



MURANGA UNIVERSITY COLLEGE

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

MAINCAMPUS

ORDINARY UNIVERSITY EXAMINATIONS

2015/2016 ACADEMIC YEAR

THIRD YEAR SECOND SEMESTER EXAMINATIONS

FOR THE DEGREE OF

BACHELOR OF COMMERCE

COURSE CODE: HBF 2306

COURSE TITLE: PROJECT APPRAISAL

DATE: 16TH DECEMBER, 2015

TIME: 2 HOURS

INSTRUCTIONS TO CANDIDATES

Question ONE (1) is compulsory
Answer any other TWO(2)) questions

MRUC observes Zero tolerance to examinations irregularities

This paper consists of 2 printed pages. Please turn over



QUESTION ONE

- a) Nidwosre 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	YEAR2 CASHFLOWS	PROBABILITY
250,000	0.7	200,000	0.4	180,000	0.6
		300,000	0.6	200,000	0.4
				300,000	0.8
				320,000	0.2
2300,000	0.3	400,000	0.7	380,000	0.7
		500,000	0.3	350,000	0.3
				400,000	0.5
				600,000	0.5

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

- b) Distinguish between “Build-own-operate- transfer” and “Build- lease-transfer” structures of project financing arrangement (4marks)
- c) Solder 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 30%. The before tax interest rate is 12%

Required:

Using NAL analysis, advise management on whether to lease the equipment. (15marks)

QUESTION TWO

Darters 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
V	525,000	262,500
W	600,000	337,500
X	975,000	570,000
Y	720,000	472,500
Z	345,000	135,000

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

Required:

Determine the optimal investment plan (14marks)

a) Explain the main components of a cash flow (6marks)

QUESTION THREE

Cassel Company had the following capital structure on 31 December 2013

200,000 ordinary shares	4,000,000
10% preference shares	500,000
8% debentures	2,500,000

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 14% debentures (9marks)

c) Explain three methods a firm can use to finance its international investments (6marks)

QUESTION FOUR

- 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 M	-25,000	4,200	4,800	7,000	8,000	2,000
CASHFLOW FOR N	-10,000	3,000	3,500	2,000	5,000	1,800

Required:

Calculate the net present value of the incremental cash flow using an interest rate 8% (6marks)

Explain the main differences between cash flow and accounting profits (6marks)

