



JARAMOGI OGINGA ODINGA UNIVERSITY OF SCIENCE AND TECHNOLOGY
SCHOOL OF BUSINESS & ECONOMICS
UNIVERSITY EXAMINATION FOR THE DEGREE OF BACHELOR OF BUSINESS
ADMINISTRATION WITH IT
3RD YEAR 2ND SEMESTER 2019/2020 ACADEMIC YEAR
MAIN CAMPUS

COURSE CODE: ABA 318

COURSE TITLE: FINANCIAL INSTITUTIONS & MARKETS

EXAM VENUE:

STREAM: (BBA FINANCE OPTION)

DATE:

EXAM SESSION:

TIME: 2 HOURS

Instructions:

- 1. Answer Question ONE (COMPULSORY) and ANY other 2 questions**
- 2. Candidates are advised not to write on the question paper.**
- 3. Candidates must hand in their answer booklets to the invigilator while in the examination room.**

QUESTION ONE

- a) Briefly explain the term of structure of interest rates and its relationship to the yield curve of bonds security. (5 Marks)
- b) What are the possible explanations as to the shape of the security yield curve? Support your answer with term structure of interest rates theories. (10 Marks)
- c) A bank enters a reverse repurchase agreement in which it agrees to buy treasury securities from one of its correspondent banks at a price of Kshs. 10,000,000 with the promise to sell these securities back at a price of Kshs. 10,008,548 after five days. What are both the discount and bond equivalent yield of this bond. (5 Marks)
- d) A bond is listed to pay 10% coupon interest per year with the coupon paid semi-annually. The bond matures in 12 years and has a face value of Kshs. 10,000/-. If the required rate of return is 8% what is the fair market value of the bond? (5 Marks)

QUESTION TWO

- a) Explain the role of Capital Markets Authority (CMA) in the operation of the Kenyan Financial Markets. (5 Marks)
- b) State the basic procedures in selling a new issue. Under what option can a security IPO be offered to the market? (5 Marks)
- c) What are three possible reasons that the price of a stock drops on the announcement of a new equity issue? (What consideration should the company evaluate when it decides to raise new long-term capital through either equity or bonds issue? (10 Marks)

QUESTION THREE

- a) Explain the difference between Security Exchange Markets and Security Market Indexes with reference to the NSE. (5 Marks)
- b) What are the characteristics of the following bonds issues?
 - i. Debenture
 - ii. Convertible
 - iii. Stock warrants
 - iv. Call provision
 - v. Junks (5 Marks)
- c) Kizito Company dividends are expected to grow perpetually at 6% with a dividend payment per share of Kshs. 8/- in the first instance. The appropriate discount rate for this kind of security is 14%. What is the market price of this share? (5 Marks)
- d) XYZ Corporation paid a dividend of Kshs. 3/50 at the end of last year and the company also maintains a constant dividend growth of 2% which it expects to maintain into the future. With the market discounting such securities at 10%, what price would you be willing to pay for the security? (5 Marks)

QUESTION FOUR

- a) Explain both the intrinsic and time value of an option. Also give two ways under which options derivative could be exercised by investors. (5 marks)
- b) What is an interest rate swap? “Interest Rate Swap can be used to hedge interest rate risk.’ Discuss. (10 marks)
- c) What is Black-Scholes Option Pricing Model? Explain also the parameters to be used in the pricing. (5 marks)

QUESTION FIVE

- a) How does one distinguish between an off balance sheet asset and off balance sheet liability? Give three examples for each category. (10 marks)
- b) Assuming you are a manager with a major financial institution (FI), how would you mitigate against the following major FI’s risks:
 - i. Credit Risk
 - ii. Interest Rate Risk
 - iii. Market Risk
 - iv. Off Balance Sheet Risk

Foreign Exchange Risk

(10 marks)