

The
Management
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UNDERGRADUATE UNIVERSITY EXAMINATIONS
SCHOOL OF MANAGEMENT AND LEADERSHIP
DEGREE OF BACHELOR OF COMMERCE

FIN 314: BANKING AND CAPITAL MARKETS

DATE: 9TH APRIL 2026

DURATION: 2 HOURS

MAXIMUM MARKS: 70

INSTRUCTIONS:

1. Write your registration number on the answer booklet.
2. **DO NOT** write on this question paper.
3. This paper contains **SIX (6)** questions.
4. Question **ONE** is compulsory.
5. Answer any other **THREE** questions.
6. Question **ONE** carries **25 MARKS** and the rest carry **15 MARKS** each.
7. **Write all your answers in the Examination answer booklet provided.**

QUESTION ONE

Read the Case Study below carefully and answer the questions that follow:

SUSTAINABILITY AND CHALLENGES OF KENYA'S FINANCIAL SYSTEM IN A GLOBALIZED ECONOMY

In 2015, Kenya's financial sector was hailed as one of the most dynamic in Sub-Saharan Africa, with innovations such as M-Pesa revolutionizing financial inclusion. However, by 2020, concerns emerged about whether this growth was sustainable. Small and medium enterprises (SMEs) still struggled to access affordable credit despite an apparent abundance of financial instruments. Commercial banks, once seen as the backbone of Kenya's financial system, had become increasingly risk-averse, focusing on large corporate clients while excluding rural populations and low-income earners.

At the same time, capital markets in Kenya remained shallow. Only a handful of companies were cross-listed in regional exchanges, and investor confidence in the Nairobi Securities Exchange (NSE) fluctuated due to governance issues. The Capital Markets Authority (CMA) made several regulatory interventions, but critics argued that enforcement was inconsistent and reactive.

Financial intermediaries such as SACCOs and microfinance institutions attempted to fill the gap left by commercial banks, but their reach was limited, and cases of mismanagement further eroded trust. Moreover, asymmetric information between lenders and borrowers continued to drive adverse selection and moral hazard problems, discouraging credit growth.

Globally, Kenya was increasingly tied into international financial markets, with Eurobond issuance becoming a common tool for government financing. While this offered access to much-needed capital, concerns about rising debt levels and exposure to global shocks persisted. The COVID-19 pandemic in 2020 highlighted vulnerabilities, as global capital inflows contracted, hurting both government financing and private investment.

In response, regulators and policymakers emphasized the need for financial deepening, improved financial literacy, and reforms aimed at strengthening resilience. However, critics warned that reforms often lagged behind market realities, risking another cycle of instability in the financial system.

Required:

- a) Evaluate the role of Kenya's financial system in promoting economic development, using evidence from the case.

(10 Marks)

- b) Analyze the challenges of financial intermediation highlighted in the case and propose strategies to enhance inclusivity and trust.

(10 Marks)

- c) Assess the impact of internationalization of financial markets on Kenya's domestic financial stability.

(5 Marks)

QUESTION TWO

- a) Compare and contrast the concepts of financial repression and financial deepening, and evaluate their effects on the growth of financial markets in Africa. **(10 Marks)**

- b) Assess why studying banking and financial institutions remains critical in the contemporary global economy. **(5 Marks)**

QUESTION THREE

- a) Discuss five challenges of cross-border listing in East African capital markets.

(10 Marks)

- b) Assess the significance of organized exchanges in enhancing transparency and investor confidence. **(5 Marks)**

QUESTION FOUR

- a) Analyze five roles played by different financial intermediaries (depository institutions, contractual savings institutions, and investment intermediaries) in reducing transaction costs and managing risk. **(10 Marks)**
- b) Evaluate how asymmetric information contributes to adverse selection and moral hazard in Kenya's financial system citing examples. **(5 Marks)**

QUESTION FIVE

- a) Using relevant theories of interest rate determination, explain how interest rates influence both financial markets and commercial banking operations in Kenya. **(10 Marks)**
- b) Distinguish between real and nominal interest rates, and explain their importance to investors and policymakers. **(5 Marks)**

QUESTION SIX

- a) Assess the factors that have contributed to the rapid development of commercial banks in Kenya. **(10 Marks)**

- b) Discuss the conditions that encourage or limit financial innovations and analyze how such innovations have reshaped the banking industry.

(5 Marks)