

CHUKA



UNIVERSITY

UNIVERSITY EXAMINATIONS
EXAMINATION FOR THE AWARD OF DIPLOMA IN PROCUREMENT AND LOGISTICS MANAGEMENT, DIPLOMA IN COOPERATIVE ACCOUNTING AND DIPLOMA IN BUSINESS MANAGEMENT
DIAC 0231: FINANCIAL MANAGEMENT
STREAMS:
TIME: 2 HOURS
DAY/DATE: FRIDAY 10/08/2018
11.30 A.M – 1.30 P.M
INSTRUCTION:

- **Answer question one and any other two questions**

1. (a) An agency relationship exists in an organization between managers and shareholders. However a conflict may arise between the two parties. Discuss.

(i) Reasons for conflict [6marks]

(ii) Any 3 solutions to the conflict [6marks]

(b) If you wish to have ksh 25,000, 5 years from now, how much should you deposit in a savings account each year for the next 5 years at an interest rate of 8%. [3marks]

(c) A company is considering to invest in a project that has the following profits before depreciation and tax.

Year	1	2	3	4	5
Profits	20,000	24,000	28,000	32,000	40,000

The cost of the project is ksh 85,000

The scarp value of the project is ksh 5000 and depreciation is charged on a straight line method.

Discount rate is 12%

Corporate tax rate is 30%

Required, calculate

- (i) Accounting rate of return [8marks]
 - (ii) Net present value [4marks]
 - (iii) Probability index [2marks]
 - (iv) Advise management whether or not to undertake the project. [1mark]
2. (a) Explain the differences between money market and capital market. [5marks]
- (b) A company has a 6 year 15% ksh 1800 par bond value. The current market value of the bond is ksh 2000. Assume a tax rate of 30%.
- (i) Calculate the yield to maturity of the bond if the discount rate is 10%. [3marks]
 - (ii) Calculate the intrinsic value of the bond. [4marks]
 - (iii) Advise management whether to buy or sell the bond. [2marks]
- (c) A manufacturing company has an expected demand of 20,000 units of a certain product during the next year. The cost of processing an order is ksh 15 and the holding cost is ksh 2 per unit.
- (i) Calculate the economic order quantity. [3marks]
 - (ii) Calculate total inventory costs. [3marks]
3. (a) Outline the characteristics of a good investment appraisal. [5marks]

(b) The following is the capital structure of Adam limited

Ordinary share capital @ksh 20	800,000
6% preference share @ ksh 15	450,000
8% debentures @ ksh 80	750,000
10% long term loan	<u>600,000</u>
	<u>2,600,000</u>

Additional information

- (i) The ordinary share is expected to pay dividends of ksh 3 and has a growth rate of 5%. The current market price is ksh 30.

- (ii) The 6% preference shares are now selling at 20 and are expected to mature in 5 years.
 - (iii) The 8% debenture is still selling at its par value and was issued 10 years ago.
 - (iv) The 10% long term loan is currently trading at 800,000
 - (v) Tax rate is 30%
- (c) Determine weighted average cost of capital. [10marks]
- (d) Describe the non financial goals of a firm. [5marks]
4. (a) A firm currently pays a dividend of ksh 4 the dividend is expected to grow at 8% for the first 3 years then at 10% for 2 years then at 12% into perpetuity. The cost of capital is 15%.
- (i) Calculate the intrinsic value of the share. [8marks]
 - (b) Explain the following sources of finance.
 - (i) Bank overdraft [2marks]
 - (ii) Long term loan [2marks]
 - (iii) Preference shares [2marks]
 - (c) State and explain the functions of Nairobi securities exchange. [6marks]
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