The Co-operative University of Kenya

SUPPLEMENTARY EXAMINATION AUGUST- 2019

EXAMINATION FOR THE DIPLOMA IN ACCOUNTING & FINANCE

UNIT CODE: DMAF 1101

UNIT TITLE: FUNDAMENTAL OF FINANCE

DATE: 30TH AUGUST, 2019 **TIME: 11:30 AM – 1:30 PM**

INSTRUCTIONS:

- Answer question **ONE (compulsory)** and any other **TWO** questions

QUESTION ONE

a) Explain the following terms as used in finance ;
   Financial intermediate
   Risk-return trade off
   Stakeholder management. (3mks)

b) Briefly explain the various valuation techniques and sub-disciplines of Finance (6mks)

c) Briefly explain three agency relationships in an organization and four ways of resolving the agency relationship in an organization (6mks)

d) State three rules of a time travel (3mks)

e) You have a relative in Nairobi and He offers you a choice of Ksh 80000 in 60years or ksh1000 today. If the money is discounted at 11% which option will you go for? (4mks)

f) A company expects to generate Cash flows as follows;

Year One, sh100, 000

Year Two, sh150, 000

Year Three, sh200, 000

Year Four, sh250, 000

The applicable discount rate is 12%.Compute the Present Value of the cash flows (8mks)

g) Determine the future value of a ksh.1000, 000 investment made at the end of every year for 5years, assume the required rate of return is 12% compounded annually (3mks)

QUESTION TWO

a) Discuss various stages in the capital budgeting process (10mks)

b)The following is a mixed stream of cash flows occurring at the end of the year. If the firm has been offered the opportunity to receive the amounts and if its required rate of return is 10%.What is the most it should pay for this opportunities in five years' time? (10mks)

YEAR	CF
1	400,000
2	800,000
3	500,000
4	400,000
5	300,000

QUESTION THREE

a) Matumaini Corporation has the following capital structure 30% debt, 10% preferred stock and 60% equity. The Corporation wishes to maintain these proportions as it raises new funds. It's before tax cost of debt is 8%, its preferred stock is 10% and its cost of equity is 15%.If the company's marginal tax rate is 40%, what is the weighted average cost of capital (10mks)

b) Mwende Mutua, a financial analyst is estimating the cost of capital for the XYZ Corporation. In the process of this estimation Mwende has estimated the before tax costs of capital for the corporations debt and equity as 4% and 6% respectively. What are the after-tax costs of debt and equity if XYZs marginal tax rate is? (10mks)

i. 30%
ii. 48%

QUESTION FOUR

a) Makori is a financial analyst with Bidii Firm.Peter is in the process of estimating the cost of capital of the firm. The following information is provided;

Bidii Firm

Market value of debt	ksh50M
Market value of equity	ksh60M

Primary competitors and their capital structure (millions)

Competitor	market value of debt	market value of equity
A	Ksh25	Ksh50
B	Ksh101	Ksh190
C	Ksh40	ksh60

What are the Firms proportion of debt and equity that Makori would use in estimating these proportions using the Firms? (10mks)

i. Current capital structure
ii. Competitors capital structure

b) Highlight the various functions of the following financial systems

i) Capital markets authority (5mks)

ii) National Securities Exchange (5mks)

QUESTION FIVE

a) In their operations banks are primarily exposed to or may potentially be exposed to the following risks. Discuss the risks associated by banks (5mks)

b) Assume that the risk free rate of return is 8%,the market expected rate of return is 12%.The standard deviation of the market return is 2%while the covariance of return for security A and the market is 2%.What is the required rate of return on security A (4mks)

c) Summarize four features of Islamic insurance mortgage (takaful) (4mks)

d) Identify and explain any FIVE short term sources of finance for an organization of your own choice (5mks)

e) Share is the unit ownership of a company. Discuss the various factors to consider when buying shares (2mks)

f) An investor with kshs.20,000 has approached you to advice on which investment to undertake among the three;

Year	A	B	C
1	14000	5000	5000
2	6000	11000	5000
3	4000	9000	16000

If the discount rate is 10%, determine the viable project to invest using the net present value method (10mks)