



# MACHAKOS UNIVERSITY

University Examinations for 2020/2021 Academic Year

SCHOOL OF BUSINESS AND ECONOMICS

DEPARTMENT OF ACCOUNTING BANKING AND FINANCE

THIRD YEAR SPECIAL/ SUPPLEMENTARY EXAMINATION FOR

BACHELOR OF COMMERCE

BAC 305 FINANCIAL MARKETS AND INSTITUTIONS

DATE: 25/3/2021

TIME:8.30-10.30 AM

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## INSTRUCTIONS:

*Answer question one and any other two questions.*

### QUESTION ONE (COMPULSORY) (30 MARKS)

- a) Distinguish the following types of financial markets (6 marks)
- Primary versus secondary markets
  - Organized exchange versus over-the-counter markets
  - Spot versus future, forward markets.
- b) One of the major indicators of stock market development is the increase in the varieties of products dealt with in the market such as derivatives. Explain why derivatives trading absent in many developing markets. (12 marks)
- c) Explain four functions of interest rates (4 marks)
- d) Explain the following economic functions of financial intermediaries. (8 marks)
- Improved diversification for the lender.
  - Economies of scale
  - Assistance in price discovery.
  - Facilitation of the flow of funds.

### **QUESTION TWO (20 MARKS)**

- a) State five features of fixed income securities (4 marks)
- b) Explain the following terminologies as used in the securities exchange market (8 marks)
  - i. Going short or going long of a share.
  - ii. Underwriting.
  - iii. Jobber.
- c) Distinguish between organized exchange and over the counter markets (4 marks)
- d) State four limitations or drawbacks of the Nairobi securities exchange (4 marks)

### **QUESTION THREE (20 MARKS)**

- a) Discuss the incentives that the government has given to companies to enable them go public (10 marks)
- b) State five objectives of bank regulation (5 marks)
- c) Analyze the factors that might lead to the existence of the global debt problem (5 marks)

### **QUESTION FOUR (20 MARKS)**

- a) Capital markets are not necessarily efficient. This therefore gives rise to information asymmetry which refers to unreliable effects in the operations of the markets. Information asymmetry interferes with the operations of the markets and achievements of its role of financial mobilization and intermediation in the various sectors of the economy.

#### **Required.**

- Explain the term adverse selection and moral hazards in relation to information asymmetry (6 marks)
- b) Explain the following functions of the financial system (6 marks)
  - i. risk function
  - ii. savings function
  - iii. Payments function
- c) Distinguish between investment trust and unit trusts (4 marks)
- d) State four roles of secondary markets (4 marks)

**QUESTION FIVE (20 MARKS)**

- a) Distinguish financial engineering and financial innovation (4 marks)
- b) Capital markets authority is a regulatory body developed and launched in 1989 to assist in creating conducive environment for the growth and development of the country's capital markets. Discuss the contribution of CMA in development of capital markets in Kenya (10 marks)
- c) State and explain three aspects of success of financial regulation in the banking sector in Kenya (6 marks)

