

EXAMINATIONS

6 April 2001 (am)

Subject 401 — UK Fellowship Investment

Paper One

**You must answer this subject only,
you may not attempt another subject in the 400 series.**

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 9 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** The yield on the UK equity market has fallen.
- (i) Discuss possible reasons for the reduction in yield. [4]
 - (ii) State other indicators that you would use to assess the relative attraction of the equity market and discuss, with reference to them, your current investment view. [8]
- [Total 12]
- 2** Your friend has received a letter from his financial adviser recommending he invest a regular monthly amount into a new series of open-ended pooled funds covering the major overseas markets. Your friend has a small portfolio of overseas shares already and asks your opinion.
- Outline the issues that your friend ought to consider, including the regulatory implications of his enquiry. [12]
- 3**
- (i) State why the following factors may influence an institutional investor's long term investment strategy:
 - (a) future accrual of liabilities
 - (b) the strategy followed by other funds
 - (c) the expected long term return from the various asset classes

[3]
 - (ii) You are the advisor to a board of pension fund trustees. In a trustees' meeting, the chairman produces a cutting from last Sunday's newspaper showing their fund manager to be bottom of the annual performance league for the second year running. The pension scheme is a money purchase arrangement offering a choice of two equity orientated pooled funds managed on an active basis and a cash fund. Believing that the membership will be very concerned by the article, the trustees decide to change manager and the chairman suggests they should move the members' investments immediately from the manager's active equity funds to their cash fund to stop any further losses.
 - (a) List the possible sources of underperformance. [3]
 - (b) Suggest reasons why the newspaper article might not be a valid basis for comparison. [4]
 - (c) Discuss the chairman's proposal including any alternative courses of action for the trustees to consider. [10]

[Total 20]

- 4** (i) Describe the ten year return from the UK Government Fixed Interest market over the last ten years comparing it with the equivalent returns over longer time periods.
- Comment on the reasons behind the returns. [6]
- (ii) Discuss the related factors that an investment manager must take into account when seeking to invest in fixed interest securities in an environment where the domestic riskless yield curve is flat and the riskless interest rate is 0.5% per annum. [4]
- (iii) Describe the economic circumstances that could result in negative real interest rates. [2]
- [Total 12]
- 5** You have been offered an investment in medium term fixed interest rate bonds to be issued by a leading European football club. The bonds will be amortising and backed by the future receipts from ticket sales for attendance at the football club's home ground.
- (i) Discuss briefly any additional information that you require in order to evaluate this investment. [4]
- (ii) Discuss briefly the key features of this investment assuming that you have received a comprehensive response to your request for additional information. [6]
- [Total 10]
- 6** You are the advisor to a large final salary pension fund. The chairman of the board of trustees has written to you following a meeting which he has just had with one of the investment managers to the scheme. This particular manager has been performing poorly over the past two years and had blamed their problems on the fact that their particular style has been out of "vogue" recently. The chairman has asked for your comments.
- (i) Outline your reply in which you should discuss the principal active management styles and explain what part they can play in the strategy of a large scheme. [8]
- (ii) Some technical analysts make investment decisions by comparing the prices of two or more securities over time.
- Describe the use of such an approach to selecting:
- (a) fixed interest securities [2]
 (b) an investment manager [2]
- In each case justify the approach to a disbeliever. [Total 12]

- 7** A UK property company has decided to expand out with the UK. The company has established a wholly owned subsidiary in a particular country and intends to purchase and manage commercial property.

Describe briefly the types of taxes you would expect to encounter and their likely impact:

- (i) for the subsidiary in the foreign country [3]
 - (ii) for the UK company in respect of cashflow from the subsidiary [3]
- [Total 6]

- 8**
- (i) Outline the nature of a gilt strip. [1]
 - (ii) Discuss the supply and demand issues that would need to be overcome before a successful Eurobond strip market could commence. [5]
- [Total 6]

- 9**
- (i) Discuss briefly the problems in constructing an emerging markets index suitable as a basis for index tracking fund management. [8]
 - (ii) Comment briefly on any additional practical problems that would be encountered by a pension fund manager in using this index. [2]
- [Total 10]