

LAIKIPIA



UNIVERSITY

# UNIVERSITY EXAMINATIONS

FIRST SEMESTER 2025/2026 ACADEMIC YEAR

THIRD YEAR EXAMINATION FOR THE DEGREE  
OF BACHELOR OF COMMERCE

**BFIN 311: CORPORATE FINANCE**

***STREAM: R***

***TIME: 2 HRS***

***DAY: THURSDAY [8.30 A.M-10.30 A.M]***

***DATE: 5/02/2026***

**THIS QUESTION PAPER CONSISTS OF THREE (3) PAGES**

**PLEASE DO NOT OPEN UNTIL THE INVIGILATOR SAYS SO.**

**Answer Question One and any other TWO questions**

**QUESTION ONE (Compulsory, 30 Marks)**

- a) Highlight the advantages and disadvantages of a Stable Dividend Policy. **(10 Marks).**
- b) Critically evaluate the five essential tools of corporate finance management. **(10 Marks).**
- c) XYZ expects a net operating income of Shs.200,000. It has 800,000, 6% debentures. The overall capitalization rate is 10%.

**Required:**

- i) Calculate the value of the firm and the equity capitalization rate (Cost of Equity) according to the net operating income approach. **(5 Marks).**
- ii) If the debentures debt is increased to Shs.1,000,000. What will be the effect on volume of the firm and the equity capitalization rate? **(5 Marks).**

**QUESTION TWO**

- a) Explain the Modigliani-Miller (MM) theorem regarding dividend policy, both with and without taxes. **(10 Marks)**
- b) Critically evaluate the relevance of dividend policy in real-world scenarios, considering factors such as signalling, agency costs, and investor preferences. **(10 Marks)**

**QUESTION THREE**

- a) Two companies Entity A and Entity B are identical in every respect, with the exception of their capital structure. Both Entities have assets of Shs.1,000,000, and both have annual profits before interest and tax of Shs.100,000. However, Entity A is an all-equity company, with 1,000,000 shares of Shs.1, and Entity B is a 50%-geared company, with 500,000 shares of Shs.1 and Shs.500,000 of 8% debt. The rate of taxation is 30%.

**Required:**

- Determine the earnings per share (EPS) of each company. **(6 marks)**
- b) Clarify the concept of 'corporate restructuring' and describe the various types of restructuring **(6 marks)**
- c) Describe the various types and sources of external funding accessible to a corporate entity. **(8 marks)**

**QUESTION FOUR**

- a) Explain the following capital structure theories and indicate their usefulness in capital structure decisions.
- i) Trade off theory. **(5 marks)**
  - ii) Pecking order theory **(5 marks)**
- b) A company paid a dividend of Shs,250,000 this year. The current return to shareholders of companies in the same industry is 12%, although it is expected that an additional risk premium of 2% will be applicable to the company, being a smaller and unquoted company.

**Required:**

The expected valuation of the company, if:

- a) The current level of dividend is expected to continue into the foreseeable future, or **(5 marks)**
- b) The dividend is expected to grow at a rate of 4% pa into the foreseeable future. **(5 marks)**