



TECHNICAL UNIVERSITY OF MOMBASA
School of Business

DEPARTMENT OF BUSINESS ADMINISTRATION

DIPLOMA IN ACCOUNTANCY

BAC 2212: FINANCIAL MANAGEMENT

SPECIAL/SUPPLEMENTARY EXAMINATIONS

SERIES: JUNE/JULY 2015

TIME: 2 HOURS

INSTRUCTIONS:

- This paper consists of **FIVE** questions.
- Answer question **ONE (Compulsory)** and any other **TWO** questions.
- Do not write on the question paper

This paper consists of Three printed pages.

QUESTION 1 (Compulsory)

Payback is an investment appraisal technique. It is used to determine the economic viability of investment proposal.

Required:

- a) i) Explain what is meant by “payback”? (2 marks)
ii) What are the advantages and disadvantages of payback. (8 marks)
- b) Distinguish by giving your own numerical illustration between compounding and discounting. Show formula used. (6 marks)
- c) Why do commercial banks prefer to lend short term rather than long term? (10 marks)
- d) What is meant by a cash operating cycle? (4 marks)

QUESTION 2

- a) What are the advantages of leasing an asset? (10 marks)
- b) What are the limitations of credit cards as a source of finance? (10 marks)

QUESTION 3

The following information was extracted from the books of Tatua Ltd as at 31st December 2014.

	£
Ordinary share capital (par value £20)	1,600,000
8% preference share capital (par value £30)	1,200,000
10% preference share capital (par value £20)	800,000
10% debentures	<u>800,000</u>

Additional information at 31st December 2014

	Market price (£)
Ordinary shares	£30 per share
8% preference shares	£24 per share
10% preference shares	£25 per share

- The market value of 10% debentures was £ 1,000,000
- The corporation tax rate is 30%
- Ordinary shares have a dividend of £6 per share with a growth rate of 10%

Required

- a) Cost of ordinary share capital (2 marks)
- b) Cost of 8% preference share capital. (2 marks)
- c) Cost of 10% preference share capital. (2 marks)
- d) Cost of 10% debentures (2 marks)
- e) Weighted average cost of capital (10 marks)
- f) What is marginal cost of capital? (2 marks)

QUESTION 4

The following information relates to Twende Ltd for the year ended 31st December 2014

- EBIT ([Earnings before interest & tax] £10,000
- Interest on loan £2000
- Preference dividend £3200
- Corporation tax rate = 40%
- No. of common ordinary shares – 1,000

Required:

- a) Compute the Earnings Per Share (EPS) (4 marks)
- b) Re-calculate the Earnings per share assuming a 40% increase in EBIT. (4 marks)
- c) Calculate the degree of financial leverage (8 marks)
- d) Interpret the degree of financial leverage obtained. (4 marks)

QUESTION 5

- a) List **THREE** advantages of a Rights issue to the company. (6 marks)
- b) What role does the Central Bank play in the economy? (14 marks)