2922/106
PROJECT FINANCING
July 2017
Time: 3 hours

THE KENYA NATIONAL EXAMINATIONS COUNCIL

DIPLOMA IN PROJECT MANAGEMENT
MODULE I

PROJECT FINANCING

3 hours

INSTRUCTIONS TO CANDIDATES

*This paper consists of **SEVEN** questions.*
*Answer any **FIVE** questions.*
All questions carry equal marks.
Write your answers in the answer booklet provided.
Candidates should answer the questions in English.

1. (a) Explain **five** features of project financing. (10 marks)

(b) Explain **five** benefits that a country may derive from public private partnerships in project financing. (10 marks)

2. (a) Describe the stages followed during project financing. (10 marks)

(b) Kreta Limited intends to invest Ksh 1,500,000 in either project A or project B. The expected cash inflows from each of the projects are as follow:

	Cash inflows	
Year	**Project A**	**Project B**
1	200,000	800,000
2	50,000	400,000
3	100,000	800,000
4	600,000	600,000
5	800,000	–
6	600,000	–

The cost of capital is 12% per annum.

(i) Determine the Net Present Value of each project.

(ii) Using the results in (i) above, advise the management on which project to invest in.

(10 marks)

3. (a) Explain **five** differences between project financing and project finance management. (10 marks)

(b) Totty Limited intends to raise additional capital for a project from the following sources.

	Amount (Ksh)
300,000 ordinary shares at Ksh 10 par value	3,000,000
10% Preference shares at Ksh 50 par value	5,000,000
15% Debentures at Ksh 100 each	4,000,000
18% Bank loan	8,000,000
	20,000,000

The market prices of the securities are as follows:

	Ksh
Ordinary shares	20
10% Preference shares	80
15% Debentures	120

The expected dividends per share from ordinary shares is Ksh 2. The dividends are expected to grow at the rate of 6% per year.

The corporation tax rate is 30%.

(i) Determine the cost of each component of capital.

(ii) Determine the Weighted Average Cost of Capital (WACC).

(10 marks)

4. (a) Explain **five** ways in which a lender can minimize the risk of lender liability.

(10 marks)

(b) Explain **five** disadvantages of bonds as a source of project finance. (10 marks)

5. (a) Two companies; A and B, have approached Bank T to finance their projects. Each of the companies has provided the following information to the bank:

	Company A (Ksh)	**Company B (Ksh)**
Net operating profit	150,000	200,000
Interest expenses	55,000	100,000
Principal payment	35,000	70,000
Sinking fund obligations	25,000	40,000

(i) Determine the Debt Service Coverage Ratio (DSCR) for each company.

(ii) Interpret the ratios determined in (i) above.

(iii) Using the results in (i) above, advise Bank T on which company is safer to finance.

(10 marks)

(b) Explain **five** roles of financial advisors in project financing. (10 marks)

6. (a) Explain **five** ways in which the local community may contribute towards financing of a project. (10 marks)

(b) A company requires Ksh 100,000,000 to finance a project. The management is considering two options; A and B, to raise the funds.

Option A – To raise a 10% ten year bond, with semi-annual interest payments.

Option B – Take a 10 year bank loan at a compound interest rate of 10% per annum.

(i) Determine the total interest payable in each option.

(ii) Using the results in (i) above, advise the management which option to choose. (10 marks)

7. (a) Explain **five** objectives of carrying out financial appraisal of a project. (10 marks)

(b) Explain **five** factors that may influence the cost of financing a project. (10 marks)