



MASENO UNIVERSITY
UNIVERSITY EXAMINATIONS 2016/2017

**FIRST YEAR SECOND SEMESTER EXAMINATIONS FOR THE
DIPLOMA IN BUSINESS ADMINISTRATION**

HOMA-BAY CAMPUS

ADB 0107: BUSINESS FINANCE

Date: 11th December, 2016

Time: 9.00 – 12.00 noon

INSTRUCTIONS:

- Answer question ONE (compulsory) and any other THREE questions.



Question One

Japith Trading Co. Ltd contemplates to raise debt finance totaling Ksh 1,000,000. It will be required to pay an annual interest of 10%. This money can be invested in one of the following two projects - A or B, which will generate the following cash inflows

Period	Project A	Project B
Year	(Kshs)	(Kshs)
1	600,000	500,000
2	160,000	40,000
3	500,000	100,000
4	100,000	600,000
5	40,000	500,000

Required

Using the following methods, advise the management accordingly as to which of the two projects would be viable:

- (a) Pay Back Period (10mks)
- (b) Net Present Value (10 mks)
- (c) Profitability Index (5 mks)

Question Two

- (a) State and explain five causes of conflict of interest between shareholders and management (10 mks)
- (b) What are the solutions to conflict of interest between shareholders and management mentioned above? (5 mks)

Question Three

Homa Bay Investment Company Ltd has had good trading period and wants to raise further finance from the following sources:

To issue 100,000 ordinary shares of shs 10 at shs 15 each

To issue 100,000 10% preference shares of shs 10 at shs12 each

To issue 100,000 15% debentures of shs 100 at shs 90 each

To raise a medium term loan of shs 5,000,000 from a financial institution at an interest rate of 20% per annum

This company will pay an annual dividend of 14% to ordinary shareholders.

Corporation tax will be 50%

Required

- (a) Compute the total amount that this company will raise if this plan is realized
(5 mks)
- (b) Work out the Weighted Average Cost of Capital (WACC)
(10 mks)

Question Four

The following information was extracted from the books of Chakula Co. Ltd. It is financed partly by ordinary share capital of 200,000 shares @ shs 10 selling @ shs 25 in the S.E. This co. reported a profit of shs 1,000,000 before tax and intends to declare a dividend of 30% on ordinary shares and preference dividend equivalent to 10% of ordinary share dividends.

Required

Compute:-

- (i) Earnings Per Share (5 mks)
- (ii) Earnings Yield (5 mks)
- (iii) Price Earnings Ratio (5 mks)

Question Five

- (a) Explain five factors that determine the working capital needs of a company (10 mks)
- (b) Define Cash Budget (2 mks)
- (c) State and explain the three steps involved in preparation of a cash budget (3 mks)

Question Six

(a) Explain 5 sources of finance available to a company. (5mks)

(b) A project has a cost of Kshs 324,000 and is expected to have a useful life of 3 years. The cash inflows expected are Kshs 160,000, Kshs 120,000 and Kshs 140,000 at the end of 1, 2 and 3 years respectively.

Required

Calculate the project's IRR using interpolation and advise the management accordingly if cost of capital under acceptance criterion is 10%. (10 mks)