JARAMOGI OGINGA UNIVERSITY OF SCIENCE AND TECHNOLOGY

SCHOOL OF BUSINESS AND ECONOMICS

UNIVERSITY EXAMINATION

FOR DEGREE OF BACHELOR OF BUSINESS

ADMINISTRATION WITH IT

4th YEAR 1ST SEMESTER 2015/2016 ACADEMIC YEAR

KISUMU LEARNING CENTRE

COURSE CODE: ABA 420

COURSE TITLE: CORPORATE FINANCE

EXAM VENUE: STREAM

DATE: EXAM SESSION:

TIME: 2.00 HOURS

Instructions:

1. **Answer question 1 (compulsory) and ANY other 2 questions.**
2. **Candidates are advised not to write on the question paper.**
3. **Candidates must hand in their answer booklets to the invigilator while in the examination room.**

QUESTION ONE

a) Explain the followings as used financial management

Accounting rate of returns **(2.5 marks)**

Internal rate of returns **(2.5marks)**

Dividend payout **(2.5marks)**

Financial risks **(2.5 marks)**

b) Explain the importance of time value of money **(10 marks)**

c) Consider a project with the following cash flow

Period	Cash flows (sh)
0	(3000,000)
1	400,000
2	350,000
3	250,000
4	200,000

Required: determine the payback period (**5 marks)**

d) Janet intends to deposit 500,00 for each year for the next four years in a bank earning an interest of 12% p.a .Compute the future annuity of the amount **(5 marks)**

QUESTION TWO

K Ltd is evaluating an investment opportunity that would require an outlay of Ksh 100M. The annual net Cash inflows are estimated to Vary according to economic conditions as follows: -

Economic Conditions	Probability	Cash flows (sh 000)
Very Good	0.1	35000
Good	0.45	28000
Fair	0.3	24000

Poor	0.15	18000

The Firm's rate of return is 14%, the project has expected life of 6years.

Required

Compute the expected NPV of the proposed Investment (10 marks)

b) Mamboleo Weavers decides to buy a small office building costly Shs 20 million and take a fixed loan over 5 years at 10% per annum. The loan is to be paid in five equal installments starting at the end of the first year.

Required

i) Compute the annual repayment (3 marks)

ii) Amortization schedules (7 marks)

QUESTION THREE

a) Marine Centre ltd has the following data.

Profit after tax Shs.30, 000,000

Total dividend for the year Shs.18, 000,000

Market price per share (MPS) shs.20

Number of ordinary shares 6,000,000

Using this data, determine the following investor ratios and explain their significance:

i) Earnings per share (EPS)

ii) Dividend per share (DPS)

iii) Price earnings ratio (P/E)

iv) Dividend payout ratio (10 marks)

a) Bahati Company has the following capital structure.

Source Amount

Debentures	8,000,000
Preference capital	2,000,000
Retained earnings	4,000,000
Ordinary share capital	6,000,000
20,000,000	

The component costs of capital are; kd is 6%, kp is10.5%, kr is 14%,ke is 17.2%

Compute the WACC. (10 marks)

QUESTION FOUR

a) Describe the roles of a financial manager in a manufacturing firm (10 marks)

b) Mr. Kazi is considering giving up his paid employment and going into business on his own account. He is considering buying a quarry pit with a "life" of about 35yrs. To buy this business he would have to pay sh.2375000 now. Mr. Kazi wishes to retire in 20yrs time. He predicts the net cash of operating receipts from this business will be sh.625, 000 p.a for the first time 15yrs and sh.500, 00p.a for the last 5yrs. He thinks that the business could be sold at the end of the 20yrs period for sh.750, 000. Additionally, he estimates that certain capital replacements and improvements would be necessary and this should amount to sh.50, 000p.a for the first 5yrs sh.75, 000p.a for the next five years, sh.100, and 000p.a for the next 7yrs and nothing for the last 3yrs. This expenditure would be incurred at the start of each year.

Mr. Kazi has excluded any compensation to himself from the above data. If he should purchase the business, however, he would have to leave his present job which he earns sh.250, 000 a year. To finance the purchase of this business, he would have to realize his present savings, which are invested to yield a return of 10% before tax and have a comparable risk factor.

Required.

b) Advice Mr. Kazi as to whether or not it is advisable to purchase the business in the right of information given. Ignore income tax (5 marks)

c) State any additional information which you would have liked to have available to you before giving advice to Mr. Kazi (5 marks)

QUESTION FIVE

A Ltd. Is considering acquiring B Ltd. The selected financial data for the two companies are as follows

	A Ltd	B Ltd
Annual sales	750 million	90 million
Net income	60 million	7.5 million
Outstanding share	15 million	3 million
Earnings per share	4 million	2.25 million
Market price per share	44 million	20 million

Both companies are in the 30% corporate tax bracket

Required

a) The maximum exchange ratio A Ltd that should agree to if it expect no dilution in the EPS (4 marks)

b) The premium that shareholders of B Ltd would receive at the exchange ratio 4 marks)

c) A Ltds post-merger EPS if the two companies settle at the price of Shs. 24.20 per share (4 marks)

d) A Ltds EPS if B Ltd. accept Shs. 6.00 dividend convertible preference shares whose stated value is Shs 100 for every five ordinary shares of their own (4 marks)

e) A Ltds EPS if every 50 ordinary shares of B Ltd are exchanged for one 8% debenture of par value Shs 1000 (4 marks)