CHUKA UNIVERSITY

UNIVERSITY EXAMINATIONS

EXAMINATION FOR THE AWARD OF DEGREE OF BACHELOR OF COMMERCE

BCOM 431: FINANCIAL MANAGEMENT II

STREAMS: ODEL Y4S1 **TIME: 2 HOURS**

DAY/DATE: THURSDAY 7/10/2021 **2.30 P.M – 4.30 P.M**

INSTRUCTIONS

Answer question one and any other two questions

QUESTION ONE

(a) Consider a one year contract to buy an asset at ksh 105, assuming that in 3 months the price of the asset will be ksh 102. What is the value and the price of forward contract at the time if the risk free rate is 5%. [5 marks]

(b) Explain the various stock market anomalities. [8 marks]

(c) An asset is priced at ksh 80 with a free rate of 8% with net storage cost after adjusting for convenience yield as ksh 5. The future expires in 6 months. Determine the futures' contract price. [5 marks]

(d) Describe the assumptions of Efficient Market Hypothesis. [5 marks]

(e) A company requires 12,500 units of a component in its manufacturing process which costs ksh 210 each. The items are available locally and the lead time is 3 weeks. Each order costs ksh 250 and the holding cost is ksh 100 to prepare. The company considers giving a quantity discount of 18% if a minimum of 500 units are ordered advice whether the quantity discount should be given. [7 marks]

QUESTION TWO

(a) Shirandura limited has set the minimum cash balance of ksh 17,500. The variance of the daily cash flow is ksh 6,250,000 and the interest rate on marketable securities is 12% per annum. The transaction cost is ksh 30. Required ;

(i) Target cash balance

(ii) Upper limit

(iii) Average cash balance

(iv) The spread [8 marks]

(b) Explain the factors that influence the working capital requirements of a firm. [6 marks]

(c) Evaluate six differences between a forward contract and a futures contract. [6 marks]

QUESTION THREE

(a) Explain the basic option trading strategies, clearly stating the circumstances under which strategy is applicable. [8 marks]

(b) A company has the following information relating to its equity share: current market price per share of ksh 60, exercise price of ksh 50, time to maturity of 6 months, variance of 0.09 and prevailing risk less rate of 14% per annum.

Required :

(i) The value of the call and put option using black and scholes model. [8 marks]

(ii) What assumption did you make in applying this model? [4 marks]

QUESTION FOUR

(a) Distinguish between equity forwards and commodity forward. [4 marks]

(b) On 1st January 2013 a trader buys gold futures contract. The current future price is USD 500 per Ounce. Assume initial margin is USD, 2,500 and maintenance margin is USD 1,500. The standard quantity is 100 ounces. Required: Determine the date when there is margin call and margin balance of last day of trading if the prices of the asset vary as follows: [10 marks]

Date	Price
1	500
2	495
3	493
4	495
5	497
6	490
7	492
8	490

(c) Explain the following margins as used in futures contract.

(i) Initial margin [2 marks]

(ii) Maintenance margin [2 marks]

(iii) Variation margin [2 marks]
