MACHAKOS UNIVERSITY

University Examinations for 2018/2019 Academic Year

SCHOOL OF BUSINESS AND ECONOMICS

DEPARTMENT OF ECONOMICS

FOURTH YEAR SUPPLEMENTARY EXAMINATION FOR

BACHELOR OF ECONOMICS

EAE 402: ECONOMICS OF MICROFINANCE II

DATE: **TIME:**

INSTRUCTIONS

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

QUESTION ONE (COMPULSORY) (30 MARKS)

a) 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)

b) Describe two ways that a microfinance institution can use to recover debt from problematic loan accounts. (4 marks)

c) Clearly outline four disadvantages of group lending. (4 marks)

d) Briefly explain the importance of preparing a business plan when starting a business. (10 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, ha 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 TWO (20 MARKS)

a) 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 FOUR (20 MARKS)

a) Three 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) 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)