CHUKA UNIVERSITY

UNIVERSITY EXAMINATIONS

**EXAMINATION FOR THE AWARD OF DEGREE OF BACHELOR OF COMMERCE AND BACHELOR OF PROCUREMENT**

**BCOM 231: BUSINESS FINANCE**
**STREAMS: BCOM Y2S2 (ODEL)** **TIME:2 HOURS**
**DAY/DATE: THURSDAY 07/08/2025** **8.30A.M. –10.30 A.M**

**Question One**

a) Agency conflict arises when agents pursue their own interests rather than the interests of the principle. Discuss the 3 causes of conflict between shareholder and creditors and any 2 solutions to this conflict (10 marks)

b) A company is considering to invest in a project that promises profit before depreciation and tax of sh 120,000 each year for 5 years. The cost of the project is sh 200,000 with sh 50,000 as the scrap value. Tax rate is 30%, depreciation is on straight line method. Required; Calculate the Accounting Rate of Return (5 marks)

c) Outline the features of a good investment appraisal technique (6 marks)

d) Kendi deposits sh 88,000 at the end of each year for 15 years at 12% interest rate. Calculate the amount she will receive after 15 years (3 marks)

e) Describe the different types of investment that a business can undertake (6 marks)

**Question Two**

a) Describe the significance of determining the cost of capital for a business (4 marks)

b) Outline the advantages of shareholders wealth maximization principle (4 marks) c)The following capital structure belongs to Kenyatta limited

| | |
|---|---|
| Ordinary shares (sh 50 par) | 1,000,000 |
| Retained Earnings | 500,000 |
| 15% Preference shares (sh 20 par) | 800,000 |
| 15% Debentures (sh 40 par) | 1,200,000 |
| | **3,500,000** |

**Additional information**

i) The company paid a dividend of sh 5 per share which is expected to grow at 11% and the market price of the ordinary shares is sh 60

ii) The preference shares will mature in 5 years and are currently selling at sh 15

iii) The debenture will mature in 10 years and is currently selling at sh 60

iv) Tax rate is 30%

Required: compute the Weighted Average Cost of Capital (WACC) (12 marks)

**Question Three**

a) Describe the non- financial goals of business enterprise (6 marks)

A project with an initial outlay of sh 100,000 has the following information

| Years | Profits before depreciation and tax |
|---|---|
| 1 | 50,000 |
| 2 | 65,000 |
| 3 | 40,000 |
| 4 | 55,000 |
| 5 | 70,000 |

**Additional information**

- Cost of capital is 10%
- Depreciation is on straight line method
- Tax rate is 20%

Required: calculate the Payback Period, Net Present Value and Profitability Index (14 marks)

**Question Four**

a) Explain the reasons for valuation of securities by a business (6 marks)

b) Outline the advantages of Net present value method of appraising projects (3 marks)

b) A company paid a dividend of sh 8 per share. The dividend is expected to grow at 5% for 3 years, 10% for 3 years after which it will fall to a constant rate of 12%. Calculate the intrinsic value of the share if the cost of capital is 15% (8 marks)

c) Star limited has invested in a 10 year 12% sh 7500 bond which is currently trading at sh 7000. The required rate of return is 16%. Calculate the intrinsic value of the bond and advice on whether it would be advisable to sell the bond (3 marks)

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