



MURANGA UNIVERSITY COLLEGE

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

TOWN LEARNING CENTRE

ORDINARY UNIVERSITY EXAMINATIONS

2015/2016 ACADEMIC YEAR

THIRD YEAR FIRST SEMESTER EXAMINATIONS

FOR THE DEGREE OF BACHELOR OF COMMERCE

COURSE CODE: HBF 2301

COURSE TITLE: FINANCIAL INSTITUTIONS AND MARKETS

DATE: 20th August, 2015

TIME: 2 HOURS

INSTRUCTIONS TO CANDIDATES

- Question ONE (1) is compulsory
- Answer ANY OTHER TWO questions

MRUC observes ZERO tolerance to examination irregularities

This Paper Consists of 3 Printed Pages. Please Turn Over.



QUESTION ONE (COMPULSORY)

- a. Kamau is an active investor in the financial markets. For him to invest in any long term security, he requires a three percent premium for every year beyond the current one year investment period in addition to the annual short term market rate of interest. He expects future short term one year market rates of 16%, 12% and 18% in the next three years.
- i. If the current one year rate is 14%, what should be the current long term rate if Kamau is to invest in a four year debt security (5 marks)
 - ii. Identify and describe the theory that explains Kamau's behaviour towards interest rates (10 marks)
- b. What is the importance of derivative financial securities in the financial markets (4 marks)
- c. For what reasons should financial markets be regulated? (6 marks)
- d. Differentiate between initial public offering (IPO) and secondary stock offering (5 marks)

QUESTION TWO

- a. Highlight the characteristics that distinguish money market securities from other financial market securities (3 marks)
- b. Identify the various participants in foreign exchange markets (6 marks)
- c. Explain the operation of the following financial market securities and institutions
- i. Put options (4 marks)
 - ii. Repurchase agreements (4 marks)
 - iii. Pension funds (3 marks)

QUESTION THREE

- a. Though they are not highly developed in Kenya, organized stock exchanges are far too important in the development of the financial system. Explain (14 marks)
- b. Differentiate between spot foreign exchange transactions and forward foreign exchange transactions (6 marks)

QUESTION FOUR

- a. Kenya has recently experienced a tremendous expansion in depository financial institutions. This can be attested by the growth in banking, deposit taking microfinance institutions and SACCOs not only locally but across the region. Explain the role of these institutions in the financial system (12 marks)
- b. The benefit of a developed financial market can be derailed by lack of efficiency in the market. Explain the various reasons why financial markets should be efficient (8 marks)