MACHAKOS UNIVERSITY

University Examinations for 2020/2021 Academic Year

SCHOOL OF BUSINESS AND ECONOMICS

DEPARTMENT OF ACCOUNTING BANKING AND FINANCE

SECOND YEAR SPECIAL/ SUPPLEMENTARY EXAMINATION FOR

BACHELOR OF COMMERCE

EAE 202: FINANCIAL INSTRUMENTS AND RISK MANAGEMENT

DATE: **TIME:**

INSTRUCTIONS:

Answer question one and any other two questions.

QUESTION ONE (30 MARKS)

a) Briefly explain and analyze four examples of financial instruments and how they are used in Kenya. (10 marks)

b) Explain any three types of derivatives in Kenya's financial system, giving their important perspectives to the Kenyan economy. (10 marks)

c) An investor buys a 10-year Kes.5, 000, 8% coupon, semiannual pay bond for Kes 4550. He sells it four years later, just after receiving the eighth coupon payment, when its yield to maturity is 2.8%. What would be the bond price at the time of sale? (10 marks)

QUESTION TWO (20 MARKS)

a) Explain four differences between bonds and shares. (10 marks)

b) Identify four possible risks of trading in shares. (10 marks)

QUESTION THREE (20 MARKS)

a) Explain any three bases of Markowitz Model in the selection of any portfolio applicable in Kenya. (10 marks)

b) Explain the differences between:

i. Modern Portfolio Analysis (5 marks)

ii. Traditional Portfolio Analysis (5 marks)

QUESTION FOUR (20 MARKS)

a) Calculate the dividend yield if company is expected to pay 12/= per share and quoted price is 160/= and expected price after one year is 200/= (10 marks)

b) Demonstrate how a preference share can be:

  i. A liability (5 marks)

  ii. An equity (5 marks)

QUESTION FIVE (20 MARKS)

a) Illustrate four reasons why hedging is a means of risk management in financial institutions. (10 marks)

b) A company buys 600 futures at 125/= each under delivery-based settlement. On the day of expiry, the futures were actually priced at 140/=.

You are required to calculate the results of the company in terms of profit**.** (10 marks)