

## DIPLOMA IN INSURANCE

Unit Name: Financial Management

Unit Code: DIP 302

### SAMPLE QUESTION

Mr. Smith is the Finance Manager at Kuredt Insurance company, one of the listed firms in the financial market. He has provided the capital structure of the company as follows:

	KSH.
Ordinary shares @ksh 20	4,000,000
Retained earnings	2,500,000
10% Preference Shares @ Ksh 50	1,500,000
Bank loan	<u>2,000,000</u>
Total capital employed	<u>10,000,000</u>

Additional information:

- The following are the current prices of the securities:

Ordinary shares            Ksh 40

10% Preference shares    Ksh 75

- The company has maintained payment of an ordinary dividend per share of Sh.3.00 and is expected to grow at 5 % per annum in perpetuity. The floatation costs for ordinary share capital are 12% per share.
- The current corporation tax rate is 30%.
- Mr. Smith has been tasked to help raise an additional Ksh 2,000,000 for expansion of the company's facilities.

- a) Determine the cost of capital for each source of finance.            (8 Marks)
- b) Compute the Weighted Average Cost of Capital (WACC) for the company.            5 marks)
- c) Describe the ways in which the manager may reduce the cost in (b) above.            (4 marks)
- d) Explain other functions carried out by Mr. Smith in the company in his capacity.            (6 marks)
- e) Advise on the other possible sources of finance in raising the additional capital.            (6 marks)

- f) Explain the ways in which the insurance company may benefit from its current status in the financial market. (6 marks)