

LAIKIPIA



UNIVERSITY

UNIVERSITY EXAMINATIONS

FIRST SEMESTER 2025/2026 ACADEMIC YEAR

THIRD YEAR EXAMINATION FOR THE DEGREE
OF BACHELOR OF EDUCATION ARTS

BUST 311: BUSINESS FINANCE

STREAM:

TIME: 2 HRS

DAY: FRIDAY [2.30 P.M-4.30 P.M]

DATE: 06/02/2026

THIS QUESTION PAPER CONSISTS OF FOUR (4) PAGES

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Answer Question One and any other TWO questions

QUESTION ONE (Compulsory, 30 Marks)

- (a) A service agency offers your business the following options for a 3-year contract:
- i. Pay only Shs.2, 500 now and no more payment during next 3 years, or
 - ii. Pay Shs.900 each at the end of first year, second year and third year from now. A client having a rate of interest at 10% p.a. can choose an option on the basis of the present values of both options as follows

Required:

Using calculations, select the best option for your business. (NB: No marks will be awarded without calculations). **(6 Marks)**

- (b) From the following Statement of Financial Position of Mr. Arvind Industries Ltd., as 31st March 2021

Liabilities Shs.		Assets Shs.	
Equity Share Capital	10,000	Non-Current assets (less depreciation Rs. 10,000)	26,000
7% Preference Share Capital	2,000	Current Assets:	
Reserves and Surplus	8,000	Cash	1,000
6% Mortgage Debentures	14,000	Investments (10%)	3,000
Current Liabilities:		Sundry debtors	4,000
Creditors	1,200	Stock	6,000
Bills payable	2,000		
Outstanding expenses	200		
Tax Provision	2,600		
	40,000		40,000

Other information:

1. Net sales Shs. 60,000
2. Cost of goods sold Shs.51,600
3. Net income before tax Shs.4,000
4. Net income after tax Shs.2,000

Required:

Calculate:

- | | |
|----------------------------|------------------|
| a) Liquidity Ratio | (2 Marks) |
| b) Debt Equity Ratio | (2 Marks) |
| c) Internal Coverage Ratio | (3 Marks) |
| d) Stock Tur-Over Ratio | (2 Marks) |
| e) Return of Investment | (3 Marks) |

- (c) Explain the scope and objectives of business finance in the context of a developing country. **(12 Marks)**

QUESTION TWO

From the following information, calculate the **Net Present Value** of the two projects and suggest which of the two projects should be accepted at a discount rate of 10%. **(10 Marks)**

	Project X (Shs,)	Project Y (Shs,)
Initial Investment	20,000	30,000
Estimated Life	5 years	5 years
Scrap Value	1,000	2,000

The profits before depreciation and after taxation (cash flows) are as follows

	Yr 1	Yr2	Yr3	Yr4	Yr5
Project x	5,000	10,000	10,000	3,000	2,000
Project Y	20,000	10,000	5,000	3,000	2,000

Describe the various external funding sources, highlighting two benefits and drawbacks for each circumstance. **(10 Marks)**

QUESTION THREE

- a) A company has 10 million shares each with a value of Shs.4.20, whose cost is 7.5%. It has Shs.30 million of 5% bonds with a market value of 101.00 and an after-tax cost of 3.5%. It has a bank loan of Shs.5 million whose after-tax cost is 3.2%. It also has 2 million 8% preference shares of Shs.1 whose market price is Shs.1.33 per share and whose cost is 6%.

Required

Show all the Calculations to determine the WACC.

(10 Marks)

- b) Evaluate the role of infrastructure development and access to finance as critical enablers or inhibitors of Small and Medium-sized Enterprise (SME) performance in the East African region. Propose specific policy and business-level interventions to enhance SME performance in these areas. **(10 Marks)**

QUESTION FOUR

- (a) A company has Shs500 million of equity capital and Shs100 million of debt capital, all at current market value. The cost of equity is 14% and the cost of the debt capital is 8%. The company is planning to raise Shs100 million by issuing new shares. It will use the money to redeem all the debt capital.

Required

According to Modigliani and Miller, if the company issues new equity and redeems all its debt capital, what will be the cost of equity of the company after the debt has been redeemed? Assume that there is no corporate taxation. **(8 Marks)**

- (b) Identify and explain the principal types of financial risks faced by cooperatives. Discuss how the cooperative structure and principles might both mitigate and exacerbate these risks compared to investor-owned firms. **(12 Marks)**