



MASENO UNIVERSITY

UNIVERSITY EXAMINATIONS 2012/2013

SECOND YEAR FIRST SEMESTER EXAMINATIONS FOR THE DIPLOMA IN BUSINESS ADMINISTRATION (HOMA BAY CAMPUS)

ADB 0107: BUSINESS FINANCE

Date: 27th July, 2013

Time: 2.00 – 4.00pm

INSTRUCTIONS:

- ◆ Section A: Question is Compulsory
- ◆ Section B: Answer any TWO questions.



SECTION A.(COMPULSORY)

QUESTION ONE

A firm is considering the purchase of a machine. Two machines A and B are available; each costing Ksh.50000. in comparing the profitability of these machines a discount rate of 10% is to be used. Earnings after taxation are expected to be as follows:

Year	Machine A cash inflows	Machine B cash inflows
1	15000	5000
2	20000	15000
3	25000	20000
4	15000	30000
5	10000	20000

You are also given the following data:

Year	1	2	3	4	5
P.v. Factor @10%	0.909	0.826	0.751	0.683	0.621

Evaluate the project using:

- The pay-back period (6 marks)
- The accounting rate of return (7 marks)
- The net present value (10 marks)
- The profitability index (7 marks)

SECTION B (ANSWER ANY TWO QUESTIONS)

QUESTION TWO

- Define agency relationship from the context of a public limited company and briefly explain how this arises. (6 marks)
- Highlight the various measures that would minimize agency problems between the owners and the management. (6 marks)
- Evaluate any three factors that may be responsible for the slow growth in the number of companies seeking listing at the Nairobi Stock Exchange or Stock Exchange in your country. (8 marks)

QUESTION THREE

- a) What are the practical difficulties of a small scale enterprise wishing to obtain credit to expand production? (10 marks)
- b) Distinguish between internal and external sources of finance for a limited liability company. (10 marks)

QUESTION FOUR

- a) Explain why proper working capital management is important for the financial success of a company. (4 marks)
- b) ABC Ltd. makes cash payments of Shs.10,000 per week. The interest rate on marketable securities is 12% and every time the company sells marketable securities, it incurs a cost of Shs.20.

Required

- (i) Determine the optimal amount of marketable securities to be converted into cash every time the company makes the transfer. (4 marks)
- (ii) Determine the total number of transfers from marketable securities to cash per year. (4 marks)
- (iii) Determine the total cost of maintaining the cash balance per year. (4 marks)
- (iv) Determine the firm's average cash balance. (4 marks)

QUESTION FIVE

- a) Discuss the factors that influence the cost of capital (10 marks)
- b) Explain the reasons why firms in the same industry with equal earnings and share capital would pay different amount of dividends? (10 marks)