



MACHAKOS UNIVERSITY

University Examinations for 2019/2020 Academic Year

SCHOOL OF BUSINESS AND ECONOMICS

DEPARTMENT OF ACCOUNTING BANKING AND FINANCE

THIRD YEAR SECOND SEMESTER EXAMINATION FOR

BACHELOR OF COMMERCE

BAC 310: MANAGEMENT OF FINANCIAL INSTITUTIONS

DATE: 10/11/2020

TIME: 8:30 – 10:30 AM

INSTRUCTIONS:

Answer Question One And Any Other Two Questions.

QUESTION ONE (COMPULSORY) (30 MARKS)

- a) The reform of the pension system in Kenya to date has had a positive impact on the occupational pension sector, but a more limited impact in terms of addressing the key weakness of the current system of poor overall levels of coverage and benefit adequacy. Explain the key motivations for further reform (8 marks)
- b) Characterise the risk exposures of the following financial institution transactions. (5 marks)
- i) A Kenyan bank sells two year fixed rate notes to Sudanese entrepreneur
 - ii) A bond dealer uses his own equity to buy Kenyan debt on the less developed countries market
 - iii) A Japanese bank acquires a Kenyan bank to facilitate clearing operations
 - iv) An Insurance company invests its policy premiums in a long term municipal bond portfolio
 - v) A bank finances a Ksh.10m six year fixed rate commercial loan by selling one year certificate of deposit
- c) Explain the following main functions of the front office of an investment bank (6 marks)
- i) Investments management
 - ii) Sales and trading
 - iii) Research
- d) Explain the three major parties involved in a securitization transaction (6 marks)

- e) Explain how loan sales and securitization help a financial institution manage its interest rate and liquidity risk exposure. (5 marks)

QUESTION TWO (20 MARKS)

- a) Financial institutions perform the essential functions of channelling funds from those with surplus funds to those with shortage of funds. In the context of the above statement, explain the following forms of loans and advances provided by the commercial banks (10 marks)
- i) Overdraft
 - ii) Cash credit
 - iii) Discounting of bills
 - iv) Housing finance
 - v) Credit creation
- b) State five objectives of bank regulation (5 marks)
- c) Explain how financial institutions alleviate the problem of liquidity risk faced by investors wishing to invest in securities of corporations (5 marks)

QUESTION THREE (20 MARKS)

- a) The central bank of Kenya (CBK) as the regulatory body mandated to license and supervise the operations of commercial banks in Kenya through provisions of Cbk Act (cap491) recently carried out an evaluation on the performance of three major commercial banks using the CAMELS rating system. The composite rating based on the CAMEL scale of 1 to 5 given below.

BANK	RATING
Commercial bank OF Africa	1
Kenya Commercial Bank	3
Equity Bank	4

Required:

- i) Interpret the results based on the composite parameter (3 marks)
 - ii) Based on the interpretation made above, identify the kind of supervisory attention that CBK should direct to each bank (3 marks)
- b) Compare and contrast pension funds benefit and the provident fund benefits (6 marks)
- c) In the year 1980s Kenya financial system underwent crisis. Identify measures that the government put in place to prevent recurrence (8 marks)

QUESTION FOUR (20 MARKS)

- a) Explain any five monetary regulatory tools used by the government. (10 marks)
- b) A financial institution should have a formal liquidity policy. The policy should be flexible, so that managers may react to unforeseen events. State ten items that a liquidity policy should specifically state. (5 marks)
- c) Explain how a financial institution can be subject to sovereign risk even if it lends to the highest quality foreign corporations (5 marks)

QUESTION FIVE (20 MARKS)

- a) Operational risk is defined as the risk of loss resulting from inadequate or failed internal processes, people and systems or from external events. This risk is categorised into seven groups according to the consultative paper, Explain any of the five groups (10 marks)
- b) What benefits could a commercial banker obtain by getting into the investment banking business (5 marks)
- c) State five functions of IRA (Insurance Regulatory Authority) (5 marks)