 15 per unit

Fixed Cost:

Under Situation I Rs. 15,000 Under Situation

II Rs. 20,000 Capital Structure:

	<i>Financial Plans</i>	
	Rs.	Rs.
Equity	10,000	15,000
Debt(Rate of Interest at 20%)	10,000	5,000
	20,000	20,000

**Ans.**

	<i>Situation I</i>	<i>Situation II</i>
<b>Operating Leverage</b>	<b>1.5</b>	<b>1.8</b>
<b>Financial Leverage</b>	<b>Plan A</b>	<b>Plan B</b>
	<b>1.07</b>	<b>1.04</b>
<b>Combined Leverage:</b>		
<b>(a) Situation I</b>	<b>1.60</b>	<b>1.560</b>



- (iii) The company may issue 25,000 equity shares of Rs 10 per share and 2,500 preference shares of Rs.100 per share bearing 10% rate of dividend.

If the company's EBIT are Rs 40, 000, Rs.80, 000, Rs.1, 20,000, what are the EPS under each financial plan? Which alternative would you recommend and why? Assume corporate tax of 35% and P/E ratio 10 times in equity plan, 9 times in equity+ debt plan

**Ans. Equity plan (when EBIT is Rs.40,000 as MPS is maximum at Rs.5.60) Equity+ Debt plan when EBIT are Rs.80,000 and Rs.1,20,000(as MPS at these levels is maximum i.e. Rs.12.48 and Rs.20.8)**

- 31 A growing company is confronted with a choice between 10% debt issue and equity issue to finance its new investments. Its pre expansion income statement is as follows: Sales (Production capacity of Rs.6,00,000 at current sales price) Rs.45,00,000

Fixed cost	5,00,000
Variable cost	30,00,000
EBIT	10,00,000
Interest at 8 %	1,00,000
Earnings before Taxes	9,00,000
Income Tax	3,15,000
Net Income	5,85,000
EPS	11.7

The expansion programme is estimated to cost Rs.5,00,000 .If this is financed through debt, the rate on new debt will be 10% and the P/E ratio will be 10. If expansion programme is financed through equity, new shares can be sold at Rs.100 per share and P/E ratio will be 12.The expansion will generate additional sales of Rs.12, 00,000. No additional fixed cost will be needed. If the company is to follow a policy of maximizing the market value of its shares, which form of financing should be employed by it

**Ans. Equity financing should be adopted MPS would be Rs 187.92**

- 32 The following data relate of Company XYZ Ltd.

	Sales	Rs.	2,00,000
Less	Variables expenses (30%)	60,000	
	Contribution	1,40,000	
	Fixed operating expenses	1,00,000	
	EBIT	40,000	
Less	Interest	5,000	
	Taxable income	35,000	



- (a) Using the concept of leverage, by what percentage will taxable income increase if sales increase by 6 percent?
- (b) Using the concept of operating leverage by what percentage will EBIT increase if there is a 10 percent increase in sales?
- (c) Using the concept of financial leverage, by what percentage will taxable income increase if EBIT increases by 6 percent?

- Ans.** (a) **CL = 4**  
**Increase in profit before tax is Rs. 8,400 i.e. 24% of Rs. 35,000.**
- (b) **OL = Contribution/EBIT = 1,40,000/40,000 = 3.50**  
**Increase in EBIT is Rs. 14,000 i.e. 35% of Rs. 40,000**
- (c) **FL = EBIT/Profit before tax = 40,000/35,000 = 1.15**  
**Increase in taxable income is Rs. 2,400 i.e. 6.9% of Rs. 35,000.**

33 Following are the details regarding the capital structure of a company

Type of capital	Book value (Rs.)	Market value (Rs.)	Specific cost (Rs.)
Debentures	40,000	38,000	5%
Preference Capital	10,000	11,000	8%
Equity Capital	60,000	1,20,000	13%
Retained Earnings	20,000	-	9%
	1,30,000	1,69,000	

You are requested to determine the weighted average cost of capital using:

- (a) Book Value as weights,  
 (b) Market Value as weights,

Do you think, there can be situation where weighted average cost of capital would be the same irrespective of the weights used.

- Ans. K = 9.54%**  
**K = 10.17%**

34 A firm has sales of Rs. 10,00,000, variable cost of Rs. 7,00,000 and fixed cost of Rs. 2,00,000 and debt of Rs. 5,00,000 at 10% rate of interest. What are the operating, financial and combined leverages? If the firm wants to double its Earning Before Interest and Tax (EBIT), how much of a rise in sales would be needed on a percentage basis?

**Ans. Operating leverage=Contribution/EBIT**  

$$= 3/1 = 3$$

**Financial leverage=EBIT/PBT**  

$$= 1/0.5 = 2$$

**Combined leverage=O.L.\*F.L. = Contribution/PBT**  

$$= 3*2 = 6$$

35 In considering the most desirable capital structure for a company, the following estimates of the cost of debt and equity capital (after tax) has been made at various levels of debt-equity mix.

Debt as percentage of total capital employed	Cost of debt(%)	Cost of equity (%)
0	5.0	12.0 12.0
10	5.0	12.5 13.0
20	5.0	14.0 16.0
30	5.5	20.0
40	6.0	
50	6.5	
60	7.0	

You are required to determine the optimal debt-equity mix for the company by calculating composite cost of capital.

**Ans. The optimal debt-equity mix for the company is at 30% debt & 70% equity mix.**

36 The capital structure of the Progressive Corporation consists of an ordinary share capital of Rs. 10,00,000 (share of Rs. 100 par value) and Rs. 10,00,000 of 10% debentures. Sales increased by 20% from 1,00,000 units to 1,20,000 units and fixed expenses amount to Rs. 10 per unit, variable cost amount to Rs. 6 per unit and fixed expenses amount to Rs. 2,00,000. The income tax rate is assumed to be 50 percent.

You are required to calculate the following:

- the percentage increase in earning per share;
- the degree of financial leverage at 1,00,000 units and 1,20,000 units;
- the degree of operating leverage at 1,00,000 units and 1,20,000 units.

Comment on the behaviour of operating and financial leverages in relation to increase in production from 1,00,000 units to 1,20,000 units.

<b>Ans. EPS</b>	<b>=</b>	<b>50000</b>	<b>90000</b>
		-----	-----
		<b>10000</b>	<b>10000</b>
		<b>= Rs.5</b>	<b>= Rs.9</b>

<b>DFL</b>	<b>=</b>	<b>200000</b>	<b>280000</b>
		-----	-----
		<b>100000</b>	<b>180000</b>
		<b>= Rs.2</b>	<b>= Rs.1.56</b>

<b>DOL</b>	<b>=</b>	<b>400000</b>	<b>480000</b>
		-----	-----
		<b>200000</b>	<b>280000</b>
		<b>= Rs.2</b>	<b>= Rs.1.71</b>

**On account of increase in sales 1 lakh units to 1.2 lakh units at the rate of Rs. 10/unit, EPS rises by 80% while the operating leverage comes down from 2 to 1.71 and financial leverage declines from 2 to 1.56. there is, therefore, a significant decrease in both the business risk and financial risk of the company on account of reduction in both the leverage. This is generally the result when there is generally the result when there is increase in sales without any increase in fixed operating or financial costs.**

37 The two companies X and Y belong to the same risk class. They have everything in common except that firm Y has 10% debentures of Rs. 5 lacs. The valuation of the two firms is assumed to be as follows:

	X	Y
Net operating income (EBIT)	Rs. 7,50,000	Rs. 7,50,000
Interest on debt	-	50,000
Earning to equity holders	7,50,000	7,00,000
Equity capitalization	0.125	0.14
Market value of equity	60,00,000	50,00,000
Overall capitalization rate	0.125	0.1363
Debt equity ratio	0	0.1
Market value of firm	60,00,000	50,00,000 + 5,00,000 = 55,00,000

An investor owns 10% of the equity shares of the overvalued firm. Determine his investment cost of earning the same income so that he is at a break even point. Will he gain by investing in the under-valued firm?

- 38 A company is considering the following to raise additional capital for its expansion schemes:

Equity (% of cost of capital)	Debt (% of cost of capital)	Cost of equity %	Cost of debt (pretax) %
75	25	16	12
50	50	18	14
25	75	24	18

Tax rate is 50%. Which option would you recommend?

**Ans. Option III**

- 39 If the combined leverage and operating leverage figures of a company are 2.5 and 1.25 respectively, find the financial leverage and P/V ratio, given that the equity dividend per share is Rs. 2, interest payable per year is Rs. 1 lakh, total fixed cost Rs. 0.5 lakh and sales Rs. 10 lakh.

**Ans. FL = 2,00,000, P/V Ratio = 25%**

- 40 X Ltd. is a widely held company. It is considering a major expansion of its production facilities and the following alternatives are available: (Rs. Lakhs)

Particulars	A	B	C
Share capital	50	20	10
14% debentures	-	20	15
Loan from a financial institution @ 18% p.a. rate of interest	-	10	25

Expected rate of return before tax is 25%. The rate of dividend of the company is not less than 20%. The company at present has low debt. Corporate taxation is 50%. Which of the alternatives would you choose? **Ans. Alt. C should be chosen.**

- 41 XYZ Ltd. is earning an annual EBIT of Rs.100 lakh. The company has Rs.200 lakh of 15% debentures in its capital structure. The equity capitalization rate for the company is 14%. The company shares can be issued in the market at a premium of Rs.10. You are required to calculate according to the net income approach.

- Value of the firm
- Overall capitalization rate
- Value of the firm after redemption of the debenture, assuming that the equity capitalization rate remains the same.

**Ans:  $K_0=14.3\%$ , Value of Firm-714.29**

- 42 Compute the degree of financial leverage for CMS ltd(tax rate 35%)
- |                          |                    |
|--------------------------|--------------------|
| Total Sales              | Rs 14,00,000       |
| Contribution Ratio       | 25% Fixed          |
| Expenses                 | Rs1,50,000         |
| Outstanding Bank Loan    | Rs 4,00,000 @12.5% |
| Preference Share Capital | Rs 2,00,000@15%    |

**Ans: Financial Leverage=1.33**

- 43 Compute the EPS for Martin Ltd
- |                                  |            |
|----------------------------------|------------|
| Return on investment             | 12%        |
| No. of outstanding equity shares | Rs1,00,000 |
| Net worth                        | Rs 25 lakh |
| Total debt                       | Rs 40 Lakh |
| Average cost of debt             | 9%         |
| Tax rate                         | 35%        |

**Ans: EPS = 2.73**

- 44 Compute present market price per share of T Ltd from following data
- |                                      |                |
|--------------------------------------|----------------|
| Current dividend:                    | Rs.2 per share |
| Constant rate of growth in dividend: | 5%             |
| Expected return from market index    | 12%            |
| Beta of stock                        | 1.5            |
| Risk free rate of return             | 6%             |

**Ans:P = Rs.20**

- 45 Two companies P and Q Ltd belong to equivalent risk group. The two companies are same in every respect except that Q is levered the outstanding debt of the levered company is Rs.600000 in 10% debenturesThe other information for the two companies is as follows:

	<b>P Ltd</b>	<b>Q Ltd</b>
EBIT(Rs)	1,50,000	1,50,000
Interest(Rs)	-----	60,000
Earnings to equity shareholders	1,50,000	90,000
Ke	0.15	0.20
Market value of Equity(Rs)	10,00,000	4,50,000
Market value of Debt(Rs)	-----	6,00,000

Total value of firm(Rs)	10,00,000	10,50,000
Overall capitalization rate	15%	14.3%
Debt equity ratio	0	1.33

An investor owns 5% equity shares of Q Ltd Show arbitrage process .Is there any limit to this process

**Ans: He reduces his outlay by Rs.2,500 through use of arbitrage process.**

- 46 Ayush Ltd issued FCD with face value of Rs 100 each .The coupon rate is 9% and interest is payable half yearly over a period of three years.Afterthreeyears each bond will be converted into 10 equity shares of face value of Rs 10 per share which is expected to fetch a dividend of Rs.1 per share every year .Presently the yield on risk free securities is 5% per annum.The bond holders of company need 3% more as the risk premium while the expected return to the equity share holders will go up by an additional risk premium of 4%.compute intrinsic value of these FCD

**Ans: Intrinsic Valuation of Fully Convertible Debentures = Rs.109.349**

47. To buy a car worth Rs.5,00,000Nitya Clothes Ltd is planning to take a loan of Rs.4,00,000 from a financial institution. The loan to be repaid in equated monthly instalment of Rs.9,000 within a period of 5 years,payable at the end of every month.However margin money of Rs.100000 is to be borrowed from local money lender that is to be repaid with interest rate of 20% by end of the year. what is implicit cost of borrowed funds?

**Ans: Overall cost of borrowed amount = 14%**

48. To expand his operations R Ltd needs Rs 500 lakh .its capital structure is in the proportion of equity capital 40% preference capital 10% and debt 50%.If company invested Rs 600 lakh what will be weighted marginal cost of capital of new financing?

**Ans: WMCC = 0.15**

- 49 Following data relates to financing of XYZ project of MBE Ltd

Description	Plan A(Rs)	Plan B(Rs)	Cost
Equity shares (Rs 10 each)	40 lakh	50 lakh	20%
Debentures	10 lakh	20 lakh	10%
Preference Shares	50 lakh	30 lakh	11%

Determine indifference point for the financial plan assuming a 35% tax rate.

**Ans: The indifference point for financial plans is EBIT = Rs.19,00,000**

A Limited Company has the following capital structure: -

Equity Share Capital (2,00,000 Shares)	Rs. 40,00,000
6% Preference Shares	10,00,000
Debentures	30,00,000
	80,00,000

The market price of the company's equity share is Rs.20. It is expected that company will pay a current dividend of Rs.2 per share which will grow at 7 percent forever. The tax rate may be presumed at 50%. You are required to compute the following: -

- i. A weighted average cost of capital based on existing capital structure.
- ii The new weighted average cost of capital if the company raises an additional Rs.20,00,000 debt by issuing 10% debentures. This would result in increasing the expected dividend to Rs.3 and leave the growth rate unchanged but the price of the share will fall to Rs.15 per share.

**Ans. WACC = 11.125% WACC (Ko) = 0.139 or 13.9%**

51. The expected EBIT of a firm is Rs. 80,000. It has Rs. 2, 00,000 8% debentures. The equity capitalization rate of the company is 10%. Calculate the value of the firm and over all Capitalization rate according to Net Income Approach. **Ans: Overall Cost of Capital, Ko = 9.52%**

**if Debentures is raised to Rs. 3, 00,000**

Overall Cost of Capital, Ko = 9.30%

**Thus with the increase in debt financing, the value of the firm has increased and the overall cost of capital has decreased.**

- 52 A company has the following capital structure and after tax costs of different sources of Capital used:

Type of Capital	Book Value	Proportion (%)	After-tax cost (%)
Debt	Rs. 4, 50,000	30	7
Preference	3, 75,000	25	10
Equity	<u>6, 75,000</u>	<u>45</u>	15
	15, 00,000	100	

- a) Determine the weighted average cost of capital using book Value weights
- b) The firm wishes to raise further Rs. 6, 00,000 for the expansion of the project as below:

Debt	Rs. 3, 00,000
Preference Capital	Rs. 1, 50,000
Equity Capital	Rs. 1, 50,000

Assuming that specific costs do not change, compute the weighted marginal cost of capital.

**Ans: Weighted Average Cost Of Capital (WACC)= 11.35% Weighted Marginal Cost Of Capital (WMCC)= 9.75%**

53. The following information is available in respect of the rate of return on investment (r), the cost of capital (k) and earning per share (E) of ABC Ltd. Rate of return on investment (r) = (i) 15% (ii) 12% and (iii) 10%

Cost of capital (K) = 12%

Earning per share (E). = Rs. 10

Determine the value of its shares using Gordon's Model assuming the following:

	<i>D/P ratio (1- b)</i>	<i>Retention ratio (b)</i>
(a)	100	0
(b)	80	20
(c)	40	60

Ans.

**Dividend policy and value of shares**

(i) r = 15%	(ii) r = 12%	(iii) r = 10%
<b>a) when D/P ratio is 100%</b>		
$P = \frac{10(1-0)}{0.12 - (0)(.15)}$ = Rs.83.33	$P = \frac{10(1-0)}{0.12 - (0)(.12)}$ = Rs.83.33	$P = \frac{10(1-0)}{0.12 - (0)(.10)}$ = Rs.83.33
<b>b) when D/P ratio is 80%</b>		
$P = \frac{10(1-0.20)}{0.12 - (0.20)(.15)}$ = Rs.88.89	$P = \frac{10(1-0.20)}{0.12 - (0.20)(.12)}$ = Rs.83.33	$P = \frac{10(1-0.20)}{0.12 - 0.20)(.12)}$ = Rs.80
<b>c) when D/P ratio is 40%</b>		
$P = \frac{10(1-0.60)}{0.12 - (0.60)(.15)}$ = Rs.133.33	$P = \frac{10(1-0.60)}{0.12 - (0.60)(.12)}$ = Rs.83.33	$P = \frac{10(1-0.60)}{0.12 - (0.60)(.10)}$ = Rs.66.67

54. Compute the earning per share for MM Ltd:-

Return on investment	11%
Number of outstanding equity shares	100000
Net worth	25 lakhs
Total debt	40 lakhs
Average cost of debt	10%
Applicable tax rate	30%

Are there any limitations of EPS in financial decision making.



**Ans.** Return on Investment =  $\frac{\text{EBIT}}{\text{Net worth}}$

$$11\% = \frac{\text{EBIT}}{2500000}$$

$$\text{EBIT} = \frac{11 \times 2500000}{100} = 275000$$

$$\text{Interest} = 400,000 \times 10/100 = 40000$$

EBIT                    275000

Less: interest        40000

PBT                    235000

Less: tax             70500

PAT                    164500

$$\text{EPS} = \frac{\text{PAT}}{\text{no of equity shares}} = 164500/100000 = 1.6$$

It should be noted that two different companies could generate the same EPS but one could do so with a lesser equity. All other things being equal, this company is better than the other one because it is more efficient at using its capital for generating profits.

It is important that the investors do not rely on only measure of earnings per share for making investment decisions. Instead they should use in conjunction with other measures and financial statement analysis.

55. Determine the optimal capital structure of a company from the following information supplied to you, assuming 35% tax rate:

Cost of debt, $K_i$ in %	Cost of equity, $K_e$ in %	Debt/ (Equity+Debt) (B/V)
11	13	0
11	13	0.1
11.6	14	0.2
12	15	0.3
13	16	0.4
15	18	0.5
18	20	0.6

**Ans.** Capital structure, having a debt of 10%, is optimal.

56. Companies U & L are identical in all respects, except that U is unlevered while L is levered. Company L has Rs 20,00,000 of 8% debentures outstanding. Assume (1) that all the MM

assumptions are met, (2) that the tax rate is 40%, (3) that EBIT is Rs 6,00,000 and the equity capitalization rate for company U is 10%. Required:-

- a. What would be the value of each firm according to MM's approach
- b. Suppose  $V_U = \text{Rs } 25,00,000$  and  $V_L = \text{Rs } 45,00,000$ . According to MM, do they represent equilibrium values? If not, explain the process by which equilibrium would be restored?

**Ans.**

- (a) Value of unlevered firm ( $V_U$ ) = 36,00,000, Value of levered firm ( $V_L$ ) = 44,00,000
- (b) Through the Arbitrage process and the substitution of personal leverage for corporate leverage, Mr. A can switch Company L to Company U, earn the same total return of Rs. 26,400, and have funds of Rs. 10,000 ( i.e. Rs. 2,50,000+ 1,20,000 - 3,60,000) left over to invest elsewhere. This process would continue till equilibrium is restored.

**57.** Mr. Ramesh is thinking of investing in equal share of ABC Ltd. The face value of the shares is Rs. 10. He requires a return of 25% on his investment. ABC Ltd. declared a dividend of Rs. 5.00 per share for the current year and its expected that the dividend of the company will grow at the rate of 30% for the next five years and after that at 20% forever. Compute the maximum price at which Mr. Ramesh may buy the shares of ABC Ltd.

**Ans. Rs. 213.60**

**58.** A bond with a face value of Rs. 100 provides 12 % annual return and pays Rs 105 at the time of maturity, which is 10 years from now. If investors, required rate of return is 13% at what price should the company issue the bond?

**Ans. Rs. 96.04**

## **UNIT - III**

### **I Test Your Skills:**

#### **(a) Multiple Choice Questions:**

- 1 In proper capital budgeting analysis we evaluate incremental \_\_\_\_\_ cash flows.
  - (a) accounting
  - (b) operating
  - (c) before-tax
  - (d) financing
- 2 The estimated benefits from a capital budgeting project are expected as cash flows rather than income flows because \_\_\_\_\_.

- (a) it is more difficult to calculate income flows than cash flows
  - (b) it is cash, not accounting income, that is central to the firm's capital budgeting decision
  - (c) this is required by the accounting profession
- 3 In estimating "after-tax incremental operating cash flows" for a project, you should include all of the following *except* \_\_\_\_\_.
- (a) changes in costs due to a general appreciation in those costs
  - (b) the amount (net of taxes) that we could realize from selling a currently unused building of ours that we intend to use for our project
  - (c) changes in working capital resulting from the project, net of spontaneous changes in current liabilities
  - (d) costs that have previously been incurred that are unrecoverable
- 4 All of the following influence capital budgeting cash flows *except* \_\_\_\_\_.
- (a) choice of depreciation method for tax purposes
  - (b) economic length of the project
  - (c) projected sales (revenues) for the project
  - (d) sunk costs of the project
- 5 The basic capital budgeting principles involved in determining relevant after-tax incremental operating cash flows require us to \_\_\_\_\_. (a) include sunk costs, but ignore opportunity costs
- (b) include opportunity costs, but ignore sunk costs
  - (c) ignore both opportunity costs and sunk costs
  - (d) include both opportunity and sunk costs
- 6 Interest payments, principal payments, and cash dividends are \_\_\_\_\_ the typical budgeting cash-flow analysis because they are \_\_\_\_\_ flows.
- (a) included in; financing
  - (b) excluded from; financing
  - (c) included in; operating
  - (d) excluded from; operating
- 7 Which of the following is least likely to be part of the calculation of the terminal-year incremental net cash flow for an energy-related expansion project?
- (a) An initial working capital investment is now returned as an additional cash inflow
  - (b) Disposal/reclamation costs
  - (c) Capitalized expenditures
  - (d) Salvage value of any sold or disposed assets

- 8 A profitability index (PI) of .92 for a project means that \_\_\_\_\_.
- (a) The project's costs (cash outlay) are (is) less than the present value of the project's benefits
  - (b) The project's NPV is greater than zero
  - (c) The project's NPV is greater than 1
  - (d) The project returns 92 cents in present value for each current rupee invested (cost)
- 9 Which of the following statements is *incorrect* regarding a normal project?
- (a) If the NPV of a project is greater than 0, then its PI will exceed 1.
  - (b) If the IRR of a project is 8%, its NPV, using a discount rate,  $k$ , greater than 8%, will be less than 0.
  - (c) If the PI of a project equals 0, then the project's initial cash outflow equals the PV of its cash flows.
  - (d) If the IRR of a project is greater than the discount rate,  $k$ , then its PI will be greater than 1.
- 10 Assume that a firm has accurately calculated the net cash flows relating to two mutually exclusive investment proposals. If the net present value of both proposals exceed zero and the firm is not under the constraint of capital rationing, then the firm should \_\_\_\_\_.
- (a) calculate the IRRs of these investments to be certain that the IRRs are greater than the cost of capital
  - (b) compare the profitability index of these investments to those of other possible investments
  - (c) calculate the payback periods to make certain that the initial cash outlays can be recovered within a appropriate period of time
  - (d) accept the proposal that has the largest NPV since the goal of the firm is to maximize shareholder wealth and, since the projects are mutually exclusive, we can only take one
- 11 Which of the following statements regarding cash flow patterns (for time periods 0, 1, 2, 3, and 4) is correct?
- (a) The sequence of -Rs.100, Rs.50, Rs.40, Rs.60, and Rs.50 is a non-conventional cash flow pattern
  - (b) The sequence of -Rs.100, Rs.600, -Rs.1,100, Rs.600, and Rs.20 *potentially* has a maximum of two internal rates of return.
  - (c) The sequence of +Rs.100, -Rs.1,100, and Rs.1,600 is a conventional cash flow pattern.
  - (d) The sequence of -Rs.50, Rs.50, Rs.70, Rs.60, and -Rs.150 potentially has at most two internal rates of return.

- 12 Which of the following statements is correct regarding the internal rate of return (IRR) method?
- (a) Each project has a unique internal rate of return
  - (b) As long as you are not dealing with mutually exclusive projects, capital rationing, or unusual projects having multiple sign changes in the cash-flow stream, the internal rate of return method can be used with reasonable confidence.
  - (c) The internal rate of return does not consider the time value of money.
  - (d) The internal rate of return is rarely used by firms today because of the ease at which net present value is calculated.
- 13 Which of the following is *not* a potential for a ranking problem between two mutually exclusive projects?
- (a) The projects have unequal lives that differ by several years (b) The costs of the two projects differ by nearly 30%.
  - (c) The two projects have cash flow patterns that differ dramatically
  - (d) One of the mutually exclusive projects involves replacement while the other involves expansion
- 14 A project whose acceptance precludes the acceptance of one or more alternative projects is referred to as \_\_\_\_\_.
- (a) a mutually exclusive project.
  - (b) an independent project.
  - (c) a dependent project
  - (d) a contingent project
- 15 A project whose acceptance requires the acceptance of one or more alternative projects is referred to as \_\_\_\_\_.
- (a) a mutually exclusive project.
  - (b) an independent project. (c) a dependent project
  - (d) a contingent project
  - (e) none of the above
16. When operating under a single-period capital-rationing constraint, you may first want to try selecting projects by descending order of their \_\_\_\_\_ in order to give yourself the best chance to select the mix of projects that adds most to firm value.
- (a) profitability index (PI)
  - (b) net present value (NPV)
  - (c) internal rate of return (IRR)
  - (d) payback period (PBP)

17. Which of the following statements is correct regarding the internal rate of return (IRR) method?
- (a) Each project has a unique internal rate of return.
  - (b) As long as you are not dealing with mutually exclusive projects, capital rationing, or unusual projects having multiple sign changes in the cash-flow stream, the internal rate of return method can be used with reasonable confidence.
  - (c) The internal rate of return does not consider the time value of money.
  - (d) The internal rate of return is rarely used by firms today because of the ease at which net present value is calculated.
18. Which of the following is not a potential for a ranking problem between two mutually exclusive projects?
- (a) The projects have unequal lives that differ by several years.
  - (b) The costs of the two projects differ by nearly 30%.
  - (c) The two projects have cash flow patterns that differ dramatically.
  - (d) One of the mutually exclusive projects involves replacement while the other involves expansion.
19. A project whose acceptance precludes the acceptance of one or more alternative projects is referred to as \_\_\_\_\_.
- (a) a mutually exclusive project.
  - (b) an independent project.
  - (c) a dependent project.
  - (d) a contingent project.
20. Two mutually exclusive projects are being considered. Neither project will be repeated again in the future after their current lives are complete. There exists a potential problem though -- the expected life of the first project is one year and the expected life of the second project is three years. This has caused the NPV and IRR methods to suggest different project preferences. What technique can be used to help make a better decision in this scenario?
- (a) Rely on the NPV method and make your choice as it will tell you which one is best.
  - (b) Use the common-life technique to replicate the one-year project three times and recalculate the NPV and IRR for the one-year project.
  - (c) Ignore the NPV technique and simply choose the highest IRR since managers are concerned about maximizing returns.
  - (d) In this situation, we need to rely on the profitability index (PI) method and choose the one with the highest PI.

21. To the nearest rupee , what is the net present value of a replacement project whose cash flows are -Rs.104,000; Rs.34,444; Rs.39,877; Rs.25,000; and Rs.52,800 for years 0 through 4, respectively? The firm has decided to assume that the appropriate cost of capital is 10% and the appropriate risk-free rate is 6%.
- (a) Rs.15,115
  - (b) Rs.26,798
  - (c) Rs.33,346
  - (d) Rs.48,121
22. A project has the following cash inflows Rs.34,444; Rs.39,877; Rs.25,000; and Rs.52,800 for years 1 through 4, respectively. The initial cash outflow is Rs.104,000. Which of the following four statements is correct concerning the project internal rate of return (IRR)?
- (a) The IRR is less than 10%.
  - (b) The IRR is greater than or equal to 10%, but less than 14%.
  - (c) The IRR is greater than or equal to 14%, but less than 18%.
  - (d) The IRR is greater than or equal to 18%.
23. You must decide between two mutually exclusive projects. Project A has cash flows of Rs.10,000; Rs.5,000; Rs.5,000; and Rs.5,000; for years 0 through 3, respectively. Project B has cash flows of -Rs.20,000; Rs.10,000; Rs.10,000; and Rs.10,000; for years 0 through 3, respectively. The firm has decided to assume that the appropriate cost of capital is 10% for both projects. Which project should be chosen? Why?
- (a) A; Project A's NPV > Project B's NPV.
  - (b) A or B; Makes no difference which you choose because the IRR for A is identical to the IRR for B and both IRRs are greater than 10 percent, the cost of capital.
  - (c) B; Project B's NPV > Project A's NPV.
  - (d) Neither A nor B; The NPVs of both projects are negative.
24. A project whose acceptance requires the acceptance of one or more alternative projects is referred to as \_\_\_\_\_. (a) a mutually exclusive project
- (b) an independent project (c) a dependent project
  - (d) None of the above are
25. Which of the following statements regarding relevant costs and sunk costs is incorrect? (a) A serious drawback associated with the incremental approach of relevant cost study is that the incremental approach is cumbersome if more than two alternatives are considered.
- (b) The type of cost presented to management for an equipment replacement decision should be limited to relevant costs.
  - (c) A sunk cost is a cost which cannot be avoided because it already has been incurred.

- (d) Relevant costs can be studied using an incremental approach but should not be considered with a full project approach.
26. Which of the following statements regarding capital budgeting decisions is incorrect?
- Capital budgeting analysis techniques are applicable to equipment replacement decisions.
  - The amount and timing of cash flows is critical to the calculation of the net present value of an investment.
  - The cost of capital is equal to a company's maximum desired rate of return.
  - In a capital budgeting decision, the amount of the initial investment required is critical to the analysis; it is not treated as a sunk cost.
27. Analyze the following statements regarding capital budgeting decisions and determine which is correct.
- The net present value of decision making and capital budgeting is superior to the payback method in that it considers the time value of money.
  - Assuming a 6% interest rate, the factor 0.94340 would be taken from a compound interest (future value) table of factors.
  - The internal rate of return capital budgeting technique does not consider the time value of money.
  - All capital budgeting techniques will produce the same decision in selecting among alternatives.
28. Which of the following methods of evaluating capital budgeting proposals rests on the assumption that income is uniform over the life of an investment?
- Internal rate of return
  - Payback method
  - Net present value
  - Accounting rate of return
29. X , purchased a machine for Rs.100,000. The machine has a useful life of five years and no salvage value. Straight-line depreciation is to be used. The machine is expected to generate cash flow from operations, net of income taxes, of Rs.30,000 in each of the five years. X's expected rate of return is 10%. Information on present value factors is as follows:

Period	Present value of Rs.1 at 10%	Present value of ordinary annuity of Rs.1 at 10%
1	0.90909	0.90909
2	0.82645	1.73554
3	0.75132	2.48685
4	0.68301	3.16986



What would be the net present value?

- (a) Rs.6,862
  - (b) Rs.13,724.
  - (c) Rs.50,000.
  - (d) Rs.62,092.
- 30 . B purchased a new machine for Rs.100,000. The machine will last ten years and is to be depreciated by the straight-line method. The estimated salvage value of the machine is zero. The machine should generate a yearly cash inflow of Rs.25,000. What is the accounting rate of return on this investment ignoring income taxes?
- (a) 5%
  - (b) 15%
  - (c) 25%
  - (d) 35%
31. In general, the presence of taxes:
- (a) Will cause the net present value of an investment to increase.
  - (b) Will cause the internal rate of return to decrease.
  - (c) Does not change the accounting rate of return. (d) All of these.
32. What is the internal rate of return associated with a Rs.20,000 investment which returns Rs.11,000 at the end of year 1 and Rs.12,100 at the end of year 2?
- (a) 10%
  - (b) 11%
  - (c) 12%
  - (d) 13%
33. F Company is considering the purchase of a new machine. The machine cost Rs.200,000 and will generate yearly cash inflow of Rs.30,000. What is the payback period?
- (a) 4 years and 8 months.
  - (b) 6 years and 8 months.
  - (c) 6 years and 9 months.
  - (d) 15 years.
34. Feasibility Set Approach to Capital Rationing can be applied in:
- (a) Accept-Reject Situations,
  - (b) Divisible Projects,
  - (c) Mutually Exclusive Projects,

- (d) None of the above
35. In case of divisible projects, which of the following can be used to attain maximum NPV?
- (a) Feasibility Set Approach,
  - (b) Internal Rate of Return,
  - (c) Profitability Index Approach,
  - (d) Any of the above
36. In case of the indivisible projects, which of the following may not give the optimum result?
- (a) Internal Rate of Return,
  - (b) Profitability Index,
  - (c) Feasibility Set Approach,
  - (d) All of the above
37. Which of the following refers to the risk associated with interest rate uncertainty?  
Select correct option:
- (a) Default risk premium
  - (b) Sovereign Risk Premium
  - (c) Market risk premium
  - (d) Maturity risk premium
38. Depreciation is incorporated into the discounted cash flow analysis of an investment proposal because it:
- (a) Is a cost of operations which cannot be avoided (b) Results in an annual cash outflow.
  - (c) Is a cash inflow.
  - (d) Reduces the cash outlay for income taxes.
39. Capital budgeting is a part of:
- (a) Investment decision
  - (b) Working capital management
  - (c) Marketing management
  - (d) Capital structure
40. Capital budgeting deals with:
- (a) Long term decisions
  - (b) Short term decisions
  - (c) Both (a) and (B)
  - (d) Neither (a) nor (b)

41. Which of the following is not used in capital budgeting?
- (a) Time Value of Money
  - (b) Sensitivity Analysis
  - (c) Net Assets Value Method
  - (d) Cash Flows
42. Capital budgeting decisions are:
- (a) Reversible
  - (b) Irreversible
  - (c) Unimportant
  - (d) All of the above
43. Which of the following is not incorporated in capital budgeting?
- (a) Tax effect
  - (b) Time Value of Money
  - (c) Required rate of return
  - (d) Rate of cash discount
44. Which of the following is not a capital budgeting decision?
- (a) Expansion programme
  - (b) Merger
  - (c) Replacement of an Asset
  - (d) Inventory Level
45. A sound capital budgeting technique is based on:
- (a) Cash Flows
  - (b) Accounting Profit
  - (c) Interest rate on borrowings
  - (d) Last dividend paid
46. Which of the following is not a relevant cost in capital budgeting?
- (a) Sunk Cost
  - (b) Opportunity cost
  - (c) Allocated overheads
  - (d) Both (a) and (c) above
47. Capital budgeting decisions are based on:
- (a) Incremental profit
  - (b) Incremental cash flows
  - (c) Incremental assets
  - (d) Incremental capital

48. Which of the following does not affect cash flows from a proposal:
- (a) Salvage value
  - (b) Depreciation amount
  - (c) Tax rate change
  - (d) Method of project financing
49. Cash inflows from a project include: (a) tax shield of depreciation
- (b) after tax operating profits
  - (c) raising of funds
  - (d) Both (a) and (b)
50. Which of the following is not followed in capital budgeting?
- (a) Cash flows principle
  - (b) Interest exclusion principle
  - (c) Accrual principle
  - (d) Post tax principle
51. Depreciation is incorporated in cash flows because it:
- (a) Is avoidable cost,
  - (b) Is a cash flow,
  - (c) Reduces tax liability,
  - (d) Involves an outflow.
52. Which of the following is not true for capital budgeting? (a) Sunk costs are ignored.
- (b) Opportunity costs are excluded.
  - (c) Incremental cash flows are considered.
  - (d) Relevant cash flows are considered.
53. Which of the following is not applied in capital budgeting?
- (a) Cash flows be calculated in incremental terms,
  - (b) All costs and benefits are measured on cash basis,
  - (c) All accrued costs and revenues be incorporated,
  - (d) All benefits are measured an after-tax basis.
54. Evaluation of Capital Budgeting Proposals is based on Cash Flows because:
- (a) Cash Flows are easy to calculate,
  - (b) Cash Flows are suggested by SEBI,
  - (c) Cash is more important than Profit,
  - (d) None of the above.
55. Which of the following is not included in incremental cash flows?

- (a) Opportunity Costs,
  - (b) Sunk Costs,
  - (c) Change in Working Capital
  - (d) Inflation effect.
56. Which of the following statement is correct? (a) If  $PI < 1$ , its NPV is less than zero,
- (b) If  $PI = 0$ , its NPV is greater than zero,
  - (c) If  $PI > 1$ , its NPV will be Negative,
  - (d) PI of a project is always greater than one.
57. Profitability Index method is an extension of :
- (a) Net Present Value,
  - (b) Internal Rate of Return,
  - (c) Payback Period,
  - (d) Accounting Rate of Return
58. Which of the following variables is not known in Internal Rate of Return?
- (a) Initial Cash Flows,
  - (b) Discount Rate,
  - (c) Terminal Inflows,
  - (d) Life of the project.
59. In case of Mutually Exclusive Proposals:
- (a) Only the best project is selected,
  - (b) All projects with positive NPV are selected,
  - (c) Even Negative NPV Project may be selected,
  - (d) At least two proposals are selected.
60. Reinvestment Rate Assumption is implied in: (a) Net Present Value,
- (b) Internal Rate of Return,
  - (c) Both (a) and (b),
  - (d) None of the above.
61. A project whose cash flows are more than capital invested for rate of return then net present value will be
- (a) positive
  - (b) independent
  - (c) negative
  - (d) zero
62. In mutually exclusive projects, project which is selected for comparison with others must have

- (a) higher net present value
  - (b) lower net present value
  - (c) zero net present value
  - (d) all of above
63. Relationship between Economic Value Added (EVA) and Net Present Value (NPV) is considered as
- (a) valued relationship
  - (b) economic relationship
  - (c) direct relationship
  - (d) inverse relationship
64. An uncovered cost at start of year is \$200, full cash flow during recovery year is \$400 and prior years to full recovery is 3 then payback would be
- (a) 5 years
  - (b) 3.5 years
  - (c) 4 years
  - (d) 4.5 years
65. In capital budgeting, positive net present value results in
- (a) negative economic value added
  - (b) positive economic value added
  - (c) zero economic value added
  - (d) percent economic value added
66. Which of the following capital budgeting techniques takes into account the incremental accounting income rather than cash flows:
- (a) Net present value
  - (b) Internal rate of return
  - (c) Accounting/Simple rate of return
  - (d) Cash payback period
67. Which of the following techniques does not take into account the time value of money?
- (a) Internal rate of return method
  - (b) Simple cash payback method
  - (c) Net present value method
  - (d) Discounted cash payback method
68. The current worth of a sum of money to be received at a future date is called:
- (a) real value

- (b) future value
- (c) present value
- (d) salvage value

69. The difference between the present value of cash inflows and the present value of cash outflows associated with a project is known as:
- (a) net present value of the project
  - (b) net future value of the project
  - (c) net historical value of the project
  - (d) net salvage value of the project
70. If present value of cash outflow is equal to present value of cash inflow, the net present value will be:
- (a) positive
  - (b) negative
  - (c) zero
  - (d) infinite

**Ans.** (1)(b), (2)(b), (3)(d), (4)(d), (5)(b), (6)(b), (7)(c), (8)(d), (9)(c), (10)(d), (11)(d), (12)(b), (13)(d), (14)(a), (15)(c) 16(a), 17(b), 18(d),19(a), 20(a), 21(a), 22(c), 23(c), 24(c), 25(d), 26(c), 27(a), 28(d), 29(b), 30(b), 31(b), 32(a), 33(b),34(a),35(c),36(c) 37(d), 38(d), 39(a), 40(a), 41(c), 42(b), 43(d), 44(d), 45(a), 46(d), 47(b), 48(d), 49(d), 50(c), (51)(c), (52)(b), (53)(c),(54)(c), (55)(b),(56)(a), (57)(a), (58)(b), (59)(a), (60)(c), (61)(a), (62)(a), (63)(c), (64)(b), (65)(b), (66)(c), (67)(b), (68)(c), (69)(a), (70)(c).

## II Short Answer Type Questions:

- 1 What is payback period?
- 2 Discuss the applicability of the concept of payback period.
- 3 Define accounting rate of return.
- 4 What are the merits of ARR as a capital budgeting technique.
- 5 Write short note on reinvestment rate.
- 6 Explain discounted payback period.
- 7 What do you understand by IRR. Explain.
- 8 Write short note on desirability factor.
- 9 Explain discounted payback period.
- 10 Briefly explain capital rationing.
- 11 Write a short note on expected value of cash flows.
- 12 Explain certainty equivalent approach.
- 13 Write a short note on risk adjusted discount rate.

- 14 Explain decision tree approach.
- 15 Write a short note on conventional cash flows.
- 16 Write a short note on Reinvestment Rate.
- 17 Write a short note on Allocated overheads.
- 18 What is meant by DCF criteria?
- 19 State three important steps in the evaluation of investments. 20 What is meant by the term value of money?
- 21 “The average accounting rate of return fails to give weight to the later cash flows.” Elaborate.
- 22 Explain the concept of value-additivity in the NPV method.

### **III Long Answer Type Questions:**

- 1 Why is it important to evaluate capital budgeting projects on the basis of after-tax cash incremental flows? Why not use accounting data instead of cash flows?
- 2 Describe the concept of discounted cash flows in making investment decisions and its superiority over the traditional methods of investment evaluation.
- 3 How is payback period calculated? How is it helpful in determining IRR.
- 4 How should working capital and sunk costs be treated in analyzing investment opportunities? Explain with suitable examples?
- 5 Discuss the major aspects, assumptions and decision rules of the Discounted Cash Flow method.
- 6 What is meant by internal Rate of Return of a project? How do you calculate IRR given the initial investment on the project and the cash flows arising during the expected life of the project?
- 7 Distinguish between NPV and IRR.
- 8 Make a comparison between NPV and IRR methods. Which one of the two you find to be more rationale and why.
- 9 “The payback period is more a method of liquidity rather than profitability.” Examine.
- 10 Do the Profitability Index and NPV criterion of evaluating investment proposals lead to the same acceptance rejection and ranking decisions? In what situations will they give conflicting results?
- 11 ‘NPV method ensures maximization of wealth of the shareholders in the long run.’ Comment.
- 12 Distinguish between Internal rate of return and Accounting rate of return with appropriate illustrations.
- 13 ‘The virtue of IRR method is that it does not require the pre-calculation of the required rate of return.’ Critically examine.



- 14 'Risk analysis is an essential feature of investment decision making process.' What are the major risk factors and how will you control them.
- 15 'The terminal value method overcomes the shortcomings of the assumption of reinvestment rate.' In light of this statement, explain the procedure of this terminal value method.
- 16 "NPV method ensures maximization of wealth of the shareholders in the long run." Comment.
- 17 What is the significance of profitability index? How is it useful in projects having different sizes? Under what circumstances is it better than NPV?
- 18 How can the inflation be incorporated in the capital budgeting decision process. Explain the difference between real and optimum replacement period.
- 19 Explain the concept of risk analysis with reference to capital budgeting.
- 20 "Risk analysis is an essential feature of investment decision making process." What are the major risk factors and how will you control them.
- 21 What is risk evaluation and sensitivity analysis? Analyse the relevance of sensitivity analysis in capital budgeting.
- 22 What do you mean by risk adjusted discount rate? How does it differ from certainty equivalent approach?
- 23 How the simulation technique can overcome the problem of risk and uncertainty. Explain.
- 24 "Risk analysis of capital investment is one of the most complex and controversial area in finance." Critically comment.
- 25 Describe the decision tree approach to capital budgeting. Examine the suitability of this approach.
- 26 Explain Modified IRR
- 27 Write a note on Inflation and Capital budgeting.
- 28 What is meant by the term time value of money? Which capital budgeting methods take into consideration this concept? How is it possible for the capital budgeting methods that do not consider the time value of money to lead to wrong capital budgeting decisions?
- 29 "The payback reciprocal has wide applicability as a meaningful approximation of the time adjusted rate of return. But it suffers from certain major limitations." Explain.
- 30 "We use payback primarily as a method of coping with risk." Comment.
- 31 What are the advantages of risk-adjusted discount rate? What is the major problem in using this approach to handle risk in capital budgeting?
- 32 "The certainty equivalent approach is theoretically superior to the risk-adjusted discount rate". Do you agree? Give reasons.
- 33 Write short notes on any three of the following: -
- a. International Capital Budgeting Decisions
  - b. Operating Cycle
  - c. Global Depository Receipt
  - d. Decision Tree

34. The cash flow approach of measuring future benefits of a project is superior to the accounting approach. Discuss.
35. How would you deal 'Sunk Cost' and 'Allocated overheads' in analyzing investment decisions?
36. Differentiate between Risk – adjusted Discount rate and certainty Equivalent methods of incorporation of risk in capital budgeting.
37. The cash flow approach of measuring future benefits of a project is superior to the accounting approach. Discuss.
38. What are mutually exclusive projects? Explain the conditions when conflicting ranking would be given by the internal rate of return and net present value methods to such projects.
39. Under what circumstances do the net present value and internal rate of return methods differ? Which methods would you prefer and why?
40. "Discounted payback ensures that you don't accept an investment with negative NPV, but it can't stop you from rejecting projects with a positive NPV." Illustrate why this can happen.
41. How can you conduct the DCF break-even analysis? Why is the DCF analysis important in risk analysis in capital budgeting?
42. How can utility theory be incorporated in the capital budgeting decisions to account for the risk preferences of the decision making?

#### **IV Practical Questions:**

- 1 ABC and Co. is considering a proposal to replace one of its plants costing Rs. 60,000 and having a written down value of Rs. 24,000. The remaining economic life of the plant is 4 years after which it will have no salvage value. However, if sold today, it has a salvage value of Rs. 20,000. The new machine costing Rs. 1,30,000 is also expected to have a life of 4 years with a scrap value of Rs. 18,000. The new machine: due to its technological superiority, is expected to contribute additional annual benefit (before depreciation and tax) of Rs. 60,000. Find out the cash flows associated with this decision given that the tax rate applicable to the firm is 40%. (The capital gain or loss may be taken as not subject to tax.)

**Ans. Initial flows: 1,10,000; subsequent flows: 44,800; terminal flows; 62,800**

- 2 KBC Ltd. is considering an expansion plan. If the plan is approved, it will give the company, an opportunity to reorganise its stores department which is expected to reduce the annual operating cost by Rs. 50,000 over next 5 years. However, this plan will cause the company to modify its replacement plans. Consequently, the expenditure plans of Rs. 1,50,000 p.a. for year 3 and 5 will have to be increase to Rs. 1,90,000 p.a. and rescheduled to occur in year 1 and 4. All other plans will remain unaffected. Find out the relevant cash

flows for the expansion plan in respect of the above for first 5 years given that the tax rate is 40% and depreciation is provided as per SL method (life 5 years).

**Ans. Net cash flows: Yr 1 Rs.-1,44,800, Yr. 2 Rs. 45,200, Yr. 3 Rs. 1,83,200, Yr 4. Rs. -1,41,600, Yr 5 Rs. 1,86,400**

- 3 XYZ is interested in assessing the cash flows associated with the replacement of an old machine by a new machine. The old machine bought a few years ago has a book value of Rs. 90,000 and it can be sold for Rs. 90,000. It has a remaining life of five years after which its salvage value is expected to be nil. It is being depreciated annually at the rate of 20 per cent (written down value method.)

The new machine costs Rs. 4,00,000. It is expected to fetch Rs. 2,50,000 after five years when it will no longer be required. It will be depreciated annually at the rate of 33 1/3 per cent (written down value method.) The new machine is expected to bring a saving of Rs. 1,00,000 in manufacturing costs. Investment in working capital would remain unaffected. The tax rate applicable to the firm is 50 per cent. Find out the relevant cash flow for this replacement decision. (Tax on capital gain/loss to be ignored)

**Ans. Yr.1 Rs. 107.6, Yr 2 Rs. 87.2, Yr 3 Rs. 73.9, Yr. 4 Rs. 65.2, Yr 5 Rs. 59.4, terminal flows: 3,09,400**

- 4 XYZ Ltd. is trying to decide whether it should replace a manually operated machine with a fully automatic version of the same machine. The existing machine, purchased ten years ago, has a book value of Rs. 2,40,000 and remaining life of 20 years. Salvage value was Rs. 40,000. The machine has recently begun causing problems with breakdowns and is costing the company Rs. 20,000 per year in maintenance expenses. The company has been offered Rs. 1,00,000 for the old machine as a trade-in on the automatic model which has a deliver price (before allowance for trade-in) of Rs. 2,20,000. It is expected to have a tenyear life and a salvage value of Rs. 20,000. The new machine will require installation modifications costing Rs. 40,000 to the existing facilities, but it is estimated to have a cost savings in materials of Rs. 80,000 per year. Maintenance costs are included in the purchase contract and are borne by the machine manufacturer. The tax rate is 40% (applicable to both revenue income as well as capital gains/losses). Straight-line depreciation over ten years will be used. Find out the relevant cash flows.

**Ans. Initial flows: Rs. 1,44,000; Subsequent Rs. 65,600 and Terminal Rs. 85,600**

- 5 A company has to make a choice between two projects namely A and B. the initial capital outlays of two projects are Rs. 1,35,000 and Rs. 2,40,000 respectively for A and B. there will be no scrap value at the end of the life of both the projects. The opportunity cost of capital of the company is 16%. The annual incomes are as under:

Year	Project A	Project B
1	-	60,000

2	30,000	84,000
3	1,32,000	96,000
4	84,000	1,02,000
5	84,000	90,000

You are required to calculate for each Project

	<b>A</b>	<b>B</b>	
i) Discounted Payback period	<b>Ans. 3.61 yrs</b>	<b>4.19 yrs</b>	ii)
Profitability Index	<b>Ans. 1.43</b>	<b>1.15</b>	
iii) NPV	<b>Ans. Rs. 58,254</b>	<b>Rs. 34,812</b>	

- 6 Z Industries Ltd. are thinking of investing in a project costing Rs. 20 lakhs. The life of the project is five years and the estimated salvage value of the project is zero. Straight line method of charging depreciation is followed. The tax rate is 50%. The expected cash flows before tax are as follows:

Year	1	2	3	4	5
Estimated cash flows before depreciation and tax (in lakhs)	4	6	8	8	10

You are required to determine the

Payback Period for the investment	<b>Ans. 3 yrs 10 months</b>
ARR on the investment	<b>Ans. 16%</b>
NPV at 10% cost of capital	<b>Ans. 0.717 lakhs</b>
Benefit cost ratio	<b>Ans. 1.036</b>

- 7 The cash flows of two mutually exclusive projects are as under:

	T0	T1	T2	T3	T4	T5	T6
Project P	(40,000)	13,000	8,000	14,000	12,000	11,000	15,000
Project J	(20,000)	7,000	13,000	12,000	-	-	-

Required:

- Estimate the net present value using 15%.
- Estimate the internal rate of return. iii) Why is there a conflict in the project choice by using NPV and IRR criterion.
- Which criteria you will use in such a situation? Estimate the value at that criterion. Make a project choice.

<b>Ans.</b>	<b>Project P</b>	<b>Project J</b>
i) NPV	<b>5,374</b>	<b>3,806</b>
ii) IRR	<b>19.75%</b>	<b>25.31%</b>

**iv) The annualized equivalent of Project J is higher than Project P, hence project J can be selected.**

8 Jolly company has an investment opportunity costing Rs. 40,000 with the following expected cash inflow (*i.e.* after tax and before depreciation):

Year	Inflows	PVF	Year	Inflows	PVF
1	Rs.7,000	0.909	6	Rs. 8,000	0.564
2	7,000	0.826	7	10,000	0.513
3	7,000	0.731	8	15,000	0.467
4	7,000	0.653	9	10,000	0.424
5	7,000	0.621	10	4,000	0.386

Using 10% as the cost of capital (rate of discount) determine the (i) Net Present Value; and (ii) Profitability Index.

**Ans. NPV = Rs. 8,961, PI = 1.22**

9 A company is engaged in evaluating an investment project which requires an initial cash outlay of Rs. 2,50,000 on equipment. The project's economic life is 10 years and its salvage value Rs. 30,000. It would require current assets of Rs. 50,000. An additional investment of Rs. 60,000 would also be necessary at the end of five years to restore the efficiency of the equipment. This would be written off completely over the last five years. The project is expected to yield annual profit (before tax) of Rs. 1,00,000. The company follows the sum of the years' digit method of depreciation. Income-tax rate is assumed to be 40%.

Should the project be accepted if the minimum required rate of return is 20%.

**Ans. NPV = Rs. – 6,662. since, NPV is negative, proposal needs to be rejected.**

10 Modern Enterprises Ltd. is considering the purchase of a new computer system for its Research and Development Division, which would cost Rs. 35 lacs. The operation and maintenance costs (excluding depreciation) are expected to be Rs. 7 lacs per annum. It is estimated that the useful life of the system would be 6 years, at the end of which the disposal value is expected to be Rs. 1 lac.

11 The tangible benefits expected from the system in the form of reduction in design and draughtsman ship costs would be Rs. 12 lacs per annum. Besides, the disposal of used drawing office equipment and furniture, initially, is anticipated to net Rs. 9 lacs Capital expenditure in research and development would attract 100% write-off for tax purposes. The gains arising from disposal of used assets may be considered tax-free. The company's effective tax rate is 50%. The average cost of capital to the company is 12%. After appropriate analysis of cash flows, please advise the company of the financial viability of the proposal.

**Ans. NPV = Rs. 41,000. the proposal may be accepted**

- 12 A Ltd. has an investment budget of Rs. 25 lakhs for next year. It has under consideration three projects A, B and C ( b and C are mutually exclusive) and all of them can be completed within a year. Further details are given below: (lakhs)

Project	Investment required	Net present value
A	14	5.6
B	12	7.2
C	10	5.0

Recommend the best policy to utilize the investment budget, supported by proper reasoning.

**Ans. A and C**

- 13 Five projects M, N, O, P and Q are available for consideration. The investment required for each project and the cash flows it yields are tabulated below. Projects N and Q are mutually exclusive. Taking the cost of capital @ 10%, which combination of projects should be taken up for a total capital outlay not exceeding Rs. 3 lakhs on the basis of NPV and benefit cost ratio.

Project	Investment	Cashflow p.a.	No. of years	P.V. @ 10%
M	50,000	18,000	10	6.145
N	1,00,000	50,000	4	3.170
O	1,20,000	30,000	8	5.335
P	1,50,000	40,000	16	7.824
Q	2,00,000	30,000	25	9.077

**Ans. The optimum combination of projects is M, N and P with total investment of Rs. 3 lakhs since it has highest NPV and BCR of Rs. 2,82,070 and 1.940 respectively.**

- 14 A company employs CE approach in the evaluation of risky investments. The capital budgeting department of the company has developed the following information regarding a new project.

Year	Expected CFAT (Rs. Thousand)	CE quotient
0	(200)	1.0
1	160	0.8
2	140	0.7
3	130	0.6
4	120	0.4
5	80	0.3

The firm's cost of equity capital is 18%, its cost of debt is 9% and the riskless rate of interest in the market on the government securities is 6%. Should the project be accepted?

**Ans. NPV = Rs. 1,29,388, so the project should be accepted**

- 15 A company is considering an investment in a project that requires an initial net investment of Rs. 3,000 with an expected cash flow (CFAT) generated over three years as follows:

CFAT	Probability	CFAT	Probability	CFAT	Probability
Rs. 800	0.1	Rs. 800	0.1	Rs. 800	0.2
1,000	0.2	1,000	0.3	1,000	0.5
1,500	0.4	1,500	0.4	1,500	0.2
2,000	0.3	2,000	0.2	2,000	0.1

- (a) What is the expected NPV of this project? (Assume that the probability distributions are independent and the risk free rate of interest in the market is 0.05.) **[Ans. Rs. 663]**
- (b) Calculate the standard deviation about the expected value. **[Ans. 662]**
- (c) Find the probability that the NPV will be less than zero. (Assume that the distribution is normal and continuous.) **[Ans. 14.23%]**
- 16 A company has the following estimates of the future cash flows after taxes associated with the investment proposal, concerned with expanding the plant capacity. It intends to use a decision tree approach to get a clear picture of the possible outcomes of this investment. The plant expansion is expected to cost Rs. 3,00,000. The respective PVs of future CFAT and probabilities are as follows:

PV of future CFAT

With expansion	Without expansion	Probabilities
Rs. 3,00,000	Rs. 2,00,000	0.2
5,00,000	2,00,000	0.4
9,00,000	3,50,000	0.4

Advise the company regarding the financial feasibility of the project.

**Ans. The expected NPV with the plant expansion and without expansion is Rs. 3,20,000 and Rs. 2,60,000 respectively. Therefore, the company is advised to expand the plant capacity.**

- 17 A software company is considering installing an air conditioning plant, for the entire company. It has two options X and Y.

Plant X cost Rs.5,00,000 to purchase and install. it has 5 years of useful life and will be depreciated over this period on S.L.M basis to a book value of Rs.25,000.However, the management hopes to sell it for Rs.40,000.Maintainence and other operating costs of running the plant are Rs.2,50,000 per year.

Plant Y has a 10 year life but costs Rs.7,00,000 to purchase and install. It will be depreciated over 8years on SLM to zero book value .However at the beginning of year 7 it is expected to cost Rs.1,00,000;it is not to be capitalized but to be expended. At year end 10, the plant is expected to have a salvage value of Rs.30,000,which is likely to be equivalent to removal cost of plant. Plant Y is less expensive to run than Plant X as it requires Rs. 2,20,000 per year to operate.

Corporate tax rate is 35% cost of capital is 12%.Assuming SLM of depreciation as well as the time period of depreciation are acceptable for tax purchase, advise which plant should be purchased by the company.

- 18 A project involving a outlay of 10 lakh has the following inflows associated with it

Year 1		Year 2		Year3	
Probability	Cash flow	Probability	Cash flow	Probability	Cash flow
0.4	4	0.4	5	0.3	3
0.5	5	0.4	6	0.5	4
0.1	6	0.2	7	0.2	5

Assume that the cash flows are independent. Calculate the expected NPV and standard deviation of NPV assuming that cost of capital is 10% Also find out probability of NPV being Zero or less if NPV and standard deviation are considered to be normal.

- 19 An educational institute is planning to install air conditioners for its new computer centre. It has received two different proposals. The first proposal is for the installation of window type air conditioners costing Rs.1,50,000. The other is for installation of split air conditioners of same capacity costing Rs.2,00,000. The useful life of window air conditioners is 6 years and that of split air conditioners is 10 years. The cash operating cost associated with each proposals are given below-

Year	Proposal 1 (Rs.)	Proposal 2 (Rs.)
1	20000	15000
2	20000	15000
3	20000	15000
4	25000	18000
5	25000	18000
6	25000	18000



7		22000
8		22000
9		22000
10		22000

The salvage value of the window air conditioners at the end of 6 years is expected to be Rs.10,000 and that of the split air conditioners Rs.15,000. Advise the educational institute which proposal should be selected by it if its opportunity cost of funds is 10%.

- 20 C is considering investing in a project. The expected investment will be Rs. 2,00,000. The life of project will be 5 years with no salvage value. The expected net cash inflows after depreciation but before tax during the life of the project will be as follows:

Year	1	2	3	4	5
Rs.	85,000	1,00,000	80,000	80,000	40,000

Project will be depreciated at the rate of 20% on original cost. Tax rate 30%. Calculate

- i) ARR (**Ans: 53.90%**) ii) Payback period (**Ans. 1year 11 months**) iii) IRR (**Ans. 39.91%**)  
iv) NPV if cost of capital is 10% (**Ans. Rs. 1,61,197**)
- 21 K company is considering to set up a coaching centre at a total outlay of Rs. 18,00,000. The operational and maintenance cost excluding depreciation are expected to be Rs. 3,00,000 p.a. life of equipment is 10 years with no salvage value. Depreciation is 30% w.d.v. tax rate if 40%. The centre will generate an income of Rs. 6,00,000 p.a. by way of tuition fee and Rs. 1,00,000 on job work. Calculate NPV and IRR if cost of capital is 12%. (**Ans. NPV = (49,216), IRR = 12.24%**)
22. A firm can make investment in either of the following two projects. The firm anticipates its cost of capital to be 10%. And the net (after tax) cash flows of the projects for the five years are as follows: -

(Figure in Rs. '000)						
Year	0	1	2	3	4	5
Project A	(500)	85	200	240	220	70
Project B	(500)	480	100	70	30	20

The discount factors are as under						
Year	0	1	2	3	4	5
PVF (10%)	1	0.91	0.83	0.75	0.68	0.62
PVF (20%)	1	0.83	0.69	0.58	0.48	0.41

Required: -

- i. Calculate the NPV and IRR of the project.
- ii. State with reason which project you would recommend.

**Ans**

	Project A	Project B
NPV	116.35	105.1
IRR	18.663%	24.107%

- i. As per NPV, Project A should be selected.
- ii. As per IRR, Project B should be selected.

- 23 No Project is acceptable unless the yield is 10%. Cash inflows of a certain project along with cash outflows are given below:

Year	Outflow (Rs.)	Inflow(Rs.)
0	150000	-
1	30000	20000
2	-	30000
3	-	60000
4	-	80000
5	-	70000

Calculate net present value

**Ans:** Net present value = Present value of Inflows - Present value of Outflows  
= Rs.186130 – Rs. 177270  
= Rs 8860

- 24 One of the two machines A and B is to be purchased. Form the following Information find out which of the two will be more profitable? The average rate of tax may be taken at 50%.

	Machine A (Rs.)	Machine B (Rs.)
Cost of machine	50000	80000
Machine Life	4 years	6 years
<b>Earnings Before Tax</b>		
1st year	10000	8000
2nd year	15000	14000
3rd year	20000	25000
4th year	15000	30000
5th year		18000
6th year		13000

**Ans:**

(a) Pay back period

Investment = Rs. 80,000

Cumulative Cash Flows shows that the recovery up to 3rd year = 63499 therefore for the balance of Rs. 16501 will be recovered in 4th year. i.e.  $16501/28333 = 0.58$  year therefore payback period is 3.58 years

(b) Average rate of return (based on original investment)

= Average Profits/net investment x 100  
=  $54000/6 \times 100$   
= 11.25%

Machine A is profitable in both the cases

Note: - It has been assumed that Earnings Before tax in the problem is after considering depreciation on straight line basis.

25. A machine costing Rs. 110 lacs has a life of 10 years, at the end of which its scrap value is likely to be Rs. 10 lacs. The firm's cut off rate is 12%. The machine is expected to yield an annual profit after tax of Rs. 10 lacs, depreciation being reckoned on straight line basis. Ascertain the net present value of the project.

**Ans. NPV of the project is Rs. 6,22,000.**

26. A company is considering the possibility of manufacturing a particular component which at present is being bought from outside. The manufacture of the component would call for an investment of Rs. 7,50,000 in a new machine besides an additional investment of Rs. 50,000 in working capital. The life of machine would be 10 years with a salvage value of Rs. 50,000. The estimated savings (after incremental depreciation but before tax) would be Rs. 1,80,000

per annum. The income tax rate is 50%. The company's required rate of return is 10%. Depreciation is provided on straight line basis. Should the company make this investment?

**Ans. NPV of the project Rs. 2,21,800. The company should make the investment.**

27. A project involving an initial investment of Rs 45L has the following probability distribution of net cash flows during its life of four years

(Rs. In Lakhs)

Year 1		Year 2		Year 3		Year 4	
Net Cash Flow	Probability	Net Cash Flow	Probability	Net Cash Flow	Probability	Net Cash Flow	Probability
16	0.3	19	0.5	16	0.2	16	0.5
24	0.1	28	0.2	24	0.3	28	0.3
32	0.6	36	0.3	40	0.5	32	0.2

The cash flows for the various years are independent of each other. The net present value of the project is expected to be approximately normally distributed. The risk free rate is 8 percent. You are required to find out the probability that the internal rate of return will exceed the risk free rate.

**Ans. Probability = 49%**

28. A government owned research organization needs sophisticated equipment for its research purposes. Three companies came forward to supply the machine whose quotations are as given below:-

Company A: Initial Cost is Rs. 62,000 and annual maintenance cost is Rs. 4,000 in the first year and increases by Rs. 1000 every year for the next 5 years. At the end of the sixth year the machine can be sold for Rs. 12,000.

Company B: Initial Cost is Rs. 85,000. The maintenance cost is Rs. 3,000 per year. But in the fourth year additional Rs. 9,000 should be spent for overhauling. Its scrap value at the end of 7<sup>th</sup> year is Rs. 15,000.

Company C: The machine costs Rs. 48,000 but its life is only 3 years with annual maintenance cost of Rs. 2,500. At the end of year 3, the company replaces the old machine with a new machine for Rs. 20,000. The new machine will last for another 2 years with an annual maintenance cost of Rs. 1,000 and a salvage value of Rs. 14,000. Which option the organization should go for? Since it is a research organization it does not pay taxes but its cost of funds is 10%.

**Ans. NPV**

Company A	-82329
Company B	-98053
Company C	-61845

Since it is a research organization, no Cash inflows are generated, hence NPV of only outflows are calculated for all quotations. Hence all NPV are **Negative**. The organization should go for highest NPV alternative offered by **Company C**.

29. A cosmetic company is considering to introduce a new lotion. The manufacturing equipment will cost Rs.5,60,000. The expected life of the equipment is 8 years. The company is thinking of selling the lotion in a single standard pack of 50 grams at Rs. 12 each pack. It is estimated that variable cost per pack would be Rs. 6 and annual fixed cost Rs. 4,50,000. Fixed cost includes (straight line) depreciation of Rs. 70,000 and allocated overheads of Rs. 30,000. The company expects to sell 1,00,000 packs of the lotion each year. Assume that tax is 45% and straight-line depreciation is allowed for tax purpose. Calculate the cashflows.

**Ans. 1,69,000**

30. ABC and Co. is considering a proposal to replace one of its plants costing Rs. 60,000 and having a written down value of Rs. 24,000. The remaining economic life of the plant is 4 years after which it will have no salvage value. However, if sold today, it has a salvage value of Rs. 20,000. The new machine costing Rs. 1,30,000 is also expected to have a life of 4 years with a scrap value of Rs. 18,000. The new machine, due to its technological superiority, is expected to contribute additional annual benefit (before depreciation and tax) of Rs. 60,000. Find out the cash flows associated with this decision given that the tax rate applicable to the firm is 40%. (The capital gain or loss may be taken as not subject to tax).

**Ans. Annual cash inflow is Rs. 44,800**

**Hint:** The amount of depreciation of Rs. 28,000 on the new machine is ascertained as follows:  $(Rs. 1,30,000 - Rs. 18,000) / 4 = Rs. 28,000$ . It may be noted that in the given situation, the benefits are given in the incremental form i.e., the additional benefits contributed by the proposal. Therefore, only the incremental depreciation of Rs. 22,000 has been deducted to find out the taxable profits. The same amount of depreciation has been added back to find out the incremental annual cash inflows.

**Terminal cash inflow:**

There will be an additional cash inflow of Rs. 18,000 at the end of 4<sup>th</sup> year when the new machine will be scrapped away. Therefore, total inflow of the last year would be Rs. 62,800 (i.e. Rs. 44,800 + Rs. 18,000).

## UNIT – IV

### I Test Your Skills:

#### (a) Multiple choice questions:

1. To financial analysts, "working capital" means the same thing as \_\_\_\_\_.
  - (a) Total assets
  - (b) fixed assets
  - (c) current assets
  - (d) current assets minus current liabilities.
  
2. Which of the following would be consistent with an aggressive approach to financing working capital?
  - (a) Financing short-term needs with short-term funds.
  - (b) Financing permanent inventory buildup with long-term debt.
  - (c) Financing seasonal needs with short-term funds.
  - (d) Financing some long-term needs with short-term funds.
  
3. Which of the following would be consistent with a conservative approach to financing working capital?
  - (a) Financing short-term needs with short-term funds.
  - (b) Financing short-term needs with long-term debt.
  - (c) Financing seasonal needs with short-term funds.
  - (d) Financing some long-term needs with short-term funds.
  
4. Which of the following would be consistent with a hedging (maturity matching) approach to financing working capital?
  - (a) Financing short-term needs with short-term funds
  - (b) Financing short-term needs with long-term debt.      (c) Financing seasonal needs with long-term funds.
  - (d) Financing some long-term needs with short-term funds.
  
5. Which of the following is a basic principle of finance as it relates to the management of working capital?
  - (a) Profitability varies inversely with risk.
  - (b) Liquidity moves together with risk.
  - (c) Profitability moves together with risk.
  - (d) Profitability moves together with liquidity.
  
6. Which of the following illustrates the use of a hedging approach to financing assets?

- (a) Temporary current assets financed with long-term liabilities.
  - (b) Permanent working capital financed with long-term liabilities.
  - (c) Short-term assets financed with equity
  - (d) All assets financed with a mixture of 50% equity and 50% long-term debt.
7. In deciding the optimal level of current assets for the firm, management is confronted with \_\_\_\_\_.
- (a) a trade-off between profitability and risk
  - (b) a trade-off between liquidity and risk
  - (c) a trade-off between equity and debt
  - (d) a trade-off between short-term versus long-term borrowing
8. Which of the following statements is most correct?
- (a) For small companies, long-term debt is the principal source of external financing.
  - (b) Current assets of the typical manufacturing firm account for over half of its total assets.
  - (c) Strict adherence to the maturity matching approach to financing would call for all current assets to be financed solely with current liabilities.
  - (d) Similar to the capital structure management, working capital management requires the financial manager to make a decision and not address the issue again for several months.
9. The amount of current assets required to meet a firm's long-term minimum needs is referred to as \_\_\_\_\_ working capital.
- (a) permanent
  - (b) temporary
  - (c) net
  - (d) gross
10. The amount of current assets that varies with seasonal requirements is referred to as \_\_\_\_\_ working capital.
- (a) permanent
  - (b) net
  - (c) temporary
  - (d) gross
11. Having defined working capital as current assets, it can be further classified according to \_\_\_\_\_.
- (a) financing method and time
  - (b) rate of return and financing method
  - (c) time and rate of return
  - (d) components and time

12. Your firm has a philosophy that is analogous to the hedging (maturity matching) approach. Which of the following is the most appropriate form for financing a new capital investment in plant and equipment?
- (a) Trade credit.
  - (b) 6-month bank notes.
  - (c) Accounts payable.
  - (d) Common stock equity.
13. Your firm has a philosophy that is analogous to the hedging (maturity matching) approach. Which of the following is the most appropriate non-spontaneous form for financing the excess seasonal current asset needs?
- (a) Trade credit.
  - (b) 6-month bank notes.
  - (c) Accounts payable.
  - (d) Common stock equity.
14. Under a conservative financing policy a firm would use long-term financing to finance some of the temporary current assets. What should the firm do when a "dip" in temporary current assets causes total assets to fall below the total long-term financing?
- (a) Use the excess funds to pay down long-term debt.
  - (b) Invest the excess long-term financing in marketable securities.
  - (c) Use the excess funds to repurchase common stock.
  - (d) Purchase additional plant and equipment.
15. Which of the following statements is correct for a conservative financing policy for a firm relative to a former aggressive policy?
- (a) The firm uses long-term financing to finance all fixed and current assets.
  - (b) The firm will see an increase in its expected profits.
  - (c) The firm will see an increase in its risk profile.
  - (d) The firm will increase its dividends per share (DPS) this period.
16. Which of the following statements is correct for an aggressive financing policy for a firm relative to a former conservative policy?
- (a) The firm will use long-term financing to finance all fixed and current assets.
  - (b) The firm will see an increase in its expected profits.
  - (c) The firm will see a decline in its risk profile.
  - (d) The firm will need to issue additional common stock this period to finance the assets.



17. How can a firm provide a margin of safety if it cannot borrow on short notice to meet its needs?
- (a) Maintain a low level of current assets (especially cash and marketable securities). (b) Shorten the maturity schedule of financing.
  - (c) Increasing the level of fixed assets (especially plant and equipment). (d) Lengthening the maturity schedule of financing.
18. Risk, as it relates to working capital, means that there is jeopardy to the firm for not maintaining sufficient current assets to \_\_\_\_\_.
- (a) meet its cash obligations as they occur and take advantage of prompt payment discounts
  - (b) support the proper level of sales and take prompt payment discounts
  - (c) maintain current and acid-test ratios at or above industry norms
  - (d) meet its cash obligations as they occur and support the proper level of sales
19. If a company moves from a "conservative" working capital policy to an "aggressive" policy, it should expect \_\_\_\_\_.
- (a) liquidity to decrease, whereas expected profitability would increase
  - (b) expected profitability to increase, whereas risk would decrease
  - (c) liquidity would increase, whereas risk would also increase
  - (d) risk and profitability to decrease
20. Which of the following types of company will have the lowest level of investment in working capital to finance?
- (a) Water suppliers
  - (b) Supermarkets
  - (c) Chemical manufacturers
  - (d) Ship builders
  - (e) Car manufacturers
21. Which of the following factors does not need to be considered when formulating policies on the level and financing of working capital?
- (a) The attitude to risk of a company's managers
  - (b) The relative cost of short-term and long-term finance
  - (c) The availability of revenue reserves and capital reserves
  - (d) Terms of trade offered by competitors
  - (e) The nature of current business operations
22. Which of the following statements relating to working capital financing is not correct?
- (a) An aggressive policy uses long-term debt to finance fluctuating current assets
  - (b) Long-term debt is less risky than short-term debt

- (c) A conservative policy uses long-term debt to finance fixed assets
  - (d) Short-term debt is cheaper than long-term debt
  - (e) The matching principle indicates that fluctuating current assets should be financed by short-term debt
23. Identify the incorrect statement in connection with working capital management.
- (a) Long-term funds are more expensive than short-term funds but also riskier
  - (b) The objectives of working capital management are profitability and liquidity
  - (c) Permanent current assets should be financed from long-term sources if a moderate or matching policy is adopted
  - (d) Conservative financing policies use short-term funds to finance only part of fluctuating current assets
  - (e) Aggressive financing policies increase profitability at the cost of higher risk
24. Which of the following will improve a company's working capital management position?
- (a) An increased level of bad debts
  - (b) An increase in the credit period allowed by suppliers
  - (c) An increased debtor collection period
  - (d) An increase in the stock turnover period
  - (e) An increase in the length of the production process
25. Identify which technique will not help a company to optimise its working capital cycle.
- (a) Offering discounts for early payment by debtors
  - (b) Using cash management models to optimise the level of cash held
  - (c) Taking full advantage of credit offered by trade suppliers
  - (d) Applying the economic order quantity model to stock management
  - (e) Adopting the use of just-in-time stock management methods
26. Which of the following is not an indicator that a firm is overtrading?
- (a) A sharp increase in sales
  - (b) Decreasing margins due to the use of discounts
  - (c) Increasing size of overdraft
  - (d) A decreasing debtor period
  - (e) An increasing creditor period
27. Factoring can best be defined as:
- (a) Sale of selected invoices to a third party
  - (b) Employment of a third party to manage purchases of goods
  - (c) Employment of a third party to collect bad debts
  - (d) Use of a third party to manage the administration of debtors

- (e) Insurance of specific accounts against risk of bad debts
28. Which of the following is least likely to be considered a short-term marketable security?
- (a) An original issue 30-year corporate bond with one-year remaining until final maturity.
  - (b) An original issue 30-year government bond with one-year remaining until final maturity.
  - (c) A 90-day Treasury bill.
  - (d) Short-term corporate debt instruments with a 9-month original maturity.
29. The optimal balance of marketable securities held to take care of probable deficiencies in the firm's cash account is referred to as the \_\_\_\_\_ segment in the firm's portfolio of short-term marketable securities.
- (a) ready cash
  - (b) controllable cash
  - (c) free cash
  - (d) cash and cash equivalent
30. The marketable securities available for unassigned purposes at the current time is referred to as the \_\_\_\_\_ segment in the firm's portfolio of short-term marketable securities.
- (a) ready cash
  - (b) controllable cash
  - (c) free cash
  - (d) cash and cash equivalents
31. Which of the following is not a standard method of transferring funds when using concentration banking?
- (a) Depository transfer check
  - (b) Automated clearinghouse electronic transfer
  - (c) Wire transfer
  - (d) Payable through draft (PTD).
32. Which would be an inappropriate investment for temporarily idle corporate cash that will be used to pay quarterly dividends three months from now?
- (a) An originally issued 30-year Treasury bond with a current annual yield of 9.4 percent that matures in 88 days
  - (b) An originally issued 30-year Treasury bond with a current annual yield of 9.7 percent that matures in 2 years
  - (c) 90-day commercial paper with a current annual yield of 9.6 percent
  - (d) A 3-month certificate of deposit with a current annual yield of 9.5 percent.
33. Which of the following marketable securities is issued by the government?

- (a) Commercial paper
  - (b) Negotiable certificates of deposit
  - (c) Repurchase agreement
  - (d) T-bills.
34. Which of the following was not suggested by John Maynard Keynes as a reason for holding cash?
- (a) Speculative motive.
  - (b) Investment motive.
  - (c) Precautionary motive.
  - (d) Transactions motive.
35. Which of the following statements most accurately describes the modern approach to cash management?
- (a) Cash management involves the efficient disbursement of cash.
  - (b) Cash management involves the efficient collection and disbursement of cash.
  - (c) Cash management involves the efficient processing, collection, and depositing of cash.
36. Collection float is the \_\_\_\_\_.
- (a) total time between the mailing of the check by the customer and the availability of cash to the receiving firm
  - (b) time consumed in clearing the check through the banking system
  - (c) time the check is in the mail
  - (d) time during which the check received by the firm remains uncollected
37. Deposit float is the \_\_\_\_\_.
- (a) total time between the mailing of the check by the customer and the availability of cash to the receiving firm
  - (b) time consumed in clearing the check through the banking system
  - (c) time the check is in the mail
  - (d) time during which the check received by the firm remains uncollected
38. Availability float is the \_\_\_\_\_.
- (a) total time between the mailing of the check by the customer and the availability of cash to the receiving firm
  - (b) time consumed in clearing the check through the banking system
  - (c) time the check is in the mail
  - (d) time during which the check received by the firm remains uncollected
39. Which of the following is not a technique to speed up collections?

- (a) Expedite the preparing and mailing of the invoice to customers.
  - (b) Replace a lockbox system with the direct mailing of payments to the firm.
  - (c) Reduce the time it takes payments received from customers to be available as \_\_\_\_\_ usable funds to the firm.
  - (d) Accelerate how quickly customers mail payments to the firm.
40. Concentration banking occurs when the firm \_\_\_\_\_.
- (a) moves cash from regional lockboxes to a centralized cash pool at a single institution
  - (b) replaces their lockbox system with a system that involves the direct payment to \_\_\_\_\_ the firm
  - (c) reduces the control over the inflow and outflow of corporate cash
  - (d) increases the quantity of cash balances that are "idle" (not earning a return)
41. The marketable securities held for meeting controllable outflows such as taxes or dividends is referred to as the \_\_\_\_\_ segment in the firm's portfolio of short-term marketable securities.
- (a) ready cash
  - (b) controllable cash
  - (c) free cash
  - (d) cash and cash equivalents
42. Which of the following statements is most correct regarding outsourcing?
- (a) Outsourcing is a "new" idea when it comes to cash management.
  - (b) "Reducing and controlling operating costs" generally ranks low when it comes to \_\_\_\_\_ reasons why outsourcing end users turn to outsourcing.
  - (c) While outsourcing is widely applied in the area of "collections," it is much less applicable to the area of "disbursements."
  - (d) Essential, but noncore areas of business are candidates for outsourcing.
43. A collection service provided by the firm's financial institution that receives electronic payments and accompanying remittance data and communicates this to the company in a specific format is referred to as what?
- (a) Electronic lockbox.
  - (b) Email.
  - (c) Electronic mail.

44. Walter's Model suggests for 100% DP ratio when
- (a)  $k_e = r$
  - (b)  $k_e < r$
  - (c)  $k_e > r$
  - (d)  $k_e = 0$
45. If a firm has  $k_e < r$ , the Walter's Model suggests for:
- (a) 0% Payout
  - (b) 100% Payout
  - (c) 50% Payout
  - (d) 25% Payout
46. Walter's Model suggests that a firm can always increase the value of the share by:
- (a) Increasing dividend
  - (b) Decreasing dividend
  - (c) Constant Dividend
  - (d) None of the above
47. Bird in hand' argument is given by
- (a) Walter's Model
  - (b) Gordon's Model (c) MM Model
  - (d) Residual's Theory
48. Residuals theory argues that dividend is a :
- (a) Relevant Decision
  - (b) Active Decision
  - (c) Passive Decision
  - (d) Irrelevant Decision
49. Dividend irrelevance argument of MM Model is based on:
- (a) Issue of Debentures
  - (b) Issue of Bonus Shares
  - (c) Arbitrage
  - (d) Hedging
50. Which of the following is not true for MM Model?
- (a) Share price goes up if dividend is paid
  - (b) Share price goes down if dividend is not paid
  - (c) Market value is unaffected by dividend policy

(d) All of the above

51. The term “Core Current assets” was coined by:

- (a) Chore Committee
- (b) Tandon Committee
- (c) Jilani Committee
- (d) None of the above

52. “Factoring makes the conversion of receivables into cash possible”. This statement is:

- (a) Only partially correct
- (b) misinterpreted
- (c) correct
- (d) wrong

53. A cash budget can be prepared by:

- (a) receipts and payments method
- (b) adjusted income method
- (c) adjusted balance sheet method
- (d) any of the above

54. Dividend Payout ratio is:

- (a)  $PAT / Capital$
- (b)  $DPS / EPS$
- (c)  $Pref. Dividend / PAT$
- (d)  $Pref. Dividend / Equity Dividend$

55. Dividend Distribution Tax is payable by:

- (a) Shareholders to Government
- (b) Shareholders to Company
- (c) Company to Government
- (d) Holding to Subsidiary Company

56. Which of the following stresses on investor’s preference for current dividend than higher future capital gains?

- (a) Walter’s Model
- (b) Residual’s Theory
- (c) Gordon’s Model
- (d) MM Model

57. MM Model of Dividend irrelevance uses arbitrage between :

- (a) Dividend and Bonus
  - (b) Dividend and Capital Issue
  - (c) Profit and Investment
  - (d) None of the above
58. If  $K_e = r$ , then under Walter's Model, which of the following is irrelevant?
- (a) Earning per share
  - (b) Dividend per share
  - (c) DP Ratio
  - (d) None of the above
59. When the items of Inventory are classified according to value of usage, the technique is known as:
- (a) XYZ analysis
  - (b) ABC analysis
  - (c) DEF analysis
  - (d) None of the above.
60. D Ltd. Has net credit sales of Rs. 7,04,00,000. Accounts receivables turnover is 12 times. Net receivable balance at the end of the period will be:
- (a) Rs. 58,66,667
  - (b) Rs. 1,17,33,333
  - (c) Rs. 88,00,000
  - (d) None of the above
61. Which of the following would be consistent with an aggressive approach to financing working capital?
- (a) Financing short-term needs with short-term funds.
  - (b) Financing permanent inventory buildup with long-term debt.
  - (c) Financing seasonal needs with
  - (d) Financing some long-term needs with short-term funds.
62. In finance, "working capital" means the same thing as
- (a) total assets
  - (b) fixed assets
  - (c) current assets
  - (d) current assets minus current liabilities
63. Which of the following would be consistent with a more aggressive approach to financing working capital?
- (a) Financing short-term needs with short-term funds



- (b) Financing permanent inventory buildup with long-term debt
  - (c) Financing seasonal needs with short-term funds
  - (d) Financing some long-term needs with short-term funds
64. Which asset-liability combination would most likely result in the firm's having the greatest risk of technical insolvency?
- (a) Increasing current assets while lowering current liabilities
  - (b) Increasing current assets while incurring more current liabilities
  - (c) Reducing current assets, increasing current liabilities, and reducing long-term debt
  - (d) Replacing short-term debt with equity
65. Which of the following illustrates the use of a hedging (or matching) approach to financing?
- (a) Short-term assets financed with long-term liabilities
  - (b) Permanent working capital financed with long-term liabilities
  - (c) Short-term assets financed with equity
  - (d) All assets financed with a 50 percent equity, 50 percent long-term debt mixture
66. In deciding the appropriate level of current assets for the firm, management is confronted with
- (a) a trade-off between profitability and risk
  - (b) a trade-off between liquidity and marketability
  - (c) a trade-off between equity and debt
  - (d) a trade-off between short-term versus long-term borrowing
67. Spontaneous financing includes
- (a) accounts receivable
  - (b) accounts payable
  - (c) short-term loans
  - (d) a line of credit
68. Financing a long-lived asset with short-term financing would be
- (a) an example of "moderate risk -- moderate (potential) profitability" asset financing
  - (b) an example of "low risk -- low (potential) profitability" asset financing
  - (c) an example of "high risk -- high (potential) profitability" asset financing
  - (d) an example of the "hedging approach" to financing
69. Net working capital refers to
- (a) total assets minus fixed assets

- (b) current assets minus current liabilities
- (c) current assets minus inventories
- (d) current assets

70. Permanent working capital

- (a) varies with seasonal needs
- (b) includes fixed assets
- (c) is the amount of current assets required to meet a firm's long-term minimum needs
- (d) includes accounts payable

### Answers

1. (c), 2. (d), 3. (b), 4. (a), 5. (c), 6. (b), 7. (a), 8. (b), 9. (a), 10. (c), 11. (d), 12. (d), 13. (b), 14. (b), 15. (a), 16. (b), 17. (d), 18. (d), 19. (a), 20. (b), 21. (c), 22. (a), 23. (a), 24. (b), 25. (b), 26. (d), 27. (d) 28. (a), 29. (a), 30. (c), 31. (d), 32. (b), 33. (d), 34. (b), 35. (c), 36. (a), 37. (d), 38. (b), 39. (b), 40. (a), 41. (b), 42. (d), 43. (a), 44. (c), 45. (a), 46. (d), 47. (b), 48. (c), 49. (c), 50. (c), (51) (b), (52)(c), (53)(d), (54) (b), (55)(c), (56)(c), (57)(b), (58)(c), (59)(b), (60)(a), (61)(d), (62)(c), (63)(d), (64)(c), (65)(b), (66)(a), (67)(b), (68)(c), (69)(b), (70)(c).

### (b) Short Answer Type Questions:

- 1 Define working capital. Distinguish between permanent and temporary working capital.
- 2 Explain how working capital management policies affect the profitability, liquidity and structural health.
- 3 Explain Gross and Net concepts of Working Capital.
- 4 Define Trade Discount and Cash Discount.
5. Write a note on Turnover ratios and their use in Working Capital Management.
- 6 Explain the concept of Level-setting in Inventory Control.
- 7 Briefly explain ABC Analysis for inventory control.
- 8 Enumerate the various Cash Management Models. 9 Write a short note on the concept of Credit Policy. 10 Graphically explain Economic Order Quantity.
- 11 Write short note on Miller-Orr Model.
- 12 Explain Lock-Box System.
- 13 Write a note on Concentration Banking.
- 14 Briefly explain working capital term loan.
- 15 Explain the concept of working capital cycle. 16 Write notes on different kinds of float.
- 17 Explain Walter's Approach to dividend policy

- 18 Write short note on Gordon's dividend policy. 19 State the assumptions of MM approach.
- 20 Write the shortcomings of Walter's Model.
21. Write short note on over- trading and under- trading.
22. Write short notes on Concept of value of the firm.
23. Elaborate the impacts of inadequate working capital.
24. Provide the Basic assumptions of Miller-Orr model.
25. List down the assumptions of Lintner model.

### III Long Answer Type Question:

- 1 What is working capital management? Bring out the role of various constituents of working capital.
- 2 What is meant by working capital management? What are the determinants of working capital needs of an enterprise?
- 3 Explain the concept of Hard Core Working Capital. How should it be determined and financed?
- 4 "Efficiency inventory management is reflected in the liquidity and profitability of the firm". Explain.
- 5 What do you understand by management of working capital and what are the constraints in the management of working capital?
- 6 (a) Define working capital. Distinguish between permanent and temporary working capital.  
(b) Explain how working capital management policies affect the profitability, liquidity and structural health.
- 7 What are the objectives of a credit policy? What is an optimum credit policy? Discuss.
- 8 Explain the importance of working capital in attaining the profit objective of an organization. Explain how working capital needs are assessed.
- 9 What is meant by working capital? What are the techniques used for analysis working capital of the company? Explain by giving suitable examples.
- 10 Explain various determinants of working capital of a concern.
- 11 How are the objectives of inventory management and cash management similar?
- 12 The major objective of inventory management is to minimize cash outlays for inventories. Explain how this is sought to be achieved.
- 13 Explain the importance of proper planning and control of working capital in a large manufacturing concern and the techniques that are used for planning and control of working capital.
- 14 What factors determine the size of the investment a company makes in accounts receivables? Which of these factors are under the control of the Finance Manager?

- 15 Explain briefly costs and benefits of inventory and some techniques of inventory control.
- 16 Show the important role which receivables play in the total financial picture and how you would control them?
- 17 What is meant by 'Operating Cycle Concept' in management of working capital?
- 18 Working capital is the life blood of a business firm and there is always an operating cycle involved in the cash to cash cycle. Draw up an operating cycle for industry. List out the individual components of the cycle and illustrate with example the computation of the operating cycle components and determination of the total cycle time.
- 19 The average age of receivable is an important yard stick of testing the efficiency of receivables management of a firm. Discuss.
- 20 Discuss the risk-return considerations in financing of current assets. Discuss the risk-return considerations in financing of current assets.
- 21 Determine the operating cycle time of a manufactured product you are familiar with to enable the forecasting of working capital requirements fairly, quickly and accurately.
- 22 How do you go about projecting the short-term financial requirements of a business firm?
- 23 Bring out the various methods through which working capital requirements be reasonably forecasted.
- 24 How would you assess the working capital requirements for a seasonal industry? Illustrate with an example.
- 25 (a) What do you understand by 'Working Capital Leverage'?
- (b) What are the aggressive and conservative current asset financing policies? State your preference with reasons.
- 26 What is conservative approach to working capital financing? 27 Explain the principal motives for holding cash.
- 28 Explain the Baumol's model of cash management.
- 29 Explain the concept of Hard Core Working Capital. How should it be determined and financed?
- 30 What key variables should be considered when evaluating possible changes in the firm's credit policy? Briefly explain the possible effects of a more restrictive credit policy on: (i) sales volume, (ii) average collection period, (iii) investment in receivables, (iv) cost of receivables investment, (v) bad debt costs.
- 31 Contrast aging accounts receivable with the accounts receivable turnover or average collection period. Are they perfect substitutes for each other? Explain.
- 32 What is the general objective of accounts receivable management? In what ways is it similar and different from cash balance management and inventory management?
- 33 Discuss the risk-return relationship involved in the firm's investment decisions as it pertains to working capital management.
- 34 Explain the Aging Schedule in the context of monitoring receivables.
- 35 In a world of no taxes and no transaction costs, a firm cannot be made more valuable by manipulating the dividend payout ratio. Examine the validity of this statement.

- 36 What are the assumptions and arguments used by Modigliani and Miller in support of the irrelevance of dividends? Are dividends really irrelevant? If not, what are the arguments for relevance of dividend policy?
- 37 What is 'informational content' of dividend payments? Explain. 38 Explain and illustrate the framework of a factoring deal.
- 39 Discuss the main forms of working capital advance by banks. What kind of security is required by them?
- 40 Discuss briefly commercial papers as a source of finance
- 41 What is factoring? Give a brief account of the major function of factor
- 42 Explain Lintner model of dividend
- 43 Explain the various reasons behind holding of cash by the companies although idle cash earns no return.
- 44 What are the essentials of Walter's dividend model? Explain its shortcomings.
- 45 What are the assumptions which underlie Gordon's model of dividend effect? Does dividend policy affect the value of the firm under Gordon's model?
- 46 "Walter's and Gordon's models are essentially based on the same assumptions. Thus, there is no basic difference between the two models." Do you agree or not? Why?
- 47 "The contention that dividends have an impact on the share price has been characterized as the bird-in-the-hand argument." Explain the essential of this argument. Why this argument is considered fallacious?
- 48 "The primary purpose for which a firm exists is the payment of dividend. Therefore, irrespective of the firm's needs and the desires of shareholders, a firm should follow a policy of very high dividend payout! Do you agree? Why or why not?
- 49 What is the importance of working capital for a manufacturing firm? What shall be the repercussions if a firm has (a) paucity of working capital, (b) excess working capital?
- 50 Illustrate the profitability-solvency tangle in the current assets holding.
- 51 What benefits and costs are associated with the extension of credit? How should they be combined to obtain an appropriate credit policy?
- 52 "The credit policy of a company is criticized because the bad debt losses have increased considerably and the collection period has also increased." Discuss under what conditions this criticism may not be justified.
- 53 "There are two dangerous situations that management should usually avoid in controlling inventories." Identify the danger points and explain.
- 54 What are the objectives of a firm in controlling its disbursements? How can the disbursements be slowed down?
- 55 Length of operating cycle is the major determinant of the working capital needs of the firm. Comment.
- 56 Explain the relationship between net working capital, technical solvency and risk.
57. Explain briefly the meaning of sensitivity analysis.

58. Explain the arbitrage process used by the Modigliani-Miller hypothesis.
59. “The assumptions underlying the irrelevance hypothesis of Modigliani-Miller are unrealistic.
60. Dividend policy affects the value of the firm under Gordon’s Model. Explain.
61. Explain with suitable example the arbitrage process of MM approach to achieve the equilibrium level.
62. What is financial distress? Examine the effects of financial distress on the value of the firm.
63. What is meant by Working capital? How is it calculated? Explain the determinants of working capital requirements.
64. What is Long-term Cash Forecasting? Also state its uses.
65. Explain the cost trade-off theory of working capital.
66. State the reasons that make working capital management as an important function of the financial manager.
67. Explain the current assets holding period method of estimating working capital.

#### IV Practical Question:

- 1 Calculate the Economic Order Quantity from the following information. Also state the number of orders to be placed in a year.

Consumption of materials per annum	10,000	kg.
Order placing costs per order	Rs. 50	
Cost per kg.of raw materials	Rs. 2	
Storage costs	8% on average inventory.	

**Ans. EOQ = 2,500 kg; No. of Orders 4**

- 2 A company predicts that 3,000 units of a certain material will be needed next year. Each unit costs Rs. 6. Past experience indicates that the storage costs are approximately equal to 10 percent of the inventory investment. The cost to place on order amounts to Rs. 9. Determine the economic order quantity so as to enable the company to balance its ordering and storage costs. How many orders will the company place in a year based upon EOQ?

**Ans. EOQ 300 units**

- 3 A firm is able to obtain quantity discounts on its orders of material as follows:

Price per tonne (Rs.)	Tonnes
Less than 250	
250 and less than 800	
800 and less than 2,000	
2,000 and less than 4,000	
4,000 and over	

The annual demand for the material is 4,000 tonnes. Stock holding costs are 20% of material cost per annum. The delivery cost per order is Rs. 6.00. You are required to calculate the best quantity to order.

**Ans. 4,000 units, if delivery can be staggered in lots of 207 tonnes. If delivery cannot be staggered EOQ is 800 units where total cost is the least i.e. Rs. 23,694**

4 Calculate the material turnover ratio for the year 2008 from the following details:

<i>Particulars</i>	<i>Material X</i>	<i>Material Y</i>
Opening Stock	Rs. 25,000	Rs. 87,500
Closing Stock	15,000	62,500
Purchases	1,90,000	1,25,000

Determine the fast moving material.

**Ans. X: 10, Y:2, X is fast moving**

5 A customer has been ordering 5,000 units at the rate of 1,000 units per order during 2008. The production cost is Rs. 12 per unit – Rs. 8 for materials and labour and Rs. 4 overhead cost. It costs Rs. 1,500 to set up for one run of 1,000 units. The inventory carrying cost is 20% of the production cost. The customer is expected to buy at least 5,000 units in 2009. The company wants to avoid making five different production runs. You are required to determine the most economic production run. **Ans. 2,500 units**

6 (a) The following details are available in respect of a firm:

- (i) Annual requirement of inventory 40,000 units
- (ii) Cost per unit (other than carrying and ordering cost) Rs. 16
- (iii) Carrying costs are likely to be 15% per year
- (iv) Cost of placing order Rs. 480 per order

Determine the economic ordering quantity.

**Ans. 4,000 units**

7 A firm has 5 different levels in its inventory. The relevant details are given. Suggest a breakdown of the items into A, B and C classifications:

<i>Item No.</i>	<i>Avg. No. of units inventory</i>	<i>Avg. Cost per unit</i>
1	20,000	Rs. 60

2	10,000	Rs. 100
3	32,000	Rs. 11
4	28,000	Rs. 10
5	60,000	Rs. 3.40

Ans.	Category	Items	% Number of Items	% Value
	A	1	20%	72
		2		
	B	3	40%	21
		4		
	C	5	40%	7

- 8 The present credit terms of P company are 1/10 net 30. Its annual sales are Rs. 80 lakhs. Its average collection period is 20 days. Its variable costs and average total costs to sales are 0.85 and 0.95 respectively and its cost of capital is 10 percent. The proportion of sales on which customers currently take discount is 0.5. P company is considering relaxing its discount terms to 2/10 net 30. Such relaxation is expected to increase sales by Rs. 5 lakhs, reduce the average collection period to 14 days and increase the proportion of discount sales to 0.8. What will be the effect of relaxing the discount policy on company's profit? Take year as of 360 days.

**Ans. Net decrease in profit Rs. 9,986 (i.e. Rs. 96,000 – Rs. 86,014). It is not advisable to relax the present discount policy**

- 9 ABC Ltd. is presently selling a product @ Rs. 10 per unit. The present sales are 30,000 units, and the variable cost per unit is Rs. 6 and the fixed costs amount to Rs. 60,000. The average collection period is of 30 days.

The company proposes to relax its credit standard resulting in a 15 percent increase in unit sales. The average collection period is expected to increase to 45 days. However, there is to be no change in losses on account of bad debts and collection expenses. The company expects a return on investment at 15%.

You are required to advise whether the company should relax its credit standard.

**Ans.**

**Increased profit on account of relaxation**

**In credit standard**

**Rs. 18,000**

**Increase investment in accounts receivables**

**Rs. 13,375**

**Cost of increased investment in receivables**

**Rs. 2,006.25**



**It would be profitable for the company to relax the credit standards**

10 The current credit terms of Mayur Ltd. are “net 30”. It is considering to change them to “3/15, net 45” credit terms in order to increase its sales. The proposed change is expected to have the following implications:

Current Sales	Rs. 50,00,000
Estimated total sales that will avail discount offer 10% increased investment in receivables	Rs. 15,00,000
Estimated increased costs:	
Bad debt losses	1% of increased sales
Production, administration and selling costs	74% of increased sales
Required return on investment	10%
Cash Discount	3% of sales

You are required to state whether it is desirable to introduce the change in credit terms.

**Ans. Increase in profit on account of increase in sales Rs. 50,400**  
**Opportunity cost of increased investment in receivables Rs. 29,600**  
**Credit standards may be relaxed**

11 STS Ltd. which sells on credit basis has ranked its customers in categories 1 to 5 in order of credit risk:

<i>Category</i>	<i>Percentage bad debts</i>	<i>Average Collection period</i>
1	0.0 30 days	
2	1.0 45 days	
3	2.0 60 days	
4	5.0 90 days	
5	10.0 120 days	

The company’s current credit policy is to allow unlimited credit to firms in categories 1 to 3, limited credit to firms in category 4 and no additional credit to firms in category 5.

As a result, orders amounting to Rs. 25,00,000 from category 4 and Rs. 75,00,000 from category 5 customers are rejected every year. If the STS Ltd. marks a 10 percent gross profit on sales and has an opportunity cost on investment in receivables of 12 percent, what would be the effect on profits of allowing full credit to all categories of customers? Should credit be extended to all categories of customers?

**Ans. Profit (loss) on extending credit: Category 4: Rs. 0.50 lakh, Category 5: (Rs. 3 lakhs)**

- 12 A group of customers want to enter into a contract with you to buy goods worth Rs. 20 lakhs during 1997, the deliveries to be made in four equal installments quarterly. The price of the commodity is Rs. 20 per unit on which you expect a profit of Rs. 10. The acceptance of this proposal would mean an additional recurring expenditure of Rs. 10,000 p.a. on your part. The aging schedule of accounts receivables in respect of this group of customers in the past was also as follows:

<i>Period</i>	<i>Percentage of bills for which payment received</i>
At the end of 30 days	15%
At the end of 60 days	25%
At the end of 90 days	40%
At the end of 100 days	20%

Assuming an opportunity cost of 20% of the funds locked up in accounts receivable, will it be desirable to accept this proposal?

**Ans. Opportunity cost of funds, Rs. 82,740, Expected return from sales – Rs. 9,90,000. Net return Rs. 9,07,260, The proposal should be accepted**

- 13 A firm has a current sales of Rs. 2,56,48,750. The firm has unutilized capacity. In order to boost its sales, it is considering the relaxation in its credit policy. The proposed terms of credit will be 60 days credit against the present policy of 45 days. As a result, the bad debts will increase from 1.5% to 2% of sales. The firm's sales are expected to increase by 10%. The variable operating costs are 72% of the sales. The Firm's Corporate Tax rate is 35%, and it requires an after-tax return of 15% on its investment. Should the firm change its credit period?

**Ans. Bad debt losses 1,79,542, Operating Profit Rs. 3,50,105, Increased investment in Receivables Rs. 14,961,777, Return 234%, The new credit policy may be accepted**

- 14 The Asbestos Company belongs to a risk class of which the appropriate capitalization rate is 10%. It currently has 1,00,000 shares selling at Rs. 100 each. The firm is contemplating the declaration of a Rs. 6 dividend at the end of the current fiscal year, which has just begun. Answer the following questions based on the Modigliani and Miller Model and the assumption of no taxes:

- What will be the price of the shares at the end of the year, if a dividend is not declared? What will it be if it is declared?
- Assuming that the firm pays dividend, has net income of Rs. 10,00,000 and makes new investments of Rs. 20,00,000 during the period, how many new shares must be issued?

(c) Is MM Model realistic with respect to valuation? What factors might mar its validity?

**Ans. (a) (i) Rs. 104, (ii) Rs. 110, (b) 15,385 shares, (c) MM Model is unrealistic**

15 Following are the details regarding three companies:

<b>A Ltd.</b>	<b>B Ltd.</b>	<b>C Ltd.</b>
$r = 15\%$	$r = 10\%$	$r = 8\%$
$k = 10\%$	$k = 10\%$	$k = 10\%$
$E = \text{Rs. } 10$	$E = \text{Rs. } 10$	$E = \text{Rs. } 10$

You are required to calculate the effect of dividend payment on the profits of each of the above companies under the following different situations:

When no dividend is paid;

When dividend is paid at Rs. 4 per share;

When dividend is paid at Rs. 8 per share; When dividend is paid at Rs. 10 per share.

**Ans.**

**A Ltd. : (a) Rs. 150 (b) Rs. 130; (c) Rs.110 (d) Rs. 100**  
**B Ltd. : (a) Rs. 100 (b) Rs. 100 (c) Rs. 100 (d) Rs. 100**  
**C Ltd. : (a) Rs. 80 (b) Rs. 88 (c) Rs. 96 (d) Rs. 100**

16 X company earns Rs. 5 per share, is capitalized at a rate of 10% and has a rate of return on investment at 18%.

According to Walter's formula, what should be the price per share at 25% dividend pay out ratio? Is this the optimum pay out ratio according to Walter?

**Ans. Rs. 80. This is not the optimum dividend pay out ratio, since Walter suggests a zero per cent dividend pay out ratio in situations where  $r > k$ .**

17 (a) The Apex Company' which earns Rs. 5 per share, is capitalized at 10% and has a return on investment of 12%. Using Walter's dividend policy model, determine (i) the optimum pay our, and (ii) the price of share at this pay out.

(b) The Agro-Chemicals Company belongs to a risk class for which the appropriate capitalization is 10%. It currently has 1,00,000 shares selling at Rs. 100 each. The firm is contemplating the declaration of Rs. 5 as dividend at the end of the current financial year, which has just begun. What will be the price of the share at the end of the year, if a dividend is not

declared? What will it be if one is declared? Answer these on the basis of Modigliani and Miller model and assume no taxes. **Ans. (a) (i) Zero per cent; (ii) Rs. 60; (b) (i) Rs. 135, (ii) Rs. 110**

18 The earning per share of a company is Rs. 16. The market capitalization rate applicable to the company is 12.5%. Retained earnings can be employed to yield a return of 10%. The company is considering a pay out of (a) 25%, (b) 50% and (c) 75%. Which of these would maximize the wealth of shareholders as per Walter's model? **Ans. (a) Rs. 108.80, (b) Rs. 115.20, (c) Rs. 121.60**

19 Details regarding three companies are given below:

A Ltd. B Ltd. C Ltd.  $r = 15\%$   $r = 10\%$   $r = 8\%$   $k_e = 10\%$

$k_e = 10\%$   $k_e = 10\%$

E = Rs. 10

E = RS. 10

E = Rs. 10

By using Walter's Model, you are required to

Calculate the value of an equity share of each of these companies when dividend pay out ratio is (a) 20%, (b) 50%, (c) 0% and (d) 100%.

Comment on the result drawn.

**Ans. (i) Value of an equity share:**

	<i>A Ltd.</i>	<i>B Ltd.</i>	<i>C Ltd.</i>	(a)	Rs. 140	Rs. 100
	Rs. 84					
(b)	Rs. 125	Rs. 100		Rs. 90		
(c)	Rs. 150	Rs. 100		Rs. 80		
(d)	Rs. 100	Rs. 100		Rs. 100		

**(ii) Company A is a growth firm, Company B is a normal firm and Company C is a declining firm.**

20 From the following details calculate the value of a right:

Existing paid-up share capital 10,000

Rs. 100 each

Additional funds to be raised

Rs. 200

Subscription price for the right issue per share

Rs. 3,00,000

The right issue is to be made in proportion of one new share for every four shares held.

**Ans. Rs. 10**

21 The following information is available in respect of a firm :

Capitalisation rate = 0.10, Earnings per share = Rs. 10

Assumed rate of return on investment (a) 14% (b) 8% (c) 10%.

Show the effect of dividend policy on market price of share assuming pay out ratio (a) 0% (b) 25% (c) 50% (d) 75% and (e) 100% using Walter Model

- 22 XYZ firm cash flows deviate randomly. If transfer cost is Rs. 1000 and variance of daily cash flows is Rs. 6,000 and cost of holding cash is 20% and if lower cash balance is Rs. 5,000 then compute :-

(a) target cash balance (b) upper cash balance

Using Miller-Orr model for optimum cash balance under uncertainty.

- 23 The following information is available in respect of a firm: Capitalisation rate = 0.12, EPS = Rs. 15

Assumed rate of return on investment (a) 15% (b) 8% (c) 10%

Show the effect of dividend policy on market price of share assuming pay out ratio (a) 0% (b) 25% (c) 50% (d) 75% and (e) 100% using Walter Model

- 24 ABC Co's stock recently paid a Rs. 2 dividend. This dividend is expected to grow by 25% for the next 3 years and then grow forever at a constant rate. The current stock price is Rs. 58.88. At what constant rate is the stock expected to grow if required return is 12%?

**Ans: Stock is expected to grow @ 6.27% p.a for indefinite period.**

- 25 Accurate Ltd. has planned to sell 6,00,000 units of output in the coming year. The cost structure of the company's product for the desired level of production is given below:

	Cost per units (Rs.)
Raw material	30
Manufacturing expenses	10
Other overheads	25
Total cost	65
Selling price	80
Profit	15

Examination of past trend reveals:

(a) Raw materials are held in stock for 1 month.

(b) Work-in-progress inventory is equal to half month's production. (c) Finish goods remain in the warehouse for a month.

(d) Three month's credit is allowed to the debtors.

(e) Manufacturing expenses are expected to occur evenly during the year.

You are required to –

- (i) Calculate the investment in various current assets.  
(ii) Estimate the gross working capital requirement if the desired cash balance is 5% of gross working capital.

**Ans: Gross Working Capital 165,13,157.89**

- 26 A company has total investment of Rs. 5,00,000 in asset and Rs. 50,000 outstanding ordinary shares at Rs. 10 per share (par value). It earns a rate of 15% on its investment and has a policy of retaining 50% of the earnings. If the appropriate discount rate of the firm is 10%, determine the price of its share using Gordon model. What will happen to the price of the share if the company has payout of 80% or 20%.

**Ans. Payout: 50%, Price – Rs. 30, Payout: 80%, Price – Rs. 17, Payout : 20%, Price: -15**

- 27 Demand for a certain product is random. It is estimated that the monthly demand of the product has a normal distribution with a mean of 390 units. The unit price of the product is Rs. 25. The ordering cost is Rs. 40 per order and the carrying cost is 35% per year. Calculate EOQ.

**Ans. EOQ = 207 units**

- 28 A Ltd. has the total sales of Rs. 3.20 crores and its average collection period is 90 days. The past experience indicates that bad debt losses are 1.5% on sales. Expenditure incurred by firm to administer its receivable collection is Rs. 5,00,000. A factor is prepared to buy the firm's receivables by charging 2% commission. The factor will pay advance on receivables to the firm at an interest rate of 18% p.a. after withholding 10% as reserves. Calculate the effective cost of factoring to the firm.

- 29 Annual cash requirement of A Ltd. is Rs. 10,00,000. The company has marketable securities in the lot sizes of Rs. 50,000, Rs. 1,00,000, Rs. 2,00,000, Rs. 2,50,000 and Rs. 5,00,000. Cost of conversion of marketable securities per lot is Rs. 1,000. The company can earn 5% annual yield on its securities. Prepare a table to indicate which lot size will have to be sold by the company. Also, show that the economic lot size can be obtained by the Baumol model. **Ans. Rs. 2,00,000**

- 30 Current assets and current liabilities of Rhythm Steels Ltd. are Rs. 36 lakhs and Rs. 26 lakhs respectively. If the company purchased raw material worth Rs. 2,00,000 on credit, took a long term loan of Rs. 25 lakh from a bank and purchased capital equipment and converted preferential shares (face value = Rs. 7 lakhs) into equity, what would be the new net working capital.

- 31 Jai Electricals Ltd. needs 60,000 pieces of aluminum bars to produce switchgears. The price of each bar is Rs. 100, cost of placing an order is Rs. 1,200 and the carrying cost is

1%. The economic order quantity based on the EOQ model is 12,000 units. Recently, a supplier has offered discounts of 3% against an order size of 20,000 units or more. What will be the incremental benefit to the company, if such discount is availed.

32. Eagle Tyres Ltd. is an existing tyre and tube manufacturing company proposing to expand its operations and increase its manufacturing capacity. Details of the working capital requirements of the company for the first year of operations after expansion are as follows:

Items	Rs. In lakhs
Raw materials	480
Sundry creditors	600
Receivables	686
Finished goods	236
Consumables	24
Work-in-progress	65
Other current assets (leaving cash)	100

The margin money requirement is 25% of the working capital gap. Existing margin money and bank finance for working capital requirement amount to Rs. 223 lakhs and Rs. 660 lakhs respectively. Determine the existing working capital with the company prior to the expansion and the increase in working capital required given that the company's existing creditors were worth Rs. 75 lakhs.

33. The earnings per share of a company are Rs. 10. It has rate of return of 15% and the capitalization rate of risk class is 12.5%. If Walter's Model is used : (i) What should be the optimum payout ratio of the firm? (ii) What would be the price of the share at this payout? (iii) How shall the price of the share be affected if a different payout was employed?

**Ans. As  $r > k_e$ , the optimal payout ratio is zero. The price of the share would be Rs. 96.**

34. Consider the following information regarding ABC Industries Ltd.

Earnings of a company	Rs.12,00,000
Dividend paid	Rs.6,00,000
No. Of shares outstanding	1,20,000
P/E Ratio	8
Return on Investment	15%

Using Walter's model, by how much amount should the price of the company shares increase so that it is maximized? What is the optimal dividend – payout ratio for ABC Industries Ltd.?

**Ans. the price of the company's share should be increased by Rs. 8 (96-88)**

35. Calculate the market price of a share of ABC Ltd. under Walter's Model and dividend growth model from the following data:  
EPS Rs. 5  
DPS Rs. 3  
Cost of capital 16%  
Internal rate of return on investment 20%  
Retention ratio 40%  
**Ans. (i) Rs. 34.38 (ii) Rs. 37.50**
36. XYZ Ltd. has a standard deviation of monthly net cash flows of Rs. 200. It's transaction cost of converting cash into marketable securities is Rs. 10 and the interest is 1% per month (12% p.a.). The minimum cash balance required by the firm is Rs. 100. Set out the upper, lower and return limit of cash flow the firm. Also find out the average cash balance. Apply Miller-Orr Model.  
**Ans. Average cash balance = Rs. 515**
37. The annual cash requirement of A Ltd. is Rs. 10 lakhs. The company has marketable securities in lot sizes of Rs. 50,000, Rs. 1,00,000, Rs. 2,00,000 Rs. 2,50,000 and Rs. 5,00,000. Cost of conversion of marketable securities per lot is Rs. 1000. The company can earn 5% annual yield on its securities. You are required to prepare a table indicating which lot size will have to be sold by the company. Also show the economic lot size which can be obtained by Baumol Model.  
**Ans. Economic lot size = 2,00,000**



# **QUESTION BANK**

## **MARKETING MANGEMENT**

### **– MS 106**

  

## **MBA II**

### **QUESTION BANK**

#### **MARKETING MANGEMENT – MS 106**

#### **MBA II**

#### **UNIT - I**

#### **(a) Multiple Choice Questions:**

- 1 The most formal definition of marketing is \_\_\_\_\_. (a) Meeting needs profitably  
(b) Identifying and meeting human and social needs  
(c) The four Ps (product, price, place, promotion)  
(d) An organizational function and a set of processes for creating, communicating, and delivering value to customers and for managing customer relationships in ways that benefit the organization and its stakeholders  
(e) Improving the quality of life for consumers

- 2 \_\_\_\_\_ takes place when at least one party to a `potential exchange thinks about the means of achieving desired responses from other parties.
- (a) Marketing management
  - (b) Forecasting
  - (c) Segmentation
  - (d) Targeting
  - (e) Distribution
- 3 Marketing management is \_\_\_\_\_.
- (a) Managing the marketing process
  - (b) Monitoring the profitability of the company's products and services
  - (c) Selecting target markets
  - (d) Developing marketing strategies to move the company forward
  - (e) The art and science of choosing target markets and getting, keeping, and growing customers through creating, delivering, and communicating superior customer value
- 4 The \_is a tool for identifying ways to create more customer value.
- (a) Value chain
  - (b) Customer survey
  - (c) Brand loyalty index
  - (d) Promotion channel
  - (e) Supplier database
- 5 The \_\_\_\_\_ household consists of a husband, wife, and children (and sometimes grandparents).
- (a) "Traditional"
  - (b) "Extended"
  - (c) "Diversity"
  - (d) "Modern"
  - (e) "Revised"
- 6 Consumer expenditures are affected by \_\_\_\_\_.
- (a) Savings
  - (b) Debt
  - (c) Credit availability
  - (d) All of the above
  - (e) None of the above

- 7 Michael Porter has identified five forces that determine the intrinsic long-run attractiveness of a market or market segment. Which of the following would NOT be among Porter's five forces?
- (a) Industry competitors
  - (b) Technological partners
  - (c) Substitutes
  - (d) Buyers
  - (e) Potential entrants
- 8 Which of the following would be the best illustration of a subculture?
- (a) A religion
  - (b) A group of close friends
  - (c) Your university
  - (d) A fraternity or sorority
  - (e) Your occupation
- 9 In \_\_\_\_\_ marketing, the seller engages in the mass production, mass distribution, and mass promotion of one product for all buyers.
- (a) Group
  - (b) Mass
  - (c) General
  - (d) Segmented
  - (e) Differentiated
- 10 A housewife requests a new treadmill for her birthday. With respect to consumer decision roles, which role is the housewife currently playing?
- (a) Initiator
  - (b) Influencer
  - (c) Decider
  - (d) Buyer
  - (e) Gatekeeper
11. The marketing mix consists of; -
- (a) Product, physical evidence, place, process
  - (b) Process, price, place, packaging
  - (c) People, process, place, promotion
  - (d) Product, place, promotion, place
12. Increasing the features and quality you offer is a decision made by which marketing mix? (a) Product

- (b) Price
  - (c) Promotion
  - (d) Place
13. Design is a \_\_\_\_\_ decision
- (a) Product
  - (b) Price
  - (c) Promotion
  - (d) Place
14. Giving retailer an incentive to sell your product/service is the responsibility of which marketing mix?
- (a) Product
  - (b) Price
  - (c) Promotion
  - (d) Place
15. Public Relations is managed by which marketing mix?
- (a) Product
  - (b) Price
  - (c) Promotion
  - (d) Place
16. Branding is a \_\_\_\_\_ decision
- (a) Product
  - (b) Price
  - (c) Promotion
  - (d) Place
17. Which one of the 4Ps is responsible for direct mail?
- (a) Product
  - (b) Price
  - (c) Promotion
  - (d) Place
18. The term "marketing mix" describes:
- (a) A composite analysis of all environmental factors inside and outside the firm
  - (b) A series of business decisions that aid in selling a product
  - (c) The relationship between a firm's marketing strengths and its business weaknesses
  - (d) A blending of four strategic elements to satisfy specific target markets

19. Newsletters, catalogues, and invitations to organization-sponsored events are most closely associated with the marketing mix activity of:
- (a) Pricing
  - (b) Distribution
  - (c) Product development
  - (d) Promotion
20. The way in which the product is delivered to meet the customer's need refers to: - (a) New product concepts
- (b) Selling
  - (c) Advertising
  - (d) Place or distribution decisions
21. Which of the following environments examines institutions and other forces that affect society's basic values, perceptions, preferences, and behaviors?
- (a) Cultural
  - (b) Demographic
  - (c) Economic
  - (d) Technological
  - (e)
22. Which of the following is NOT part of the external marketing environment?
- (a) Political
  - (b) Legal
  - (c) Product
  - (d) Socio-cultural
23. A firm has decided to alter its pricing and promotional strategies in response to slower than expected job growth and declining personal incomes. The firm is responding to changes in its:
- (a) Socio-cultural environment
  - (b) Political environment
  - (c) Economic environment
  - (d) Competitive environment
24. Robert is a marketer for a global consumer products company. He is working on the promotional campaign designed to reach a target audience in a new international market. Robert is working hard to make sure that the promotional campaign is clearly understood by the nation's consumers and doesn't offend anyone. Which of the factors in the external environment is he being influenced by?

- (a) Socio-cultural environment
  - (b) Competitive environment
  - (c) Economic environment
  - (d) Legal environment
25. The process of collecting information about the external marketing environment is
- (a) Environmental management
  - (b) Environmental scanning
  - (c) Marketing management
  - (d) Marketing research
26. Consumer behavior is a term that refers to
- (a) Organizational and institutional buying behavior
  - (b) Organizational and consumer buying behavior
  - (c) Commercial and government buying behavior
  - (d) Individual and/or household buying behavior
27. Which of the following is NOT an example of consumer behavior:
- (a) Claire buying a new car
  - (b) Ashley buying a new home theatre/cinema system
  - (c) Sarah deciding on a college or university to attend
  - (d) Marcus ordering a new computer system for his work
28. Which of the following is NOT an internal factor that influences the consumer product acquisition process include
- (a) Learning
  - (b) Family
  - (c) Self-concept
  - (d) Perceptions
29. With respect to consumer behavior, one's friends, and relatives could be considered a:
- (a) Impersonal influence
  - (b) Reference group influence
  - (c) Perceptual influence
  - (d) Institutional influences
30. With respect to consumer behavior, the function of one's perceptions, learning and memory processes is to:
- (a) Attend to messages
  - (b) Filter messages

- (c) Store messages
  - (d) All of the above
31. \_\_\_\_\_ is one of the most basic influences on an individual's needs, wants, and behavior. (a) Brand
- (b) Culture
  - (c) Product
  - (d) Price
32. In terms of consumer behavior; culture, social class, and reference group influences have been related to purchase and \_\_\_\_\_.
- (a) Economic situations
  - (b) Situational influences
  - (c) Consumption decisions
  - (d) Physiological influences
33. Marketing managers should adapt the marketing mix to \_\_\_\_\_ and constantly monitor value changes and differences in both domestic and global markets.
- (a) Sales strategies
  - (b) Marketing concepts
  - (c) Cultural values
  - (d) Brand images
34. \_\_\_\_\_ has become increasingly important for developing a marketing strategy in recent years.
- (a) Change in consumers' attitudes
  - (b) Inflation of the dollar
  - (c) The concept and the brand
  - (d) Age groups, such as the teen market, baby boomers, and the mature market
35. Two of the most important psychological factors that impact consumer decision-making process are product and product involvement.
- (a) Marketing
  - (b) Strategy
  - (c) Price
  - (d) Knowledge
36. \_\_\_\_\_ are factors that have been shown to affect consumer behavior.
- (a) Brand name, quality, newness, and complexity
  - (b) Advertising, marketing, product, and price

- (c) Outlets, strategies, concept, and brand name
  - (d) Quality, advertising, product positioning, and strategy
37. Marketing strategies are often designed to influence \_\_\_\_\_ and lead to profitable exchanges.
- (a) Consumer decision making
  - (b) Sales strategies
  - (c) Advertising strategies
  - (d) Export strategies
38. One of the key tasks of marketers is \_\_\_\_\_ and to create consumer perceptions that the product is worth purchasing.
- (a) To make products easily visible and available
  - (b) To promote sales of products
  - (c) To differentiate their products from those of competitors
  - (d) To do marketing surveys
39. Marketing communications play a critical role in informing consumers about \_\_\_\_\_ including where they can be purchased and in creating favorable images and perceptions.
- (a) Buying their products
  - (b) Price reductions
  - (c) Products and services
  - (d) The advantage over competition
40. Marketers can create brand equity \_\_\_\_\_.
- (a) By selling them in prestigious outlets
  - (b) By overpricing the product
  - (c) Preparing comparative information about competitive brands
  - (d) By making the products available in all locations
41. The process of selecting the segments to serve by offering product is referred as
- (a) Market segmentation
  - (b) Targeting
  - (c) Marketing
  - (d) Both a and b
42. Firm's performance can be better measured by
- (a) Current sales
  - (b) Customer equity
  - (c) Market share
  - (d) Both a and b



43. The particular communication that must be achieved within definite target audience within specific time is classified as
- (a) message decision
  - (b) media decision
  - (c) advertising objective
  - (d) advertising evaluation
44. The customer classification depends on
- (a) Potential profitability
  - (b) Projected loyalty
  - (c) Both a and b
  - (d) None of above
45. The potential profitable but less loyal group is of
- (a) Butterflies
  - (b) Strangers
  - (c) True friends
  - (d) Barnacles
46. The suitable example of 'The Selling Concept' is
- (a) Insurance or blood donations
  - (b) Lenovo
  - (c) Southwest Airlines
  - (d) Bottled water industry
47. In 'Butterflies' group, the customer needs and company's market offering has
- (a) Good fit
  - (b) Little fit
  - (c) Strong fit
  - (d) Limited fit
48. The company's future value of customer base is
- (a) Share of customer
  - (b) Customer equity
  - (c) Customer lifetime value
  - (d) All of above
49. The 'outside in' perspective is another name of
- (a) The selling concept

- (b) The product concept
  - (c) The marketing concept
  - (d) The production concept
50. Considering individual customers, the purchasing portion of each buyer is called (a)
- Share of customer
  - (b) Customer equity
  - (c) Customer lifetime value
  - (d) None of above
51. A change in an individual's behavior prompted by information and experience refers to which one of the following concept?
- (a) Learning
  - (b) Role selection
  - (c) Perception
  - (d) Motivation
52. While buying milk which kind of behaviour is displayed by a person?
- (a) Extensive problem solving behaviour
  - (b) Routinized buying behavior
  - (c) Variety seeking behavior
  - (d) None of the above
53. The promotion “P” of marketing is also known as \_\_\_\_\_.
- (a) Product Differentiation
  - (b) Distribution
  - (c) Cost
  - (d) Marketing Communication
54. When a company distributes its products through a channel structure that includes one or more resellers, this is known as \_\_\_\_\_.
- (a) indirect marketing
  - (b) direct marketing
  - (c) multi-level marketing
  - (d) integrated marketing
56. In marketing theory, every contribution from the supply chain adds \_\_\_\_\_ to the product.
- (a) value
  - (b) costs

- (c) convenience
  - (d) ingredients
57. Which of the following information forms available to the marketing manager can usually be accessed more quickly and cheaply than other information sources?
- (a) Marketing intelligence
  - (b) Marketing research
  - (c) Customer profiles
  - (d) Internal databases
58. All of the following are considered to be drawbacks of local marketing EXCEPT :
- (a) it can drive up manufacturing and marketing costs by reducing economies of scale.
  - (b) it can create logistical problems when the company tries to meet varied requirements.
  - (c) it can attract unwanted competition.
  - (d) it can dilute the brand's overall image.
59. Cognitive dissonance occurs in which stage of the buyer decision process model?
- (a) Need recognition
  - (b) Information search
  - (c) Evaluation of alternatives
  - (d) Post purchase behavior
60. That the company that overlooks new and better ways to do things will eventually lose customers to another company that has found a better way of serving customer needs is a major tenet of:
- (a) innovative marketing.
  - (b) consumer-oriented marketing.
  - (c) value marketing.
  - (d) sense-of-mission marketing.
61. The biggest or greatest amount of involvement in a foreign market comes through which of the following?
- (a) Exporting
  - (b) Joint venturing
  - (c) Licensing
  - (d) Direct investment
62. A is a good offered either free or at low cost as an incentive to buy a product.

- (a) patronage reward
  - (b) spiff
  - (c) price pack
  - (d) premium
63. Setting call objectives is done during which of the following stages of the selling process?
- (a) Prospecting
  - (b) Pre approach
  - (c) Approach
  - (d) Handling objections
64. Pricing to cover variable costs and some fixed costs, as in the case of some automobile distributorships that sell below total costs, is typical of which of the following pricing objectives?
- (a) Current profit maximization
  - (b) Product quality leadership
  - (c) Market share leadership
  - (d) Survival
65. In determining sales force size, when a company groups accounts into different size classes and then determines the number of salespeople needed to call on them the desired number of times, it is called the:
- (a) key-size approach.
  - (b) work-load approach.
  - (c) product-need approach.
  - (d) call-service approach.
66. \_\_\_ is products bought by individuals and organizations for further processing or for use in conducting a business.
- (a) Consumer products
  - (b) Services
  - (c) Industrial products
  - (d) Specialty products
67. \_\_\_ has contractual authority to sell a manufacturer's entire output.
- (a) Selling agents
  - (b) Rack jobbers
  - (c) Manufacturer's agents
  - (d) Purchasing agents

68. Sellers that handle their own exports are engaged in: (a) direct exporting.  
 (b) indirect exporting.  
 (c) licensing.  
 (d) contract manufacturing.
69. More and more salespeople are being evaluated and compensated based on different measures than in the past. All of the following are illustrations of those measures EXCEPT :  
 (a) long-term customer satisfaction.  
 (b) competitive predatory pricing performance.  
 (c) full customer service.  
 (d) d retention rates.
70. includes practices such as overstating the product's features or performance, luring the customer to the store for a bargain that is out of stock, or running rigged contests.  
 (a) Deceptive promotion  
 (b) Deceptive packaging  
 (c) Deceptive pricing  
 (d) Deceptive cost structure

**Ans.** (1)(d), (2)(a), (3)(e), (4)(a), (5)(a), (6)(d), (7)(b), (8)(a), (9)(b), (10)(a), (11)(d), (12)(a), (13)(a), (14)(d), (15)(c), (16)(a), (17)(c), (18)(d), (19)(d), (20)(d), (21)(a), (22)(c), (23)(c), (24)(a), (25)(b), (26)(d), (27)(d), (28)(b), (29)(b), (30)(d), (31)(b), (32)(c), (33)(3), (34)(d), (35)(d), (36)(a), (37)(a), (38)(c), (39)(c), (40)(a), (41)(b), (42)(b), (43)(c), (44)(c), (45)(a), (46)(a), (47)(a), (48)(b), (49)(c), (50)(a), (51)(A), (52)(b), (53)(d), (54)(a), (55)(a), (56)(a), (57)(d), (58)(c), (59)(d), (60)(a), (61)(d), (62)(d), (63)(b), (64)(d), (65)(b), (66)(c), (67)(a), (68)(a), (69)(b), (70)(a)

## **II Short Answer Type Questions:**

**(a) Write short note on the following:**

- 1 Marketing myopia
- 2 Selling concept of marketing 3 Consumer behavior.
- 4 Market testing.
- 5 Five force model.

**(b) Differentiate the following:**

- 1 Selling and Marketing
- 2 Production and Product concept of marketing
- 3 Market segmentation and Targeting
- 4 Niche Marketing and Mass Marketing
- 5 Consumer and Organization Buyer Behavior

**(c) Short Questions**

- 1 State the nature of marketing. How does marketing satisfy the wants of people?
- 2 “The present-day marketing is consumer-oriented” Explain this statement with the help of suitable examples
- 3 What do you mean by marketing management? Explain its objectives.
- 4 How does marketing affect the lives of people? Explain with reference to various utilities created by marketing.
- 5 Distinguish between marketing concept and selling concept.
- 6 Illustrate the implementation of marketing concept by modern business organizations.
- 7 What is “Morph” marketing?
- 8 Write a brief note on ‘augmented’ marketing.
- 9 Discuss how demographic and economic environment are relevant to a marketer.
- 10 Explain the impact of (i) Demography and (ii) Social and cultural environment on marketing management.
- 11 What do you understand by premium segment marketing?
- 12 How should marketers respond to the changing environment? 13 Name and describe the elements of the company’s micro-environment? 14 Compare and contrast business and consumer market?
- 15 Explain how marketers can segment international market?
- 16 Explain the major features of the marketing concept.
- 17 Describe the characteristics of Industrial markets.
- 18 Describe the different levels of a product using an example to illustrate.
- 19 Describe the elements of a promotion mix.
- 20 Explain the factors to be considered in channel design.
- 21 Describe the advantages of direct marketing.
- 22 What are segmentation challenges in B2B market.
- 23 Can we communicate our unique brand position in a way that is understandable and compelling to our consumers?
- 24 Differentiate between the following:
  - a) Points of parity and Point of difference association
  - b) Product specialization and Market specialization
- 25 What are the various patterns of target market selection?

26. Discuss the concept of internal marketing with suitable examples.
27. Explain in brief the product mix for KFC.
28. What is Marketing Mix ? Explain the various Marketing Mix elements taking the example of small sized passenger car.
29. What is consumer behavior ? Elaborate the different types of purchase behaviour in the purchase of a product, giving suitable examples.
30. Explain the marketing criteria to be used for selection of a brand name. Based on these criteria suggest a suitable brand name for the following Products and Services (any two) :
  - (i) fruit juice
  - (ii) Indian fast food chain
  - (iii) footwear
31. What are the major objectives of pricing ? How do the different stages of PLC affect the pricing decision ? Explain giving suitable example.
32. Write short notes on any three of the following :
  - (a) Implications of social marketing
  - (b) Perceptual mapping techniques
  - (c) Matrix organisation
  - (d) Primary data Vs Secondary data
  - (e) Characteristics of organisational consumer
33. How is marketing a service different from marketing a good?
34. Differentiate between marketing and selling
35. Write the role of marketing in modern business organization.
36. What is modern concept of marketing? Does it apply in India .Discuss.
37. Explain how business and marketing are changing?
38. Differentiate orientation and selling orientation between marketing.
39. Explain the concept of Marketing Mix. Discuss the rationale for extended marketing mix for services
40. Discuss the meaning, scope and role of marketing function in the exchange process. Illustrate with suitable examples.

### **III Long Answer Type Questions:**

1. What is marketing? What environmental forces have led to the growth of different forms of marketing in today's world?
2. Which orientation to marketing do you find more relevant social or management? Support your answer with suitable justification.
3. Explain the origin and development of the marketing concepts.
4. Explain the importance and scope of marketing in today's competitive environment.
5. Throw some light on the challenges involved in marketing of goods and services in today's context.

- 6 Elaborate the concept of Marketing Mix. Is 4 Ps of marketing complete in itself? Comment.
- 7 What do you mean by marketing environment? How can the external environment be studied?
- 8 What do you mean by Value chain analysis? How is it done?
- 9 What is SWOT analysis? Do a SWOT analysis of any IT/Manufacturing/Electronics/FMCG based organization.
- 10 “In today’s turbulent business environment competitive intelligence is a hygiene factor”. In view of this statement explain why the study of competitive environment is important.
- 11 Write short notes on :
- (a) PEST analysis
  - (b) SWOT analysis
  - (c) Five force model
- 12 Why is an understanding of a consumer's buyer behavior such an important issue? Discuss using an example. What are the factors that influence consumer buying behavior?
- 13 What factors affect buying decision making process in industrial buying? Also explain the process of industrial buying.
- 14 How can an understanding of consumer behavior be useful in developing marketing strategies? Give concrete examples. List and briefly describe each of the stages of the consumer decision making process.
- 15 Describe various participants of consumer buying process.
- 16 What is market demand? What do you mean by market measurement? What tools can be used for the same. What is the importance of estimating market demand?
- 17 What is segmentation? What are the characteristics of effective segmentation?
- 18 What do you mean by targeting and positioning of a product? What strategies can be used for the same? Also explain some common positioning errors.
- 19 What are the bases for segmentation? Explain your answer with suitable examples.
- 20 What do you mean by targeting? What are strategies for targeting a market? 21 Write an explanatory note on market segmentation selection.
- 22 “With products being differentiated, more and more markets are certain to become increasingly segmented.” Discuss this statement and outline the benefits of market segmentation.
- 23 “Pricing and promotion are integral elements of marketing-mix of a firm”. Comment. 24 Explain the concept and scope of expanded marketing-mix.
- 25 “Marketing is the performance of business activities that direct the flow of goods and services from producer to users or consumers”. Explain this statement in the light of importance of marketing.
- 26 (a) How does marketing mix influence the organization’s growth?
  - (b) Discuss how service quality can be used for positioning services.
- 27 Discuss the following and apply to the current marketing scenario



- (a) Howard and sheth model of consumer behavior
- (b) Henry Assael's model of consumer decision making

Make relevant assumptions to elucidate the models and their application in the present dynamic marketing environment.

- 28 Name and describe the types of consumer buying behavior. Which one you are most likely use if deciding on a laptop computer purchase and which for picking a restaurant for dinner?
- 29 Discuss current trends in the economic environment of which marketers must be aware and provide examples of companies' response to each trend.
- 30 List the major influences on business buyer behavior. Why is it important for the businessto-business marketer to understand these major influences? Also describe the stages of business buying process.
- 31 According to Peter Drucker "Marketing is so basic that it cannot be considered a separate function of the firm... it is a central dimension of the whole business". Discuss this idea, with particular reference to how this attitude to marketing is displayed by any one of the following firms:  
(a) Tata Motors      (b) Videocon      (c) Bharti Telecom
- 32 Briefly explain the stages of consumer buying-decision making process giving suitable examples.
- 33 (a) What are the pre-requisites for segmenting a market?  
(b) The world's cheapest eco- friendly car, Tata Nano, aims to bring the joys of motoring to millions of Indians as did the Volkswagen Beetle for Germany and mini for Britain.  
Says Tata chairman RatanTata : "I observed families riding on two-wheelers – the father driving the scooter, his young kid standing in front of him, his wife seated behind him holding a little baby. It led me to wonder whether one could conceive of a safe, affordable, all- weather form of transport for such a family." However many car users have expressed desire to add Nano to their fleet of cars. What demographic and psychographic features should Tata examine for segmenting the Indian market for their Nano car?
- 34 (a) Explain why demographic data alone is frequently insufficient for marketing decisions?  
(b) Differentiate among homogeneous, clustered and diffused consumer demands. What are the marketing implications for each?
- 35 Discuss various approaches for market targeting? Illustrate with the help of examples.
- 36 Differentiate between the following:  
(a) Mass marketing and Segmentation  
(b) Concentrated Marketing (Niche) and Individual marketing
- 37 What is positioning? How can a marketer position his product or service offering?
- 38 How consumers proceed for purchasing a High Involvement product as in contrast to Low Involvement Product.

39. Differentiate between the selling and marketing concept. What would a firm need to do to implement the marketing concept in the organization?
40. What is meant by the macro elements of the marketing environment? Discuss the significance of any three of these elements for marketers.
41. What are various factors in the marketing environment which must be kept in mind while designing marketing strategies? Elaborate with illustrations.
42. Why is it important to study consumer behaviour? Identify factors influencing consumer buying behaviour?
43. Describe the various stages involved in the new product development, with illustrations.
44. Explain the communication process. Describe the various elements of the promotion mix, with examples.
45. Explain salient features of Customer relationship management, with illustrations.
46. Write notes on:
  - (a) E-commerce.
  - (b) Managing the Sales Management.
47. Discuss the scope and relevance of the concept of market segmentation. Will the scope change with the opening of Indian economy? Illustrate how firms would be benefited in marketing their products and services by segmentation.
48. Briefly discuss the concept of positioning. What is the positioning of i) Luxury car ii) Indian airlines iii) Pepsi iv) Dalda ghee
49. As a marketing manager, propose and formulate STP strategy for home fitness kit targeted at women. Discuss the base for your strategy.
50. Marketing success largely depends on the effective STP strategies adopted by the firm. Discuss the above statement with two examples of your choice. What would be suitable segmentation basis for the following and why? (i) Premium brand of after shave lotion (ii) Rs. 1 lac small car proposed by a leading Indian car manufacturer (TATA NANO)

## UNIT - II

### (a) Multiple Choice Questions:

1. The customer will judge the offering by three basis elements: \_\_\_\_\_, services mix and quality, and price.
  - (a) Performance
  - (b) Salespeople
  - (c) Price
  - (d) Product features and quality
  - (e) None of the above

- 2 The five product levels constitute a \_\_\_\_\_. At each level more customer value is added.
- (a) Customer-augmented product
  - (b) Customer consumption system
  - (c) Customer value-hierarchy
  - (d) Customer-perceived value
  - (e) Customer hierarchy
- 3 Marketers have traditionally classified products on the basis of three characteristics: \_\_\_\_\_, tangibility, and use.
- (a) Customer value hierarchy
  - (b) Expected
  - (c) Augmented
  - (d) Durability
  - (e) None of the above
- 4 The \_\_\_\_\_ of a product mix refers to how many variants are offered of each product in the line.
- (a) Width
  - (b) Length
  - (c) Depth
  - (d) Consistency
  - (e) Height
- 5 The \_\_\_\_\_ of the product mix refers to how closely related the various product lines are in end use, production requirements, distribution channels, or some other way.
- (a) Consistency
  - (b) Depth
  - (c) Width
  - (d) Length
  - (e) Composition
- 6 The definition of \_\_\_\_\_ prices is: In considering an observed price, consumers often compare it to an internal memory reference price or an external frame of reference (such as a posted “regular retail price”).
- (a) Historical
  - (b) Reference
  - (c) Promotional
  - (d) Everyday low price
  - (e) None of the above

- 7 Pricing cues such as sale signs and prices that end in 9 become more influential when\_\_\_\_\_.
- (a) Consumer price knowledge is poor
  - (b) Items are purchased frequently
  - (c) Items have been on the market a long time
  - (d) Prices are consistent year-round
  - (e) They are employed frequently
- 8 In market-penetration pricing, the company's objective is to \_\_\_\_\_, believing that higher sales volume will lead to lower unit costs and higher long-run profits.
- (a) Block competitive launches
  - (b) Maximize their market share
  - (c) Minimize their market share
  - (d) Maximize volume
  - (e) None of the above
- 9 To maximize market share, a firm may use \_\_\_\_\_ pricing, which is based on the theory that as sales volume increases, unit costs will decrease.
- (a) Market-penetration
  - (b) Market-skimming
  - (c) Value pricing
  - (d) Demand pricing
  - (e) Price bands
- 10 Consumers \_\_\_\_\_ low-cost products or items they buy infrequently.
- (a) Prefer the lowest total cost of ownership of
  - (b) Remember prices of
  - (c) Are ambivalent to prices of
  - (d) Are more price sensitive to
  - (e) Are less price sensitive to
11. Sigma-Sunco has decided to introduce its new sunscreen eye drops in a limited market consisting of only two cities and closely monitor the reactions of potential customers to the product and marketing program. This is called
- (a) Diffusion analysis
  - (b) Use test
  - (c) Concept test
  - (d) Test marketing (e) Laboratory test.

12. At the *Melting Moments*, an ice cream parlour, customers place their orders, watch their ice-cream sundaes being prepared, and then quickly eat the sundaes in the store before the ice cream melts. This is an example of a characteristic of services known as
- (a) Inseparability
  - (b) Intangibility
  - (c) Heterogeneity
  - (d) Perishability (e) Dependency.
13. Raw materials such as forest and food are termed as a.
- (a) Infinite resources
  - (b) Finite resources
  - (c) Finite renewable resources
  - (d) Finite non renewable resources
  - (e) All of the above
14. In a recent research study initiated by Tel-E-Fone Telecommunications, survey calls were made to a randomly selected group in which every member has an equal chance of selection. This type of sample selection is called
- (a) Probability sample
  - (b) Convenience sample
  - (c) Judgment sample
  - (d) Quota sample (e) Area sample.
15. Which of the following is not one of the problems typically associated with secondary data?
- (a) It is too expensive to obtain
  - (b) It may not be current
  - (c) It may not exist (d) It may not be impartial (e) It may not be reliable.
16. Primary data can be collected through all the four ways except –
- (a) Observation
  - (b) Surveys
  - (c) Focus group
  - (d) Chatting
  - (e) Experiments
17. The research instruments that a marketing researcher can make use of are.
- (a) Questionnaires, Qualitative measure and mechanical devices
  - (b) Questionnaires, experimental research and behavioral data
  - (c) Questionnaires, qualitative measure and experimental research

- (d) Qualitative measure, Experimental research and survey research
  - (e) Experimental research, behavioral data and mechanical devices.
18. Intercept interviews involves
- (a) Asking questions and recording observations
  - (b) Seeking an appointment from respondents and paying some incentive for being interviewed.
  - (c) Stopping people at a shopping mall and requesting an interview.
  - (d) Calling up people and requesting an interview
  - (e) Sending online questionnaire and asking respondents to fill
19. If Wrigley's makes all the world's bubble gum but sells it through middlemen who market under individual store brands, Wrigley's is utilizing which type of brand- sponsorship?
- (a) Manufacturer's brand
  - (b) Slotting brand
  - (c) Private brand
  - (d) Licensed brand (e) Dealer brand.
20. Which of the following is not one of the major steps involved in the marketing research process?
- (a) Defining the problem and research objectives
  - (b) Developing the research plan
  - (c) Collecting and tabulating data
  - (d) Establishing a marketing information system (e) Interpreting and reporting the findings.
21. Ellen decided to conduct an experiment in her mall's car park to see if shoppers would respond to a lower parking price to park in some of the under-utilized sections of the car park. Which of the following types of market research Ellen is using?
- (a) Exploratory
  - (b) Causal
  - (c) Descriptive
  - (d) Investigative
  - (e) Behavioral
22. Whenever a new product eliminates another product because of its improvements, such as CDs to Cassettes, this phenomena is referred as
- (a) Improvements
  - (b) Creative destruction
  - (c) Creative construction

- (d) Improvement destruction (e) Creative innovation.
23. Sigma-Sunco has decided to introduce its new sunscreen eye drops in a limited market consisting of only two cities and closely monitor the reactions of potential customers to the product and marketing program. This is called
- (a) Diffusion analysis
  - (b) Use test
  - (c) Concept test (d) Test marketing
  - (e) Laboratory test.
24. Which of the following stages is not included in AIDAS theory?
- (a) Gaining interest
  - (b) Evaluation
  - (c) Securing attention (d) Inducing action (e) Building satisfaction.
25. Which of the following see(s) the product, in a commodity market as very important and demand the deepest discount and the highest service?
- (a) Bargain hunters
  - (b) Programmed buyers
  - (c) Relationship buyers (d) Transaction buyers (e) Gatekeepers.
26. Which of the following is not one of the major “product” variable decisions to be made by a retailer?
- (a) Target market selection
  - (b) Product assortment decision
  - (c) Merchandising
  - (d) Store atmosphere decision (e) Services mix decision.
27. When the *Gap* branched out to offer clothing targeted to infants, children, and mothers-to-be, they were segmenting the market based on
- (a) Age and life cycle
  - (b) Gender
  - (c) Income (d) Psychographics (e) Generation.
28. Which of the following consists of a set of buyers who share common needs or characteristics that the company decides to serve?
- (a) Mass market
  - (b) Government market
  - (c) Reseller market
  - (d) Target market
  - (e) Heterogeneous market.

29. Marketing chewable vitamins for children and a different version for adults is an example of
- (a) Geographic segmentation
  - (b) Psychographic segmentation
  - (c) Regional segmentation
  - (d) Age and life-cycle segmentation
  - (e) Physiological segmentation.
30. A firm that bases its price on how it thinks the competitors will price, rather than on its own costs or demand, in order to win a contract is most likely using
- (a) Going-rate pricing
  - (b) Cost-plus pricing
  - (c) Perceived-value pricing
  - (d) Sealed-bid pricing
  - (e) Auction-type pricing.
31. ----- is the amount of money charged for a product or service.
- (a) Price
  - (b) Accountancy
  - (c) Demand
  - (d) Value
32. \_\_\_\_\_ is the sum of the values that consumers exchange for the benefits of having or using the product or service.
- (a). Price
  - (b). Elasticity
  - (c). Demand
  - (d). Value estimate
33. Throughout most of history, prices were set by \_\_\_\_\_.
- (a). Fixed-price policies constructed by sellers
  - (b). Negotiation between buyers and sellers
  - (c). Governments and regulatory agencies
  - (d). Ruling monarchs
34. A \_\_\_\_\_ policy means that a firm sets one price for all buyers in a given product or service line.
- (a). Fixed-price
  - (b). Variable-price
  - (c). Dynamic-price
  - (d). Standard-price



35. Which of the following factors is spurring a new movement in pricing toward dynamic pricing?
- (a) The federal government
  - (b) Strong retailers
  - (c) The Internet
  - (d) Strong wholesalers
36. \_\_\_\_\_ is the practice of charging different prices depending on individual customers and situations.
- (a) Fixed-pricing
  - (b) Standard-pricing (c) Barter-pricing
  - (d) Dynamic pricing
37. -----\_is the only element of the marketing mix that produces revenue.
- (a). Product
  - (b). Price
  - (c). Place (distribution)
  - (d). Promotion
38. All of the following are among the internal factors that affect pricing EXCEPT: (Pick the LEAST LIKELY.) (a). Globalization.
- (b). The company's marketing objectives.
  - (c). Marketing mix strategy.
  - (d). The organization.
39. Before setting price, the company must decide on its strategy for:
- (a). Distribution.
  - (b). Promotion.
  - (c). The environment.
  - (d). The product.
40. Companies set \_\_\_\_\_ as their major objective if they are troubled by too much capacity, heavy competition, or changing consumer wants.
- (a) Current profit maximization
  - (b) Survival
  - (c) Market share leadership
  - (d) Product quality leadership
41. An idea for a possible product that the company will offer is classified as
- (a) product idea
  - (b) product image

- (c) customer management
  - (d) none of the above
42. The major sources of ideas for product development comes from
- (a) internal sources
  - (b) external sources
  - (c) product lines extension
  - (d) both a and b
43. The products such as "VHS tapes" are examples of
- (a) product classes
  - (b) product forms
  - (c) branding
  - (d) product perception
44. In the new product development process, after the analysis of business the next step to be taken is
- (a) test marketing
  - (b) one channel marketing
  - (c) penetration marketing
  - (d) individual marketing
45. When the new developed product concept is tested, the next immediate step is to
- (a) develop market strategy
  - (b) develop a testing technique
  - (c) develop intermediaries
  - (d) develop logistic network
46. The pricing strategy used to set prices of the products that are must be used with the main product is called
- (a) optional product pricing
  - (b) product line pricing
  - (c) competitive pricing
  - (d) captive product pricing
47. The new product pricing strategy through which the companies set lower prices to gain large market share is classified as
- (a) optional product pricing
  - (b) skimming pricing
  - (c) penetration pricing
  - (d) captive product pricing

48. The pricing strategy in which prices are set lower to actual price to trigger short term sales is classified as
- (a) promotional pricing
  - (b) short term pricing
  - (c) quick pricing
  - (d) cyclical pricing
49. The pricing strategy in which company divides location into different sectors and charge same price for each sector is classified as
- (a) freight on board origin pricing
  - (b) zone pricing
  - (c) basing point pricing
  - (d) uniform delivered pricing
50. The kind of reduction made to those buyers who buy large volumes of products is classified as
- (a) cash discount
  - (b) seasonal discount
  - (c) functional discount
  - (d) quantity discount
51. A computer based system that facilitates the transfer of money or the processing of financial transactions between two financial institutions the same day or over night is.....
- (a) ETB
  - (b) EFT
  - (c) E-cash
  - (d) E-money
52. A digital analog of various forms of payment backed by a bank or financial institution is .....
- (a) ETB
  - (b) EFT
  - (c) E-cash
  - (d) E-money
53. Which of the following is not a type of e-payment system.
- (a) ETB
  - (b) EFT

- (c) E-cash
  - (d) None of these
54. ....involves some one masquerading as someone else.
- (a) Spoofing
  - (b) Unauthorized action
  - (c) Eavesdropping
  - (d) Phishing
55. When information about transactions is transmitted in transparent way hackers can catch the transmissions to obtain customers sensitive information. This is known as.....
- (a) Spoofing
  - (b) Unauthorized disclosure
  - (c) Eavesdropping
  - (d) Phishing
56. A competitor or an unhappy customer can alter a website so that it refuses services to potential clients. This is known as .....
- (a) Unauthorized action
  - (b) Unauthorized disclosure
  - (c) Eavesdropping
  - (d) Phishing
57. .... Is a specialized form of online identity theft.
- (a) Spoofing
  - (b) Unauthorized disclosure
  - (c) Eavesdropping
  - (d) Phishing
58. A security tool to verify the authenticity of the message and claimed identity of the sender and to verify the message integrity is
- (a) encryption
  - (b) firewalls
  - (c) digital certificates
  - (d) digital signature
59. An electronic file that uniquely identifies individuals and websites on the internet and enables secure, confidential communications.
- (a) Digital signature

- (b) Digital certificates
  - (c) Encryption
  - (d) Firewalls
60. ....is online identity theft.
- (a) Eavesdropping
  - (b) Phishing
  - (c) Spoofing
  - (d) None of these
61. ....is not an e-payment media.
- (a) Credit card
  - (b) Debit card
  - (c) Electronic cheque
  - (d) Wallet
62. The financial exchange that takes place online between buyers and sellers is known as
- (a) E-branding
  - (b) E-marketing
  - (c) E-advertisement
  - (d) E-payment system
63. EFT means
- (a) Electronic fund transfer
  - (b) Efficient fund transfer
  - (c) Eligible fund transfer
  - (d) None of these
64. All of the following would be ways to segment within the category of psychographic Segmentation EXCEPT: (a) social class.
- (b) occupation.
  - (c) lifestyle.
  - (d) personality.
65. The is a person within a reference group who, because of special skills, knowledge, personality, or other characteristics, exerts influence on others.
- (a) facilitator
  - (b) referent actor
  - (c) opinion leader

- (d) social role player
66. .... describes changes in an individual's behavior arising from experience.
- (a) Modeling
  - (b) Motivation
  - (c) Perception
  - (d) Learning
67. Concerns that the manufacturers of harmful products such as tobacco have influence on lawmakers to the detriment of the public interest is used as evidence of which criticism of marketing?
- (a) Too much advertising.
  - (b) Too few social goods.
  - (c) Cultural pollution.
  - (d) Too much political power.
68. The Internet evolved from a network created by during the 1960s.
- (a) the Commerce Department
  - (b) the Massachusetts Institute of Technology (MIT)
  - (c) Northwestern University
  - (d) the Defense Department
69. In terms of execution styles, a family seated at the dinner table enjoying the advertised product would be an example of which of the following types of advertising?
- (a) Slice of life
  - (b) Lifestyle
  - (c) Mood or imagery
  - (d) Personality symbol
- 70 A child in the United States is normally exposed to all of the following values EXCEPT : (a) achievement and success.
- (b) activity and involvement.
  - (c) material comfort.
  - (d) collectivism.

Ans. (1)(d), (2)(c), (3)(d), (4)(c), (5)(a), (6)(b), (7)(a), (8)(b), (9)(a), (10)(e), (11)(d), (12)(d), (13)(c), (14)(a), (15)(a), (16)(d), (17)(a), (18)(c), 19(c), (20)(d), (21)(b), (22)(b), (23)(d), (24)(b), (25)(a), (26)(a), (27)(a), (28)(d), (29)(d), (30)(c), (31) (a), (32) (a), (33) (b), (34) (a), (35) (b), (36) (d), (37) (b), (38) (a), (39) (d), (40) (b), (41)(a), (42)(d), (43)(b), (44)(a),

(45)(a),(46)(d),(47)(c),(48)(a),(49)(b),(50)(d),,51(b),52(a),53(d),54(a),55(b),56(a),57(d),58(d),59(b),60(b),61(d),62(d),63(a),(64)(b),(65)(c),(66)(d),(67)(d),(68)(d),(69)(a),(70)(d).

## **II Short Answer Type Questions:**

- 1 Define a product. What are the various viewpoints to explain the concept of a product?
- 2 What are the objectives and strategies considered as the pillars for the success of any product? Discuss with examples.
- 3 “The elements of a product policy are difficult to determine.” Comment. 4 Define product planning. How it is different from product development?
- 5 Explain the concepts of product-line width, length, depth, and consistency.
- 6 What is meant by product differentiation? Compare the advantages of product differentiation and market segmentation.
- 7 Distinguish between product planning and product life-cycle.
- 8 Describe concept testing as it is used to manage the development process.
- 9 Briefly discuss the reasons for failure of new products.
- 10 What is meant by pricing? Why pricing is an important element of marketing mix?
- 11 What are the determinants of price of a product? Discuss.
- 12 Explain the objectives of pricing policy of a business firm.
- 13 Illustrate and explain the factors that affect pricing decisions by a firm. What factors push up the prices? Discuss.
- 14 Explain the price quotations based on geographical location of buyers.
- 15 Explain (a) skimming and (b) penetration pricing. Point out the reasons for such pricing strategies. What are their advantages?
- 16 Write short notes on the following
  - (a) Product life cycle
  - (b) Emotional product motives
  - (c) Product myopia
  - (d) Psychological pricing
- 17 Briefly state the important criteria used to screen new product ideas.
- 18 Explain the relevance of individual brand and family brand.
- 19 Is there any relation between the price of the good or services and their quality? How do you think customer relate price to quality?
- 20 “High price is equivalent to high quality product”. Comment 21 Explain the concept of PLC?
- 22 Can companies rescue product foundering in the maturity phase of their life cycle and return them to the growth phase? Suggest strategies that marketers may use to force consumers mental shift.
- 23 Explain the AIDA model in brief?
- 24 What do you understand by test marketing?

- 25 What do you understand by value pricing and going rate pricing techniques of determining price for a product?
- 26 Describe the methods for pricing policies and strategies.
- 27 Discuss the pricing techniques application to a FMCG product being launched in a highly competitive market.
- 28 What is meant by product line. Elaborate the various Line Management Strategies.
- 29 Give the steps in launching a new product. Also give various methods of test marketing a new Product.
- 30 Write about analyzing the macro environment of marketing?
- 31 As a marketing manager, propose and formulate STP strategy for home fitness kit targeted at women. Discuss the base for your strategy.
- 32 What do you mean by a product? Discuss major consumer goods and industrial goods classification?
- 33 Explain the following terms:
  - a) Premium Pricing
  - b) Discount Pricing
  - c) Tender Pricing
  - d) Product line Pricing
  - e) Cost Plus pricing
34. Discuss the meaning, scope and role of marketing function in the exchange process. Illustrate with suitable examples.
35. Distinguish Marketing mix vs. Marketing strategy.
36. When is Personal Selling more appropriate than other methods of Sales Promotion? Explain with examples.
37. What are the major considerations involved in designing the marketing organisation for a global furniture manufacturer foraying into Indian market?
38. Briefly explain the concept of positioning. Suggest positioning strategy for the following
  - (i) A new domestic airline
  - (ii) flat Screen TV
 (b) How does marketing research aid marketing managers?
39. Write short notes on any three of the following
  - (a) Cybermarketing
  - (b) Relationship of a segment to a market
  - (c) Market potential
  - (d) Concept of PLC
  - (e) Marginal cost Pricing
40. Explain the term Market Segmentation. Why should marketers consider segmentation as an important marketing decision? Discuss with the help of suitable examples.
- 41 Briefly explain the concept of positioning, with suitable example?
- 42 What are purposes of segmentation? Suggest various alternative bases of segmentation with suitable examples.



- 43 Explain the concept of PLC and its utility for marketers?
- 44 Discuss the marketing strategies that may be used at the introductory and maturity stages of the product life cycle.
- 45 Identify at what stages of their respective PLCs are the following products in the Indian market and accordingly suggest suitable strategies for these products :
  - (i) Mobile Phones
  - (ii) Portable two-in-one stereo systems

### **III Long Answer Type Questions:**

- 1 Write an essay on product policy of any marketing organization.
- 2 What is meant by product line expansion? Are the product line expansion and diversification synonyms? What are the reasons of going in for diversification?
- 3 Explain with the help of examples.
- 4 In an economy of change, continuous innovation is necessary. Most companies rarely innovate, some innovate occasionally, and a few innovate continuously. Comment on why a company should continuously develop new products.
- 5 What are the steps involved in new product launch. Discuss with the help of suitable examples.
- 6 Describe the important criteria used to screen new product ideas.
- 7 How can the test of PLC be used in the following:
  - (a) As a tool of plan market share strategies
  - (b) As an indication of opportunity to a firm
- 8 How PLC concept works as a guidelines for formulating and implementing the marketing strategies.
- 9 In planning its market offering, the marketer must address the five product levels of the customer-value hierarchy. Describe the “customer-value hierarchy” and identify the five levels of product contained within.
- 10 Customer needs and wants are the logical place to start the search for new product ideas. Identify four ways a company can draw new ideas from its customers.
- 11 Prior research has shown that although consumers may have fairly good knowledge of the range of prices involved, surprisingly few can recall specific prices of products accurately. When examining products, consumers often employ reference prices. List the possible prices consumers use as their “reference.”
- 12 What is meant by pricing policy? How can the pricing policy be developed for an organization? Discuss in detail the basic methods of pricing adopted by Indian industry.
- 13 Write an essay on legal restrictions on fixing a price for a product.
- 14 Why do pricing objectives vary from organization to organization? What is the importance of pricing objectives? Discuss.
- 15 What are the factors that affect pricing decisions in a marketing organization?

- 16 “Price is the only element of marketing mix that produces revenue”. Discuss. Identify and discuss the six steps of the pricing procedure. Explain.
- 17 An increasing number of companies are basing their prices on the customer’s perceived value. Explain the concept of “perceived value” and identify the key to pricing in this manner.
- 18 As a president of a home video recording Machine Company, you must decide between penetration or skimming pricing policy. Explain the factors you would consider in making your choice.
- 19 Define pricing as a function of marketing and discuss its contribution in the success of the marketing strategy of a company.
- 20 What are various kind of pricing strategies? Discuss in detail. What are the factors affecting price – sensitivity? Describe the factors that influence the pricing strategy of a firm.
- 21 Suggest appropriate pricing strategies for the following products/services:  
(a) Insurance policy (b) Car batteries  
(c) Chocolate bars
- 22 Write an essay on Total Quality Management highlighting the importance of quality products in marketing.
- 23 Examine the salient factors that ought to be taken into account while introducing a new product. Illustrate your answer.
- 24 Suggest appropriate marketing strategies for each of the stages of the product life-cycle.
- 25 What do you understand by psychological pricing and premium pricing? Based on your personal experience, give examples of both
- 26 Describe the various internal and external forces that influence the pricing strategy of a firm.
- 27 Is pricing a lethal weapon in the marketer’s armory? If yes, then why is it that some managers pay little attention to evolving optimal pricing strategies for their products?
- 28 Can a firm have differing pricing objectives in the short run as opposed to long run? Discuss the cost oriented and demand-oriented methods of pricing.
- 29 A major issue in marketing and consumer behavior today is acceptance of new product and services. Explain the stages and processes that a consumer goes through for adopting new product and services.
- 30 How do you think customer relate price to quality? In times of cost transparency customer will high price be at all considered a signal of high quality? Do companies try to send specific cues about its product quality by its pricing strategy? Give examples of product where such a proposition be successful and also of product where this strategy would not work. Justify your answer citing relevant examples from the industry? 31 Discuss the four distinct stages in product life cycle.
- 32 Identify at what stages of their PLC’s are the following products in the Indian market and accordingly suggest suitable strategies for these products:  
(a) Mobile phones

- (b) Portable two-in-one stereo systems
- 33 What are the major objectives of product line decisions? List out the merits and demerits that accrue from these decisions. Explain by giving suitable examples.
  - 34 Explain the extended P's of marketing mix with suitable corporate examples.
  - 35 (a) Describe the attributes of a good brand name. Give examples.  
(b) Explain the major functions of packaging. Use examples.
  - 36 (a) A firm may pursue more than one pricing objectives. Explain.  
(b) Describe demand based pricing and its advantages.
  - 37 Explain the benefits of segmentation and suggest ways for segmenting the market for:
    - (a) Toothpaste
    - (b) Air Conditioners
  - 38 How can a firm manage the various stages of its products' Lifecycle? Explain with the help of suitable examples.
  - 39 If you are the head of sales and distribution and you have been assigned the task of selecting distributors to handle your company's line of white goods. What criteria will you use to select among the 10 distributors which have been shortlisted.
  - 40 Explain in detail the pricing strategy as an important component of marketing mix and also describe the various methods of pricing used by the marketers.
  - 41 Explain the process of Segmentation, Targeting and Positioning with respect to any consumer durable product.
  42. (a) What is meant by Product Mix, Product Line Length and Product Mix Consistency? Explain the reasons marketers opt for downward product line stretch.  
(b) Explain the strategies that marketers can opt in the maturity stage of Product Life Cycle.
  43. Explain the various factors that are likely to influence pricing decisions. Explain the various methods used for determining the price of any product.
  44. Read the case given below and answer the questions given at the end of the case.

India is among the hottest growth markets for AC makers, just like other consumer goods companies. Daikin entered India in 2000 as an 80:20 JV with Siddharth Shriram group company Siel. In 2004, it bought out Siel's 20% stake to make the Indian firm a wholly owned subsidiary. All these years, Daikin's sold bulk of its ACs to offices and factories and served only the upper middle class homes.

Since entry-level products are driving volumes across categories, the company could not afford to stay away from that segment for long. Daikin launched 14 models for homes last year and the starting model was only 10-15% costlier than similar models offered by the competition. Earlier the price gap used to be 50%.

Changing lifestyle, increasing disposable income, falling prices and wider availability have all contributed to the rise in air-conditioners sales. Demand is also rising in smaller cities and towns as well as more households join the buoying middle class segment.

With introduction of cheaper products, enhanced distribution network and aggressive promotional activities in the last one year, the company claims to have already increased its market share marginally which is encouraging and it wants to become one of the top three room air conditioners marketers. The company plans to introduce more mass products, which account for more than 80% of the country's room AC market.

Questions :

Develop suitable promotional strategies for the company for the following segments :

(a) Home segment

(b) Offices and factories segment

45. Discuss the implications of new product development decision on the business enterprise.

Briefly describe the stages in new product development strategy What are the various stages of the new product development and launch. Explain with examples. Describe new product development and mention the various stages of new product development?

46. What are the major objectives of product-line decisions ? List out the merits and demerits that accrue from these decisions. Explain by giving suitable examples.

47. What are the criteria marketers must evaluate before selecting a brand name? Q3) Explain the term Product , Product line and Product mix ? What do you mean by a product? Discuss major consumer goods and industrial goods classification?

48. Discuss in brief the various pricing strategies used by marketers. Suggest suitable pricing strategy for

i) Mobile Phone

ii) Mid-sized passenger car

49. Discuss in brief the various pricing strategies used by marketers. Suggest suitable pricing strategy for

i) Mobile Phone    ii) Titan Watch    iii) Luxury car

iv) Tablet PC

50 Briefly explain the various pricing methods available for Indian marketers, with suitable illustrations. Identify factors affecting pricing decision How price of a product is determined? Explain the factors affecting price.

51. What is pricing method? Describe the different methods of pricing? How cost based pricing and market based pricing methods are useful in fixing the price of a new product? What do you mean by the term “What traffic can bear pricing”? Define market skimming and market penetration?

52 Explain the following terms:

- (a) Premium Pricing
- (b) Discount Pricing
- (c) Tender Pricing
- (d) Product line Pricing
- (e) Cost Plus pricing

53. Define Pricing. Discuss the importance of pricing in marketing mix.

### **UNIT - III**

#### **I Test your Skills:**

##### **(a) State whether the following statements are True or False:**

- 1 Advertising is not paid for by an identified sponsor.
- 2 Personal selling and direct marketing are one and same thing.
- 3 Pull strategy involves pulling up the dealers to sell more.
- 4 Companies can facilitate and speed external communication among customers by creating online and off-line “buzz” through brand advocates and user communities.
- 5 The proliferation of targeted media and communication channels has allowed marketers to become much more aware of their target consumers’ preferences and to customize both products and messages for individual consumers.
- 6 The lower price of generics is made possible by lower-quality ingredients, lower-cost labeling and packaging, and minimal advertising.
- 7 Retailers develop their own “store brands” to differentiate themselves from other retailers and the national branded merchandise.
- 8 Wholesaling includes all the activities involved in selling goods or services to those who buy for resale or business use. Wholesaling includes manufacturers and farmers who sell directly to consumers.
- 9 Retailers are generally eager to stock new products, making it difficult for manufacturers to keep older, but proven brands on the shelves.
- 10 Because wholesalers do not actually manufacture a product, they are unable to effectively manage asset productivity.

Ans. (1)(F), (2)(F), (3)(F), (4)(T), (5)(T), (6)(T), (7)T, (8)(F), (9)(F), (10)(F)

**(b) Multiple Choice Questions:**

- 1 A \_\_\_\_\_ is someone seeking a response (attention, a purchase, a vote, a donation) from another party, called the \_\_\_\_\_.
  - (a) salesperson; customer
  - (b) fund-raiser; contributor
  - (c) politician; voter
  - (d) marketer; prospect
  - (e) celebrity; audience
  
- 2 In a hypercompetitive economy such as ours, a company can win only by fine-tuning the value delivery process and choosing, providing, and \_\_\_\_\_ superior value.
  - (a) communicating
  - (b) selecting target markets with
  - (c) composing
  - (d) developing
  - (e) researching
  
- 3 Rising promotion costs and shrinking profit margins are the result of \_\_\_\_\_.
  - (a) changing technology
  - (b) globalization
  - (c) deregulation
  - (d) privatization
  - (e) heightened competition
  
- 4 Intermediaries include retailers, \_\_\_\_\_, and logistical organizations.
  - (a) Internet companies
  - (b) wholesalers
  - (c) competitors
  - (d) box stores
  - (e) none of the above
  
- 5 Major retailer types include the following EXCEPT \_\_\_\_\_.
  - (a) specialty store
  - (b) discount store
  - (c) catalog showroom
  - (d) the Internet
  - (e) superstore

- 6 In a franchising system, individual franchisees are \_\_\_\_\_.
- (a) a tightly knit group of enterprises whose systematic operations are planned, directed, and controlled by the franchisor
  - (b) regional managers of corporately owned facilities
  - (c) employees working in front-line service roles for the entrepreneur
  - (d) independent businesspeople who have the freedom to develop their own processes, brands, and images, facilitated by a retailing cooperative
  - (e) none of the above
- 7 Intermediaries sponsor their own brands because \_\_\_\_\_.
- (a) private-label brands sell at higher volumes
  - (b) private-label brands are recognizable to the consumer as being widely available from many different retailers
  - (c) private-label brands are always of better quality than national brands
  - (d) private-label brands can be sold at lower prices yet generate a higher profit margin because of their lower cost structure
  - (e) all of the above
- 8 Wholesaler-distributors have faced mounting pressure in recent years. They have had to develop appropriate strategic responses. One major drive has been to increase \_\_\_\_\_ productivity by managing their inventories and receivables better.
- (a) product assortment
  - (b) buying practices
  - (c) personnel
  - (d) asset
  - (e) products
- 9 \_\_\_\_\_ is the cornerstone of all discount operations.
- (a) Self-service
  - (b) Self-selection
  - (c) Limited service
  - (d) Full service
  - (e) Custom service
- 10 Nonstore retailing falls into four major categories. Which of the following is NOT one of the four nonstore retailing categories?
- (a) Buying service
  - (b) Internet sales
  - (c) Automatic vending
  - (d) Direct marketing

- (e) Direct selling
11. A large oil company runs advertisements that show how its employees are involved in the community development activities. This is an example of
- (a) Informative advertising
  - (b) Institutional advertising
  - (c) Comparative advertising
  - (d) Reminder advertising
  - (e) Product advertising
12. When Procter & Gamble introduced Swiffer, a new product to make it easier to clean increasingly popular hardwood floors, it knew it had to achieve high brand awareness among its potential consumers because the product was low-tech and fairly easily imitated. Which promotional element did P & G emphasize?
- (a) Advertising
  - (b) Personal selling
  - (c) Sales promotion
  - (d) Public relations
  - (e) All of the above equally.
13. The college recruiter who visits a high school campus to convince its leading scorer to play basketball for his university, is involved in which type of promotion?
- (a) Online marketing
  - (b) Publicity
  - (c) Personal selling
  - (d) Public relations
  - (e) Sales Promotion.
14. There are a number of objectives of advertising that need to be considered. Which of the following is not one of the objectives of advertising?
- (a) Persuasion
  - (b) Information
  - (c) Reminder
  - (d) Entertainment
  - (e) All are the objectives
15. The service mark of Jet Airways is
- (a) “We love flying “
  - (b) “Let us fly high “
  - (c) “The joy of flying”



- (d) “Come let us fly together “
  - (e) “Flying high “
16. POP stands for \_\_\_\_\_
- (a) Print-offer proposal
  - (b) Publicity over protocol
  - (c) Point of purchase
  - (d) Place of publication
  - (e) Promotion on purchase
17. The “Sumo” in the Tata Sumo gets its inspiration from
- (a) The fire dragons of China
  - (b) The kangaroos of Australia
  - (c) The wrestlers of Japan
  - (d) The Indian army
  - (e) Chambers
18. When a company advertises, develops consumer promotions, such as a contest, and develops other marketing communications as a tie-in with an event marketing program, it is called \_\_\_\_\_
- (a) A local promotion
  - (b) A corporate promotion
  - (c) An advertising promotion
  - (d) A cross-promotion
  - (e) Trade promotion
19. Direct-marketing programs create \_\_\_\_\_
- (a) One-to-one contacts with customers
  - (b) Frequency programs
  - (c) Re-analysis of databases
  - (d) New mass media messages
  - (e) Goodwill of company
20. In terms of goals for public relations, a hit is \_\_\_\_\_
- (a) An advertisement that is successful
  - (b) A consumer promotions’ tie in with publicity
  - (c) Mention of the company’s name in a news story
  - (d) An advertising slogan with high recall
21. When a car dealer complains to the manufacturer that another dealer of the same make of cars is selling outside their assigned territories, it is a type of
- (a) Parallel conflict

- (b) Customer-service conflict
  - (c) Vertical conflict (d) Horizontal conflict
  - (e) Multi-level conflict.
22. When a seller requires that a dealer not handle competitors' products, the agreement is called a/an
- (a) Exclusive distribution
  - (b) Exclusive dealing
  - (c) Control criterion
  - (d) Dual distribution
  - (e) Dealer's rights.
23. Which of the following statements about retailing is not true?
- (a) Retailing involves selling to final consumers
  - (b) Retailing is a major industry
  - (c) Manufacturers and wholesalers never make retail sales
  - (d) Retail sales may be done by person, mail, telephone, vending machines or from a Web site
  - (e) Technology advancement constitutes an uncontrollable element in retailing.
24. A Brazilian NGO Reciclar-t3 makes clothes out of recycled clothes. This is an example of
- (a) Blue marketing
  - (b) Green marketing
  - (c) Community relations (d) Value added engineering (e) Global warming.
25. The reseller market mainly consists of
- (a) Consumers
  - (b) Manufacturers
  - (c) Wholesalers and retailers
  - (d) Industrial users (e) Government.
26. A branded, high volume, low value consumer good is most likely to be sold through which of the following types of distribution channels?
- (a) Direct sale from the manufacturer to consumer
  - (b) Sale through brokers
  - (c) Sale through specialist retail outlets
  - (d) Sale through many general retail outlets
  - (e) Directly from the wholesalers without retailers.

27. Airline travel is very price competitive. People will switch airlines if the price of a round trip ticket is lower on one airline than another. This is an example of
- (a) Pure competition
  - (b) Monopolistic competition
  - (c) Pure monopoly
  - (d) Brand Mindset
  - (e) Oligopolistic competition.
28. Which of the following describes the use of electronic means and platforms to conduct a company's business?
- (a) E-tailing
  - (b) E-purchasing
  - (c) E-business (d) E-marketing (e) E-mail.
29. The shift in marketing from trying to maximize profit on individual transactions to maximizing mutually beneficial relationships with consumers and others is called
- (a) Sales marketing
  - (b) Production marketing
  - (c) Mega marketing (d) Relationship marketing (e) Proactive marketing.
30. "Friends don't let friends drive drunk" is an example of
- (a) Niche marketing
  - (b) Social marketing
  - (c) Selling (d) Advertising
  - (e) Sales promotion.
31. Another name for a company's marketing communications mix is: (a) the advertising program.
- (b) the sales force. (c) the image mix.
  - (d) the promotion mix
32. Which tool of the promotional mix is defined as any paid form of nonpersonal presentation and promotion of ideas, goods, or services by an identified sponsor?
- (a). advertising
  - (b). public relations
  - (c). direct marketing
  - (d). sales promotion

33. The \_\_\_\_\_ is the specific mix of advertising, personal selling, sales promotion, public relations, and direct marketing tools that the company uses to pursue its advertising and marketing objectives.
- (a) value mix
  - (b) integrated dealer mix
  - (c) marketing communications mix
  - (d) marketing control mix
34. Which tool of the promotional mix consists of short-term incentives to encourage the purchase or sale of a product or service?
- (a). advertising
  - (b). public relations
  - (c). direct marketing
  - (d). sales promotion
35. If a company wants to build a good “corporate image,” it will probably use which of the following marketing communications mix tools?
- (a) advertising
  - (b) public relations
  - (c) direct marketing
  - (d) sales promotion
36. Consumers today receive commercial messages from a broad range of sources. However, consumers \_\_\_\_\_ the way marketers do.
- (a) don't distinguish between message sources
  - (b) are able to differentiate among messages sources
  - (c) don't care about buzz marketing
  - (d) are not able to block out messages
  - (e) block them all out
37. Shaping and fitting the offer to the buyer/s needs, including activities such as manufacturing, grading, assembling, and packaging, describes which of the following key functions performed by members of the marketing channel?
- (a). information
  - (b). promotion
  - (c). contact
  - (d). matching

38. Caterpillar (famous for earth moving equipment) has a powerful partnership with its dealers. Which of the following is one of the basic principles upon which this successful partnership is built? (a). the Internet  
(b). advertising  
(c). dealer profitability  
(d). global networks
39. Through their contacts, experience, specialization, and scale of operation, \_\_\_\_\_ usually offer the firm more than it can achieve on its own.  
(a). manufacturers  
(b). producers  
(c). direct marketers  
(d). intermediaries
40. Transporting and storing goods is part of which of the following marketing channel functions? (a). negotiation  
(b). physical distribution  
(c). contact  
(d). matching
41. The promotion technique for consumers according to which demonstrations and displays of \_\_\_\_\_ products made at place of sale is called  
(a) point of purchase promotion  
(b) cents off deals (c) sales premium  
(d) advertising specialties
42. The personal selling step in which the sales person asks for an order to the customer is classified as  
(a) shipper approach  
(b) handling shipment  
(c) closing  
(d) follow up
43. The sales force structure in which a sales representatives works to sell specific items of product line is classified as  
(a) indirect sales force structure  
(b) territorial sales force structure  
(c) customer sales force structure  
(d) product sales force structure
44. The third step in personal selling process after completion of pre-approach step is to  
(a) prospecting and qualifying

- (b) handling objections
  - (c) approach
  - (d) presentation and demonstration
45. The step in personal selling process which consists of first meeting first meeting between customer and sales person is called
- (a) qualifying
  - (b) prospecting
  - (c) follow up
  - (d) approach
46. The way in which marketing channels work well with each other to provide each customer with their preferred services is classified as
- (a) functional integration
  - (b) product integration
  - (c) channel integration
  - (d) location integration
47. The system in which company creates partnerships with different channels to source and deliver their market offering is classified as
- (a) functional network
  - (b) predatory network
  - (c) hybrid network
  - (d) value network
48. The strategy of marketing channel system in which company's sales force carry, promote and sell products to end users is classified as
- (a) shallow strategy
  - (b) push strategy
  - (c) pull strategy
  - (d) bundle strategy
49. Considering marketing channel system, the strategies used by companies to manage intermediaries are
- (a) push strategy
  - (b) pull strategy
  - (c) bundle strategy
  - (d) both a and b
50. The guarantees of products by its manufacturers and established payment terms are classified as

- (a) price policy
  - (b) distribution policy
  - (c) conditions of sale
  - (d) territorial rights
51. .... is also known as buzz marketing.
- (a) Word of mouth marketing
  - (b) viral marketing
  - (c) guerilla marketing
  - (d) morph marketing
52. In Japan .....marketing is known as 'Kuchikomi'.
- (a) Word of mouth
  - (b) viral
  - (c) guerilla
  - (d) morph
53. The term ..... Marketing was coined by Steven Jurvetson in 1997.
- (a) Word of mouth
  - (b) viral
  - (c) guerilla
  - (d) morph
54. Under .....marketing every customer is treated as unique.
- (a) Word of mouth
  - (b) viral
  - (c) guerilla
  - (d) one-on-one
55. An airline working with a tour operator or a hotel group is an example of.....marketing (a) Partnership
- (b) viral
  - (c) guerilla
  - (d) morph
56. Marketing to babies in the womb is .....marketing.
- (a) Galimatias
  - (b) viral
  - (c) guerilla
  - (d) morph

57. .... is the marketing of products that are regarded to be safe for the environment.
- (a) Green marketing
  - (b) Social marketing
  - (c) Gaimatias marketing
  - (d) none of these
58. A product with the ..... is a green product.
- (a) Ecomark
  - (b) Agmark
  - (c) ISI Mark
  - (d) none of these
59. .... is the marketing of a social message with a view to change behavior of people's habit.
- (a) Green marketing
  - (b) Social marketing
  - (c) Gaimatias marketing
  - (d) none of these
60. Which of the following is not an element of Social marketing mix?
- (a) Product
  - (b) Price
  - (c) Distribution
  - (d) People
- 61 Marketing channel that involves one or more intermediaries to made their products available to final buyers is classified as
- (a) A flexible channel
  - (b) static channel
  - (c) direct channel
  - (d) indirect channel
62. Process which involves controlling, implementing and planning materials and final goods to meet final customer at high profits is classified as
- (a) exclusive distribution
  - (b) exclusive dealing
  - (c) physical distribution
  - (d) supply chain management



- 63 Independent service provider of logistics who can do all functions required by clients is classified as
- (a) public held logistic provider
  - (b) privately held logistic provider
  - (c) Third party logistics provider
  - (d) single part logistics provider
- 64 If company B sell its products through retailers and wholesalers then channel used by company B is classified as
- (a) direct channel
  - (b) indirect channel
  - (c) flexible channel
  - (d) static channel
- 65 Personal selling step in which sales person asks for an order to customer is classified as
- (a) shipper approach
  - (b) handling shipment
  - (c) closing
  - (d) follow up
- 66 Sales force structure in which a sales representative works to sell specific items of product line is classified as
- (a) indirect sales force structure
  - (b) territorial sales force structure
  - (c) customer sales force structure
  - (d) product sales force structure
- 67 Third step in personal selling process after completion of pre-approach step is to
- (a) prospecting and qualifying
  - (b) handling objections
  - (c) approach
  - (d) presentation and demonstration
- 68 Step in personal selling process which consists of first meeting first meeting between customer and sales person is called
- (a) qualifying
  - (b) prospecting
  - (c) follow up

(d) approach

69. Two major factors are changing the face of today's communications. One of these factors is the fact that:

- (a) Costs of promotion are rising.
- (b) Mass markets are fragmented and marketers are shifting away from mass (c) Marketing.
- (d) Global communications are not growing rapidly enough.
- (e) Marcom managers have achieved more power and control.

70. The shift from \_\_\_\_\_ has had a dramatic impact on marketing communications.

- (a) Brand management to value management
- (b) Media manipulation to media control
- (c) Mass marketing to segmented marketing
- (d) Mass marketing to global marketing

Ans. (1)(d), (2)(a), (3)(e), (4)(b), (5)(d), (6)(a), (7)(d), (8)(d), (9)(a), (10)(b), (11)(b), (12)(b), (13)(c), (14)(d), (15)(c), (16)(c), (17)(c), (18)(d), (19)(a), (20)(c), (21)(d), (22)(d), (23)(c), (24)(b), (25)(c), (26)(d), (27)(e), (28)(c), (29)(c), (30)(b), 31(d), 32(a), 33(c), 34(d), 35(b), 36(a), 37(d), 38(c), 39(d), 40(b), (41)(a), (42)(c), (43)(d), (44)(c), (45)(d), (46)(c), (47)(d), (48)(b), (49)(d), (50)(c), 51(a), 52(a), 53(b), 54(d), 55(a), 56(a), 57(a), 58(a), 59(b), 60(d), 61(d), 62(c), 63(c), 64(b), 65(c), 66(d), 67(c), 68(d), 69(b), 70(c)

## II Short Answer Type Questions:

- 1 What are the major issues involved in developing a promotion campaign?
- 2 Enumerate the various components of communication mix
- 3 Draw a flowchart of the integrated marketing communication process.
- 4 What is the difference between Personal Selling and On-line selling?
- 5 Compare and Contrast the nature of working of a Retailer and a Wholesaler.
- 6 What do you understand by Publicity?
- 7 Enumerate the objectives of sales promotion.
- 8 Explain industrial states and telemarketing as non-traditional methods of communication.
- 9 Enumerate the components of an advertisement copy.
- 10 How can one motivate the intermediaries?
- 11 How does the nature of a product influence the choice of a particular channel of distribution?

- 12 What are the ethical issues involved in choice of an intermediary?
- 13 What factors lead to the growth of sales promotion?
- 14 Write a short note on Direct Marketing as an emerging channel of distribution.
- 15 Write a short note on the effectiveness of celebrity endorsements.
- 16 Write a short note on public relations.
- 17 What do you understand by distribution logistics?
- 18 What is the purpose of marketing communication?
- 19 Write a short note on agency payment system.
- 20 What are the necessary traits of an effective salesman?
- 21 Explain consumer promotion as a technique of sales promotion. 22 Write a brief note on channel dynamics.
- 23 “Sales promotion and Advertising are two names of the same thing’. Comment. 24 Are Publicity and Word -of- mouth Communication similar? Why or why not?
- 25 Compare a Store and a Non-Store based retailer.
- 26 What are the merits and demerits of advertising?
- 27 Write short notes (on any three)
  - a) Co-branding
  - b) Channel conflicts
  - c) Types of advertising
  - d) Non-store retailing
  - e) New trends in packaging.
- 28 Distinguish between the various elements of promotion mix.
- 29 Discuss the factors that influence channel design decisions.
- 30 When is Personal Selling more appropriate than other methods of Sales Promotion? Explain with examples.
- 31 Middlemen are parasites. This charge has been made by many over the centuries. Is this likely to be the case in a competitive economic system? Why or why not?
- 32 Define marketing management in present content
33. Distinguish between marketing and selling as the basis of (a) meaning (b) objective and (c) scope
34. Explain the factors affecting pricing of product. 5
35. Explain any six facilitating functions of Marketing.
36. Define promotion mix.
37. How personal selling is important to (a) business men (b) Customer and (c) Society
38. What is marketing mix? Explain different elements (or components) of marketing mix
- 39 Explain the various Channels of distribution
40. State briefly the objectives of Advertising

### III Long Answer Type Questions:

- 1 What do you mean by marketing communication mix? What is the role of marketing communication in today's marketing environment?
- 2 What steps should be taken ensure that the marketing communication is effective?
- 3 What do you mean by promotion mix? What are its determinants?
- 4 Explain the different elements of promotion mix. Also bring out the advantages and disadvantages of each element over the other.
- 5 What do you mean by personal selling? What are the steps in the personal selling process?
- 6 What do you mean by sales promotion? What are its types? Elaborate on some tools of trade promotion.
- 7 What in your opinion will be suitable consumer promotion scheme for branded Atta in Delhi?
- 8 What is advertising? What is the relevance of advertising in today's markets?
- 9 "Advertisements pays when business is bad and it also pays when business is good". Justify this statement with examples.
- 10 "A marketing communication must starts with a clear target audience in mind". Elaborate.
- 11 Explain the role of personnel selling in rural marketing?
- 12 Explain the concept of distribution channels. What are the functions performed by distribution channels?
- 13 What factors influence the selection of intermediaries? How can channel members be managed effectively?
- 14 Explain meaning and nature of marketing Channel?
- 15 Discuss various types of Intermediaries.
- 16 Discuss the channel functions with relevant examples 17 Discuss the factors affecting channels choice.
- 18 A large sized company is planning to introduce a range of consumer electronic products in India. Briefly discuss various decisions company needs to make in connection with the development of its channel strategy.
- 19 Explain the major considerations in the selection of a distribution channel for consumer products. What are the criteria that can be used for the evaluation of channel members? Give examples also.
- 20 GATI, the cargo services company, plans to launch 'The Millennium Parcel Express' a coenterprise between Gati and Indian Railways, that consists of a cargo train, having a capacity of 230 tonnes, specially designed to carry high-value express cargo. What do you think the promotional objective of GATI should be? Which of the promotion mix elements would be best suited to launch 'The Millennium Parcel Express'?
- 21 Fit & Fine, a leading chain of health and fitness centers brings out advertisements which say "Bring this advertisement and avail free 5kg weight loss program". What is the motive behind such promotions?

- 22 Charms Spa, a Spa chain having branches all over India is setting up its new branch at Hyderabad. As the spa concept is new to many Indian customers, it is planning to run a sales promotion campaign to attract customers and create awareness about its service offerings. What are the various sales promotion schemes that Charms Spa can adopt?
- 23 Syscom, a computer education provider operating successfully in Hyderabad is planning to expand nationally. However the company is uncertain as to whether it should adopt the direct distribution route or the franchising route. Which option will be appropriate for Syscom?
- 24 Insurance companies sell their services mainly through agents and brokers, instead of selling them through their own personnel. What are the major reasons for their adopting such a distribution strategy?
- 25 Is channel policy always determined by the manufacturer? What factors influence the selection of channel for distribution of the following products: -
- (a) Soft drinks
  - (b) Cosmetics
- 26 WestSide, a departmental store chain with 14 stores spread across the country, is planning to enter the hypermarket segment under the brand name 'Star India Bazaar'. The stores are mainly aimed at middle class customers who are cost conscious. The product range includes grocery, durables, apparels, utensils, and plastics. If you were marketing director for the company, how would you go about planning the service promotion for the hypermarket venture?
- 27 "Call Us Cabs" is a new service provider in the city. The market is already nearing saturation with the city hosting several other service providers in the same industry like "Maxi cabs", "Citi Taxi", "City Cabs", etc. What pricing strategy should the new service provider adopt for each of the stages of its life cycle?
- 28 American Pizzas, a leading fast food chain in the US, entered the Indian market through the franchising route in 1999. It replicated its American style of functioning and within one year of inception, the outlets increased from 4 to 20 and the company recorded sales revenue of Rs 50 crore. However, with increasing competition from other US fast food chains and local players, sales have dipped drastically. The company's in-house study revealed that the low motivational levels of the franchisees and poor service quality were the main factors for the poor performance. Suggest an intermediary management strategy that will help American Pizzas resurrect sales in India.
- 29 Pantaloon Retail India Ltd, a leading retailer in India with brands Pantaloons, Big Bazaar, Food Bazaar, and Gold Bazaar, has recently entered into mall management services by opening a chain of malls in various cities under the brand 'Central'. It leases its mall to various consumer product manufacturers and service providers. In November 2004, it opened 'Hyderabad Central' with an investment of Rs 70 crore. While deciding the leasing rate for the stores in the mall, what pricing objective will Pantaloon seek to implement?

- 30 ABN-Amro Bank has surprised the banking industry by announcing the lowest interest rate of 6.5% for its housing loans, which is 1% less than what other banks are offering. What kind of pricing strategy has ABN-Amro Bank adopted in this case? Describe the pricing strategy.
- 31 IndiaTV is a new Hindi news channel launched in the cluttered Indian television channel market with well-entrenched names like NDTV, ZeeNews, Aajtak, and StarNews. Mr.Rajat Sharma the head of IndiaTV wants to establish the channel as a “mouthpiece of the common man.” As the channel is free-to-air, its only source of revenue is advertising. Therefore, while pricing the advertising space in the channel what are various factors that the channel management must keep in mind?
- 32 Assure USA a leading insurance company in the US has established its BPO subsidiary in India for managing its inbound and outbound telemarketing activities. However, the company received complaints from customers regarding poor customer service and improper response at the Indian subsidiary. What may be the factors that are responsible for such poor communication process?
- 33 (a) What factors must be considered in the selection of marketing channels? (b)A new firm is designing and marking trendy and highly stylish women’s clothing. Should the firm establish a website to sell its products?
- 34 Discuss the major objectives of Sales Promotion. As a marketer of a leading consumer durable company. When do you consider it an appropriate time to organize such promotions and why?
- 35 (a) “Advertising is a waste of consumers’ money.” Do you agree? Why?  
(b)Explain the objectives of and types of consumer sales promotions commonly used in the fast-moving consumer goods category.
- 36 (a) “Marketing channels play an important role in delivering value to customers.” Explain.  
(b) Explain how product and distribution strategies are being adapted by marketers to tap rural markets.
- 37 Discuss the benefits for branding and explain the various branding strategies available to the marketers. Give examples to illustrate.
- 38 Explain the significance of IMC and describe the characteristics of any four elements of the communication mix. Select any brand and explain the different forms of communication it has used.
- 39 You are the marketing manager of Citi Bank’s Online Banking Division. How would you provide the concepts of providing customer satisfaction and customer retention to designing and marketing effective online banking?
- 40 Explain the promotional strategy that you would use during the Growth and Maturity stages of the following products :
- (i) Men's shoes (footwear)
  - (ii) Laptops

- 41 (a) Explain various functions performed by distribution channel intermediaries.  
 (b) What are the various factors taken into consideration at the time of establishing a distribution channel? Discuss in brief.
42. Read the case given below and answer the questions given at the end.

For many years McDonald's enjoyed worldwide success built on a few well-known, highly standard conditions. The company with the golden arches served a simple menu — hamburgers, French fries, and milk-shakes or soft drinks. The food was priced low, its quality was consistent, and it was served speedily from establishments that all looked alike and were extremely clean.

In recent years, however, McDonald's has seen its growth rate slow down and its dominant market position slip. Why? The changes that have been occurring in the company's external environment.

Let's start with the population scene. For many years McDonald's main customer group was young couples with several kids. Today, people are marrying at a much later age and families have fewer children. So McDonald's traditional customer base is eroding. Then there are the cultural changes. Also consumers have become more health conscious. Let's face it — burgers, fries and shakes (the foundation of McDonald's success) are not exactly at the top of the dietitian's menu recommendations today.

Consumers want convenience. In the past, they hopped in the car and drove to McDonald's. Today they can pop something into the microwave oven or phone Domino's to have a pizza delivered. Another challenge came as consumers became more concerned about their physical environment. McDonald's polystyrene hamburger packaging was attacked by people who demand the use of recycled and/or biodegradable products. Paralleling all these challenges were the growing number and effectiveness of competitors.

Questions :

- (a) List out and discuss the major environmental changes being faced by McDonald's.  
 (b) What should be the course of action to regain its dominant market position and to tackle competition?
- 43 You are advertising manager of organization producing refined oil. Which media will you choose to advertise your product and why?  
 44. Explain the functions of marketing.  
 45. Are the critics really justified in raising objections to advertising?  
 46. Explain the importance of personal selling.  
 47. State any four advantages of branding.

48. What are the major activities involved in physical distribution of goods.
49. Explain the role of marketing in Indian economy.
50. Explain three functions of labeling.
51. Explain the functions of packing
52. With examples of your choice, show the usefulness of the following: (a) Brand advertising; (b) Corporate advertising; (c) Generic advertising.
53. Outline some of the major sales promotion tools available to the marketer.
- 54 Which 'publics' might a public relations campaign be aimed at?
55. Give examples of each of the following: (a) Advertisements using the USP; (b) Advertisements based on 'imagery'; (c) Advertisements using rationality as the main motivator.
56. To what extent do you believe that below-the-line promotions are particularly useful in encouraging impulse purchases?

#### **UNIT- IV**

##### **I Test Your Skills:**

##### **(a) State Whether the Following Statements are True or False:**

- 1 Tele- marketing is a method of direct selling.
- 2 Entrepreneurs require huge investment for direct marketing.
- 3 In mail order sales, customers do visit the seller's business premises personally. 4 Distribution costs in developing the rural market is low.
- 5 For success in rural marketing, packaging should be simpler and more functional than ornamental.
- 6 Reaching the rural consumer is a major constraint in rural marketing.
- 7 The duty to make consumers aware of his rights and remedies available fall under the right to consumer education.
- 8 National commission, machinery for redressal of consumer grievances is set up by state government.
- 9 Green marketing encourages of use of environment friendly products.
- 10 The law of the deed end street says: Attract visitors to your site by giving away something free and then try to sell something additional to those who visit.

Ans. (1)(T), (2)(F), (3)(F), (4)(F), (5)(T), (6)(T), (7)(T), (8)(F), (9)(T), (10)(F)

##### **(b) Multiple Choice Questions:**



- 1 Direct marketing provides customers with
  - (a) Standard Product
  - (b) Customized Marketing Offering
  - (c) None of the above
  
- 2 Problems in Rural Marketing are:
  - (a) Illiteracy and Media Habits
  - (b) Inadequate Infrastructural Facilities
  - (c) High initial market development expenditure
  - (d) All of the above
  
- 3 The benefits of consumer education to society includes:
  - (a) Customer satisfaction
  - (b) An increase in sales
  - (c) Encourages citizen awareness
  
- 4 When a car dealer complains to the manufacturer that another dealer of the same make of cars is selling outside their assigned territories, it is a type of
  - (a) Parallel conflict
  - (b) Customer-service conflict
  - (c) Vertical conflict
  - (d) Horizontal conflict (e) Multi-level conflict.
  
- 5 When a seller requires that a dealer not handle competitors' products, the agreement is called a/an
  - (a) Exclusive distribution
  - (b) Exclusive dealing
  - (c) Control criterion
  - (d) Dual distribution
  - (e) Dealer's rights.
  
- 6 Which of the following statements about retailing is not true?
  - (a) Retailing involves selling to final consumers
  - (b) Retailing is a major industry
  - (c) Manufacturers and wholesalers never make retail sales
  - (d) Retail sales may be done by person, mail, telephone, vending machines or from a Web site
  - (e) Technology advancement constitutes an uncontrollable element in retailing.
  
7. A Brazilian NGO Reciclar-t3 makes clothes out of recycled clothes. This is an example of

- (a) Blue marketing
  - (b) Green marketing
  - (c) Community relations (d) Value added engineering (e) Global warming.
8. The reseller market mainly consists of
- (a) Consumers
  - (b) Manufacturers
  - (c) Wholesalers and retailers
  - (d) Industrial users (e) Government.
9. A branded, high volume, low value consumer good is most likely to be sold through which of the following types of distribution channels?
- (a) Direct sale from the manufacturer to consumer
  - (b) Sale through brokers
  - (c) Sale through specialist retail outlets
  - (d) Sale through many general retail outlets
  - (e) Directly from the wholesalers without retailers.
10. Airline travel is very price competitive. People will switch airlines if the price of a round-trip ticket is lower on one airline than another. This is an example of
- (a) Pure competition
  - (b) Monopolistic competition
  - (c) Pure monopoly
  - (d) Brand Mindset
  - (e) Oligopolistic competition.
11. Which of the following describes the use of electronic means and platforms to conduct a company's business? (a) E-tailing
- (b) E-purchasing
  - (c) E-business (d) E-marketing (e) E-mail.
12. The shift in marketing from trying to maximize profit on individual transactions to maximizing mutually beneficial relationships with consumers and others is called
- (a) Sales marketing
  - (b) Production marketing
  - (c) Mega marketing (d) Relationship marketing (e) Proactive marketing.
13. "Friends don't let friends drive drunk" is an example of
- (a) Niche marketing
  - (b) Social marketing

- (c) Selling (d) Advertising (e) Sales promotion.
14. When a company stocks the product in as many outlets as possible, it is using
- (a) Selective distribution
  - (b) Convenience-based distribution
  - (c) Exclusive distribution
  - (d) Intensive distribution (e) Warehousing.
15. When a service firm effectively trains and motivates its customer-contact employees and the support personnel to work as a team to provide customer satisfaction, it is practicing
- (a) Results-oriented marketing
  - (b) Internal marketing
  - (c) Interactive marketing
  - (d) Marketing myopia (e) Captive marketing.
16. Which of the following are runner-up companies that aggressively attack competitors to get more market share? (a) Market leaders
- (b) Market challengers
  - (c) Market followers (d) Market nichers (e) Market penetrator.
17. From a buyer's viewpoint, which of the following elements of the market mix is designed to provide convenience of purchase?
- (a) People
  - (b) Product
  - (c) Promotion (d) Process (e) Place.
18. Walt Disney originated as an animated film producer and moved into licensing characters for merchandised goods, entering the broadcast industry with its own Disney channel and also developed theme parks and vacation and resort properties, this is a form of a
- (a) Downsizing businesses
  - (b) Divesting older businesses
  - (c) Integrative growth
  - (d) Intensive growth
  - (e) Diversification growth
19. Bata Shoe Company sells its products through its own chain of retail showrooms/outlets. Which of the following marketing strategies does Bata employ?
- (a) Backward integration
  - (b) Forward integration
  - (c) Horizontal integration (d) Diversified strategy (e) Concentration.

20. RPG's *Giant* is the first of its kind to be set up in India.
- (a) Supermarket
  - (b) Discount store
  - (c) Specialty store
  - (d) Hypermarket (e) Department store.
21. General Electric sells large home appliances both through independent retailers (Department stores and discount houses) and directly to large housing-tract builders. This is an example of
- (a) Intensive distribution
  - (b) Selective distribution
  - (c) Exclusive distribution
  - (d) Dual distribution
22. When IBM and Apple Computer announced a joint operation to develop a new computer operating system, it was an example of a (n) (a) Corporate marketing system
- (b) Administered marketing system
  - (c) Conglomerate marketing system (d) Horizontal marketing system (e) Contractual marketing system.
23. Klean Detergent is the market leader of detergents and is in the maturity stage of its life cycle. There are many competitors in the market that challenge Klean's leadership. Which of the following statements is most likely true about Klean's pricing?
- (a) As a market leader, Klean does not need to worry about price
  - (b) Klean uses price promotion in order to maintain its market leadership
  - (c) Klean must price lower than the other brands to maintain its leadership
  - (d) Klean can increase its price since it is in the maturity stage
  - (e) Klean should maintain a high price to maintain a high quality image.
24. Forecasting or estimating the actual size of a market is often a key goal in a marketing research study. Good sales forecasts are important for a firm as it schedules production. Which of the following statements about sales forecasting is true?
- (a) The most expensive forms of sales forecasting are trend extrapolation and a survey of experts
  - (b) With the lost-horse forecast, former customers are asked if they are likely to buy the product again
  - (c) A lost-horse survey is more expensive to conduct than a survey of buyers' intentions
  - (d) Trend extrapolation is the easiest method of sales forecasting
  - (e) A sales force survey forecast is less expensive to conduct than trend extrapolation.

25. To facilitate self-checkout, a food-retailing store has instituted electronic machines for use by its customers. These machines are examples of
- (a) Vending Machines
  - (b) Online retailing
  - (c) Video texts (d) Direct Mail (e) Kiosks.
26. A branded, high volume, low value consumer good is most likely to be sold through which of the following types of distribution channel?
- (a) Direct sale from the manufacturer to consumer
  - (b) Sale through brokers
  - (c) Sale through many general retail outlets (d) Sale through specialist retail outlets (e) Sale through discount stores.
27. Italian eyewear maker Luxottica sells its many famous eyewear brands-including Giorgio Armani, Yves Saint Laurent and Ray Ban- through the world's largest optical chain, Lens Crafters which it also owns. Luxottica therefore follows
- (a) Corporate VMS
  - (b) Contractual VMS
  - (c) Franchise Organization
  - (d) Administered VMS
  - (e) None of the above
28. Toothpaste, Candy and other similar items are sold in millions of outlets to provide maximum brand exposure and consumer convenience, this is form of
- (a) Exclusive distribution
  - (b) Selective distribution
  - (c) Intensive distribution
  - (d) Direct distribution
  - (e) Industrial distribution
29. A company that produces and heavily markets cigarettes, with many promotions aimed at young (although legal age) nonsmokers, most likely follows which of the following as a guiding principle?
- (a) the philosophy of consumer-oriented marketing
  - (b) the philosophy of consumerism
  - (c) the philosophy that companies can do in good conscience whatever the market and legal systems allow
  - (d) the philosophy that companies should have a social conscience

- (e) the philosophy of enlightened marketing
30. Consumer advocates call for all of the following additional consumer rights except which one?
- (a) The right to be protected against questionable products and marketing practices.
  - (b) The right to be well informed about important product aspects.
  - (c) The right to influence products in ways that will improve the quality of life.
  - (d) The right to influence marketing practices in ways that will improve the quality of life.
  - (e) The right to be protected from unwanted marketing messages.
31. If there is low involvement and the product/market is established then sale promotions should be used for:
- (a) Loyal to increase loyalty
  - (b) Loyal to reward and increase usage
  - (c) Loyal to encourage trial
  - (d) All to block out the competition
32. Building long-term relationships with customers is essential for any business. The application of technology to achieve CRM is a key element of e-business but what does CRM stand for?
- (a) Customer relationship management
  - (b) Customer resource management
  - (c) Consumer relationship management
  - (d) Customer retailing management
33. Using the Internet for relationship marketing involves integrating the customer database with websites to make the relationship targeted and personalized. Through doing this there are many benefits to be gained but which of the below is not an advantage?
- (a) Achieve mass customization of the marketing messages
  - (b) Targeting more effectively

- (c)
  - (d) Minimises breadth, depth and nature of relationship Lower costs
34. A marketing campaign will not be successful if the costs of acquiring site visitors and \_\_\_\_\_ customers are too high. The term used to describe the cost of acquiring a new customer is known as:
- (a) Cost per acquisition
  - (b) Bounce rate
  - (c) Allowable cost per acquisition
  - (d) Referrer cost
35. Generally speaking, a department store salesperson that stands behind a counter is \_\_\_\_\_ classified as a(n):
- (a). order getter.
  - (b). order taker.
  - (c). creative selling person.
  - (d). missionary salesperson.
36. Which is direct communications with carefully targeted individual consumers to obtain an immediate response. (a). Direct marketing
- (b). Mass marketing
  - (c). Integrated marketing
  - (d). Demand marketing
37. The concept of which marketing term accepts the limitations of marketing philosophy, acknowledging the need to impose regulatory constraints on the market mechanism in \_\_\_\_\_ economic development (van Dam and Apeldoorn, 1996), particularly the impact of \_\_\_\_\_ marketing activity on the environment.
- (a). Sustainable marketing
  - (b). Green marketing
  - (c). Relationship marketing
  - (d). Ethics
38. Sustainable marketing can also be characterized as the 'third age' of which concept:
- (a). planned obsolescence
  - (b). green marketing

- (c)
  - (d)
  - (c). pollution
  - (d). recycling
39. Companies collude over production quotas, companies abuse their monopoly status, and companies overcharge or exploit their supply chain partners. These are examples of ethical breaches in: (a) Promotion.
- (b) Distribution management.
  - Products. Process.
40. This branch of ethics stresses the importance of developing virtuous principles, with 'right' character, and the pursuit of a virtuous life: (a) Virtue ethics.
- (b) Utilitarianism.
  - (c) Normative ethics.
  - (d) Teleological ethics
41. The kind of marketing through which company connect with targeted segments on one to one interaction basis is classified as
- (a) event marketing
  - (b) stress marketing
  - (c) direct marketing
  - (d) indirect marketing
42. The direct marketing through which products are sold directly to customer on phone call is classified as
- (a) Viral Marketing
  - (b) telephone marketing
  - (c) online marketing
  - (d) offline marketing
43. The kind of online marketing domain which is initiated by consumers to target the consumers is classified as
- (a) consumer to business domain
  - (b) consumer to consumer domain
  - (c) business to consumer domain



- (c)
  - (d)
  - (d) business to business domain
44. The marketing in which product is described to customers with air television spots providing \_\_\_\_\_ customers with toll free numbers or Website to order is called
- (a) kiosk marketing
  - (b) offline marketing
  - (c) telephone marketing
  - (d) direct response TV marketing
45. The kind of online marketing domain which is initiated by business to target consumers is \_\_\_\_\_ classified as
- (a) business to consumer domain
  - (b) business to business domain
  - consumer to business domain
  - consumer to consumer domain
46. The kind of advertising that appears while consumers are browsing internet such as search \_\_\_\_\_ related ads, online classifieds and display ads is classified as
- (a) inbound advertising
  - (b) outbound advertising
  - (c) online advertising
  - (d) buzz advertising
47. The marketing of products done by companies by placing ordering and information machines \_\_\_\_\_ is called
- (a) kiosk marketing
  - (b) offline marketing
  - (c) telephone marketing
  - (d) direct response TV marketing
48. The companies that buy and sell only on the internet are classified as
- (a) premium companies
  - (b) direct companies
  - (c) click only companies
  - (d) click and mortar companies

- (c)
- (d)
- 49. The group of online social communities such as virtual worlds, social networking sites and                blogs where people exchange opinions is classified as
  - (a)     inbound social networks
  - (b)     outbound social networks
  - (c)     offline social networks
  - (d)     online social networks
  
- 50. The web of computer networks that connects users from all around the world to interact with                each other is classified as
  - (a)     interactive net
  - (b)     internet
  - (c)     intranet
  - (d)     extranet
  
- 51. 140. ----- is not a consumer promotion scheme
  - (a)     Samples
  - (b)     Advertising material
  - (c)     Coupons
  - (d)     Rebates

52. In ----- appeals are emotional
- (a) Consumer promotion
  - (b) Advertising
  - (c) Dealer Promotion
  - (d) All of these
53. -----is not a dealer promotion scheme.
- (a) Free goods
  - (b) Trade allowance
  - (c) Coupons
  - (d) All of these
54. ----- is not a sales force promotion scheme.
- (a) Bonus to sales force
  - (b) Slotting allowance
  - (c) Sales force contests
  - (d) None of these
54. Dealer promotion is also known as
- (a) Trade promotion
  - (b) Goods promotion
  - (c) Commerce promotion
  - (d) None of these
55. Which of the following is not an element of promotion mix
- (a) Advertisement
  - (b) Branding
  - (c) Personal selling (d) Sales promotion
56. -----type of advertisement is used when the product enters into growth stage of PLC
- (a) Selective advertising
  - (b) Reminder advertising
  - (c) Primary advertising
  - (d) None of these

57. The strategy of choosing one attribute to excel to create competitive advantage is known as
- (a) Under positioning
  - (b) Unique selling proposition
  - (c) Over positioning
  - (d) None of these
58. The Concept of USP was introduced by
- (a) Rosser Reeves
  - (b) Theodore Levitt
  - (c) NH Borden
  - (d) None of them
59. Which of the following is not a sales promotion tool
- (a) Discount
  - (b) Dealer contest (c) Advertisement (d) Consumer contest.
60. The process of direct communication between the sales person and a prospect is called
- (a) Personal selling
  - (b) Direct marketing
  - (c) Advertising
  - (d) None of these
61. Pointing out the high cost of research and development efforts for new products like prescription drugs or high technology items is among the responses marketers provide in answer to which of the following criticisms of marketing?
- (a) high costs of distribution
  - (b) high advertising and promotion costs
  - (c) excessive markups
  - (d) excessive demand
62. Falsely advertising “factory” or “wholesale” prices or a large price reduction from a phony high retail price is an example of
- (a) Deceptive promotion
  - (b) Deceptive packaging
  - (c) Deceptive pricing

- (d) Deceptive cost structure
63. Claiming a “wholesale price” as a reduction from a phony high list price is a form of (a) deceptive pricing.  
(b) deceptive promotion. (c) deceptive packaging.  
(d) high pressure selling.
64. overstating the product’s features or performance, would be a case of  
(a) Deceptive promotion  
(b) Deceptive packaging  
(c) Deceptive pricing  
(d) Deceptive cost structure)
65. All of the following are criticisms leveled at marketing from society’s viewpoint EXCEPT:  
(a) too many jobs without regulation of activities.  
(b) false wants and too much materialism.  
(c) too few social goods.  
(d) cultural pollution.
- 66 “Greed is good” and “Shop ‘till you drop” are slogans that might characterize which of the following social criticisms leveled at marketing?  
(a) false wants and too much materialism  
(b) too few social goods  
(c) cultural pollution  
(d) too much political power
- 67 Concept of logistics which focuses on teamwork in whole supply chain management to maximize performance of a distribution system is classified as  
(a) integrated logistics management  
(b) intermodal logistics management  
(c) intra-modal logistics management  
(d) exclusive logistics management
68. Claiming a “wholesale price” as a reduction from a phony high list price is a form of  
(a) deceptive pricing.  
(b) deceptive promotion.  
(c) deceptive packaging.  
(d) high pressure selling.:

69. overstating the product's features or performance, would be a case of

- (a) Deceptive promotion
- (b) Deceptive packaging
- (c) Deceptive pricing
- (d) Deceptive cost structure

70 All of the following are criticisms leveled at marketing from society's viewpoint EXCEPT:

- (a) too many jobs without regulation of activities.
- (b) false wants and too much materialism.
- (c) too few social goods. (d) cultural pollution.

**Ans.** (1)(b), (2)(d), (3)(c), (4)(d), (5)(d), (6)(c), (7)(b), (8)(c), (9)(d), (10)(e), (11)(c), (12)(c), (13)(b), (14)(d), (15)(d), (16)(b), (17)(e), (18)(e), (19)(b), (20)(d), (21)(d), (22)(d), (23)(b), (24)(e), (25)(e), (26)(c), (27)(a), (28)(c), (29)(c), (30)(e), (31)(b), (32)(c), (33)(c), (34)(a), (35)(b), (36)(a), (37)(a), (38)(b), (39)(b), (40)(a), (41)(c), (42)(b), (43)(b), (44)(d), (45)(c), (46)(c), (47)(a), (48)(c), (49)(d), (50)(b), (51)(b), (52)(c), (53)(b), (54)(a), (55)(b), (56)(a), (57)(b), (58)(a), (59)(c), (60)(a), (61)(a), (62)(g), (63)(a), (64)(a), (65)(a), (66)(a), (67)(a), (69)(a), (70)(a)

(c) **Fill in the Blanks:**

- 1 Direct customer marketing system allows complete \_\_\_\_\_ to purchase products.
- 2 Directing marketing is seen as \_\_\_\_\_ with existing intermediaries.
- 3 The rural market is made of two broad areas which are \_\_\_\_\_ and \_\_\_\_\_.
- 4 \_\_\_\_\_ and \_\_\_\_\_ contribute to purchasing capacity in rural areas.
- 5 The State Commission for Consumer Protection Act shall consist of a President who either is or has been a \_\_\_\_\_ and \_\_\_\_\_.
- 6 The benefit of consumer iducal to individual is it \_\_\_\_\_.
- 7 The data based application and application for sharing information within the organization are \_\_\_\_\_.

**Ans.** (1)(Flexibility), (2)(Competing), (3)(The market for consumption on goods and the market for agriculture inputs), (4)(Government Expenditure and Dispersal of Industry), (5) Sedge of a High Court & Other two members), (6)(Improves the availability of life), (7)(Net worked application)

## II Short Answer Type Question:

- 1 Discuss the advantages and two disadvantages of Direct Marketing? 2 Explain the terms – Consumer and Consumerism.
- 3 Write a short note on ‘Right to Information’.
- 4 How is a Consumer different from Customer?
- 5 What are the responsibilities of the consumers?
- 6 What are the three basic properties of Direct Marketing?
- 7 Briefly describe the challenges of Rural Marketing
- 8 Discuss the salient features of the Consumer Protection Act, 1986.
- 9 Discuss the advantages of being Consumer-oriented in today’s marketing era.
- 10 Define Niche Rural Marketing Strategies.
- 11 What are the advantages and disadvantages of branding in rural market?
- 12 Discuss “The law of pull and push” in context of Internet Marketing.
- 13 How can you differentiate “The Law of Niche” from “The Law of Giving and Selling”?
- 14 Explain the “Green Marketing”. What are its advantages? 15 Distinguish between rural markets and urban markets.
- 16 What are the most effective direct marketing techniques?
- 17 What is the most important word in direct marketing?
- 18 What is Umbrella Marketing? Name 3 Products of HLL which comes under Umbrella Marketing?
- 19 How is Online Marketing different from Direct Marketing?
20. Write notes on the following:-
  - i. Concept testing, product testing and Test marketing. Give examples.
  - ii. Characteristics of business-to-business markets.
21. (a) Briefly explain the various pricing methods available for Indian marketers, with suitable illustrations.  
(b) Discuss the variables that affect the distribution decision for the following :
  - (i) Fast food joint restaurant
  - (ii) Personal Computers
22. Why and how do psychological factors influence consumer buying behaviour ? As a potential buyer of a latest brand of DVD, briefly explain the social and cultural factors that affect your buying decision.

23. (a) Discuss the major objectives of Sales Promotion. As a marketer of a leading consumer durable company, when do you consider it an appropriate time to organise such promotions and why ?
- (b) Personal Selling and Advertising are the two major vehicles of communication for marketing industrial products. Discuss with a suitable example of your choice.
24. Write notes on any three of the following :
- (a) PLC as a tool for market development
- (b) Matrix organisation
- (c) Bases for Segmentation
- (d) Approaches to Sales forecasting
- (e) Limitations of Cyber marketing
25. What are the main elements of the communications process?
26. Briefly the key steps in the planning of marketing communications strategies
27. Explain difference between advertising and sales promotion with suitable examples
28. What are the major criticisms against? Explain
29. Why direct marketing has become an important tool of marketing promotion in present days? Explain

### III Long Answer Type Question:

1. Direct selling is a two-way communication best suited to a company marketing consumer products with a poor brand loyalty. Discuss.
2. For selling, FMCG in today's context, Examine the role of direct selling as a tool of direct marketing.
3. Enumerate and discuss the direct marketing strategies for the following
- (a) FMCG Company
- (b) Indian Airlines
- (c) Santro Car
4. With suitable examples, distinguish between "Distribution Channels" and "Distribution Logistics" for rural market. Briefly describe the role of warehousing in this context.
5. How will you segment the rural markets in the case of the following products:
- (a) Fair and Lovely cream
- (b) Hajmola
- (c) TajMahal Tea
- (d) Nirma Detergent Powder
6. "Indian rural culture is entirely different from west but still we accept western products and we appreciate their culture also". Discuss in detail.



- 7 Enumerate the different types of rural buyer characteristics. Elucidate them with examples from real life situations.
- 8 What are the different ways of segmenting a rural market? What bases would you choose for marketing T.V. sets in rural India?
- 9 “An educated buyer makes a better buyer”. Discuss the implication of this statement.
- 10 Why do you think the concept of consumerism is getting so much attention these days? What is the state of consumerism in India?
- 11 In the summer of 1998, Mr. Sood brought a cooler from a local manufacturer. After about a week, he realized that the pump of the cooler was not able to suck water properly. As a result the house was not getting cooled.  
Discuss that which right of Mr. Sood has been violated and how under the Consumer Protection Act, 1986 can he go about fighting the case?
- 12 Explain the importance of the right to consumer (a) Education  
(b) Explain how can consumer complaints be a useful asset for a business organization?
- 13 How being responsive to consumer issues helps the business organization? Discuss in detail.
- 14 What are the factors that influence the IT enabled marketing environment of an organization?
- 15 “The Indian Market is gradually becoming consumer oriented”. Discuss the statement with reference to consumerism.
- 16 Do you agree that “Consumer and the IT Enabled Environment are mutually inclusive.” One cannot exist without the other. Explain with suitable examples.
- 17 As a consumer try to think how your right has been violated and what steps have been taken by you.
- 18 Sales promotion is an important tool for  
(a) Increasing sales. Explain the relevant tools which can be used in rural marketing.  
(b) Explain the problem of Rural banking with example.
- 19 Your company has recently launched a range of technically superior television sets in rural market. The constraint that you face the favor of incurring huge advertising expenditure. Suggest the route you will take in your advertising planning.
- 20 Use of plastic bags for shopping purpose is not desirable because it is not an environmental friendly behavior. In order to bring the plastic bag usage, down from its present level on would need to bring about the change in user’s attitude towards plastic bags. How can the attitude change be brought about? Use attitude framework and recommend strategy.
- 21 Write short notes on any two of the following:  
(a) Impact of Social weblogs on consumer buying behavior  
(b) Rural Marketing  
(c) Limitations of cyber marketing  
(d) Price wars

22 Discuss the reasons for companies to engage in green marketing. Briefly describe five green marketing initiatives being undertaken by companies in India. 23 Write note on any two:

- (a) Positioning Errors
- (b) Transaction versus relationship selling
- (c) Pros and cons of test marketing
- (d) Cause related marketing

24 Why do we use direct marketing? How do we measure the results of direct marketing? 25 What are the various macro variables of the marketing environment? How do these variables influence the four P's of marketing? Give examples.

26 How the organizations procure the required inputs from the suppliers. Explain in detail the entire process of organizational buying behavior.

28 Explain in detail the term Viral Marketing? How it is different from Retail Marketing?

29 What is green marketing? What are the major reasons that influence organizations to adopt green marketing? Give example to illustrate your example.

30 Study the case given below and answer the questions given at the end. BPL has launched the digital camera VPC-G200EX at Rs. 39,000. It does not require conventional films as it can store images in its memory. A niche segment of PC users, journalists, multimedia agencies, architects, doctors and professionals are the primary segments for the product. The benefits of the product include viewing pictures on a builtin LCD screen, and the voice memo (6 seconds) that could be added to every picture. Web page designers could have pictures on the Internet through their personal computers. These images could also be retouched or modified using appropriate software. Photo albums can be created on floppies. The product may compete with scanners which could scan conventional photographs into a computer. BPL has positioned the product as 'future of photography'. The product is available in 25 showrooms of BPL- Phillips, a competing brand, has also launched digital cameras.

### Questions:

- 31 (a) Who, in your view, would be the most appropriate target consumers for the product and why?  
(b) Outline suitable promotion and positioning strategies for the product.
- 32 How is Digital Marketing different from interactive and Internet Marketing? Explain
- 33 What is meant by social Web marketing? What are its four main characteristics? Discuss
- 34 Compare and contrast the difference between the Pull and Push approaches to Digital Marketing
- 35 How are ethics defined in marketing? What role does ethics play in the marketing decision making process?
- 36 Do ethics play any role in the i) pricing and ii) distribution of goods and services? What are the key ethical considerations when pricing and distribution of goods and services