UGANDA MARTYRS UNIVERSITY, LUBAGA, MASAKA AND MBALE CAMPUSES

FACULTY OF BUSINESS ADMINISTRATION AND MANAGEMENT

DEPARTMENT OF MANAGEMENT ACCOUNTING AND FINANCE

MBA PT II

SEMESTER TWO 2023/2024

COURSE UNIT: CORPORATE FINANCE AND INTERNATIONAL FINANCIAL MANAGEMENT

CODE: MBA7217

DATE: 7TH OCTOBER, 2023

TIME: 3 HOURS

Instructions:

- Carefully read through ALL the questions before attempting
- Read the instructions on the cover of the answer book and the question paper
- The total number of questions in this paper is **SIX.** Attempt **FOUR** questions
- **QUESTION ONE IS COMPULSORY**
- Relevant examples will earn you marks
- Write legibly.
- **Don't write anything on the question paper.**

Question One

Kabanda Ltd is considering diversifying its operations away from its main area of business into a construction business. It wishes to evaluate an investment project, which involves the purchase of a new machine that costs UGX 200,000,000. The project is expected to produce net annual operating cash flows of UGX 130,000,000 for each of the five years of its life. At the end of this time its scrap value is UGX10.

The assets of the firm can support a debt finance of 50% of its initial cost (including issue costs). Kabanda Ltd is considering borrowing the balance.

The government has offered to lend the balance with no issue costs, at a subsidize rate of 3% p.a, the full amount will be repayable after five years. The balance of finance will be provided by a placing of new equity. Issue costs will be 7% of funds raised for the equity placing. Debt issue costs are allowable deductions for corporation tax. The construction industry has an average equity beta of 0.9 and an average debt: equity ratio of 7:5 at market values. Kabanda's current equity beta is 1.3 and 20% of its long-term capital is represented by debt which is generally regarded to be risk-free. The risk-free rate is 10% p.a and the expected return on an average market portfolio is 20%. Corporation tax is at a rate of 30%, payable in the same year. The machine will attract a 75% capital allowance and the balance is to be written evenly over the remainder of the asset life and is allowable against tax. The firm is certain that it will earn sufficient profits against which to offset these allowances.

NB: Take Ke/ cost of capital to be 14.5%

Required: Calculate the APV and determine whether the project is worthwhile **(25 marks)**

Question Two

UMU Inc, a Uganda company is considering undertaking a new project in the DRC. This will require initial capital expenditure of UGX I,250 million, with no scrap value envisaged at the end of the five-year lifespan of the project. There will also be an initial working capital requirement of UGX 500 million, which will be recovered at the end of the project. The initial capital will therefore be UGX 1,750 million. Pre-tax net cash inflows of UGX 800 million are expected to be generated each year from the project.

Company tax will be charged at the rate of 40% in the DRC, with depreciation on a straight-line basis being an allowable deduction for tax purposes. DRC tax is paid at the end of the year following that in which the taxable profits arise.

There is a double taxation agreement between the Uganda and the DRC, which means that no Uganda tax will be payable on the project profits.

The current UGX/DRC Franc spot rate is UGX1 = DRC Franc 0.625, inflation rates are 4% in the Uganda and 5% in the DRC. A project of similar risk recently undertaken by UMU Inc in the Uganda had a cost of capital of 10%.

Required: Calculate the NPV of the project. **15marks)**

[b] As a commissioner of Trade in the Ministry of trade and industry, how would you respond to criticism that mergers, acquisitions and takeovers by multinational business organizations are not the solutions to their growth **(10 marks). Note: Prepare the presentation in report format**

Question Three

Odoki Ltd, in recent years has been experiencing financial constraints. They say although sales have remained stable at shs 3.5 billion per year. The level of debtors has increased significantly. A recent survey conducted indicates that an average settlement period for debtors stand at 60 days compared with the industries' average of 40 days. The level of bad debts increased to 40 million in recent years and at present the Company finances its debtors with overdraft at 14% interest rate per year. However, in order to speed up collection of debts, Odoki ltd is considering hiring a factor who will offer advance equal to 85% of the trade debtor base on assumption that the level of debts will be in line with the industries' average. The factor will take over the sales ledger of the Odoki Ltd and will charge a service fee of 5% of sales. Odoki Ltd believe that the service offered will eliminate bad debts and lead to saving of the administrative cost of shs 51 million per year.

NB: Factor can provide the funding at 10%

Required

Calculate the effect of employing debt factor on the profit and describe your finding **(17 marks)**

[a] "Trend analysis provides users of financial statements with a history of the financial and operating performances of an entity over a protracted time period. It gives a more in-depth portrayal of what is going on" As an expert in analyzing the financial statements of a business, discuss the key objectives of using ratio analysis **(8 marks)**

Question Four

[a] K Ltd is planning to obtain a stock exchange listing by offering 45% of its existing shares to the public. No new shares will be issued. Its recent summarized financial and operating results are as follows: -

Turnover	Shs 120,000,000 p.a
10% Bank loan	Shs 2,000,000
Net operating income	Shs 1,700,000
Number of shares	3,000

K ltd regularly pays 50% of earnings as dividends and it is expected to achieve 5 % dividend growth each year. The company has low gearing. The summarized details of two listed companies in the same industry as K are given below: -

	P Limited	F Limited
Market Value of Equity	Shs 100,000,000	Shs 80,000,000
Market Value of Debt	Shs 45,000,000	Shs 8,000,000
Required Return on Equity	12%	10%
Turnover	Shs 190,000,000 p.a.	Shs 115,000,000 p.a.

Your Company has been appointed as a co-underwriter of the share issue and is required to estimate the price at which they should be issued to the public. It was unanimously agreed, in a meeting between your Company, the other underwriter and K ltd that the shares should be issued at a discount of 15 % to the price that would be estimated in order to increase the prospects of success for the share issue.

Required: Calculate the price at which K should issue its shares and comment on your finding **(5 marks)**

(b) Company A Limited produces residential house gates. Comparative statements of profit or loss and statements of financial position for the years ended 31st December 2022 and 2021 are given below:

Company A Ltd

Statements of Financial Position as at 31st December

	2022	2021
	Shs. '000'	Shs. '000'
Non-Current Assets:		
Land	69,000	66,000
Machinery and Equipment	172,000	156,000
Accumulated Depreciation,		
Machinery and Equipment	(113,000)	(102,000)
Total Non-Current Assets	128,000	120,000
Current Assets:		
Cash and Cash Equivalents	11,000	13,000
Accounts Receivable (net)	92,000	77,000
Inventory	103,000	92,000
Prepaid Expenses	6,000	5,000
Total Current Assets	212,000	187,000
Total Assets:	**340,000**	**307,000**
Current Liabilities:		
Accounts Payable	66,000	78,000
Dividends Payable	2,000	0
Income Taxes Payable	3,000	5,000
Total Current Liabilities	71,000	83,000
Long-Term Debt	75,000	42,000
Total Liabilities	146,000	125,000
Shareholder's Equity:		
Equity Share capital	26,000	26,000
Retained Earnings	168,000	156,000
Total Shareholders' Equity	194,000	182,000
Total Liabilities and Share holders' Equity	**340,000**	**307,000**

Company A

Statements of Profit or Loss for the years ended 31st December

	2022	2021
	Shs. '000'	Shs '000'
Net Sales Revenue	600,000	575,000
Cost of Goods Sold	500,000	460,000
Gross Margin	100,000	115,000
Operating Expenses	66,000	60,000
Operating Income	34,000	55,000
Interest Expenses	4,000	3,000
Income before Tax	30,000	52,000
Income Tax	12,000	21,000
PROFIT	**18,000**	**31,000**

The following additional information is also available:

i) Dividends declared during 2022 were Shs.8,000,000.

ii) Market price per share on 31st December 2022 was Shs.15,000

iii) Equipment worth Shs.20,000,000 was acquired by the issuance of a long-term note (Shs.10,000,000) and the balance by paying cash.

iv) Land was acquired for Shs.3,000,000 cash.

v) Depreciation of Shs.11,000,000 was included in operating expenses for 2022.

vi) There were no accruals or prepaid amount for interest

Required:

a) Prepared a Statement of Cash Flows of Company A Ltd. And briefly comment on the Statement you have prepared. **(14 marks)**

b) In the long run, is it more important for a business to have positive cash flows from its operating activities, investing activities, or financing activities? **Why? (6 marks)**

Question Five

[a] Forecasting Cash Flows from an Overseas Project calls for clear understanding of the followings: Subsidies, Exchange restrictions, Impact of Transaction Costs, Taxes and the Adjusted Present Value. Using illustrations, elucidate how each of these concepts affect forecast cash flows from overseas under international business management **(20 marks)**

[b] Using applicable example, examine the key roles of financial manager in organization in formulating budgets **(5marks)**

Question Six

[a] Mars Limited is in the process of negotiating with Star Limited a firm of certified valuers to establish the value of Mars Limited shares.

1. Explain why a company may decide to value its shares. **(4 marks)**
2. Distinguish between break up valuation and going concern valuation **(4marks)**
3. Absolute Group of companies specializes in manufacturing of Fast-moving consumables goods in East Africa. Off late, Absolute Group of company's distributors have been failing to clear their debts obligations on time and this prompted the company to start offering training and seminars on working capital management for their distributors' staff to enable them manage their working capital better. Absolute Group of companies has approach you to provide guidance on the need have credit policy and factors to be consider in assessing credit worthiness of their customers. Required, provide advice based on their request **(12 marks)**

[b] Discuss any five considerations an investor should make in building a portfolio of investments **(5 marks)**