

1922/203  
PROJECT FINANCING  
November 2022  
Time: 3 hours



THE KENYA NATIONAL EXAMINATIONS COUNCIL  
CRAFT CERTIFICATE IN PROJECT MANAGEMENT  
MODULE II

PROJECT FINANCING

3 hours

INSTRUCTIONS TO CANDIDATES

*This paper consists of FOURTEEN questions in TWO sections; A and B.  
Answer ALL the questions in both sections in the answer booklet provided.  
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 **four** goals of project financing. (4 marks)
2. Differentiate between an annuity and a perpetuity in project financing. (4 marks)
3. Highlight **three** advantages of factoring, as a source of project finance. (3 marks)
4. State **three** factors that may lead to increased cost of an ongoing project. (3 marks)
5. The ordinary shares of Deto Limited are currently selling at Ksh 60 each. The company had paid a previous dividend of Ksh 6 per share. The dividend is expected to grow at the rate of 6% per annum. Calculate the cost of equity. (3 marks)
6. Highlight **four** disadvantages of using retained earnings as a source of project finance. (4 marks)
7. State the meaning of mutually exclusive projects. (2 marks)
8. Highlight **three** ways in which the concept of time value of money is important in project financing. (3 marks)
9. Differentiate between a financial lease and operating lease. (4 marks)
10. State **two** advantages of Internal Rate of Return (IRR) method of investment projects evaluation. (2 marks)

## SECTION B (68 marks)

Answer **ALL** the questions in this section.

11. (a) Explain **four** causes of agency conflict between creditors and shareholders of a company. (8 marks)

- (b) The following is an extract of the balance sheet of Stemo Limited.

<b>Stemo Limited</b>		
<b>Balance Sheet</b>		
<b>As at 31 December,</b>		
	<b>2019</b>	<b>2020</b>
	<b>(Ksh '000')</b>	<b>(Ksh '000')</b>
<b>Current Assets:</b>		
Cash	400	520
Accounts receivable	170	190
Inventory	<u>90</u>	<u>100</u>
Total current assets	660	810
<b>Long term assets:</b>		
Plant and equipment	<u>2,790</u>	<u>2,760</u>
Total assets	<u>3,450</u>	<u>3,570</u>
<b>Current liabilities:</b>		
Accounts payable	300	350
Bank overdraft	<u>250</u>	<u>120</u>
Total current liabilities	<u>550</u>	<u>470</u>
Long-term debt	<u>500</u>	<u>450</u>
Total liabilities	<u>1,050</u>	<u>920</u>
Owners' equity	600	650
Retained earnings	<u>1,800</u>	<u>2,000</u>
Total owners' equity	<u>2,400</u>	<u>2,650</u>
Total liabilities and equity	<u>3,450</u>	<u>3,570</u>

- (i) For each year, calculate the:
- I. current ratio;
  - II. quick assets ratio.
- (ii) Using the results in (i) above, comment on the liquidity position of the company over the two years. (9 marks)
12. (a) Explain four uses of a cash flow statement in project financing. (8 marks)
- (b) Outline six financial needs of a new project. (9 marks)

$$C = A + L$$

$$A = C - L$$

$$L = C - A$$

$$\text{Capital} = \text{Asset} + L$$

$$\text{Asset} = \text{Capital} - L$$

$$L = C - A$$

$$\text{Assets} = \text{Capital} + L$$

$$\text{Capital} = \text{Asset} - L$$

$$L = \text{Asset} - \text{Capital}$$

13. (a) Explain **four** ways in which a project may negatively affect the local community. (8 marks)
- (b) A company intends to invest Ksh 4,600,000 in either Project A or Project B. The following are the expected net cash inflows from the projects.

Net Cash Inflows		
Year	Project A (Ksh)	Project B (Ksh)
1	1,200,000	1,570,000
2	1,750,000	1,900,000
3	2,000,000	1,800,000
4	800,000	700,000
5	200,000	300,000

The company's cost of capital is 12%.

- (i) Calculate the Net Present Value (NPV) of each project.
- (ii) Based on the results in (i) above, advise the management on the project to invest in. (9 marks)
14. (a) Explain **four** circumstances under which trade credit may be a suitable source of project financing. (8 marks)
- (b) The following is the capital structure of Tajiril Limited as at 31 December 2020.

Source of capital	Amount (Ksh)
Debt	4,000,000
Preference share capital	2,000,000
Equity share capital	7,000,000
Retained earnings	2,000,000

The cost of debt, preference shares, equity shares and retained earnings is 14%, 12%, 16% and 16%, respectively. Calculate the Weighted Average Cost of Capital (WACC). (9 marks)

**Table A Present Value of Sh 1 Received at the End of n Periods:**  
 $PVIF_{r,n} = 1/(1+r)^n = (1+r)^{-n}$

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	.7695	.7561	.7432	.7182	.6944	.6504	.6104	.5739	.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	.8895	.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	.6499	.6209	.5674	.5194	.4972	.4761	.4371	.4019	.3411	.2910	.2495	.2149
6	.9420	.8880	.8375	.7903	.7462	.7050	.6653	.6302	.5963	.5645	.5066	.4556	.4323	.4104	.3704	.3349	.2751	.2274	.1890	.1590
7	.9327	.8706	.8131	.7599	.7107	.6651	.6227	.5835	.5470	.5132	.4523	.3996	.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	.1389	.1085	.0854
9	.9143	.8368	.7664	.7026	.6446	.5919	.5439	.5002	.4604	.4241	.3606	.3075	.2843	.2630	.2255	.1938	.1443	.1084	.0822	.0628
10	.9053	.8203	.7441	.6756	.6139	.5584	.5083	.4632	.4224	.3855	.3220	.2697	.2472	.2287	.1911	.1615	.1164	.0847	.0623	.0462
11	.8963	.8043	.7224	.6496	.5847	.5268	.4751	.4289	.3875	.3505	.2875	.2366	.2149	.1954	.1619	.1346	.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	.4383	.3714	.3166	.2703	.2311	.1978	.1456	.1078	.0929	.0802	.0600	.0451	.0258	.0150	.0089	.0054
18	.8360	.7002	.5874	.4936	.4155	.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	.0168	.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	.6095	.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	.0116	.0070	.0042	.0016	.0006	.0002	.0001
40	.6717	.4529	.3066	.2083	.1420	.0972	.0668	.0460	.0318	.0221	.0107	.0053	.0037	.0026	.0013	.0007	.0002	.0001	.	.
50	.6080	.3715	.2281	.1407	.0872	.0543	.0339	.0213	.0134	.0085	.0035	.0014	.0009	.0005	.0003	.0001	.	.	.	.
60	.5504	.3048	.1897	.0951	.0535	.0303	.0173	.0099	.0057	.0033	.0011	.0004	.0002	.0001	.	.	.	.	.	.

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