CHUKA UNIVERSITY

UNIVERSITY EXAMINATIONS

RESITS/SPECIAL EXAMINATIONS

EXAMINATION FOR THE AWARD OF DEGREE OF BACHELOR OF COMMERCE

BCOM 231: BUSINESS FINANCE

STREAMS: Y2S2 **TIME: 2 HOURS**

DAY/DATE: TUESDAY 29/8/2023 **11.30 A.M. – 1.30 P.M.**

ANSWER QUESTION ONE AND ANY OTHER TWO QUESTIONS

QUESTION ONE

a) Agency problem exists when agents pursues their own interests rather than the interest of their principles. Discuss the causes of conflicts that occurs when auditors pursues their own interest rather than the interest of shareholders and the solutions to the conflicts. (6 marks)

b) Discus the managerial finance functions. (6 marks)

c) A project with an initial outlay of sh 420,000 promises the following Profit before depreciation and tax.

Years	**Profits before depreciation and tax**
1	130,000
2	120,000
3	110,000
4	100,000
5	90,000
6	80,000

Depreciation is on straight line method, tax rate is 40% and the cost of capital is 11%. Determine the NPV, PI and IRR. (15 marks)

d) Peter deposited sh 50,000 at the beginning of each year in his account that earns an interest of 14%. How much will he have if he wanted to withdraw the money after 25 years. (3 marks)

QUESTION TWO

a) The following information has been extracted from the books of Sasha limited

Earnings before interest and tax	15,000,000
10% debenture	30,000,000
Tax rate	50%
Ordinary shares @40	3,200,000
Ordinary dividends	40% of Earnings after tax
6% preference shares	10,000,000
Market price per share	Sh 100
Current assets	20,000,000
Current Liabilities	12,500,000
Stock	5,000,000

Required (10 marks)

i. Dividend per share
ii. Current ratio
iii. Acid test ratio
iv. Earnings per share
v. Earnings yield
vi. Dividend cover

vii. Dividend yield

b) Discuss the purpose of ratio analysis . (6 marks)

c) John is considering investing in a 7 year 11% sh 5,000 debenture currently selling at sh 4,400 in the market. Calculate the intrinsic value of the bond if the required rate of return is 14% and advice John since he intends to purchase the bond. (4 marks)

QUESTION THREE

a) The following is the capital structure of Shirandula company

	Sh (000)
Ordinary shares (sh 70 par)	14,000
12% Preference shares (sh 60 par)	6,000
15% Debentures (sh 100 par)	8,000
18% Medium Term Loan	8,000
Retained Earnings	4,000
	40,000

Additional information

i. The company expects to pay a dividend of sh 18 per share which is expected to grow at 5%. The current market price of the ordinary shares is sh 150 including sh 30 as floatation cost
ii. The 12% preference shares were issued 5 years ago and currently sell for sh90
iii. The 15% debentures currently sell for sh 150 and will mature in 20 years
iv. The medium term loan currently sell at sh 10,000,000
v. The tax rate is 30%

Required calculate the Weighted average cost of capital (WACC) (10 marks)

b) Explain the following sources of funds (6 marks)

1. Debentures
2. Mortgage
3. Venture capital

c) Highlight the significance of cost of capital (4 marks)

QUESTION FOUR

a) A company currently pays a dividend of 18 per share. The dividend is expected to grow at 10% for 4 years, 15% for 3 years and 20% for 2 years after which it will fall to a constant rate of 11%. Calculate the intrinsic value of the share if the required rate of return is 15%. (11 marks)

b) A company is considering investing in two mutually exclusive projects both costing sh 600,000 and has the following cash flows

Years	project A Cash flows	project B Cash flows
1	100,000	200,000
2	300,000	300,000
3	150,000	80,000
4	80,000	100,000
5	180,000	170,000

Required: advise the company on which project to invest in (5 marks)

c) State the reasons for valuation of securities (4 marks)

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