

# UGANDA MARTYRS UNIVERSITY

## UNIVERSITY EXAMINATIONS

### FACULTY OF BUSINESS ADMINISTRATION & MANAGEMENT

### DEPARTMENT OF FINANCE & FINANCE &

### END OF SEMESTER FINAL ASSESSMENT

SEMESTER II, 2018/19

### THIRD YEAR EXAMINATIONS FOR BACHELOR OF BUSINESS ADMINISTRATION & MANAGEMENT

### CORPORATE FINANCE II

DATE: 21<sup>st</sup> JUNE 2019

TIME: 4:00pm – 6:00 pm

DURATION: 3Hrs

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**Instructions:**

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Read the following before answering the examination questions.

Attempt any Four (4) Questions.

Do not write anything on the question paper.

Your work must be neat and show all relevant workings

Mobile phones are not allowed in the Examination room

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**DO NOT WRITE ON THIS QUESTION PAPER**

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### Question one.

Success Ltd is planning to construct a building complex along Work hard street. The complex will consume Shs 1.8 billion. Success Ltd's current capital structure is as follows.

Source	Debt	Ordinary Shares	Retained Earnings	Total
Amount "000"	3,840,000	4,800,000	960,000	9,600,000

The following information has also been provided.

- New debt will be raised from the issue of debentures at an interest rate of 15%. No additional costs will be incurred.
- Ordinary shares have a current market price of Shs. 300 per share with a dividend of Shs. 50 per share and are expected to grow at a rate of 5% per annum. Floatation costs amount to 4%.

### Required.

- How much of the Shs. 1.8 billion should be raised by equity if the capital structure is to remain unchanged? **(5 marks)**
  - How much of the capital must be raised via debentures? **(5 marks)**
- b) What factors should Success Ltd consider when raising capital for such a structure? **(15 marks)**

### Question two.

Build Uganda ltd currently has a total capital structure of Shs. 100 million composed as;

20%	Long Term Bank Loan	40m
10%	Preference Shares	10m
	Common Shares	30m
	Retained Profits	20m
	<b>Total</b>	<b>100m</b>

The business anticipates that dividends on ordinary shares will be Shs. 5,000 per share and the market value of the share is Shs 22,000 per share. The dividend is expected to grow at a rate of 6% per year for ever and the company is in the 30% tax bracket.

### Required;

- Determine the weighted average cost of capital (WAAC) for the firm. **(15 marks)**
- Explain why the Capital Asset Pricing Model would be superior as a method of determining cost of capital as compared to the weighted average cost capital method. **(10 marks)**

### Question three.

Shareholders of Better Service (U) Ltd a leading garment factory wish to diversify to real estate business project which they will finance 100% by equity. The average risk in the real estate business is 1.8 and has a market return of 16% and government bonds presently earn a risk –less rate of return of 6%.



**Required.**

- i) Estimate the required rate of return to be used to evaluate this investment proposal. (10 marks)
- ii) Give the limitations of the Capital Asset Pricing Model (CAPM) (15 marks)

**Question four**

(5 Marks)

- a) Explain the term "financial distress"
- b) Discuss the causes of financial distress in business entities that may lead to business failure (10Marks)
- c) Discuss the possible courses of action that can be taken to address financial distress (10Marks)

**Question five**

In a corporate meeting, an issue of dividends was raised by a disgruntled shareholder. The CEO responded by saying "a number of questions have to be answered before a sustainable dividend policy is drawn. After all the level and form of dividends is irrelevant".

**Required**

- a) Defend the disgruntled shareholder by showing how relevant dividends are to an entity. (5Marks)
- b) What are the likely questions that need to be answered if a sustainable dividend policy is to be drawn and what are the possible answers? (10 Marks)
- c) What may constrain a company if it desires to give out dividends? (10 Marks)

**Question six**

- a) Explain the concept of Islamic banking in general terms. (5 Marks)
- b) Describe any **five** principles of Islamic banking Known to you. (10 Marks)
- c) Explain any five forms of entry for foreign direct investment (FDI) (10 Marks)

**"End"**