

1903/203  
1906/203  
1926/203  
BUSINESS FINANCE  
July 2022  
Time: 3 hours



THE KENYA NATIONAL EXAMINATIONS COUNCIL

CRAFT CERTIFICATE IN SUPPLY CHAIN MANAGEMENT  
CRAFT CERTIFICATE IN BUSINESS MANAGEMENT  
CRAFT CERTIFICATE IN HUMAN RESOURCE MANAGEMENT

BUSINESS FINANCE

3 hours

### INSTRUCTIONS TO CANDIDATES

*This paper consists of TWO sections: A and B.*

*Answer ALL the questions from the two sections in the answer booklet provided.*

*Show all your workings clearly.*

*Maximum marks for each part of a question are as shown.*

*Candidates should answer the questions in English.*

**This paper consists of 5 printed pages.**

**Candidates should check the question paper to ascertain that all the pages are printed as indicated and that no questions are missing.**

**SECTION A (32 marks)**

Answer **ALL** questions in this section.

1. State **three** sources of finance for a business organization. (3 marks)
2. Outline **four** component costs of capital in a firm. (4 marks)
3. Teda Limited issued a Ksh. 1,000,000, 8% debenture at par. The corporation tax rate is 30%. Determine the cost of the debenture. (3 marks)
4. Highlight **four** functions of the Central Bank of Kenya. (4 marks)
5. Mary intends to invest Ksh. 2,000,000 in a project. The following are the expected net cash inflows from the project:

Year	1	2	3	4	5
Net cash inflows (Ksh)	400,000	300,000	600,000	800,000	200,000

Determine the PayBack Period (PBP) of the project.

(3 marks)

6. Distinguish between business finance and private finance. (2 marks)
7. Jane expects to receive Ksh. 600,000 from a pension fund at the end of 5 years. The discounting rate is 12%. Calculate the present value of this amount. (3 marks)
8. Differentiate between cash cycle and cash turnover, as used in working capital management (2 marks)
9. Outline **four** types of inventories in a manufacturing firm. (4 marks)
10. The following information relates to Waku Limited for the year ended 31 December 2021:

Net profit before interest and tax - Ksh 200,000  
18% long term debt - Ksh 100,000

Calculate the interest coverage ratio.

(4 marks)

**SECTION B (68 marks)**

*Answer ALL questions in this section.*

11. (a) Explain **four** uses of finance in a business organization. (8 marks)
- (b) Beta Limited intends to purchase either machine X or machine Y, each costing Ksh. 500,000. The following are the expected net profits before tax during the useful life of the machines:

Year	Machine X (Ksh)	Machine Y (Ksh)
1	100,000	50,000
2	180,000	250,000
3	200,000	100,000
4	200,000	200,000
5	100,000	300,000

The corporation tax rate is 30%

- (i) Determine the Accounting Rate of Return (ARR) for each project;
- (ii) Based on the results in (i) above, advise the management on the machine to purchase. (9 marks)
12. (a) Explain **four** features of preference shares as a source of business finance. (8 marks)

- (b) A company intends to select an optimal capital structure. The following are the options available:

Option	Debt (Ksh)	Equity (Ksh)	After tax cost of debt	Cost of equity
A	4,000,000	1,000,000	10%	15%
B	2,500,000	2,500,000	7%	12%
C	2,000,000	5,000,000	6%	11%

- (i) Calculate the weighted average cost of capital (WACC) under each option.
- (ii) Based on the results in (i) above, advise the management on the optimal capital structure to select.

(9 marks)

13. (a) Explain **four** functions of investment banks in a country. (8 marks)
- (b) Peter borrowed a loan amounting to Ksh. 2,000,000 from a bank that is to be repaid in 6 equal annual instalments. The interest rate of the loan is 12% per annum. Prepare a loan amortization schedule. (9 marks)
14. (a) Explain **four** objectives of ratio analysis in business decision making. (8 marks)
- (b) The following data relates to a stock item B40 in a manufacturing firm.

Normal usage (units)	220 per day
Minimum usage (units)	100 per day
Maximum usage (units)	280 per day
Lead time	25-3- days
Economic Order Quantity (EOQ)	10,000

Determine the:

- (i) re-order level;
- (ii) minimum stock level;
- (iii) maximum stock level;
- (iv) average stock level.

(9 marks)