



**MASINDE MULIRO UNIVERSITY OF
SCIENCE AND TECHNOLOGY
(MMUST)
MAIN CAMPUS**

**UNIVERSITY MAIN EXAMINATIONS
2022/2023 ACADEMIC YEAR**

**END OF SEMESTER MAIN EXAMINATIONS
FOR**

COURSE CODE: MBA 808

COURSE TITLE: FINANCIAL MANGEMENT

DATE: Wednesday 19TH April 2023

TIME: 2.00–6.00PM

INSTRUCTIONS TO CANDIDATES

Attempt **QUESTION ONE** and any other two questions

TIME: 3 Hours

MMUST observes ZERO tolerance to examination cheating

This Paper Consists of 3 Printed Pages. Please Turn Over. ►

QUESTION ONE (30 MARKS)

- a) Define agency relationship from the context of public limited company and briefly explain how this arises and give 5 measures that would minimize agency problem between the owners and the management (10 mks)
- b) Briefly describe the greatest difficulties faced in capital budgeting in the real world (5mks)
- c) You client has received confusing advice from 3 investment advisers and he is aware that you studying financial management at MMUST -University and has come to you for advice. He wishes to invest Kshs 100,000 for 2 years with interest compounded but with right to withdraw at a moment notice
 - ✓ “Pesa pap” one of the investment advices has recommended Idakho holdings currently holding interest 8% pa after tax with interests paid half yearly.
 - ✓ “Wepukhulu brokers have recommended investing with GD bank at interest rate of 10% before tax with interest paid half yearly
 - ✓ “Mkombero assurances” have suggested investing with Sitirira bank return which is offering interest rate of 9% before tax interest is payable every 3 month.

Required

- a) After carrying out a suitable analysis make a recommendation to your client regarding which of the three price of investment advice she would take assume a standard rate of tax at 30% (12mks)
- b) What situation might occur that would make you to consider you advice (3mks)

QUESTION TWO (20 MKS)

- (a) Differentiate systematic risk and unsystematic risk giving one examples for each. (4 marks)
- (b) The expected return for securities X and Y are as shown below.

Economy	Probability	X	Y
1	0.2	-10	12
2	0.1	8	-6
3	0.4	6	-8
4	0.1	3	13
5	0.2	-6	18

- i. Determine the risk for each of the securities x and y (6 marks)
- ii. Determine the risk of efficient portfolio or minimum variance portfolio when x and y are combined. (10 marks)

QUESTION THREE (20MKS)

- a) Explain any three alternative dividend policies a firm may adopt (6 mks).
- b) Identify any six factors a firm must consider when designing dividend policies (3 marks).
- c) ABC Ltd. makes cash payments of Shs.10,000 per week. The interest rate on marketable securities is 12% and every time the company sells marketable securities, it incurs a cost of Shs.20.

Required

- i. Determine the optimal amount of marketable securities to be converted into cash every time the company makes the transfer. (3 marks)

- ii. Determine the total number of transfers from marketable securities to cash per year. (3 marks)
- iii. Determine the total cost of maintaining the cash balance per year. (3 marks)
- iv. Determine the firm's average cash balance. (2 marks)

QUESTION FOUR (20MKS)

- a) The management of a computer manufacturer is considering opening a new factory. Explain the usefulness to management of both the payback period and net present value and techniques of investment appraisal when deciding where to locate the new factory. (3marks)
- b) The following information was from XYZ feasibility studies. It has studied two ventures:
 - i. Cost 100,000/= and 160,000/= at the beginning of the 4th year and it will generate inflows 1-3rd year 80,000/= and from 4-6th year 50,000/= per annum.
 - ii. Initial cost 200,000/= and 80,000/= at the beginning of the 4th year and it will generate the following inflows: 1st – 2nd year - Shs.100,000 per annum 3rd – 6th year -Shs.70,000 per annum
 Using the cost of finance of 12% compute the P.I. of these two ventures, advise the company accordingly.

QUESTION FOUR (20 MKS)

- a) Kikuyu Investment Company has had a good trading and want to raise further finance from the following sources.
 - To issue 100 000 ordinary shares of Kshs. 10 at Kshs. 15 each
 - To issue 100,00 10% preference shares of Kshs. 10 at Kshs. 12 each
 - To issue 100 000 15% debentures of Kshs. 100 at Kshs. 90 each
 - To raise a medium term loan of Kshs. 5 million from a financial institution which will be at an interest rate of Kshs. 20% pa.

This company will pay an annual dividend to ordinary shares of 14% and corporation tax of 50%

Required

- i. The total amount this company will raise if this plan is realized (4mks)
- ii. The cost of each source of finance (8 mks)
- iii. The weighted average cost of capital of additional finance (4mks)

- b) Consider a 4 year project with initial outlay of sh.300000 p.a. using the following cash flows.

Yr.	1	2	3	4
C/Fs (000)	140	120	80	60

If the cost of capital is 14%, calculate IRR of the project.(4 marks)