MASENO UNIVERSITY

UNIVERSITY EXAMINATIONS 2016/2017

FOURTH YEAR FIRST SEMESTER EXAMINATIONS FOR THE DEGREE OF BACHELOR OF BUSINESS ADMINISTRATION WITH INFORMATION TECHNOLOGY

HOMA-BAY CAMPUS

ABA 406: MANAGEMENT OF FINANCIAL SERVICES

Date: 17th June, 2017 Time: 9.00 - 12.00 noon

INSTRUCTIONS:

- Answer question ONE and any other THREE questions.

QUESTION ONE

a) Royal Investments Ltd has made a project investment decision requiring the use of a piece of capital equipment costing Kshs, 280,000. The equipment has a five year life with no residual value and its operating costs are identical under either a lease or buy option. If the company purchases the equipment, straight line depreciation applies for tax purposes. The company is considering either buying the equipment or entering into a five year financial lease with annual lease payments of Kshs. 80,000. The first lease payments are made at the beginning of the year. The cost of debt is 12% and the company's tax rate is 30%

Required

Using Net Advantage of Leasing Method (NAL) advise the company on whether to lease or buy the equipment (15mks)

b) Differentiate a financial lease from operating lease (10mks)

QUESTION TWO

Airtel Company wants to acquire an equipment worth Kshs. 80,000 Kuber Finance Company offers a hire purchase financing to Airtel Company. The hire purchase installments will be paid annually for eight years and Kuber will calculate interest at a flat rate of 14%

Required:

i. Calculate the interest distribution over the eight years using the sum of years digit (SYD) approach (7mks)

ii. Calculate Kuber's Internal Rate of Return (IRR) for financing Airtel company (8mks)

QUESTION THREE

a) Discuss the role of Venture Capital in Economic Development (8mks)

b) Discuss elaborately the stages of venture capital financing process (7mks)

QUESTION FOUR

a) Explain the difference in assumptions in the Gordon's growth model and Solomon's model in the calculation of share price (2mks)

b) Kirengo Company Ltd is expected to announce a dividend per share of Shs. 10 next year. The future annual growth rate in dividends and hence capital gain is expected to be 4%. The company's existing assets generate in perpetuity a constant annual amount of earnings per share (EPs) of Shs. 0.37 and retains in perpetuity a constant annual proportion of 0.4 of EPs from existing assets and a constant annual rate of return of 15%. The company's discount rate is 12%

Required:

Calculate the share price using:

i. Gordon's' ground model (2mks)

ii. Solomon's model (3mks)

c) The government is proposing to sell a 10 year Kengen bonds of Kshs. 100,000 at 12.5% rate of interest per annum. The bond will be amortized equally over its life. Assuming a hurdle rate of 18%, calculate the bonds present value for an investor willing to buy the bond (8mks)

QUESTION FIVE

~~Safaricom Company Ltd is contemplating a complete share acquisition of Orange~~ Company Ltd.

Safaricom is offering two of its shares for every 3 shares of Orange Ltd. The data relating to the two companies are shown below:

	Safaricom Ltd	Orange Ltd
	Kshs	**Kshs**
Earnings	5,190,360.00	2,340,000.00
Earnings Per Share	14.80	29.25
Market Price Per Share	322.00	222.00

Required:

i. Determine the effect of the acquisition on each company's earnings per share (10mks)

ii. Given that the growth rate of X Ltd is 8% and that of Y Ltd is 12%. Compute he combined growth rate of the two companies (5mks)

QUESTION SIX

a) Discuss the challenges faces by the Kenyan economy by moving towards being a cashless economy (8mks)

b) Discuss the challenges faced by credit rating bodies in Kenya (7mks)