

**TECHNICAL UNIVERSITY OF MOMBASA**  
***Faculty of Business and Social Studies***  
**DEPARTMENT OF ACCOUNTING AND FINANCE**

HIGHER DIPLOMA IN HUMAN RESOURCE MANAGEMENT

**BAC 3101: FINANCIAL MANAGEMENT**

END OF SEMESTER EXAMINATIONS

**SERIES: APRIL SERIES**

**TIME: 2 HOURS**

**INSTRUCTIONS TO CANDIDATES:**

- This paper consists of **FIVE** Questions.
- Answer Question **ONE (Compulsory)** and any other **TWO** questions.
- Do **NOT** Write on the question paper.
- You are only allowed to have writing materials, an Answer booklet and a scientific non programmable calculator in the examination room.
- Mobile phones are not allowed in the examination room.
- Cheating leads to disqualification.
- This paper consists of Four printed pages***

### QUESTION ONE (COMPULSORY)

- a. You are the Chief Executive Officer of Balozzi Ltd, a company that deals with the Import of motor vehicles. The sales of the company have gone down and the company is unable to pay dividends to Shareholders to its Shareholders for three consecutive years. The shareholders are threatening to sell their shares due to no returns.

#### Required

Explain the factors that may be influencing dividend policy at Balozzi Ltd. **(10 marks)**

- b. Define the terms **Risk** and **Return** as may be applicable in business finance. **(5 marks)**

- c. The shares of two companies Panga Ltd and Kisu Ltd have the following probability distributions

State of Economy	Probability	Return on Panga Ltd	Return on Kisu Ltd
Boom	0.3	22%	5%
Steady Growth	0.5	10%	20%
Slump	0.2	2%	2%

#### Required

- i. Compute expected return for each Company **(5 marks)**
- ii. Compute the standard deviation of the returns for each company **(10 marks)**

### QUESTION TWO

- a. Distinguish between money market and capital market giving examples of each **(10 marks)**
- b. An investor wishes to purchase an annuity of Sh. 200,000 for the next three years. If the bank pays interest rate of 6%, how much should be invested today? **(10 marks)**

### QUESTION THREE

- a. In a company, an agency problem may exist between management and shareholders on one hand and the debt holders (creditors and lenders) on the other because management and shareholders, who own and control the company, have the incentive to enter into transactions that may transfer wealth from debt holders to shareholders. Hence the need for agreements by debt holders in lending contracts.

**Required**

Explain how a company can minimize agency problems **(10 marks)**

- b. The capital structure of Makinon Ltd as at 31<sup>st</sup> December 2015 was made up as follows:

1. Ordinary Share Capital Sh. 16,000,000
2. 10% preference shares of Sh.2,000,000
3. 14% Bond Capital Sh. 14,000,000

The market value of the company's ordinary shares is Sh.40 per share. The company paid ordinary share dividends for the year ended 31<sup>st</sup> December 2015 of Sh.4 per share. The average annual growth rate in dividends has been 7% over the past ten years and this growth rate is expected to be maintained in the foreseeable future. Assuming a tax rate of 30%;

**Required:**

Compute the Weighted Average Cost of Capital of Makinon Ltd as at 31<sup>st</sup> March 2015 **(10 marks)**

### QUESTION FOUR

- a. Find the Future Value of Sh. 100,000 compounded at 6% for 3 years:
- i. Annually **(4 marks)**
  - ii. Semi-annually **(4 marks)**
  - iii. Quarterly **(4 marks)**

- b. Ayet Ltd. and Bayet Ltd. are two small size companies operating in Mombasa, Kenya.  
The following information has been provided for the year ended 30<sup>th</sup> April 2013

	<b>Ayet Ltd</b>	<b>Bayet Ltd</b>
	<b>Sh.</b>	<b>Sh.</b>
Ordinary share capital @ 10 par	600,000	1,800,000
10% Preference share capital @ Sh.10 par	<u>600,000</u>	_____ -
	1,200,000	1,800,000
Retained Profits	<u>800,000</u>	<u>1,200,000</u>
	2,000,000	3,000,000
15% Debenture capital	<u>2,000,000</u>	<u>1,000,000</u>
	<b><u>4,000,000</u></b>	<b><u>4,000,000</u></b>

### Required

Calculate the gearing ratio of each company and state in each case whether the gearing is high or low. (Calculate to 3 decimal places). **(8 marks)**

### QUESTION FIVE

- a. Highlight the FIVE steps in capital budgeting **(10 marks)**

- b. Projects W, X, Y and Z have initial capital outlays of Sh. 36,000 each. The cash flows for each project is as indicated below:

Project	Year 1	Year 2	Year 3	Year 4
W	18,000	6,000	12,000	4,000
X	20,000	16,000	0	0
Y	24,000	6,000	12,000	0
Z	16,000	20,000	2,000	2,000

### Required:

- i. Compute the payback period for each project **(8 marks)**
- ii. Assuming the maximum payback period is 2 years, which project should be selected and why? **(2 marks)**