

CHUKA



UNIVERSITY

**UNIVERSITY EXAMINATIONS**

**RESIT/SPECIAL EXAMINATION**

**EXAMINATION FOR THE AWARD OF DIPLOMA IN**

**DIAC 0231: FINANCIAL MANAGEMENT**

**STREAMS:**

**TIME: 2 HOURS**

**DAY/DATE: TUESDAY 24/07/2018**

**8.30 A.M. – 10.30 A.M.**

**INSTRUCTIONS:**

- Answer question **ONE** and any other **TWO** questions.

**QUESTION ONE**

- (a) Discuss the managerial functions of a finance manager in the contemporary business environment. (6 marks)
- (b) Agency problem exists when agents pursue their own interests rather than the interest of their principals. Discuss the causes of conflicts between creditors and shareholders and the solutions to the problems. (6 marks)
- (c) Mary deposits Sh 100,000 at the end of each year for 10 years. If she decides to withdraw the amount after 10 years. How much should she withdraw altogether if the interest rate is 10%. (3 marks)
- (d) State the reasons for time preference for money. (3 marks)
- (e) A project with an initial outlay of Sh 200000 promises the following cash flows

Years	Cash flows
1	100000
2	90000
3	80000
4	60000
5	70000

Depreciation is on straight line method, tax rate is 30% and the cost of capital is 12%. Determine the NPV, P1 and IRR. (12 marks)

**QUESTION TWO**

- (a) Briefly discuss the significance of cost of capital. (4 marks)
- (b) The following is the capital structure of Bimbo Company

	Sh
Ordinary shares (sh 25 par)	750000
Retained Earnings	300000
12% Preferences shares (sh 15 par)	450000
10% Debentures (Sh 100 par)	<u>500000</u>
	<u>2,000,000</u>

Additional information

- (i) The company has already paid a dividend of sh 10 per share which is expected to grow at 10%. The current market price of the ordinary shares is sh 50 and incurs a floatation cost of 10% of the market price.
- (ii) The 12% preference shares are currently selling for Sh 25
- (iii) The 10% debentures currently sell for Sh 90 and will mature in 20 years
- (iv) The tax rate is 30%

Required calculate the Weighted average cost of capital (WACC). (9 marks)

- (c) Briefly explain the functions of the security market. (4 marks)
- (d) Differentiate between mutually exclusive and dependent investment decisions. (3 marks)

**QUESTION THREE**

- (a) Rael is considering investing in a 5 year 10% Sh 10000 bond currently selling for Sh. 9,000. Calculate the intrinsic value of the bond if the discount rate is 15% and basing on this calculation should Rael purchase the bond. (5 marks)
- (b) Discuss the determinants of working capital needs of a firm. (6 marks)
- (c) ABC Ltd requires 3750 units of a component in its manufacturing process in the coming year. The items are available and the lead time is 2 weeks. Each order costs Sh 150 to prepare while the holding cost is Sh. 50. Calculate the EOQ, Reorder level, number of orders placed and total relevant costs. (9 marks)

**QUESTION FOUR**

(a) Explain the sources of funds (6 marks)

- (i) Debentures
- (ii) Mortgage
- (iii) Venture capital
- (iv) Treasury bills

(b) State the reasons for valuation of securities. (4 marks)

(c) The following dividend patterns relates to XYZ limited. Calculate the value of the firm if the cost of capital is 22%. (5 marks)

Years	Dividends
2000	2.5
2001	3
2002	4
2003	4.5
2004	5

(d) Explain the non-financial goals of a firm. (5 marks)

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