

1903/203

1906/203

1926/204

BUSINESS FINANCE

July 2019

Time: 3 hours

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THE KENYA NATIONAL EXAMINATIONS COUNCIL

CRAFT CERTIFICATE IN SUPPLY CHAIN MANAGEMENT
CRAFT CERTIFICATE IN BUSINESS MANAGEMENT
CRAFT CERTIFICATE IN HUMAN RESOURCE MANAGEMENT

BUSINESS FINANCE

3 hours

INSTRUCTIONS TO CANDIDATES

*This paper consists of **FOURTEEN** questions in **TWO** sections: **A** and **B**.*

*Answer **ALL** the questions in both sections in the answer booklet provided.*

*Show **ALL** your workings clearly.*

Maximum marks for each part of a question are as shown.

Candidates should answer the questions in English.

This paper consists of 6 printed pages.

**Candidates should check the question paper to ascertain that
all the pages are printed as indicated and that no questions are missing.**

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Turn over

SECTION A (32 marks)

Answer **ALL** the questions in this section.

1. Outline **two** differences between debentures and retained earnings, as sources of business finance. (4 marks)
2. Highlight **two** services rendered by commercial banks to their customers. (4 marks)
3. The following information relates to Waka Limited for the last quarter of the year 2017.

Ordinary share capital	200,000 at Kshs. 1 each
Net profit after tax	Kshs. 1,000,000
Ordinary share dividend paid	Kshs. 400,000
Market price per ordinary share	Kshs. 20

Using the information above, calculate each of the following ratios;

- (i) Dividend per share;
- (ii) Earnings per share;
- (iii) Dividend yield;
- (iv) Earnings yield.

(4 marks)

4. State **two** types of policies that may be used in the management of credit in an organization. (2 marks)
5. The following information shows the net cash inflows of Tambako Limited.

Year	Net Cash Inflows (Kshs.)
1	400,000
2	450,000
3	600,000
4	480,000

Initial investment Ksh. 2,000,000

Target return 30%

- (a) Calculate the Accounting Rate of Return (ARR) of Tambako Limited.

- (b) Using the result in (i) above, comment on the performance of the company.

(4 marks)

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6. John intends to buy a car in three years' time, at a cost of Ksh. 1,000,000. At the beginning of the first year, he deposited Ksh. 300,000 in a bank, which pays compound interest at the rate of 10% per annum. At the beginning of the second year, he deposited Ksh. 400,000 in the same bank.
- Calculate the amount John should deposit in the bank at the beginning of the third year to enable him buy the car.

(3 marks)

7. Outline the relationship between business finance and each of the following disciplines:

- (a) Financial Accounting;
(b) Economics.

(4 marks)

8. Sismo Limited has ordinary share capital of Ksh. 1,000,000 with a par value of Ksh. 20 per share. The ordinary shares are currently selling at Ksh. 35 each. The company paid ordinary share dividends totalling Ksh. 100,000 during a particular year.
- Calculate the cost of equity of the company.

(3 marks)

9. The following balances were extracted from the books of account of Viewpoint Limited:

	Ksh.
Fixed Assets	2,000,000
Current Assets	500,000
Current liabilities	150,000
Capital	2,350,000

- (a) Calculate the company's current ratio.
- (b) Compare the ratio in (i) above with the industry's ratio of 2:1.

(2 marks)

10. Highlight **two** advantages of internal financing to an organization.

(2 marks)

Answer **ALL** the questions in this section.

11. (a) Explain **four** measures that an organization may take to shorten its cash operating cycle. (8 marks)

- (b) The following information was extracted from the books of account of Nyakari Limited and Gabo Limited.

	Nyakari Limited	Gabo Limited
	Ksh.	Ksh.
Ordinary share capital	1,400,000	1,000,000
13% preference share capital	50,000	400,000
15% debentures	60,000	100,000
Bank loan (5 years)	90,000	100,000
Total	<u>1,600,000</u>	<u>1,600,000</u>

- (i) Calculate the gearing ratio for each of the companies.
- (ii) Based on the results in (i) above, determine the company that has a higher risk, with regard to lending. (9 marks)

12. (a) Explain **four** functions of merchant banks. (8 marks)

- (b) Kesta Limited intends to borrow Ksh. 4,000,000 to finance either project X or project Y. The following are the expected net cash inflows for each project:

Year	NET CASH INFLOWS	
	Project X	Project Y
	(Ksh.)	(Ksh.)
1	1,500,000	2,000,000
2	1,000,000	1,100,000
3	2,400,000	9,000,000
4	1,200,000	1,500,000

- (i) Calculate the payback period for each project.
- (ii) Based on the results in (i) above, advise the management on the project to invest in. (9 marks)

13. (a) Outline **four** factors which influence the choice of finance for a business.
- (b) The following is the capital structure of Nakum Ventures Limited.

	Ksh.
100,000 ordinary shares of Ksh. 20 each	2,000,000
Retained earnings	800,000
12% preference shares of Ksh. 10 each	1,000,000
13% debentures	900,000

The company paid ordinary dividend of Ksh. 3 per share. The ordinary shares are currently selling at Ksh. 25 per share. The preference shares are selling at Ksh. 16 per share. The corporation tax rate is 30%.

- (i) Calculate the cost of each component of capital.
- (ii) Calculate the Weighted Average Cost of Capital (WACC).

(9 marks)

14. (a) Explain **four** differences between ordinary shares and preference shares. (8 marks)
- (b) The following information relates to material B24 of a firm.

Maximum consumption	7,500 units
Minimum consumption	3,400 units
Lead time	2 - 4 weeks
Economic Order Quantity (EOQ)	10,500

Calculate each of the following:

- (i) Re-order level;
- (ii) Minimum stock level;
- (iii) Maximum stock level;
- (iv) Average stock level.

(9 marks)

Present Value of 1 Received at the End of n Periods

$$PVIF_{r,n} = 1/(1+r)^n = (1+r)^{-n}$$

Period	1%	2%	3%	4%	5%	6%	7%	8%	9%	10%	12%	14%	15%	16%	18%	20%	24%	28%	32%	35%
1	.9901	.9804	.9709	.9615	.9524	.9434	.9346	.9259	.9174	.9091	.8929	.8772	.8696	.8621	.8475	.8333	.8065	.7813	.7576	.7353
2	.9803	.9612	.9426	.9246	.9070	.8900	.8734	.8573	.8417	.8264	.7972	.7695	.7561	.7432	.7182	.6944	.6504	.6104	.5739	.5407
3	.9706	.9423	.9151	.8890	.8638	.8396	.8163	.7938	.7722	.7513	.7118	.6750	.6575	.6407	.6086	.5787	.5245	.4768	.4348	.3975
4	.9610	.9238	.8885	.8548	.8227	.7921	.7629	.7350	.7084	.6830	.6355	.5921	.5718	.5523	.5158	.4823	.4230	.3725	.3294	.2923
5	.9515	.9057	.8626	.8219	.7835	.7473	.7130	.6806	.6499	.6209	.5674	.5194	.4972	.4761	.4371	.4019	.3411	.2910	.2495	.2149
6	.9420	.8880	.8375	.7903	.7462	.7050	.6663	.6302	.5963	.5645	.5066	.4556	.4323	.4104	.3704	.3349	.2751	.2274	.1890	.1580
7	.9327	.8706	.8131	.7599	.7107	.6651	.6227	.5835	.5470	.5132	.4523	.3996	.3759	.3538	.3139	.2791	.2218	.1776	.1432	.1162
8	.9235	.8535	.7894	.7307	.6768	.6274	.5820	.5403	.5019	.4665	.4039	.3506	.3269	.3050	.2660	.2326	.1789	.1388	.1085	.0854
9	.9143	.8368	.7664	.7026	.6446	.5919	.5439	.5002	.4604	.4241	.3606	.3075	.2843	.2630	.2255	.1938	.1443	.1084	.0822	.0628
10	.9053	.8203	.7441	.6756	.6139	.5584	.5083	.4632	.4224	.3855	.3220	.2697	.2472	.2267	.1911	.1615	.1164	.0847	.0623	.0462
11	.8963	.8043	.7224	.6496	.5847	.5268	.4751	.4289	.3875	.3505	.2875	.2366	.2149	.1954	.1619	.1346	.0938	.0662	.0472	.0340
12	.8874	.7885	.7014	.6246	.5568	.4970	.4440	.3971	.3555	.3186	.2567	.2076	.1869	.1685	.1372	.1122	.0757	.0517	.0357	.0250
13	.8787	.7730	.6810	.6006	.5303	.4688	.4150	.3677	.3262	.2897	.2292	.1821	.1625	.1452	.1163	.0935	.0610	.0404	.0271	.0184
14	.8700	.7579	.6611	.5775	.5051	.4423	.3878	.3405	.2992	.2633	.2046	.1597	.1413	.1252	.0985	.0779	.0492	.0316	.0205	.0135
15	.8613	.7430	.6419	.5553	.4810	.4173	.3624	.3152	.2745	.2394	.1827	.1401	.1229	.1079	.0835	.0649	.0397	.0247	.0155	.0099
16	.8528	.7284	.6232	.5339	.4581	.3936	.3387	.2919	.2519	.2176	.1631	.1229	.1069	.0930	.0708	.0541	.0320	.0193	.0118	.0073
17	.8444	.7142	.6050	.5134	.4363	.3714	.3166	.2703	.2311	.1978	.1456	.1078	.0929	.0802	.0600	.0451	.0258	.0150	.0089	.0054
18	.8360	.7002	.5874	.4936	.4155	.3503	.2959	.2502	.2120	.1799	.1300	.0946	.0808	.0691	.0508	.0376	.0209	.0118	.0068	.0039
19	.8277	.6864	.5703	.4746	.3957	.3305	.2765	.2317	.1945	.1635	.1161	.0829	.0703	.0596	.0431	.0313	.0168	.0092	.0051	.0029
20	.8195	.6730	.5537	.4564	.3769	.3118	.2584	.2145	.1784	.1486	.1037	.0728	.0611	.0514	.0365	.0261	.0135	.0072	.0039	.0021
25	.7798	.6095	.4776	.3751	.2953	.2330	.1842	.1460	.1160	.0923	.0589	.0378	.0304	.0245	.0160	.0105	.0046	.0021	.0010	.0005
30	.7419	.5521	.4120	.3083	.2314	.1741	.1314	.0994	.0754	.0573	.0334	.0196	.0151	.0116	.0070	.0042	.0016	.0006	.0002	.0001
40	.6717	.4529	.3066	.2083	.1420	.0972	.0668	.0460	.0318	.0221	.0107	.0053	.0037	.0026	.0013	.0007	.0002	.0001		
50	.6080	.3715	.2281	.1407	.0872	.0543	.0339	.0213	.0134	.0085	.0035	.0014	.0009	.0006	.0003	.0001				
60	.5504	.3048	.1697	.0951	.0535	.0303	.0173	.0099	.0057	.0033	.0011	.0004	.0002	.0001						

* The factor is zero to four decimal places

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