



# MACHAKOS UNIVERSITY

University Examinations for 2019/2020 Academic Year

SCHOOL OF BUSINESS AND ECONOMICS

DEPARTMENT OF ECONOMICS

..... YEAR SPECIAL/SUPPLEMENTARY EXAMINATION FOR

BACHELOR OF ECONOMICS AND STATISTICS

BACHELOR OF ECONOMICS

EAE 402: ECONOMICS OF MICROFINANCE II

DATE:

TIME:

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## INSTRUCTIONS:

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

### QUESTION ONE (30 MARKS)

- a) In statistical measurement of the impact of microfinance, an enterprise may be used as a unit of assessment.
- i) Illustrate and explain a conceptual framework that is suitable for such an analysis (5 marks)
  - ii) Outline four limitations of using the enterprise as a unit of assessment (6 marks)
- b) When starting a business, it is important to have a business plan. Assume that you are presenting your business plan to potential investors. Describe three main components of business plan that would be bankable and competitive. Base your points on an actual business idea for clarity. (6 marks)
- c) Outline two examples of external non-ownership capital and discuss three advantages of using external sources of funds to fund a business. (7 marks)

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

- a) In the paper: Bold, Calvo and Dercon (2006) “Insurance for the poor?” QEH Working Paper Series, No. 125, the authors explain that there is failure in the insurance market since insurance is underprovided for the poor. The poor however, have easy and means of dealing with these inefficiencies. Discuss four of the possible ways that the poor use to deal with under-provision of insurance/ the lack of insurance.  
(8 marks)
- b) Explain the meaning of adverse selection and explain how it leads to credit rationing  
(6 marks)
- c) Name two types of external sources of capital and clearly outline four advantages of these external sources of capital.  
(6 marks)

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

- a) An NGO has been providing funds to businessmen in a village in your country. The NGO has engaged you to measure the impact of credit. Using a relevant framework discuss how you would quantitatively measure the credit impact.  
(10 marks)
- b) Using appropriate diagrams, explain the challenge that many microfinance institutions face when seeking to trade-off between their objectives of poverty reduction and profitability.  
(10 marks)

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

- a) Using relevant examples distinguish the following pairs  
(10 marks)
- i. Hire-purchase and lease
  - ii. Debt factoring and invoice discounting
  - iii. Moral hazard and principal –agent conflict
  - iv. Corporate and retail microfinance clients
  - v. Garnishee order and warrant of execution
- b) Explain three differences between conventional insurance and microinsurance  
(6 marks)

- c) Why is monitoring and control of credit important while undertaking credit appraisal?  
(4 marks)

**QUESTION FIVE (20 MARKS)**

- a) Describe the multitask agency problem and how it relates to microfinance and briefly describe how the management of microfinance institutions deals with this problem  
(10 marks)
- b) Some banks and SACCOs offer insurance services (the model of bancassurance). Discuss the challenges associated with this model. (10 marks)



## **MACHAKOS UNIVERSITY**

### **EXAMINATIONS 2019/2020**

#### **MAIN EXAM**

#### **EXAMINATION FOR THE DEGREE OF BACHELOR OF ECONOMICS**

#### **EAE 402: ECONOMICS OF MICROFINANCE II**

#### **INSTRUCTIONS**

- 1. This examination consists of FIVE questions**
- 2. Answer question ONE (COMPULSORY) and any other TWO Questions**

#### **QUESTION ONE (30 MARKS)**

- In the measurement of impact of microfinance access, different units of assessment may be used. Discuss four of these units, clearly describing an advantage and 2 disadvantages of each. (12 marks)
- Describe two ways that a microfinance institution can use to recover debt from problematic loan accounts. (4 marks)
- Clearly outline four disadvantages of group lending. (4 marks)
- Briefly explain the importance of preparing a business plan when starting a business. (10 marks)

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

- It is argued that households should save their way out of subsistence borrowing constraints. That is, a credit-constrained household that acts with foresight will always slowly and steadily accumulate until credit constraints are overcome. However, this does not happen.

- Give five explanations why this does not happen. (10 marks)
- b) Explain the meaning of selection bias in the assessment of the impact of microcredit access. (2 marks)
- c) Describe four causes of selection bias. (8 marks)

**QUESTION THREE (20 MARKS)**

- a) Economic theory suggests that a rational household that suffers some credit constraint would always strive to save until the credit constraint is overcome. Explain why this is not always the case. (10 marks)
- b) In Barboza, G., & Trejos, S. (2009) Micro credit in Chiapas, Mexico: Poverty Reduction Through Group Lending. Journal of Business Ethics Vol. 88: pp 283-299, the study uses Akerlof's (1970) terminology to describe Micro Credit programs to the poor. That is Micro Credit lend money to "the lemons". Briefly explain why these markets where Micro credit ventures in developing countries to reduce poverty are referred to as the lemons. (6 marks)
- c) Clearly outline four disadvantages of group lending (4 marks)

**QUESTION FOUR (20 MARKS)**

- a) There have been recent cases of failure/closing down of microfinance institutions. Discuss some of the challenges faced by these institutions leading to their closure. (10 marks)
- b) Clearly outline reasons why despite the profitability in the micro-credit business, a few entrants enter the market, leaving existing money lender with the monopoly powers that allow them to make exorbitant profits in the short terms. (10 marks)

**QUESTION FIVE (20 MARKS)**

- a) Assuming you are a member of a local SACCO and has just qualified for a micro loan. In your considered opinion, how would this affect your household? (6 marks)
- b) What is the meaning of market failure with respect to the insurance market and insurance services to the poor and people in the informal sector and give four reasons for the aforementioned market failure (6 marks)

- c) You have been employed as a credit officer in a SACCO having completed your course work at Machakos University. Advise the management on five aspects to include in a checklist to ensure that all required information from a borrower is collected.

(8 marks)