

**INSTITUTE OF BANKERS IN MALAWI**

**DIPLOMA IN BANKING EXAMINATION**

**SUBJECT: PRINCIPLES OF INVESTMENT (IOBM-D208)**

**Date: Tuesday, 10th May 2016**

**Time Allocated: 3 hours (08:00 -11:00 Hours)**

**INSTRUCTIONS TO CANDIDATES**

1 This paper consists of **TWO** Sections, A and B.

2 Section A consists of 20 multiple choice questions, each question carries 2 marks. Answer **ALL** questions.

3 Section B consists of 5 questions, each question carries 20 marks. Answer **ANY THREE** questions.

4 You will be allowed **10 minutes** to go through the paper before the start of the examination when 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 sheets 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. You are a financial analyst working for a financial institution. A pensioner approaches you for advice regarding a K20 000 000.00 investment he would like to make. Explain to him the meaning of required rate of return and its two components. *(5 marks)*
2. Evaluate the riskiness of the following two investments by calculating the expected return for each of the following alternatives. *(10 marks)*

|  |  |  |
| --- | --- | --- |
| **INVESTMENT A** | **PROBABILITY** | **ASSOCIATED RETURN** |
| Boom | 0.3 | 25% |
| Normal | 0.4 | 20% |
| Recession | 0.3 | 10% |
|  |  |  |
|  |  |  |
| **INVESTMENT B** | **PROBABILITY** | **ASSOCIATED RETURN** |
| Boom | 0.3 | 16% |
| Normal | 0.4 | 12% |
| Recession | 0.3 | 8% |

**(Total 15 marks)**

**QUESTION 2**

1. Calculate the Beta of a portfolio which consists of the following assets and their associated betas. *(5 marks)*

**Security Beta Value**

X 0.9 K1 000 000

Y 1.2 K2 000 000

Z 0.7 K2 000 000

1. An analyst has gathered the following information;

Expected return on the market = 15%

Risk free rate = 8%

Estimated rate of return of NBM shares = 17%

Beta of NBM= 1.25

**Required:**

Based on the above mentioned information, determine whether it is worthy investing in NBM shares or not. *(5 marks)*

1. Define a preference share and briefly explain any **two**  of its types. *(5 marks)*

**(Total 15 marks)**

**QUESTION 3**

You are an investment manager of a pension fund and you have been allocated some funds from a pool of investors. Briefly outline the **five** steps you would follow to ensure that funds under your control are well managed.  **(Total 15 marks)**

**QUESTION 4**

Discuss the function of money markets, with emphasis to Its categories, participants and instruments that are used in these markets

**(Total 15 marks)**

**SECTION B (40 MARKS)**

Answer **ANY TWO** questions from this section

**QUESTION 5**

1. K460 000.00 is deposited in a fixed account at Nedco Bank on April 1, 2011 and will remain in the account until March 31, 2012 earning an interest of 8% per annum compounded quarterly.

**Required:**

Calculate the future value. *(5 marks)*

1. Calculate the present value of receiving a single amount of K5 000 000.00 at the end of three years, if the time value of money is 8% per year, compounded quarterly. *(5 marks)*
2. Distinguish Capital Market Line from Security Market Line. *(10 marks)*

**(Total 20 marks)**

**QUESTION 6**

1. The table below has two investment proposals and it is presented to you for analysis. Which one will you recommend for implementation, if the Net Present Value technique is used? Assume the cost of capital is 12% per annum.

*(10 marks)*

|  |  |  |
| --- | --- | --- |
|  | **Proposal A** | **Proposal B** |
| Year 0 (initial outlay) | 100,000 | 120,000 |
|  | Cash inflows | Cash inflows |
| 1 | 85,000 | 90,000 |
| 2 | 65,000 | 90,000 |

1. How do Net Present Values (NPV) differ from Internal Rate of Return (IRR). In your answer include the decision making criteria. *(10 marks)*

**(Total 20 marks)**

**QUESTION 7**

1. Briefly discuss **three** classes of bond markets with an emphasis on risk versus return and their advantages and disadvantages *(15 marks)*
2. Using the Capital Asset Pricing Model (CAPM): Calculate the expected return of a stock, if the risk-free rate is 6%, the beta (risk measure) of the stock is 1.2 and the expected market return over the period is 13 %. *(5 marks)*

**(Total 20 Marks)**

**QUESTION 8**

1. What is the advantage of analysing the company’s macroeconomic influences and the industry before investing in individual companies? *(10 marks)*
2. Michael porter (1985) highlighted five determinants of competition. Briefly discuss how these determinants drive industry competition. *(10 marks)*

**(Total 20 marks)**

**END OF THE EXAMINATION PAPER**