

CHUKA



UNIVERSITY

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**EXAMINATION FOR THE AWARD OF
DIPLOMA IN PROCUREMENT AND LOGISTICS MANAGEMENT AND DIPLOMA
IN BUSINESS MANAGEMENT**

DIAC 0231: FINANCIAL MANAGEMENT

STREAMS: DIAC

TIME: 2 HOURS

DAY/DATE: MONDAY 03/12/2018

2.30 PM – 4.30 PM

INSTRUCTIONS:

Answer Question One and any other Two Questions

QUESTION ONE

- (a) Explain the following terms as used in financial management
- (i) Agency relationship
 - (ii) Venture capital
 - (iii) Mortgage finance
 - (iv) Time value of money [6 marks]
- (b) Discuss the functions performed by finance managers in a contemporary organization. [6 marks]
- (c) A company is considering investing in a project that promises profit before depreciation and tax of sh 50,000 each year for 3 years. The cost of the project is sh 100,000 with sh 10,000 as the scrap value. Depreciation is on straight line method and the tax rate is 30%. Determine the accounting rate of return. [4 marks]
- (d) Peter deposited sh 120,000 at the end of each year for 15 years. He wanted to withdraw the money after 15 years. How much did he withdraw if the interest rate is 15%? [3 marks]
- (e) State the causes of conflicts between shareholders and auditors. [3 marks]

- (f) A firm is considering investing in the following two projects both costing sh 400,000

Years	Project A cashflows	Project B cashflows
1	100,000	120,000
2	150,000	80,000
3	80,000	100,000
4	120,000	150,000
5	90,000	60,000

Determine the payback period and advise on which project the company can invest in.

[5 marks]

- (g) Highlight the circumstances under which NPV and IRR rules conflicts in ranking the projects. [3 marks]

QUESTION TWO

- (a) Discuss the factors that affect the cost of finance. [5 marks]

- (b) The following is the capital structure of a certain company

	Sh
Ordinary shares (sh 50 par)	5,000,000
10% preference shares (sh 30 par)	3,000,000
15% debentures (sh 120 par)	4,800,000
Retained earnings	3,200,000
10% medium term loan	<u>4,000,000</u>
	20,000,000
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Additional information

- (i) The company currently pays a dividend of sh. 15 per share. The dividend is expected to grow at 12%. The market price of the ordinary shares is sh 80.
- (ii) The preference shares are currently selling at sh 36
- (iii) The denture is currently selling at sh 150 and will mature in 20 years time
- (iv) the loan is currently selling for sh 5,000,000
- (v) Tax rate is 30%

Required: weighted Average cost of capital [12 marks]

- (c) Distinguish between matching and conservative approaches. [3 marks]

QUESTION THREE

- (a) A firm is considering investing in a project costing sh 300,000 with the following information

Years	Earnings before depreciation and tax
1	120,000
2	100,000
3	80,000
4	60,000
5	50,000

Additional information:

Depreciation is on straight line method, tax rate is 30% and the cost of capital is 12%. Required NPV, PI and IRR. [12 marks]

- (b) Explain the function of the security markets. [5 marks]
- (c) Differentiate between capital and money markets. [3 marks]

QUESTION FOUR

- (a) A company is considering investing in a 8 year 15%, sh 8000 bond which is currently selling at the market at sh 10,000, the cost of capital is 14%.

Calculate

- (i) The intrinsic value of the bond [4 marks]
- (ii) The yield to maturity of the bond if the tax rate is 30% [3 marks]
- (b) Describe the factors that influence the working capital needs of a firm. [5 marks]
- (c) A company required 12,500 units of a component. Each order costs sh 250 and the holding cost is sh 100 to prepare and process. The lead time is 3 weeks. Determine EOQ, reorder level, number of orders to be placed and the total relevant costs. [8 marks]
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