



THE CATHOLIC UNIVERSITY OF EASTERN AFRICA

A. M. E. C. E. A

KISUMU CITY CAMPUS

MAIN EXAMINATION

AUGUST – DECEMBER 2014 TRIMESTER

FACULTY OF COMMERCE

DEPARTMENT OF ACCOUNTING AND FINANCE

EVENING PROGRAMME

CFI 311: CORPORATE FINANCE

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Date: December 2014

Duration: 2 Hours

Instructions: Answer question one and any other two

- Q1. (i) Define corporate finance (2 marks)
- (ii) With the aid of a chart, give a summarized presentation of the first principles of corporate finance (8 marks)

(iii) Cedes Ltd has the following details of two of the future production plans. Only one of these machines will be purchased and the venture would be taken to be virtually exclusive. The standard model costs Kshs 50,000 and the Deluxe costs Kshs 88,000 payable immediately. Both machines will require the input of the following

- (a) Installation costs of Kshs 20,000 for standard and Kshs 40,000 for Deluxe
(b) A Kshs 10,000 working capital through their working lives
- Both machines have no expected scrap value at the end of their expected working lives of 4 years for the standard machine and 6 years for Deluxe. The operating pre – tax net cash flows associated with the two machines are;

Year	1	2	3	4	5	6
Standard	28,500	25,860	24,210	23,410	-	-
Deluxe	36,030	30,110	28,380	25,940	38,500	35,100

The Deluxe machine has only been fully tested in the operating conditions; because of the high risk involved, the appropriate discount rate for the deluxe machine is believed to be 14% per annum, 2% higher than the rate of the standard machine. The company is proposing the purchasing of either machine with a term loan of a fixed rate of interest of 11% per annum taxation at 30% is payable on operating cash flows one year in arrears and capital allowance are available at 25% per annum on a reducing balance basis.

Required:

(i) For both the standard and the Deluxe machines calculate the payback period. (20 marks)

Q2 (i) Explain why Mr Wanjala the finance officer of Fedha Capita; Ltd, would opt for mergers as one of his major finance decisions (10 marks)

(ii) Describe the features of long – term investment decisions (10 marks)

END