

EXAMINATIONS

19 April 2004 (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. *Enter all the candidate and examination details as requested on the front of your answer booklet.*
2. *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.*
3. *You must not start writing your answers in the booklet until instructed to do so by the supervisor.*
4. *Mark allocations are shown in brackets.*
5. *Attempt all 8 questions, beginning your answer to each question on a separate sheet.*

AT THE END OF THE EXAMINATION

Hand in BOTH your answer booklet, with any additional sheets firmly attached, and this question paper.

<p><i>In addition to this paper you should have available Actuarial Tables and your own electronic calculator.</i></p>
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- 1** A trustee of a large UK pension fund has questioned why the fund has no direct exposure to commodities.
- (i) Set out the points you would make to explain why the fund is not exposed to commodities. [6]
 - (ii) Detail the various methods by which the fund can achieve exposure together with their advantages and disadvantages. [9]
- [Total 15]
- 2**
- (i) Detail the charges relating to dealing that an institution operating in the UK equity market will expect to pay and compare them with the charges the same institution would expect to pay if dealing in the US market. [5]
 - (ii) Describe what is meant by a programme trade and how the charges will differ from those outlined in part (i). [3]
 - (iii) Explain why an equity analyst may prefer to look at:
 - (a) Earnings before interest, tax, depreciation and amortisation of goodwill rather than pre-tax profit.
 - (b) Cash-flow yield rather than dividend yield.
 - (c) Interest cover rather than the debt equity ratio.
- [8]
[Total 16]
- 3** Briefly describe the three elements of institutional finance of a property development and explain how the profit is determined. [6]
- 4**
- (i) Describe an Individual Savings Account (ISA). [4]
 - (ii) List the stocks and shares that are eligible for inclusion in an ISA. [2]
- [Total 6]
- 5** The client of a medium-sized fund manager would like its existing portfolio to be managed on an ethical basis. You, as an employee of the fund manager, have been asked to produce a report on the issues that need to be addressed by both the client and the fund management group before the portfolio can be transitioned into the ethically-based portfolio.
- Outline the points you would make in a report. [14]

- 6** (i) Outline the features and operation of:
- (a) long gilt futures contracts
 - (b) short interest rate futures contracts
 - (c) UK equity index futures contracts
- [12]

A fund has £600 million invested in UK equities, £300 million in gilts and £100 million in cash. The UK equity index is at 4400, the long gilt future is at 106 and short-term interest rates are 4.0%. Without selling any of the existing assets the manager wishes to change the asset allocation to 50% equities, 45% gilts and 5% cash.

- (ii) Demonstrate how this can be achieved. [4]
- (iii) Explain why the performance of the fund may differ from a notional fund allocated in the same proportions (50% equities, 45% gilts and 5% cash). [4]
- [Total 20]

- 7** Outline the Financial Services Authority's principles for conduct of investment business. [10]

8

	<i>Fund at start of period</i>	<i>Fund at end of period</i>	<i>New investment income</i>	<i>Benchmark Return</i>	<i>Benchmark Weight</i>
UK Equities	600	675	25	9.0%	50%
UK Gilts	300	325	(5)	8.0%	45%
Cash	100	104	0	3.5%	5%

- (i) Using the above information calculate the component parts of the fund's investment performance, stating any assumptions you make. [10]
- (ii) Comment on the results. [3]
- [Total 13]

END OF PAPER