

1903/203  
1906/203  
1926/203  
**BUSINESS FINANCE**  
November 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** questions in **BOTH** sections in the answer booklet provided.*

*All questions carry equal marks.*

*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. Outline four short-term sources of business finance. (4 marks)
2. State the difference between average cost of capital and marginal cost of capital. (2 marks)
3. A company intends to issue ordinary shares at a par value of Ksh 100. The floatation costs are expected to be 5% of the share price. The company recently paid an ordinary dividend of Ksh 4 per share. The dividends are expected to grow at the rate of 7% per annum. Calculate the cost of equity. (3 marks)
4. Highlight four roles played by commercial banks in a country. (4 marks)
5. The following information relates to two projects: A and B.

	Project	
	A	B
	(Ksh)	(Ksh)
Initial cost	2,000,000	2,500,000
Present value of cash inflows	2,500,000	1,900,000
	25,000,000	

- (i) Calculate the Profitability Index (PI) of each project.
  - (ii) Using the results in (i) above, advise the management on the project to invest in. (3 marks)
6. Distinguish between Business Finance and Financial Accounting. (2 marks)
  7. An investor plans to deposit Ksh 50,000 in a bank account at the beginning of each year for the next 10 years. The discounting rate is 10%. Calculate the present value of the amount. (3 marks)
  8. Outline three parties with whom a company may negotiate a reduction in cash outflow. (3 marks)
  9. State four types of holding costs in a firm. (4 marks)
  10. The current ratio and quick ratio of a company are 4 : 1 and 2.5 : 1, respectively. The value of inventory is Ksh 150,000. Determine the:
    - (i) current assets;
    - (ii) current liabilities. (4 mark)

**SECTION B (68 marks)**

*Answer ALL questions in this section.*

11. (a) Explain **four** ways in which business finance may be significant to a firm. (8 marks)
- (b) John intends to invest Ksh 1,500,000 in a project. The following are the expected net cash inflows from the project.

Year	Net cash inflows (Ksh)
1	400,000
2	600,000
3	500,000
4	400,000
5	200,000

The cost of capital is 14%.

- (i) Determine the Net Present Value (NPV) of the project.
- (ii) Based on the results in (i) above, advise John on whether to invest in the project or not. (9 marks)
12. (a) Explain **four** disadvantages of retained earnings as a source of business finance. (8 marks)
- (b) The ordinary shares of Kwetu Limited are currently trading at Ksh 50 each. The company expects to pay an ordinary dividend of Ksh 2.50 per share. The dividend is expected to grow at the rate of 6% per annum.
- (i) Determine the company's cost of equity.
- (ii) Based on the results in (i) above, determine the market price per share, if the dividend growth rate is:
- I. 8%
- II. 7%. (9 marks)
13. (a) Explain **four** factors that may contribute to the failure of indigenous financial institutions in Kenya. (8 marks)

- (b) Mary received a lump sum pension amounting to Ksh 5,000,000. She is considering investing the amount in either of the following options:

**Option I**

Invest in a bank paying interest at the rate of 12% per annum, compounded annually.

**Option II**

Invest in a bond paying interest at the rate of 14% per annum, compounded semi-annually.

- (i) Determine:

- I. the amount that will be in her account at the end of the 5 years under each option;
- II. the interest earned under each option\*

- (ii) Based on the results in (II) above, advise Mary on the option to select.

(9 marks)

14. (a) Outline **four** areas in which the concept of time value of money may be applied in a business. (8 marks)

- (b) The following is an extract from the books of account of Peta Pata Limited for the year ended 31 December 2021.

	<b>Ksh</b>
Credit sales	1,750,000
Trade creditors	180,000
Bills receivable	96,000
Bills payable	104,000
Credit purchases	840,000
Trade debtors	118,000

(Take 1 year = 365 days)

Calculate the:

- (i) trade receivable turnover ratio;
- (ii) average collection period;
- (iii) trade payable turnover ratio;
- (iv) average payment period.

(9 marks)



Table A Present Value of Sh 1 Received at the End of n Periods:

$$PVIF_{r,n} = 1/(1+r)^n$$

Period	1%	2%	3%	4%	5%	6%	7%	8%	9%	10%	12%	14%	15%	16%	18%	20%	24%	28%	32%	36%
1	.9901	.9804	.9709	.9615	.9524	.9434	.9346	.9259	.9174	.9091	.8929	.8772	.8696	.8621	.8475	.8333	.8065	.7813	.7576	.7353
2	.9803	.9612	.9428	.9246	.9070	.8900	.8734	.8573	.8417	.8264	.7972	.7685	.7561	.7432	.7182	.6944	.6504	.6104	.5736	.5407
3	.9706	.9423	.9151	.8890	.8638	.8396	.8163	.7938	.7722	.7513	.7118	.6750	.6575	.6407	.6086	.5787	.5245	.4768	.4348	.3975
4	.9610	.9238	.8885	.8548	.8227	.7921	.7629	.7350	.7084	.6830	.6355	.5921	.5718	.5523	.5158	.4823	.4230	.3725	.3294	.2923
5	.9515	.9057	.8626	.8219	.7835	.7473	.7130	.6806	.6498	.6208	.5674	.5194	.4972	.4761	.4371	.4019	.3411	.2910	.2495	.2149
6	.9420	.8880	.8375	.7903	.7462	.7050	.6663	.6302	.5963	.5645	.5066	.4556	.4323	.4104	.3704	.3349	.2751	.2274	.1890	.1580
7	.9327	.8706	.8131	.7599	.7107	.6651	.6227	.5835	.5470	.5132	.4523	.3966	.3759	.3538	.3139	.2791	.2218	.1776	.1432	.1162
8	.9235	.8535	.7894	.7307	.6768	.6274	.5820	.5403	.5019	.4665	.4039	.3506	.3269	.3050	.2660	.2326	.1789	.1388	.1085	.0854
9	.9143	.8368	.7664	.7026	.6446	.5919	.5439	.5002	.4604	.4241	.3606	.3075	.2843	.2630	.2255	.1938	.1443	.1094	.0822	.0628
10	.9053	.8203	.7441	.6756	.6139	.5584	.5083	.4632	.4224	.3855	.3220	.2697	.2472	.2267	.1911	.1615	.1164	.0847	.0623	.0462
11	.8963	.8043	.7224	.6496	.5847	.5268	.4751	.4289	.3875	.3505	.2875	.2368	.2149	.1954	.1619	.1345	.0938	.0662	.0472	.0340
12	.8874	.7885	.7014	.6246	.5568	.4970	.4440	.3971	.3555	.3186	.2567	.2076	.1869	.1685	.1372	.1122	.0757	.0517	.0357	.0250
13	.8787	.7730	.6810	.6006	.5303	.4688	.4150	.3677	.3262	.2897	.2292	.1821	.1625	.1452	.1163	.0935	.0610	.0404	.0271	.0184
14	.8700	.7579	.6611	.5775	.5051	.4423	.3878	.3405	.2992	.2633	.2046	.1597	.1413	.1252	.0985	.0779	.0492	.0316	.0205	.0135
15	.8613	.7430	.6419	.5553	.4810	.4173	.3624	.3152	.2745	.2394	.1827	.1401	.1229	.1079	.0835	.0649	.0397	.0247	.0155	.0099
16	.8528	.7284	.6232	.5339	.4581	.3936	.3387	.2919	.2519	.2176	.1631	.1229	.1069	.0930	.0708	.0541	.0320	.0193	.0118	.0073
17	.8444	.7142	.6050	.5134	.4363	.3714	.3166	.2703	.2311	.1978	.1456	.1078	.0929	.0802	.0600	.0451	.0258	.0150	.0089	.0054
18	.8360	.7002	.5874	.4936	.4156	.3503	.2959	.2502	.2120	.1799	.1300	.0946	.0808	.0691	.0508	.0376	.0208	.0118	.0068	.0039
19	.8277	.6864	.5703	.4746	.3957	.3305	.2765	.2317	.1945	.1635	.1161	.0829	.0703	.0596	.0431	.0313	.0169	.0092	.0051	.0029
20	.8195	.6730	.5537	.4564	.3769	.3118	.2584	.2145	.1784	.1486	.1037	.0728	.0611	.0514	.0365	.0261	.0135	.0072	.0039	.0021
25	.7798	.6085	.4776	.3751	.2953	.2330	.1842	.1460	.1160	.0923	.0588	.0378	.0304	.0245	.0160	.0105	.0046	.0021	.0010	.0005
30	.7419	.5521	.4120	.3083	.2314	.1741	.1314	.0994	.0754	.0573	.0334	.0196	.0151	.0115	.0070	.0042	.0016	.0006	.0002	.0001
40	.6717	.4529	.3088	.2063	.1420	.0972	.0688	.0480	.0318	.0221	.0107	.0053	.0037	.0026	.0013	.0007	.0002	.0001	.0001	.0001
50	.6080	.3715	.2281	.1407	.0872	.0543	.0339	.0213	.0134	.0085	.0035	.0014	.0009	.0006	.0003	.0001	.0001	.0001	.0001	.0001
60	.5504	.3048	.1897	.0951	.0535	.0303	.0173	.0099	.0057	.0033	.0011	.0004	.0002	.0001	.0001	.0001	.0001	.0001	.0001	.0001

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