



JARAMOGI OGINGA UNIVERSITY OF SCIENCE AND TECHNOLOGY

SCHOOL OF BUSINESS AND ECONOMICS

MASTERS OF BUSINESS ADMINISTRATION

TIME: 3.00 HOURS

UNIVERSITY EXAMINATION

COURSE CODE: MBM 5123

ACADEMIC YEAR OF STUDY: 2018/2019

COURSE TITLE: FINANCIAL MANAGEMENT

DATE:

INSTRUCTIONS:

- 1. Answer ANY FOUR 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**
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QUESTION ONE

- a) Identify various stages of capital budgeting process (3 marks)
- b) The following financial statements related to the A B C company

Assets	Kshs.	Liabilities & net worth	
Cash	28,500	Trade credit	116,250
Debtors	270,000	Notes payable (9%)	54,000
Stock	649,500	other current liabilities	100,500
Total current assets	948,800	long term debt (10%)	300,000
Net fixed assets	285,750	Net worth	663,000
	<u>1,233,750</u>		<u>1,233,750</u>

Income statement for the year ended 31 March 2016.

Sales	sh.1, 972,500
Less cost of sales	<u>1, 368, 00</u>
Gross profit	604, 500
Selling and distribution expenses	<u>498, 750</u>
Earnings before interest and tax	105,750
Interest expense	<u>34,500</u>
	71,250
Estimated taxation (40%)	28,500
Earnings after interest and tax	<u>42, 750</u>

Required:

- a) Calculate
- Inventory turnover ratio (2 marks)
 - Times interest earned ratio (2 marks)
 - Total assets turnover (2 marks)
 - Net profit margin (2 marks)

(Note: Round off your ratio to one decimal place)

b) The ABC company operates in an industry whose norms are as follows:

Ratio	Industry Norm
Inventory turnover	6.2 times
Times interest earned ratio	5.3 times
Total assets turnover	2.2 times
Net profit margin	3%

Required:

Comment on the revelation made by the ratios you have computed in part (a) above when compared with the industry average. (4 marks)

QUESTION TWO

- a) Identify the objectives of working capital management and discuss the central role of working capital management in financial management (5 marks)
- b) Suggest and discuss any three policies that a Limited Company may be using in the management of the working capital (6 marks)
- c) A firm may adopt a conservative policy or an aggressive policy in financing its working capital needs. Clearly distinguish between:
 - i) A conservative policy and (2 marks)
 - ii) An aggressive policy. (2 marks)

QUESTION THREE

- a) Write short notes on the following:
 - i) Financial implication (1 marks)
 - ii) Capital Rationing (2 marks)
- b) 'Value maximization is a key objective of private firms' Discuss (3 marks)
- a) Briefly explain the yardsticks used in ratios analysis. (4 marks)

b) List and explain at least FIVE differences between Debt Capital and Equity Capital

(5 marks)

QUESTION FOUR

a) List and Explain the advantages and limitations of the following capital investment methods:

- i) Payback methods (2 marks)
- ii) Accounting Rate of Return (ARR) (2 marks)
- iii) Net Present Value (NPV) (2 marks)
- iv) Internal Rate of Return (IRR) (2 marks)

b) A firm is considering two mutually exclusive projects where each require an initial outlay of Kshs: 50,000 with the following net cash flows:

Year	Project A	Project B
1	20,000	30,000
2	30,000	20,000
3	10,000	10,000
4	5,000	5,000

The firms cost of capital is 10%. For each project calculate:

- i) Payback period
- ii) Net present value
- iii) Comment on the results

(7 marks)

QUESTION FIVE

a) Distinguish between the following:

- i) Degree of Operating Leverage (DOL) (1 mark)
- ii) Degree of Financial Leverage (DFL) (1 mark)

- iii) Degree of Combined Leverage (DCL) (1 mark)
- b) Space Rocket Company had Earnings Before Income and Tax (EBIT) of Kshs: 50 million for the current financial year and an EBIT of Kshs: 40 million for the previous fiscal year, or a 25 percent increase year over year (YOY). Space Rocket Limited reported sales of kshs: 80 million for the current fiscal year and sales of Kshs: 65 million for the previous fiscal year, a 23.08 percent increase. Additionally SpaceRocket reported an Earning Per Share (EPS) of Kshs: 2.50 for the current fiscal year and an EPS of Kshs: 2 for the previous fiscal year, a 25 percent increase.

Calculate:

- i) Degree of Operating Leverage (DOL) (3 marks)
- ii) Degree of Financial Leverage (DFL) (3 marks)
- iii) Degree of Combined Leverage (DCL) (4 marks)
- iv) What percent change in EPS would be if Space Rocket's sales changed by 1 percent. (2 marks)

QUESTION SIX

- a) Explain any SIX qualities of an effective investment evaluation technique (3 marks)
- b) XYZ Company Limited is a distributor of air filters to retail shops. It buys its filters from several manufacturers. Filters are ordered in lot sizes of 100 and each order costs Sh.400 to place. Demand from retail shops is 200,000 filters per month and the carrying cost is Sh.10 per filter per month.

Required

- i) Compute the optimal order quantity with respect to number of lot sizes”
(3 marks)
- ii) If a safety stock of 2,000 filters is desired calculate the total relevant costs
(3 marks)
- iii) A certain manufacturer offers a discount of 2% for purchases of 50 lot sizes or more. Determine whether the discount should be taken. (Assume that each filter costs Sh.100).
(6 marks)