



MUEO

**MOI UNIVERSITY**

**OFFICE OF THE DEPUTY VICE CHANCELLOR, ACADEMIC  
AFFAIRS, RESEARCH & EXTENSION**

**UNIVERSITY EXAMINATIONS  
2015/2016 ACADEMIC YEAR**

***SECOND YEAR END OF SEMESTER EXAMINATIONS***

**FOR THE DEGREE OF  
BACHELOR OF BUSINESS MANAGEMENT**

**EXAM CODE:-       BBM 224**

**COURSE TITLE:-   BUSINESS FINANCE**

**DATE:- 26<sup>TH</sup> APRIL, 2016       TIME:- 9.00 A.M. – 12.00 NOON.**

---

**INSTRUCTION TO CANDIDATES**

➤ **SEE INSIDE.**

**THIS PAPER CONSISTS OF (3) PRINTED PAGES**

**PLEASE TURN OVER**

UNIVERSITY EXAMINATION 2015/2016 ACADEMIC YEAR 2<sup>ND</sup> SEMESTER

BBM 224: BUSINESS FINANCE

Instructions to Candidates: Question ONE and any other THREE questions.

QUESTION ONE

- a. State and explain factors considered in choosing an appropriate source of capital. (6marks)
- b. A milling company has proposal to purchase a new machine subject to initial screening processes. The machine will cost Sh.2,200,000 and has an estimated useful life of five years at the end of which the disposal value will be zero. Sales revenue to be generated by the new machine is estimated as follows

Year	Revenue (Sh.'000')
1	1,320
2	1,440
3	1,560
4	1,600
5	1,500

Additional information

- Operating costs are estimated to be Sh.700,000 per annum.
- Prevailing tax rate is 30% payable in the year in which revenue is received.
- Machine is to be written off at a fixed annual rate of 20% on cost. *dep.*
- Financial accounting statements issued by the company in recent years shows that profits after tax have averaged 18% on total assets.

Calculate the Net Present Value (N.P.V) on this investment proposal (13 marks)

- c). Briefly explain the importance of working capital management to small and medium-sized enterprises (SMEs) (6 marks)

(Total: 25 marks)

QUESTION TWO

- a). State and explain ways of solving shareholders management conflict of interest (8 marks)

- b). Highlight the mandatory requirements that a company must fulfill before being listed at the Nairobi securities exchange( N.S.E) (10 marks)

- c). State and explain theories explaining why companies pay dividends to its shareholders (7 marks)

(Total: 25 marks)

### QUESTION THREE

- a. Discuss the importance and limitations of Executive share Option Plans (ESOPs) in mitigating management/shareholder agency conflicts. ( 8 marks)
- b. Bandaptai limited company management team would like to extend their business to make use of the favourable trading conditions. The company intends to raise the additional finance from various sources as follows:-
- To issue 200,000 ordinary shares (Shs 10 nominal value) at Shs. 12 each.
  - To issue 400,000 12% Preference Share (Shs. 6 nominal value) at Shs. 9 each
  - To issue 100,000 11% preference shares (shs12 nominal value) at shs. 16 each
  - To issue 200,000 15% Debentures of shs.110 at shs.100 each.

The company's corporate tax rate is 30% and ordinary shareholders are paid a dividend of 10%.

#### Required:

- i). The total amount the company will raise if the plan is realized. (8 marks)
- ii). The average cost of the additional finance (9marks)
- (Total: 25 marks)

### QUESTION FOUR

- a). State and explain factors that influence capital structure decisions for a Firm (9 marks)
- b). Baringo ltd. has the following capital structure:

	Sh. "000"
Long -term debt	3,600
Ordinary share capital	6,500
Retained earnings	4,000

The finance manager of Baringo ltd. has a proposal for a project requiring sh .45 million. He has proposed the following method of raising the funds.

- Utilize all the existing earnings. *no tax*
- Issue 100,000 10% preference shares at the current market price of sh.100 per share which is the same as the par value.
- Issue 3,000 10% debentures at the current market price of sh 1,000 per debenture.

#### Additional information:

- i. Currently, Baringo Ltd. Pays a dividend of sh. 5 per share which is expected to grow at the rate of 6% due to increased returns from the intended project. Baringo Ltd.'s price/earnings (P/E) ratio and earnings per share (EPS) are 6 and sh 9 respectively.
- ii. The ordinary shares would be issued at a floatation cost of 10% based on the market price.
- iii. The debenture par value is sh 1,100 per debenture.
- iv. The corporate tax rate is 30%

**Required:**

Calculate Baringo Ltd's weighted average cost of capital (WACC). (15 marks)

(Total: 25 marks)

**QUESTION FIVE**

- a. State and explain three motives of holding cash by a firm (6 marks)
- b. Discuss key functions performed by financial institutions in an economy (12marks)
- c. Explain why the weighted average cost of capital (W.A.C.C) of a firm that uses relatively more debt capital is generally lower than that of a firm that uses relatively less debt capital. (5marks)

(Total: 25 marks)

**QUESTION SIX**

a). Differentiate between the following pairs of terms:

- i. Primary market and secondary market (6 marks)
- ii. Capital structure and financial structure. (6 marks)

b). Ethical responsibility arises not as a result of legal requirement but as a moral imperative for companies to operate in an ethical and fair manner. Discuss the main features in which the ethical responsibility of a company is discharged (13 marks)

(Total: 25 marks)

\*\*\*\*\*END\*\*\*\*\*

