



MURANGA UNIVERSITY COLLEGE

(A Constituent college of JKUAT)

MAIN CAMPUS

ORDINARY UNIVERSITY EXAMINATION

2014/2015 ACADEMIC YEAR

SECOND YEAR SECOND SEMESTER EXAMINATIONS

FOR THE DEGREE OF

BACHELOR OF COMMERCE

COURSE CODE: HBF 2306

COURSE TITLE: PROJECT APPRAISAL

DATE: 27th April, 2015

TIME: 2.00-4.00p.m

INSTRUCTIONS

Question one is compulsory

Answer any other two questions

QUESTION ONE

a) Explain four conditions when conflicting ranking would be given by the internal rate of return and net present value for two or more projects in appraising projects (8marks)

b) A company is considering two mutually exclusive projects which have a life of five years. The following are the cash flows of the two projects

YEAR	0	1	2	3	4	5
CASHFLOW FOR A	-20,000	4,200	4,800	7,000	8,000	2,000
CASHFLOW FOR B	-15,000	4,000	4,500	4,000	5,000	1,000

Required:

Calculate the net present value of the incremental cashflow using an interest rate 12% (7marks)

c) Midwere company is considering investing sh 300,000 in a new project . The project’s net cash flows have been estimated as follows

YEAR1 CASHFLOWS	PROBABILITY	YEAR2 CASHFLOWS	PROBABILITY
250,000	0.7	200,000	0.4
		300,000	0.6
300,000	0.3	400,000	0.7
		500,000	0.3

Calculate the expected net present value if the risk free rate is 10% (11marks)

d) Distinguish between “Build-own-operate- transfer” and “Build- lease-transfer” structures of project financing arrangement (4marks)

QUESTION TWO

Dassel Company had the following capital structure on 31 December 2014

200,000 ordinary shares 2,000,000

10% preference shares	500,000
8% debentures	1,500,000

It is expected that the company will pay next year dividends of sh 2 per share which will grow at 8%.
The corporation tax rate is 30%

- a) Calculate a weighted average cost of capital (5marks)
- b) Calculate the new weighted average cost of capital if the company raises additional sh 1,000,000 by issuing a 14% debentures (9marks)
- c) Explain three methods a firm can use to finance its international investments (6marks)

QUESTION THREE

Byers Company has a cost of capital of 10% and has a limit of sh1,500,000 available for investment in the current period. The following indivisible projects are being considered

Project	Investment	Net present value
A	525,000	262,500
B	600,000	337,500
C	975,000	570,000
D	720,000	472,500
E	345,000	135,000

Surplus funds can be invested to produce 12% in perpetuity.

Required:

Determine the optimal investment plan (20marks)

QUESTION FOUR

- a) Sildre ltd is considering the lease of an equipment which has a purchase price of sh 612,500. The equipment has an estimated economic life of 5years. Depreciation is 25% on written down values. The lease rentals per year are sh 210,000. The corporation tax rate is 50%. The before tax rate is 12%

Required:

Using NAL analysis, advise management on whether to lease the equipment. (14marks)

- b) Explain any three components of a cashflow (6marks)

