

**INSTITUTE OF BANKERS IN MALAWI**

**ADVANCED DIPLOMA IN BANKING EXAMINATION**

**SUBJECT: INVESTMENTS (IOBM - AD310)**

**Date: Friday, 18th May 2018**

**Time Allocated: 3 hours (08:00 – 11:00 Hours)**

**INSTRUCTIONS TO CANDIDATES**

1 This paper consists of **TWO** Sections, A and B.

2 Section A consists of 4 questions, each question carries 15 marks.

Answer **ALL** questions.

3 Section B consists of 4 questions, each question carries 20 marks. Answer **ANY TWO** questions.

4 You will be allowed **10 minutes** to go through the paper before the start of the examination, you may write on this paper but not in the answer book.

5 Begin each answer on a new page.

6 **Please write your examination number on each answer book used. Answer books without examination numbers will not be marked.**

7 All persons writing examinations without payment will risk expulsion from the Institute.

8 If you are caught cheating, you will be automatically disqualified in all subjects seated this semester.

9 DO NOT open this question paper until instructed to do so.

**SECTION A (60 MARKS)**

Answer **ALL** questions from this section

**QUESTION 1**

Explain why analysts always look at the following ratios before deciding which company stock to buy;

a) Return on capital employed ratio.  *(5 marks)*

b) Return on Assets ratio. *(4 marks)*

c) Current and Quick ratio. *(6 marks)*

**(Total 15 marks)**

**QUESTION 2**

Price Index for a country moved from 4129.80 to 4835.60 during period 31 December 2016 to 31 December 2017 respectively. A foreign investor is considering investing in this economy and has taken keen interest in the inflation statistics.

**Required**

1. Compute the inflation rate in year 2017. *(2 marks)*
2. Describe the price index that is used in calculating inflation rate. *(5 marks)*
3. Explain factors that can cause domestic currency to weaken against other currencies. *(6 marks)*

1. How can inflation rate movement affect the spread between nominal interest rate and real interest rate in an economy? (*2 marks)*

**(Total 15 marks)**

**QUESTION 3**

1. Describe Repurchase Agreements and how they are transacted on the financial market. *(9 marks)*
2. A Treasury bill worthy K 5,000,000 was sold by Bank **Q** to Bank **P**. Bank **Q** undertook to repurchase it after 54 days and will pay Bank **P** an interest rate of 22 % p.a.

**Required**

Calculate the interest rate payable on this deal*. (3 marks)*

1. If the underlying Treasury bill had a term to maturity of 182 days and a yield of 17 %, Calculate its purchase value. *(3 marks)*

**(Total 15 marks)**

**QUESTION 4**

Capital markets are known for their ability to uplift the economy as the make available cheaper capital for companies to access.

**Required**

1. Discuss **four** merits and three demerits of investing in capital markets. (*14 marks*)
2. Mention **one** characteristic of a capital market security. (*1 mark*)

**(Total 15 marks)**

**SECTION B (40 MARKS)**

Answer ANY **TWO** questions from this section

**QUESTION 5**

Futures contracts are agreements between two parties to undertake a transaction at an agreed price on a specified future date.

1. Give **three** attributes of a contract on whose basis an underlying asset can be established. *(6 marks)*
2. The spot price of a stock – index future is K1,500,000. If the purchase was to be financed by borrowed funds at an interest rate of 15 % p.a, calculate the price of the future in a year`s time given a storage and insurance cost of K35,000 for the period. *(4 marks)*
3. Explain **five** factors that have an influence on the price of a futures contract but are ignored when computing the price.  *(10 marks)*

**(Total 20 marks)**

**QUESTION 6**

A client approached a life insurer for investment on his behalf of an amount worthy K 60,000,000.

1. Describe **four** points the insurer is likely to consider in planning for this investment. *(8 marks)*
2. Discuss **two** reason why the insurer will not prefer placing these funds in hard assets. (*4 marks)*
3. The insurer participated in a bond tender which is to pay coupon at the rate of 16% p.a payable semi-annually. The tender was accepted at a discount price of 95.85.

**Required**

1. Calculate the purchase price if a nominal value of K 15,800,00 was invested. *(2 marks)*

1. Calculate total value of cash flow if the bond was sold at a discount rate of 98.15 after holding it for 18 months. *(4 marks)*
2. Calculate return on the bond investment. *(2 marks)*

**(Total 20 marks)**

**QUESTION 7**

1. Differentiate convertible preference share from Redeemable preference share.

*(4 marks)*

1. Explain how the basis of computing interest by compounding method differ from that of simple interest method. *(3 marks)*
2. Compute how much interest income will an investor get after 3 years if he deposits K 2,000 in a pure save account which pays interest semi-annually at the rate of 15 % p.a. *(5 marks)*
3. An investor was offered to buy a bond which is to pay coupon income every quarter for the next four years. Explain four assumptions that should be used in calculating purchase value of this offer. *(8 marks)*

**(Total 20 marks)**

**QUESTION 8**

Options for Futures contracts and Equity markets are highly patronised. Options can either be call option or put option.

1. Explain **four** reasons why option markets are so attractive and considered to be among the most liquid markets in the world. (*8 marks)*
2. Discuss **two** composition of an option price. *(6 marks)*
3. The current market price for a share is K65.00. The share carries a call option of K15.00 with an agreement that it can be purchased at K60.00 for the next three months. The option holder wants to exercise his rights in the next two months and it is expected that the share price will move to K70.00.

**Required**

Advise the holder whether to exercise the rights or not (show your calculations.) (*4 marks)*

1. Two parties entered into an option agreement. In course of the agreement, the seller forced the buyer to pay while the buy chose not to fulfil their arrangement.

**Required**

Advise whether the buyer has a case to answer for breaking the agreement.

(*2 marks)*

**(Total 20 marks)**

**END OF EXAMINATION PAPER**