JARAMOGI OGINGA ODINGA UNIVERSITY OF SCIENCE AND TECHNOLOGY

UNIVERSITY EXAMINATIONS FOR BACHELOR OF LOGISTICTS SUPPLY CHAIN MANAGEMENT YEAR FOR SEMESTER ONE

DECEMBER 2016

BBM3411: FINANCIAL MANAGEMENT

DURATION: 2HOURS

INSTRUCTIONS:

1. QUESTION ONE IS **COMPULSORY**
2. ANSWER **THREE QUESTIONS** IN THIS PAPER

QUESTION ONE (30 MARKS - Compulsory)

a) The following information relates to XY ltd's capital structure:

Ordinary shares (kshs 25 Par Value) kshs 8,000,000

8% Preference Shares (kshs 24 par Value) kshs 6,000,000

9% Participating Preference Shares (kshs 25 Par Value) kshs 8,000,000

10% Preference Shares (kshs 20 par Value) kshs 3,000,000

10% debentures (kshs 20 each) kshs 4,000,000

12% debentures (kshs 30 each) kshs 9,000,000

15% debentures (kshs30 each) kshs 9,000,000

Additional Information

i) The firm intends to raise a medium term loan of 15 million from a commercial bank at an interest charge of 12% p.a, and 5.6 million long term loan at an interest charge of 10.6% p.a.

ii) The current market prices for the above sources of capital are:

- kshs 31 for ordinary shares and this is inclusive of a floatation cost of kshs 1.0 per share
- 8% preference shares were issued in 2004 and currently sell for kshs 20
- 9% Participating Preference Shares were issued in 2010 and currently sell for kshs 30.
- The 10% preference shares were issued in 2008 and currently sell for kshs 25.
- 10 % debentures that were issued in 2006 are perpetuities and currently sell for kshs 25
- 12% debentures were issued in 2010 and currently sell at kshs 40.
- 15% debentures were issued in 2012 and currently sell at kshs 35.

The ordinary shareholders expect cash dividends of kshs 3.80 per share indefinitely with a dividend growth rate of 3% p.a. the company pays a

corporation tax rate at 40%. Use this information to calculate the weighted average cost of capital (WACC) for the company **(12 marks).**

b) Actarm PLC ltd is examining two projects A and B whose projected cash flows are given below:

Year	Project A	Project B
	Kshs	Kshs
0	-3,800,000	-3,400,000
1	2,600,000	2,000,000
2	1,300,000	1,200,000
3	-700,000	2,200,000
4	100,000	500,000
5	550,000	-760,000

The projects salvage value is kshs 480,000 and kshs 785,000 for projects A and B respectively. Using the discount rates of 8% and 16 %; compute the NPV values and advice the management on investment superiority **(10 marks).**

c) The following is an extract of information contained in the financial statements of ABC limited

ABC ltd

Income Statement (extract)

	2006	2005
	Kshs	Kshs
Sales	31,000	25,500
Cost of sales	18,000	16,000
Gross profit	**13,000**	**9,500**
Operating expenses	9,500	7,500
Profit before taxation	3,500	2,000
Current years taxation	1,600	900
Profit after taxation	**1,900**	**1100**
Dividends	600	600
Retained profit for the year	**1,300**	**500**

Use the information to compute the gross profit and net profit rations; advice the management **(4 marks)**

d) Modigliani and Miller approach on the Capital structure and financing decision is based on a number of assumptions; briefly state these assumptions **(4 marks)**

QUESTION TWO (20 MARKS)

a) Distinguish between money markets and Capital Markets **(5marks).**

b) Discuss any four managerial finance functions of a manager **(4 marks).**

c) Explain the uses of financial statement analysis information **(4 marks).**

d) Briefly state the main characteristics of a sound financial plan **(3marks)**

e) Using a suitable illustration, describe the working capital cycle of a manufacturing firm **(3marks)**

QUESTION THREE (20MARKS)

a) The dividend policy of a firm depends on the availability of investment opportunity and the relationship between firms internal rate of return and its cost of capital; based on this assumption critic Walter's Model on Dividend relevance **(8marks).**

b) Discuss the causes of conflict between shareholders and debenture-holders in a firm. **(3marks)**

c) Discuss the limitations of using IRR technique **(2marks)**

d) XYZ ltd. is considering three possible capital projects for next year. Each project has a 1 year life, and project returns depend on next year's state of the economy. The estimated rates of return are shown below.

State of the Economy	Probability of Occurrence	Rate of Return		
		M	**N**	**Q**
High	0.25	10%	9%	14%
Medium	0.5	14%	13%	12%
Low	0.25	16%	18%	10%

Use the information to Determine the expected rate of return, variance, standard deviation and coefficient of variation **(7marks)**

QUESTION FOUR (20 MARKS)

The following information relates to Kahangi Ltd's balance sheets for the year ended 30th September 2013 and 2014 are as follows:

	2013	2014
	(kshs)	**(kshs)**
Issued share capital	7,000,000	9,000,000
Revenue reserve	3,200,000	3,900,000
Debentures	2,400,000	3,000,000
Creditors	1,300,000	1,400,000
Tax provision	1,100,000	1,200,000
Proposed dividends	350,000	400,000
	15,350,000	**18,950,000**
Fixed assets	7,000,000	8,500,000
Current assets:		
Stocks	5,000,000	6,000,000
Debtors	1,800,000	1,750,000
Bank balance	1,550,000	2,650,000
	15,350,000	**18,980,000**

Additional Information

i. Accumulated depreciation as at 30th September 2009 was Kshs 2,500,000 and Kshs 2,300,000 at 30th Sep 2013.

ii. During the year ended 30th September 2014 fixed assets were purchased at a cost of Kshs 2,700,000 while fixed assets whose original cost was Kshs 1,000,000 were disposed of for Kshs 750,000. The net book values of the assets were Kshs 409,000 and the profit on the sale of the fixed asset has been included in the revenue reserve.

You are required to prepare Kahangi Ltd's cash flow statement for the year ended 30th September 2014 **(20 MARKS)**

QUESTION FIVE (20Marks)

A firm intends to invest in projects A, B and C the projected cash flows are as in the table below. If the rate of return is 10%. Advice the management.

Year	Cash flows		
	Project A	**Project B**	**Project C**
0	-200,000	-200,000	-200,000
1	140,0000	120,000	90,000
2	30,000	20,0000	50,000
3	90,000	20,000	50,000
4	40,000	70,000	80,000

You are required Calculate the Net Present Value for the projects and advice the management (20marks)