MACHAKOS UNIVERSITY

University Examinations for 2018/2019 Academic Year

SCHOOL OF BUSINESS AND ECONOMICS

DEPARTMENT OF BANKING, ACCOUNTING & FINANCE

FOURTH YEAR SPECIAL/SUPPLEMENTARY EXAMINATION FOR

BACHELOR OF COMMERCE

AGB 412 INTERNATIONAL CORPORATE FINANCE

DATE: 24/7/2019 **TIME: 2.00-4.00 PM**

INSTRUCTIONS: Attempt Question One and any other Two Questions

QUESTION ONE

(a) (i) What is capital budgeting and what is its significance to a corporation? (4 Marks)

(ii) Explain the following Dividend theories:

(i) Dividend Irrelevance Theory
(ii) Bird-In-The-Hand Theory
(iii) Tax Preference Theory (6Marks)

(b) The following information below relates to Excel Ltd. for last year.

Description	Amount (in millions)
Purchase of raw materials	67
Usage of raw materials	65
Credit sales (of finished goods)	250
Cost of sales of finished goods	180
Average trade payables	14
Average raw materials inventories	12
Average work in progress	10
Average finished goods inventories	21
Average trade receivables.	47

Calculate the cash conversion cycle in days. (10 Marks)

(c) The following information relate to a Top Investors Ltd. Annual interest rate is 7%. Fixed transaction cost is Shs.10m. The total cash needed for transactions over the relevant planning period is Shs.10,000m

Required:

Calculate

a) The target cash balance using the Baumol Model (3 Marks)

b) The opportunity cost of maintaining this cash balance. (3Marks)

c) The trading cost (2 Marks)

d) The total cost (2 Marks)

QUESTION TWO

a) Amodil Manufacturing Co. is a reputable company operating in the heart of Nairobi city. It starts each period with 10,000 units in stock. This stock is depleted each month and is re-ordered. If the carrying cost per unit is Shs.100, and the fixed order cost is Shs.500, Calculate the Economic Order Quantity of Amodil Manufacturing.

Required:

(i) Determine the total carrying cost. (5 Marks)

(ii) Determine the total restocking cost (5 Marks)

(iii) Is Amodil following an economically advisable strategy? (4 Marks)

b) Using the EOQ Model, determine the optimal inventory level for Amodil Manufacturing Co. (6 Marks)

QUESTION THREE

(a) Explain the following theories of capital Structure

(i) The pecking order theory

(ii) The trade-off theory (6 Marks)

(b) ABC Company has reported EBIT of Shs.120,000 in the current year and is forecasting that due improved market conditions, it will increase this amount by Shs.60,000 in the following year. It has a Shs.200,000 bond with a 10% coupon rate of interest and 6,000 shares of preferred stock with annual dividend per share of Shs. 4. It also has 10,000 shares of common stock outstanding . Assume a tax rate of 30%.

Required

(i) Calculate earnings per share for the two EBIT levels. (10 Marks)

(ii) Calculate the degree of Financial Leverage. (4 Marks)

QUESTION FOUR

The domestic Australian beta of Billiton Ltd is 1.4whis is above beta risk level. The expected return on the Australian market portfolio is 10%and that the risk free rate is 5%.

a) Calculate the expected return on Billiton Ltd stock if the Australian Capital Markets are segmented from the rest of the world. (5Marks)

b) If Australian Capital Markets are integrated with the rest of the Word and that the World beta measure of Billiton Stock is 1.1, assuming that the risk free rate is 5%, and the expected return on the world market portfolio is 10%,calculate the expected return on the Billiton Stock. (10Marks)

(c)The ordinary shares of a Company are currently trading at Shs.20 (ex dividend) each in the capital market. Next years dividend is expected to be Shs.1.4 per share and subsequent dividends are expected to grow at an annual rate of 5% of the previous years dividend. What is the cost of equity? (5Marks)

QUESTION FIVE

a) An acquisition is defined as a corporate transaction where one company purchases a portion or all of another company's shares or assets. Acquisitions are typically made in order to take control and build on the target company's weaknesses or strengths and capture Synergies. Explain the three basic forms of Acquisition. (6 Marks)

b) Explain how companies achieve efficient asset allocation (6 Marks)

c) Describe eight factors that determine capital structure in Corporations (8 Marks)