



TECHNICAL UNIVERSITY OF MOMBASA

SCHOOL OF BUSINESS

DEPARTMENT OF ACCOUNTING AND FINANCE

UNIVERSITY EXAMINATION FOR:

BACHELOR OF COMMERCE/BACHELOR OF BUSINESS ADMINISTRATION

BFI 4304 CORPORATE FINANCE

END OF SEMESTER EXAMINATION

SERIES: APRIL 2025

TIME: 2 HOURS

DATE: Pick Date Select Month Pick Year

Instructions to Candidates

You should have the following for this examination.

-Answer Booklet, examination pass and student ID

This paper consists of **FIVE** questions. Attempt question ONE (Compulsory) and any other **TWO** questions.

Do not write on the question paper.

Question ONE

- a. The time value of money concept is a financial principle that states the value of a shilling today is worth more than the value of a shilling in the future. This philosophy holds true because money today can be invested and potentially grow into a larger amount in the future. Required
 - i. Discern between discounting and compounding (2 marks)
 - ii. Distinguish between simple interest and compound interest (2 marks)
 - iii. Distinguish between lump sum and annuity values (2 marks)
- b. Describe the merits of using market value weights over book value weights in computing the weighted average cost of capital. (4 marks)
- c. Describe the need for asset pricing models in investment evaluation (5 marks)
- d. ABC LTD is a new company had the following facts as at 31st December 2024:
 - 1) The company had issued 300,000 common stocks in the year 2024 that sold for sh.25 per share and their expected dividend was sh.2.50 per share which was expected to grow at 9% indefinitely.

- 2) It also issued 14%, 40,000 debentures of sh.90 at sh.75 each in the year 2010 with a maturity period of 8 years.
 - 3) The company raised additional funds for expansion purpose by issuing 8%, 40,000 non-redeemable preference shares of sh.15 each at a price of sh.13 per share.
 - 4) A 7 year loan was borrowed in 2008 also for expansion purpose of sh.4,000,000 at 16% interest rate.
 - 5) The retained earnings for the year 2010 amounted to Kshs.3 million.
- Required: Assuming a tax rate of 30%, compute the weighted average cost of capital for the company. (15 marks)

Question TWO

The expected returns for assets A and B alongside their probabilities are given below

Probabilities	Asset A	NSE Index returns
0.1	8%	14%
0.2	10%	-5%
0.3	12%	6%
0.2	5%	15%
0.2	-5%	20%

Assuming proportions of 50:50

Required: Compute

- a) The asset returns of the assets A and B (4Marks)
- b) The asset risk of the assets A and B (5Marks)
- c) The asset covariance of the assets A and B (5Marks)
- d) The asset portfolio risk of the assets A and B (6Marks)

Question THREE

- a) Explain the following terms as used in corporate finance:
 - i. Certainty and uncertainty in portfolio analysis (3 marks)
 - ii. Overtrading and overcapitalization. (4 marks)
 - iii. Assignment and factoring of accounts receivables (3 marks)
- b) Describe the causes of overtrading (4 marks)
- c) Describe factors influencing dividend policy of firms. (6 marks)

Question FOUR

- a) If the slope of the SML in an economy is 8.9%. The risk-free rate prevailing in the economy is 4.9%. A security has a correlation coefficient of 0.23 with the market. The market's standard deviation is 15% while that of the security is 19%. Calculate the expected return on the portfolio (4Marks)
- b) A security is fairly priced and has an expected rate of return of 0.13. The market expected rate of return is 0.13 and the risk-free rate is 0.04. Calculate the beta of the stock (3Marks)
- c) Katana invested 50% of his money in security A with a beta of 1.6 and the rest of his money in security B with a beta of 0.7. Calculate the beta of the resulting portfolio (3Marks)
- d) Describe the capital structure decision with aid of diagrams (10 marks)

Question FIVE

- a) Explain **four** advantages of stock repurchase (8Marks)
- b) Safi Limited intends to borrow Ksh 4,000,000 or Ksh 3,400,000 to finance either project A or project B respectively. The following are the expected net cash inflows for the four years.

Year	project A Ksh	project B Ksh.
1	1,800,000	1,600,000
2	1,500,000	1,200,000
3	1,300,000	1,400,000
4	1,700,000	1,200,000

The cost of capital is 12% per annum

Required:

For each project, determine the:

- Net present value (6Marks)
- Profitability index (4Marks)
- Advise the management on the project to invest using each of the above two methods (2Marks)