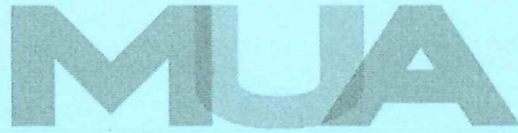


The
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POST GRADUATE UNIVERSITY EXAMINATIONS

SCHOOL OF MANAGEMENT AND LEADERSHIP

DEGREE OF MASTER OF MANAGEMENT AND LEADERSHIP

MML 5202: STRATEGIC FINANCIAL MANAGEMENT

DATE: 1ST AUGUST 2024

DURATION: 3 HOURS

MAXIMUM MARKS: 60

INSTRUCTIONS:

1. Write your registration number on the answer booklet.
2. **DO NOT** write on this question paper.
3. This paper contains **FOUR (4)** questions.
4. Question **ONE** is **compulsory**.
5. Answer any other **TWO** questions.
6. Question **ONE** carries **30 MARKS** and the rest carry **15 MARKS** each.
7. **Write all your answers in the Examination answer booklet provided**

QUESTION ONE

Read the Case Study below carefully and answer the questions that follow:

CASE STUDY

- A. As assistant to the Finance Director of MUA Co, a company that has been listed on the Nairobi Stock Market for several years, you are reviewing the draft Annual Report of the company, which contains the following statement made by the chairman:

'This company has consistently delivered above-average performance in fulfilment of our declared objective of creating value for our shareholders. Apart from 20X2, when our overall performance was hampered by a general market downturn, this company has delivered growth in dividends, earnings and ordinary share price. Our shareholders can rest assured that my directors and I will continue to deliver this performance in the future'.

The five-year summary in the draft Annual Report contains the following information:

Year	20X4	20X3	20X2	20X1	20X0
Dividend per share	2.8p	2.3p	2.2p	2.2p	1.7p
Earnings per share	19.04p	14.95p	11.22p	15.84	13.43p
Price/earnings ratio	22.0	33.5	25.5	17.2	15.2
General price index	$\frac{11}{7}$	113	$\frac{11}{0}$	105	100

A recent article in the financial press reported the following information for the last five years for the business sector within which MUA Co. operates:

Share price growth average increase per year of 20%

Earnings growth average increase per year of 10%

Nominal dividend growth average increase per year of 10%

Real dividend growth average increase per year of 9%

You may assume that the number of shares issued by MUA Co has been constant over the five-year period. All price/earnings ratios are based on end-of-year share prices.

Required

1. Analyse the information provided and comment on the views expressed by the chairman in terms of:
 - (i) growth in dividends per share;
 - (ii) share price growth;
 - (iii) growth in earnings per share.

Your analysis should consider both arithmetic mean and equivalent annual growth rates. **(6 marks)**

2. Calculate the total shareholder return (dividend yield plus capital growth) for 20X4 and comment on your findings. **(2 marks)**
3. With the help of appropriate examples and discuss the factors that should be considered when deciding on a management remuneration package by MUA Co. **(4 marks)**

B. Describe the Agency Problem **(5 Marks)**

C. Discuss six indicators of overtrading in a business **(6 Marks)**

D. A business is considering investing in a new project. They have already spent Ksh 20,000 on a feasibility study which suggests that the project will be profitable.

The headquarters of the company has spare floor space which will be allocated to the project with Ksh7,000 of the current monthly rent allocated to the project.

New equipment costing Ksh2.5m will have to be bought and will be depreciated on a straightline basis over 10 years.

A manager who earns Ksh30,000 per year and currently runs a similar project will also manage the new project taking up 25% of his time.

State whether each of the following items are relevant cash flows and explain your answer. **(7 Marks)**

- I. The cost of the feasibility study.
- II. The rent charged to the project.
- III. The new equipment.
- IV. The depreciation on the new equipment.
- V. The Managers salary.

QUESTION TWO

Thomas Co values, advertises and sells residential property on behalf of its customers. The company has been in business for only a short time and is preparing a cash budget for the first four months of 20X6. Expected sales of residential properties are as follows.

Month	20X5 December	20X6 January	20X6 February	20X6 March	20X6 April
Units sold	10	10	15	25	30

The average price of each property is Ksh180,000 and Thomas Co charges a fee of 3% of the value of each property sold. Thomas Co receives 1% in the month of sale and the remaining 2% in the month after sale. The company has nine employees who are paid on a monthly basis. The average salary per employee is Ksh35,000 per year. If more than 20 properties are sold in a given month, each employee is paid in that month a bonus of Ksh140 for each additional property sold.

Variable expenses are incurred at the rate of 0.5% of the value of each property sold and these expenses are paid in the month of sale. Fixed overheads of Ksh4,300 per month are paid in the month in which they arise. Thomas Co pays interest every three months on a loan of Ksh200,000 at a rate of 6% per year. The last interest payment in each year is paid in December.

An outstanding tax liability of Ksh95,800 is due to be paid in April. In the same month Thomas Co intends to dispose of surplus vehicles, with a net book value of Ksh15,000, for Ksh20,000. The cash balance at the start of January 20X6 is expected to be a deficit of Ksh40,000.

Required

- Prepare a monthly cash budget for the period from January to April 20X6. Your budget must clearly indicate each item of income and expenditure, and the opening and closing monthly cash balances. **(6 marks)**
- Discuss the factors to be considered by Thomas Co when planning ways to invest any cash surplus forecast by its cash budgets. **(3 marks)**
- Discuss the advantages and disadvantages to Thomas Co of using overdraft finance to fund any cash shortages forecast by its cash budgets. **(3 marks)**
- Explain how the Baumol model can be employed to reduce the costs of cash management and discuss whether the Baumol cash management model may be of assistance to Thomas Co for this purpose. **(3 marks)**

QUESTION THREE

Lillies Co is a UK-based company which has the following expected transactions.

One month:

Expected receipt of \$240,000

One month:

Expected payment of \$140,000

Three months:

Expected receipts of \$300,000

The finance manager has collected the following information:

Spot rate (\$ per £):	1.7820 ±
One month forward rate (\$ per £):	.0002
Three months forward rate (\$ per £):	1.7829 ±
	.0003
	1.7846 ±
	.0004

Money market rates for Lillies Co:	Borrowing	Deposit
One year sterling interest rate:	4.9%	4.6
One year dollar interest rate:	5.4%	5.1

Assume that it is now 1 April.

Required

- Discuss the differences between transaction risk, translation risk and economic risk **(6 marks)**
- Explain how inflation rates can be used to forecast exchange rates. **(3 marks)**
- Calculate the expected sterling receipts in one month and in three months using the forward market. **(2 marks)**
- Calculate the expected sterling receipts in three months using a money-market hedge and recommend whether a forward market hedge or a money market hedge should be used. **(2 marks)**
- Discuss how sterling currency futures contracts could be used to hedge the three-month dollar receipt. **(2 marks)**

QUESTION FOUR

A) The Framework of Strategic Cost Management provides a clear plan of attack for addressing costs and decisions that affect organizations, Discuss the three core components of this framework **(6 Marks)**

B) The causes of financial difficulties are specific to each individual company. It is very often not possible to isolate just one cause of financial difficulty due to its high complexity. One of the reasons is the complexity of multiple-causation (pluricausality) because many factors interact in causing financial difficulties.

The second reason is the hierarchical relationship between different patterns. It should be noted that the causes cannot be attributed solely to endogenous or exclusively exogenous factors. Discuss **(6 Marks)**

C) Differentiate between bankruptcy and financial distress **(3 Marks)**