



# MERU UNIVERSITY OF SCIENCE AND TECHNOLOGY

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## University Examinations 2023/2024

THIRD YEAR SECOND SEMESTER EXAMINATION FOR THE DEGREE OF BACHELOR  
OF SCIENCE IN FINANCE

### BFS 3355: CREDIT MANAGEMENT

DATE: APRIL 2024

TIME: 2 HOURS

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INSTRUCTIONS: Answer question *one* and any other *two* questions

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#### QUESTION ONE (30 MARKS)

- a) You have recently become Credit Manager of a chain of retail outlets that have their own in-house finance facilities available for their customers. The company does not have a credit policy and your financial director suggested you use the same credit policy document you used in your previous company, which was a manufacturing company. State whether or not you believe this to be appropriate and give reasons for your views. (10 marks)
- b) Happy Life Corporation presently gives terms of net 30 days. It has Ksh 60 million in sales, and its average collection period is 45 days. To stimulate demand, the company may give terms of net 60 days. If it does instigate these terms, sales are expected to increase by 15 per cent. After the change, the average collection period is expected to be 75 days, with no difference in payment habits between old and new customers. Variable costs are Ksh. 0.80 for every Ksh. 10.00 of sales, and the company's required rate of return on investment in receivables is 20 per cent.

**Required:**

Should the company extend its credit period? (Assume a 360-day year) (10 marks)

c) Discuss credit management strategies used by businesses to mitigate risk (10 marks)

**QUESTION TWO (20 MARKS)**

a) Explain any four functions of a credit department and outline what is involved in carrying out these functions. (8 marks)

b) A company is planning to offer a discount for payment within 10 days to its customers, who currently pay after 45 days. Only 40 per cent of credit customers would take the discount, although alternative cost savings of £4450 per year would be gained. If credit sales, which are unaffected by the discount, are £1 600,000 per year and the cost of short-term finance is 11 per cent, what is the maximum discount that could be offered?

(12 marks)

**QUESTION THREE (20 MARKS)**

a) Discuss the main duties of a credit manager (10 marks)

b) Mugambi is the credit manager of Heltex plc. He is concerned that the pattern of monthly cash receipts from credit sales shows that credit collection is poor compared with earlier forecasts. Heltex's sales director believes that Tariq is to blame for this situation, but Tariq insists that he is not. Why might Tariq not be to blame for the deterioration in the credit collection period? (10 marks)

**QUESTION FOUR (20 MARKS)**

a) Assume that you are the credit manager of a business and that a limited company approaches you with a view to buying goods on credit. What sources of information might you decide to use to help assess the financial health of the potential customer? (10 marks)

b) Discuss the factors that determine the length of the credit period to a customer (10 marks)

**QUESTION FIVE (20 MARKS)**

- a) Torrance Ltd produces a new type of golf putter. The business sells the putter to wholesalers and retailers and has an annual turnover of Ksh 600,000. The following data relate to each putter produced.

Selling Price	40
Variable costs	(20)
Fixed cost apportionment	(6)
<i>Profit</i>	14

The business's cost of capital is estimated at 10 per cent a year.

Torrance Ltd wishes to expand the sales volume of the new putter. It believes that offering a longer credit period can achieve this. The business's average receivables collection period is currently 30 days. It is considering three options in an attempt to increase sales revenue. These are follows:

	Option		
	1	2	3
Increase in average collection period (days)	10	20	30
Increase in sales revenues (Kshs)	30,000	45,000	50,000

Which is the best option to adopt (12 marks)

- b) Discuss the risk of credit selling to an organisation (8 marks)