

EXAMINATIONS

12 September 2001 (am)

Subject 301 — Investment and Asset Management

Time allowed: Three hours

INSTRUCTIONS TO THE CANDIDATE

1. *You have 15 minutes at the start of the examination in which to read the questions. You are strongly encouraged to use this time for reading only but notes may be made. You then have three hours to complete the paper.*
2. *You must not start writing your answers in the booklet until instructed to do so by the supervisor.*
3. *Write your surname in full, the initials of your other names and your Candidate's Number on the front of the answer booklet.*
4. *Mark allocations are shown in brackets.*
5. *Attempt all 10 questions, beginning your answer to each question on a separate sheet.*

AT THE END OF THE EXAMINATION

Hand in BOTH your answer booklet and this question paper.

*In addition to this paper you should have available
Actuarial Tables and an electronic calculator.*

1 Bank A and Bank B are two investment banks operating in the swaps market around highly developed and liquid bond markets in a country. A and B enter a swap agreement under which A “lends” cash to B in return for “borrowing” securities.

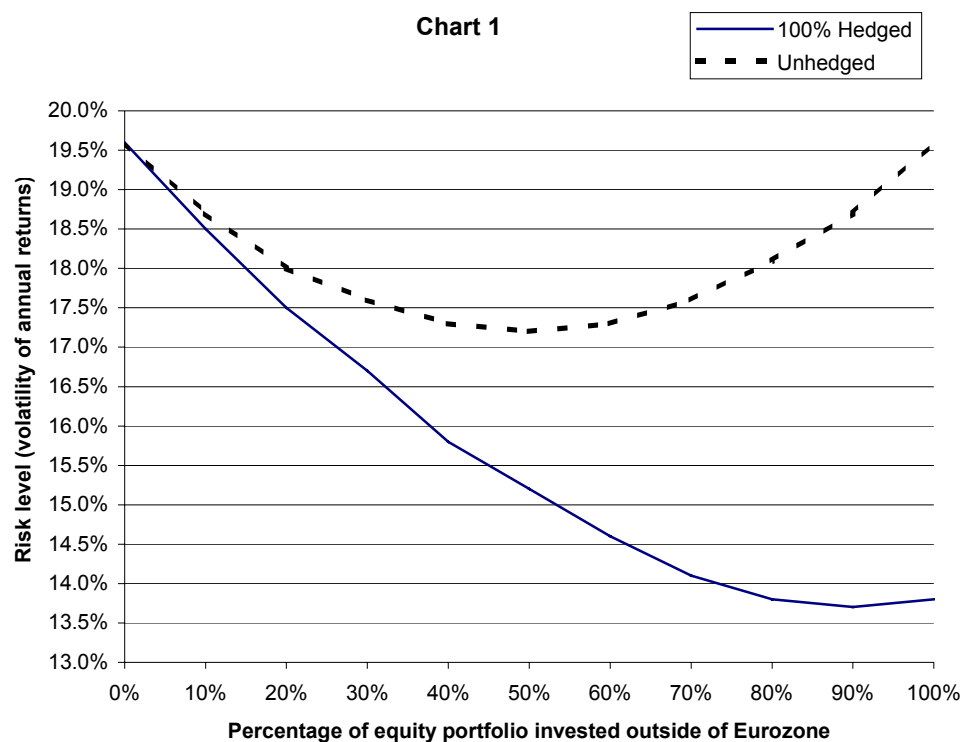
(i) Describe briefly the credit and market risk exposures faced by Bank A under the swap agreement. [2]

(ii) Describe briefly the steps that could be taken by A to mitigate the risks in (i) above. [4]

[Total 6]

2 Chart 1 below shows how the risk level of a portfolio of equities varies with the percentage of the portfolio invested outside of the countries of the European Monetary Union (Eurozone).

(i) Discuss briefly the risk implications of Chart 1 for a Eurozone investor who wishes to invest in equities outside the Eurozone but who has decided not to hedge the foreign currency exposure. [2]



(ii) Compare and contrast your answer to part (i) with the case where the Eurozone investor decides to fully hedge the foreign currency exposure in the portfolio. [4]

[Total 6]

- 3** (i) State the main aims of regulation in financial services markets. [2]
(ii) Discuss briefly the different ways a regulatory regime can be established. [4]
[Total 6]
- 4** (i) State briefly how you would expect returns from short-term and long-term fixed-interest government bonds to compare with original expectations:
(a) if inflation turns out to be lower than expected
(b) if yields are falling more than expected [4]
(ii) In a particular country, over the last ten years government bonds have outperformed property. Suggest briefly possible reasons for this. [6]
[Total 10]
- 5** (i) Outline the features of:
(a) unit trusts [3]
(b) investment trusts [3]
(ii) State two differences between unit trusts and open-ended investment companies. [1]
[Total 7]
- 6** (i) Describe briefly four methods of valuing an equity investment. [4]
(ii) For each method, comment on the main drawbacks. [4]
(iii) State with reasons your approach to valuing:
(a) a company operating in a number of different industries
(b) a property company [4]
[Total 12]
- 7** Discuss how economic influences have an impact on the property market. [13]
- 8** (i) Define immunisation and state the conditions for it. [4]
(ii) Describe briefly the problems in putting immunisation theory into practice. [7]
[Total 11]

- 9** You are the finance director of a motor car manufacturer who owns the freehold on the manufacturing facility. A property developer has offered to purchase the freehold. Outline the factors that you would need to take into account in deciding whether to recommend to your board the offer. [10]
- 10** You are an independent adviser to a French-based fashion clothing retailer, which is considering setting up a new internet subsidiary to sell its clothing range into the US market. Currently it has no distribution outside France.
- (i) Discuss the methods you would use to determine whether to pursue this venture. [7]
 - (ii) Identify the major risks involved in launching the subsidiary together with ways that these risks might be mitigated. [6]
 - (iii) Describe how you would choose the discount rate to be used in evaluating this project. [6]
- [Total 19]