

**JARAMOGI UNIVERSITY**

**BUSIA CAMPUS**

**ABA 320: INVESTMENT AND PORTFOLIO MANAGEMENT**

**ANSWER QUESTION ONE AND ANY OTHER 2 QUESTIONS. TIME: 3 HRS.**

**QUESTION ONE**

- a) Unpredictable market environment is leading investing to turn to fixed income investments (real assets investments).
- i. Name five examples of real assets investments (3mks).
  - ii. Explain the potential benefits of investments in real assets (or estate) (10mks).
  - iii. Describe the pitfalls of real assets investments. (5mks).
  - iv. State five assumptions of capital assets pricing model (CAPM) and two uses of CAPM. (7mks).
  - v. Mary is considering a private equity investment in a new sweet project. The project is inherently risky with a deviation of 80% p.a. the beta of the project is 0.51. The risk free rate is 5% and the expected market return is 13.56%.
  - vi. What is the required rate of return on the project? (5mks).

**QUESTION TWO**

- (a) Discuss the three forms of capital markets efficiency (10mks).
- (b) Differentiate between debt financing and equity financing (5mks).
- (c) What types of short-term and long term expenditures does a firm make? (3mks).
- (d) Define the following terms –
  - (i) Convertibles
  - (ii) Warrants (2mks).

**QUESTION THREE**

- (a) Y ltd Co. has an issued ordinary share capital of 500,000 shares of Kshs. 1 each. It also has revenue reserves totaling Kshs. 300,000 and a capital reserve of Kshs. 80,000. What is its assets cover? (10mks).
- (b) XYZ Ltd Co. cash flow statement reflect a net cash flows from operation activities for the year ended 31<sup>st</sup> Dec 2013 as Kshs (150,000,000) i.e. negative net cash flows; while its net profit

after tax for the same period is Kshs. 11,000,000. Briefly comment on its performance or financial analysis red flag. (5mks).

(c) Bondo Ltd Co. has in issue a debenture quoted at a value par kshs.100 nominal stock. This debenture is a 5<sup>1/2</sup>% irredeemable debenture. The current market rate of interest on investments of this kind is 9% p.a. What is the value of this debenture? (5mks).

#### QUESTION FOUR

The following figures have been extracted from the annual financial statements of Busia Ltd. Calculate some ratios likely to be of interest to a shareholder in fundamental analysis.

	Kshs.
Ordinary share capital (1 Share = Kshs. 1)	5,000,000
Reserves	1,200,000
Loan capital	1,200,000
Profit after tax and loan interest	550,000
Divided	300,000

The current market price of the shares is Kshs. 1.50 each (20mks).

(a) Define briefly the difference between perfect capital markets and imperfect capital markets.

(6mks).

(b) If  $E(R_m) - R_f = 0.085$  and  $R_f = 0.034$ . Calculate the expected return based on beta of 1.25 (5mks).

(c) If beta is 1.25 and is offering an expected return of 16% instead of security market line return stated under 5 (b) above, comment on the pricing of the security or the arbitrage opportunity (4mks).

(d) Explain briefly the difference between systematic risk and unsystematic risk under CAPM (3mks).

(c) CAPM and APT are ex-ante models and ex-post models respectively. Briefly explain (2mks).

