

LAIKIPIA



UNIVERSITY

UNIVERSITY EXAMINATIONS

FIRST SEMESTER 2025/2026 ACADEMIC YEAR

FOURTH YEAR EXAMINATION FOR THE DEGREE
OF BACHELOR OF COMMERCE

BFIN 412: FINANCIAL MANAGEMENT II

STREAM:

TIME: 2 HRS

DAY: MONDAY [11.30 A.M-1.30 P.M]

DATE: 2/02/2026

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) Evaluate the core assumptions of the Capital Asset Pricing Model (CAPM) and explain how violations of these assumptions might impact its practical application and validity in real-world financial markets. Provide examples of such violations.

(10 Marks)

- b) Wisdom Plc wishes to determine its historic beta coefficient in order to decide the cost of capital. Its financial manager has decided to use linear regression using a sample of 6 months data about the return on Wisdom PLC ordinary shares and the market as a whole. The sample data for the first 6 months are given below:

Monthly Return On:	Month Market Index (%)	Wisdom's shares (%)
1	+7	+4
2	+5	+3
3	-2	-5
4	0	-3
5	+1	+2
6	+2	+4

A dividend of Shs.15 per share was paid by Wisdom plc in six months. The month-end price is shown ex-dix

Required

- a) Use the data above to calculate a beta value for Wisdom Plc. **(6 Marks)**
- b) If the risk-free rate of return is 8% per annum, calculate the required return on the shares of Wisdom Plc **(4 Marks)**
- c) Discuss the foundational contributions of Harry Markowitz's Modern Portfolio Theory (MPT) to investment management. **(10 Marks)**

QUESTION TWO

- a) Explain the concept of risk-neutral valuation in the context of derivative pricing and highlight its underlying assumptions including why it is a fundamental principle in valuing financial derivatives. **(10 Marks)**
- b) The information below relates to the options in TYZ Co.
- The current share price of TYZ Co = Shs.120
 - The exercise price = Shs.100
 - The risk-free interest rate = 12%
 - Standard deviation of return on the shares = 40%
 - Time to Expiry = 3 months

Required:

- a) Calculate the value of this call option. **(6 Marks)**
- b) Differentiate between Call options and put options. **(4 Marks)**

QUESTION THREE

- a) Explain the various types of swaps commonly used in financial markets, and elucidate on their primary characteristics and applications. **(5 Marks)**
- b) Provide examples of how different entities might use these swaps to manage risk or achieve specific financial objectives. **(5 Marks)**
- c) Explain the four basic categories of e-commerce and explain how the dynamic nature of e-commerce has impacted traditional strategic planning **(10 Marks)**

QUESTION FOUR

- a) Explain the concept of "internal reconstruction" versus "external reconstruction" and provide examples of situations where each type of reconstruction would be more appropriate. **(10 Marks)**
- b) X Ltd. is considering the proposal to acquire Y Ltd. and their financial information is given below

Particulars	X Ltd	Y Ltd
No. of Equity shares	1,000,000	600,000
Market price per share (Shs.) 30 18	(Shs.) 30 18	
Market Capitalization	30,000,000	10,800,000

X Ltd. intend to pay Shs. 14,000,000 in cash for Y Ltd., if Y Ltd.'s market price reflects only its value as a separate entity.

Required:

Calculate the cost of merger:

- (i) When merger is financed by cash. **(3 Marks)**
- (ii) When merger is financed by stock. **(7Marks)**