This paper is not to be removed from the Examination Halls

UNIVERSITY OF LONDON **279 0029 ZB**

BSc degrees and Diplomas for Graduates in Economics, Management, Finance and the Social Sciences, the Diploma in Economics and Access Route for Students in the External Programme

Financial Intermediation

Wednesday, 14 June 2006 : 2.30pm to 5.30pm

Candidates should answer **FOUR** of the following **EIGHT** questions. All questions carry equal marks.

A hand held calculator may be used when answering questions on this paper but it must not be pre-programmed or able to display graphics, text or algebraic equations. The make and type of machine must be stated clearly on the front cover of the answer book.

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1. Describe the primary functions of financial intermediaries, and appraise the benefits and risks associated with the liquidity and maturity transformation services offered by banks.

2. Explain the role of financial institutions in terms of 'delegated monitoring', and outline the costs and benefits involved in delegated monitoring.

3. Critically appraise the relative importance of the different risks faced by banks, and comment briefly on the quantitative risk measures commonly used by banks.

4. Explain the nature and importance of 'credit risk', and discuss the relative value of internal and external credit ratings in assessing default risk.

5. In the context of bank asset and liability management, explain the principles involved in 'gap analysis', and the application of gap analysis in the management of liquidity risk and interest rate risk in particular.

6. Explain the importance of bank capital, with particular reference to current regulatory requirements for the maintenance and management of adequate bank capital.

7. Discuss the need for measures of bank performance, and explain the relevance of the 'risk-adjusted return on capital' and 'economic value added'.

8. Outline the features and pay-offs associated with forwards, futures, options and swaps, and explain how to price forward contracts using absence of arbitrage arguments.

END OF PAPER