



MERU UNIVERSITY OF SCIENCE AND TECHNOLOGY

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UNIVERSITY EXAMINATIONS 2024/2025

THIRD YEAR FIRST SEMESTER EXAMINATION FOR DEGREE OF BACHELOR OF
BUSINESS ADMINISTRATION

BFC 3333: CORPORATE FINANCE

DATE: DECEMBER 2024

TIME: 2 HOURS

INSTRUCTIONS: Answer Question ONE and any other TWO questions.

QUESTION ONE (30 MARKS)

- Explain the concept of corporate finance and its importance in business decision-making. (5 marks)
- Discuss the main objectives of corporate finance in business decision-making. (5 marks)
- Explain how agency costs arise in the context of a corporation and suggest strategies that can be used to reduce them. (10 marks)
- Analyze the role of financial managers in achieving corporate financial goals. (10 marks)

QUESTION TWO (20 MARKS)

- Discuss the different forms of business organizations and their affect on financial decisions of the firm (6 marks)
- Explain the relationship between capital structure and firm value and the key theories of capital structure. (10 marks)
- Discuss how the trade-off theory of capital structure applies in deciding the optimal capital structure? (4 marks)

QUESTION THREE (20 MARKS)

- Explain the steps involved in preparing a financial plan for a corporation. (10 marks)



- b) Calculate the sustainable growth rate for a firm with the following data: Return on Equity(ROE) = 15%, Dividend Payout Ratio = 40%. Show your calculations. (5 marks)
- c) Explain the significance of financial forecasting for businesses and how it impacts corporate growth. (5 marks)

QUESTION FOUR (20 MARKS)

- a) Explain the concept of working capital management and describe its key components. (10 marks)
- b) Discuss how efficient working capital management can contribute to a firm's profitability. (5 marks)
- c) Differentiate between liquidity and profitability trade-offs in the context of working capital management. (5 marks)

QUESTION FIVE(20MARKS)

- a) Discuss how weighted average cost of capital (WACC) is calculated and it's importance for investment decisions (10 marks)
- b) A company is considering a project with the following cash flows:

| Year 1 | Year 2 | Year 3 |
|------------|------------|------------|
| Sh 300,000 | Sh 400,000 | Sh 500,000 |

Additional information

- i. Initial investment: Sh 1,000,000
- ii. The discount rate is 10%,

Required;

- Compute the Net Present Value (NPV) of the project. Show your workings. (5 marks)
- c) Explain the impact of risk on a firm's cost of capital and how firms adjust their discount rates to account for risk. (5 marks)

