



MURANGA UNIVERSITY COLLEGE

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

MAIN CAMPUS

SPECIAL UNIVERSITY EXAMINATIONS

2015/2016 ACADEMIC YEAR

SECOND YEAR FIRST SEMESTER EXAMINATIONS

**FOR THE DEGREE
OF
BACHELOR OF COMMERCE**

COURSE CODE: HBC2202

**COURSE TITLE: INTRODUCTION TO FINANCIAL
MANAGEMENT**

DATE: TIME: 2 HOURS

INSTRUCTIONS TO CANDIDATES

Question ONE (1) is Compulsory
Answer ANY OTHER TWO (2) questions

MRUC observes ZERO tolerance to examination irregularities

This Paper Consists of 2 Printed Pages. Please Turn Over. ►

QUESTION ONE (30mks)

- (a) In a company an agency problem may exist between management and shareholders on one hand and the debt holders on the other because management and shareholders, who own and control the company have incentives to enter into transactions that may transfer wealth from debt holders to shareholders, hence the need for agreement by debt holders in lending contracts. Explain any four actions or transactions by management and shareholders that could be harmful to the interests of debt holders. (8mks).
- (b) ABC is contemplating purchasing a 3 year bond worth 40,000 carrying a nominal coupon rate of interest of 10%. ABC required rate of return is 6%. What should he be willing to pay now to purchase the bond if it matures at par? (5mks).
- (c) Explain any four disadvantages of the Net Present Value method of analyzing investments. (8mks).
- (d) Discuss the reasons why it may be difficult for small companies to raise debt finance in Kenya. (10mks).

QUESTION TWO (20mks).

- (a) Explain any five functions of the Nairobi securities exchange. (10mks).
- (b) Highlight any five factors that determine the working capital needs of a firm. (10mks).

QUESTION THREE (20mks)

- (a) Explain five factors that affect capital structure of a firm. (10mks).
- (b) Highlight the advantages of using ordinary share capital in financing. (10mks).

QUESTION FOUR (20mks).

- (a) The following is the capital structure of ABC Ltd as at 31/12/2014

	Sh. (millions)
Ordinary Share Capital Sh. 10 par value	400
Retained earnings	200
10% preference share capital sh. 20 par value	100
12% debenture sh. 100 par value	200
Total	900

Additional information

- (i) Corporate tax rate is 30%.
- (ii) Preference shares were issued 10 years ago and still selling at par value.
- (iii) The debenture has a 10 year maturity period. It is currently at sh. 90 in the market.
- (iv) Currently the firm has been paying dividend per share of sh. 5. The Dividend per share is expected to grow at 5% p.a. in future. The current market value per share is sh. 40. Determine the Weighted Average Cost of Capital (WACC). (10mks).
- (b) Explain any five functions of commercial banks. (10mks)