MACHAKOS UNIVERSITY

University Examinations for 2017/2018 Academic Year

SCHOOL OF BUSINESS AND ECONOMICS

DEPARTMENT OF BANKING, ACCOUNTING & FINANCE

THIRD YEAR FIRST SEMESTER EXAMINATION FOR

BACHELOR COMMERCE (FINANCE OPTION)

BAC 310: MANAGEMENT OF FINANCIAL INSTITUTIONS

DATE: 15/12/2017 **TIME: 2:00 – 4:00 PM**

INSTRUCTIONS:

Answer question one and any other two questions

a) The central bank of Kenya (CBK) as the regulatory body mandated to license and supervise the operations of commercial banks in Kenya through the provisions of CBK Act (cap 491) recently carried out an evaluation on the performance of three major commercial banks using the CAMELS rating system. The results of this evaluation based on the CAMELS scale of 1 to 5 are given below.

BANK	CAPITAL	ASSETS	MANAGEMENT	EARNINGS	LIQUIDITY	COMPOSITE
BARCLAYS BANK	1	2	1	1	1	1
STANDARD CHARTERED	2	1	3	3	3	3
EQUITY	4	4	4	5	5	4

Required

i. Interpret the results obtained based on the composite parameter (3 marks)

ii. Based on the interpretation made in (a) above, identify the kind of supervisory attention that CBK should direct to each bank (3 marks)

b) How do financial institutions help individual severs diversify their portfolio risks? Which type of financial institution. (3 marks)

c) In the management of pension funds, some principles emerge from international practice to ensure prudent management and improve the efficiency of public funds explains any three of these principles. (6 marks)

d) An investment bank is split in the so called front office, middle office and back office. Which are the main functions of the front office. (6 marks)

e) Explain the following risks faced by insurance companies

i) Underwriting risk (2 marks)

ii) Liquidity risk (2 marks)

iii) Insolvency risk (2 marks)

f) State six items that should appear in a liquidity policy (3 marks)

QUESTION TWO (20 MARKS)

a) Discuss the banking crisis that Kenya financial system underwent in the 1980s and identity the measures that the government put in place to prevent a recurrence (16 marks)

b) How does the regulation of insurance companies compare with that of commercial banks? (4 marks)

QUESTION THREE (20 MARKS)

a) By law the activities of most financial institutions were limited so that for several decade their financial management was not a terribly complex process. Regulators set prices and costs such that financial institutions were usually profitable and relatively few failed. Explain the challenges that face the present day financial institutions especially those operating in a financially liberalize environment. (10 marks)

b) Distinguish between Tier 1 capital and Tier 2 capital (2 marks)

c) Explain the following parties involved in a securitization transaction

i) Structure (2 marks)

ii) Investor (2 marks)

iii) The rating Agency (2 marks)

iv) Special purpose vehicle (2 marks)

QUESTION FOUR (20 MARKS)

a) State and explain six functions of insurance regulatory authority (IRA) (6marks)

b) When a steel company goes bankrupt, other companies in the same industry benefit because they have one less competitor. But when a bank goes bankrupt other banks do not necessarily benefit. Explain this statement (6 marks)

c) Explain the following areas of financial institution specialness:

i) Transmission of monetary policy (2 marks)

ii) Denomination intermediation (2 marks)

iii) Maturity intermediation (2 marks)

iv) Liquidity and price risk (2 marks)

QUESTION FIVE (20 MARKS)

a) In what ways does the credit analysis of a mid market borrower differ from that of a small business borrower. (4 marks)

b) Monetary regulation is one of the regulatory norms in the banking sector. Explain how the following tools are used in the regulation of value, supply and cost of money:

i) Discount window (2 marks)

ii) Moral suasion (2 marks)

iii) Cash reserve (2 marks)

c) If a financial institution funds long-term assets with short term liabilities, what will be the impact of an interest rate increase on turnings (4 marks)

d) Explain the main objectives of bank regulation (6 marks)