(*Knowledge for Development*)

KIBABII UNIVERSITY

UNIVERSITY EXAMINATIONS
2020/2021 ACADEMIC YEAR
FOURTH YEAR, SECOND SEMESTER EXAMINATIONS

SUPP/ SPECIAL EXAMINATION

FOR THE DEGREE IN BACHELOR OF COMMERCE

COURSE CODE: BCF 440E

COURSE TITLE: STRATEGIC FINANCIAL MANAGEMENT

DATE: 17TH FEBRUARY, 2021 **TIME: 11.00AM – 1.00PM**

INSTRUCTIONS TO CANDIDATES

- **Answer Question ONE and ANY another TWO**
- **Do not write anything on the question paper**

QUESTION ONE

a) Show the steps of financial planning in strategic management [10 marks]

b)

Discuss the shortcomings of accounting ratios in Financial modeling [10 marks]

c)

a) Limuru Tea limited, a listed firm on NSE, had the following data;

- Sales: Shs1000000
- EBIT: Shs 500,000
- Total Assets: Shs 2000000
- Book Value of Total Liabilities: 1000000
- Retained Earnings: 1000000
- Market Value of Equity:shs 3000000
- Working Capital: shs 500,000

Required; Calculate the firms Altman Z- score, and comment on your answer. (10 marks)

QUESTION TWO

Year	0	1	2	3	4	5
FCF	50000	16000	16000	16000	16000	8000

Unleaverd cost of capital = 12.5%, value of project 2249

Debt Amount	10000
Cost	7%
Interest	5%
Tax	25%
PV of debt financing	1911

Required; Calculate the Adjusted NPV (10 marks)

b) Discuss the benefits of a merger and acquisition strategy (10 marks)

QUESTION THREE

Tin Co is planning an expansion of its business operations which will increase profit before interest and tax by 20%. The company is considering whether to use equity or debt finance to raise the shs2m needed by the business expansion. If equity finance is used, a 1 for 5 rights issue will be offered to existing shareholders at a 20% discount to the current ex dividend share price of shs5·00 per share. The nominal value of the ordinary shares is shs1·00 per share. If debt finance is used, Tin Co will issue 20,000 8% loan notes with a nominal value of shs100 per loan note.

Financial statement information prior to raising new finance;

	SHS.000,000	SHS.000,000	
EBIT	1597	EQUITY & LIABILITY	
INT	(315)	Ordinary Shares	2500
TAX	(282)	Retained Earnings	5488
EAT	1000	Long term liabilities	4500
		Total Equity & Liability	12488

The current price/earnings(P/E) ratio of Tin Co is 12·5 times. Corporation tax is payable at a rate of 22%.Companies undertaking the same business as Tin Co have an average debt/equity ratio (book value of debt divided by book value of equity) of 60·5% and an average interest cover of 9 times.

Required:

(a)

(i) Calculate the theoretical ex rights price per share. (3 marks)

(ii)Assuming equity finance is used, calculate the revised earnings per share after the business expansion (4 marks)

(iii)Assuming debt finance is used, calculate the revised earnings per share after the business expansion. (3 marks)

b)

Use calculations to evaluate whether equity finance or debt finance should be used for the planned business expansion. (10 marks)

QUESTION FOUR

The following are abstracts of Income statement and Balance sheet from the books of Unga limited

	2018	2017
Revenue:		
Project Advisory Fees	200,000	186,000
Total Revenue (A)	**200,000**	**186,000**
Expenses:		
Direct Expenses	100000	95000
Total Operating Expenses (B)	**100,000**	**95000**
Operating Income (C = A minus B)	100,000	91,000
Tax Rate	30%	30%
Tax on operating income (D = C * Tax Rate)	30,000	$27,300
Net Operating Income After Tax (C minus D)	**70,000**	**63,700**

Particulars	**Balance Sheet**	
	2018	**2017**
Equity	20,000	17,000
Debt	10,000	7,000
Sources of Funds (A)	**30,000**	**24,000**
Fixed Assets	20,000	18,000
Current Assets	20,000	16,000

Less: Current Liabilities	10,000	10,000
Uses of Funds (B)	**30,000**	**24,000**
Cost of Debt	8%	8%
Cost of Equity	10%	12%

Required;

a) Calculate the Weighted Average Cost of Capital (WACC) [5 marks]

b) Calculate the Economic Value Added (EVA) for the year 2017 [15 marks]