



# **MAASAI MARA UNIVERSITY**

**REGULAR UNIVERSITY EXAMINATIONS  
2018/2019 ACADEMIC YEAR  
FIRST YEAR SECOND SEMESTER**

**SCHOOL OF BUSINESS AND ECONOMICS  
MASTERS IN BUSINESS ADMINISTRATION**

**COURSE CODE: MBA 8101**

**COURSE TITLE: FINANCIAL MANAGEMENT**

**DATE: 7<sup>TH</sup> MAY, 2019**

**TIME: 1430 – 1730 HRS**

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**INSTRUCTIONS TO CANDIDATES**

- Question **ONE** is compulsory
- Answer any other **THREE Questions**

## QUESTION ONE

- (a) Define agency relationship from the context of a public limited company and briefly explain how this arises. **(5 marks)**
- (b) Highlight the various measures that would minimize agency problems between the owners and the management. **(10 marks)**
- (c) In a company, an agency problem may exist between management and shareholders on one hand and the debt holders (creditors and lenders) on the other because management and shareholders, who own and control the company, have the incentive to enter into transactions that may transfer wealth from debt holders to shareholders. Hence the need for agreements by debt holders in lending contracts. State and explain any four actions or transactions by management and shareholders that could be harmful to the interests of debt holders (sources of conflict). **(10 marks)**

## QUESTION TWO

Although profit maximization has long been considered as the main goal of a firm, shareholder wealth maximization is gaining acceptance amongst most companies as the key goal of a firm.

Required:

- (i) Distinguish between the goals of profit maximization and shareholder wealth maximization. **(4 marks)**
- (ii) Explain three limitations of the goal of profit maximization. **(6 marks)**
- (iii) Describe four non-financial objectives that a company might pursue that have the effect of limiting the achievement of the financial objectives. **(5 marks)**

### QUESTION THREE

- (a) Briefly explain the importance of capital budgeting in a business organization. **(4 marks)**
- (c) Several methods exist for evaluating investment projects under capital budgeting.

Identify and explain three features of an ideal investment appraisal method.

**(6 marks)**

- (d) In evaluating investment decisions, cash flows are considered to be more relevant than profitability associated with the project. Explain why this is the case.

**(5 marks)**

### QUESTION FOUR

Pwani ltd is planning advertising campaigns in three different markets. The estimates of probability associated profits in each of the three markets are provided bellow;

	<u>Market1</u>		<u>Market2</u>		<u>Market3</u>	
	Profit	probability	profit	probability	profit	probability
Fair	10000	0.40	5000	0.20	16000	0.50
Normal	18000	0.50	8000	0.60	20000	0.30
Excellent	25000	0.10	12000	0.20	25000	0.20

Required;

- (i) Compute the expected value and standard deviation of profits resulting from advertising campaigns in each of the market areas. **(10 marks)**

- (ii) Rank the three markets according to riskiness using the coefficient of variations. **(5 marks)**

### QUESTION FIVE

A proposal to purchase a new lathe machine is to be subjected to these initial screening processes. The machine will cost Sh.2,200,000 and has an estimated useful life of five years at the end of which the disposal value will be zero. Sales revenue to be generated by the new machine is estimated as follows:

Year	Revenue (Sh.'000')
1	1,320
2	1,440
3	1,560
4	1,600
5	1,500

Additional operating costs are estimated to be Sh.700,000 per annum. Tax rates may be assumed to be 35% payable in the year in which revenue is received. For taxation purpose the machine is to be written off as a fixed annual rate of 20% on cost.

The financial accounting statements issued by the company in recent years shows that profits after tax have averaged 18% on total assets.

**Required:**

Present a report which will indicate to management whether or not the proposal to purchase the lathe machine meets each of the selection criteria. **(15 marks)**

**//END**