NATIONAL UNIVERSITY OF SCIENCE AND TECHNOLOGY
FACULTY OF COMMERCE
DEPARTMENT OF FINANCE

B.COMM HONORS IN MANAGEMENT, MARKETING, BANKING,
ACCOUNTING, FINANCE, RISK MANAGEMENT AND ACTURIAL SCIENCE

CORPORATE FINANCE CFI 2101

SUPPLEMENTARY EXAMINATION   **SEPTEMBER 2010**

Instructions
- **Answer any five questions**

Question 1

(a) Explain the concept of the Agency Problem/ Agency theory.   (6 marks)
(b) What initiatives can company/shareholders take to minimize the Agency problem?
                                                                                     (14 marks)

Question 2

(a) You are given the following information pertaining to two projects, A and B.

	A	B
Initial Outlay	$120 000	$ 90 000
Cash flow: Year 1	20 000	70 000
Year 2	60 000	20 000
Year 3	20 000	30 000
Year 4	70 000	10 000
Year 5	10 000	10 000

(i)   Use the following the Net Present Value and Internal Rate of Return methods
        to choose the better project.   (8 marks)
(ii)   Why do the two methods sometimes give conflicting results?   (6 marks)
(iii)   Highlight the draw backs of the Internal Rate of Return method. (6 marks)

Question 3

(a) You are given that the Beta of Econet share is 1.5, the return on government securities is 13.5% while the return on the Zimbabwe Stock Exchange is 18%.

(i) Interpret the Beta of the Econet Share   (3 marks)
(ii) Illustrate the given information diagrammatically in relation to the Capital Asset
    Pricing Model.   (5 marks)
(iii) If the actual return on Econet Share is 24%, is the share undervalued or overvalued?
    Explain your answer.   (4 marks)

(b) Given that asset A and B have returns of 24% and 30%, while the standard deviations
    are 40% and 65% respectively.

(i)   Which asset will a rational investor buy? Support your answer with relevant
       calculations.   (4 marks)
(ii)   If the correlation coefficient between the two assets is 0.9 what does this
       signify for diversification purposes?   (4 marks)

Question 4

(a) Given below is information pertaining to asset X and Y.

	X	Y
Expected Return	20%	25%
Standard Deviation	35%	33%
Covariance		0.04

(i) Calculate the Expected return on a portfolio which invests 60% in X and 40% in Y.
                                                                       (3 marks)
(ii)   Calculate the risk of the portfolio in (i) above.
                                                                       (4 marks)
(iii) Investigate the response of risk of portfolio in (i) when the correlation coefficient
       is 0.5 and it is reduced to -0.5. Comment your findings.
                                                                       (8 marks)
(iv)   Find the Minimum Variance Portfolio made up of X and Y.
                                                                       (5 marks)

Question 5

With particular reference to the Zimbabwe Stock Exchange, discuss the Efficient Market Hypothesis. (20 marks)

Question 6

'………..the objective of shareholder value maximization is always superior to the profit maximization objective…………'. Provide a discussion in support of this statement. (20)

End of paper.