KARPAGAM ACADEMY OF HIGHER EDUCATION
(Established Under section 3 of the UGC Act, 1956)
Pollachi Main Road, Eachanari (Post),
Coimbatore – 641 021.

DEPARTMENT OF COMMERCE

List of Practical

SUBJECT CODE: 16BPU611A

SUBJECT NAME: FINANCIAL MANAGEMENT (PRACTICAL)

1. Preparation of capital budgeting process in a industry.
2. Evaluation of risk-return analysis of a company.
3. Estimation of components of Cost of Capital of a new started business.
4. Evaluate theories of capital structure with an analysis of a company.
5. Comparison of IRR and NPV techniques of an organization.
6. Preparation of dividend policy in current corporate practice of a company.
7. Collection of difference source of long term and short term financing of a business unit.
8. Preparation of the principal yardsticks for measuring financial characteristics of investment proposal.
9. Evaluation of different methods used for ranking of investment proposal.
10. Choose any MNC and analyze the cost of capital and leverages.
11. Collection of the source of working capital of a new starting business.
12. Choose any company, Evaluate working capital management and give suitable suggestions.

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LECTURE PLAN
DEPARTMENT OF COMMERCE

STAFF NAME: T.N.P.NALINI
SUBJECT NAME: FINANICIAL MANAGEMENT - PRATICAL
SUB.CODE: 16BPU611A
SEMESTER: VI
CLASS: III B.COM[BPS]

EX.NO:I

S. No.	Lecture Duration Period	Topics to be Covered
1	1	To prepare the capital budgeting process in an industry.
2	1	To prepare the capital budgeting process in an industry.
Total No of Hours Planned For Ex.No:1=2		

EX.NO:II

S. No.	Lecture Duration Period	Topics to be Covered
1	1	Evaluation of risk-return analysis of a company
2	1	Evaluation of risk-return analysis of a company
Total No of Hours Planned For Ex.No:2=2		

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EX.NO:III

S. No.	Lecture Duration Period	Topics to be Covered
1	1	To estimate the components of cost of capital of a new started business.
2	1	To estimate the components of cost of capital of a new started business.
Total No of Hours Planned For Ex.No:3=2		

EX.NO:IV

S. No.	Lecture Duration Period	Topics to be Covered
1	1	To evaluate theories of capital structure with an analysis of a company
2	1	To evaluate theories of capital structure with an analysis of a company
3	1	To evaluate theories of capital structure with an analysis of a company
Total No of Hours Planned For Ex.No:4=3		

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EX.NO:V

S. No.	Lecture Duration Period	Topics to be Covered
1	1	To compare IRR and NPV techniques of an organization
2	1	To compare IRR and NPV techniques of an organization
Total No of Hours Planned For Ex.No:5=2		

EX.NO:VI

S. No.	Lecture Duration Period	Topics to be Covered
1	1	To prepare the dividend policy in current corporate practice of a company.
2	1	To prepare the dividend policy in current corporate practice of a company
Total No of Hours Planned For Ex.No:6=2		

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EX.NO:VII

S. No.	Lecture Duration Period	Topics to be Covered
1	1	To collect the difference source of long and short term financing of the business unit
2	1	To collect the difference source of long and short term financing of the business unit
Total No of Hours Planned For Ex.No:7=2		

EX.NO:VIII

S. No.	Lecture Duration Period	Topics to be Covered
1	1	To prepare the principal yardsticks for measuring financial characteristics of investment proposal
2	1	To prepare the principal yardsticks for measuring financial characteristics of investment proposal
Total No of Hours Planned For Ex.No:8=2		

EX.NO:IX

S. No.	Lecture Duration Period	Topics to be Covered
1	1	To evaluate different methods used for ranking of investment proposal
2	1	To evaluate different methods used for ranking of investment proposal
Total No of Hours Planned For Ex.No:9=2		

EX.NO:X

S. No.	Lecture Duration Period	Topics to be Covered
1	1	To prepare cost of capital and leverages for an MNC
2	1	To prepare cost of capital and leverages for an MNC
Total No of Hours Planned For Ex.No:10=2		

EX.NO:XI

S. No.	Lecture Duration Period	Topics to be Covered
1	1	To collect the source of working capital of a new starting business
2	1	To collect the source of working capital of a new starting business
Total No of Hours Planned For Ex.No:11=2		

EX.NO:XII

S. No.	Lecture Duration Period	Topics to be Covered
1	1	To evaluate working capital management and give suggestion for a company
2	1	To evaluate working capital management and give suggestion for a company
Total No of Hours Planned For Ex.No:12=2		

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SUPPORT MATERIALS

Text Book:

1. S.N.Maheswari.(2014). *Financial Management- Principles and practices,* [14th Edition] , New Delhi: Sultan Chand & Sons.

Reference Books:

1. James C. Van Horne and Sanjay Dhamija. (2012). *Financial Management and Policy* [12th Ed], New Delhi, Pearson Education.
2. Levy H. and M. Sarnat (2004). *Principles of Financial Management* New Delhi, Pearson Education.
3. Joy, O.M.(2007). *Introduction to Financial Management*. New Delhi, TataMc Graw Hill Education
4. Singh, J.K .*Financial Management-text and Problems* [2nd Ed] New Delhi, Dhanpat Rai and Company.
5. Rustagi, R.P. *Fundamentals of Financial Management*. New Delhi, Taxmann Publication Pvt. Ltd.

Ex no: 1 Preparation of capital budgeting process in a industry.

Date :

Aim:

To prepare capital budgeting process in an industry.

Procedure:

1.Identification of investment proposal:

The first step in the capital budgeting process is the conception of a profit making idea. The investment proposal of various types may originate at different levels within a firm, depending on their nature.

2.Screening the proposals:

In large organization, the capital expenditure planning committee is established to screen the various proposal received from different department heads.

3.Project evaluation:

The following are some of the technique used to evaluate the financial aspect of the project

a) Pay back method

b) Discounted cash flow method

c) Accounting rate of return

4.Establishing priorities:

After evaluation, the uneconomic or unprofitable proposal should be rejected. But it may not be possible for a firm.

5.Final approval:

Proposal finally recommended by the committee are sent to the top management along with the detailed report, both of capital expenditure and of sources of funds to meet them.

6.Implementation:

While implementing the project, it is better to assign responsibilities to project management for completing the project within the given frame and the cost limit.

7.Performance review:

⇨

The last stag in the process of capital budgeting is the evaluation of the performance of the project performance review or post completion audit is a feed back device.

- Pay back period method:

A project requires Rs.20000 as initial investment that will generate a cash inflow of Rs.5000 for 10 years. The pay back period will be 4 years , calculated as follows:

Pay back period=Initial investment \ Annual cash inflow
=20000\5000
=4 YEARS

- Discounted pay back period:

The following particulars relating to a project.
Cost of the project Rs.50500 Annual cash inflow

1 year	5000
2 year	20000
3 year	30000
4 year	30000
5 year	10000

Year	1	2	3	4	5
PV Factor @10%	0.909	0.826	0.751	0.683	0.621

Calculate discounted pay back period.

Solution:

Calculation of cumulative discounted cash inflows:

Year	Cash inflow	P.V factor	P.V for cash inflow	C.D cash inflow
1	5000	0.909	4545	4545
2	20000	0.826	16520	21065
3	30000	0.751	22530	43594
4	30000	0.683	20490	64085
5	10000	0.621	6210	70295

Discount pay back period= (3 years+50000-43595\20490)*100
=4 months(approx)
=3 years and 4 months.

- Accounting (or)average rate of return method:

Investment data for a new product are as follows
Capital outlay Rs.200000
Depreciation 20%p.a on written down value
Calculate accounting rate of return ignore taxation

Solution :

Year	Earning before depreciation	Depreciation@20%	Earnings at tax depreciation
1	100000	40000	60000
2	100000	32000	68000
3	80000	25600	54400
4	80000	25480	59520
5	45000	16384	23616

TOTAL PROFIT FOR 5 YEARS = 265536

Average profit = 265536\5

= 53107

Accounting rate of return original investment

= (Average profit\original investment)*100

= (53107\200000)*100

= 26.55%

Average investment = (Average profit\Average investment)*100

= (53107\100000)*100

= 53.11%

= (Investment in the beginning + Investment at the end)\2

= (200000+0)\2

= 100000

Ex no: 2 Evaluation of risk-return analysis of a company.

Date :

Aim:

To prepare and evaluate risk return analysis of a company.

Procedure:

- **RISK ADJUSTED DISCOUNT RATE:**

  Risk adjusted discount rate assumes that investors expect a higher rate of return on more risky project as compared to loss risky projects.

1.**The following details related to two project X and Y**

Risk free discount ratio is 5% project X is less risky as compared to project Y.

Risk adjusted discount rate = risk free rate + risk premium rate

Project X =5+5=10%

Project Y =5+10=15%

Calculation of net present value

Project X

Year	Cash inflow (Rs)	PVF @10%	P.V of cash inflow (Rs)	Cash inflow (Rs)	PVF @15%	P.V of cash inflow (Rs)
1	6000	0.909	5454	9000	0.870	7830
2	7000	0.826	5782	10000	0.756	7560
3	8000	0.651	6008	11000	0.658	7238
TPV of cash inflow		17244				22628
Less investment		20000				20000
NPV		2756				2268

NPV is positive in the case of project Y Hence it recommended .

2. Certainty Equivalent Method:

This is another method of dealing with risk in capital budgeting in this method estimated uncertain cash inflow (risky cash flow) of each year is reduced to certain cash inflow.

1.A firm used certainty equivalent coefficient method in capital budgeting decisions the initial cost of project is 150000 the expected cash inflow and the certainty coefficient are as under.

Year	Cash inflows	Certainty Equivalent coefficient
1	60000	0.9
2	70000	0.8
3	80000	0.7
4	50000	0.6

In risk loss rate of return is 12% suggest whether the project should be accepted .

Calculation of certainty cash inflows and net present value

Year	Cash inflow	CEC	Certain cash inflow	Discount factor 12%	P.V cash inflow
1	60000	0.9	54000	0.893	48202
2	70000	0.8	56000	0.797	44632
3	80000	0.7	56000	0.712	39872
4	50000	0.6	30000	0.636	19080

Total PV cash inflow=153780

(_) Initial investment=150000

Net present value=3780

3. Sensitivity analysis:

In the above two methods we have considered only one estimate of cash inflow for each year but there are chances of making some estimation errors.

2.Mr. Suriya is considering two mutually exclusive investment proposals X and Y the initial outlay is Rs.60000 in each case the useful economic life is 10years with no salvage value. Forecast of annual probable cash inflows under the three catagories is as follows.

Probable annual cash inflow	Project X (Rs)	Project Y (Rs)
Optimistic	25000	40000
Most likely	20000	20000
Pessimistic	10000	2000

Cut off rate may be assumed to be 10% calculate NPV and state which project is better.

Project X Calculation of Net present value

	A.C.I(Rs)	PVF@10%	PV (Rs)	Investment (Rs)	NPV (Rs)
Optimistic	25000	6.145	153625	60000	93625
Most likely	20000	6.145	122900	60000	629000
Pessimistic	10000	6.145	6450	60000	1450

Project Y Calculation of Net present value

	A.C.I(Rs)	PVF@10%	PV (Rs)	Investment (Rs)	NPV (Rs)
Optimistic	25000	6.145	245800	60000	125800
Most likely	20000	6.145	122900	60000	62900
Pessimistic	10000	6.145	12290	60000	47710

4.Probability distribution:

Sensitive analysis provides different cash flow estimates under different circumstances. However, it does not provide chances of occurrence of each of those estimates .

Two mutually exclusive investments are being considered the following information is available.

Cost of the investment **Project A** **Project B**

Rs.60000 **Rs.60000**

Year	Cash inflow (Rs)	Probability	Cash flows (Rs)	Probability
1	40000	0.2	70000	0.2
2	80000	0.6	80000	0.6
3	120000	0.2	90000	0.2

Assuming cost of capital @ 10% advice the selection of the project.

Project A Calculation of Net present value

Year	Cash inflows	Probability	Monetary value(Rs)	PVF@10%	Present value
1	40000	0.2	8000	0.909	7272
2	80000	0.6	48000	0.826	39.648

3	120000	0.2	24000	0.751	18.024

Total present value of cash inflow	64,944
Less cost of investment	60,000
Net present value	5892

As the NPV of project B is more than of project A ,Project B is more than profitable.

5.Standard Deviation:

Probability distribution approach does not provide a precise value indicating the variability of each flows and the amount of risk involved.

From the following information , ascertain which projects is more risky and the basis of standard deviation.

Project A **Project B**

Cash inflow	**Probability**	**Cash inflow**	**Probability**
4000	0.3	10000	0.2
6000	0.4	8000	0.3
8000	0.2	6000	0.5
10000	0.1	20000	0.2

Project A **Calculation of standard deviation**

Cash inflow X	**Deviation from mean (mean7000)**	**d**	**Probability f**	**fd**
4000	-3000	9000000	0.3	2700000
6000	-1000	1000000	0.4	400000
8000	1000	1000000	0.2	200000
10000	3000	9000000	0.1	900000

Coefficient of variation:

Standard deviation is an absolute measure of dispersion it is not useful for comparison particularly where the projects involve different cash outflows are different are mean values .

Decision tree analysis:

Another approach for revaluating risky investment proposal is the decision tree analysis in modern business investment decision are complex involving a sequence of decision over a period of time.

Ex no : 3 Estimation of components of Cost of Capital of a new started business.

Date :

Aim:

To prepare estimation of components of cost of capital of new started business.

Procedure:

COST OF CAPITAL

The cost of capital is the minimum rate of return expected by investors. Solmonezra defines cost of capital as, "The Minimum required rate of earnings or the cut of rate of capital expenditure."

COST OF DEBT

1. COST OF IRREDEEMABLE DEBT:

Irredeemable debt (or perpetual debt) is debt which is not redeemable during the life time of the company.

Before tax cost of debt(k_{db}) = Interest /net proceeds (NP)

A. When debt is issued @par:
   NP = Fare value – issue expenses
B. When debt is issued @ premium:
   NP = Face value+ premium -issue expenses

After tax cost of debt:

In the computation of income tax, interest is allowed as deduction.

= Interest- tax saving / Net proceeds

2 . COST OF REDEEMABLE DEBT:

Redeemable debt refers to debt which is to be a redeemable after the stipulated period. For ex ,is may be repayable after 5 or 7or 10 years.

The before tax cost of redeemable debt is calculated as under,

Before tax cost of debt = Annual cost before tax / Average value of debt (AV)

3 . COST OF EXISTING DEBT :

The method of computing the cost of debt raised has been explained in the proceeding section .sometimes, 'Current cost ' of the existing debt may have to be calculated. In such a case, cost of debt is approximate by the current market yield of the debt.

Before tax of cost existing debt = Annual cost before tax / Average value of debt (AV)

4. FLOATING RATE DEBT:

Floating rate debt is also as a variable rate debt. The rate of interest is net fixed. It is linked some other standard rate such as the primary lending rate (PLR) of the bank or the interest rate of gilt edged securities.

5. INFLATION ADJUSTING COST OF DEBT:

During the periods of inflation, the company pays only a fixed rate of interest, although there is a fall in the value of money ,due to increase in general price level.

Real cost of debt = 1 + nominal cost of capital / 1 + inflation rate

COST OF PREFERENCE SHARE CAPITAL

A Fixed rate of dividend is payable on preference shares. The dividend is payable at discretion of directors.

1. COST OF IRREDEEMABLE PREFERENCE SHARE CAPITAL:

   The cost of preference share capital which is perpetual is calculated by the following formula,

   Cost of preference share capital = D / NP or Annual dividend / net proceeds

   Annual dividend = Annual preference dividend payable
2. Net proceeds = Net amount relaisedfrom the issue of preference share

COST OF REDEEDMABLE PREFERENCE SHARE CAPITAL (RPS)

Preference shares which are to be redeemable after the expiry of the stipulated period are known as redeemable preference shares .

Annual cost /Average value of (RPS)

AVERAGE VALUE OF RPS :

Average value is the average of net proceeds (NP) of the issue redemption on value.

Average value= NP+RV/2

It is not legally binding on a company to pay dividend on equity shares even if it earns profit.

1. DIVIDEND PRICE METHOD (DIP) OR DIVIDEND YIELD METHOD:

According, to this method cost of equity capital is the discount rate at which the present value of expected future dividends per share is equal to the next proceeds (or current market price per share)

=P1/NP or D1/MP

2. DIVIDEND PRICE GROWTH METHOD:

   Under this method, cost of equity capital determined on basis of dividend yield and growth rate in dividend

   K=D1/NP+G or D1/MP+G

3. EARNING PRICE METHOD (E/P):

   Earning price method is also called earning price method. It considers as a more appropriate the dividend in company the cost of equity capital .

   K=EPS/NP or EPS/MP

4. REALISED YIELD METHOD:

   Under this method, the cost of equity capital is computed on the basis of return actually realized by the shareholders. The return to shareholders contents of dividend and capital gains.

   COST OF RETAINED EARNINGS

   All the profit earned by a company are not distributed a dividends to shareholders. Generally, companies retain a portion of the earnings for use in business this is called retained earnings.

Ex.no :4 Prepare theories of Capital Structure with an analysis of a company
Date :

Aim:

To prepare theories of Capital Structure with an analysis of a company

Procedure:

According to Geresternberg Capital Structure of a company refers to the make up of its capitalization and it includes all long term sources via, loans, reserves, shares &bonds.

Theories of Capital Structure:

The four major theories or approaches which explains the relationship between capital structure ,cost of capital,and valuation of firm are,

- Net Income Approach
- Net Operating Income Approach
- The Traditional Approach
- Modigliani-Miller Approach

1. NET INCOME APPROACH :
   According to Net Income Approach , Capital Structure decision is a relevant to the valuation of firm. A firm can minimize to overall cost of capital by maximizing the use of debt in the capital structutre.
   V=S+D
   V=Total market value of the firm
   S=Market value of equity shares
   - Net income/ Equity Capitalisation Rate (or)
   - Earning available shareholder/cost of equity
2. NET OPERATING INCOME APPROACH:
   Net operating income approach is also suggested by Durand. It is diametrically opposite to the Net income approach. According to this theory capital structure does not effect the overall cost of capital and the value of the firm.
   V=net operating income (EBIT)/overall cost of capital
   Market value of equity shares is ascertained by deducting the value of debt from the total value of the firm.
   S=V-D
   S= market value of equity shares
   V=value of the firm

D=market value of debt

3. THE TRADITIONAL APPROACH:

   The Traditional approach is also called as the intermediate approach. It is compromise between the Net income approach & Net operating income approach. Thus use of debt upto a point is favourable. Therefore that level of debt –equity mix-capital syructure will be optimum.

4. MODIGLIANI –MILLER APPROACH

   Modigliani and Miller explain the relation between Capital structure and cost of capital and the value of the firm under two conditions

   a. When there are no corporate taxes
   b. When there are corporate taxes

A. When there are no corporate taxes :

   The Modigliani-Millers approach is a=identical to et operating income approach ,when there are no separate taxes Modiglaini and Miller argues that in the absence of taxes. The cost of capital and value of the firm are not affected by capital structure debt equity mix.

B. When there are corporate taxes:

   Miller have recognized that capital structure would affect the cost of capital and value of the firm, when there are corporate taxes. If a firm uses debt in its capital structure , the cost of capital will decline and market value will increase. This is because of the deductibility of interest charges for computation of tax.

   Vu= Earning available to shareholders /cost of equity=Eat/Ke

   Vl= Vu+(T*D)

   Value of levered firm = value of unlevered firm +(tax*rate*debt).

PROBLEM:1

A company needs Rs. 6,00,000 for construction of a new plant. The following three financial plan are feasible.

1. The company issues 30,000 equity shares of Rs 10 each
2. The company may issue 3000 equity shares of Rs 10 each and 3000 debentures of Rs 10 each bearing 8% coupon rate of interest
3. The company may issue 30,000 equity shares of Rs 10 each
   and 3000 preference share of Rs 100 each bearing 8% rate of dividend .

The profit before interest the taxes (EBIT) is expected to be Rs 1,50,000 corporate tax rate is 50%

Calculate the earnings per share under the 3 plan which plan would you recommend and why?

EPS UNDER DIFFERENT PLAN

	Plan 1 equity	Plan 2 equity &debt	Plan 3 equity & preference
Profit before interest and taxes	1,50,000	1,50,000	1,50,000
(-)Interest 8% on 3,00,000	-	24,000	-
Profit before tax	1,50,000	1,26,000	1,50,000
(-)Tax @ 50%	75,000	63,000	75,000
Profit after tax			
(-)Preference dividend 8% on 3,00,000	-	-	24,000
Profit available to equity share holders (a)	75,000	63,000	51,000
No: of equity shares (b)	60,000	30,000	30,000
Earnings per share (a/b)	1.25	2.10	1.70

AIM:

TO prepare a collection of difference sources of long term financing of a business unit

Procedures:

Sources of Short-Term and Long-Term Financing for Working Capital

A constant flow of working capital is an intrinsic component of a successful business. This is especially true considering the outflow that is a part and parcel of every cycle: salaries and wages need to be paid; raw materials need to be purchased and equipment need to be serviced; funds are needed for marketing, advertising, and other general overhead costs; reserves are required till the customers make their payment. Working capital is truly the lifeline for any company.

Short Term Financing

Banks can be an invaluable source of short term working capital finance.

1. Overdraft Agreement:

By entering into an overdraft agreement with the bank, the bank will allow the business to borrow up to a certain limit without the need for further discussion. The bank might ask for security in the form of collateral and they might charge daily interest at a variable rate on the outstanding debt. However, if the business is confident of making the repayments quickly, then an overdraft agreement is a valuable source of financing, and one that many companies resort to.

2. Accounts Receivable Financing:

Many banks and non-banking financial institutions provide invoice discounting facilities. The company takes the commercial bills to the bank which makes the payment minus a small fee.

Then, on the due date the bank collects the money from the customer. This is another popular method of financing especially among small traders. Businesses that offer large terms of credit can carry on their operations without having to wait for the customers to settle their bills.

3. Customer Advances:

There are many companies that insist on the customer making an advance payment before selling them goods or providing a service. This is especially true while dealing with large orders that take a long time to fulfill. This method also ensures that the company has some funds to channelize into its operations for fulfilling those orders.

4. Selling Goods on Installment:

Many companies, especially those that sell television sets, fans, radios, refrigerators, vehicles and so on, allow customers to make their payments in installments. Since many of these items have become modern day essentials, their customers might not come from well-to-do backgrounds or the cost of the product might be too prohibitive for immediate payment. In such a case, instead of waiting for a large payment at the end, they allow the customers to make regular monthly payments. This ensures that there is a constant flow of funds coming into the business that does not choke up the accounts receivable numbers.

Long-Term Financing

Relying purely on short-term funds to meet working capital needs is not always prudent, especially for industries where the manufacture of the product itself takes a long time:

automobiles, aircraft, refrigerators, and computers. Such companies need their working capital to last for a long time, and hence they have to think about long term financing.

1. Long-Term Loan from a Bank:

Many companies opt for a full-fledged long term loan from a bank that allows them to meet all their working capital needs for two, three or more years.

2. Retain Profits:

Rather than making dividend payments to shareholders or investing in new ventures, many businesses retain a portion of their profits so that they may use it for working capital. This way they do not have to take loans, pay interest, incur losses on discounted bills, and they can be self-sufficient in their financing.

3. Issue Equities and Debentures:

In extreme cases when the business is really short of funds, or when the company is investing in a large-scale venture, they might decide to issue debentures or bonds to the general public or in some cases even equity stock. Of course, this will be done only by conglomerates and only in cases when there is a need for a huge quantum of funds.

Companies cannot rely only on limited sources for their working capital needs. They need to tap multiple avenues. They also need to constantly evaluate what their needs are, through analysis of financial statements and financial ratios, and choose their working capital channels judiciously.

This is an ongoing process, and different routes are appropriate at different points in time. The trick is to choose the right alternative as per the situation.

Long-Term Financing Options Are:

Depending on your business type and size, there are various long-term sources of finance available. These include:

- Equity shares
- Preference shares
- Venture funding
- Term loans
- Bonds and debentures
- Retained earnings

Ex no:
Date :

Aim:

To prepare of dividend policy in current corporate practice of a company

Procedure:

The issue of dividends and dividend policy is of great significance to owners of closely held and family businesses and deserves considered attention.

(Net) Earnings of a Business

The earnings of a business can be expressed by the simple equation:

Earnings = Total Revenue – Total Cost

Costs include all the operating costs of a business, including taxes.

(Net) Cash Flow

Companies have non-cash charges like depreciation and amortization related to fixed assets and intangible assets. They also have cash charges for things that don't flow through the income statement. Capital expenditures for plant and equipment, buildings, computers and other fixed assets are netted against depreciation and amortization, and the result is either positive or negative in a given year. Capital expenditures tend to be "lumpy" while the related depreciation expenses are amortized over a period of years, often causing swings in the net of the two.

Net Cash Flow is the Source of Good Things

We focus on cash flow because it is the source of all good things that come from a business. The current year's cash flow for a business is, for example, the source of:

Long-term debt repayment. Paying debt is good. Bankers are extremely focused on cash flow, because they only want to lend long-term funds to businesses that have the expectation of sufficient cash flow to repay the debt, including principal and interest on the scheduled basis. Interest expense has already been paid when we look at net cash flow. Companies borrow on a long-term basis to finance a number of things like land, buildings and equipment, software and hardware, and many other productive assets that may be difficult to finance currently. They may also borrow on a long term basis to finance stock repurchases or special dividends.

Reinvestment for future growth. Investment in a business is good if adequate returns are available. If a company generates positive cash flow in a given year, it is available to reinvest in the business to finance its future growth. Reinvested earnings are a critical source of investment capital for closely held and private companies Reinvesting with the expectation of future growth (in dividends and capital gains) is an important source of shareholder returns, but the return is deferred, at least in the form of cash, until a future date.

Dividends or distributions. Corporate dividends are also good, particularly if you are a recipient. Cash flow is also the normal source for dividends (for C corporation owners) or what we call "economic distributions," or distributions net of shareholder pass-through taxes (for S corporation and LLC owners).

Assuming that there were no realized capital gains from a business during a given year, the annual return (AR) is measured as follows:

$$AR = \frac{(\text{Dividends} + \text{Unrealized Appreciation})}{\text{Beginning Portfolio Balance}}$$

Now, we add to this any discretionary expenses that are above market or not normal operating expenses of the business that are taken out by owners:

$$AR = \frac{\left(\text{Dividends} + \text{Discretionary Benefits} + \text{Unrealized Appreciation}\right)}{\text{Beginning Value of a Business}}$$

We now know what dividends are, and they include discretionary benefits that will likely be ceased and normalized into earnings in the event of a sale.

The main consideration in determining the dividend policy is the objective of maximisation of wealth of shareholders. Thus, a firm should retain the earnings if it has profitable investment opportunities, giving a higher rate of return than the cost of retained earnings, otherwise it should pay them as dividends.

Ex no :

Date :

Aim:

To preparation of the principal yardsticks for measuring financial charcterstic of investment proposal

Procedure:

Yardsticks

The third form1 of incentive regulation provides competition between comparable operators in separate markets. When using this form of regulation, regulators generally should choose performance measures that are general in nature and that operators can affect. An example of a general performance measure might be cost per kilowatt hour and an example of a more granular performance measure might be line maintenance cost per kilowatt hour. General performance measures allow operators to make economic tradeoffs – for example, between capital investments and operating expenses – while granular performance measures restrict the means by which operators can improve measured performance. In addition to being used for regulating overall price levels, benchmarking can be used for regulating such items as service quality and network expansion.

Financial Performance:

The first priority is to identify and understand the overall impact that the various financial realities represented by your KPI numbers have on your business. Then, use the insights you acquire from these invaluable financial management performance indicators to identify and implement changes that correct problems with policies, processes, personnel, or products that are impacting one or more of your KPI values.

Primary KPIs that you're undoubtedly already using include revenue, expense, gross profit, and net profit. Here are other key indicators that should be tracked, analyzed, and acted upon as needed.

1. Operating Cash Flow

Monitoring and analyzing your Operating Cash Flow is an essential for understanding your ability to pay for deliveries and routine operating expenses. This KPI is also used in comparison with total capital you have in use—an analysis that reveals whether or not your operations are generating sufficient cash for support of capital investments you are making to advance your business.

The analysis of your ratio of operating cash flow compared to your total capital employed gives you deeper insight into your business's financial health, allowing you to look beyond just profits, when making capital investment decisions.

2. Working Capital

Cash that is immediately available is "working capital". Calculate your Working Capital by subtracting your business's existing liabilities from its existing assets. Cash on hand, accounts receivable, short-term investments are all included, as well as accounts payable, accrued expenses, and loans are all part of this KPI equation.

This especially meaningful KPI informs you of the condition of your business in terms of its available operating funds, by showing the extent to which your available assets can cover your short-term financial liabilities.

3. Current Ratio

While the Working Capital KPI discussed above subtracts liabilities from assets, the Current Ratio KPI divides total assets by liabilities to give you an understanding the solvency of your business—i.e., how well your company is positioned to meet its financial obligations consistently on time and to maintain a level of credit rating that is required to order to grow and expand your business.

4. Debt to Equity Ratio

Debt to Equity is a ratio calculated by looking at your business's total liabilities in contrast to your shareholders' equity (net worth). This KPI indicates how well your business is funding its growth and how well you are utilizing your shareholders' investments. The number indicates how profitable the business is. It tells you and your shareholders how much debt the business has accrued in effort to become profitable. A high debt-to-equity ratio reveals a

practice of paying for growth by accumulating debt. This critical KPI helps you focus on your financial accountability.

5. LOB Revenue Vs. Target

This KPI compares your revenue for a line of business to your projected revenue for it. Tracking and analyzing discrepancies between the actual revenues and your projections helps you understand how well a particular department is performing financially. This is one of the two primary factors in the calculation of the Budget Variance KPI—the comparison between projected and actual operating budget totals, which is necessary in order for you to budget more accurately for needs.

6. LOB Expenses Vs. Budget

Comparing actual expenses to the budgeted amount produces this KPI. The comparison helps you understand where and how some budgeted spending went off track, so that you can budget more effectively going forward. Expenses vs. Budget is the other primary factor of the Budget Variance KPI. Knowing the amount of variance between the total assumed and total actual ratio of revenues to expenses helps you become an expert on the relationship between your business's operations and finances.

7. Accounts Payable Turnover

The Accounts Payable Turnover KPI shows the rate at which your business pays off suppliers. The ratio is the result of dividing the total costs of sales during a period (the costs your company incurred while supplying its goods or services), by your average accounts payable for that period.

This is a very informative ratio when compared over multiple periods. A declining accounts payable turnover KPI may indicate that the length of time your company is taking to pay off its suppliers is increasing and that action is required in order to keep your good standing with your vendors, and to enable your business to take advantage of significant time-driven discounts from vendors.

8. Accounts Receivable Turnover

The accounts receivable turnover KPI reflects the rate at which your business is successfully collecting payments due from your customers. This KPI is calculated by dividing your total sales for a period by your average accounts receivable for that period. This number can serve as an alert that corrections need to be made in managing receivables, in order to bring payment collections within appropriate timeframes.

9. Inventory Turnover

Inventory continuously flows in and out of your production and warehousing facilities. It can be hard to visualize the amount of turnover that is actually taking place. The inventory turnover KPI allows you to know how much of your average inventory your company has sold in a period. This KPI is calculated by dividing sales within a given period by your average inventory in the same period. The KPI gives you a picture of your company's sales strength and production efficiency.

10. Return on Equity

The Return on Equity (ROE) KPI measures your company's net income in contrast to each unit of shareholder equity (net worth). By comparing your company's net income to its overall wealth, your ROE indicates whether or not your net income is appropriate for your company's size.

Regardless of how much your company is currently worth (its net worth), your current net income will determine its probable worth in the future. Therefore, your business's ROE ratio both informs you of the amount of your organization’s profitability and quantifies its general operational and financial management efficiency. An improving, or high ROE clearly indicates to your shareholders that their investments are being optimized to grow the business.

11. Quick Ratio

Your Quick Ratio KPI measures your organization's ability to utilize its highly liquid assets to immediately meet your business's short-term financial responsibilities. This is the measurement of your company’s wealth and financial flexibility. It is understood as a more conservative evaluation of a business's fiscal health than the Current Ratio, because calculation of the Quick Ratio excludes inventories from assets.

This Quick Ratio KPI has the popular nickname of "Acid Test" (after the nitric acid test used in detecting gold). Similarly, the Quick Ratio is a quick and easy way of assessing the

wealth and health of your company. If you' are a new adopter of KPIs, the Quick Ratio KPI is a good approach to getting a quick view of your business's overall health.

12. Customer Satisfaction

While budget-linked KPIs are important, the ultimate indicator of a company's potential for long-term success is in its Customer Satisfaction quantification. The Net Promoter Score (NPS) is the result of calculating the various levels of positive response that customers provide on very brief customer satisfaction surveys. The NPS a simple and accurate measurement of likely rates of customer retention (future sales to current customers) across your revenue base, and of potential for generating referral business to grow that base.

Investment Proposals:

There is no standard application form for IFC financing. A company or entrepreneur, foreign or domestic, seeking to establish a new venture or expand an existing enterprise can approach IFC directly. This is best done by reading how to apply for financing, and by submitting an investment proposal.

Proposals can be submitted to IFC's industry departments; regional departments at IFC headquarters in Washington; or the regional field office closest to the location of the proposed project.

An investment proposal should include the following preliminary information:

- Brief description of project.
- Sponsorship, management & technical assistance:
- History and business of sponsors, including financial information.
- Proposed management arrangements and names and curricula vitae of managers.
- Description of technical arrangements and other external assistance (management, production, marketing, finance, etc.).

3. Market & sales:

Projected production volumes, unit prices, sales objectives, and market share of proposed venture.

Potential users of products and distribution channels to be used.

Present sources of supply for products.

Future competition and possibility that market may be satisfied by substitute products.

Tariff protection or import restrictions affecting products.

Critical factors that determine market potential.

4. Technical feasibility, manpower, raw material resources & environment:

Comments on special technical complexities and need for know-how and special skills.

Possible suppliers of equipment.

Availability of manpower and of infrastructure facilities (transport and communications, power, water, etc.).

Breakdown of projected operating costs by major categories of expenditures.

Source, cost, and quality of raw material supply and relations with support industries.

Import restrictions on required raw materials.

Proposed plant location in relation to suppliers, markets, infrastructure, and manpower.

Proposed plant size in comparison with other known plants.

Potential environmental issues and how these issues are addressed.

5. Investment requirements, project financing, and returns:

Proposed financial structure of venture, indicating expected sources and terms of equity and debt financing.

Type of IFC financing (loan, equity, quasi-equity, a combination of financial products, etc.) and amount.

Projected financial statement, information on profitability, and return on investment.

Critical factors determining profitability.

6. Government support & regulations:

Specific government incentives and support available to project.

Expected contribution of project to economic development.

Outline of government regulations on exchange controls and conditions of capital entry and repatriation.

7. Timetable envisaged for project preparation and completion.

Ex no:

Date :

Aim:

To preparation of evaluation of different methods used for ranking of investment proposal

Procedure:

Ranking Investment Proposals:

Several methods are commonly used to rank investment proposals, including NPV, IRR, PI, payback period, and ARR.

Net Present Value (NPV):

NPV can be described as the "difference amount" between the sums of discounted: cash inflows and cash outflows. In the case when all future cash flows are incoming, and the only outflow of cash is the purchase price, the NPV is simply the PV of future cash flows minus the purchase price (which is its own PV). The higher the NPV, the more attractive the investment proposal. NPV is a central tool in discounted cash flow (DCF) analysis and is a standard method for using the time value of money to appraise long-term projects. Used for capital budgeting and widely used throughout economics, finance, and accounting, it measures the excess or shortfall of cash flows, in present value terms, once financing charges are met.

NPV formula

Each cash inflow/outflow is discounted back to its present value (PV). Then they are summed. Therefore, NPV is the sum of all terms.

In financial theory, if there is a choice between two mutually exclusive alternatives, the one yielding the higher NPV should be selected. The rules of decision making are:

When NPV > 0, the investment would add value to the firm so the project may be accepted

When NPV < 0, the investment would subtract value from the firm so the project should be rejected

When NPV = 0, the investment would neither gain nor lose value for the firm. We should be indifferent in the decision whether to accept or reject the project. This project adds no monetary value. Decision should be based on other criteria (e.g., strategic positioning or other factors not explicitly included in the calculation).

An NPV calculated using variable discount rates (if they are known for the duration of the investment) better reflects the situation than one calculated from a constant discount rate for the entire investment duration.

Internal Rate of Return (IRR)

The internal rate of return on an investment or project is the "annualized effective compounded return rate" or "rate of return" that makes the net present value (NPV as NET*1/(1+IRR)^year) of all cash flows (both positive and negative) from a particular investment equal to zero.

IRR calculations are commonly used to evaluate the desirability of investments or projects. The higher a project's IRR, the more desirable it is to undertake the project. Assuming all projects require the same amount of up-front investment, the project with the highest IRR would be considered the best and undertaken first.

Profitability Index (PI)

It is a useful tool for ranking projects, because it allows you to quantify the amount of value created per unit of investment. The ratio is calculated as follows:

Profitability index = PV of future cash flows / Initial investment

As the value of the profitability index increases, so does the financial attractiveness of the proposed project. Rules for selection or rejection of a project:

If PI > 1 then accept the project

If PI < 1 then reject the project

Payback Period

Payback period intuitively measures how long something takes to "pay for itself. " All else being equal, shorter payback periods are preferable to longer payback periods. Payback period is widely used because of its ease of use despite the recognized limitations: The time value of money is not taken into account.

Accounting Rate of Return (ARR)

The ratio does not take into account the concept of time value of money. ARR calculates the return, generated from net income of the proposed capital investment. The ARR is a percentage return. Say, if ARR = 7%, then it means that the project is expected to earn seven cents out of each dollar invested. If the ARR is equal to or greater than the required rate of return, the project is acceptable. If it is less than the desired rate, it should be rejected. When

comparing investments, the higher the ARR, the more attractive the investment. Basic formulae:

ARR = Average profit / Average investment

The process for selecting capital projects can require much thought and analysis. Many financial evaluation methods have been employed to determine whether to accept or reject a project. Choosing the correct method for ranking projects can be complicated when a choice must be made between mutually exclusive projects. (When projects are mutually exclusive, only one project can be chosen and the others must be abandoned.) The choice in this case must be made based on the ranking of projects in order of increasing shareholder wealth. Choices are made based on various financial evaluation methods, one of which is to discount future net cash flows into present value terms using the cost of capital or a discount rate. Net Present Value (NPV) and Internal Rate of Return (IRR) are the most common methods for ranking projects in terms of the present value of future cash flows. This article will help decision makers determine which of these two evaluation methods—NPV or IRR—is better for evaluating mutually exclusive projects.

Net Present Value Method

The Net Present Value (NPV) Method is "a method of ranking investment proposals using the NPV, which is equal to the present value of future net cash flows, discounted at the marginal cost of capital."1 The equation for NPV is as follows:

NPV Equation

In this equation, CFt represents the expected cash flow at the Period t, k represents the cost of capital, and n is the life of the project. When NPV is zero, the project's cash flows are great enough to meet the project's required rate of return and pay back the capital invested. When NPV is positive, there are enough cash flows to pay back the project's debt and provide a return to shareholders. NPV is also expressed as a dollar value, which provides a good indicator of profitability and growth in shareholder wealth.

Internal Rate of Return Method

The Internal Rate of Return (IRR) Method is "a method of ranking investment proposals using the rate of return on an investment, calculated by finding the discount rate that equates the present value of future cash inflows to the project's cost" 1. It is the rate that forces NPV to equal 0 as shown in the following equation.

NPV = Equation

The IRR is always expressed as a percentage. For a project to be acceptable under the IRR method, the discount rate must exceed the project's cost of capital, otherwise known as the hurdle rate. An IRR less than the hurdle rate represents a cost to shareholders, while an IRR greater than the hurdle rate represents a return on investment, increasing shareholder wealth.

We must first analyze the reinvestment rate assumptions for each evaluation method. The NPV method assumes that cash flows will be reinvested near or at the project's current cost of capital, while the IRR method assumes that the firm can reinvest cash flows at the

project's IRR. The assumption that the firm will reinvest its cash flows at the current cost of capital is more realistic than the assumption that cash flows can be reinvested at the projects IRR. This is because the IRR may not reflect the true rate at which cash flows can be reinvested. To correct this problem, a modified IRR (MIRR) is used that incorporates the cost of capital as the reinvestment rate; however, the NPV method still has the advantage when compared to the MIRR method (an example is when IRR and MIRR methods return conflicting results under certain project conditions).

The NPV and IRR methods will return conflicting results when mutually exclusive projects differ in size, or differences exist in the timing of cash flows. When mutually exclusive projects exhibit these attributes, their NPV profiles will cross when plotted on a graph. This point at which they cross is defined as the crossover rate, which happens because one project's NPV is more sensitive to the discount rate caused by the differences in the timing of cash flows. In most cases, utilizing either the NPV or IRR method will lead to the same accept-or-reject decision. An exception exists when evaluating mutually exclusive projects with crossing NPV profiles and the cost of capital is less than the crossover rate. When these conditions are present, the NPV and IRR results will conflict in which project to accept or reject. Because the NPV method uses a reinvestment rate close to its current cost of capital, the reinvestment assumptions of the NPV method are more realistic than those associated with the IRR method.

NPV also has an advantage over IRR when a project has non-normal cash flows. Non-normal cash flows exist if there is a large cash outflow during or at the end of the project.

The presence of non-normal cash flows will lead to multiple IRRs. Hence, the IRR method cannot be employed in the evaluation process. Mathematically, this problem will not occur if the NPV method is employed. The NPV method will always lead to a singular correct accept-or-reject decision.

In conclusion, NPV is a better method for evaluating mutually exclusive projects than the IRR method. The NPV method employs more realistic reinvestment rate assumptions, is a better indicator of profitability and shareholder wealth, and mathematically will return the correct accept-or-reject decision regardless of whether the project experiences non-normal cash flows or if differences in project size or timing of cash flows exist.

The Martin Company is considering the four different investment opportunities. The selected information about each proposal is given below:

	Project 1	Project 2	Project 3	Project 4	Project 5
Investment required	$ (960,000)	$(720,000)	$(540,000)	$ (900,000)	$(800,000)
Present value of cash inflows	1,134,540	866,800	672,280	1,045,940	759,520
Net present value	$ 174,540	$ 146,800	$ 132,280	$ 145,940	(40,480)
Project life	6 years	12 years	6 years	3 years	5 years
Internal rate of return	16%	14%	18%	19%	8%

Required:

Compute the profitability index (present value index) for all the projects.

Rank the four investment projects according to preference using:

(a). net present value (NPV).

(b). profitability index (PI).

(c). internal rate of return (IRR).

Which one is the best approach for Martin Company to rank five competing projects?

Solution:

(1). Computation of profitability index:

Formula of profitability/present value index is:

Profitability index = Present value of cash inflows/Investment require

Project 1: rs1,134,540/rs960,000 = 1.18

Project 2: rs866,800/rs720,000 = 1.20

Project 3: rs672,280/rs540,000 = 1.24

Project 4: rs1,045,490/rs900,000 = 1.16

Project 5: rs759,520/rs800,000 = 0.95

3. The best ranking approach:

The best method of ranking projects depends on the availability of good reinvestment opportunities. Under internal rate of return (IRR) method, we assume that the funds released from a project are reinvested in another project yielding the internal rate of return equal to the previous project. According to IRR, the project 4 is ranked at number one with 19% IRR. It means any funds released from project 4 must be reinvested in another project yielding an internal rate of return of at least 19% but It might be difficult to find a project with such a high IRR.

The profitability index (PI) shows the present value of cash inflow generated by each dollar invested in a project. It assumes that the funds released from a project are reinvested in another project with a return equal to the discount rate. In our problem, the discount rate is only 10%. Generally, the profitability index is considered the most dependable method of ranking competing projects.

The net present value (NPV) method considers the net present value figure but does not take into account the amount of investment required for the project. Therefore, this method is not appropriate for comparing or ranking competing projects that require different amounts of investment. For example, project 3 is ranked at number four because of its low net present value but it is the best option if we see at the present value of net cash inflow generated by each dollar invested in the project (as shown by the profitability index).

Conclusion: From above discussion, we can conclude that the profitability index is the most appropriate and dependable method of ranking projects for Martin Company.

Ex.No:

Date:

Aim :

To prepare and analysis the cost of capital and leverages

Procedures:

A multinational company, known more commonly as a multinational corporation or transnational corporation in North America, is a business with branches, offices or production facilities in more than one country.

Some people say that any firm that derives at least one quarter of all its business abroad is considered a multinational corporation. However, if all that foreign business comes purely from exports and the company has no offices, premises or production facilities abroad, it is not a multinational.

Multi-National Company:

International Business Machines (IBM), is a global technology company that provides hardware, software, cloud-based services and cognitive computing.

ounded in 1911 following the merger of four companies in New York State by Charles Ranlett Flint, it was originally called Computing-Tabulating-Recording Company. It would be renamed to IBM in 1924.

Given that the company is over 100 years old it is no surprise that it has had to adjust to different technological trends throughout the decades.

The company is now transitioning from being an infrastructure player to one that is more cloud and data driven.

Nicknamed ‘Big Blue’, the company offers cloud products in the shape of Bluemix, a SoftLayer cloud, and data analytics, or cognitive computing capabilities, with the Watson supercomputer.

While the company has expanded its portfolio from server hardware, this is still an area that it operates in with the z Series mainframe.

The company also offers software with the likes of its DB2 database offering, and IBM SPSS.

GinniRometty, IBM CEO, said: “Digital is the wires, but digital intelligence, or artificial intelligence as some people call it, is about much more than that. This next decade is about how you combine those and become a cognitive business. It’s the dawn of a new era.”

IBM has been focused on continuous innovation for more than a century. Patenting is an important barometer of that innovation, and IBM has topped the annual list of U.S. patent recipients for the 20th consecutive year.

Cost of Capital:

ith trillions of dollars in cash sitting on their balance sheets, corporations have never had so much money. How executives choose to invest that massive amount of capital will drive corporate strategies and determine their companies' competitiveness for the next decade and beyond. And in the short term, today's capital budgeting decisions will influence the developed world's chronic unemployment situation and tepid economic recovery.

Although investment opportunities vary dramatically across companies and industries, one would expect the process of evaluating financial returns on investments to be fairly uniform. After all, business schools teach more or less the same evaluation techniques. It's no surprise, then, that in a survey conducted by the Association for Financial Professionals (AFP), 80% of more than 300 respondents—and 90% of those with over $1 billion in revenues—use discounted cash-flow analyses. Such analyses rely on free-cash-flow projections to estimate the value of an investment to a firm, discounted by the cost of capital (defined as the weighted average of the costs of debt and equity). To estimate their cost of equity, about 90% of the respondents use the capital asset pricing model (CAPM), which quantifies the return required by an investment on the basis of the associated risk.

But that is where the consensus ends. The AFP asked its global membership, comprising about 15,000 top financial officers, what assumptions they use in their financial models to quantify investment opportunities. Remarkably, no question received the same answer from a

majority of the more than 300 respondents, 79% of whom are in the U.S. or Canada. (See the exhibit “Dangerous Assumptions.”)

The Risk-Free Rate

Errors really begin to multiply as you calculate the cost of equity. Most managers start with the return that an equity investor would demand on a risk-free investment. What is the best proxy for such an investment? Most investors, managers, and analysts use U.S. Treasury rates as the benchmark. But that’s apparently all they agree on. Some 46% of our survey participants use the 10-year rate, 12% go for the five-year rate, 11% prefer the 30-year bond, and 16% use the three-month rate. Clearly, the variation is dramatic. When this article was drafted, the 90-day Treasury note yielded 0.05%, the 10-year note yielded 2.25%, and the 30-year yield was more than 100 basis points higher than the 10-year rate.

In other words, two companies in similar businesses might well estimate very different costs of equity purely because they don’t choose the same U.S. Treasury rates, not because of any essential difference in their businesses. And even those that use the same benchmark may not necessarily use the same number. Slightly fewer than half of our respondents rely on the current value as their benchmark, whereas 35% use the average rate over a specified time period, and 14% use a forecasted rate.

The Equity Market Premium

The next component in a company’s weighted-average cost of capital is the risk premium for equity market exposure, over and above the risk-free return. In theory, the market-risk premium should be the same at any given moment for all investors. That’s because it’s an

estimate of how much extra return, over the risk-free rate, investors expect will justify putting money in the stock market as a whole.

The estimates, however, are shockingly varied. About half the companies in the AFP survey use a risk premium between 5% and 6%, some use one lower than 3%, and others go with a premium greater than 7%—a huge range of more than 4 percentage points. We were also surprised to find that despite the turmoil in financial markets during the recent economic crisis, which would in theory prompt investors to increase the market-risk premium, almost a quarter of companies admitted to updating it seldom or never.

International Business Machines's Leverage Ratio

IBM's quarterly Leverage Ratio and Total Liabilities, Equity growth

IBM Leverage Ratio	(Dec 31 2018) IV. Quarter	(Sep 30 2018) III. Quarter	(Jun 30 2018) II. Quarter	(Mar 31 2018) I. Quarter	(Dec 31 2017) IV. Quarter
Y / Y Equity Change	*-4.49 %*	*0.81 %*	*0.56 %*	*-0.86 %*	*-3.63 %*
Y / Y Total Liabilities Change	*3.23 %*	*0.19 %*	*5.77 %*	*13.18 %*	*4.06 %*
Leverage Ratio MRQ	**6.3**	**5.13**	**5.53**	**5.86**	**5.83**
Overall Ranking	#	#	#	#	#
Seq. Equity Change	*-15.01 %*	*6.81 %*	*1.96 %*	*3.19 %*	*-10.28 %*
Seq. Total Liabilities	*4.29 %*	*-0.87 %*	*-3.75 %*	*3.75 %*	*1.22 %*

Change					

Result:

In designing the capital structure for any firm, the first major policy decision facing the firm is that of determining the appropriate level of debt. For most of the firms, the decision involves a choice between the long-term debt and the equity. The firm's debt capacity may be best defined not as the maximum amount which the lenders or debt investors are willing to lend to the firm, but as the amount of debt that the firm should us

Ex.No:

Date :

Aim:

To prepare source of working capital for a new starting new business

Procedure:

Sources of working capital can be spontaneous, short term and long term. Spontaneous working capital includes mainly trade credit such as the sundry creditor, bills payable, and notes payable. Short term sources are tax provisions, dividend provisions, bank overdraft, cash credit, trade deposits, public deposits, bills discounting, short-term loans, inter-corporate loans, and commercial paper. Long-term sources are retained profits, provision for depreciation, share capital, long-term loans, and debentures.

Spontaneous Sources	Short Term Sources		Long Term Sources	
	Internal Sources	External Sources	Internal Sources	External Sources
Trade Credit	*Tax Provisions*	*Bank Overdraft*	*Retained Profits*	*Share Capital*
Sundry Creditors	*Dividend*	*Trade Deposits*	*Depreciation*	*Long Term*

Spontaneous Sources	Short Term Sources		Long Term Sources	
	Provisions		*Provision*	*Loans*
Bills Payable		*Public Deposits*		*Debentures*
Notes Payable		*Bills Discounting*		
Accrued Expenses		*Short Term Loans*		

SPONTANEOUS SOURCES OF WORKING CAPITAL FINANCE

The word ‘spontaneous’ itself explains that this source of working capital is readily or easily available to the business in the normal course of business affairs. The quantum and terms of this credit depend on the industry norms and the relationship between buyer and seller. These sources include trade credit allowed by the sundry creditors, credit from employees, and other trade-related credits. The biggest benefit of spontaneous sources as working capital is its ‘effortless raising’ and ‘insignificant cost’ compared to traditional ways of financing.

List of spontaneous sources of working capital

TRADE CREDIT

SUNDRY CREDITORS

BILLS PAYABLE

NOTES PAYABLE

ACCRUED EXPENSES

The cost factor and the quantum depends a lot on the terms of such credit viz. maximum credit limit, the period of credit, and discount on cash payment. Each supplier will have a maximum credit limit defined for the buyer depending on the business capacity and creditworthiness of the buyer. Similarly, the credit period is defined say 30 days, 45 days etc. Discount on cash payment is allowed to the buyer if the payment immediately on buying the materials. This percentage of discount is an opportunity cost for the buyer.

SHORT TERM SOURCES OF WORKING CAPITAL FINANCE

Short term sources can be further divided into internal and external sources of working capital finance.

TAX PROVISIONS

DIVIDEND PROVISIONS

Short-term External Sources

Short-term working capital financing from banks such as

BANK OVERDRAFTS,

CASH CREDITS,

TRADE DEPOSITS,

BILLS DISCOUNTING,

SHORT-TERM LOANS OR WORKING CAPITAL LOANS,

INTER-CORPORATE LOANS,

COMMERCIAL PAPER, ETC.

Tax and dividend provisions are current liabilities and cannot be delayed. The fund that would have been used in paying these provisions act as working capital till the point these are not paid.

Short-term working capital finance availed from banks and financial institutions are costly compared to spontaneous and long-term sources in terms of rate of interest but have a great time flexibility. Due to time flexibility, the finance manager can use the funds and pay interest on the money which his business utilizes and can pay them anytime when cash is available. Overall, in comparison to long-term sources where you have to hold funds even when not required, these facilities prove cheaper.

LONG-TERM SOURCES OF WORKING CAPITAL FINANCING

Long-term sources can also be divided into internal and external sources. Long-term internal sources of finance are retained profits and provision for depreciation whereas external sources are Share Capital, long-term loan, and debentures.

Working capital can be classified as temporary working capital and permanent working capital. It is advisable to use long-term sources for permanent and short-term sources for temporary

working capital requirements. This will optimize the working capital cost and enforce good working capital management practices.

working capital is needed to start a business:

To answer this question, you need to understand how money will flow through your business – in other words, you need to understand your "working capital cycle." The flow or cycle consists of (1) how quickly current assets (e.g. accounts receivables & inventory) are turned into cash and (2) how quickly that cash is used to pay current liabilities (e.g. accounts payable). The working capital cycle is also referred to as the "turnover rates" for accounts receivables, inventory, and accounts payable.

Turnover rates. When starting a business, you will have created projections for key items such as sales, cost of goods sold and other expenses. You also need assumptions on the following: How many days of inventory do you need to keep on hand ("inventory turnover")? How many days will you give customers to pay you (accounts receivable terms)? How many days will your vendors give you to pay them (accounts payable terms)?

Armed with this information, you can calculate how much working capital is needed to start your business. See the example below.

Conclusion

When you start a small business, you will need working capital financing to invest in inventory and accounts receivable. How much money you need for working capital can be estimated by

using a formula that uses assumptions on “Turnover Rates” for inventory, accounts receivable, and accounts payable as shown in the example above. If you are a small business owner in need of working capital financing, avoid the high cost associated with financing products such as factoring, merchant cash advance, and peer-to-peer online lending by exploring alternative, lower cost financing options available through your local CDFI. You can start by learning more about Excelsior Growth Fund’s SmartLoan, which offers loans up to $100,000 with affordable monthly payments.

Ex.No:
Date :

Aim:

To prepare and evaluate capital management and give suitable suggestions

Procedures:

TATA CONSULTANCY SERVICES LTD. (TCS):

Tata Consultancy Services Ltd is a leading global IT services consulting and business solutions organization. The company offers a range of IT services outsourcing and business solutions. They also offer IT infrastructure services business process outsourcing services engineering and industrial services global consulting and asset leveraged solutions. Their segments include banking financial services and insurance; manufacturing; retail and distribution and telecom. The company is a part of Tata Group one of India's most respected business conglomerates and most respected brands. They are headquartered in Mumbai. They are having 142 offices in 42 countries as well as 105 delivery centers in 20 countries. The company shares are listed on the National Stock Exchange and Bombay Stock Exchange of India.Tata Consultancy Services Ltd was incorporated in the year 1968. Tata Sons Ltd established the company as division to service their electronic data processing (EDP) requirements and provide management consulting services. In the year 1971 they started their first international assignment. The company pioneered the global delivery model for IT services with their first offshore client in 1974.In the year 1981 the company set up India's first IT R&D division the Tata Research Design and Development Centre at Pune.

Working Capital:

Working capital management is very important element to measure the short term solvency position of a firm and for profitability. Without its proper management, no corporate can run their business smoothly. The purpose of this study is to investigate the impact of working capital management on liquidity, profitability and element of risk on the Infosys and TCS Company. To achieve these objectives, data has been collected from secondary sources and for getting results various kind of financial ratios are used. The financial ratios of both companies are analyzed with paired T-test. This study will help to both companies in management of their working capital and improving short term solvency position of the companies.

Key Financial Ratios of Tata Consultancy Services:

	Mar '17	Mar '16	Mar '15	Mar '14	Mar '18
Investment Valuation Ratios					
Face Value	1.00	1.00	1.00	1.00	1.00
Dividend Per Share	50.00	47.00	43.50	79.00	32.00
Operating Profit Per Share (Rs)	145.25	137.48	137.30	107.36	109.94
Net Operating Profit Per Share (Rs)	508.58	470.42	435.76	375.64	330.18
Free Reserves Per Share (Rs)	--	--	--	--	--
Bonus in Equity Capital	79.13	79.13	79.13	79.59	79.59
Profitability Ratios					

Operating Profit Margin(%)	28.56	29.22	31.50	28.57	33.29
Profit Before Interest And Tax Margin(%)	25.35	26.23	28.55	25.15	30.17
Gross Profit Margin(%)	26.86	27.52	29.80	26.68	31.62
Cash Profit Margin(%)	26.06	25.93	27.37	25.78	28.84
Adjusted Cash Margin(%)	26.06	25.93	27.37	25.78	28.84
Net Profit Margin(%)	25.92	25.51	26.87	26.17	28.56
Adjusted Net Profit Margin(%)	24.46	24.31	25.74	24.67	27.25
Return On Capital Employed(%)	42.00	38.43	45.03	52.77	53.39
Return On Net Worth(%)	33.27	30.31	35.49	42.40	41.87
Adjusted Return on Net Worth(%)	33.27	30.31	35.49	41.23	41.87
Return on Assets Excluding Revaluations	396.31	395.96	329.94	231.87	224.90
Return on Assets Including Revaluations	396.31	395.96	329.94	231.87	224.90
Return on Long Term Funds(%)	42.10	38.53	45.11	52.99	53.39
Liquidity And Solvency Ratios					
Current Ratio	2.85	3.09	3.41	2.78	3.18
Quick Ratio	2.67	2.93	3.27	2.80	3.16
Debt Equity Ratio	--	--	--	0.01	--
Long Term Debt Equity Ratio	--	--	--	--	--
Debt Coverage Ratios					
Interest Cover	1,065.37	1,880.13	2,257.85	302.89	1,006.74
Total Debt to Owners Fund	0.00	0.00	0.00	0.01	0.00

Financial Charges Coverage Ratio	1,120.27	1,978.56	2,370.08	320.41	1,052.90
Financial Charges Coverage Ratio Post Tax	897.27	1,577.75	1,888.23	260.53	836.35
Imported Composition of Raw Materials Consumed	--	--	72.42	71.30	78.95
Selling Distribution Cost Composition	--	--	--	--	--
Expenses as Composition of Total Sales	94.76	93.17	95.36	97.60	96.27
Cash Flow Indicator Ratios					
Dividend Payout Ratio Net Profit	36.78	38.73	34.63	80.35	33.97
Dividend Payout Ratio Cash Profit	34.52	36.31	32.57	74.93	32.09
Earning Retention Ratio	63.22	61.27	65.37	17.38	66.03
Cash Earning Retention Ratio	65.48	63.69	67.43	23.11	67.91
AdjustedCash Flow Times	0.01	0.01	0.01	0.01	0.00

TCS Income Statement Analysis

- Operating income during the year rose 4.4% on a year-on-year (YoY) basis.
- The company's operating profit increased by 0.6% YoY during the fiscal. Operating profit margins witnessed a fall and stood at 26.4% in FY18 as against 27.4% in FY17.
- Depreciation charges and finance costs increased by 1.4% YoY and 62.5% YoY, respectively.
- Other income declined by 13.7% YoY.

- Net profit for the year declined by 1.8% YoY.
- Net profit margins during the year declined from 21.6% in FY17 to 20.4% in FY18.

TCS Income Statement 2017-18

No. of Mths Year Ending		12 Mar-17*	12 Mar-18*	% Change
Net Sales	Rs m	1,179,660	1,231,040	4.4%
Other income	Rs m	42,210	36,420	-13.7%
Total Revenues	Rs m	1,221,870	1,267,460	3.7%
Gross profit	Rs m	323,110	325,160	0.6%
Depreciation	Rs m	19,870	20,140	1.4%
Interest	Rs m	320	520	62.5%
Profit before tax	Rs m	345,130	340,920	-1.2%
Tax	Rs m	81,560	82,120	0.7%
Profit after tax	Rs m	263,570	258,800	-1.8%
Gross profit margin	%	27.4	26.4	
Effective tax rate	%	23.6	24.1	
Net profit margin	%	21.6	20.4	

TCS Balance Sheet Analysis:

- The company's current liabilities during FY18 stood at Rs 178 billion as compared to Rs 145 billion in FY17, thereby witnessing an increase of 22.9%.
- Long-term debt down at Rs 540 million as compared to Rs 710 million during FY17, a fall of 23.9%.
- Current assets rose 1% and stood at Rs 812 billion, while fixed assets rose 0% and stood at Rs 133 billion in FY18.
- Overall, the total assets and liabilities for FY18 stood at Rs 1,063 billion as against Rs 1,033 billion during FY17, thereby witnessing a growth of 3%.

TCS Balance Sheet as on March 2018

No. of Mths Year Ending		**12 Mar-17***	**12 Mar-18***	**% Change**
Networth	Rs m	862,140	849,561	-1.5
Current Liabilities	Rs m	145,120	178,280	22.9
Long-term Debt	Rs m	710	540	-23.9
Total Liabilities	Rs m	1,032,520	1,062,960	2.9
Current assets	Rs m	803,160	812,240	1.1
Fixed Assets	Rs m	132,420	132,510	0.1
Total Assets	Rs m	1,032,520	1,062,960	2.9

Current Valuations for TCS:

- The trailing twelve-month earnings per share (EPS) of the company stands at Rs 135.2, an improvement from the EPS of Rs 133.8 recorded last year.
- The price to earnings (P/E) ratio, at the current price of Rs 1,975.0, stands at 13.9 times its trailing twelve months earnings.
- The price to book value (P/BV) ratio at current price levels stands at 6.2 times, while the price to sales ratio stands at 4.3 times.
- The company's price to cash flow (P/CF) ratio stood at 13.6 times its end-of-year operating cash flow earnings.

Per Share Data/Valuations

No. of Mths Year Ending		**12 Mar-17***	**12 Mar-18***
Sales per share (Unadj.)	Rs	598.7	643.1
TTM Earnings per share	Rs	133.8	135.2
Diluted earnings per share	Rs	137.7	135.2
Price to Cash Flow	x	13.7	13.6
TTM P/E ratio	x	14.3	13.9
Price / Book Value ratio	x	5.5	6.2
Market Cap	Rs m	3,891,599	3,780,717
Dividends per share (Unadj.)	Rs	47.0	29.0

Ratio Analysis for TCS

Solvency Ratios

Current Ratio:

The company's current ratio improved and stood at 4.6x during FY18, from 5.5x during FY17. The current ratio measures the company's ability to pay short-term and long-term obligations.

Interest Coverage Ratio:

The company's interest coverage ratio deteriorated and stood at 656.6x during FY18, from 1,079.5x during FY17. The interest coverage ratio of a company states how easily a company can pay its interest expense on outstanding debt. A higher ratio is preferable.

Profitability Ratios

Return on Equity (ROE): The ROE for the company declined and down at 30.5% during FY18, from 30.6% during FY18. The ROE measures the ability of a firm to generate profits from its shareholders capital in the company.

Return on Capital Employed (ROCE): The ROCE for the company improved and stood at 40.2% during FY18, from 40.0% during FY17. The ROCE measures the ability of a firm to generate profits from its total capital (shareholder capital plus debt capital) employed in the company.

Return on Assets (ROA): The ROA of the company declined and down at 24.4% during FY18, from 25.6% during FY17. The ROA measures how efficiently the company uses its assets to generate earnings.

SUGGESTIONS

In the challenging economic climate, IT companies should find new ways and means to stimulate growth, improve financial performance and reduce risk. The following are the suggestions offered to improve the financial performance of these companies.

- Working capital tied up in cash flow is quickly being seen as a 'hidden reservoir' of efficiencies that can be tapped to fund growth strategies, such as capital expansion. Cash flow locked in receivables can be freed up by using a recipe of business process improvements, specialized technology and effective change management.

- Free cash flow is a measure of how well corporations are generating cash after capital expenditures. It is increasingly being seen as a signpost of corporate efficiency. As the IT companies improve their working capital management, their free cash flow also increases and subsequent increases in shareholder value.

- The pressure to improve margins and profitability has led many ITcompanies to take a two – pronged approach to centralizing financefunctions, along with leveraging third party service providers. Credit,receivables and payable functions are not exceptions to this, and are primecandidates for shared services, where a smaller specialized team ofprofessionals services for the global business units.
- Balancing receivables and payables performance both in house andoutsourcing teams is critical to ensure financial success. This often requires aspecialized technology platform with multi-language and multi-currencycapabilities that both teams can use, while offering measurement and management capabilities to finance executives.
- While the daily operational aspects of managing cash flow are done at thelevels of credit, collections and payable departments, the job of optimizing short term liquidity is often done by treasury and corporate finance departments. These personnel have the task of accurately forecasting cash 244 from receivables and payables and managing any gaps in liquidity.
- The problem of excessive investments in the IT companies can largely betackled through improved coordination in the functioning of some strategic departments such as finance, personnel, purchase and maintenance. For ensuring effective coordination, strengthening up of management information system in IT companies is essential.
- IT companies need to adopt weekly reporting system in respect of Cash andbank balances. Moreover, the responsibility for arranging funds to meet theworking capital requirements should not be thrust upon the financemanagers only, rather it should be made a collective responsibility of all themiddle level managers.

- During the course of research investigation, it has been found that themanagement normally consider the liability aspects of the selected ITcompanies. It is important that these companies do not pay much attention tothe profitability of funds employed in it. That is why, the main problem ofthese companies is to invest in various current assets without properfinancial analysis. To overcome this difficulty, the management shouldconsidered working capital as equally important and realize that only properbalancing of liquidity and profitability would ensure efficient financialoperations.
- Cash management in IT companies can be streamlined by proper planningand control of cash. These IT companies must increasingly adopt objectivemethods rather than intuitive methods of cash forecasting. Moreover, cashinflows and outflows must be individually managed.
- As better financial performance needs, frequent financial decision making. Itis proposed that every IT company should set up a separate ‘portfolio’ to keepvigilance on the global environmental conditions and economic trends.

AIM:

TO prepare a collection of difference sources of long term financing of a business unit

Procedures:

Sources of Short-Term and Long-Term Financing for Working Capital

A constant flow of working capital is an intrinsic component of a successful business. This is especially true considering the outflow that is a part and parcel of every cycle: salaries and wages need to be paid; raw materials need to be purchased and equipment need to be serviced; funds are needed for marketing, advertising, and other general overhead costs; reserves are required till the customers make their payment. Working capital is truly the lifeline for any company.

Short Term Financing

Banks can be an invaluable source of short term working capital finance.

1. Overdraft Agreement:

By entering into an overdraft agreement with the bank, the bank will allow the business to borrow up to a certain limit without the need for further discussion. The bank might ask for security in the form of collateral and they might charge daily interest at a variable rate on the outstanding debt. However, if the business is confident of making the repayments quickly, then an overdraft agreement is a valuable source of financing, and one that many companies resort to.

2. Accounts Receivable Financing:

Many banks and non-banking financial institutions provide invoice discounting facilities. The company takes the commercial bills to the bank which makes the payment minus a small fee.

Then, on the due date the bank collects the money from the customer. This is another popular method of financing especially among small traders. Businesses that offer large terms of credit can carry on their operations without having to wait for the customers to settle their bills.

3. Customer Advances:

There are many companies that insist on the customer making an advance payment before selling them goods or providing a service. This is especially true while dealing with large orders that take a long time to fulfill. This method also ensures that the company has some funds to channelize into its operations for fulfilling those orders.

4. Selling Goods on Installment:

Many companies, especially those that sell television sets, fans, radios, refrigerators, vehicles and so on, allow customers to make their payments in installments. Since many of these items have become modern day essentials, their customers might not come from well-to-do backgrounds or the cost of the product might be too prohibitive for immediate payment. In such a case, instead of waiting for a large payment at the end, they allow the customers to make regular monthly payments. This ensures that there is a constant flow of funds coming into the business that does not choke up the accounts receivable numbers.

Long-Term Financing

Relying purely on short-term funds to meet working capital needs is not always prudent, especially for industries where the manufacture of the product itself takes a long time:

automobiles, aircraft, refrigerators, and computers. Such companies need their working capital to last for a long time, and hence they have to think about long term financing.

1. Long-Term Loan from a Bank:

Many companies opt for a full-fledged long term loan from a bank that allows them to meet all their working capital needs for two, three or more years.

2. Retain Profits:

Rather than making dividend payments to shareholders or investing in new ventures, many businesses retain a portion of their profits so that they may use it for working capital. This way they do not have to take loans, pay interest, incur losses on discounted bills, and they can be self-sufficient in their financing.

3. Issue Equities and Debentures:

In extreme cases when the business is really short of funds, or when the company is investing in a large-scale venture, they might decide to issue debentures or bonds to the general public or in some cases even equity stock. Of course, this will be done only by conglomerates and only in cases when there is a need for a huge quantum of funds.

Companies cannot rely only on limited sources for their working capital needs. They need to tap multiple avenues. They also need to constantly evaluate what their needs are, through analysis of financial statements and financial ratios, and choose their working capital channels judiciously.

This is an ongoing process, and different routes are appropriate at different points in time. The trick is to choose the right alternative as per the situation.

Long-Term Financing Options Are:

Depending on your business type and size, there are various long-term sources of finance available. These include:

- Equity shares
- Preference shares
- Venture funding
- Term loans
- Bonds and debentures
- Retained earnings

EX NO 6

Aim:

To prepare of dividend policy in current corporate practice of a company

Algorithim:

The issue of dividends and dividend policy is of great significance to owners of closely held and family businesses and deserves considered attention.

(Net) Earnings of a Business

The earnings of a business can be expressed by the simple equation:

Earnings = Total Revenue – Total Cost

Costs include all the operating costs of a business, including taxes.

(Net) Cash Flow

Companies have non-cash charges like depreciation and amortization related to fixed assets and intangible assets. They also have cash charges for things that don't flow through the income statement. Capital expenditures for plant and equipment, buildings, computers and other fixed assets are netted against depreciation and amortization, and the result is either positive or negative in a given year. Capital expenditures tend to be "lumpy" while the related depreciation expenses are amortized over a period of years, often causing swings in the net of the two.

Net Cash Flow is the Source of Good Things

We focus on cash flow because it is the source of all good things that come from a business. The current year's cash flow for a business is, for example, the source of:

Long-term debt repayment. Paying debt is good. Bankers are extremely focused on cash flow, because they only want to lend long-term funds to businesses that have the expectation of sufficient cash flow to repay the debt, including principal and interest on the scheduled basis. Interest expense has already been paid when we look at net cash flow. Companies borrow on a long-term basis to finance a number of things like land, buildings and equipment, software and hardware, and many other productive assets that may be difficult to finance currently. They may also borrow on a long term basis to finance stock repurchases or special dividends.

Reinvestment for future growth. Investment in a business is good if adequate returns are available. If a company generates positive cash flow in a given year, it is available to reinvest in the business to finance its future growth. Reinvested earnings are a critical source of investment capital for closely held and private companies Reinvesting with the expectation of future growth (in dividends and capital gains) is an important source of shareholder returns, but the return is deferred, at least in the form of cash, until a future date.

Dividends or distributions. Corporate dividends are also good, particularly if you are a recipient. Cash flow is also the normal source for dividends (for C corporation owners) or what we call "economic distributions," or distributions net of shareholder pass-through taxes (for S corporation and LLC owners).

Assuming that there were no realized capital gains from a business during a given year, the annual return (AR) is measured as follows:

$$AR = \frac{(\text{Dividends} + \text{Unrealized Appreciation})}{\text{Beginning Portfolio Balance}}$$

Now, we add to this any discretionary expenses that are above market or not normal operating expenses of the business that are taken out by owners:

$$AR = \frac{\left(\text{Dividends} + \text{Discretionary Benefits} + \text{Unrealized Appreciation}\right)}{\text{Beginning Value of a Business}}$$

We now know what dividends are, and they include discretionary benefits that will likely be ceased and normalized into earnings in the event of a sale.

The main consideration in determining the dividend policy is the objective of maximisation of wealth of shareholders. Thus, a firm should retain the earnings if it has profitable investment opportunities, giving a higher rate of return than the cost of retained earnings, otherwise it should pay them as dividends.

EX.NO 8

Aim:

To preparation of the principal yardsticks for measuring financial charcterstic of investment proposal

Procedures:

Yardsticks

The third form1 of incentive regulation provides competition between comparable operators in separate markets. When using this form of regulation, regulators generally should choose performance measures that are general in nature and that operators can affect. An example of a general performance measure might be cost per kilowatt hour and an example of a more granular performance measure might be line maintenance cost per kilowatt hour. General performance measures allow operators to make economic tradeoffs – for example, between capital investments and operating expenses – while granular performance measures restrict the means by which operators can improve measured performance. In addition to being used for regulating overall price levels, benchmarking can be used for regulating such items as service quality and network expansion.

Financial Performance:

The first priority is to identify and understand the overall impact that the various financial realities represented by your KPI numbers have on your business. Then, use the insights you

acquire from these invaluable financial management performance indicators to identify and implement changes that correct problems with policies, processes, personnel, or products that are impacting one or more of your KPI values.

Primary KPIs that you're undoubtedly already using include revenue, expense, gross profit, and net profit. Here are other key indicators that should be tracked, analyzed, and acted upon as needed.

1. Operating Cash Flow

Monitoring and analyzing your Operating Cash Flow is an essential for understanding your ability to pay for deliveries and routine operating expenses. This KPI is also used in comparison with total capital you have in use—an analysis that reveals whether or not your operations are generating sufficient cash for support of capital investments you are making to advance your business.

The analysis of your ratio of operating cash flow compared to your total capital employed gives you deeper insight into your business's financial health, allowing you to look beyond just profits, when making capital investment decisions.

2. Working Capital

Cash that is immediately available is "working capital". Calculate your Working Capital by subtracting your business's existing liabilities from its existing assets. Cash on hand, accounts

receivable, short-term investments are all included, as well as accounts payable, accrued expenses, and loans are all part of this KPI equation.

This especially meaningful KPI informs you of the condition of your business in terms of its available operating funds, by showing the extent to which your available assets can cover your short-term financial liabilities.

3. Current Ratio

While the Working Capital KPI discussed above subtracts liabilities from assets, the Current Ratio KPI divides total assets by liabilities to give you an understanding the solvency of your business—i.e., how well your company is positioned to meet its financial obligations consistently on time and to maintain a level of credit rating that is required to order to grow and expand your business.

4. Debt to Equity Ratio

Debt to Equity is a ratio calculated by looking at your business's total liabilities in contrast to your shareholders' equity (net worth). This KPI indicates how well your business is funding its growth and how well you are utilizing your shareholders' investments. The number indicates how profitable the business is. It tells you and your shareholders how much debt the business has accrued in effort to become profitable. A high debt-to-equity ratio reveals a practice of paying for growth by accumulating debt. This critical KPI helps you focus on your financial accountability.

5. LOB Revenue Vs. Target

This KPI compares your revenue for a line of business to your projected revenue for it. Tracking and analyzing discrepancies between the actual revenues and your projections helps you understand how well a particular department is performing financially. This is one of the two primary factors in the calculation of the Budget Variance KPI—the comparison between projected and actual operating budget totals, which is necessary in order for you to budget more accurately for needs.

6. LOB Expenses Vs. Budget

Comparing actual expenses to the budgeted amount produces this KPI. The comparison helps you understand where and how some budgeted spending went off track, so that you can budget more effectively going forward. Expenses vs. Budget is the other primary factor of the Budget Variance KPI. Knowing the amount of variance between the total assumed and total actual ratio of revenues to expenses helps you become an expert on the relationship between your business's operations and finances.

7. Accounts Payable Turnover

The Accounts Payable Turnover KPI shows the rate at which your business pays off suppliers. The ratio is the result of dividing the total costs of sales during a period (the costs your company incurred while supplying its goods or services), by your average accounts payable for that period.

This is a very informative ratio when compared over multiple periods. A declining accounts payable turnover KPI may indicate that the length of time your company is taking to pay off

its suppliers is increasing and that action is required in order to keep your good standing with your vendors, and to enable your business to take advantage of significant time-driven discounts from vendors.

8. Accounts Receivable Turnover

The accounts receivable turnover KPI reflects the rate at which your business is successfully collecting payments due from your customers. This KPI is calculated by dividing your total sales for a period by your average accounts receivable for that period. This number can serve as an alert that corrections need to be made in managing receivables, in order to bring payment collections within appropriate timeframes.

9. Inventory Turnover

Inventory continuously flows in and out of your production and warehousing facilities. It can be hard to visualize the amount of turnover that is actually taking place. The inventory turnover KPI allows you to know how much of your average inventory your company has sold in a period. This KPI is calculated by dividing sales within a given period by your average inventory in the same period. The KPI gives you a picture of your company's sales strength and production efficiency.

10. Return on Equity

The Return on Equity (ROE) KPI measures your company's net income in contrast to each unit of shareholder equity (net worth). By comparing your company's net income to its

overall wealth, your ROE indicates whether or not your net income is appropriate for your company's size.

Regardless of how much your company is currently worth (its net worth), your current net income will determine its probable worth in the future. Therefore, your business's ROE ratio both informs you of the amount of your organization’s profitability and quantifies its general operational and financial management efficiency. An improving, or high ROE clearly indicates to your shareholders that their investments are being optimized to grow the business.

11. Quick Ratio

Your Quick Ratio KPI measures your organization's ability to utilize its highly liquid assets to immediately meet your business's short-term financial responsibilities. This is the measurement of your company’s wealth and financial flexibility. It is understood as a more conservative evaluation of a business's fiscal health than the Current Ratio, because calculation of the Quick Ratio excludes inventories from assets.

This Quick Ratio KPI has the popular nickname of "Acid Test" (after the nitric acid test used in detecting gold). Similarly, the Quick Ratio is a quick and easy way of assessing the wealth and health of your company. If you’ are a new adopter of KPIs, the Quick Ratio KPI is a good approach to getting a quick view of your business’s overall health.

12. Customer Satisfaction

While budget-linked KPIs are important, the ultimate indicator of a company's potential for long-term success is in its Customer Satisfaction quantification. The Net Promoter Score (NPS) is the result of calculating the various levels of positive response that customers provide on very brief customer satisfaction surveys. The NPS a simple and accurate measurement of likely rates of customer retention (future sales to current customers) across your revenue base, and of potential for generating referral business to grow that base.

Investment Proposals:

There is no standard application form for IFC financing. A company or entrepreneur, foreign or domestic, seeking to establish a new venture or expand an existing enterprise can approach IFC directly. This is best done by reading how to apply for financing, and by submitting an investment proposal.

Proposals can be submitted to IFC’s industry departments; regional departments at IFC headquarters in Washington; or the regional field office closest to the location of the proposed project.

An investment proposal should include the following preliminary information:

- Brief description of project.
- Sponsorship, management & technical assistance:
- History and business of sponsors, including financial information.
- Proposed management arrangements and names and curricula vitae of managers.

- Description of technical arrangements and other external assistance (management, production, marketing, finance, etc.).

3. Market & sales:

Projected production volumes, unit prices, sales objectives, and market share of proposed venture.

Potential users of products and distribution channels to be used.

Present sources of supply for products.

Future competition and possibility that market may be satisfied by substitute products.

Tariff protection or import restrictions affecting products.

Critical factors that determine market potential.

4. Technical feasibility, manpower, raw material resources & environment:

Comments on special technical complexities and need for know-how and special skills.

Possible suppliers of equipment.

Availability of manpower and of infrastructure facilities (transport and communications, power, water, etc.).

Breakdown of projected operating costs by major categories of expenditures.

Source, cost, and quality of raw material supply and relations with support industries.

Import restrictions on required raw materials.

Proposed plant location in relation to suppliers, markets, infrastructure, and manpower.

Proposed plant size in comparison with other known plants.

Potential environmental issues and how these issues are addressed.

5. Investment requirements, project financing, and returns:

Proposed financial structure of venture, indicating expected sources and terms of equity and debt financing.

Type of IFC financing (loan, equity, quasi-equity, a combination of financial products, etc.) and amount.

Projected financial statement, information on profitability, and return on investment.

Critical factors determining profitability.

6. Government support & regulations:

Specific government incentives and support available to project.

Expected contribution of project to economic development.

Outline of government regulations on exchange controls and conditions of capital entry and repatriation.

7. Timetable envisaged for project preparation and completion.

Ex.No:9

Aim:

To preparation of evaluation of different methods used for ranking of investment proposal

Procedures:

Ranking Investment Proposals:

Several methods are commonly used to rank investment proposals, including NPV, IRR, PI, payback period, and ARR.

Net Present Value (NPV):

NPV can be described as the "difference amount" between the sums of discounted: cash inflows and cash outflows. In the case when all future cash flows are incoming, and the only outflow of cash is the purchase price, the NPV is simply the PV of future cash flows minus the purchase price (which is its own PV). The higher the NPV, the more attractive the investment proposal. NPV is a central tool in discounted cash flow (DCF) analysis and is a standard method for using the time value of money to appraise long-term projects. Used for capital budgeting and widely used throughout economics, finance, and accounting, it measures the excess or shortfall of cash flows, in present value terms, once financing charges are met.

NPV formula

Each cash inflow/outflow is discounted back to its present value (PV). Then they are summed. Therefore, NPV is the sum of all terms.

In financial theory, if there is a choice between two mutually exclusive alternatives, the one yielding the higher NPV should be selected. The rules of decision making are:

When NPV > 0, the investment would add value to the firm so the project may be accepted

When NPV < 0, the investment would subtract value from the firm so the project should be rejected

When NPV = 0, the investment would neither gain nor lose value for the firm. We should be indifferent in the decision whether to accept or reject the project. This project adds no monetary value. Decision should be based on other criteria (e.g., strategic positioning or other factors not explicitly included in the calculation).

An NPV calculated using variable discount rates (if they are known for the duration of the investment) better reflects the situation than one calculated from a constant discount rate for the entire investment duration.

Internal Rate of Return (IRR)

The internal rate of return on an investment or project is the "annualized effective compounded return rate" or "rate of return" that makes the net present value (NPV as NET*1/(1+IRR)^year) of all cash flows (both positive and negative) from a particular investment equal to zero.

IRR calculations are commonly used to evaluate the desirability of investments or projects. The higher a project's IRR, the more desirable it is to undertake the project. Assuming all projects require the same amount of up-front investment, the project with the highest IRR would be considered the best and undertaken first.

Profitability Index (PI)

It is a useful tool for ranking projects, because it allows you to quantify the amount of value created per unit of investment. The ratio is calculated as follows:

Profitability index = PV of future cash flows / Initial investment

As the value of the profitability index increases, so does the financial attractiveness of the proposed project. Rules for selection or rejection of a project:

If PI > 1 then accept the project

If PI < 1 then reject the project

Payback Period

Payback period intuitively measures how long something takes to "pay for itself. " All else being equal, shorter payback periods are preferable to longer payback periods. Payback period is widely used because of its ease of use despite the recognized limitations: The time value of money is not taken into account.

Accounting Rate of Return (ARR)

The ratio does not take into account the concept of time value of money. ARR calculates the return, generated from net income of the proposed capital investment. The ARR is a percentage return. Say, if ARR = 7%, then it means that the project is expected to earn seven cents out of each dollar invested. If the ARR is equal to or greater than the required rate of return, the project is acceptable. If it is less than the desired rate, it should be rejected. When comparing investments, the higher the ARR, the more attractive the investment. Basic formulae:

ARR = Average profit / Average investment

The process for selecting capital projects can require much thought and analysis. Many financial evaluation methods have been employed to determine whether to accept or reject a project. Choosing the correct method for ranking projects can be complicated when a choice must be made between mutually exclusive projects. (When projects are mutually exclusive, only one project can be chosen and the others must be abandoned.) The choice in this case must be made based on the ranking of projects in order of increasing shareholder wealth. Choices are made based on various financial evaluation methods, one of which is to discount future net cash flows into present value terms using the cost of capital or a discount rate. Net Present Value (NPV) and Internal Rate of Return (IRR) are the most common methods for ranking projects in terms of the present value of future cash flows. This article will help decision makers determine which of these two evaluation methods—NPV or IRR—is better for evaluating mutually exclusive projects.

Net Present Value Method

The Net Present Value (NPV) Method is "a method of ranking investment proposals using the NPV, which is equal to the present value of future net cash flows, discounted at the marginal cost of capital."1 The equation for NPV is as follows:

NPV Equation

In this equation, CFt represents the expected cash flow at the Period t, k represents the cost of capital, and n is the life of the project. When NPV is zero, the project's cash flows are great

enough to meet the project's required rate of return and pay back the capital invested. When NPV is positive, there are enough cash flows to pay back the project's debt and provide a return to shareholders. NPV is also expressed as a dollar value, which provides a good indicator of profitability and growth in shareholder wealth.

Internal Rate of Return Method

The Internal Rate of Return (IRR) Method is "a method of ranking investment proposals using the rate of return on an investment, calculated by finding the discount rate that equates the present value of future cash inflows to the project's cost" 1. It is the rate that forces NPV to equal 0 as shown in the following equation.

NPV = Equation

The IRR is always expressed as a percentage. For a project to be acceptable under the IRR method, the discount rate must exceed the project's cost of capital, otherwise known as the hurdle rate. An IRR less than the hurdle rate represents a cost to shareholders, while an IRR greater than the hurdle rate represents a return on investment, increasing shareholder wealth.

We must first analyze the reinvestment rate assumptions for each evaluation method. The NPV method assumes that cash flows will be reinvested near or at the project's current cost of capital, while the IRR method assumes that the firm can reinvest cash flows at the project's IRR. The assumption that the firm will reinvest its cash flows at the current cost of capital is more realistic than the assumption that cash flows can be reinvested at the projects IRR. This is because the IRR may not reflect the true rate at which cash flows can be

reinvested. To correct this problem, a modified IRR (MIRR) is used that incorporates the cost of capital as the reinvestment rate; however, the NPV method still has the advantage when compared to the MIRR method (an example is when IRR and MIRR methods return conflicting results under certain project conditions).

The NPV and IRR methods will return conflicting results when mutually exclusive projects differ in size, or differences exist in the timing of cash flows. When mutually exclusive projects exhibit these attributes, their NPV profiles will cross when plotted on a graph. This point at which they cross is defined as the crossover rate, which happens because one project's NPV is more sensitive to the discount rate caused by the differences in the timing of cash flows. In most cases, utilizing either the NPV or IRR method will lead to the same accept-or-reject decision. An exception exists when evaluating mutually exclusive projects with crossing NPV profiles and the cost of capital is less than the crossover rate. When these conditions are present, the NPV and IRR results will conflict in which project to accept or reject. Because the NPV method uses a reinvestment rate close to its current cost of capital, the reinvestment assumptions of the NPV method are more realistic than those associated with the IRR method.

NPV also has an advantage over IRR when a project has non-normal cash flows. Non-normal cash flows exist if there is a large cash outflow during or at the end of the project. The presence of non-normal cash flows will lead to multiple IRRs. Hence, the IRR method cannot be employed in the evaluation process. Mathematically, this problem will not occur if

the NPV method is employed. The NPV method will always lead to a singular correct accept-or-reject decision.

In conclusion, NPV is a better method for evaluating mutually exclusive projects than the IRR method. The NPV method employs more realistic reinvestment rate assumptions, is a better indicator of profitability and shareholder wealth, and mathematically will return the correct accept-or-reject decision regardless of whether the project experiences non-normal cash flows or if differences in project size or timing of cash flows exist.

The Martin Company is considering the four different investment opportunities. The selected information about each proposal is given below:

	Project 1	Project 2	Project 3	Project 4	Project 5
Investment required	$ (960,000)	$(720,000)	$(540,000)	$ (900,000)	$(800,000)
Present value of cash inflows	1,134,540	866,800	672,280	1,045,940	759,520
Net present value	$ 174,540	$ 146,800	$ 132,280	$ 145,940	(40,480)
Project life	6 years	12 years	6 years	3 years	5 years
Internal rate of return	16%	14%	18%	19%	8%

Required:

Compute the profitability index (present value index) for all the projects.

Rank the four investment projects according to preference using:

(a). net present value (NPV).

(b). profitability index (PI).

(c). internal rate of return (IRR).

Which one is the best approach for Martin Company to rank five competing projects?

Solution:

(1). Computation of profitability index:

Formula of profitability/present value index is:

Profitability index = Present value of cash inflows/Investment require

Project 1: rs1,134,540/rs960,000 = 1.18

Project 2: rs866,800/rs720,000 = 1.20

Project 3: rs672,280/rs540,000 = 1.24

Project 4: rs1,045,490/rs900,000 = 1.16

Project 5: rs759,520/rs800,000 = 0.95

3. The best ranking approach:

The best method of ranking projects depends on the availability of good reinvestment opportunities. Under internal rate of return (IRR) method, we assume that the funds released from a project are reinvested in another project yielding the internal rate of return equal to the previous project. According to IRR, the project 4 is ranked at number one with 19% IRR. It means any funds released from project 4 must be reinvested in another project yielding an internal rate of return of at least 19% but It might be difficult to find a project with such a high IRR.

The profitability index (PI) shows the present value of cash inflow generated by each dollar invested in a project. It assumes that the funds released from a project are reinvested in another project with a return equal to the discount rate. In our problem, the discount rate is

only 10%. Generally, the profitability index is considered the most dependable method of ranking competing projects.

The net present value (NPV) method considers the net present value figure but does not take into account the amount of investment required for the project. Therefore, this method is not appropriate for comparing or ranking competing projects that require different amounts of investment. For example, project 3 is ranked at number four because of its low net present value but it is the best option if we see at the present value of net cash inflow generated by each dollar invested in the project (as shown by the profitability index).

Conclusion: From above discussion, we can conclude that the profitability index is the most appropriate and dependable method of ranking projects for Martin Company.

Ex.No:10

Aim :

To prepare and analysis the cost of capital and leverages

Procedures:

A multinational company, known more commonly as a multinational corporation or transnational corporation in North America, is a business with branches, offices or production facilities in more than one country.

Some people say that any firm that derives at least one quarter of all its business abroad is considered a multinational corporation. However, if all that foreign business comes purely from exports and the company has no offices, premises or production facilities abroad, it is not a multinational.

Muliti National Company:

International Business Machines (IBM), is a global technology company that provides hardware, software, cloud-based services and cognitive computing.

ounded in 1911 following the merger of four companies in New York State by Charles Ranlett Flint, it was originally called Computing-Tabulating-Recording Company. It would be renamed to IBM in 1924.

Given that the company is over 100 years old it is no surprise that it has had to adjust to different technological trends throughout the decades.

The company is now transitioning from being an infrastructure player to one that is more cloud and data driven.

Nicknamed ‘Big Blue’, the company offers cloud products in the shape of Bluemix, a SoftLayer cloud, and data analytics, or cognitive computing capabilities, with the Watson supercomputer.

While the company has expanded its portfolio from server hardware, this is still an area that it operates in with the z Series mainframe.

The company also offers software with the likes of its DB2 database offering, and IBM SPSS.

GinniRometty, IBM CEO, said: “Digital is the wires, but digital intelligence, or artificial intelligence as some people call it, is about much more than that. This next decade is about how you combine those and become a cognitive business. It’s the dawn of a new era.”

IBM has been focused on continuous innovation for more than a century. Patenting is an important barometer of that innovation, and IBM has topped the annual list of U.S. patent recipients for the 20th consecutive year.

Cost of Capital:

ith trillions of dollars in cash sitting on their balance sheets, corporations have never had so much money. How executives choose to invest that massive amount of capital will drive corporate strategies and determine their companies' competitiveness for the next decade and beyond. And in the short term, today's capital budgeting decisions will influence the developed world's chronic unemployment situation and tepid economic recovery.

Although investment opportunities vary dramatically across companies and industries, one would expect the process of evaluating financial returns on investments to be fairly uniform. After all, business schools teach more or less the same evaluation techniques. It's no surprise, then, that in a survey conducted by the Association for Financial Professionals (AFP), 80% of more than 300 respondents—and 90% of those with over $1 billion in revenues—use discounted cash-flow analyses. Such analyses rely on free-cash-flow projections to estimate the value of an investment to a firm, discounted by the cost of capital (defined as the weighted average of the costs of debt and equity). To estimate their cost of equity, about 90% of the respondents use the capital asset pricing model (CAPM), which quantifies the return required by an investment on the basis of the associated risk.

But that is where the consensus ends. The AFP asked its global membership, comprising about 15,000 top financial officers, what assumptions they use in their financial models to quantify investment opportunities. Remarkably, no question received the same answer from a

majority of the more than 300 respondents, 79% of whom are in the U.S. or Canada. (See the exhibit “Dangerous Assumptions.”)

The Risk-Free Rate

Errors really begin to multiply as you calculate the cost of equity. Most managers start with the return that an equity investor would demand on a risk-free investment. What is the best proxy for such an investment? Most investors, managers, and analysts use U.S. Treasury rates as the benchmark. But that’s apparently all they agree on. Some 46% of our survey participants use the 10-year rate, 12% go for the five-year rate, 11% prefer the 30-year bond, and 16% use the three-month rate. Clearly, the variation is dramatic. When this article was drafted, the 90-day Treasury note yielded 0.05%, the 10-year note yielded 2.25%, and the 30-year yield was more than 100 basis points higher than the 10-year rate.

In other words, two companies in similar businesses might well estimate very different costs of equity purely because they don’t choose the same U.S. Treasury rates, not because of any essential difference in their businesses. And even those that use the same benchmark may not necessarily use the same number. Slightly fewer than half of our respondents rely on the current value as their benchmark, whereas 35% use the average rate over a specified time period, and 14% use a forecasted rate.

The Equity Market Premium

The next component in a company’s weighted-average cost of capital is the risk premium for equity market exposure, over and above the risk-free return. In theory, the market-risk premium should be the same at any given moment for all investors. That’s because it’s an

estimate of how much extra return, over the risk-free rate, investors expect will justify putting money in the stock market as a whole.

The estimates, however, are shockingly varied. About half the companies in the AFP survey use a risk premium between 5% and 6%, some use one lower than 3%, and others go with a premium greater than 7%—a huge range of more than 4 percentage points. We were also surprised to find that despite the turmoil in financial markets during the recent economic crisis, which would in theory prompt investors to increase the market-risk premium, almost a quarter of companies admitted to updating it seldom or never.

International Business Machines's Leverage Ratio

IBM's quarterly Leverage Ratio and Total Liabilities, Equity growth

IBM Leverage Ratio	(Dec 31 2018) IV. Quarter	(Sep 30 2018) III. Quarter	(Jun 30 2018) II. Quarter	(Mar 31 2018) I. Quarter	(Dec 31 2017) IV. Quarter
Y / Y Equity Change	*-4.49 %*	*0.81 %*	*0.56 %*	*-0.86 %*	*-3.63 %*
Y / Y Total Liabilities Change	*3.23 %*	*0.19 %*	*5.77 %*	*13.18 %*	*4.06 %*
Leverage Ratio MRQ	**6.3**	**5.13**	**5.53**	**5.86**	**5.83**
Overall Ranking	#	#	#	#	#
Seq. Equity Change	*-15.01 %*	*6.81 %*	*1.96 %*	*3.19 %*	*-10.28 %*
Seq. Total Liabilities	*4.29 %*	*-0.87 %*	*-3.75 %*	*3.75 %*	*1.22 %*

Change					

Result:

In designing the capital structure for any firm, the first major policy decision facing the firm is that of determining the appropriate level of debt. For most of the firms, the decision involves a choice between the long-term debt and the equity. The firm's debt capacity may be best defined not as the maximum amount which the lenders or debt investors are willing to lend to the firm, but as the amount of debt that the firm should us

Ex.No:11

Aim:

To prepare source of working capital for a new starting new business

Procedure:

Sources of working capital can be spontaneous, short term and long term. Spontaneous working capital includes mainly trade credit such as the sundry creditor, bills payable, and notes payable. Short term sources are tax provisions, dividend provisions, bank overdraft, cash credit, trade deposits, public deposits, bills discounting, short-term loans, inter-corporate loans, and commercial paper. Long-term sources are retained profits, provision for depreciation, share capital, long-term loans, and debentures.

Spontaneous Sources	**Short Term Sources**		**Long Term Sources**	
	Internal Sources	**External Sources**	**Internal Sources**	**External Sources**
Trade Credit	*Tax Provisions*	*Bank Overdraft*	*Retained Profits*	*Share Capital*
Sundry Creditors	*Dividend Provisions*	*Trade Deposits*	*Depreciation Provision*	*Long Term Loans*

Spontaneous Sources	Short Term Sources	Long Term Sources
Bills Payable	*Public Deposits*	*Debentures*
Notes Payable	*Bills Discounting*	
Accrued Expenses	*Short Term Loans*	

SPONTANEOUS SOURCES OF WORKING CAPITAL FINANCE

The word ‘spontaneous’ itself explains that this source of working capital is readily or easily available to the business in the normal course of business affairs. The quantum and terms of this credit depend on the industry norms and the relationship between buyer and seller. These sources include trade credit allowed by the sundry creditors, credit from employees, and other trade-related credits. The biggest benefit of spontaneous sources as working capital is its ‘effortless raising’ and ‘insignificant cost’ compared to traditional ways of financing.

List of spontaneous sources of working capital

TRADE CREDIT

SUNDRY CREDITORS

BILLS PAYABLE

NOTES PAYABLE

ACCRUED EXPENSES

The cost factor and the quantum depends a lot on the terms of such credit viz. maximum credit limit, the period of credit, and discount on cash payment. Each supplier will have a maximum credit limit defined for the buyer depending on the business capacity and creditworthiness of the buyer. Similarly, the credit period is defined say 30 days, 45 days etc. Discount on cash payment is allowed to the buyer if the payment immediately on buying the materials. This percentage of discount is an opportunity cost for the buyer.

SHORT TERM SOURCES OF WORKING CAPITAL FINANCE

Short term sources can be further divided into internal and external sources of working capital finance.

TAX PROVISIONS

DIVIDEND PROVISIONS

Short-term External Sources

Short-term working capital financing from banks such as

BANK OVERDRAFTS,

CASH CREDITS,

TRADE DEPOSITS,

BILLS DISCOUNTING,

SHORT-TERM LOANS OR WORKING CAPITAL LOANS,

INTER-CORPORATE LOANS,

COMMERCIAL PAPER, ETC.

Tax and dividend provisions are current liabilities and cannot be delayed. The fund that would have been used in paying these provisions act as working capital till the point these are not paid.

Short-term working capital finance availed from banks and financial institutions are costly compared to spontaneous and long-term sources in terms of rate of interest but have a great time flexibility. Due to time flexibility, the finance manager can use the funds and pay interest on the money which his business utilizes and can pay them anytime when cash is available. Overall, in comparison to long-term sources where you have to hold funds even when not required, these facilities prove cheaper.

LONG-TERM SOURCES OF WORKING CAPITAL FINANCING

Long-term sources can also be divided into internal and external sources. Long-term internal sources of finance are retained profits and provision for depreciation whereas external sources are Share Capital, long-term loan, and debentures.

Working capital can be classified as temporary working capital and permanent working capital. It is advisable to use long-term sources for permanent and short-term sources for temporary working capital requirements. This will optimize the working capital cost and enforce good working capital management practices.

working capital is needed to start a business:

To answer this question, you need to understand how money will flow through your business – in other words, you need to understand your "working capital cycle." The flow or cycle consists of (1) how quickly current assets (e.g. accounts receivables & inventory) are turned into cash and (2) how quickly that cash is used to pay current liabilities (e.g. accounts payable). The working capital cycle is also referred to as the "turnover rates" for accounts receivables, inventory, and accounts payable.

Turnover rates. When starting a business, you will have created projections for key items such as sales, cost of goods sold and other expenses. You also need assumptions on the following: How many days of inventory do you need to keep on hand ("inventory turnover")? How many days will you give customers to pay you (accounts receivable terms)? How many days will your vendors give you to pay them (accounts payable terms)?

Armed with this information, you can calculate how much working capital is needed to start your business. See the example below.

Conclusion

When you start a small business, you will need working capital financing to invest in inventory and accounts receivable. How much money you need for working capital can be estimated by using a formula that uses assumptions on "Turnover Rates" for inventory, accounts receivable, and accounts payable as shown in the example above. If you are a small business owner in need

of working capital financing, avoid the high cost associated with financing products such as factoring, merchant cash advance, and peer-to-peer online lending by exploring alternative, lower cost financing options available through your local CDFI. You can start by learning more about Excelsior Growth Fund's SmartLoan, which offers loans up to $100,000 with affordable monthly payments.

Ex.No:12

Aim:

To prepare and evaluate capital management and give suitable suggestions

Procedures:

TATA CONSULTANCY SERVICES LTD. (TCS):

Tata Consultancy Services Ltd is a leading global IT services consulting and business solutions organization. The company offers a range of IT services outsourcing and business solutions. They also offer IT infrastructure services business process outsourcing services engineering and industrial services global consulting and asset leveraged solutions. Their segments include banking financial services and insurance; manufacturing; retail and distribution and telecom. The company is a part of Tata Group one of India's most respected business conglomerates and most respected brands. They are headquartered in Mumbai. They are having 142 offices in 42 countries as well as 105 delivery centers in 20 countries. The company shares are listed on the National Stock Exchange and Bombay Stock Exchange of India.Tata Consultancy Services Ltd was incorporated in the year 1968. Tata Sons Ltd established the company as division to service their electronic data processing (EDP) requirements and provide management consulting services. In the year 1971 they started their first international assignment. The company pioneered the global delivery model for IT services with their first offshore client in 1974.In the year 1981 the company set up India's first IT R&D division the Tata Research Design and Development Centre at Pune.

Working Capital:

Working capital management is very important element to measure the short term solvency position of a firm and for profitability. Without its proper management, no corporate can run their business smoothly. The purpose of this study is to investigate the impact of working capital management on liquidity, profitability and element of risk on the Infosys and TCS Company. To achieve these objectives, data has been collected from secondary sources and for getting results various kind of financial ratios are used. The financial ratios of both companies are analyzed with paired T-test. This study will help to both companies in management of their working capital and improving short term solvency position of the companies.

Key Financial Ratios of Tata Consultancy Services:

	Mar '17	Mar '16	Mar '15	Mar '14	Mar '18
Investment Valuation Ratios					
Face Value	1.00	1.00	1.00	1.00	1.00
Dividend Per Share	50.00	47.00	43.50	79.00	32.00
Operating Profit Per Share (Rs)	145.25	137.48	137.30	107.36	109.94
Net Operating Profit Per Share (Rs)	508.58	470.42	435.76	375.64	330.18
Free Reserves Per Share (Rs)	--	--	--	--	--
Bonus in Equity Capital	79.13	79.13	79.13	79.59	79.59
Profitability Ratios					

Operating Profit Margin(%)	28.56	29.22	31.50	28.57	33.29
Profit Before Interest And Tax Margin(%)	25.35	26.23	28.55	25.15	30.17
Gross Profit Margin(%)	26.86	27.52	29.80	26.68	31.62
Cash Profit Margin(%)	26.06	25.93	27.37	25.78	28.84
Adjusted Cash Margin(%)	26.06	25.93	27.37	25.78	28.84
Net Profit Margin(%)	25.92	25.51	26.87	26.17	28.56
Adjusted Net Profit Margin(%)	24.46	24.31	25.74	24.67	27.25
Return On Capital Employed(%)	42.00	38.43	45.03	52.77	53.39
Return On Net Worth(%)	33.27	30.31	35.49	42.40	41.87
Adjusted Return on Net Worth(%)	33.27	30.31	35.49	41.23	41.87
Return on Assets Excluding Revaluations	396.31	395.96	329.94	231.87	224.90
Return on Assets Including Revaluations	396.31	395.96	329.94	231.87	224.90
Return on Long Term Funds(%)	42.10	38.53	45.11	52.99	53.39
Liquidity And Solvency Ratios					
Current Ratio	2.85	3.09	3.41	2.78	3.18
Quick Ratio	2.67	2.93	3.27	2.80	3.16
Debt Equity Ratio	--	--	--	0.01	--
Long Term Debt Equity Ratio	--	--	--	--	--
Debt Coverage Ratios					
Interest Cover	1,065.37	1,880.13	2,257.85	302.89	1,006.74
Total Debt to Owners Fund	0.00	0.00	0.00	0.01	0.00

Financial Charges Coverage Ratio	1,120.27	1,978.56	2,370.08	320.41	1,052.90
Financial Charges Coverage Ratio Post Tax	897.27	1,577.75	1,888.23	260.53	836.35
Imported Composition of Raw Materials Consumed	--	--	72.42	71.30	78.95
Selling Distribution Cost Composition	--	--	--	--	--
Expenses as Composition of Total Sales	94.76	93.17	95.36	97.60	96.27
Cash Flow Indicator Ratios					
Dividend Payout Ratio Net Profit	36.78	38.73	34.63	80.35	33.97
Dividend Payout Ratio Cash Profit	34.52	36.31	32.57	74.93	32.09
Earning Retention Ratio	63.22	61.27	65.37	17.38	66.03
Cash Earning Retention Ratio	65.48	63.69	67.43	23.11	67.91
AdjustedCash Flow Times	0.01	0.01	0.01	0.01	0.00

TCS Income Statement Analysis

- Operating income during the year rose 4.4% on a year-on-year (YoY) basis.
- The company's operating profit increased by 0.6% YoY during the fiscal. Operating profit margins witnessed a fall and stood at 26.4% in FY18 as against 27.4% in FY17.
- Depreciation charges and finance costs increased by 1.4% YoY and 62.5% YoY, respectively.
- Other income declined by 13.7% YoY.

- Net profit for the year declined by 1.8% YoY.
- Net profit margins during the year declined from 21.6% in FY17 to 20.4% in FY18.

TCS Income Statement 2017-18

No. of Mths Year Ending		**12 Mar-17***	**12 Mar-18***	**% Change**
Net Sales	Rs m	1,179,660	1,231,040	4.4%
Other income	Rs m	42,210	36,420	-13.7%
Total Revenues	Rs m	1,221,870	1,267,460	3.7%
Gross profit	Rs m	323,110	325,160	0.6%
Depreciation	Rs m	19,870	20,140	1.4%
Interest	Rs m	320	520	62.5%
Profit before tax	Rs m	345,130	340,920	-1.2%
Tax	Rs m	81,560	82,120	0.7%
Profit after tax	Rs m	263,570	258,800	-1.8%
Gross profit margin	%	27.4	26.4	
Effective tax rate	%	23.6	24.1	
Net profit margin	%	21.6	20.4	

TCS Balance Sheet Analysis:

- The company's current liabilities during FY18 stood at Rs 178 billion as compared to Rs 145 billion in FY17, thereby witnessing an increase of 22.9%.
- Long-term debt down at Rs 540 million as compared to Rs 710 million during FY17, a fall of 23.9%.
- Current assets rose 1% and stood at Rs 812 billion, while fixed assets rose 0% and stood at Rs 133 billion in FY18.
- Overall, the total assets and liabilities for FY18 stood at Rs 1,063 billion as against Rs 1,033 billion during FY17, thereby witnessing a growth of 3%.

TCS Balance Sheet as on March 2018

No. of Mths Year Ending		**12 Mar-17***	**12 Mar-18***	**% Change**
Networth	Rs m	862,140	849,561	-1.5
Current Liabilities	Rs m	145,120	178,280	22.9
Long-term Debt	Rs m	710	540	-23.9
Total Liabilities	Rs m	1,032,520	1,062,960	2.9
Current assets	Rs m	803,160	812,240	1.1
Fixed Assets	Rs m	132,420	132,510	0.1
Total Assets	Rs m	1,032,520	1,062,960	2.9

Current Valuations for TCS:

- The trailing twelve-month earnings per share (EPS) of the company stands at Rs 135.2, an improvement from the EPS of Rs 133.8 recorded last year.
- The price to earnings (P/E) ratio, at the current price of Rs 1,975.0, stands at 13.9 times its trailing twelve months earnings.
- The price to book value (P/BV) ratio at current price levels stands at 6.2 times, while the price to sales ratio stands at 4.3 times.
- The company's price to cash flow (P/CF) ratio stood at 13.6 times its end-of-year operating cash flow earnings.

Per Share Data/Valuations

No. of Mths Year Ending		**12 Mar-17***	**12 Mar-18***
Sales per share (Unadj.)	Rs	598.7	643.1
TTM Earnings per share	Rs	133.8	135.2
Diluted earnings per share	Rs	137.7	135.2
Price to Cash Flow	x	13.7	13.6
TTM P/E ratio	x	14.3	13.9
Price / Book Value ratio	x	5.5	6.2
Market Cap	Rs m	3,891,599	3,780,717
Dividends per share (Unadj.)	Rs	47.0	29.0

Ratio Analysis for TCS

Solvency Ratios

Current Ratio:

The company's current ratio improved and stood at 4.6x during FY18, from 5.5x during FY17. The current ratio measures the company's ability to pay short-term and long-term obligations.

Interest Coverage Ratio:

The company's interest coverage ratio deteriorated and stood at 656.6x during FY18, from 1,079.5x during FY17. The interest coverage ratio of a company states how easily a company can pay its interest expense on outstanding debt. A higher ratio is preferable.

Profitability Ratios

Return on Equity (ROE): The ROE for the company declined and down at 30.5% during FY18, from 30.6% during FY18. The ROE measures the ability of a firm to generate profits from its shareholders capital in the company.

Return on Capital Employed (ROCE): The ROCE for the company improved and stood at 40.2% during FY18, from 40.0% during FY17. The ROCE measures the ability of a firm to generate profits from its total capital (shareholder capital plus debt capital) employed in the company.

Return on Assets (ROA): The ROA of the company declined and down at 24.4% during FY18, from 25.6% during FY17. The ROA measures how efficiently the company uses its assets to generate earnings.

SUGGESTIONS

In the challenging economic climate, IT companies should find new ways and means to stimulate growth, improve financial performance and reduce risk. The following are the suggestions offered to improve the financial performance of these companies.

- Working capital tied up in cash flow is quickly being seen as a 'hidden reservoir' of efficiencies that can be tapped to fund growth strategies, such as capital expansion. Cash flow locked in receivables can be freed up by using a recipe of business process improvements, specialized technology and effective change management.

- Free cash flow is a measure of how well corporations are generating cash after capital expenditures. It is increasingly being seen as a signpost of corporate efficiency. As the IT companies improve their working capital management, their free cash flow also increases and subsequent increases in shareholder value.

- The pressure to improve margins and profitability has led many ITcompanies to take a two – pronged approach to centralizing financefunctions, along with leveraging third party service providers. Credit,receivables and payable functions are not exceptions to this, and are primecandidates for shared services, where a smaller specialized team ofprofessionals services for the global business units.
- Balancing receivables and payables performance both in house andoutsourcing teams is critical to ensure financial success. This often requires aspecialized technology platform with multi-language and multi-currencycapabilities that both teams can use, while offering measurement and management capabilities to finance executives.
- While the daily operational aspects of managing cash flow are done at thelevels of credit, collections and payable departments, the job of optimizing short term liquidity is often done by treasury and corporate finance departments. These personnel have the task of accurately forecasting cash 244 from receivables and payables and managing any gaps in liquidity.
- The problem of excessive investments in the IT companies can largely betackled through improved coordination in the functioning of some strategic departments such as finance, personnel, purchase and maintenance. For ensuring effective coordination, strengthening up of management information system in IT companies is essential.
- IT companies need to adopt weekly reporting system in respect of Cash andbank balances. Moreover, the responsibility for arranging funds to meet theworking capital requirements should not be thrust upon the financemanagers only, rather it should be made a collective responsibility of all themiddle level managers.

- During the course of research investigation, it has been found that themanagement normally consider the liability aspects of the selected ITcompanies. It is important that these companies do not pay much attention tothe profitability of funds employed in it. That is why, the main problem ofthese companies is to invest in various current assets without properfinancial analysis. To overcome this difficulty, the management shouldconsidered working capital as equally important and realize that only properbalancing of liquidity and profitability would ensure efficient financialoperations.
- Cash management in IT companies can be streamlined by proper planningand control of cash. These IT companies must increasingly adopt objectivemethods rather than intuitive methods of cash forecasting. Moreover, cashinflows and outflows must be individually managed.
- As better financial performance needs, frequent financial decision making. Itis proposed that every IT company should set up a separate ‘portfolio’ to keepvigilance on the global environmental conditions and economic trends.