

Name _____ Index No. _____

2906/306

FINANCIAL MANAGEMENT

July 2015

Time: 3 hours

Candidate's Signature _____

Date _____



THE KENYA NATIONAL EXAMINATIONS COUNCIL

**DIPLOMA IN BUSINESS MANAGEMENT
MODULE III**

FINANCIAL MANAGEMENT

3 hours

INSTRUCTIONS TO CANDIDATES

Write your name and index number in the spaces provided above.

Sign and write the date of the examination in the spaces provided above.

*This paper consists of **SEVEN** questions.*

*Answer any **FIVE** questions in the spaces provided in this question paper.*

All questions carry equal marks.

Marks to each part of a question are as indicated.

*Do **NOT** remove any pages from this question paper.*

Candidates should answer the questions in English.

For Examiner's Use Only

Question	1	2	3	4	5	6	7	TOTAL SCORE
Candidate's Score								

This paper consists of 26 printed pages.

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

2. (a) Explain **four** challenges that may be faced when borrowing funds from international financial markets. (8 marks)
- (b) On 31 December 2014, Ngaho Limited had an optimal capital structure with weighted average cost of capital of 7.5%. On 1 January 2015, the company proposed to raise additional capital as follows:
- To issue 250,000 ordinary shares of Ksh 8 at Ksh 10 each.
 - To issue 80,000 10% preference shares of Ksh 10 at Ksh 12 each.
 - To issue 10,000 9% debentures of Ksh 100 at Ksh 90 each.

Additional information:

- The company will pay a 5% ordinary dividend.
 - The corporation tax rate is 30%.
- (i) Determine the amount of money that will be realized by the proposed plan;
- (ii) Calculate the company's marginal cost of capital;
- (iii) Advise the management on the viability of this proposal. (12 marks)

5. (a) Explain the role played by commercial banks in the economic development of a country. (10 marks)
- (b) Explain five factors that should be considered when designing a dividend policy. (10 marks)

6. (a) Highlight **four** limitations of using ratios to analyse the finance statement of a firm. (8 marks)
- (b) The following are summarized financial statement of Zedi Limited.

Income statement for the year ended 31 December

	2014 Ksh	2013 Ksh
Sales	4,600,000	5,300,000
Cost of sales	<u>1,800,000</u>	<u>2,200,000</u>
	2,800,000	3,100,000
Less operating expenses	<u>700,000</u>	<u>850,000</u>
	2,100,000	2,250,000
Less finance interest	<u>150,000</u>	<u>300,000</u>
	1,950,000	1,950,000
Less corporation tax	<u>585,000</u>	<u>585,000</u>
	1,365,000	1,365,000
Less dividends	<u>435,000</u>	<u>335,000</u>
	<u>930,000</u>	<u>1,030,000</u>

Statement of financial position as at 31 December

	2014 Ksh	2013 Ksh
Non current assets at cost	2,200,000	2,500,000
Less acc. dep.	<u>575,000</u>	<u>570,000</u>
	1,625,000	1,930,000
Current assets		
Inventory	560,000	540,000
Trade receivables	220,000	180,000
Bank	<u>480,000</u>	<u>460,000</u>
	1,260,000	1,180,000
Less current liabilities		
Trade payable	185,000	125,000
Taxation	585,000	385,000
Proposed dividends	<u>335,000</u>	<u>300,000</u>
	1,105,000	1,010,000
Working capital	<u>155,000</u>	<u>170,000</u>
	<u>1,780,000</u>	<u>2,100,000</u>
Ordinary shares of Ksh 24 each	600,000	600,000
Retained profit	<u>1,030,000</u>	<u>1,200,000</u>
	1,630,000	1,800,000
10% bank loan	<u>150,000</u>	<u>300,000</u>
	<u>1,780,000</u>	<u>2,100,000</u>

For each of the years ended 31 December 2013 and 31 December 2014. Calculate:

(i) Calculate:

- (I) gross profit margin;
- (II) acid test ratio;
- (III) rate of stock turnover;
- (IV) average collection period (1 year = 365 days);
- (V) capital gearing ratio.

(ii) Based on the gross profit percentage, comment on the company's performance.

(iii) Advise the management on two measures to put in place regarding the average collection period. (12 marks)

7. (a) Explain **five** functions of financial management in an organization. (10 marks)

- (b) Capital budgeting decisions require careful considerations before being undertaken. Explain five reasons for such consideration. (10 marks)
