MAASAI MARA UNIVERSITY

REGULAR UNIVERSITY EXAMINATIONS
2023/2024 ACADEMIC YEAR
FOURTH YEAR FIRST SEMESTER

SCHOOL OF BUSINESS AND ECONOMICS

BACHELOR OF COMMERCE & BED (ARTS).

COURSE CODE: BCM 4113-1
COURSE TITLE: FINANCIAL MANAGEMENT

DATE: 14TH DECEMBER 2023 **TIME: 0830-1030HRS**

INSTRUCTIONS TO CANDIDATES

Answer Question **ONE** and any other **THEE** Questions

*This paper consists of **4**printed pages. Please turn over.*

Question One

a) Discuss **three** drawbacks of profit maximization objective in financial management. **(3 Marks)**

b) Highlight **four** differences between financial structure and capital structure. **(4 Marks)**

c) A Company expects a net income of sh. 1,000,000. It has sh. 2,500,000, 8% debentures. The equality capitalization rate of the company is 12%. Assume the tax rate of 30%.

Required:

i) The value of the firm and overall capitalization rate according to the net income approach. **(4 Marks)**

ii) If the debenture debts are increased to sh. 4,000,000. What shall be the value of the firm and the overall capitalization rate? **(5 Marks)**

d) Akim Ltd. issues sh. 1,000,000, 9% debentures at par. The tax rate applicable to the company is 35%. Compute the cost of debt capital. **(4 Marks)**

Question Two

a) Explain the following terminologies as used in Financial Management:

i) Break Even point **(2 mark)**

ii) Required rate of return **(1 mark)**

iii) Economic value added **(1 mark)**

b) There are two projects' Uko and Wapi, each project involves an investment of Ksh. 500,000. The expected cash inflows and the certainty co-efficient are as under:

Year	**Project Uko**		**Project Wapi**	
	Cash inflows	**Certainty Coefficient**	**Cash inflows**	**Certainty coefficient**
1	350,000	0.7	250,000	0.9
2	300,000	0.8	350,000	0.8
3	200,000	0.9	200,000	0.7

If the Risk-free cutoff rate is 12%, advice which of the two projects should be preferred. **(6 marks)**

Question Three

a) Heavy Weight Ltd. Company needs sh. 4,000,000 for the installation of a new factory. The new factory expects to yield annual earnings before interest and tax (EBIT) of sh. 600,000. In choosing a financial plan Heavy Weight Ltd. Company, has an objective of maximizing earnings per share (EPS). The company proposes to issuing ordinary shares and raising debt of sh. 400,000, sh. 1,000,000 or sh. 1,500,000. The current market price per share is sh. 250 and is expected to drop to sh. 200 if the funds are borrowed in excess of sh. 1,200,000. Funds can be raised at the following rates:

   i. Up-to sh. 400,000 at 8%
   ii. Over sh. 400,000 to sh. 1,500,000 at 10%
   iii. Over sh. 1,500,000 at 15%

Required:
Assuming a tax rate of 35% advice the company. **(10 Marks)**

Question Four

a) Critically evaluate objectives of financial management. **(5 marks)**

b) Fairmount Ltd. has a capital of sh. 1,500,000 in equity shares of Ksh. 100 each. The shares are currently quoted at par. The company proposes to declare a dividend of Ksh.10 per share at the end of the current financial year. The capitalization rate for the risk class to which the company belongs is 13%. What will be the market price of the share at the end of the year, if:

(i) Dividend is not declared. **(3 marks)**

(ii) Dividend is declared. **(2 marks)**

Question Five

a) From the following information, ascertain which project should be selected on the basis of standard deviation. **(6 marks)**

Project Ako		**Project Wapi**	
Cash inflow	**Probability**	**Cash inflow**	**Probability**
Ksh.		Ksh	
3,200	0.4	32,000	0.3
5,500	0.3	5,500	0.4
7,400	0.5	7,400	0.2
8,900	0.2	8,900	0.3

b) Discuss two importance of capital rationing in capital budgeting. **(4 marks)**

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