

TECHNICAL UNIVERSITY OF MOMBASA

SCHOOL OF BUSINESS

DEPARTMENT OF ACCOUNTING AND FINANCE

UNIT CODE: BFI 4402 UNIT TITLE: PORT FOLIO MANAGEMENT AND INVESTMENT ANALYSIS

SERIES: SEP/DEC SERIES

TERM PAPER ONE

TIME: 2 HOUR

INSTRUCTIONS: ANSWER ANY TWO QUESTIONS.

QUESTION 1

a) Write brief notes on the following Mutual funds schemes and give examples of these Unit trust in Kenya.

i) Money Market fund (5 Marks)

ii) Balanced Fund (5Marks)

b) The following are the possible net cash flows of projects X and Y and their associated probabilities. Both projects have a discount of 10per cent. Calculate the expected net present value for each project. Which project is preferable? (10 Marks)

Project X			Project Y	
Possible Event	Cash Flow	Probability	Cash Flow	Probability
A	40,000	0.10	120,000	0.10
B	50,000	0.20	100,000	0.15
C	60,000	0.40	80,000	0.50
D	70,000	0.20	60,000	0.15
E	80,000	0.10	40,000	0.10

- c) Mabati Ltd is a fast growing manufacturing firm. It earns above –industry return on its investment. It has been earning a rate in excess of 25% on its investments in the past and has good prospects of earnings at the same rate in future as well .Mabati has been following a dividend policy of paying 70% of the earnings to shareholders and retaining 30% .This dividend policy is justified on the grounds that the sole objective of a company is to pay dividends and that dividends have a positive impact upon the price of the share.

Required

If most of the company’s shareholders are young wealthy persons in high tax brackets, is current policy of the company justified? **(5 Marks)**

- d) With the aid of graphs ,write brief notes on the Capital Market Line **(5Marks)**

QUESTION 2

Given the probability distribution for the returns on Stock A and B as follows, compute the security expected returns, risk and portfolio returns. **(10marks)**

State	Probability	Return on Stock A	Return on Stock B
1	20%	5%	50%
2	30%	10%	30%
3	30%	15%	10%
4	20%	20%	-10%

- b) Discuss the differences between of the Capital Asset Pricing Model and Arbitrage Model **(10Marks)**

Question 3

GoldStar Manufacturing Limited is evaluating an investment opportunity that would require an outlay of Shs. 100 million. The annual net cash inflows are estimated to vary according to economic Conditions.

Economic Conditions	Probability	Cash flow Sh.Million
Very good	0.10	35
Good	0.45	28
Fair	0.30	24
Poor	0.15	18

The firm's required rate of return is 14 percent. The project has an expected life of Six years.

Required:

- Compute the expected net present value (NPV) of the proposed investment. **(7Marks)**
- Pwani Limited is planning advertising campaigns in three different market areas. The estimates of probability of success and associated additional profits in each of the three markets are provided below:

	Market 1		Market 2		Market3	
	Profit Sh	Probability	Profit Shs	Probability	Profit Shs	Probability
Fair	10,000	0.40	5,000	0.20	16,000	0.50
Normal	18,000	0.50	8,000	0.60	20,000	0.30
Excellent	25,000	0.10	12,000	0.20	25,000	0.20

Required

- Compute the expected value and standard deviation of profits resulting from advertising campaigns in each of the market areas.**(7Marks)**
- Rank the three markets according to riskiness using the coefficient of variation.**(6Marks)**

Question 4

The risk and expected returns of the two companies is as tabulated below

Company	Expected return %	Standard deviation%	Beta %
P	22	40	.86
Q	24	38	1.24

The correlation between the returns of P and Q is 0.72% the standard deviation of the market return is 20%

Required:-

- Is investing in Q better than investing in P?(3Marks)
- If you invest 30 percent in Q and 70 percent in P, what is your expected rate of return and the portfolio standard deviation? (5Marks)
- What is the market portfolio's expected rate of return and how much is the risk-free rate:? (10 Marks)
- What is the beta of portfolio if P's weight is 70 percent and Q is 30percent?(2Marks)

Question 5

- "Do not put all your eggs in one basket" Discuss this phrase based on HM model of portfolio management.(10Marks)
- Briefly explain the advantages of Mutual Fund.(10Marks)