



**UNDERGRADUATE UNIVERSITY EXAMINATIONS**

**SCHOOL OF MANAGEMENT AND LEADERSHIP**

**DEGREE OF BACHELOR OF COMMERCE**

**FIN 322 : FINANCIAL RISK MANAGEMENT**

**DATE: 28<sup>TH</sup> JULY 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**

**a)** The financial manager of Town Ltd. is concerned about the volatility of interest rates. His company needs to borrow Sh. 100 million in six months' time for a period of two years. Current interest rates are 15% per year for the type of loan that Town Ltd. needs. The financial manager does not wish to pay an interest rate higher than this. He is considering using different alternatives. For the following four alternatives, briefly explain how each could be useful to the financial manager:

- i.** Forward rate agreement. **(3 marks)**
- ii.** Interest rate futures **(3 marks)**
- iii.** Interest rate options. **(3 marks)**
- iv.** Interest rate swaps. **(3 marks)**

**b)** Explain two ways in which a firm can hedge against a currency transaction exposure  
**(6 marks)**

**c)** Cotts Importers Ltd, a company based in Kenya, has been a regular importer of goods from the United States of America (USA). The Kenyan currency is the Shilling (Sh.) while the USA currency is the dollar (\$).

On 1 June 2023, Cotts Ltd imported a consignment of goods from a supplier in the USA. The consignment cost \$1,000 and was payable on 1 September 2023.

The spot rates on 1 June and 1 September 2023 were as follows:

|             | \$/Sh. |
|-------------|--------|
| 1 June      | 0.007  |
| 1 September | 0.006  |

September 2004 shilling futures were trading at \$0.00625/Sh (contract size Sh.1,194,000) as at 1 June 2023.

**Required:**

- 1) Demonstrate how Cotts Ltd could have used a futures contract as a hedging tool, indicating any hedging profit or loss.

**(5 Marks)**

- 2) How many futures contracts would Cotts Ltd. have purchased if the contract size was Sh.2 million?

**(2 Marks)**

## **QUESTION TWO**

- a) Identify and explain five challenges associated with traditional models of credit risk analysis.

**(10 marks)**

- b) Explore five emerging trends or innovations in managing commodity price risk.

**(5 marks)**

## **QUESTION THREE**

- a) Examine five external factors in the broader economic environment that may impact a company's financial risk.

**(10 marks)**

- b) Explore five ways in which financial institutions assess and manage counterparty credit risk in their operations.

**(5 marks)**

## **QUESTION FOUR**

- a) Discuss five ways in which COVID-19 pandemic impacted financial risk management practices in the financial sector in Kenya.

**(10 marks)**

- b) Describe the role of Credit Default Swap (CDS) in hedging and speculative strategies.

**(5 marks)**

## **QUESTION FIVE**

a) Define a straddle strategy and describe how it is used in anticipating significant price movements.

**(10 marks)**

b) Discuss five roles of futures contracts in hedging financial risks **(5 marks)**

### **QUESTION SIX**

a) Differentiate between transaction risk, translation risk, and economic risk in the context of foreign currency risk.

**(9 Marks)**

b) Discuss the importance of scenario planning in preparing for extreme and unexpected events.

**(6 Marks)**