

2805/303
INVESTMENT
March/April 2025
Time: 3 hours



THE KENYA NATIONAL EXAMINATIONS COUNCIL
DIPLOMA IN BANKING AND FINANCE

INVESTMENT

3 hours

INSTRUCTIONS TO CANDIDATES

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

This paper consists of 4 printed pages.

**Candidates should check the question paper to ascertain that
all the pages are printed as indicated and that no questions are missing.**

1. (a) Paul intends to invest Ksh 70 million in a manufacturing plant. The cash inflows from the plant are expected to be as follows:

YEAR	1	2	3	4	5
	Ksh million	Ksh million	Ksh million	Ksh million	Ksh million
Net profit	0	-7	15	45	60
Interest	0	2	3	3	4
Depreciation	0	4	4	4	4

- (i) Determine the payback period of the investment. (6 marks)
- (ii) Explain **two** advantages of the payback period method of evaluating investment projects. (4 marks)
- (iii) Explain **two** other methods of evaluating projects. (2 marks)
- (b) Explain **four** principles of investment. (8 marks)
2. (a) Explain **four** methods by which a company may obtain listing at the Nairobi Securities Exchange. (8 marks)
- (b) Mrs Maweu intends to invest in the shares of Mara Limited. The following relates to the company:

Dividend paid	Ksh 800,000
Dividend growth rate	5%
Number of equity shares	200,000
Required rate of return	13%
Expected price per share	Ksh 40

- (i) Using Gordon's constant growth model, determine whether Mrs Maweu should invest in the shares or not. (8 marks)
- (ii) Explain **two** disadvantages of high dividend pay-out ratio to a company. (4 marks)

3. (a) Outline four objectives of taxation. (8 marks)
- (b) A portfolio consists of two securities with the following characteristics.

	RETURN	PROBABILITY
SECURITY R:	50%	0.5
	40%	0.6
SECURITY S:	65%	0.7
	10%	0.4

- (i) Calculate the expected return for security R and security S. (4 marks)
- (ii) Calculate the standard deviation of security R and security S and state the security with a higher risk. (8 marks)
4. (a) Explain four benefits of investing in life insurance policies. (8 marks)
- (b) The following information relates to Masawa Limited.

Year	Dividends paid (Ksh '000')	No. of shares	Total earnings (Ksh '000')
2021	25,000	7,000,000	60,000
2022	30,500	7,200,000	75,000

The market prices for 2021 and 2022 were Ksh 70 and Ksh 80 respectively.

- (i) For each of the years 2021 and 2022, calculate the following:
- I. dividend per share; (2 marks)
 - II. dividend yield; (2 marks)
 - III. earnings per share; (2 marks)
 - IV. earnings yield. (2 marks)
- (ii) Highlight four limitations of financial ratios in measuring business performance. (4 marks)
5. (a) Auditors play a critical role in the protection of investors funds. Explain five such roles. (10 marks)
- (b) Explain five interest bearing securities traded at the securities exchange market. (10 marks)

6. (a) You are the Managing Director of Durban Investment Consultant Limited. Elizabeth Makau a client received Ksh 10,000,000 in gratuity from Damarian Insurance Company after her husband's death. Explain four reasons why you may advise her to undertake offshore investments. (8 marks)
- (b) Describe the procedure of forming a trust in Kenya. (12 marks)
7. (a) Efficient Market Hypothesis (EMH) is frequently used in security market analysis. Explain **five** of its assumptions. (10 marks)
- (b) Tamai Investment Limited would like to place Ksh 50 million in Kenya Government Treasury bills. The three month treasury bill rate is 10% per annum and the investment manager would like the principal plus interest to accumulate over a period of two years at the same rate. The tax rate on interest is 15%.
- (i) Calculate the amount the investor will receive at the end of the two years. (6 marks)
- (ii) Determine the effective yield earned on the investment. (4 marks)

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