



**STRATHMORE UNIVERSITY BUSINESS SCHOOL**  
**BACHELOR OF FINANCIAL SERVICES**  
**END OF SEMESTER EXAMINATION**  
**BFS 2104: FINANCIAL MANAGEMENT I**

**Date:** Wednesday, 27<sup>th</sup> July 2022

**Time:** 2 Hours

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**Instructions:**

1. This examination consists of **FIVE** questions.
2. Answer **Question ONE (COMPULSORY)** and any other **TWO** questions.

**QUESTION ONE**

a) Read the **Case extract** below and answer the questions that follow

It is January and Fred is once more concerned about the pressures that the new year brings. Having been in the JAZA SACCO (Savings and Credit Cooperative Society) management board for some years now, he is fully aware that January to March are periods of pressure and tension. Pressure from the SACCO members, the Ministry of Industry Trade and Cooperatives, auditors: who in most cases are rarely ready with the audited annual report until the eve of the Annual General Meetings commonly known as the AGM and a new pressure from the Sacco Societies Regulatory Authority (SASRA). Interestingly, the pressure from the SACCO members comes in a rather friendly manner. This is the season that he receives numerous greetings from colleagues some of whom he might have even never thought knew him well.

“Good morning, Fred,” Kevin, an ever-jovial telephone operator would quip as Fred passes by. Only this time, the greetings would be a bit laden. “How is our SACCO? We hope for an increase in our dividends and interest?”

As he tries to respond, Kyalo, a bus driver and a colleague who was passing by stops on his tracks:

“Ah, Kevin, do not bother the Chairman. You know how he is taking good care of us. Chairman, where is your car key so that we help you clean the car?” You might want to pass by the car shed later. I am sure members would love to talk to you.”

The pressure from the Ministry of Industry Trade and Cooperatives is experienced every year. According to the Ministry regulations, all SACCO societies have until April 31st every year to hold their AGM. Certainly, this demands that the SACCO's annual report must have been fully audited with accredited and registered auditing firms which leads to the pressures with the auditors. Most of the audit firms find themselves with huge files from different SACCOs and other financial institutions to audit within a limited period before the annual reports are forwarded to the ministry for registration. After this process, the SACCO gets the final green light of issuing a two-weeks notification of the AGM.

The auditors were able to deliver the SACCO's audited annual report before the SACCO's AGM scheduled for 12<sup>th</sup> March 2022 relieving Fred of three of the yearly pressures. Appendix 1 shows the financial statements extracted from the 2022 annual report.

#### **Appendix 1: Extracted Financial Statements 2020 – 2021**

##### **Income statements for years ended 2020, 2021**

<b>INCOME STATEMENT</b>	<b>2020 ('000')</b>	<b>2021 ('000')</b>
Sales	115,200	72,000
Cost of sales	(70,800)	(42,000)
<b>Gross profit</b>	<b>44,400</b>	<b>30,000</b>
<b>Expenses</b>		
Selling & administrative expenses	(10,800)	(10,200)
Depreciation	(3,300)	(2,300)
Interest expense	(6,600)	(4,600)
<b>Total expenses</b>	<b>(20,700)</b>	<b>(17,100)</b>
<b>Profit before taxes</b>	<b>23,700</b>	<b>12,900</b>
Taxes (30%)	(7,110)	(3,870)
<b>Net profit (EAT)</b>	<b>16,590</b>	<b>9,030</b>

<b>BALANCE SHEET</b>	<b>2020 ('000')</b>	<b>2021 ('000')</b>
Cash and marketable securities	-	2,880
Receivables	12,600	9,000
Stock	19,800	14,400
<b>Total Current assets</b>	<b>32,400</b>	<b>26,280</b>
<b>Total Fixed assets</b>	<b>35,400</b>	<b>26,400</b>
<b>TOTAL ASSETS</b>	<b>67,800</b>	<b>52,680</b>
Payables	9,200	6,320
Taxation	7,110	3,870
Proposed dividends	8,505	4,500
Bank overdraft	2,545	790
<b>Total Current liabilities</b>	<b>27,360</b>	<b>15,480</b>
<b>NET ASSETS</b>	<b>40,440</b>	<b>37,200</b>
<b>FINANCED BY:</b>		
Long term debt	6,360	9,000
Issued share capital	18,000	18,000
Profit for the year	16,080	10,200
<b>CAPITAL EMPLOYED</b>	<b>40,440</b>	<b>37,200</b>

**Required**

- i. Briefly discuss the financial terms indicated in the case above: Annual report, AGM, Audit, Shares and Interest **(10 marks)**
- ii. JAZA SACCO was considering a bank loan to facilitate automation of its services. The bank requested a report from the company showing “a positive trend in the volume of business it generates for its size of fixed assets, positive interest coverage, meeting its short-term obligations and that dividends have not been paid unless earnings are positive”. Write the report and include the computations from ratio analysis relevant for the report **(10 marks)**

- b) Kevin your chief accountant is 30 years old and wishes to provide for his old age. He decides to invest Kshs. 50,000 per year at an interest rate of 9% p.a. for the next 30 years with the first deposit accruing one year from now. At the age of 60 he plans to tour around the world for five years and on returning to Kenya, he wants to withdraw 530,000 p.a. for the next 15 years.

**Required:**

What is the maximum amount Kevin can consume each year during his world tour, if the 9% return remains constant? **(10 marks)**

**Total: 30 marks**

**QUESTION TWO**

- a) CIH Investment group, borrowed an 8-year loan of Kshs. 1,600,000 at 12% interest rate from ABSA Bank.

**Required**

- i. If the bank requires 8 equal end of year repayments, prepare CIH Investment group's loan amortization schedule. **(10 marks)**
- ii. From the schedule prepared in (i) above indicate the following: Annual installment every year, 7<sup>th</sup> year outstanding balance and 8<sup>th</sup> year Interest amount.

**(5 marks)**

- b) The various statements below relate the questions done on e-learning. Explain why the statements are TRUE/FALSE for marks allocation **(Each 2 marks)**

- i. Deepak won Kshs. 100,000 from a competition. It will take him 5 years to double his money if it grows at 15% annually. **(True/False)**
- ii. Shareholders use the dividend policy of the firm to minimize agency conflict **(True/False)**.
- iii. The company is not legally obliged to pay common dividend therefore in times of financial difficulties it can reduce or not pay common dividends **(True/False)**
- iv. Business risk is the risk that a company will not have adequate cash flow to meet its financial obligations **(True/False)**.
- v. Shareholders are risk averse while financial managers are usually risk seekers. This results to conflict in decision making hence one key cause to agency problems **(True/False)**.

**QUESTION THREE**

a) Read the **Case extract** below and answer the questions that follow

Tumaini Ltd was founded in 2012 by Tracie and Jamin on the basis of fair dealing and respect. Tumaini Ltd credits its ongoing commitments to “doing well by doing good” to other stakeholders as a major reason why employees, suppliers, customers and shareholders seek it out. Tumaini is clear on its obligations to increase the market value of its common stock, yet it strives to maintain the integrity of each employee in every country in which it does business.

Its “Standards of Business Conduct” includes a provision that triggers immediate dismissal of an employee who does wrong to the company e.g. by telling a lie. The company has had a series of growth in its earnings and it intends to put some funds for its future. In all its aspirations, the company has to achieve all these within some ethical constraints.

Some critics have mistakenly assumed that the objective of maximizing shareholders wealth is somehow the cause of unethical behaviour, ignoring the fact that any business goal might be cited as a factor pressurizing an individual to be unethical.

**Required**

Illustrate and explain the objectives/goals from the Case above for Tumaini Ltd (**10 marks**)

b) **Multiple Choice Questions: Each 2 marks (Answers based on your workings)**

- I. Neeti has an opportunity to receive Kshs.50,000 at the end of every year for 7 years. If she can earn 13% return on her investment, what is the most she should pay now for this opportunity?
  - a. Kshs.249,876.90
  - b. Kshs.520,250
  - c. Kshs.587,882.5
  - d. Kshs.221,130
- II. Richard an investor is considering investing in security A and B. Security A has a Beta of 1.1 and expected rate of return of 16%. Security B has a Beta of 0.5 and expected rate of return of

11%. Assume that the return on treasury bills is 8% and average return in the market is 14%.

Advice Richard on whether he buys or sell the security

- a. A = 14.6% (Undervalued) and B = 11% (Fairly valued)
- b. A = 16.8% (Undervalued) and B = 9.5% (Overvalued)
- c. A = 14.6% (Overvalued) and B = 11% (Undervalued)
- d. A = 16.8% (Overvalued) and B = 9.5% (Undervalued)

III. Bakhita wants to invest in a fund in order to repay a 7-year loan of Kshs 500,000. How much should Bakhita invest annually in the fund, earning 11% interest, in order to repay the loan?

- a. Kshs.240,824.58
- b. Kshs.106,107.55
- c. Kshs.51,107.50
- d. Kshs.1,037,990.45

IV. Victor wishes to determine how much he will have at the end of five years if he deposits Sh.2000 at the beginning of each year at an interest rate of 11%.

- a. Kshs.8,204.90
- b. Kshs. 3,740.92
- c. Kshs. 12,455.60
- d. Kshs. 13,825.72

V. Ivy wants to invest in a project that will give her Sh.4000 at the beginning of each year for six years. What is the maximum amount she will be willing to pay now for that project if the rate is 13%?

- a. Kshs.18,068.93
- b. Kshs.15,990
- c. Kshs.33,290.80
- d. Kshs.37,618.60

**Total: 20 marks**

## QUESTION FOUR

Miss. Peris, CFO of Zuza Ltd was presented with four projects that required her approval. Each project required Kshs. 18 million in capital-expenditure. With the fiscal year ending, there was need to determine which projects best fit Zuza Ltd future growth plans.

The expected cashflows for each project are show below:

Year	Project A (Kshs.)	Project B (Kshs.)	Project C	Project D(Kshs.)
1	6,500,000	3,500,000	2,500,000	8,200,000
2	5,500,000	4,500,000	1,500,000	6,600,000
3	3,500,000	2,500,000	3,500,000	5,500,000
4	1,500,000	2,000,000	4,000,000	4,000,000
5	2,600,000	4,500,000	5,200,000	2,500,000
6	3,100,000	5,800,000	6,400,000	1,800,000
7	3,700,000	5,400,000	6,600,000	2,400,000

The recommended required rate of return is 11%

### Required

- Using the Net Present Value and Profitability Index approach, rank the projects based on the value they will create for Zuza Ltd. **(17 marks)**
- Mrs. Peris can only select two of the projects given budget constraints. Which of the two will she select and why **(3 marks)**

**Total: 20 marks**

## QUESTION FIVE

The financial management class implemented the financial principles and techniques they learned to a Micro enterprise contributing to the Sustainable Development Goals. The different groups in class prepared Case Studies on each of the Micro enterprises. You have been requested to present from your Group Case Study the following:

- Brief history of Micro enterprise and its operations **(6 marks)**
- The financial management dilemma experienced by the Micro enterprise **(6 marks)**
- The solution proposed by your group to the Micro enterprise **(8marks)**

**Total: 20 marks**