

**INSTITUTE OF BANKERS IN MALAWI**

**ADVANCED DIPLOMA IN BANKING EXAMINATION**

**SUBJECT: FINANCIAL MARKETS 2 (IOBM – AD303)**

**Date: Sunday, 12th 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**

Discuss **five** factors that affect the price of an Option.

**(Total 15 marks)**

**QUESTION 2**

1. Differentiate spot rate from a forward rate. *(3 marks)*
2. Consider the following exchange rates:

**Bid Offer**

Dollar/sterling ($/£) 1.4580 1.4980

Sterling/Euro (£/€) 0.4570 0.4890

**Required:**

1. What would be received in pounds sterling by a UK company expecting to receive $400,000? *(3 marks)*
2. What would be paid in pound sterling by a UK company expecting to pay $500,000?

*(3 marks)*

1. What would be received in pounds sterling by a UK company expecting to receive €400,000? *(3 marks)*
2. What would be paid in pound sterling by a UK company expecting to pay €500,000?

*(3 marks)*

**(Total 15 marks)**

**QUESTION 3**

1. Mention **two** strategies that might be used in order to limit the exposure to interest rates volatility and explain **three** problems that the strategy may have. *(9 marks)*
2. Define the following:
   * 1. Default risk. *(2 marks)*
     2. Risk structure of interest rates.  *(2 marks)*
     3. Reinvestment risk. *(2 marks)*

**(Total 15 marks)**

**QUESTION 4**

1. Discuss **four** objectives of economic policy. **(***12 marks)*
2. Explain the relationship between interest rate and quantity of money. *(3 marks)*

**(Total 15 marks)**

**SECTION B (40 MARKS)**

Answer **ANY TWO** questions from this section

**QUESTION 5**

A company wants to issue a bond that is redeemable in four years for its par value or face value of MK1000, and wants to pay an annual coupon of 5% on the par value.

**Required**

1. Estimate the price at which the bond should be issued, and *(17 marks)*
2. calculate its gross redemption yield. *(3 marks)*

The annual spot yield curve for a bond of this risk class is as follows:

Year Rate

1. 3.5%
2. 4.0%
3. 4.7%
4. 5.5%

**(Total 20 marks)**

**QUESTION 6**

For any country to develop its economy it has to put in place sound economic policies that will assist in achieving this goal.

**Required:**

Discuss **seven** problems that may affect the country in the implementation of the economic policies.

**(Total 20 marks)**

**QUESTION 7**

1. Differentiate demand pull inflation from cost push inflation? (*4 marks)*
2. Illustrate the causes of inflation and their policy control methods used to reduce the effects. (*16 marks)*

**(Total 20 marks)**

**QUESTION 8**

Malawi Financial sector is currently using the free floating system as regards to Interest rates. There have been calls from some quarters of the society for interest rates to be capped as they believe that Banks are charging exorbitant rates that cripple the economy.

**Required**

Discuss whether or not Malawi financial sector need interest rate capping.  **(Total 20 marks)**

**END OF EXAMINATION PAPER**