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**GARISSA UNIVERSITY**

**UNIVERSITY EXAMINATION 2017/2018 ACADEMIC YEAR FOUR**

**THIRD SEMESTER EXAMINATION**

**SCHOOL OF BUSINESS AND ECONOMICS**

**FOR THE DEGREE OF BACHELOR OF BUSINESS MANAGEMENT**

**COURSE CODE: BBM 410**

**COURSE TITLE: FINANCIAL MANAGEMENT**

**EXAMINATION DURATION: 3 HOURS**

**DATE: 10/08/18 TIME: 09.00-12.00 PM**

**INSTRUCTION TO CANDIDATES**

* **The examination has FIVE (5) questions**
* **Question ONE (1) is COMPULSORY**
* **Choose any other THREE (3) questions from the remaining FOUR (4) questions**
* **Use sketch diagrams to illustrate your answer whenever necessary**
* **Do not carry mobile phones or any other written materials in examination room**
* **Do not write on this paper**

**This paper consists of THREE (3) printed pages *please turn over***

**QUESTION ONE (COMPULSORY)**

1. Briefly explain the role of the following
   * 1. Retirement benefit authority **[2 marks]**
     2. Central bank of Kenya **[2 marks]**
     3. Nairobi stock exchange **[2 marks]**
     4. Capital market authority **[2 marks]**
     5. Commercial banks **[2 marks]**
2. Briefly discuss what is portfolio theory and risk diversification in regards to financial management **[5 marks]**
3. Investors have an expected rate of return of 8% from ordinary shares in Pumwani Ltd. Pumwani Ltd have a beta factor of 1.2. The expected returns to the market are 7%. What will be the expected rate of return from ordinary shares in kwetu Ltd, which have a beta of 1.8? **[10 marks]**

**QUESTION TWO**

1. Hassan Noor wants to borrow loan of Shs 1,000,000 at equity bank Garissa branch which is being offered at interest rate of 15%. The loan is to be repaid at the end of each of the next 5 years.
   1. What will be his annual installment? **[5 marks]**
   2. Prepare loan amortization schedule **[10 marks]**

**QUESTION THREE**

1. What is the role of financial managers in organization (10 marks)
2. Diani resort is currently earning Kshs 100,000 and its shares is selling at a market price of Kshs 80. It has 10,000 shares outstanding and has no debt. earnings are expected to remain stable and it has a payout ratio of 100%. What is the cost of equity? (5 marks)

**QUESTION FOUR**

* 1. Explain agency conflict in financial management and highlight the major agency relationships that exist in financial management framework. **[5 marks]**

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
|  |  |  |  |  |
| b) |  |  | Returns % |  |
| State of economy | Probability | | X | Y |
| A | 0.1 |  | -8 | 14 |
| B | 0.2 |  | 10 | -4 |
| C | 0.4 |  | 8 | 6 |
| D | 0.2 |  | 5 | 15 |
| E | 0.1 |  | -4 | 20 |

* 1. Iftin limited company invests 50% of its wealth in X and 50% in Y, calculate the expected return of the portfolio. **[10 marks]**

**QUESTION FIVE**

1. Bamato traders is considering two mutually exclusive projects requiring an initial cash outlay of Sh 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 cash flows expected to be generated by the projects are as follows.

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
| ***YEAR*** | ***1*** | ***2*** | ***3*** | ***4*** | ***5*** |
| Project A | Shs 4,000 | 4,000 | 4,000 | 4,000 | 4,000 |
| Project B | Shs 6,000 | 3,000 | 2,000 | 5,000 | 5,000 |

***Required:***

Calculate for each project

1. The payback period **[3 marks]**
2. The average rate of return **[3 marks]**
3. The net present value **[3 marks]**
4. Profitability index **[2 marks]**
5. The internal rate of return **[3 marks]**

Which project should be accepted? Why? **[1 mark]**

**QUESTION SIX**

1. Njeri was given Kshs 100,000 by her husband on her 25th birthday. She deposited this amount to a bank at 10% value of interest for one year. What will be the future value of this amount on her next birthday? Illustrate your answer using compound value **[7 marks]**
2. Recently controversy has been arising in shareholders meeting on issue regarding payment and non-payment of dividends. In others the shareholders hold the view that the recommended dividend is too high. describe six factors to be considered by the directors in the design of the company dividend policy **[8 marks]**