

TECHNICAL UNIVERSITY OF MOMBASA

School of business

DEPARTMENT OF ACCOUNTING AND FINANCE

UNIVERSITY EXAMINATIONS FOR DEGREE IN BACHELOR OF
COMMERCE/BUSINESS ADMINISTRATION & MATHS, BACHELOR OF
BUSINESS AND INFORMATION TECHNOLOGY AND FINANCE

BFI 4301: FINANCIAL MANAGEMENT

SPECIAL/SUPPLEMENTARY EXAMINATIONS

SERIES; MARCH 2025

TIME; 2 HOURS

Instructions;

Answer question one and any other TWO questions

Do not write on this paper

Question One

a) Sakyiama Poultry Farms is considering purchasing a new incubator that will improve its incubation efficiency to 90% as against the current 50%. The incubator, which is to be purchased immediately will cost sh.120,000. The incubator has a useful life of 4 years, after which it would be sold for scrap at sh.10,000. The current contribution of sh.3 per day old chick will not change. The number of day-old chicks sold are 12,000 units per annum will increase by 80%. Fixed cost will be sh.20,000 per annum. Sakyiama Farms have after tax cost of capital of 12.5% and pays tax in the year in which profit is made at a rate of 15% per annum. The farm is also entitled to capital allowance at 25% on reducing balance.

Required:

i) Calculate the Net Present Value (NPV) and the viability of the investment. **(6 marks)**

ii) Calculate the Internal Rate of Returns (IRR). **(8 marks)**

(b) Royal Yellow Berhad reports sales of sh.6,000,000, average variable costs at 15% of sales and fixed operating costs of sh.1,800,000. The company's total debt is sh.2,000,000 with an interest rate of 10% and its marginal tax rate is 28%.

Required:

i) What is Royal Yellow Berhad's degree of operating leverage, degree of financial leverage and degree of total leverage at this level of output? **(3 Marks)**

ii) Calculate the new EPS for Royal Yellow Berhad next year when sales increase by 20%. Currently the firm has 800,000 shares outstanding. **(3 Marks)**

c) Modigliani and Miller asserted that "dividends payment is irrelevant to shareholders because whatever they appear to be losing if dividends are not paid are gained when the shares are finally sold at a higher price" and management should concentrate on increasing the company's sales. Critically analyses this assertion **(10 marks)**

Question Two

a) The annual demand for Praise Limited's inventory is 10,500 units. The item costs sh.400 a unit to purchase. The holding cost for one unit for one year is 12% of the unit cost and ordering costs are sh.450 per order. The supplier offers a 2% discount for orders of 700 units or more and a discount of 3% for orders of 950 units or more.

Required:

Determine the cost minimising order size of the company. **(8 marks)**

b) Five years ago, Gasoto Ltd. issued 12 per cent irredeemable debentures at their par value of sh.100. The current market price of these debentures is sh.94. The company pays corporation tax at a rate of 30 per cent.

Required:

Calculate the company's current cost of debenture. **(3 marks)**

c) Zeb Limited offers 2 percent discount to its customers who pay within ten (10) days. The company normally collects its debt within thirty (30) days. Assume 365 days in a year.

Required:

Determine the cost of the discount to the company **(3 marks)**

d) Brothers Limited enters into a forward rate agreement (FRA) with Bank of Frica in which Brothers Limited will receive a fixed rate of 8% for nine (9) months on a loan of sh.1million. Bank of Frica agrees to receive a nine (9) months LIBOR rate to be determined in nine (9) months' time on the loan principal.

Required:

Determine the results of the FRA and the effective loan rate if the spot rate for the LIBOR in nine (9) months is: i) 5% ii) 10% **(6 marks)**

Question Three

(a) Discuss how government actions can influence the tasks of the financial manager and explain how these actions can affect the attainment of financial objectives. **(10 marks)**

b) It is believed that the goal of the firm is to maximize profits. However, profit maximization faces a number of challenges. Discuss in detail, FIVE short comings of profit maximization as a goal of the firm. **(10 marks)**

Question Four

a) Anape Ltd is considering issuing a new 10-year bond in the domestic market. The interest rate on the bond is 20%. Interest will be paid semi-annually. The directors are considering the appropriate price at which the new bonds should be sold. The market required return is 25%.

Required:

i) Compute the price investors would be willing to pay for each sh.100 face value bond.

(6 marks)

ii) Explain how changes in average interest rate affect the value of bonds. **(4 marks)**

(b) Mustard Berhad had total earnings last year of sh.12,000,000, but expects total earnings to increase to sh.12,500,000 this year because of the launching of new models.

There are currently 1,000,000 shares of common stock outstanding.

The company has sh.8,000,000 worth of investments to undertake this year. The company finances its investment based on debt: equity ratio of 2:3. The company paid sh.7 per share in dividends last year.

Required:

a) What portion of the new investment will be financed by equity and what portion by debt? **(2 Marks)**

b) If the company follows a pure residual dividend policy, how large a dividend will each shareholder receive this year? **(4 Marks)**

c) If the company maintains a constant dividend payout ratio each year, how large a dividend will each shareholder receive this year? **(4 Marks)**

Question Five

Capit SA is a large firm listed on the Warsaw Stock Exchange. It has the following capital structure:

Long Term Capital	Sh. million
Convertible Debt - 5 yrs; 8%	25
Preferred Shares - 5% coupon + nominal value of 100	15
Common Equity (nominal value PLN 10/share)	10
Retained Earnings	23

The current dividend for the company is Sh. 50/share and is expected to grow at 3% per year in the foreseeable future. The equity shares trade at Sh. 450/share. The preferred shares trade at Sh. 104/share. The convertible debt has a conversion privilege of 2 shares per 1,000 Sh. face value at maturity. The debt currently trades at Sh. 950. The firm's income tax rate is 30%

Required:

- (i) Calculate the firm's weighted average cost of capital (WACC): (10 marks)
- (ii) Discuss the firm's dividend payout policy and whether it has an impact on share price? (5 marks)
- (iii) Explain why the different sources of capital have different levels of risk and return. (5 marks)