

**INSTITUTE OF BANKERS IN MALAWI**

**DIPLOMA IN BANKING EXAMINATION**

**SUBJECT: FINANCIAL MARKETS 1 (IOBM – D203)**

**Date: Thursday, 17th May 2018**

**Time Allocated: 3 hours (13:30 – 16:30 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**

1. Describe the **three** types of users of the derivatives markets. *(5 marks)*
2. Calculate the expected three month (91day) forward foreign exchange (FX) Rate if the current spot FX rate is USD/MWK 735 and the three-month interest rates are 1.5% in USD and 23% in MWK. *(10 marks)*

**(Total 15 marks)**

**QUESTION 2**

1. What is a Reverse Repo? *(2 marks)*
2. Describe Repo Operations? *(8 marks)*
3. Your firm is involved in a Repo transaction involving a large investment banking firm dealing in government securities, selling K10 million par value of Malawi government bonds to a medium sized bank at a price of K8,890,000.00. The investment bank agrees to repurchase the bind at MK10 Million the next day.

**Required:**

Calculate the Repo rate on this transaction. *(5 marks)*

**(Total 15 marks)**

**QUESTION 3**

1. Define an Annuity.  *(2 marks)*
2. An investment is expected to produce annual cash inflows of K1Million for 20 years, starting in one year’s time.

**Required:**

Using the estimated cost of capital of 15%, calculate the total present value of

these cash flows. *(5 marks)*

1. Describe how floating rate bonds operate in Malawi. *(8 marks)*

**(Total 15 marks)**

**QUESTION 4**

Today’s short-term forward yield is quoted as:

|  |  |  |
| --- | --- | --- |
| **Maturity** | **Quoted forward yield** | **Period** |
| 0-3 months | 2% | 1 |
| 3-6 months | 2% | 2 |
| 6-9 months | 2.5% | 3 |

Assuming an initial investment of K1Million, with re-investment of maturity proceeds in the later periods:

1. Calculate the face value at the end of period 1,2 and 3 *(10 marks)*

(**hint**: use months and not days in your calculations e.g. 1 month =1/12)

1. Calculate the periodic yields for the periods 0-6 months and 0-9 months from the cash flows of 6 and 9 months respectively (as calculated in part (i) above. *(5 marks)*

**(Total 15 marks)**

**SECTION B (40 MARKS)**

**Answer ANY TWO questions from this section**

**QUESTION 5**

1. Define the **three** types of financial markets. *(3 marks)*
2. Describe any **four** characteristics of good financial markets. *(12 marks)*
3. A company has just paid a dividend of K10 per share. Dividend growth is anticipated to be 5% and cost of equity is 8%.

**Required:**

Calculate the current share price of the company. *(5 marks)*

**(Total 20 marks)**

**QUESTION 6**

1. Discuss whether a Commercial Paper program is issued in the public or private markets. *(5 marks)*
2. Explain any **three** factors that should be considered when a company is to consider setting up a Commercial Paper program. *(10 marks)*
3. Mention any **five** types of costs arising from operating a Commercial Paper programme. *(5 marks)*

**(Total 20 marks)**

**QUESTION 7**

In an economy interest rates volatility is mostly experienced in short, medium and long-term run.

**Required:**

Discuss any **five** factors that affect general level of interest rates in an economy.

**(Total 20 marks)**

**QUESTION 8**

1. Discuss the contents of a liquidity plan and its importance to banks. *(10 marks)*
2. Explain how bank runs happen and strategies for mitigating bank runs. *(10 marks)*

**(Total 20 marks)**

**END OF EXAMINATION PAPER**