CHARTERED INSTITUTE FOR SECURITIES & INVESTMENT

December 2014 Examination

Financial Markets

Date of exam	Wednesday 03 December 2014
3 hours	2.00 pm – 5.00 pm
Rubric	Section A – answer **four** questions in this section
	Section B – answer **both** question in this section
	Section C – answer **all** parts of the question in this section

Candidates are reminded that no marks will be awarded for illegible work

Notes to candidates

1. Please insert your candidate number on the cover of your answer book. **Do not insert your name.**
2. Show **all** workings in your answer book.
3. Candidates may attempt the sections in any order. Please indicate clearly in your answer book which questions you are answering.
4. Please insert in the box provided on the cover of your answer book the numbers of the questions you have attempted in the order in which they appear in the answer book.
5. You may use the calculator provided or a model approved by the CISI.
6. You must hand your answer book to an invigilator before you leave the examination hall. **Failure to do so will result in disqualification**.
7. Once submitted, the examination scripts become the property of the CISI and will not be returned to candidates.

Please turn over when instructed

Section A Total 20 Marks

Answer **four** questions in this section.

1. Explain how the “expectations theory” is used in the bond markets. (5 marks)

2. Discuss the potential problems with the accounting concepts of “true and fair” value. (5 marks)

3. Explain the dealing and settlement system for Eurobonds. (5 marks)

4. The Market Abuse Directive covers the “Misuse of Information”. Discuss exactly what the misuse of information means. (5 marks)

5. Explain “purchased goodwill” as an intangible non-current asset. (5 marks)

6. Discuss the disadvantages of offshore banking for an investor. (5 marks)

Section B Total 40 Marks

Answer **both** questions in this section.

Each question carries 20 marks.

Question 7

Mr Whyte has inherited investments in many countries of the world, denominated in various currencies, and has some questions for you about international investments.

a) Explain to him comments he has seen that the Euro should **not** be considered a "Reserve Currency". (4 marks)

b) He has also been told that his portfolio now includes Synthetic Agreements for Foreign Exchange (SAFEs).
   i) Explain to Mr Whyte what these are. (3 marks)
   ii) Discuss the reasons why they would be included in his portfolio. (3 marks)

c) He is worried about reports that the BRIC economies are not necessarily such good investments as they once were thought to be. Briefly discuss the attractiveness and subsequent worries about the BRIC economies. (10 marks)

Question 8

Mr Mason has been informed that a company in his portfolio intends to initiate a "reverse stock split" and that this will have no effect on his overall position. He does not understand what this means and has asked you for information.

a) Explain what a "reverse stock split" is and the reasons why a company might choose to do this. (3 marks)

b) The efficient markets hypothesis (EMH) says that a reverse stock split would have no effect on overall value. Discuss why this may not be the case.(10 marks)

c) He wonders if a "share repurchase" might be better for him and the company. Discuss the implications of a repurchase (including the impact on any financial ratios). (7 marks)

Section C — Total 40 Marks

Answer **all** parts of the question in this section.

Question 9

Ms Hart owns 100,000 shares in Ocset plc, which have a market price of £2.25. The dividend is 14.7p and the growth rate is 2%. She has seen that the value of Ocset plc's shares has been falling recently and believes that they will continue to fall for the near future. She is aware that she can take advantage of this potentially falling market price by using derivative solutions.

a) Explain how, in her review of the share price, she can evaluate the variability of its returns. (5 marks)

b) Critically discuss which derivative instruments Ms Hart could **best** use to benefit from the projected share price movement. (12 marks)

Ms Hart has seen that she could purchase an Ocset issued 10 year Convertible Bond which allows her to convert to shares at a rate of £2.50 per share and pays a coupon of 6.5% (she would wish to receive a return of at least 7.5% on all of her investments). It is trading today at £90, having just paid its last coupon yesterday.

c) Using the dividend growth model, what should the share price be? Show your working. (5 marks)

d) Discuss how she could price the convertible bond to see if the current market price would allow her to make her desired return. (8 marks)

e) Ms Hart thinks that the entire market may be going to go through a volatile period for a few years and is therefore considering investing in a hedge fund, in distressed companies or infrastructure funds. Critically appraise these potential investments for her. (10 marks)

Total 40 marks