

CHUKA



UNIVERSITY

UNIVERSITY EXAMINATIONS

**SECOND YEAR EXAMINATION FOR THE AWARD OF
DEGREE OF BACHELOR OF COMMERCE, PROCUREMENT AND LOGISTICS AND
ENTREPRENEURSHIP MANAGEMENT**

BCOM 231: BUSINESS FINANCE

STREAMS: Y2 S2

TIME: 2 HOURS

DAY/DATE: TUESDAY 13 /07/ 2021

11.30 AM – 1.30 PM

INSTRUCTIONS:

- Answer Question One and any other TWO questions.
- Do not write on the question paper

QUESTION ONE

- a) Financial ratio analysis is conducted by managers, equity investors, suppliers and creditors. Describe the importance of ratio analysis to each of these groups.[6 Marks]
- b) The following dividend pattern relates to A nkara limited for the last five years. Calculate the value of the share in the year 2019. If the required rate of return is 15%. [4 Marks]

Year	Dividend Per Share
2015	12
2016	13.5
2017	14
2018	15.2
2019	16.8

- c) Outline the features of a good investment appraisal techniques. [4 Marks]
- d) Jabez expects to receive sh 250,000 in 10 years. How much should he deposit each year at an interest rate of 18% to accumulate to the required amount. [3 Marks]

e) Royalty Company manufactures a product “pent” which has the following information.

Year	2013	2014	2015	2016	2017
Production in units	3,000	3,200	4,000	4,500	5,000
Selling price per unit	25	40	35	30	35
Variable cost	40,000	45,000	50,000	55,000	65,000

Additional Information

- The Initial cost is sh 150,000
- The fixed costs per year is sh 8000
- Depreciation is charged on straight line basis
- The tax rate is 30%
- The required rate of return is 15%

Required;

- | | | |
|------|-------------------------|-----------|
| i. | Net Cashflows | [5 Marks] |
| ii. | Net present value | [2 Marks] |
| iii. | Profitability Index | [2 Marks] |
| iv. | Internal rate of return | [4 Marks] |

QUESTION TWO

a) A company is considering investing in a project that promises profit before depreciation and tax of sh.30,000 each year for four years. The cost of the project is sh.100,000 with sh.20,000 as the scrap values depreciation is on straight line method and the tax rate is 30%.

Required Accounting rate of return and the payback period of the project. [5 Marks]

b) Explain the following sources of finance

- | | | |
|------|----------------------|-----------|
| i. | Venture Capital | [2 Marks] |
| ii. | Factoring of debtors | [2 Marks] |
| iii. | Debentures | [2 Marks] |

c) A company currently pays a dividend of sh 4 per share and this dividend is expected to grow at 15% for 3 years, 12% for the next 3 years after which it will fall to a constant rate of 8% thereafter. The cost of capital is 15%

Required: Determine the intrinsic value of the company's share [9 Marks]

QUESTION THREE

a) A firm has the following capital structure as at 31.12.2018

	shs '000'
Ordinary Share Capital (shs 20 par)	12,000
Retained Earnings	5,000
10% Preference Share Capital (shs 24 par)	2,500
15% Debt (shs.150 par)	6,000
12% Long term loan	8,000
	16,000

Additional Information

- i. Corporate tax rate is 30%
- ii. Preference shares were issued 10 years ago and are still selling at par value
- iii. The 15% debt has a 10 year maturity period. It is currently selling at sh.200 in the market.
- iv. The firm expects to pay a dividends of shs.5 per share and the dividend per share is expected to grow at 6% in the future. The market price per share is shs.50 including sh.10 as floatation cost.
- v. The long term loan is currently valued at sh.12,000,000

Required

- i) The components cost of capital [12 Marks]
 - ii) State the reasons why the cost of debt is cheaper than cost of equity. [3 Marks]
- b) Discuss the factors that affect the cost of finance. [5 Marks]

QUESTION FOUR

a) The following information was extracted from the books of Instagram Limited for the year ended 31.12.2017

Statement of financial position

	SH.
Cash	80,500
Receivables	336,000
Inventories	241,500
Total current assets	658,000
Net fixed assets	292,500
	950,500

Accounts payable	132,000
Notes payable	84,000
Other current liabilities	117,000
Total current liabilities	333,000
Long-term debt	256,500
Equity @Sh.25	361,000

Income Statement

Sales	1,607,500
Cost of goods sold	1,392,500
Gross profit	215,000
Selling, general and administrative expenses	145,000
Earnings before interest and taxes (EBIT)	70,000
Income taxes (40%)	18,200
EAT	27,300
Preferred dividends	1,800
	25,500
Ordinary dividend	15,000
Retained Profits	10,500

Required; Calculate

- i. Gross profit margin
- ii. Debt ratio
- iii. Dividend per share
- iv. Earnings per share

- v. Dividend cover [10 Marks]

b) A conflict may arise between shareholders and managers as a result of managers pursuing their own interest. As a finance student discuss the following:

- i. The reasons for conflict between shareholders and managers of company. [6 Marks]
- ii. Explain the solutions for conflict between shareholders and managers. [4 Marks]

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