



**TECHNICAL UNIVERSITY OF MOMBASA**  
**Faculty of Business and Social Studies**

DEPARTMENT OF BUSINESS STUDIES

UNIVERSITY EXAMINATIONS FOR DEGREE IN  
BACHELOR OF BUSINESS ADMINISTRATION  
BACHELOR OF COMMERCE

**BFI 4301: FINANCIAL MANAGEMENT**

END OF SEMESTER EXAMINATIONS

**SERIES: APRIL 2015**

**TIME: 2 HOURS**

**INSTRUCTIONS:**

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

*This paper consists of Two printed pages*

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**QUESTION 1 (Compulsory)**

- a) What is the importance of investment decisions? **(5 marks)**
- b) Mamba Ltd wishes to invest in either project A or B each project would require a capital outlay of sh. 100,000. The projects are expected to generate the following cash inflows.

Year	Project A	Project B
	Shs.	Shs.
1	20,000	15,000
2	28,000	40,000
3	30,000	45,000
4	50,000	40,000
5	20,000	16,000

The cost of capital is 10%

**Required:**

- i) Compute the N.P.V for each project
  - ii) Advise the management on the projects to invest in. **(10 marks)**
- c) What are the merits of using IRR as one of the methods of investment appraisal? **(5 marks)**
- d) Financial decisions refers to the decision on the sources of funds to finance investment projects. Briefly identify specific roles of finance manager in respect of financial decisions. **(10 marks)**

**QUESTION 2**

- a) Determine the present value of sh. 1,000,000 expected in 6 years time at a discount rate of 6%. **(5 marks)**
- b) Why should financial assets and securities be valued? **(10 marks)**
- c) The share of Rea Vipingo Ltd are trading at sh. 15.50 at the N.S.E. The company paid a dividend of sh. 1.50 for the year just ended. The dividends are expected to grow at a constant rate of 5% p.a

**Required**

Determine the costs of retained earning for the company. **(5 marks)**

**QUESTION 3**

- a) Distinguish between the following terms:
  - i) Weighted Average Cost of Capital and Marginal Cost of Capital.
  - ii) Bears and Bulls **(5 marks)**
- b) The most recent financial data for Kasneb disclosed the following:  
Dividend per share            sh. 3  
Expected growth rate        6%  
Required rate of return      15%

The company is considering a variety of proposal to redirect the firms activities. The following four activities have been suggested:

- i) Do nothing in which case the key financial variables remain unchanged.
- ii) Invest in a venture that will increase the dividend growth rate to 7% and lower the required rate of return to 14%.
- iii) Eliminate an unproductive productline. This action will increase the dividend growth rate to 8% and raise the required rate of return to 17%.

- iv) Acquire a subsidiary operation from another firm. This action will increase the dividend growth rate to 9% and the required rate of return to 18%.

**Required:**

For each of the proposed action determine the resulting impact price and recommend the best alternative. **(15 marks)**

**QUESTION 4**

- a) What are the features of an appropriate capital structure? **(10 marks)**
- b) Explain the limitations of using WACC as investment discount rate. **(10 marks)**

**QUESTION 5**

- a) Distinguish between the following pairs of terms:
- i) Systematic and unsystematic risk.
  - ii) Primary and secondary markets
  - iii) Investing decisions and financing decisions. (8 marks)
- b) Shanzu Ltd has capital structure as given below as on 30<sup>th</sup> September 2010:

	<b>Shs. '000'</b>
Ordinary share capital (par sh. 10)	750,000
Retained earnings	150,000
16% preference share capital (par sh. 10)	400,000
12% bonds (par value sh. 1,000)	<u>200,000</u>
	<b><u>1,500,000</u></b>

The financial year has just ended and Shanzu Ltd declared ordinary dividend s. 5.40 per share. Dividends are expected to growth at a rate of 7% p.a. the current cum-dividend market price per share for Shanzu's ordinary share is sh. 50.40. Preference shares are trading at sh. 12.50 while the bonds which are redeemable at par value in 5 years are trading at sh. 960 each. Corporations tax is chargeable at a rate of 30%.

**Required;**

- i) Compute the cost of each component of longterm financing. **(6 marks)**
- ii) Determine the Weighted Average Cost of Capital for the company. **(6 marks)**