



*(Knowledge for Development)*

**UNIVERSITY EXAMINATIONS**  
**2021/2022 ACADEMIC YEAR**  
**FOURTH YEAR FIRST SEMESTER**  
**MAIN EXAMINATION**

**FOR THE DEGREE OF BACHELOR OF COMMERCE**

**COURSE CODE: BCF 211**

**COURSE TITLE: FINANCIAL MANAGEMENT**

**DATE:** 24<sup>TH</sup> JANUARY, 2022      **TIME:** 9.00AM - 11.00AM

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**INSTRUCTIONS TO CANDIDATES**

1. Answer Question One in Section A and Any other TWO (2) Questions in Section B

2. Question **one** carries **30** marks and each of the other two questions carry **20** marks each.

TIME: 2 Hours

KIBU observes ZERO tolerance to examination cheating

**SECTION A (COMPULSORY)**

**QUESTION ONE(30mrks)**

- a) The role of the financial manager in a modern organization is pervasive in all the activities of any business entity.

In the light of the above statement, examine six roles of a finance manager in an organization

(6

marks)

- b) Propose six factors to consider when choosing between long term loan capital and ordinary share capital as a source of finance (6 marks)
- c) One of the ways creditors could protect themselves against the inherent risk that might arise from agency conflict is through adopting restrictive covenants.

With reference to the above, describe restrictive covenants in a debt contract (6marks)

- d) Bungoma Limited intends to invest in a four year mini projects whose initial outlay is sh. 32,000,000. The is expected to generate the following cash flows at the end of each year:

Year	1	2	3	4
Cash flows (sh.000)	12,000	15,000	9,000	6,000

Additional information:

- i) The cost of capital is 12%
- ii) Ignore taxation.

**Required**

Compute the following in each case and advise the management on whether to undertake the project:

- i) Net present value (NPV) (4 marks)
- ii) Internal rate of returns (IRR) (4 marks)
- iii) Profitability index (4 mark)

**SECTION B**  
**ANSWER ANY TWO QUESTIONS**

**QUESTION TWO**

- a) Describe five reasons for valuing financial assets (5 marks)
- b) XYZ Limited is forecasting a growth rate of 12% per annum for the next 2 years. The growth rate is likely to fall to 10% for the third and fourth years. Thereafter, the rate is expected to stabilize at 8% per annum.

The company has just paid a dividend of sh. 1.50 per share and the investor's required rate of return is 16%.

**Required:**

The company's theoretical value of the share (6 marks)

- c) The earning yield of Omega Limited is 20% and the market price per ordinary share is sh.100. Each share has a par value of sh.50. The company has declared a 10 % dividend for the period.

Required:

- i) The earnings per share (3 marks)
- ii) The dividend cover (3 marks)
- iii) The price earnings ratio (3 marks)

**QUESTION THREE**

- a) Discuss the conflicts that might arise among the objectives of working capital management

(6 marks)

- b) Identify and explain the approaches that could be used to finance the company's working capital requirements (5 marks)
- c) The following information was extracted from the books of Kibabii Emporium Ltd as at 31 December 2020.

	2018	2019
Stock of raw materials	40,000	60,000
Work in progress	10,000	18,000
Finished goods in stock	50,000	70,000
Trade debtors	140,000	180,000
Annual sales	2,000,000	2,200,000
Cost of production	1,000,000	1,050,000
Annual cost of sales	1,200,000	1,250,000
Trade creditors	110,000	100,000
Annual purchase of raw materials	700,000	780,000

**Required:**

- i) The working capital cycle in days of Kibabii Emporium Ltd (6 marks)

- ii) Explain ways in which Kibabii Emporium Ltd might reduce its working capital cycle (3 marks)

#### QUESTION FOUR

- a) Explain the factors that influence the company's dividend policy (5 marks)  
 b) Examine the arguments which have been advanced in favour of a stable dividend policy (4 marks)  
 c) Peter Abraham is considering investing in security X and security Y in equal proportions. The following forecasts have been provided:

State	Probability	Returns (%)	
		Security X	Security Y
Recession	0.30	12	6
Stable	0.40	15	7.5
Expansion	0.30	10	5

Required:

- i) Expected return for the portfolio (3 marks)  
 ii) Standard deviation for security X and Y (3 marks)  
 iii) Coefficient of variation for security X and Y (3 marks)  
 iv) Using a relevant measure, advise the Peter Abraham on the security worth investing

(2 marks)

#### QUESTION FIVE

- a) Indicate four uses of cost of capital to a business firm (4 marks)  
 b) The finance manager of Ufanisi Ltd has compiled the following information regarding the company's capital structure as at 31 December 2019:

	Item sh.
Ordinary share capital (par value sh.25)	800,000
8% preference share capital (par value sh.24)	600,000
10% Debentures	400,000
10% preference share capital	400,000
	<b>2,200,000</b>

Additional information:

i) The share prices as at 31 December 2019 were as follows:

	Market price per share (sh.)
Ordinary shares	30
8% preference shares	20
10% preference shares	25

Market value of the 10% debenture on 31 December 2019 was sh. 500,000

ii) The company has maintained payment of an ordinary dividend per share of sh. 3.80 over the past five years.

iii) The corporation tax rate is 30%

Required:

- |   |           |
|---|-----------|
| i) Cost of ordinary share capital           | (3 marks) |
| ii) Cost of 8% preference share capital     | (3 marks) |
| iii) Cost of 10% debentures                 | (4 marks) |
| iv) Market weighted average cost of capital | (6marks)  |