



# THE CO-OPERATIVE UNIVERSITY OF KENYA

SPECIAL / SUPPLEMENTARY EXAMINATION OCTOBER -2022

EXAMINATION FOR THE DEGREE OF BACHELOR OF SCIENCE IN FINANCE,  
COMMERCE, AND CO-OPERATIVE BUSINESS

UNIT CODE: BFIN 4203/BCFF 2405

UNIT TITLE: CONTEMPORARY ISSUES IN FINANCIAL MANAGEMENT

DATE: TUESDAY 25<sup>TH</sup> OCTOBER, 2022

TIME: 9:00 AM – 11:00 AM

## INSTRUCTIONS:

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

### QUESTION ONE

#### QUESTION ONE

- (a) Explain the meaning of Risk Diversification (2 Marks)
- (b) A share unit acquired six months ago costs KES. 100 and is sold today for KES. 106. Over that duration, it has received a dividend of KES. 3. Calculate the annual rate of return. (3 Marks)
- (c) Explain the relationship between risk and time as relates to investments (2 Marks)
- (d) Explain the meaning of beta in investments. (2 Marks)
- (e) Describe the concept of the Capital Market Line (2 Marks)
- (f) Distinct between Offeror and Offeree in Mergers & Acquisition (2 Marks)
- (g) State **THREE** methods used in valuation related to mergers and acquisitions (3 Marks)
- (h) Why is Book value per share not a useful basis for valuation in most mergers (2 Marks)
- (i) State **THREE** types of Foreign Exchange Risk (3 Marks)
- (j) State **FIVE** defenses against Mergers & Acquisitions (5 Marks)
- (k) State **FOUR** types of derivatives (4 Marks)

### QUESTION TWO

- (a) What element of the required rate of return compensates for risk in an investment (2 Marks)
- (b) The financial manager of CUK Technologies wishes to determine the expected rate of return from a proposed investment projects. The expected returns from the project are related to future performance of the economy over the period as follows:

Economic scenario	Probability of occurrence (p)	Rate of return (r)
Strong	0.25	14%
Moderate	0.50	16%
Low	0.25	18%

Calculate the E(r) (3 Marks)

- (c) Johnny Bravo is considering a number of investment opportunities. Assuming that the risk-free rate is currently 5% and the expected return from the market is 12%, the beta for the investments are as below;

Security	Beta

A	0.9
B	1.3
C	0.6
D	1.5

- Use CAPM to calculate the rate each investment is expect to earn. (5 Marks)
- (d) Explain **TWO** categorizations of Mergers (4 Marks)
- (e) State **SIX** reasons that have been highlighted as a reason for failed Mergers (6 Marks)

### QUESTION THREE

- (a) Explain the meaning of recapitalization and state **THREE** ways it is done (5 Marks)
- (b) Describe **FIVE** kinds of Strategic Alliance (5 Marks)
- (c) State **TWO** ways the ratio of exchange may have been considered for the merger of CBA and NIC Bank (2 Marks)
- (d) Company CBA is considering the acquisition by shares of Company NIC. The following information is also available.

	Company CBA	Company NIC
Present earnings	KES. 30,000,000	KES. 5,000,000
Shares	7,500,000	2,500,000
Earnings per share	KES. 4	KES. 2.00
Price/Earnings ratio	16	15
Price of shares	KES. 64	KES. 30

Company NIC has agreed to an offer of Shs 35 a share to be paid in Company CBA shares. Consider the effect of the acquisition to the earnings per share. (8 Marks)

### QUESTION FOUR

- (a) Distinct between Offeror and Offeree in Mergers & Acquisitions (2 Marks)
- (b) State the **THREE** pieces of legislation that offer legal provisions on takeovers and mergers in Kenya (3 Marks)
- (c) Explain the difference between futures contract and an option on futures contract (5 Marks)
- (d) APA Ltd. is considered acquiring Amaco Ltd. The following information relates to Amaco Ltd. for the next five years. The projected financial data are for the post-merger period. The corporate tax rate is 30% for both companies and the prevailing interest rate is 19%

	2016	2017	2018	2019	2020
Net sales	1,050	1,260	1,510	1,740	1,910
Cost of sales	735	882	1,057	1,218	1,337
Selling & admn. expenses	100	120	130	150	160
Interest expenses	40	50	70	90	110

Other information

1. After the fifth year the cash flows available to XYZ from ABC is expected to grow by 12% per annum in perpetuity.
2. ABC will retain Sh. 40,000 for internal expansion every year.

**Required**

- i Estimate the annual cashflows (5 Marks)
- ii Determine the maximum amount APA would be willing to acquire Amaco (5 Marks)

**QUESTION FIVE**

- (a) Define risk and explain THREE attitudes to risk (5 Marks)
- (b) Describe the Arbitrage Pricing Theory (5 Marks)
- (c) Describe FIVE different types of e-Commerce (5 Marks)
- (d) An investor had a portfolio made of Text Book Centre and Safaricom shares. The yield on a 3-month T-bill is 4%, and the yield on a 10-year T-bond is 6%.

	Text Book Centre (50%)	Safaricom (50%)
Expected return, r	15%	20%
Beta	80%	40%
Standard Deviation	5%	5%

**Required**

- i. Calculate Treynor's Measure of Portfolio (3 Marks)
- ii. Calculate the Portfolio Coefficient of Variation (2 Marks)