



ZIMBABWE EZEKIEL GUTI UNIVERSITY

FACULTY OF BUSINESS, ECONOMICS AND ACCOUNTING

DEPARTMENT OF ACCOUNTING AND FINANCE

EXAMINATION PAPER

COURSE CODE : CAC 209
COURSE TITLE : FINANCIAL MANAGEMENT
DURATION : 3 Hours
DATE :

INSTRUCTIONS TO CANDIDATES:

1. No cell phones are allowed in the examination venue.
2. Use of silent, non-programmable calculators is allowed.
3. Answer all questions.
4. Begin each question on a new page.
5. The number of marks for each question or part question is shown in brackets.

Section A

Answer all questions in this section. Each question carries 2 marks.

Select the most appropriate answer

1. In 3 years, you are to receive \$5,000. If the interest rate were to suddenly increase, the present value of that future amount to you would
 - A. fall.
 - B. rise
 - C. remain unchanged
 - D. cannot be determined without more information

2. Under the payback period
 - A. we compute the time required to recoup the original investment
 - B. there is no consideration of inflows after the cutoff period
 - C. the time value of money is ignored
 - D. all of the above are correct

3. The capital budgeting decision involves the planning of expenditures for projects with a life of at least:
 - A. one year
 - B. five years
 - C. ten years
 - D. fifteen years

4. The standard deviation
 - A. is the square root of the variance
 - B. measures dispersion or variability around the expected value
 - C. may be used to compare investments with the same expected return
 - D. all of the above are correct

5. The efficient frontier represents
 - A. the difference between investment returns
 - B. optimal risk-return tradeoffs
 - C. the correct investment for all firms to make
 - D. the correlation between profits and the portfolio effect

6. The field of finance is closely related to the fields of
 - A. statistics and economics
 - B. statistics and risk analysis
 - C. economics and accounting
 - D. accounting and comparative return analysis

7. Which of the following constitutes an internal source of funds:
- A. corporate bonds
 - B. common stock
 - C. commercial paper
 - D. retained earnings and amortization cash flow
8. It would be fair to say that securities markets in the future
- A. will become more competitive as an international market system develops
 - B. will be less efficient
 - C. will be more highly segregated than they are today
 - D. will be less automated than today's markets
9. You are considering borrowing \$10,000 for 3 years at an annual interest rate of 6%. The loan agreement calls for 3 equal payments, to be paid at the end of each of the next 3 years. (Payments include both principal and interest.) The annual payment that will fully pay off (amortize) the loan is closest to
- A. \$2,674.
 - B. \$2,890
 - C. \$3,741
 - D. \$4,020
10. Preferred equity has all of the following characteristics except
- A. fixed dividends
 - B. the cumulative right to annual dividends
 - C. precedence over common stock dividends
 - D. residual claim to income
11. Agency theory examines the:
- A. relationship between the owners and managers of the firm
 - B. insurability of the firm's assets
 - C. relationship between dividend policy and firm value
 - D. value of the firm relative to other firms in the industry

[Total 20marks]

Section B

Answer all questions from this section

Question One

Emily is considering two investments and can only invest in either the shares of Company X or in the shares of Company Y. The following information regarding returns and probability distributions of returns is relevant:

Share X		Share Y	
Probability	Return X	Probability	Return Y
0.20	10%	0.20	0%
0.60	15%	0.30	10%
0.20	20%	0.30	20%
		0.20	30%

Required:

- a) Calculate the expected return of X and Y? [6 marks]
 - b) Calculate the standard deviations of X and Y's returns [6 marks]
 - c) Calculate the co-efficient of variation? [4 marks]
 - d) Recommend the best share and explain why you recommend it? [4 marks]
 - e) Instead of Share Y offering a probability of 20% of achieving a 30% return, assume instead that the possible return is 40%. Explain the effect to the investment decision? [5 marks]
 - f) Explain the roles of a financial manager? [5 marks]
- [Total 30marks]**

Question Two

You have been asked to evaluate a new machine that is being considered by Eagle Manufacturing Ltd. The machine will require a \$15m investment now, and there will be a \$2m salvage value at the end of five years. The net cash inflows are estimated to be \$4m per year for five years.

Required:

- a) Calculate the net present value for the machine assuming a 10% cost of capital for the firm. [6 marks]
- b) Estimate the internal rate of return for the machine. [6 marks]
- c) Calculate the payback period. [4 marks]
- d) Based on your net present value calculation in (a), would you recommend that Roxlee Manufacturing purchase the machine? [3 marks]

e) Describe the relationship between the Capital Market Line and the Security Market Line.

[6 marks]

[Total 25marks]

Question Three

a) 'Preference shares are a hybrid of debt and equity and contain the best features of each as far as the issuing company is concerned. It follows that companies should make extensive use of preference shares for their long-term financing requirements.' Discuss.

[13 marks]

b) Mark Ltd can invest in the projects below. Its capital budget is, however, limited to \$400m. The company's cost of capital is 12%.

Project	A	B	C	D	E	F
Cost	80	120	180	160	40	60
NPV	16	18	21	12	10	-5.5

Required:

Which projects should the company accept if the projects are:

a) divisible

[6 marks]

b) indivisible?

[6 marks]

[Total 25marks]

END OF EXAMINATION QUESTION PAPER