

# Tutorial Letter 201/1/2018

Money and Banking

**BAN2601**

**Semester 1**

**Finance, Risk Management and Banking**

**IMPORTANT INFORMATION**

This tutorial letter contains the answers for Assignment 1 and 2

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## 1. INTRODUCTION

Dear Student

I hope you are finding the module interesting and that you were able to complete both assignments. You are again reminded to visit <https://my.unisa.ac.za>, especially before the examination. At *myUnisa* you will be able to get in touch with fellow students, update your details, find revision questions and additional resources, as well as participate in discussion forums. It is also important that you provide Unisa with your cellular number because announcements may be sent to you by sms.

The purpose of this tutorial letter is to provide you with suggested answers to Assignments 1 & 2 and give you guidelines for the examination.

## 2. SUGGESTED ANSWERS TO ASSIGNMENT 01

### SEMESTER 01

### ASSIGNMENT 01

**Due date:** 19 March 2018

**Unique number:** 694801

**Aim:** to evaluate your knowledge of some of the fundamental aspects of banking.

Answer the following questions and submit your assignment at <https://my.unisa.ac.za>

**Question 1** **(25 marks)**

**Why do economies need banks? Guided by the functions of a bank as an intermediately, discuss why banks are catalyst in the growth of economies.**

Banks are a critical ingredient to the growth of any economy.

Guided by the functions of a bank as an intermediary, discuss how banks can influence the growth of economies.

Banks provide 5 major functions:

*1. Create employment*

One of the biggest economic benefits emanating from the banking function is that they create employment to a number of a country's citizens.

As they go along serving their clients bank need manpower in the form of human labor and thus in that regard they become critical catalysts for economic growth.

## *2. Facilitate national payments*

Banks in the main make any economy tick. They facilitate national payments under the supervision of the Central Bank. A country's citizens are able to access their salaries through banks, international trade and other cross border payments are facilitated through commercial banks which make them pivotal in economic development.

## *3. Attract funds from depositors and on lend to deficit units of the economy there by encouraging economic growth.*

Through their branch infrastructure, banks are able to tap resources in the form of savings from surplus units of the economy and they then on lend that mostly to large corporations who in turn use the money to grow commerce and industry thus developing the economy.

In the case of governments, the government borrows mostly to fund infrastructure development which acts as a catalyst for economic development.

## *4. Cut (Reduce) Transaction costs*

As intermediaries one of the functions of a bank is to minimize transaction costs. Through intermediation, banks provide an avenue/platform for parties that are unfamiliar to each other to meet and transact thus in the process reducing cost of doing business with one another. Banks gather information on borrowers in bulk, and by the mere fact that they have that infrastructure that both borrowers and lenders utilizes, this results in the cost of doing business going down for parties

## *5. Facilitate and participate in the dissemination of monetary policy objectives.*

Banks are an agent to The Central Bank of any country. They assist in the dissemination of monetary policy objectives. As an example when there is a fight against inflation spearheaded by the Central Bank, banks are the main tool that the central bank will use in terms of curbing growth in money supply.

When The Central Bank changes the repo rate either way, banks are expected to adopt that and allow that to filter to the rest of the economy thus impacting negatively or positively on interest rates depending on the main drive from the Central Bank

*6. Maturity transformation and risk transformation.*

Converting short-term liabilities to long term assets (banks deal with large number of lenders and borrowers, and reconcile their conflicting needs and in the process they aid in economic development)

Banks also play a big role in converting risky investments into relatively risk-free ones. (Lending to multiple borrowers to spread the risk)

**(Student may discuss any 5 from the above. Maximum 5 Points per discussion point and credit to be given for citing examples. Two marks for listing and discussion point)**

**Total marks [25]**

### **3. SUGGESTED ANSWERS TO ASSIGNMENT 02**

#### **SEMESTER 01**

#### **ASSIGNMENT 02**

**Due date: 18 April 2018**

**Unique number: 792730**

**Aim:** To evaluate your knowledge of some of the fundamental aspects of the role of a Central Bank.

**Question1 (5 Marks)**

**Discuss inflation targeting with the reference to the role of South African Reserve Bank (example; why does the Reserve Bank use inflation targeting?)**

South African Reserve Bank formally introduced inflation targeting in February 2000, after announcing the intention to adopt the framework. Inflation targeting is the monetary policy framework in which South African Reserve Bank announces an explicit inflation target and implement policy to achieve this target directly.

**Example:**

The primary objective of using inflation targeting is to achieve and maintain price stability in the interest of sustainable and balanced. Price stability reduces uncertainty in the economy and therefore, provides favourable environment for growth and employment creation.

Inflation targeting protect living standards and not shift to prioritise growth as has been suggested in burgeoning row over bank independence. Changes to inflation targeting will include or focus on growth would lead to depreciation of the rand, deeper debt downgrades and uncertainty in the financial markets.

**(Students must give relevant discussion of inflation targeting. Maximum 3 marks for discussion and 2 marks for citing example)**

**Question 2**

**(10 Marks)**

**Credit markets play an essential role in sustaining economic growth. Briefly describe credit market participants and their role in the economy.**

1. *Borrowers*
2. *Small and medium enterprises*
3. *Credit providers*
4. *Credit rating agencies*
5. *Credit bureaus*
6. *Financial guarantee insurers or monopolies products*

**(Students must give a subheading and the discussion, may discuss any 5 from the above. Maximum 2 marks for point discussed. reference: Understanding South African financial markets 2012:pg 510)**

**Question 3**

**(10 Marks)**

**African Bank was recently on the brink of failure; however, the South African Reserve Bank intervened and placed it under curatorship. List and discuss three possible scenarios that led African Bank to the brink of failure.**

1. *Corporate governance issues by senior management*
2. *Breaching core banking principles which is credit and liquidity risk*
3. *Poor management of the bank*
4. *Excessive lending*
5. *Failure of bank management to conduct the business of the bank in a prudent*
6. *Failure to follow banking practices*
7. *Failure to comply with regulators*

**(Students must give a subheading that relates to African Bank failure and relevant discussion based on the subheading)**

**Total Marks**

**[25]**

#### **4. EXAMINATION GUIDELINES**

The examination will be a two-hour paper with a total of 70 marks.

The examination consists of six essay type questions all of which must be answered.

#### **5. CONCLUDING REMARKS**

Allow me to wish you well in the examination. Please note that you are welcome to contact me via *myUnisa* or by email at [endouaa@unisa.ac.za](mailto:endouaa@unisa.ac.za) if you have any questions regarding the assignments or the examination.

Adam Ndou

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