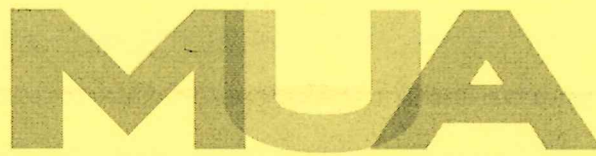


The
Management
University
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UNDERGRADUATE UNIVERSITY EXAMINATIONS

SCHOOL OF MANAGEMENT AND LEADERSHIP

DEGREE OF BACHELOR OF COMMERCE

FIN 421 : SECURITY ANALYSIS AND SECURITIZATION

DATE: 5TH DECEMBER 2023

DURATION: 2 HOURS

MAXIMUM MARKS: 70

INSTRUCTIONS:

1. Write your registration number on the answer booklet.
2. **DO NOT** write on this question paper.
3. This paper contains **SIX (6)** questions.
4. Question **ONE** is compulsory.
5. Answer any other **THREE** questions.
6. Question **ONE** carries **25 MARKS** and the rest carry **15 MARKS** each.
7. **Write all your answers in the Examination answer booklet provided.**

QUESTION ONE

- a) Explain the factors that finance managers should analyse before making a dividend decision. **(5 marks)**
- b) Assume all things are held constant other than the item in question, for each of the companies below:
- i) A company with a large proportion of insider ownership all of whom are high-income individuals.
 - ii) A growth company with an abundance of good investment opportunities.
 - iii) A company experiencing ordinary growth that has high liquidity and much unused borrowing capacity.
 - iv) A dividend paying company that experiences an unexpected drop in earnings from a trend. A company with volatile earnings and high business risk.

Required:

Examine whether or not you would expect each company to have a medium/high or a low dividend payment ratio and the reasons for such categorisation. **(8 marks)**

- c) Company A is considering investing in a project which has a three-year life. The project would involve an initial investment of Sh.20 million. The finance manager has come up with expected probabilities for various possible economic conditions as follows:

Year	Economic Conditions	Sh.'000'	
		Net cash flows	Probability
0		(20,000)	1.0
1	High growth	10,000	0.2
	Average growth	6,000	0.7
	No growth	2,000	0.1
2	High growth	12,000	0.3
	Average growth	8,000	0.5
	No growth	4,000	0.2
3	High growth	16,000	0.4
	Average growth	12,000	0.3
	No growth	6,000	0.3

Required:

Assuming a discount rate of 15% should company A invest in the project?

(12 marks)

QUESTION TWO

- a) Examine the difference between fundamental and a chartist's analysis in the valuation of shares? (5 marks)
- b) Corporate bonds have recently started gaining prominence as disintermediation financial instruments in developing countries.
- i) Distinguish between financial intermediation and financial facilitation. (4 marks)
- ii) Explain the relationship between the price of bonds and:
1. Interest rates in the market generally. (2 marks)
 2. Term to maturity of the bonds. (2 marks)
- c) Examine two advantages of net present value (2 marks)

QUESTION THREE

- a) In the recent past, the government has been aggressively wooing multinational companies to come and invest their resources in Kenya. Analyze the key decision areas that a financial analyst would have to advise a company that is considering making direct investment in Kenya and discuss the risks involved. (10 Marks)
- b) Evaluate five reasons why most investors prefer to hold a diversified portfolio of securities as opposed to placing all of their wealth in a single asset (5 Marks)

QUESTION FOUR

- a) Explain the three forms of informationally efficient capital markets. (6 marks)
- b) Discuss the benefits that may accrue to a company that uses securitization in preference to traditional financing through intermediaries. (5 marks)
- c) Examine four variables that will affect the level of interest rates in an economic set up. (4 marks)

QUESTION FIVE

- a) Mr. Kobe is contemplating acquiring Mfalme Flower Company. Incremental cash flows arising from the acquisition are expected to be the following:

Average of years	Net cash flows Sh. millions
1 - 5	50
6 - 10	90
11 - x	130

Mfalme has an all-equity capital structure. Its beta is 0.8 based on the past 60 months of data relating its excess returns to that of the market. The risk free rate is 9% and the expected return on the market portfolio is 14%.

Required:

- a) Compute the maximum price that Kobe should pay for Mfalme? **(10 marks)**
- b) Define a financial system and discuss its roles in economic development.
(5 Marks)

QUESTION SIX

- a) Enumerate the advantages of financing a project from common stock over debt financing. **(5 Marks)**
- b) Explain the factors that causes the interest rates to either rise or fall. **(10 Marks)**