



# MACHAKOS UNIVERSITY

University Examinations for 2020/20201Academic Year

SCHOOL OF BUSINESS AND ECONOMICS

DEPARTMENT OF ACCOUNTING BANKING AND FINANCE

SECOND YEAR SECOND TERM EXAMINATION FOR

CERTIFICATE IN BUSINESS MANAGEMENT

CERTIFICATE IN SUPPLY CHAIN MANAGEMENT

**BUSINESS FINANCE**

**DATE: 3/6/2021**

**TIME: 8.30-11.30 AM**

---

## INSTRUCTIONS:

*Answer any FIVE questions*

*Show all your working*

*All questions carry Equal marks*

*The questions should be answered in English*

1. a) Explain FIVE ways in which business finance is important to a business organization (10 marks)
- b) Explain five factors that the management should consider when choosing a source of finance for a business organization. (10 marks)
2. a) Explain **four** functions of commercial banks in Kenya (8 marks)
- b) The following financial statements relate to ABC limited Income statement for the year ended 31 December 2017

	Ksh
Sales	10,480,000
Less cost of sales	4,380,000
Gross profit	<b>6,100,000</b>
Less operating expenses	2,700,000
Profit before tax	<b>3,400,000</b>
Less corporation tax @ 30%	1,020,000
Net profit after tax	<b>2,380,000</b>

**Statement of financial position as at 31 December 2017**

<b>Assets</b>	<b>Ksh</b>
Land and buildings	47,000,000
Plant and equipment	26,000,000
Motor vehicle	11,500,000
Inventory	2,700,000
Accounts receivable	1,100,000
Bank	850,000
	<b>89,150,000</b>
<b>Capital and liabilities</b>	
5,000,000 ordinary shares @ sh 10 each	50,000,000
Retained profits	7900,000
1,200,000 10% preference shares @ sh 10 each	12,000,000
8% debentures	15,000,000
Accounts payable	4,250,000
	<b>89,150,000</b>

Calculate the following ratios

- i. Return on owners' equity
  - ii. Gross profit margin
  - iii. Acid test ratio
  - iv. Total assets turnover ratio
  - v. Interest coverage ratio
  - vi. Debtors turnover ratio (12 marks)
3. a) Explain three theories of business finance (6 marks)
- b) Assume a Macan construction company has a target capital structure of 40% debt and 60% common stock equity. Other key information is as follows;
- i.  $P_0 = \text{sh } 160$
  - ii. Dividend per share in the end of the last period = sh 10.18
  - iii. Growth rate = 12%
  - iv. The cost of borrowing is 14% and the tax is 40%

**Calculate;**

1. The required rate of return (4 marks)
2. After tax cost of capital (3 marks)

- c) Assume the company needs to raise sh 90 million to keep its capital structure on the target. The components value being 8.2% and 19.0% for debt and equity respectively. What is;
- i. The company's capital structure (2 marks)
  - ii. Weighted average cost of new capital (5 marks)
4. a) Explain the two objectives of working capital and the tradeoff that exists between the objectives (6 marks)
- b) Explain the difference between marginal cost of capital and weighted average cost of capital (4 marks)
- c) Tablers LTD had the following capital structure;

	Ksh
Ordinary share capital	200,000
Reserves	160,000
11.5% preference shares	100,000
10% Debentures	50,000
Capital employed	<b>510,000</b>

Ordinary shareholders of the company are used to expecting at least 20% dividends which are normally covered by 2 times after tax profits, and the balance of profits is transferred to reserves.

Calculate;

- a) the rate of growth of the equity (4 marks)
  - b) the weighted average cost of capital (6 marks)
5. a) Mr Njoroge wants to raise additional capital in order to expand his business. He is considering different methods to raise the additional finance. Explain to him 5 different sources of finance he can use to raise the additional capital. (10 marks)
- b) Explain factors leading to the failure of financial institutions in Kenya (10 marks)
6. a) Explain five advantages of having adequate working capital in a business(10 marks)
- b) Working capital is a crucial aspect in any business. Explain five factors that should be considered when deciding the working capital requirement of a business. (10 marks)
6. a) Explain the 3 motives for holding stock (6 marks)
- b) What is meant by "Cost of Capital" and what is the significance of cost of capital in a business? (6 marks)
- c) Explain the limitations of having excessive working capital in a business (8 marks)