

MURANG'A UNIVERSITY COLLEGE (MRUC)
(A Constituent College of Jomo Kenyatta university of Agriculture & Technology)

SCHOOL OF BUSINESS AND ECONOMICS

DEPARTMENT OF COMMERCE

SPECIAL/SUPPLEMENTARY EXAMS

HBF 2302; ADVANCED FINANCIAL MANAGEMENT

YEAR 3, SEMESTER I, (BCom,)

2015/2016 ACADEMIC YEAR

DATE:

TIME: 3 HOURS

INSTRUCTIONS

Answer Question *ONE* and any *OTHER TWO* Questions.

COMPULSORY QUESTION (30 MARKS)

QUESTION ONE

- (a) Discuss the methods that can be used by a company to resolve agency conflicts between managers and shareholders (7 Marks)
- (b) Differentiate between;
- i) External and internal capital rating (2 Marks)
 - ii) Divisible and indivisible projects (2 Marks)
- (c) ABC LTD has the following proposed independent projects for the year ending December 31/2013

Project	Net Investment	Present value of future
	Outlay	Net cash flow
	sh '000'	sh '000'
A	500	1000
B	1,000	2,500
C	400	300
D	300	400

E

200

300

Required

- i) Assuming that there is no capital rationing indicate which project should be selected (3 Marks)
 - ii) Total net present value (NPV) of the selected projects (3 Marks)
 - iii) Assuming a single period internal capital constraints of sh. 1,700,000 is imposed indicate which projects should be selected based on NPV and profitability index(PI) respectively (4 Marks)
 - iv) Which of the two techniques is to be preferred. Justify your choice (2 Marks)
- (d) Outline the role of a finance manager in contemporary setup (7 Marks)

(TOTAL:30 MARKS)

QUESTION TWO

- (a) KK Ltd and PK Ltd are in the same business risk class each with operating profits of sh. 4million. However, they differ in their capital structure since PK Ltd has 8% sh10 million debt. The corporate tax rate is 30% and the cost of equity of KK Ltd is 14%

Required

- i. Compute the market value of each firm (4 Marks)
 - ii. Compute the market value of equity of PK Ltd (4 Marks)
 - iii. Compute the cost of equity of PK Ltd (5Marks)
- (b) Discuss the pecking order theory of capital structure by Masilluf (7 Marks)

(TOTAL: 20 MARKS)

QUESTION THREE

Kilimo Ltd is a newly incorporated firm which wants to raise shs.10million to finance an acquisition of machinery. Three financing plans have been suggested earnings before interest and tax (EBIT) is sh 1,500,000 p.a

1. Issue 1,000,000 ordinary shares at sh10mps
2. Issue 500,000 ordinary shares at sh10mps and a 10% sh 5 million debenture

3. Issue 300,000 ordinary shares at sh10 mps and a 10 % shs 7 million debenture

Required

- a. Dividend paid and Dps (4 Marks)
- b. The cost of equity (3 Marks)
- c. The cost of debt (3 Marks)
- d. The Mps (3 Marks)
- e. WACC (4Marks)
- f. Total market value of the firm (3 Marks)

(TOTAL:20 MARKS)

QUESTION FOUR

- (a) Discuss the effect of the following concepts on the firms dividend policy
 - i) Clientele effect (4 Marks)
 - ii) A bird in the hand (4 Marks)
 - iii) “Home-made” dividend (3 Marks)
- (b) Bright ltd undertook project x with the following cash flow over its useful life of 3 years.

The cost of capital for the project have been shown below

Year	cash flow	Abandonment value
	Sh ‘000’	sh’000’
0	(9,600)	9600
1	4000	6000
2	3750	3800
3	3500	0

Required

Advice the management of Bright ltd when the abandon project ‘X’

(9 Marks)

(TOTAL:20 MARKS)

