

MURANG'A UNIVERSITY COLLEGE (MRUC)

(A Constituent College of Jomo Kenyatta University of Agriculture & Technology)

MURANG'A UNIVERSITY COLLEGE DEPARTMENT OF COMMERCE

COURSE CODE: COURSE TITLE: FINANCE

MARKING SCHEME:

EXAM TIME: 2 HOURS, ANSWER QUESTION ONE AND ANY OTHER TWO QUESTIONS IN SECTION B.

SECTION A

QUESTION 1.

I) What are the characteristics of an efficient market?

II) How are financial trades made on an organized exchange?

III) How are financial trades made in an over the counter market? Discuss the role of a dealer in the OTC market.

List and explain the three financial factors that influence the value of a business.

QUESTION TWO:

i) Explain why accounting profits and cash flows are not the same thing.

II) Why would an analyst use the Modified Du Pont system to calculate ROE when ROE may be calculated more simply? Explain.

III) Why are trend analysis and industry comparison important to financial ratio analysis?

QUESTION THREE:

i) Explain the risk–return relationship.

II) What is the difference between business risk and financial risk?

III) What is compound interest? Compare compound interest to discounting.

Compound interest occurs when interest is earned on interest and on the original principal of an investment. Discounting is the inverse of compounding. Compound interest causes the value of a beginning amount to increase at an increasing rate. Discounting causes the present value of a future amount to decrease at an increasing rate.

QUESTION FOUR:

i) What is capital rationing? Should a firm practice capital rationing? Why?

ii) Compare and contrast the book value and liquidation value per share for common stock. Is one method more reliable? Explain.