

NATIONAL UNIVERSITY OF SCIENCE AND TECHNOLOGY
FACULTY OF COMMERCE
DEPARTMENT OF FINANCE
BACHELOR OF COMMERCE HONOURS DEGREE IN FINANCE
PART IV 2ND SEMESTER SUPPLEMENTARY EXAMINATION – AUGUST 2011
CORPORATE FINANCIAL STRATEGY & RESTRUCTURING [CFI 4201]
TIME ALLOWED : 3 HOURS

Instructions

1. The paper is 3 hours
2. Answer any four questions
3. Electronic calculators may be used.
4. All workings to be shown.
5. Write legibly.

Question 1 **[25 marks]**

- 1.1 The value of a firm is independent of the dividend decision. Prove this statement in the context of MM article of 1951, highlighting the critical assumptions made. [17 marks]
- 1.2 Discuss two other theories on dividend policy that you have come across in your studies. [8 marks]

Question 2 **[25 marks]**

MNO Limited is considering diversifying into the hospitality industry. The industry has an average equity beta of 1.5, an average Debt equity ratio of 20% and an average marginal rate of corporate tax of 35%.

The project is expected to cost \$400 million and generate after tax real asset cashflows of \$100 million per year in years 1 to 5 and \$120m per year thereafter fro the foreseeable future. In addition, the project is expected to generate additional Debt capacity, which will be fully utilized, resulting in Project Debt/Equity ratio of 25%.

- 2.1 Assuming the riskfree rate of return and the market risk premium are 20% and 10% respectively, should the project be undertaken. [17 marks]
- 2.2 State the critical assumptions of the models that you have used in “2.1” above. [8 marks]

