PAN AFRICA CHRISTIAN UNIVERSITY

BACHELORS OF COMMERCE

END OF TERM EXAMINATION

DEPARTMENT: BUSINESS

COURSE CODE: BUS4213|BCM302

COURSE TITLE: FINANCIAL MANAGEMENT

EXAM DATE: WEDNESDAY

TIME: 5.30PM – 8.30PM

INSTRUCTIONS

- This examination script consists of **six (6)** questions.
- Answer question ONE and ANY other three Questions.
- Show all your workings
- Read all questions carefully before attempting.

Write your **student number** on the answer booklet provided.

QUESTION ONE

a) Explain why investing decisions are based on cash flows more than on profits in capital budgeting (4marks)

b) Capital structure does not affect the shareholder's wealth. Discuss this statement citing a relevant capital structure theory (6marks)

QUESTION TWO

a) Explain the term agency problem (2marks)

b) Describe any two ways in which agency problem is costly (4marks)

c) Using relevant examples, explain how agency problem in b) above can be minimized (4marks)

QUESTION THREE

RQ Co. plans to invest in a new machine whose estimated cash outlay is sh1.2M. During the first year, its expected revenue is sh200,000 while its operating cost is sh120,000. The revenue is projected to increase by 9% every year for the remaining years while its operating costs might increase by 4% every year for the remaining years. The accounts receivables and payables are estimated at sh65,000 and sh330,000 respectively. The end of the three years, the machine will be scrapped at sh100,000. The tax rate is 33%.

Required:

a) Estimate the net operating cash flows for each year (6marks)

b) Evaluate the viability of the project on the basis of Net Present Value if the required rate of return is 10% (4marks)

QUESTION FOUR

a) Explain the importance of the time value of money concept in finance (4marks)

b) Using relevant examples, explain any three factors a finance officer should consider while making working capital decisions (6marks)

QUESTION FIVE

Danli Ltd has a net operating income of sh1,000,000, the value of equity of Sh2,200,000 and zero debt. Cheko Co. has a net operating income of sh1,000,000, the value of equity of Sh1,300,000 and the value of 19% debt of sh2,800,000. The corporate tax is 33%.

Using the assumptions of traditional approach, determine

a) Value of each firm (2mark)
b) Cost of equity of each firm (3marks)
c) Weighted average cost of capital of each firm (5marks)

QUESTION SIX

c) Dividends decisions does not affect the wealth of the firm. Discuss this statement citing a relevant dividend theory (4marks)
d) Sinda Co. has the following forecast figures for its first year of trading:

    Sales Sh1,800,000

    Purchases sh1,500,000

    Average receivables sh 148,000

    Average inventory sh 248,000

    Average payables sh 115,000

    Average overdraft sh 250,000

    Assume there are 365 days in the year.

    REQUIRED:
    Calculate and comment on Sinda Co's cash operating cycle (6marks)