AFRICA UNIVERSITY®
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COLLEGE OF BUSINESS PEACE LEADERSHIP GOVERNANCE (CBPLG)

MAC403: FINANCIAL MANAGEMENT I

END OF SECOND SEMESTER FINAL EXAMINATIONS

NOVEMBER 2019

LECTURER: MR. GABRIEL MUZAH

DURATION: 3 HRS

INSTRUCTIONS

The Paper contains four (4) Questions

Answer **all four (4) questions**

All questions carry equal marks (25).

DO NOT repeat material.

Write legibly. Write your answer clearly. Use numbered headings or subheadings to show which part of your answer refers to which question. Example: Question 2 (a)

Question One

A company has the following long-term capital outstanding as on 31 March 2018:

a. 10% debentures with a face value of $500 000. The current market price of a debenture is $950.

b. Preference shares with a face value of $400 000. The annual dividend is $6,00 per share. The preference shares are currently selling at $60,00 per share.

c. Sixty thousand ordinary shares of $10,00 par value. The share is currently selling at $50,00 per share. The dividends per share are expected to grow at a rate of 9%

Required; Assuming a tax rate of 35%, compute the firm's weighted average cost of capital (WACC)

(Total 25 marks)

Question Two

Property Investments Group Ltd is considering an investment in a small industrial property which is currently offering a gross rental of $120 000 per year. The asking price for the property is $1, 32 million. Operating costs such as maintenance, administration and rates are expected to amount to $36 000 per year. Rentals and costs are expected to increase at a rate of 4% per year for the next three years. The group intends to hold onto its property for three years when the group expects to sell the property for $1, 68 million. Tax is charged at a rate of 28% and the company will also pay Capital Gains Tax on any profit on disposal. The required rate of return is 9%.

You are required to:

a. Compute the Net Present Value from investing in this property. [10 marks]
b. Compute the Internal Rate of Return. [10 marks]

c. Explain why the NPV and the IRR capital budgeting techniques are preferred to other methods of project valuation. [5 marks]

(Total 25 Marks)

Question Three

This semester you were required to select and study a specific public company of choice which you eventually analysed. Can you write an initiation of coverage report for this company?

(Total 25 Marks)

Question Four

a. Briefly discuss factors, both shareholder and firm oriented, which could influence a firm's dividend policy. (10 marks)

b. Explain two (2) dividend policies a company can adopt? (5 marks)

c. A dictionary defines risk as "the chance of bad consequences" and uncertainty as "not to be depended on". Discuss these terms in the context of financial management. (5 marks)

d. Explain why an investment in a government security maybe considered being a riskless investment. (5 marks)

(Total 25 Marks)

End of Exam (Total 100 marks)

FORMULAES

$$NPV = CF_0 + \frac{CF_1}{(1+r)} + \frac{CF_2}{(1+r)^2} + \frac{CF_3}{(1+r)^3} + \frac{CF_4}{(1+r)^4} + \cdots$$

$$\text{PV of an annuity} = C \times \left[\frac{1}{r} - \frac{1}{r(1+r)^T} \right]$$

$$\text{PV of a perpetuity} = \frac{C}{r}$$

$$\text{PV of a growing perpetuity} = \frac{C}{r - g}$$

$$\text{Real risk free rate } (R_f) = \frac{(1 + \text{nominal risk-free rate})}{(1 + \text{inflation rate})} - 1$$

Nominal risk-free rate = (1 + risk-free rate) x (1 + rate of inflation) – 1

IRR (%) = A + [(B-A) * (a / (a+b))]

$$\text{A.R.R.} = \frac{\text{Average profits}}{\text{Average Investment}}$$

$$WACC = \left(\frac{Ve}{Ve+Vd+Vp}\right) k_e + \left(\frac{Vd}{Ve+Vd+Vp}\right) k_{d(1-T)} + \left(\frac{Vp}{Ve+Vd+Vp}\right) k_{pref}$$

$$Ke = \frac{Do(1+g)}{Po} + g$$

$$Ke = CAPM = Rf + \beta(Rm - Rf)$$

$$K_{pref} = \frac{d}{P_0}$$

$$Kd = \frac{i(1 - t)}{Po}$$

$$\text{Approximate Yield to Maturity} = \frac{I + (Fd - Vd)/\, n}{[(Fd + 2Vd)]/3}$$