THE CATHOLIC UNIVERSITY OF EASTERN AFRICA

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MAIN EXAMINATION

JANUARY – APRIL 2014 TRIMESTER

FACULTY OF COMMERCE

MBA- PROGRAMME

CFI 520: FINANCIAL MANAGEMENT

Date: APRIL 2014	Duration: 3 Hours
INSTRUCTIONS: Answer ALL the Questions	

Q1. Kweya Uni has been particularly concerned with its liquidity position in recent months. The most recent Income Statement and Balance Sheet of the Uni are as follows:

Income Statement for the Year ended 31 May 2011

	Sh. Million	Sh. Million
Sales		452
Opening stock	125	
Purchases	341	
Closing stock	(143)	
Cost of sales		323
		129
Expenses		(132)
Loss		(3)

Balance Sheet (Position Statement) as at 31 May 2011

	Sh. Million	Sh. Million
Fixed assets		
Freehold premises at valuation		280
Fixtures and fittings (NBV)		25
Motor vehicles (NBV)		52

		357
Current assets		
Inventory	143	
debtors	163	
	306	
Less trade creditors	(145)	
Bank overdraft	(140)	
	21	(99)
Less: Long-term	(120)	258
Capital and reserves		
Ordinary share capital		100
Retained profit		158
		258

The debtors and creditors were maintained at a constant level throughout the year.

Required:

a) Explain why Kweya Uni is concerned with its liquidity position. (**7 marks**)

b) Explain the term "operating cash cycle" and state why this concept is important in the financial management of a business. (**5 marks**)

c) Calculate the operating cash cycle for Kweya Uni based on the information above (assume a 360 day year). (**8 marks**)

d) State what steps may be taken to improve the operating cash flow cycle of the Uni. (**5 marks**)

(**Total 25 marks**)

Q2. The following are financial details for JG, a private company Income Statement for the years ended 31 December.

	2008	2009	2010
	Sh 000	Sh. 000	Sh. 000
Profit after tax	300	359	435
Dividends	(150)	(155)	(163)
	150	204	272

Balance sheet as at 31 December

	2008	2009	2010
	Sh 000	Sh. 000	Sh. 000
Fixed assets	750	900	1120

Working capital	400	460	520
Loans	(100)	(106)	(114)
	1050	1254	1526
Share capital	100	100	100
Reserves	950	1154	1426
	1050	1254	1526

The required return on the company's equity is estimated to be 20%. The P/E Ratio of similar quoted companies is around 18X. The dividend yield of similar companies is 11%. The fixed assets are shown at cost which is approximately Sh. 200000 below market value. The loans are shown at market value.

Required:

Estimate the value of JG Ltd, using the following methods:

a) Dividend valuation model. (**8 marks**)
b) Dividend yield (**5 marks**)
c) P/E ratio (**7 marks**)
d) Asset value. (**5 marks**)

(NB: As a private company discount valuation by 30% as appropriate. Dividend is net of tax at 10%).

Q3. a) As a financial consultant you have been approached by a group of women entrepreneurs from your county who plan to operate bee keeping with a view to the production of honey for the local market. The details of the project are as follows:

Factory cost Shs. 300,000
Sales of bottles of honey 15000 for ten years
Each bottle will cost Ksh 10 and will retail at Shs. 50.
Annual fixed costs Kshs. 500,000
Cost of capital 13%

Required:

i) Calculate the net present value of the project and decide whether it is viable. (**10 marks**)

ii) Indicate how sensitive your decision will be to changes in the volume of:

a. Bottles sold (**3 marks**)

b. The retail price of bottle (**3 marks**)

c. The annual fixed cost (**3 marks**)

b) Assume that the group of women have to borrow initial capital from a local bank and list out the key attributes the bank would like before the approval of the credit facility. (**NB: in bullets**) (**9 marks**)

Q4. a) Discuss the theoretical concepts which underlie a company's weighted average cost of capital (WACC) indicating the purpose of the WACC. (**10 marks**)

b) Extract form the balance sheet of ABC Ltd.

	Shs.
Issued share capital	
Ordinary share of Shs 25 each	25,000,000
Retained earnings	35,000,000
Undated 15% unsecured loan stock	25,000,000
Undated 7% preference shares of Shs. 100 each	15,000,000
	100,000,000

The ordinary shares are currently quoted at Shs. 125 each, the loan stock at Shs. 85 per Shs. 100 and the preference shares at Shs. 65 each. The cost of equity shares is 16% and the company is a tax payer at 33%.

Required:

Calculate weighted average cost of capital. (NB: Use market values). (**15 marks**)

(**NB: Ignore Retained Earnings**)

END