

KASNEB

CIFA PART I SECTION 2

FINANCIAL INSTITUTIONS AND MARKETS

PILOT PAPER

September 2015.

Time Allowed: 3 hours.

Answer any FIVE questions.

ALL questions carry equal marks.

QUESTION ONE

- (a) Discuss four evidence against market efficiency that exist in securities market. (8 marks)
- (b) (i) Summarise three attributes of a good capital market. (3 marks)
- (ii) Highlight five limitations facing capital formation in emerging economies. (5 marks)
- (iii) Define the term "Demutualisation". (1 mark)
- (iv) Highlight three objectives of demutualising the securities exchange market. (3 marks)

(Total: 20 marks)

QUESTION TWO

- (a) Highlight six roles played by the Capital Markets Regulator in your country in the development of financial markets. (6 marks)
- (b) In relation to foreign markets, describe four limitations of high frequency trading. (4 marks)
- (c) Define the term "margin trading" as used in secondary equity markets. (2 marks)
- (d) Explain four principles of financial sector regulations in your country. (8 marks)

(Total: 20 marks)

QUESTION THREE

- (a) Explain five roles of an Investment and Financial Analysts Institute in financial markets. (5 marks)
- (b) (i) Highlight six attributes of an ideal securities market index. (6 marks)
- (ii) A securities market is comprised of the following:

Security	Shares (millions)	Share prices		
		1 July 2013 Sh.	1 July 2014 Sh.	1 July 2015 Sh.
W	180	80	100	80
X	890	30	40	60
Y	500	60	70	75
Z	200	25	15	15

Required:

Compute the total return on the stock index over the two year period using:

- (i) A price weighted index. (5 marks)
- (ii) A value weighted index. (4 marks)

(Total: 20 marks)

QUESTION FOUR

- (a) Evaluate five differences between a financial forward contract and a financial future contract. (10 marks)
- (b) Following the economic conditions in your country, insurance companies have revised their yearly premiums charged for the policy holders as shown in the table below:

Company	Market Shares	Premium last year Sh.	Revised premium Sh.
A	3%	1019	1019
J	7%	861	?
B	21%	852	795
K	47%	938	887
C	5%	731	731

Company B intends to revise its premium charged to customers due to the competition in the industry.

Required:

- (i) Determine the key competitor company in the insurance industry, citing your reasons. (2 marks)
 - (ii) Using the parity based pricing principle, compute the revised price that company B should charge as premium to its policy holders. (4 marks)
 - (iii) Explain four advantages of using the parity pricing approach in pricing financial services. (4 marks)
- (Total: 20 marks)**

QUESTION FIVE

- (a) Outline four functions of financial markets in the economy of your country. (4 marks)
 - (b)
 - (i) Describe six factors that have contributed to the slow growth and development of capital market in many developing countries. (6 marks)
 - (ii) Name two reasons why channeling the capital from savers to spenders is important to the economy. (2 marks)
 - (iii) Explain four main challenges facing financial intermediaries in an emerging economy. (8 marks)
- (Total: 20 marks)**

QUESTION SIX

- (a) Discuss the factors that have slowed down the growth of financial markets in developing countries. (10 marks)
 - (b) Analyse the principles of fundamental analysis as applied in financial markets. (10 marks)
- (Total: 20 marks)**

QUESTION SEVEN

- (a) Describe five risks prevalent in foreign exchange markets. (10 marks)
 - (b) Summarise five factors that attract investors to unit trusts. (10 marks)
- (Total: 20 marks)**
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