



NATIONAL OPEN UNIVERSITY OF NIGERIA
14/16 AHMADU BELOW WAY, VICTORIA ISLAND, LAGOS
SCHOOL OF MANAGEMENT SCIENCES
MARCH 2014 EXAMINATION

COURSE CODE: BHM 713

CREDIT UNIT: 2

COURSE TITLE: CAPITAL INVESTMENT AND FINANCIAL DECISIONS

TIME ALLOWED: 2 hrs

- Instructions:**
- 1. Attempt question Number one (1) and any other two (2).**
 - 2. Question number 1 is compulsory and carries 30 marks, while the other questions carry equal marks each.**
 - 3. Present all points in a coherent and orderly manner**

QUESTION 1

1a) What are the features of investment

10 Marks

1b) Bola Plc is considering the following three projects whose associated cash flows are given thus:

YEAR	PROJEC T A	PROJEC T B	PROJEC T C
	N'000	N'000	N'000
0	- 500,000	- 500,000	- 500,000
1	100,000	150,000	200,000
2	150,000	250,000	250,000
3	250,000	300,000	300,000
4	500,000	300,000	450,000

Required: Calculate the payback periods for each of the projects and advice Bola Plc accordingly.

15 Marks

1c) Explain compound interest.
Marks

5

QUESTION 2

2a) Discuss fully the term 'relevant cost

8 Marks

2b) What are the components of cash flows according to Lucey (1988)

7 Marks

2c) Give the basic definition of Accounting Rate of Return (ARR) and the other variants that exist.

5 Marks

QUESTION 3

3a) Explain the following terms

Marks

- I. Single period capital rationing.**
- II. Multi-Period Capital rationing**
- III. Divisible projects**
- IV. Indivisible projects**

8

3b) Give brief explanations of the following terms

2 Marks each

- **Differential Costs**
- **Incremental Cost**
- **Committed Costs**
- **Notional (Imputed) Costs**

3c) Today, Uche purchased an annuity of N250, 000 per year for 15 years from an insurance company, which uses 3% compound annually. If the first payment is due in one year, what did the annuity cost him?

4 Marks

QUESTION 4

4a) Modern Tech Services Ltd is considering two alternative projects for a business expansion programme in the Northern part of the country. The projects have the following Naira cash flow profiles according to the data supplied by the company's accountant:

Year	Project I	Project II
0	-1 Million	-3 Million
1	-2 Million	0.20 Million
2	-95 Million	-50 Million
3	0.85 Million	0.65 Million
4	0.78 Million	0.75 Million
5	0.62 Million	0.80 Million
6	0.40 Million	1.90 Million
7	0.10 Million	0.20 Million

Required:

a. Calculate the payback period for each project

8 marks

b. Based on payback periods, advice which of the two projects should be chosen

1mark

4b) List three advantages and three disadvantages of Sensitivity Analysis

6 Marks

4c) How does incremental cost differ from differential cost?

5 Marks

QUESTION 5

5a) What are the two ways identified for the treatment of sensitivity analysis?

5 Marks

5b) What is the weakness of sensitivity analysis?

5 Marks

5c) List 10 methods of incorporating uncertainty and risk when appraising projects

10 Marks

