



STRATHMORE BUSINESS SCHOOL

MASTER OF SCIENCE IN DEVELOPMENT FINANCE

END OF SEMESTER EXAMINATION

MDF 8205: FINANCIAL RISK MANAGEMENT

Date: Wednesday 5th April 2023

Time: 3 Hours

Instructions

1. This examination consists of **FIVE** questions.
2. Answer Question **ONE** and **ANY OTHER THREE** Questions

Question 1 (Compulsory) (40 Marks)

- a. The rise in the adoption and use of virtual currencies worldwide is a concern to most central banks as such currencies have the potential to affect the effectiveness of monetary policy as well as threaten the stability of a country's financial systems.
 - i. Describe how virtual currencies can affect monetary policies as well as stability of financial systems **[8marks]**
 - ii. What actions are the central banks taking to avert the threats posed by these currencies? **[4marks]**
- b. Apart from digital currencies most African countries are facing several challenges posed by happenings in the global markets which hamper their monetary as well as fiscal policies. Highlight such global challenges that are currently affecting your country **[7marks]**
- c. The Monetary Policy Committee of your country is due to meet in April to determine the monetary stance of the Central bank for the next three months. The central bank rate which is the base rate for all interest rates is currently at 9%p.a and the headline inflation in the country is at 11.5%p.a and has been steadily rising from a level of 8% in the last three months to the current rate of 11.5%p.a in April. The country is currently facing several challenges which have the potential to affect monetary policy key among them being:
 - A rising domestic public debt currently estimated at 70% of GDP. The country has no commercial external public debt apart from loans from the Bretton Wood institutions at low concessionary rates.
 - Rising food inflation brought about by drought which is expected to continue until July when the long rains will begin.

- Devaluation of the local currency against USD by 15% in the last three months which has led to the dollarization of some parts of the economy where traders are demanding to be paid in dollars.
- Rising long term interest rates due to excessive borrowing by the government in the domestic markets, for example the latest 15year bond issue in the February had a coupon rate of 15% p.a
- Excess liquidity in the economy due to weak KYC and anti-money laundering regulations as well as a growing informal sector which currently stands at 50% of GDP
- High volatility in the interbank market ranging from daily rates at high of 12% to very low rates of 5%

Required:

- Assuming you were the governor of the central bank in your country, stating at least three reasons what decision would you make regarding the central bank rate
[7marks]
- Given your action(s) in (i) above advice the monetary implementation committee on the Open Market Operations tools that they can use to implement your decision.
[6marks]
- What extraordinary monetary policy tools can you use to tackle the problems highlighted above?
[8marks]

Question 2 (20 Marks)

The International Monetary Fund (IMF) has been heavily criticized by African countries due to the conditionalities that the institution places when granting loans to these countries.

- Using examples describe two types of conditions that IMF may place on your country
[4marks]
- What has been the impact of these conditionalities on the education sector? [6marks]
- Suggest the options that your country can adopt to free herself form huge IMF loans
[5marks]
- Highlight the impediments that a country may face in implementing your suggestions to c. above.
[5marks]

Question 3 (20 Marks)

Africa's insurance industry is largely underdeveloped, and insurance penetration levels are low compared to global standards. However, the large numbers of un(der)insured and the potential to speed up access to them make the possibility of insurance growth in Africa strong. The growth of the insurance industry can also assist to deepen and widen the largely underdeveloped African stock exchanges.

- Discuss the unique trends occurring in Africa which the insurance industry can exploit to expand this sector.
[10marks]
- How can African countries deepen and expand their stock exchanges?
[10marks]

Question 4 (20 Marks)

You want to carry out a study to examine the relationship between financial development and economic growth. Similar studies have used Gross Domestic Product (GDP) as a measure of growth; however, you feel GDP suffers from several weaknesses and you want to explore other alternative measures of growth.

- a. Discuss the limitations of using GDP as a measure economic growth. **[8marks]**
- b. Highlight two other measures that you would use in addition to GDP to strengthen your measure of growth **[4marks]**
- c. You also wish to develop measures of financial development which are unique to your country
 - i. Suggest four measures that you would use to proxy financial development **[4marks]**
 - ii. What limitations will you encounter when carrying out such a study? **[4marks]**

Question 5 (20 Marks)

Refer to the case titled- **Bank Simpanan Nasional: Pioneering Financial Inclusion In Malaysia**

Required

- a. Although the agency banking model for BSN has been hailed as a success it has not been smooth sailing
 - i. Highlight the challenges that BSN faced while implementing its agency banking model **[5marks]**
 - ii. Describe the challenges faced by agency banks in Kenya; is there any similarity with Malaysia? **[6marks]**
- b. Datuk Adinan is pleased with BSN's achievement and outreach so far, but he believes there is a lot the bank can do to elevate the living standard of the rural community.

Suggest to Datuk what BSN can do to achieve its objectives in the nine areas (appendix1) that the bank wishes to focus on **[9marks]**