



**UNIVERSITY EXAMINATIONS**  
**SECOND YEAR EXAMINATION FOR THE AWARD OF THE**  
**DIPLOMA IN FINANCIAL MANAGEMENT II**  
**FIRST SEMESTER 2023/2024**  
**[AUGUST-DECEMBER, 2023]**

**DIAF 0123: FINANCIAL MANAGEMENT II**

**STREAM: Y1 S2**

**TIME: 2 HOURS**

**DAY: WEDNESDAY, 3.00 – 5.00 P.M.**

**DATE: 29/11/2023**

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**INSTRUCTIONS**

- 1. Do not write anything on this question paper.***
- 2. Answer Questions ONE and any other THREE Questions***

**QUESTION ONE: 25 MARKS**

a) A company is considering two mutually exclusive projects requiring an initial cash outlay of sh.10 million each and with a useful life of 5 years. The company required rate of return is 10% and the appropriate corporate tax rate is 30%. The projects will be depreciated on a straight line basis. The before depreciation and taxes cash flows expected to be generated by the projects are as follows.

YEAR	1	2	3	4	5
Project A	4 million	4 million	4 million	4 million	4 million
Project B	6 million	3 million	2 million	5 million	5 million

Required:

Calculate for each project:

- i. The accounting rate of return. (4marks)
  - ii. The payback period. (3marks)
  - iii. The profitability index. (3marks)
- b) Outline three basic assumptions of Capital Asset Pricing Model (CAPM). (3marks)
- c) Discuss four factors influencing the cost of capital. (4 marks)
- d) Highlight four uses of financial ratios to companies. (4 marks)
- e) List four importance of capital structure. (4 marks)

### **QUESTION TWO**

a) Modern portfolio theory applies advanced mathematical models to determine the correlation between risk and return on investments. While it's commonly used, it does have some potential drawbacks.

In relation to the above statement, examine six shortcomings of the modern portfolio theory. (8 marks)

b) Outline four objectives of financial analysis. (7 marks)

### **QUESTION THREE**

a) ABC ltd wishes to expand its output by purchasing a new machine worth sh 170,000 and installation costs are estimated at sh.40, 000. In the 4<sup>th</sup> year this machine will call for an overhaul cost of sh.80, 000 and the company can raise finance to purchase the machine at 12% interest rate. Its expected inflows are:

Period	Sh
Year 1	60,000
Year 2	72,650
Year 3	35,720
Year 4	48,510
Year 5	91,630
Year 6	83,715

Required:

- i) Compute the net present value (NPV) and advise the management accordingly. (10 marks)
- ii) Outline five functions of public sector finance. (5 marks)

**QUESTION FOUR**

- a) Explain five techniques of managing risks. (7 marks)
- b) Outline the steps in capital budgeting process. (8 marks)

**QUESTION FIVE**

- a) Discuss and give examples of how government assist companies in their financing requirements. (8 marks)
- b) Explain five sources of public finance. (7 marks)