MAASAI MARA UNIVERSITY

REGULAR UNIVERSITY EXAMINATIONS

2018/2019 ACADEMIC YEAR

SECOND YEAR FIRST SEMESTER

SCHOOL OF BUSINESS AND ECONOMICS

BACHELOR OF BUSINESS MANAGEMENT

COURSE CODE: BBM 206

COURSE TITLE: PRINCIPLES OF FINANCE

DATE: …………………………………………… **TIME: ……………………………**

INSTRUCTIONS TO CANDIDATES

Answer question 1 and any other TWO questions.

QUESTION 1

a) Describe the determinants of working capital needs **(5mks)**

b) Explain four sources of short term capital **(8mks)**

c) The Dallas Development Corporation is considering the purchase of an apartment project for $100,000. They estimate that they will receive $15,000 at the end of each year for the next 10 years. At the end of the 10th year, the apartment project will be worth nothing. If Dallas purchases the project, what will be its internal rate of return? If the company insists on a 9 percent return compounded annually on its investment, is this a good investment? **(3mks)**

d) Explain the functions of the central bank of Kenya **(9mks)**

QUESTION 2

A company is considering two mutually exclusive projects requiring an initial cash outlay of Ksh 10,000 each and with a useful life of 5 years. The company required rate of return is 10% and the appropriate corporate tax rate is 50%. The projects will be depreciated on a straight line basis. The before depreciation and taxes cashflows expected to be generated by the projects are as follows:

YEAR	1	2	3	4	5
Project A	Ksh 4,000	4,000	4,000	4,000	4,000
Project B	Ksh 6,000	3,000	2,000	5,000	5,000

Required:
Calculate for each project:

i) The net present value **(6mks)**

ii) The internal rate of return (**9mks)**

Which project should be accepted? Why?

QUESTION 3

a) Describe Modigliani and Miller Hypothesis II on capital structure **(10mks)**

b) Explain the key feature of a corporation as a form of business ownership (**5mks)**

QUESTION 4

a) Explain the factors that companies consider in deciding on the dividend payout policy**.** **(10mks)**

b) Describe five methods of issuance of shares (**5mks)**

QUESTION 5

a) Assume that the finance manager of ABC Ltd expects to generate sales of £500 000 in the current financial year. Analysis of the firms operating cost structure reveals that variable operating cost is 40% of sales and fixed operating cost at £250 000. The manager wishes to explore the effect of changes in sales and has developed 2 scenarios.

Required

Sales revenue is 10% less than expected

Sales revenue is 10% greater than expected

Compute the degree of combined (total) leverage (gearing) (**10mks)**

(b) Differentiate between open-ended and closed ended investment companies **(5mks)**

……………………………………………………………END…………………………………………………