



# MURANGA UNIVERSITY COLLEGE

(A constituent College of Jomo Kenyatta University of Agriculture & Technology)

**MAIN CAMPUS**

**SPECIAL/SUPPLEMENTARY EXAMINATIONS**

**2015/2016 ACADEMIC YEAR**

**FOURTH YEAR SECOND SEMESTER EXAMINATIONS**

**FOR THE DEGREE  
OF  
BACHELOR OF COMMERCE**

**COURSE CODE:** HBB 2403

**COURSE TITLE:** FINANCIAL RISK MANAGEMENT

**DATE:**

**TIME:**

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## **INSTRUCTIONS TO CANDIDATES**

Question ONE (1) is COMPULSORY

Answer ANY OTHER TWO (2) questions

MRUC observes ZERO tolerance to examination irregularities

**QUESTION ONE (COMPULSORY)**

- a. Differentiate between actuarial and financial risk (4 marks)
- b. Modern Portfolio theory is one of the oldest attempts to quantify risk in an investment. Highlight the assumptions upon which this theory is based (7 marks)
- c. Risk arises in capital budgeting because of the difficulties in predicting future cash flows correctly. What factors influence the cash flows in investment projects (9 marks)
- d. When is the coefficient of variation suitable in analysis risk in capital budgeting (3 marks)
- e. Explain the components of non-systematic risk (8 marks)
- f. Explain the meaning of the following types of risk in the context of financial institutions
  - i. Off-balance sheet risk (3 marks)
  - ii. Solvency risk (3 marks)
  - iii. Liquidity risk (3 marks)

**QUESTION TWO**

The problem of credit risk in the management of financial institutions is compounded by the challenges of adverse selection and moral hazards. Explain the various methods used by financial institutions to manage these challenges and by extension credit risk (15 marks)

**QUESTION THREE**

- a. Explain the two types of illiquidity that financial institutions are faced with (6 marks)
- b. In the context of risk, explain the effects of debt financing on the owners of a business (6 marks)
- c. How is liquidity risk resolved in financial institutions (3 marks)

**QUESTION FOUR**

- a. Highlight the steps involved in sensitivity analysis as a method of risk analysis in capital budgeting (6 marks)
- b. Explain the benefits that accrue to a firm adopting an active risk management approach (9 marks)