TECHNICAL UNIVERSITY OF MOMBASA

SCHOOL OF BUSINESS

DEPARTMENT OF ACCOUNTING & FINANCE

UNIVERSITY EXAMINATION FOR:

DIPLOMA IN ACCOUNTANCYAND DLTM

BAC 2212: FINANCIAL MANAGEMENT

END OF SEMESTER EXAMINATION

SERIES:AUGUST2019

TIME:2HOURS

DATE: Pick DateAug2019

Instructions to Candidates
You should have the following for this examination
-*Answer Booklet, examination pass and student ID*
This paper consists of **FIVE** questions. Attemptquestion ONE (Compulsory) and any other TWO questions.
Do not write on the question paper.

Question ONE

a) Market classification is based on the maturity of financial instruments as capital or money markets. Differentiate the two markets. (14 marks)

b) Highlight factors to consider when raising capital finance of a business. (4 marks)

a) Biashara Ltd. has the following capital structure:

	'000
Long term debt	3,600
Ordinary share capital	6,500
Retained earnings	4,000

The finance manager of Biashara Ltd. has a proposal for a project requiring Sh.45 million. He has proposed the following method of raising the funds:

- Utilise all the existing retained earnings

- Issue ordinary shares at the current market price.
- Issue 100,000 10% preference shares at the current market price of Sh.100 per share which is the same as the par value.
- Issue 10% debentures at the current market price of Sh.1, 000 per debenture.

Additional information;-

1. Currently, Biashara Ltd. pays a dividend of Sh.5 per share which is expected to grow at the rate of 6% due to increased returns from the intended project. Biashara Ltd.'s price/earnings (P/E) ratio and earnings per share (EPS) are 5 and Sh.8 respectively.

2. The ordinary shares would be issued at a floatation cost of 10% based in the market price.

3. The debenture par value is Sh.1, 000 per debenture.

4. The corporate tax rate is 30%.

Required:

Biashara Ltd.'s weighted average cost of capital (WACC). (12 marks)

Question TWO

a) Explain factors influencing dividend policies. (10 marks)

b) Dividend refers to the business concerns net profits distributed among the shareholders. Explain FIVE main dividends theories. (10 marks)

Question THREE

A company is considering two mutual exclusive projects requiring an initial cash outlay of Sh. 10,000 each and with a useful life of 5 years. The company required rate of return is 10% and the appropriate corporate tax is 50%. The projects will be depreciated on a straight line basis. The before depreciation and taxes cash flows expected to be generated by the projects are as follows.

YEAR	1	2	3	4	5
Project A	Shs. 4,000	4,000	4,000	4,000	4,000
Project B	Shs. 6,000	3,000	2,000	5,000	5,000

Required:

Calculate for each project

i. The payback period (advice which project is better) (14 marks)

ii. Highlight 3 advantages and 3 disadvantages of payback period (6 marks)

Question FOUR

a) Explain the role of the Nairobi Securities Exchange in economic development in Kenya. (10 marks)

b) Explain the role of central bank of Kenya in financial markets. (10 marks)

Question FIVE

XYZ Ltd wants to raise new capital to finance a new project. The firm will issue 200,000 ordinary shares (Sh. 10 par value) at Sh. 16 with Sh. 1 floatation costs per share, 75,000 12% preference shares (Sh. 20 par value) at Sh. 18 with sh.150, 000 total floatation cost, 50,000 18% debentures (sh. 100 par) at Sh. 80 and raised a Sh. 5,000,000 18% loan paying total floatation costs of Sh. 200,000. Assume 30% corporate tax rate. The company paid 28% ordinary dividends which is expected to grow at 4% p.a.

Required:

Determine the total capital to raise net of floatation costs (10 marks)

Compute the marginal cost of capital of (10 marks)

1. Cost of equity
2. Cost of preference shares
3. Cost of debenture