KENYATTA UNIVERSITY

UNIVERSITY EXAMINATIONS 2016/2017

SECOND SEMESTER EXAMINATION FOR THE DEGREE OF BACHELOR OF COMMERCE

BAC 310: MANAGEMENT OF FINANCIAL INSTITUTIONS

DATE: MONDAY 15TH MAY 2017 **TIME: 11.00 A.M. - 1.00 P.M.**

INSTRUCTIONS
Answer ALL Questions

Question One

a) Explain the general guiding principles in management of commercial banks (10 marks)

b) Consider two banks with the following balance sheets.

BANK A

Ratio of Capital to Assets: - 10%

Reserves	10,000,000	Deposits	90,000,000
Loans	90,000,000	Bank Capital	10,000,000

BANK B

Ratio of Capital to Assets: - 4%

Reserves	10,000,000	Deposits	96,000,000
Loans	90,000,000	Bank Capital	4,000,000

Required

Show the effect of a non-recoverable loan of Ksh 5 millions on the total value of both bank's assets and the resultant implication to the banks. (7 marks)

Question Two

a) Kenyan insurance companies face a number of risks in conducting their business. Credit risk is among the key risks emanating from uncertainty in a counterparty's (also called an obligor's) ability to meet its obligations. Discuss the issues an insurer must consider in assessing credit risk from a single counterparty. (6 marks)

b) CARAMELS Framework was established to assist in management and evaluation of insurance company's financial soundness. Explain how the framework can be used to insulate insurers from facing liquidity risk. (12 marks)

Question Three

a) Describe the factors that determine the interest rates applicable in a country.(7 marks)

b) Explain how the following two tools can be applied in management of interest rates

   i) Gap Analysis (2 marks)

   ii) Duration Analysis (2 marks)

c) To manage the exchange rate risk inherent in multinational financial institution's operations, an institution needs to determine the specific type of currency risk exposure, the hedging strategy and the available instruments to deal with these currency risks. Explain three main types of exchange rate risk. (6 marks)

Question Four

a) Basel committee on Banking Supervision (BCBS) has a set of recommendations for regulations in the banking industry issued as supervisor Accords BASEL 1, BASEL 2 and BASEL 3. Explain the objectives of BASEL 2 Accord and it's three pillars concept. (9 marks)

b) An investor has held his investment in a sh 1,000,000 portfolio containing sh 600,000 worth of stock X and sh 400,000 worth of Stock Y. Given the data below, compute the Value at risk (VaR) of this portfolio with a 95% confidence level over the coming: day, month and year assuming a 22 days month and 252 days trading year

DATA

$W_X = 0.60,$ $W_Y = 0.40$ $\sigma_X = 0.016284,$ $\sigma_Y = 0.015380$

$P = -0.19055$ (9 marks)