JARAMOGI OGINGA ODINGA UNIVERSITY OF SCIENCE AND TECHNOLOGY

SCHOOL OF BUSINESS AND ECONOMICS

UNIVERSITY EXAMINATION FOR THE MASTER OF SCIENCE IT SECURITY &AUDIT

YEAR 1 SEMESTER 2

2019/20 20 ACADEMIC YEAR

KISUMU CAMPUS

YEAR ONE SEMESTER TWO

COURSE CODE: MBM 5123

COURSE TITLE: FINANCIAL MANAGEMENT

EXAM VENUE:

DATE:

DURATION: 3 Hours

INSTRUCTIONS

1.Answer QUESTION ONE and any other TWO questions

2.Show all your workings.

3.Do not write anything on the question paper

QUESTION ONE

CASE STUDY

Read the extract below and answer Question ONE (a-c) that follows

Cap 486 of the laws of Kenya, main objective is to have an enterprise for equitable distribution of financial commodities at affordable prices whilst creating an outlet for the local manufactures.

On 17th December 1976 Uchumi shareholders, industrial commercial and development corporation (ICDC), Kenya Wines Agencies and Kenya National Trading Corporation (KNTC) and all Government owned Parastatals entered into a management contract with stands SPA of Italy.

Standa, a leading supermarket group with presence in Europe and Vast retail enterprise was given task to manage and train Kenya personnel who would eventually take over the running of the organization. The first three branches were opened in 1976 with the branch making the first milestone. In 1990s Uchumi spearheaded the hypermarket concept in Kenya.

The early 2000's Uchumi started to expanse financial and operational difficulties occasional by sub – optional expansion strategy coupled with weak control systems. This resulted in a market diminution of the company's resources which culminated in its morbidity to meet its obligation in an ongoing basis.

The retail giant was to dive finance strains when it posted a loss of Kshs. 690 million in June 2004 after two years of poor performance. It was headed for collapse until the PTA Bank gave it a bridging loan of Kshs. 500 million.

Although on the strength of advice from its financial adviser, Royal investment management services, the PTA Balls facility was converted into six-year loan to case the repayment burden, the bridging on board either a strategic equity partner or financer.

An attempt to negotiate with stratified partner felt flat due to the Boards Wavering and a feeling that Uchumi was a national institution that should not be sold to foreigners its suitors included Shoprite which has a strong presence in Tanzania, Pick and Pay and Metro Cash & Carry, all of South Africa.(Source business Review,2017)

a) Identify the expansion strategy of Uchumi before it collapsed in 2006 ***(5mks)***

b) Why did the Board of Directors refuse to sell Uchumi Supermarket to the foreigners ***(10mks)***

c) Discuss what caused the collapse of Uchumi Supermarket in early 2000's. ***(10mks)***

d) Highlight the financial strategy of in restructuring the financially distressed company ***(5mks)***

QUESTION TWO

Sonko Sololo limited consider to invest in security X and Y as shown in the data below

Probability	X%	Y %
0.3	35	28
0.4	30	24
0.3	25	**20**

Required:

i) Compute expected returns if the investor spends 40% in security X and the remainder in security Y **(2.5marks)**

ii) Calculate the covariance of X and Y (**2.5 marks)**

b) b) Consider two firms L and U with the following features

	L	U
EBIT	900,000	900,000
Ks	10%	10%
7.5%	2,000,000	

Required;

i) Calculate WACC of L and U **(7marks)**

ii) Calculate the value of each firm using net income approach**(8marks)**

QUESTION THREE

Pepe limited expects earnings and dividends to grow at a constant rate of 9% in the future. The company has just paid dividend of Sh.3.6 per share and its stock currently sell at a price of sh.60 per share.

Required: Compute the cost of Equity (**5 marks)**

b) Differentiate Residual theory and M&M theory of dividend **(10 marks)**

QUESTION FOUR

The Kaluma Corporation is a manufacturing of pencils. It has received an order for 5,000 pencils and the company has to decide whether to accept the order. From recent experience, the company knows that each pencil requires 5cents in raw materials and 50 cents in direct labor costs. The variable costs are expected to continue to apply in the future. What will Kaluma's total variables cost, if it accepts the order? **(5marks)**

b) Mauwa construction company is considering investing Ks.500,000 in a project which have expected useful life of 5 years with no salvage value. The project is estimated to generate the following cash flows after tax

Year	Cash flows
1	100,000
2	106,000
3	124,000
4	130,000
5	190,000

The company's cost of capital is 10%

Required

Evaluate the above and give your recommendation in each case using the following **techniques**

a) Net present value **(5marks)**

b) Internal rate of returns **(5marks)**

QUESTION FIVE

a) Explain capital structure theories **(8marks)**

b) What are specific assumptions relevant to Net Income Approach (NIA) to achieve the capital structure **(7marks)**?