Mock Test Paper - Series I: March 2026

Date of Paper: 27th March, 2026

Time of Paper: 10 A.M. – 1 P.M.

INTERMEDIATE: GROUP – II

PAPER – 6A : FINANCIAL MANAGEMENT & STRATEGIC MANAGEMENT

PAPER 6A: FINANCIAL MANAGEMENT

Time Allowed – 3 Hours (Total time for 6A and 6B) **Maximum Marks – 50**

1. *The question paper comprises two parts, Part I and Part II.*
2. *Part I comprises Case Scenario based Multiple Choice Questions (MCQs)*
3. *Part II comprises questions which require descriptive type answers.*
4. *Working note should form part of the answer. Wherever necessary, suitable assumptions may be made by the candidates and disclosed by way of note. However, in answers to Questions in Division A, working notes are not required.*

PART I – Case Scenario based MCQs (15 Marks)

Write the most appropriate answer to each of the following multiple choice questions by choosing one of the four options given. All questions are compulsory.

Case Scenario

XYZ Limited is a mid-sized manufacturing company operating in the industrial equipment sector. The company has been in operation for over 15 years and has established a strong market presence. As part of the annual financial review, the CFO has tasked you, a financial analyst, with analyzing the company's capital structure, determining the cost of capital components and evaluate a proposed investment project. The finance team has compiled the following information from the company's latest financial statements and market data:

Balance Sheet Data (Book Values)

- **Equity Share Capital:** ₹ 15 lakhs
- **Reserves & Surplus:** ₹ 5 Lakhs
- **Book Value of Debt:** ₹ 10 lakhs

Market Data

The market has assigned different valuations to the company's securities:

- **Market Value of Equity:** The current market valuation of equity is 3 times its book value
- **Market Value of Debt:** The current market valuation of debt is 2 times its book value

Weighted Average cost of capital(WACC)

The finance team has calculated the Weighted Average cost of capital of the firm under two different approaches:

1. **As per Book Value:** 10%
2. **As per Market Value:** 10.5%

The company is considering a new project requiring an initial investment of ₹ 20 lakhs. The project has the following additional features:

- **Working Capital Requirement:** ₹ 3 lakhs (fully recoverable at end of Year 3)
- **Salvage Value:** ₹ 2 lakhs (end of Year 3)
- **Depreciation:** Straight-line over 3 years.

Expected Cash Inflows (before depreciation & tax):

Year	Cash Inflows (₹ lakhs)
1	8
2	9
3	10

Assume the tax rate is 25% and the investment rate is 2% more than the Pre tax cost of debt. The project is evaluated based investment rate.

	Year 1	Year 2	Year 3
6%	0.943	0.890	0.840
8%	0.926	0.857	0.794
10%	0.909	0.826	0.751
12%	0.893	0.797	0.712

You are required to answer the following questions (MCQs 1 to 5):

1. Cost of equity is –
   (a) Ke = 6%
   (b) Ke = 8%
   (c) Ke = 12%
   (d) Ke = 10%
2. Cost of debt is –
   (a) Kd = 12%
   (b) Kd = 10%
   (c) Kd = 12%
   (d) Kd = 6%
3. The Net Present Value (NPV) of the project is –
   (a) ₹ 1.35 lakhs
   (b) -₹ 0.55 lakhs
   (c) ₹ 1.14 lakhs
   (d) -₹ 0.95 lakhs
4. The Profitability Index (PI) of the project is –
   (a) 1.05
   (b) 1.08
   (c) 1.10
   (d) 0.98
5. The Discounted Payback Period is approximately –
   (a) 2.32 years
   (b) 2.60 years
   (c) 2.95 years
   (d) 2.89 years **(5 x 2 = 10 Marks)**

6. The capital structure of JKL Limited consists of 12% debentures of ₹ 50 lakhs, 10% preference shares of ₹ 25 lakhs, 14% term loan of ₹ 15 lakhs and equity share capital of ₹ 48 lakhs. Its reserves & surpluses are ₹ 24 lakhs. What would be the capital-gearing ratio?

(a) 1.04

(b) 1.25

(c) 1.33

(d) 1.56 **(2 Marks)**

7. The following information is given for QB Ltd.

Earnings per share	₹ 180
Dividend per share	₹ 45
Cost of capital	17%
Internal Rate of Return on investment	20%

What is the market price per share using Walter's formula:

(a) ₹ 1,200

(b) ₹ 1,800

(c) ₹ 2,250

(d) ₹ 1,960 **(2 Marks)**

8. A firm has sales of ₹ 75,00,000, variable cost of ₹ 42,00,000 and fixed cost of ₹ 6,00,000.

It has a debt of ₹ 45,00,000 at 9% and equity of ₹ 55,00,000. Does it have favourable financial leverage?

(a) ROI is less than interest on loan funds and hence it has no favourable financial leverage.

(b) ROI is equal to interest on loan funds and hence it has favourable financial leverage.

(c) ROI is greater than interest on loan funds and hence it has favourable financial leverage.

(d) ROI is greater than interest on loan funds and hence it has unfavourable financial leverage. **(1 Marks)**

PART II – Descriptive Questions (35 Marks)

*Question No. **1** is compulsory.*

*Attempt any **two** questions out of the remaining **three** questions.*

1. (a) The following information pertains to P Limited for the year ended 31st March, 2025:

Particulars	Amount
Sales	₹ 3,60,00,000
Rate of Income Tax	40%
Return on Net Worth	30%
Share Capital to Reserves Ratio	6 : 4
Current Ratio	2 : 1
Percentage of Net Profit to Sales	8%
Inventory Turnover (based on cost of goods sold)	12
Cost of goods sold	₹ 1,44,00,000
Sundry Debtors	₹ 12,00,000
Sundry Creditors	₹ 16,00,000
Interest on 14% debentures	₹ 3,36,000

You are required to CALCULATE:

(i) Operating Expenses

(ii) Share Capital and Reserves

(iii) Closing Stock

(iv) Fixed Assets **(5 Marks)**

(b) Mr. Raman, a portfolio manager, is analyzing a set of securities using the **Capital Asset Pricing Model (CAPM)**. He has gathered the following information:

Security	Beta	CAPM Return
A Ltd	1.2	15.20%
B Ltd	0.8	12.80%
C Ltd	1.1	?
Cash in hand	?	Nil
Treasury Bill	?	?
Stock Market i.e. Nifty	?	?

(i) Complete the above table with all missing values.

(ii) CAPM explains the relationship between systematic risk and expected return on a security. DISCUSS the nature of the relationship between Beta and expected return under CAPM. **(5 Marks)**

(c) A company wants to invest in a machinery that would cost ₹ 50,000 at the beginning of year 1. It is estimated that the net cash inflows from operations will be ₹ 18,000 per annum for 3 years, if the company opts to service a part of the machine at the end of year 1 at ₹ 10,000. In such a case, the scrap value at the end of year 3 will be ₹ 12,500. However, if the company decides not to service the part, then it will have to be replaced at the end of year 2 at ₹ 15,400. But in this case, the machine will work for the 4th year also and get operational cash inflow of ₹ 18,000 for the 4th year. It will have to be scrapped at the end of year 4 at ₹ 9,000. Assuming cost of capital at 10% and ignoring taxes, will you RECOMMEND the purchase of this machine based on the net present value of its cash flows?

If the supplier gives a discount of ₹ 5,000 for purchase, WHAT would be your decision? (The present value factors at the end of years 0, 1, 2, 3, 4, 5 and 6 are respectively 1, 0.9091, 0.8264, 0.7513, 0.6830, 0.6209 and 0.5644). **(5 Marks)**

2. (a) Zanshu Ltd. is an all equity financed company with a market value of ₹ 25,00,000 and cost of equity (K_e) 21%. The company wants to buyback equity shares worth ₹5,00,000 by issuing and raising 15% perpetual debt of the same amount. Rate of tax may be taken as 30%. After the capital restructuring and applying MM Model (with taxes), you are required to CALCULATE:

(i) Market value of Zanshu Ltd.

(ii) Cost of Equity (K_e)

(iii) Weighted average cost of capital (using market weights) and comment on it. **(6 Marks)**

(b) The following particulars are related to PQR Ltd:

Sales ₹ 1,50,00,000

Variable Cost ₹ 84,00,000

Fixed Cost ₹ 12,00,000

The company has borrowed ₹ 90,00,000 at 10% and its equity capital is ₹ 1,10,00,000.

You are required to CALCULATE:

(i) Return on Investment (ROI).

(ii) Operating and Financial Leverages.

(iii) Combined Leverage.

(iv) Earnings Before Interest and Taxes (EBIT), if the sale is dropped to ₹ 1,00,00,000. **(4 Marks)**

3. Being a financial controller of Shilpa Limited, they have provided you with the debt collection policy of the debtors' ageing analysis as on the date of analysis –

Name of Customers	Current	31 – 60 Days	61 – 90 Days	91 or More Days	Total
Customer A	3,12,500	1,05,000	-	-	4,17,500
Customer B	-	-	3,11,200	-	3,11,200
Customer C	6,81,600	-	-	-	6,81,600
Customer D	-	-	-	1,62,000	1,62,000
Customer E	-	3,01,500	2,10,000	38,000	5,49,500
	9,94,100	**4,06,500**	**5,21,200**	**2,00,000**	**21,21,800**

Collection Policy –

(a) Normal Credit terms are for 30 days

(b) Interest of 2% is charged on accounts overdue for 45 days

(c) Interest of 4% is charged on accounts overdue for more than 75 days

(d) Cash Discount of 2% is given to customers who make payment within 10 days of invoice getting due.

Additional Information –

(a) 40% of the invoice value after bad debt falling in the ageing criteria of 31-60 days' pay after 45th day but pay within the 60th day with 1.5% of the total being uncollectible

(b) 25% of the invoice value after bad debt falling in the ageing criteria of 61-90 days' pay after 75th day but pay within the 90th day with 3% of the total being uncollectible.

(c) 15% of the total invoice value overdue for 91 days or more are uncollectible.

(d) 50% of the customers (invoice value) avail the cash discount.

(e) Administration cost for managing the above customers would also be involved amounting to ₹ 50,000.

(i) CALCULATE the effective cost involved in the collection process assuming that the operating cost of sales ratio is 0.75.

(ii) EXPLAIN three aspects of management of receivables. **(10 Marks)**

4. (a) "The profit maximization is not an operationally feasible criterion." COMMENT on it. **(4 Marks)**

(b) EXPLAIN any four types of Preference Shares along with its Salient Features.

(4 Marks)

(c) A company is analyzing its risk profile using combined leverage. It observes that its Degree of Operating Leverage (DOL) is low while its Degree of Financial Leverage (DFL) is high. The management believes this combination helps balance overall risk. Based on the concept of combined leverage, EXPLAIN whether this is a suitable risk combination and JUSTIFY your answer briefly. **(2 Marks)**

OR

(c) Pecking order theory suggests that managers may use various sources for raising of fund in an order. EXPLAIN the preferred order of financing sources suggested by this theory. **(2 Marks)**

PAPER 6B: STRATEGIC MANAGEMENT

1. *The question paper comprises two parts, Part I and Part II.*
2. *Part I comprises case scenario based multiple choice questions (MCQs)*
3. *Part II comprises questions which require descriptive answers.*

PART I – Case scenario based MCQs (15 Marks)

1. (A) (Compulsory)

1. (A) PlaySphere Interactive was founded in Bangalore in 2010 as a small startup developing mobile puzzle games for local users. For several years, its growth remained modest, as the Indian gaming industry was still in its infancy.

In 2015, the new CEO redefined the company's vision as "To be India's leading creator of immersive gaming experiences," and its mission as "To design culturally relevant games with global quality." This gave PlaySphere both long-term direction and concrete operational purpose.

The company's breakthrough came when it launched a fantasy role-playing game, MythQuest, based on Indian mythology. Within a year, it reached millions of downloads. Success was partly due to its core competitive advantage an in-house game engine optimized for low-bandwidth conditions, which allowed seamless multiplayer play. This helped PlaySphere survive intense industry rivalry and the threat of substitutes from foreign gaming platforms, both of which are key forces in Porter's Five Forces model.

As player volumes increased, PlaySphere benefited from the experience curve costs per unit declined as developers became more efficient and processes standardized. This improved profitability despite rising competition.

To manage its expanding portfolio, the company restructured into two Strategic Business Units (SBUs): Mobile Games (casual and puzzle titles) and Immersive Games (RPGs and multiplayer). Each SBU was given autonomy for faster decision-making, while the corporate office focused on resource allocation.

Leadership also played a role. The CEO adopted a participative leadership style, involving development teams in key creative and technical decisions, which boosted morale and innovation.

In 2020, sudden regulations on in-app purchases threatened revenues. PlaySphere responded using special alert control, adjusting its monetization models quickly to stay compliant. At the same time, it relied on premise control to monitor assumptions about growth in internet penetration and youth demographics, ensuring its strategies remained valid.

Today, PlaySphere stands as one of Bangalore's fastest-growing gaming companies, with revenues crossing ₹ 4,000 crore, symbolizing how strategic clarity and adaptive execution can turn a startup into a national leader.

Based on the above Case Scenario, answer the Multiple-Choice Questions.

(i) PlaySphere's declaration "To be India's leading creator of immersive gaming experiences" is best classified as which element of strategic intent, and why?

(a) Mission – because it defines operational purpose

(b) Objective – because it is short-term and measurable

(c) Vision – because it describes long-term aspirations

(d) Corporate Strategy – because it defines resource allocation

(2 Marks)

(ii) The success of MythQuest despite foreign competitors highlights which forces from Porter's Five Forces model that PlaySphere managed to withstand?

(a) Bargaining Power of Suppliers and Threat of New Entrants

(b) Industry Rivalry and Threat of Substitutes

(c) Bargaining Power of Buyers and Threat of New Entrants

(d) Industry Rivalry and Bargaining Power of Suppliers **(2 Marks)**

(iii) As PlaySphere scaled up, development costs per unit declined due to learning efficiencies and process standardization. Which strategic management concept explains this phenomenon?

(a) Economies of Scale

(b) Value Chain Analysis

(c) Experience Curve

(d) Cost Leadership **(2 Marks)**

(iv) The restructuring of PlaySphere into two SBUs (Mobile Games and Immersive Games) represents which level of strategy, and how does it help execution?

(a) Functional-level – focuses on departmental activities

(b) Corporate-level – manages a portfolio of businesses

(c) Business-level – defines competitive positioning in one industry

(d) Operational-level – deals with day-to-day activities **(2 Marks)**

(v) When regulations on in-app purchases suddenly changed, PlaySphere applied which type of strategic control and why?

(a) Premise Control – checking underlying assumptions

(b) Implementation Control – tracking key projects

(c) Special Alert Control – responding to sudden events

(d) Strategic Surveillance – scanning broad signals **(2 Marks)**

(B) Compulsory Application Based Independent MCQs

(i) Bright Screens' LED TV division has high market share in a fast-growing electronics segment. It invests heavily in advertising and R&D to stay ahead of competitors. How should this division be classified in the BCG Matrix?

(a) Dog

(b) Star

(c) Cash Cow

(d) Question Mark **(2 Marks)**

(ii) A company has strong R&D capability, but competitors can easily replicate its products. However, its organisational culture enables continuous innovation which competitors cannot imitate. What is MOST likely the firm's core competency?

(a) R&D capability

(b) Product design

(c) Organisational culture enabling innovation

(d) Manufacturing efficiency **(2 Marks)**

(iii) What is the critical final step in Kurt Lewin's three-step model for institutionalizing organizational change?

(a) Unfreeze (Creating the motivation to change)

(b) Change (Implementing the new processes)

(c) Refreeze (Stabilizing the change by institutionalizing new norms)

(d) Innovate (Creating a brand-new process) **(1 Mark)**

PART II – Descriptive Questions (35 Marks)

*Question No. **1** is compulsory.*

*Attempt any **two** questions out of the remaining **three** questions.*

1. (a) A strategic analyst wants to study the competitive positioning of companies in the smartphone industry based on price range and product features. Explain how the analyst can use Strategic Group Mapping to analyse the industry. Also, state the insights that can be derived from such a map. **(5 Marks)**

(b) A Mumbai-based conglomerate, PQR Ltd., has announced a major restructuring of its business operations. The company has decided to split its business into four separate units: Manufacturing, Retail, Services, and Technology. Each unit will operate as a separate business, with delegated responsibility for day-to-day operations and strategy to the respective unit managers. Identify the organization structure that PQR Ltd. has planned to implement. Discuss any four attributes and the benefits the firm may derive by using this organization structure. **(5 Marks)**

(c) GreenHarvest Foods, a well-established organic food company in the domestic market, is planning to expand globally. As part of its international strategy, the company is introducing region-specific organic products by adapting ingredients, flavours and packaging to suit local consumer preferences in different countries. Through this approach, GreenHarvest Foods aims to cater to diverse markets and strengthen its global footprint. Which expansion strategy from Ansoff's Product-Market Growth Matrix best aligns with GreenHarvest Foods' approach?

(5 Marks)

2. (a) "A well-defined vision and mission statement provide direction and purpose to an organization." Explain the significance of vision and mission statements in strategic planning. **(5 Marks)**

(b) "A close and continuous interaction between a business and its environment helps in strengthening the business firm and using its resources more effectively." Explain Business environment and discuss how does the interaction between a business and its environment helps the business firm. **(5 Marks)**

3. (a) Write a short note on the Key Strategic Drivers of an organization. **(5 Marks)**

(b) "International development is expensive and challenging". In the context of the statement, explain the internationalization of business and the steps involved in such strategic planning. **(5 Marks)**

4. (a) Explain the 'product market growth matrix' as propagated by Igor Ansoff as a device for identifying growth opportunities for the future. **(5 Marks)**

(b) Why Strategic Performance Measures are essential for organizations?

OR

Why is change management crucial during digital transformation, and what are some key strategies for navigating change effectively? **(5 Marks)**

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PAPER – 6: FINANCIAL MANAGEMENT & STRATEGIC MANAGEMENT

PAPER 6A : FINANCIAL MANAGEMENT

Suggested Answers/ Hints

DIVISION A

Case Scenario 1

1. (c) **Ke = 12%,**

2. (d) **Kd = 6%**

Working Note:

Let the cost of equity be 'X' and cost of debt be 'Y'

WACC under BV

Item	Cost	Weight	Product
Equity	X	20 Lakhs /30 Lakhs = 2/3	$\frac{2X}{3}$
Debt	Y	10 Lakhs /30 Lakhs = 1/3	$\frac{Y}{3}$
		1	**10%**

$10 = \frac{2X}{3} + \frac{Y}{3}$

$30 = 2X + Y$ ....(1)

WACC under MV

Item	Cost	Weight	Product
Equity	X	60 Lakhs /80 Lakhs = 3/4	$\frac{3X}{4}$
Debt	Y	20 Lakhs /80 Lakhs = 1/4	$\frac{Y}{4}$
		1	**10.5%**

10.5 $= \frac{3X}{4} + \frac{Y}{4}$

42 = 3X + Y ….(2)

By Solving both equations

42 = 3X + Y

30 = 2X + Y

Cost of equity (X) = 12%

Substituting in Equation 1,

30 = 24 + Y

Cost of Debt (Y) = 6%

3. (c) ₹ 1.14 lakhs

Statement Showing Calculation of Cash Inflows

Particulars	Year 1	Year 2	Year 3
Cash Inflows (before dep & tax)	8.00	9.00	10.00
Less: Depreciation	6.00	6.00	6.00
Profit Before Tax (PBT)	2.00	3.00	4.00
Less: Tax @ 25%	0.50	0.75	1.00
Profit After Tax (PAT)	1.50	2.25	3.00
Add: Depreciation	6.00	6.00	6.00
Operating Cash Flow	**7.50**	**8.25**	**9.00**
Add: Salvage Value	–	–	2.00
Add: Working Capital Recovery	–	–	3.00
Total Cash Inflow	**7.50**	**8.25**	**14.00**

Investment rate = (6% / 0.75) + 2% = 10%

Statement showing calculation of PV

Year	CF	PV Factor @ 10%	PV (₹ in lakhs)
0	23	1	23
1	7.50	0.909	6.82
2	8.25	0.826	6.81
3	14.00	0.751	10.51
NPV			**1.14**

4. (a) 1.05

$$\text{Profitability Index (PI)} = \frac{\text{Sum of discounted cash in flows}}{\text{Initial cash outlay or Total discounted cash outflow (as the case may)}}$$

= 24.14 / 23

= 1.05 (approx)

5. (d) 2.89 years

Year	Discounted cash inflows	Cumulative Discounted cash inflows
1	6.82	6.82
2	6.81	13.63
3	10.51	24.14

$$\text{Discounted Payback Period} = 2 \text{ years} + \left(\frac{23 - 13.63}{10.51}\right) = 2.89 \text{ years}$$

6. (b) 1.25

$$\text{Capital gearing ratio} = \frac{\text{(Pref share capital + Debentures + Other borrowed funds)}}{\text{Equity Share Capital + Reserves and Surplus - Losses}}$$

$$= \frac{₹\ 25 \text{ lakhs} + ₹\ 50 \text{ lakhs} + ₹\ 15 \text{ lakhs}}{₹\ 48 \text{ lakhs} + ₹\ 24 \text{ lakhs}}$$

= ₹ 90 lakhs / ₹ 72 lakhs = 1.25

7. (a) ₹ 1,200

As per Walter's Model, Price per share is computed using the formula:

$$\text{Price (P)} = \frac{D + \frac{r}{Ke}(E-D)}{K_e}$$

Where,

E = Earnings per share.

D = Dividend per share.

K_e = Cost of equity/ rate of capitalization/ discount rate.

r = Internal rate of return/ return on investment

$$\text{Price} \quad P = \frac{45 + \frac{0.20}{0.17}(180-45)}{0.17}$$

Or, $P = \frac{45 + 158.82}{0.17}$ = ₹ 1,200 (approx.)

8. (c) **ROI is greater than interest on loan funds and hence it has favourable financial leverage.**

EBIT = 75,00,000 - 42,00,000 - 6,00,000 = 27,00,000,

ROI = 27,00,000/(45,00,000 + 55,00,000) = 27%,

Rate of Interest lower than Return on investment.

Therefore, there is favourable leverage.

Division B: Descriptive Question

1. (a) (i) **Operating Expenses**

Net Profit = 8% on Sales = 8% x ₹ 3,60,00,000	₹ 28,80,000
Add: Income Tax = 40% x ₹ 28,80,000/60%	₹ 19,20,000
Profit Before tax	₹ 48,00,000
Add: Debenture Interest	₹ 3,36,000
Profit before interest and tax	₹ 51,36,000
Sales	₹ 3,60,00,000
Less:	
Cost of goods sold ₹ 1,44,00,000	
Profit before interest & tax ₹ 51,36,000	₹ 1,95,36,000
Operating Expenses	₹ 1,64,64,000

(ii) **Share Capital and Reserves**

Return on Net worth is 30%, hence profit after tax of ₹28,80,000 is equivalent to 30% of Net Worth.

Net worth x 30/100	= ₹ 28,80,000
Net Worth	= 28,80,000 x 100/30
	= ₹ 96,00,000
Ratio of Share Capital to Reserves	= 6:4
Share Capital	= ₹ 96,00,000 x 6/10 = ₹ 57,60,000
Reserves	= ₹ 96,00,000 x 4/10 = ₹ 38,40,000

(iii) Closing Stock

Inventory Turnover (based on cost of goods sold) = 12

Cost of goods sold = ₹ 1,44,00,000

Inventory Turnover Ratio = Cost of goods sold / Closing Stock = 12

12 = ₹ 1,44,00,000/Closing Stock

Therefore, Closing Stock = ₹ 1,44,00,000/12

= ₹ 12,00,000

(iv) Fixed Assets

Calculation of Total liabilities

Interest on 14 % Debentures = ₹ 3,36,000

Therefore debentures $= \frac{₹\ 3,36,000 \times 100}{14\%}$

= ₹ 24,00,000

Total of Liabilities Side

Share Capital	₹ 57,60,000
Reserves	₹ 38,40,000
Debentures	₹ 24,00,000
Sundry Creditors	₹ 16,00,000
Total Liabilities	₹ 1,36,00,000

Current Ratio = 2:1

Sundry Creditors = ₹ 16,00,000

Current Assets / Current Liabilities = 2

Current Assets / Sundry Creditors = 2

Current Assets /₹16,00,000 = 2

Current Assets = 2 x ₹ 16,00,000

= ₹ 32,00,000

Fixed Assets = Total Liabilities – Current Assets

= ₹ 1,36,00,000 - ₹ 32,00,000

= ₹ 1,04,00,000

(b) **(i)** According to CAPM

Rs = Rf + Beta x RP

15.20 = Rf + 1.2Rp …..(1)

12.80 = Rf + 0.8Rp …..(2)

By solving, 0.4Rp = 2.4.

So Risk Premium = 6%

Substituting in Eqn. 1

15.20 = Rf + 1.2*6%

Rf = 15.20 – 7.20 = 8%

Hence, Risk Free Return = 8%

Rp = Rm – Rf

6 = Rm – 8%

Rm = 14%

Rs (C Ltd.) = 8% + 1.1 x 6% = 14.6%

Security	Beta	CAPM Return
A Ltd	1.2	15.20%
B Ltd	0.8	12.80%
C Ltd	1.1	14.60%
Cash in hand	0	Nil
Treasury Bill	0	8.00%
Stock Market (Nifty)	1	14.00%

(ii) Risk-averse investors may prefer securities with low Beta (<1) i.e. B Ltd. Aggressive investors may choose high Beta (>1) securities for higher potential returns i.e. A or C Ltd.

(c) **Option I : Purchase Machinery and Service Part at the end of Year 1.**

Net Present value of cash flow @ 10% per annum discount rate.

$$NPV = -50{,}000 + \frac{18{,}000}{(1.1)} + \frac{18{,}000}{(1.1)^2} + \frac{18{,}000}{(1.1)^3} - \frac{10{,}000}{(1.1)} + \frac{12{,}500}{(1.1)^3}$$

$= -\ 50{,}000 + 18{,}000\ (0.9091 + 0.8264 + 0.7513) - (10{,}000 \times 0.9091) + (12{,}500 \times 0.7513)$

$= -\ 50{,}000 + (18{,}000 \times 2.4868) - 9{,}091 + 9{,}391$

$= -\ 50{,}000 + 44{,}762 - 9{,}091 + 9{,}391$

NPV $= -\ 4{,}938$

Since, Net Present Value is negative; therefore, this option is not to be considered.

If Supplier gives a discount of ₹ 5,000 then,

NPV = +5,000 – 4,938 = + 62

In this case, Net Present Value is positive but very small; therefore, this option may not be advisable.

Option II : Purchase Machinery and Replace Part at the end of Year 2.

$$\text{NPV} = -50{,}000 + \frac{18{,}000}{(1.1)} + \frac{18{,}000}{(1.1)^2} + \frac{18{,}000}{(1.1)^3} - \frac{15{,}400}{(1.1)^2} + \frac{27{,}000}{(1.1)^4}$$

$= -\ 50{,}000 + 18{,}000\ (0.9091 + 0.8264 + 0.7513) - (15{,}400 \times 0.8264) + (27{,}000 \times 0.6830)$

$= -\ 50{,}000 + 18{,}000\ (2.4868) - (15{,}400 \times 0.8264) + (27{,}000 \times 0.6830)$

$= -\ 50{,}000 + 44{,}762 - (15{,}400 \times 0.8264) + (27{,}000 \times 0.6830)$

$= -\ 50{,}000 + 44{,}762 - 12{,}727 + 18{,}441$

$= -\ 62{,}727 + 63{,}203 = +476$

Net Present Value is positive, but very low as compared to the investment.

If the Supplier gives a discount of ₹ 5,000, then

NPV = 5,000 + 476 = 5,476

Decision: Option II is worth investing as the net present value is positive and higher as compared to Option I.

2. (a) Market Value of Equity = ₹ 25,00,000

K_e = 21%

$$\frac{\text{Net income (NI) for equity - holders}}{K_e} = \text{Market Value of Equity}$$

$$\frac{\text{Net income (NI) for equity holders}}{0.21} = 25,00,000$$

Net income for equity holders = 5,25,000

EBIT= 5,25,000/0.7 = 7,50,000

	All Equity	Debt and Equity
EBIT	7,50,000	7,50,000
Interest to debt-holders	-	75,000
EBT	7,50,000	6,75,000
Taxes (30%)	2,25,000	2,02,500
Income available to equity shareholders	5,25,000	4,72,500
Income to debt holders plus income available to shareholders	5,25,000	5,47,500

Present value of tax-shield benefits = ₹ 5,00,000 × 0.30 = ₹ 1,50,000

(i) Value of Restructured firm

= ₹ 25,00,000 + ₹ 1,50,000 = ₹ 26,50,000

(ii) Cost of Equity (K_e)

Total Value = ₹ 26,50,000

Less: Value of Debt = ₹ 5,00,000

Value of Equity = ₹ 21,50,000

$$K_e = \frac{4,72,500}{21,50,000} = 0.219 = 21.98\%$$

(iii) WACC (on market value weight)

Cost of Debt (after tax) = 15% (1- 0.3) = 0.15 (0.70) = 0.105 = 10.5%

Components of Costs	Amount	Cost of Capital (%)	Weight	WACC (%)
Equity	21,50,000	21.98	0.81	17.80
Debt	5,00,000	10.50	0.19	2.00
	26,50,000			19.80

Comment: At present the company is all equity financed. So, $K_e = K_o$ i.e. 21%. However, after restructuring, the K_o would be reduced to 19.80% and K_e would increase from 21% to 21.98%.

(b) (i) ROI = EBIT/Investment

EBIT = Sales - VC – FC

= ₹ 1,50,00,000 – 84,00,000 – 12,00,000

= ₹ 54,00,000

ROI = ₹ 54,00,000/₹ 2,00,00,000 = 27%

(ii) Operating Leverage $= \dfrac{\text{Contribution}}{\text{EBIT}} = \dfrac{₹\,66,00,000}{₹\,54,00,000} = 1.222 \text{ times}$

Financial Leverage $= \dfrac{\text{EBIT}}{\text{EBT}} = \dfrac{₹54,00,000}{₹45,00,000} = 1.2 \text{ times}$

(iii) Combined Leverage = OL × FL = 1.222 × 1.2 = 1.466 times.

(iv) Operating Leverage = 1.222

$$1.222 = \frac{\Delta\,\text{EBIT}}{1/3}$$

$$\Delta\,\text{EBIT} = 0.4074$$

New EBIT = ₹ 54,00,000 – 40.74% of 54,00,000

= ₹ 32,00,000

3. (i) (a) Total cost involved in the collection would include bad debts, cash discount & administration cost i.e. Cost of Carrying debtors

WN – 1 Calculation of Bad debts:

= 4,06,500 x 1.5% + 5,21,200 x 3% + 2,00,000 x 15%

= 6,098 + 15,636 + 30,000

= ₹ 51,734

WN – 2 Calculation of Cash Discount:

= (9,94,100 x 50%) x 2% = ₹ 9,941

WN – 3 Calculation of Interest Income charged on account of delayed payment:

	Amount
Total Invoice value for 31 – 60 days	4,06,500
Less: Bad debts @ 1.5%	(6,098)
	4,00,402

40% of above (payment after 45th day but within 60th day)	1,60,161
Interest @ 2% (160161 x 2%)	**3,203**

	Amount
Total Invoice value for 61 – 90 days	5,21,200
Less: Bad debts @ 3%	(15,636)
	5,05,564
25% of above (payment after 75th day but within 90th day)	1,26,391
Interest @ 4% (126391 x 4%)	**5,056**

∴ Total Interest Income = 3,203 + 5,056 = ₹ 8,259

Operating Cost of Sales = 21,21,800 x 0.75 = ₹ 15,91,350

Effective Cost of Debtors Policy

$$= \frac{\text{Bad debts + Cash discount + Administration Cost - Interest Charged Received}}{\text{Operating Cost of Sales}}$$

$$= \frac{51{,}734 + 9{,}941 + 50{,}000 - 8{,}259}{15{,}91{,}350}$$

∴ Effective Cost of Debtors Policy = 6.50%

Notes -

i. In absence of information on Opportunity Rate of return on Investment, Opportunity Cost of Investment in receivables is not calculated.

(ii) There are basically three aspects of management of receivables:

1. ***Credit Policy:*** A balanced credit policy should be determined for effective management of receivables. Decision of Credit standards, Credit terms and collection efforts is included in Credit policy. It involves a trade-off between the profits on additional sales that arise due to credit being extended on the one hand and the cost of carrying those debtors and bad debt losses on the other. This seeks to decide credit period, cash discount and other relevant matters.

2. ***Credit Analysis:*** This requires the finance manager to determine as to how risky it is to advance credit to a particular party. This involves due diligence or reputation check of the customers with respect to their credit worthiness.

3. ***Control of Receivable:*** This requires finance manager to follow up debtors and decide about a suitable credit collection policy. It involves both laying down of credit policies and execution of such policies.

4. **(a)** "The profit maximisation is not an operationally feasible criterion." This statement is true because Profit maximisation can be a short-term objective for any organisation and cannot be its sole objective. Profit maximization fails to serve as an operational criterion for maximizing the owner's economic welfare. It fails to provide an operationally feasible measure for ranking alternative courses of action in terms of their economic efficiency. It suffers from the following limitations:

(i) Vague term: The definition of the term profit is ambiguous. Does it mean short term or long term profit? Does it refer to profit before or after tax? Total profit or profit per share?

(ii) Timing of Return: The profit maximization objective does not make distinction between returns received in different time periods. It gives no consideration to the time value of money, and values benefits received today and benefits received after a period as the same.

(iii) It ignores the risk factor.

(iv) The term maximization is also vague.

(b) Various types of Preference shares can be as below:

Sl. No.	Type of Preference Shares	Salient Features
1	Cumulative	Arrear Dividend will accumulate.
2	Non-cumulative	No right to arrear dividend.
3	Redeemable	Redemption should be done.
4	Participating	Can participate in the surplus which remains after payment to equity shareholders.
5	Non-Participating	Cannot participate in the surplus after payment of fixed rate of Dividend.
6	Convertible	Option of converting into equity Shares.

(c) A combination of low DOL and high DFL is considered the best balanced combination of risk.

- Low DOL indicates lower operating (business) risk and higher EBIT
- High DFL indicates higher financial risk due to the use of debt.

This combination is suitable because the Higher financial risk is balanced by lower total business risk, resulting in a moderate and well-balanced total risk.

OR

(c) 1. Managers first choice is to use internal finance.

2. In absence of internal finance, they can use secured debt, unsecured debt, hybrid debt etc.

3. Managers may issue new equity shares as a last option.

PAPER 6B: STRATEGIC MANAGEMENT

ANSWERS

PART I

1. (A)	**(i)**	**(c)**	**(ii)**	**(b)**	**(iii)**	**(c)**	**(iv)**	**(b)**	**(v)**	**(c)**
(B)	**(i)**	**(b)**	**(ii)**	**(c)**	**(iii)**	**(c)**				

PART II PART II – Descriptive Questions

1. **(a)** The strategic analyst can use **Strategic Group Mapping** to analyse the competitive positioning of smartphone companies based on **price range** and **product features** as follows:

Steps to use Strategic Group Mapping:

1. **Identify key variables:** Select relevant competitive dimensions such as **price (low to high)** and **product features (basic to advanced)**.
2. **Plot companies on a graph:** Position each smartphone company on a two-dimensional map using these variables.
3. **Form strategic groups:** Companies with similar strategies (e.g., high price–high features or low price–basic features) will cluster together forming strategic groups.
4. **Represent market share:** The size of each group (circle) may indicate the **market share** of firms within that group.

Insights derived from the map:

- Helps in understanding the **competitive positioning** of firms in the industry.
- Identifies **direct competitors** within the same strategic group.
- Reveals **market gaps or opportunities** (e.g., underserved segments).
- Highlights **mobility barriers** between groups (e.g., difficulty in moving from low-end to premium segment).
- Assists in analysing the **intensity of competition** within and across groups.

Thus, Strategic Group Mapping provides a visual and analytical tool for better strategic decision-making in the smartphone industry.

(b) PQR Ltd. has planned to implement the Strategic Business Unit (SBU) structure. Very large organisations, particularly those running into several products, or operating at distant geographical locations that are extremely diverse in terms of environmental factors, can be better managed by creating strategic business units. SBU structure becomes imperative in an organisation with an increase in number, size and diversity.

The attributes of an SBU and the benefits a firm may derive by using the SBU Structure are as follows:

- ♦ A scientific method of grouping the businesses of a multi – business corporation which helps the firm in strategic planning.
- ♦ An improvement over the territorial grouping of businesses and strategic planning based on territorial units.
- ♦ Strategic planning for SBU is distinct from rest of businesses. Products/ businesses within an SBU receive same strategic planning treatment and priorities.
- ♦ Each SBU will have its own distinct set of competitors and its own distinct strategy.
- ♦ The CEO of SBU will be responsible for strategic planning for SBU and its profit performance.
- ♦ Products/businesses that are related from the standpoint of function are assembled together as a distinct SBU.
- ♦ Unrelated products/ businesses in any group are separated into separate SBUs.
- ♦ Grouping the businesses on SBU lines helps in strategic planning by removing the vagueness and confusion.
- ♦ Each SBU is a separate business and will be distinct from one another on the basis of mission, objectives etc.

(c) The strategy adopted by **GreenHarvest Foods** is **Diversification**. Diversification refers to a growth strategy where a company introduces **new products in new markets**. In the given case, GreenHarvest Foods is entering **international markets (new markets)** and simultaneously offering **region-specific organic products (new products)** tailored to local tastes and preferences.

This indicates that the company is not only expanding geographically but also modifying and innovating its product offerings to suit different customer segments across countries.

Diversification is considered the **most risky strategy** in Ansoff's Product-Market Growth Matrix as it involves operating in unfamiliar markets and dealing with new customer preferences, regulatory environments, and competitive dynamics. However, it also offers **high growth potential** by creating new revenue streams and reducing dependence on existing markets. Thus, GreenHarvest Foods' approach clearly reflects a **diversification strategy**.

2. (a) Strategic Management is a dynamic process of formulation, implementation, evaluation and control of strategies to realise the organisation's **strategic intent.** Strategic intent clarifies *what the organisation wants to do* and *why it wants to do it*, which forms the basis of **vision and mission statements.**

A **vision statement** describes the organisation's future aspirations and desired position while a **mission statement** explains its present business scope, purpose, goals and the means to achieve them. Together, they provide **direction and purpose** in strategic planning.

Significance of Vision in Strategic Planning:

- Provides a blueprint of where the organisation wants to be.
- Aligns organisational efforts on a chosen path.
- Creates enthusiasm and mould's identity.
- Clarifies aspirations in products, markets, customers and technology.

Significance of Mission in Strategic Planning:

- Explains the reason for the firm's existence.
- Ensures unanimity of purpose and efficient resource use.
- Standard for allocation and goal translation.
- Gives distinct identity and direction.
- Reflects present activities and ensures legitimacy.

Thus, a well-defined vision and mission provide clarity of purpose, direction for growth and a framework for decision-making. Vision answers, *"where we want to go,"* and mission answers *"what business we are in and why we exist."* Together, they form the philosophical base of strategy and guide the organisation toward long-term success.

(b) The term **business environment** refers to all **external factors, influences, or situations that** in some way **affect business decisions, plans, and operations.** It is highly dynamic and continuously evolving. Organizational success depends not only on its internal abilities but also on its relationship with the external environment.

Interaction between Business and Environment: A close and continuous interaction strengthens the business firm and enables effective utilization of resources in the following ways:

i. **Determine opportunities and threats:** The interaction between the business and its environment would explain opportunities and threats to the business. It helps to find new needs and wants of the consumers, changes in laws, changes in social behaviours and tells what new products the competitors are bringing in the market to attract consumers.

ii. **Give direction for growth:** The interaction with the environment enables the business to identify the areas for growth and expansion of their activities. Once the business is aware and understands the changes happening around, it can plan and strategies to have successful business.

iii. **Continuous Learning:** The managers are motivated to continuously update their knowledge, understanding and skills to meet the predicted changes in the realm of business.

iv. **Image Building:** Environmental understanding helps the business organizations to improve their image by showing their sensitivity to the environment in which they operate.

v. **Meeting Competition:** It helps the businesses to analyse the competitors' strategies and formulate their own strategies accordingly. The idea is to flourish and beat competition for its products and services.

3. (a) Key Strategic Drivers of an Organization

Strategic drivers are essential elements that influence an organization's ability to differentiate itself from its competitors and achieve competitive advantage. These drivers assess the current performance of the business and provide insights into areas that need focus. The key strategic drivers include:

1. **Industry and Markets:** Understanding the industry and markets is crucial for identifying the organization's relative position. Industries group similar companies based on their primary products, while markets are defined by the buyers and sellers of these products. Analyzing industry and market

dynamics, often through tools like strategic group mapping, helps organizations evaluate competition and refine strategies.

2. **Customers:** Identifying and understanding customers is a critical driver. Customers are segmented based on their needs and spending capacity, which guides product development and marketing strategies. Differentiating between customers (buyers) and consumers (users) is vital to tailoring pricing, design, and usability strategies effectively.

3. **Products and Services:** Products and services are central to defining the business. Organizations must assess their offerings, classify products, and devise strategies for differentiation, branding, and pricing. Product innovation and marketing are key to maintaining competitiveness.

4. **Channels:** The channels through which products and services are delivered impact on accessibility and customer satisfaction. Strategies related to direct, digital, or relationship-based marketing ensure the efficient distribution of offerings to target customers.

By aligning these drivers with organizational goals, businesses can achieve sustained growth and maintain a competitive edge.

(b) Internationalization has become a pivotal trend for businesses aiming to enhance profitability and access cheaper resources. **It allows companies to explore new markets, achieve economies of scale, and prolong product lifecycles.** However, the process of internationalization is complex due to additional variables and linkages that differ from domestic operations.

To navigate this complexity, businesses should adopt a structured approach to international strategic planning. The steps involved include:

1. **Evaluate Global Opportunities and Threats:** Businesses must assess potential global markets, identifying opportunities and threats while aligning them with their internal capabilities.

2. **Describe the Scope of Operations:** Clearly defining the extent of the firm's international commercial activities is crucial for focused strategy development.

3. **Create Global Business Objectives:** Establishing clear objectives helps guide the organization's international efforts and aligns with its overall mission.

4. **Develop Distinct Corporate Strategies:** Formulating specific strategies tailored for global operations ensures that the organization can effectively compete in diverse markets.

These steps facilitate the identification of market opportunities and the formulation of effective global strategies, enabling businesses to thrive in the international arena despite the inherent challenges and costs associated with such expansion.

4. **(a)** The Ansoff's Product Market Growth Matrix, developed by Igor Ansoff, is a strategic tool that helps businesses identify growth opportunities by analyzing the interplay between products and markets.

It offers four distinct strategies based on whether the products and markets are existing or new. These strategies are:

1. **Market Penetration**: Focuses on selling existing products in existing markets. This involves increasing market share by enhancing sales through advertising, promotions, competitive pricing, or encouraging higher usage among current customers.
2. **Market Development**: Entails selling existing products in new markets. This could involve exploring new geographical regions, utilizing alternative distribution channels, or creating new market segments.
3. **Product Development**: Involves introducing new or modified products into existing markets. This strategy often requires innovation and developing products that meet current market needs.
4. **Diversification**: Refers to marketing new products in new markets. It is a high-risk strategy as the business ventures into unfamiliar products and markets.

As market dynamics evolve, companies may transition between these strategies to adapt and sustain growth. The matrix provides a structured framework for businesses to align their growth strategies with their capabilities and market conditions.

(b) Strategic performance measures are essential for organizations for several reasons:

- ♦ **Goal Alignment:** Strategic performance measures help organizations align their strategies with their goals and objectives, ensuring that they are on track to achieve their desired outcomes.
- ♦ **Resource Allocation:** Strategic performance measures provide organizations with the information they need to make informed decisions about resource allocation, enabling them to prioritize their efforts and allocate resources to the areas that will have the greatest impact on their performance.

- ♦ **Continuous Improvement:** Strategic performance measures provide organizations with a framework for continuous improvement, enabling them to track their progress and make adjustments to improve their performance over time.
- ♦ **External Accountability:** Strategic performance measures help organizations demonstrate accountability to stakeholders, including shareholders, customers, and regulatory bodies, by providing a clear and transparent picture of their performance.

OR

Change management is essential during digital transformation to ensure the success of the process. Here are some key strategies to navigate change effectively:

- **Specify the digital transformation's aims and objectives:** Clearly defining the intended outcomes and objectives helps ensure everyone is aligned and working towards the same goals.
- **Always communicate:** Regular and transparent communication is crucial to help people understand the goals of digital transformation and how it will impact various stakeholders, including employees, clients, and other parties.
- **Be ready for resistance:** Change, even if beneficial, can be met with resistance. Having a strategy in place to address resistance is important for overcoming challenges and ensuring a smooth transition.
- **Implement changes gradually:** Instead of making all changes at once, gradual implementation allows individuals to adapt to new ways of doing things without feeling overwhelmed by too much change simultaneously.
- **Offer assistance and training:** Providing support, guidance, and training for employees is crucial as they navigate new procedures, software applications, and other aspects of digital transformation.

In conclusion, meticulous planning and effective change management are vital for the successful completion of digital transformation projects. Without proper change management, these efforts are more likely to fail, and organizations can enhance the integration of new digital systems by anticipating and managing the necessary changes.