



PENINSULA
COLLEGE
GEORGETOWN

FINAL SEMESTER EXAMINATION
(in compliance with MQA's requirement)

Programme	:	BA (HONOURS) ACCOUNTING & FINANCE
Academic year	:	2022/23
Stage	:	3
Course	:	UNDERSTANDING FINANCIAL MARKETS
Course Code	:	MAL1026
Time Allowed	:	3 HOURS

INSTRUCTIONS TO CANDIDATES:

1. Please read the instructions given in the question paper **CAREFULLY**.
2. This question paper consists of **FOUR (4)** questions.
3. Answer **ALL** questions.
4. Answers to the questions are to be written into the examination booklet.
5. Electronic dictionaries, lecture notes, files or any unauthorised materials except writing equipment are strictly prohibited.

This question paper must be submitted along with all used and/or unused rough papers and/ or graph papers (if any). Candidates are **NOT ALLOWED** to take any examination papers out of the examination hall.

(This booklet contains 4 printed pages including this page)

DO NOT OPEN THIS BOOKLET UNTIL YOU ARE ALLOWED TO DO SO

WARNING:

The Examination Board of Peninsula College Georgetown regards cheating as a very serious offence and will not hesitate to mete out the appropriate punitive actions according to the severity of the offence committed, and in the accordance with the clauses stipulated in the Students' Handbook, up to and including expulsion from Peninsula College Georgetown.

For examiner's use only

QUESTION NO.	MARKS
1	/ 25
2	/ 25
3	/ 25
4	/ 25
Total	/ 100

Answer **ALL** questions.

1. a) Orien Bhd. has RM5 million floating rate loan outstanding. The interest rate on the said loan is reset every six (6) months. Due to the recent volatile money market, the corporate treasurer thinks that interest rate is likely to rise in the future. The current 6-month interest rate is 5.5% per annum and the corporate treasurer can get a rate of 6% per annum for a 6-month forward rate agreement (FRA) starting one month from now which is the contracted review period for each 6-month roll-over of the loan. Instead of entering into an FRA, she was told by the company's banker that interest rate futures could also be used to protect the company's interest. She is now undecided on which course of action to take.

Required:

Assuming that the corporate treasurer has decided to enter into a forward rate agreement with the company's banker, calculate the potential gain or loss if the following two scenarios were to occur:

- i. If the interest rate rises to 7% per annum. (4 marks)
 - ii. If the interest rate falls to 4.5% per annum. (4 marks)
- b) Briefly explain **FOUR (4)** differences between forward contract and futures contract. (8 marks)
- c) Stock BB is currently trading at RM16 in the market. Andrew, an investor, is anticipating that there will be a fall in the price of Stock BB in the future. A six-month expiration option is written by an underwriter with a strike price of RM17.50 and premium of RM185 per contract. Consider that each option contract consists of 100 shares.

Required:

- i. Explain how Andrew can make a profit from trading in the option of Stock BB if the market is up to his expectation. (3 marks)
- ii. Explain the maximum amount of loss that Andrew will face if the market is not up to his expectation. (2 marks)
- iii. If Andrew has purchased the option based on his expectation, calculate the profit/loss that he will make if the market price rises to RM25 at expiry. Justify your answer. (4 marks)

[Total: 25 marks]

2. a) Due to the rising interest rate, the stock market collapsed out of investors' fear and panic. Jessica is a full-time housewife, she is concerned about the benefits of investing part of her savings with financial institutions and has approached you for advice.

Required:

As a professional financial analyst, explain **ANY THREE (3)** types of financial intermediaries and justify **ANY FOUR (4)** benefits of financial intermediation to Jessica. (21 marks)

- b) Distinguish between primary markets and secondary markets. (4 marks)
[Total: 25 marks]

3. a) Bonds are units of corporate debt issued by companies. Currently, bonds are known as one of the most popular investments in the market.

Required:

- i. Discuss **ANY THREE (3)** features of a bond. (9 marks)
- ii. Explain the term "premium bond". (2 marks)
- iii. Calculate and explain how an investor can earn from the premium bond with a 10-year 9% coupon bond which is selling at RM112 with a par value of RM100. (6 marks)

- b) Different types of stocks have different characteristics.

The following are the details about your clients, Anne and Mathew:

	Anne	Mathew
Age	26	52
Investment objectives	Capital gains	Balance between capital gains and income
Risk Appetite	High	Moderate
Liquidity needs	Low	High
Time Horizon	Long term	Medium Term

Required:

Recommend **TWO (2)** types of stocks to each of them with justifications. (8 marks)
[Total: 25 marks]

4. a) Assume the following spot and forward rates for the US dollar against the Australian dollar (USD/AUD).

Spot rate	USD 0.7510
90-day forward rate	USD 0.7564
120-day forward rate	USD 0.7590

Required:

- i. Suppose you issued a 120-day forward contract to exchange 100,000 Australian dollars into U.S. dollars. Compute how many U.S. dollars are involved. (2 marks)
 - ii. Compute how many Australian dollars can you get for one US dollar in the spot market. (2 marks)
- b) Distinguish between transaction risk and translation risk. (6 marks)
- c) The spot exchange rate between Pound Sterling and Ringgit Malaysia is £1 = RM5.30. Based on the law of one price and purchasing power parity theory, a cup of drink costs £3 in the United Kingdom will cost RM15.90 in Malaysia. Inflation in Malaysia is expected to be 5% per year, while inflation in the United Kingdom is expected to be 7% per year.

Required:

Compute the future spot rate in a year's time. (3 marks)

- d) Assess **ANY FOUR (4)** factors that could affect the movements in exchange rates. (12 marks)
[Total: 25 marks]

- END OF QUESTIONS -