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KIRIRI WOMENS' UNIVERSITY OF SCIENCE AND TECHNOLOGY
UNIVERSITY EXAMINATION, 2018/2019 ACADEMIC YEAR
DIPLOMA IN BUSINESS INFORMATION TECHNOLOGY

DBT 1001 – BUSINESS FINANCE

Date: 11th April, 2018
Time: 2.00pm –4.00pm

INSTRUCTIONS TO CANDIDATES

ANSWER QUESTION ONE (COMPULSORY) AND ANY OTHER TWO QUESTIONS

QUESTION ONE (30 MARKS)

- a) i) What type of compounding would you prefer in your savings accounts? Explain. (2 Marks)
ii) Rodgers just closed a Sh.1, 000,000 business loans that is to be repaid in 4 equal end-of year repayments. The interest rate on the loan is 13%.
Required;
iii) Determine the annual payments to fully amortize the loan (2 Marks)
- b) Prepare an amortization schedule for the loan. (8 Marks)
- b) Explain four limitations of the use of ratios as a basis of financial analysis. (4 Marks)
- c) Briefly explain any three forms of agency relationship in finance (6 Marks)
- d) Describe the characteristics of long term capital investment decisions. (2 Marks)
- e) Distinguish between Working capital and Net working capital (2 Marks)
- f) Discuss the main objectives of a business (4 Marks)

QUESTION TWO (20 MARKS)

- a) Explain some of the factors that have led to growth of financial institutions in Kenya (8 Marks)
- b) Practical problems faced by finance managers in capital budgeting (4 Marks)
- c) The following information was from XYZ feasibility studies. It has studied two investment ventures
Cost is shs 100,000 and shs 160,000 at the beginning of the 4th year and it will generate cash inflows
1-3rd year shs 80,000 and from 4-6th year shs 50,000 per annum.
Initial cost shs 200,000 and shs 80,000 at the beginning of the 4th year and it will generate the
following inflows: 1st – 2nd year is Shs.100, 000 per annum and 3rd – 6th year is Shs.70, 000 per annum
Required; using the cost of finance of 12% compute the P.I. of these two ventures, advise the company
accordingly. (8 Marks)

QUESTION THREE (20 MARKS)

- a) Explain any 3 types of preference shares (6 Marks)
- b) Preference shares are often considered to be hybrid securities since they have features similar to both common shares and debt finance. Explain how they are similar to;
- i) Common shares (7 Marks)
 - ii) Debt finance (7 Marks)

QUESTION FOUR (20 MARKS)

- a) An extract from the finance statements of Kango Ltd is shown below:

Issued share capital:	Shs.
150,000 ordinary shares of Sh.10 each fully paid	1,500,000
10% loan stock 2010	2,000,000
Share premium	1,500,000
Revenue Reserve	<u>7,000,000</u>
Capital employed	<u>12,000,000</u>

The profit after 30% tax is Sh.600, 000. However, interest charge has not been deducted. Ordinary dividend payout ratio is 40% and the current market value of ordinary shares Shs.36

Required

- i) Return on capital employed
 - ii) Earnings per share (EPS)
 - iii) Price earnings ratio (P/E)
 - iv) Book value per share
 - v) Gearing ratio
 - vi) Market to book value per share (10 Marks)
- b) Distinguish the following;
- i) Stakeholders and shareholder of a firm (2 Marks)
 - ii) Ordinary annuity and annuity due (2 Marks)
 - iii) Profit maximization and shareholders wealth maximization (6 Marks)

QUESTION FIVE (20 MARKS)

- a) The basic strategies that should be employed by the business firm in managing its cash (6 Marks)
- b) Given the following capital structure.

	Shs.M
Ordinary share capital Sh.10 par value	400
Retained earnings	200
10% preference share capital Sh.20 par value	100
12% debenture Sh.100 par value	<u>200</u>
	<u>900</u>

Additional information

1. Corporate tax rate is 30%
2. Preference shares were issued 10 years ago and are still selling at par value MPS = Par value
3. The debenture has a 10 year maturity period. It is currently selling at Sh.90 in the market.
4. Currently the firm has been paying dividend per share of Sh.5. The DPS is expected to grow at 5% p.a. in future. The current MPS is Sh.40.

Required

- i) Cost of equity (K_e) (2 Marks)
- ii) Cost of preference capital (K_p)(2 Marks)
- iii) Cost of debt (K_d) (2 Marks)
- iv) WACC (4 Marks)
- v) What are the weaknesses associated with WACC when used as the discounting rate, in project appraisal. (4 Marks)