

EXAMINATIONS

September 1999

Subject 201 — Communications

Time allowed: 1½ hours

INSTRUCTIONS TO THE CANDIDATE

Write your surname in full, the initials of your other names and your Candidate's Number on the front of the answer booklet.

AT THE END OF THE EXAMINATION

Hand in BOTH your answer booklet and this question paper.

<p><i>In addition to this paper you should have available Actuarial Tables and an electronic calculator.</i></p>
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Your aunt has decided that she will invest a lump sum in a UK equity fund. She has compared two funds and has noted that they both describe charges as having the effect of absorbing 1.6% of the fund p.a. over a five year period for a typical investment.

She has also noticed that the second fund allows subscribers to invest amounts on a monthly basis. Under this option the charges have the effect of absorbing 2.5% p.a. over five years. Although she has already decided that she will invest a lump sum rather than a monthly amount, she is curious and wants to understand why the monthly investment option is so much more expensive.

The information you have available is as follows:

- The first fund has an initial charge of 2.5% of the investment which does not vary according to the size of investment. In addition an annual charge of 1.0% of the value of the fund is levied.
- The second fund has an initial charge of 4.75% of the investment. This is reduced to 3.75% for investments of £20,000 or above. In addition an annual charge of 0.5% of the value of the fund is levied.

Your aunt has said that she intends to invest the lump sum “for a few years”. She has not said how much she intends to invest.

Draft a letter to your aunt in 500–600 words explaining how the charges should influence her choice of fund and why the impact of the charges is greater under the monthly option.

Notes

Your answer should be confined to addressing the impact of charges for these two funds. It should not discuss other investment performance differences. It should not discuss whether a UK equity fund is appropriate or discuss alternative investments.

You should assume that:

- there are no other charges.
- the charges are the only difference between the two funds.
- the same charges apply to funds invested as a lump sum or on a monthly basis
- for both funds, the investment can be cashed-in at any time.
- there are no restrictions on giving investment advice.
- your aunt is intelligent, but not expert in actuarial matters.