

JARAMOGI OGINGA ODINGA UNIVERSITY OF SCIENCE AND TECHNOLOGY

BACHELOR OF BUSINESS ADMINISTRATION PROGRAMME

ABA 303 (Financial Management)

QUESTION ONE

- i. Explain the term 'financial innovation' (2mks)
- ii. State and explain any three financial innovations (3mks)
- iii. Explain the term credit risk (2mks)
- iv. State and explain the term working capital (3mks)
- v. Differentiate a call option from a put option (4mks)
- vi. Explain the term efficient frontier as used in risk management (3mks)
- vii. Explain three benefits of diversification of investments (3mks)

QUESTION TWO

- a) A businessman wants to purchase an annuity of Ksh 200,000 for the next 3 years. If a financial institution has accepted to pay an interest at the rate of 8%. How much should be invested today (6mks)
- b) Explain the difference between debt and equity (4mks)
- c) State and explain the factors that affect the working capital of a company (10mks)

QUESTION THREE

- a) Explain the term financial intermediation (3mks)
- b) What are the services rendered by the capital markets authority? (10mks)
- c) Explain the factors that financial institution take into consideration as they advance to their customers (7mks)

QUESTION FOUR

- a) State and explain the problem associated with CAPM (14mks)
- b) Clearly explain some of the limitations associate with the use of accounting ratios(6mks)
- c) A stock has a beta of 1.4, if the risk free rate is 10% and the expected return on the market portfolio is 15%. Calculate the expected return (6mks)

QUESTION FIVE

- a) State the advantages of the net present value as a capital budgeting method (4mks)
- b) Clearly explain the objectives of capital budgeting (6mks)
- c) Lion limited has to choose between three projects A, B and C the cash flows of each of the projects would be as follows

| YEAR | PROJECT A | PROJECT B | PROJECT C |
|------|-----------|-----------|-----------|
| 0 | 320,000 | 240,000 | 200,000 |
| 1 | 80,000 | 120,000 | 60,000 |
| 2 | 80,000 | 100,000 | 60,000 |
| 3 | 120,000 | 100,000 | 60,000 |
| 4 | 120,000 | 80,000 | 60,000 |
| 5 | 30,000 | 20,000 | 60,000 |
| 6 | | | |

The firms cost of capital is 15% which project if any should be undertaken. Using both NPV and profitability Index. (10mks)