



**STRATHMORE INSTITUTE
DIPLOMA IN ENTREPRENEURSHIP
END OF SEMESTER EXAMINATION
DE 1204: FINANCING YOUR BUSINESS**

DATE: 14th December 2021

Time: 14:30pm-16:30pm

Instructions

1. This examination consists of FIVE questions.
2. Answer Question ONE (COMPULSORY) and any other TWO questions.

QUESTION ONE

Mr. Hassan Yussuf started a small business to supply construction materials to his clients. His business is five years old with an annual profit of \$50,000. He operates with a bank overdraft of \$20,000. Recently, he won a tender to supply tissue paper to KMSB Himalaya Inter College which is one of the best schools in India. Mr. Hassan Yussuf will be paid in 120 days after delivery. He calls his suppliers and orders for the tissue papers to fulfill the tender in the coming months.

Month 1- Transactions go on well and the suppliers deliver the orders as promised but he is short of space to store them.

Month 2- Business is still good. He makes his first delivery to the school which increases his overdraft.

Month 3- Hassan Yussuf is in a ditch. He has made more deliveries to the school but his overdraft is at the limit and is getting calls from unpaid suppliers.

Month 4- Hassan Yussuf is in a crisis. He cannot pay all the suppliers. Some suppliers stop delivering and threaten legal action. However he thinks the situation will stabilize since he is still supplying the school.

Month 5- His overdraft is \$40,000 over the limit. Two suppliers start legal action. The bank refuses to pay anymore cheques. Luckily enough he receives his first payment from KMSB Himalaya Inter College.

Month 6- The subsequent payments from the school delay and he cannot fulfill any more orders. The bank demands for payment of the overdraft within 10 working days. Hassan Yussuf closes the business and blames the bank.

Required:

- a) Give any five (5) reasons why Hassan Yussuf failed to manage his business effectively
(5 marks)
- b) Assume you are the owner of this business; discuss how you could have managed this situation differently?
(5 marks)

- c) Working capital is referred as the most sensitive blood nerve for every business which involves the management of all the current assets (receivables, cash, inventories and near cash assets) that can be used to meet the day to day obligations of a business. Discuss Ten (10) measures that can be used by Hassan Yussuf to manage his receivables, payables, and inventory and business cash. **(15 marks)**
- d) With Three (3) reasons, advice Hassan Yussuf on how to manage his working capital and how it can be used to finance his business **(5 marks)**

[Total: 30 Marks]

QUESTION TWO

- a) Hussein and James have decided to combine their talents and open a competitive Cheer and Dance business. Hussein expertise is the business side. He has a degree in Business Administration with a minor in Entrepreneurship; while James has a degree in Sports Management and has been coaching the local high school cheerleading team, while his wife has been coaching the school's dance team. The problem is that James does not have as much capital to invest. In fact, they are having a little trouble figuring out how they will be able to get the startup capital for the business. Some of their friends/relatives might be willing to invest in the firm. There are no other competitive Cheer and Dance companies in the area. They have found a building to lease at \$4,000 per month and expect that utilities and water will cost approximately \$350 per month. Liability insurance has been estimated to be \$1,000 per month, due to possible injuries. Hussein, James and Jame's wife will do all the coaching and will also do all the paper work.

Required:

- i. Which type of business organization is described above? **(1 marks)**
 - ii. List the two advantages and two disadvantages of your choice **(4 marks)**
- b) Entrepreneurs have the opportunity to turn their ideas into a business but determining minimum capital required significantly slows most people to start. Such requirements also fail them to serve their intended purpose of serving their customers from hastily established and potentially operating businesses. Most entrepreneurs get their businesses started by bootstrapping. Assume you have an idea of starting a business in your community.

Required:

- i. State two main components of start-up capital for your business **(1 marks)**
- ii. Calculate approximate start-up capital needed to start your business **(7 marks)**
(Use example of a business and show all calculations).
- iii. Explain two reasons why it is important to estimate business start-up capital **(2 marks)**

[Total: 15 Marks]

QUESTION THREE

- a) State three (3) limitations of ratio analysis **(3 marks)**

- b) Planning means thinking about and organizing the activities required to achieve a desired goal. For your business, financial planning means thinking about and working out what to do in the future to improve your business. Some business people do not make plans. They do not think ahead to prevent problems. They do not know how well their business will perform in the future. Miss Hellen operates Danda Music and Video Shop in Dabur Shopping Complex.



Required:

- a) Give two valid reasons why this business didn't make profit last year **(2 marks)**
- b) Explain how could financial planning have helped Danda Music and Video business to improve its performance **(3 marks)**
- c) Discuss **three (3)** important reasons why making a financial plan is important for any business venture **(7 marks)**

[Total: 15 Marks]

QUESTION FOUR

- a) Differentiate between money market and capital markets **(3 marks)**
- b) Financial values and decisions can be assessed by using either future value (FV) or present value (PV) techniques. A shilling today is worth more than a shilling tomorrow.

You are required to:

- i. State **three (3)** reasons why people would prefer to receive money today rather than same amount in the future **(3 marks)**
- c) Assume that you have just invested \$100, 000. The investment is expected to earn interest at a rate of 20% compounded annually. Determine the future value of the investment after 3 years. **(2 marks)**

d) The following is a mixed stream of cash flows occurring at the end of year

| Year | Cash flow (\$ 000) |
|-------------|---------------------------|
| 1 | 400 |
| 2 | 800 |
| 3 | 500 |
| 4 | 400 |
| 5 | 300 |

Required:

- i. If a firm has been offered the opportunity to receive the above amounts and if it's required rate of return is 9% what is the most it should pay for this opportunities? **(7 marks)**

[Total: 15 marks]

QUESTION FIVE

- a) After three years of operations, your business managed to close a \$20,000 long-term loan to finance its activities that is to be repaid in eight equal end-of year repayments. The interest rate on the loan is 14%.

Required:

- (i) Prepare an amortization schedule for the loan **(show all calculations)** **(8 marks)**

- b) During the growth of a small business, a company will go through the stages of the business life cycle and encounter different challenges that require different financing sources.

Required:

- i. Describe the concept of business life cycle and give examples of sources of finance available at each stage **(use a diagram)** **(7 marks)**

[Total: 15 marks]