



CHARTERED INSTITUTE OF STOCKBROKERS

March 2007 Professional Examination Level 3

PAPER 3.1: SECURITIES ANALYSIS AND PORTFOLIO MANAGEMENT

Tuesday, March 27, 2007 Morning Session

Time allowed: 3 hours (9.00 a.m. to 12.00 noon)

Additional Material: Answer Booklet

Instructions to candidates

This paper is divided into two sections.

Answer five questions in total:

*In **Section A**, answer **all** parts of **Question 1**.*

*In **Section B**, answer any **four** of the six questions.*

The number of marks is given at the end of each question or part question.

*The question in **Section A** carries, in total, **30 marks**.*

*The questions in **Section B** carry, in total, **70 marks**.*

Follow the instructions on the front cover of the Answer Booklet.

Answer your questions in the Answer Booklet provided, additional sheets may be used. At the end of the examination, fasten all your work securely together.

All workings should be shown. Where calculations are required using formulae, calculators may be used but steps in the workings must be shown. Calculations with no evidence of this (for example, using the scientific functions of calculators) will receive no credit. Programmable calculators are not permitted in the examination room.

Statistical tables and graph paper are available from the invigilator, where applicable.

SECTION A

**Answer ALL parts of this question.
Each part question carries 3 marks.
Total marks for this question: 30 marks**

- 1** (a) List the advantages and disadvantages of a convertible bond to the issuer.
- (b) State the disadvantages of a sinking fund provision to the investor.
- (c) What is the efficient frontier and how is it identified?
- (d) What is bull campaign of bear raid?

Write short notes on the following terms:

- (e) Roll
- (f) Characteristic line
- (g) Collateral trust bond
- (h) Asset plays
- (i) Pay-in-kind feature
- (j) Repo

SECTION B

**Answer four questions from this section.
Total marks for this section: 70 marks**

- 2** You are the Investment Manager of the Holloway Limited Pensions Fund which operated an in-house contributory pension scheme for its employees. As at June 2004, the value of the pension funds was N350 million and the company was desirous of continuing to administer the scheme.

Required:

Prepare a report to the Board advising them on how to make the pension scheme conform to the Pension Reform Act, 2004.

Total 17 marks

- 3 (a)** You are considering investment in one or two securities, X and Y, and you are given the following information:

Security	Possible rates of return %	Probability of occurrence
X	30	0.3
	25	0.4
	20	0.3
Y	50	0.2
	30	0.6
	10	0.2

Required:

- (i) Calculate the expected return for each security separately and for a portfolio comprising 60% X and 40% Y, assuming neutral correlation between the possible rates of return from the shares comprising the portfolio;
- (ii) Calculate the expected risk of each security separately and of the portfolio as defined above. (For this purpose the measure of risk may be taken as the standard deviation of probable variances from the expected rate of return); and
- (iii) Outline the objectives of portfolio diversification, and to explain in general terms why the risk on individual securities may differ from that of a portfolio as a whole.

(15 marks)

- (b) In examining a company's straight debentures and subordinated convertible debentures, both issued at the same time with the same maturity and at par, you note that the coupon and yield for the subordinated convertible debenture are lower than for the straight debenture.

Required:

Discuss the return potential for the convertible bond in an environment of stable interest rates and rising stock prices that would explain its lower coupon and yield.

(3 marks)

Total 18 marks

- 4** A client wants to know the basic differences between (i) Classical immunization, (ii) Contingent immunization, (iii) Cash-matched dedication, and (iv) Duration-matched dedication.

- (a) Briefly describe each of these four techniques.
- (b) Briefly discuss the ongoing investment action you would have to carry out if managing an immunized portfolio.
- (c) Briefly discuss three of the major considerations involved with creating a cash-matched dedicated portfolio.
- (d) Describe two parameters that should be specified when using contingent immunization.
- (e) Select one of the four alternative techniques that you believe requires the last degree of active management and justify your selection.

Total 17 marks

5 Required:

- (a) Briefly discuss the implications of the efficient market hypothesis for investment policy as it applies to:
(i) technical analysis in the form of charting, and (ii) fundamental analysis.
- (c) Briefly explain two major roles or responsibilities of portfolio managers in an efficient market environment.
- (d) Briefly discuss whether active asset allocation among countries could consistently outperform a world market index. Include a discussion of the implications of integration versus segmentation of international financial markets as it pertains to portfolio diversification, but ignore the issue of stock selection.

Total 18 marks

- 6** (a) Musa Ltd has an opportunity to invest in a project lasting one year. Usman Ltd has three projects, each lasting one year, but in different industries. The net cash flows and the beta factors for each of the projects are as follows:

	N'000	β
Musa Ltd	500	1.20
Usman Ltd	200	1.25
	100	0.80
	200	1.35

The market return is 12% and the risk-free rate of interest is 7%.

Required:

- (i) Calculate the total present value of the projects that can be undertaken by Musa Ltd and Usman Ltd.
- (ii) Calculate the overall beta factor for Usman Ltd's projects, assuming that all three are undertaken.
- (iii) Using this information, discuss which company is likely to be valued more highly by investors.

(11 marks)

- (b) **Required:**

- (i) Briefly discuss three disadvantages of the constant growth dividend discount model in its application to investment analysis.
- (ii) Identify three alternative methods to the dividend discount model for the valuation of companies.

(6 marks)

Total 17 marks

7 Required:

Explain fully each of the following:

- (a) Disintermediation
- (b) Securitisation
- (c) Financial conglomerate

Total 18 marks



CHARTERED INSTITUTE OF STOCKBROKERS

March 2007 Professional Examination Level 3

PAPER 3.2: FINANCIAL FUTURES AND OPTIONS

Tuesday, March 27, 2007 Afternoon Session

Time allowed: 3 hours (2.00 p.m. to 5.00 p.m.)

Additional Material: Answer Booklet

Instructions to candidates

This paper is divided into two sections.

Answer five questions in total:

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SECTION A

**Answer all parts of this question.
Each part question carries 2 marks.
Total marks for this question: 30 marks**

- 1** (a) Laworo Salabo pays N2.45 to buy a call option with a strike price of N42. What stock price will make Laworo Salabo to earn N3 from her call option position?
- (b) Consider a hypothetical futures contract in which the current price is N240. The initial margin requirement is N15, and the maintenance margin requirement is N10. When could there be a margin call from the point of view of
- the long, and
 - the short.
- (c) The current spot exchange rate for the dollar against the Japanese Yen is 146 Yen per dollar. What is the corresponding US dollar value of one Yen?
- (d) A call option is currently trading at N10. The option has an exercise price of N50. If the stock price is N54, what is the speculative value of the option?
- (e) What is normal backwardation?
- (f) A delta-neutral hedged position included a long stock position and 10,000 short call option with a delta of 0.7. If the delta changes to 0.5, what action needs to be taken in order to maintain the hedge?
- (g) The spot price of an asset is N232 and the 1-year futures price is N351. What is the implied repo rate, continuously compounded?
- (h) Explain why a swaption can be regarded as a type of bond option.
- (i) How does the exercise price affect the price of a call? Explain.
- (j) Explain why brokers require margins from clients when they write options but not when they buy options.
- (k) UACN declares a 3-for-1 stock split. Explain how the terms of a call option with an exercise price of N90 change.
- (l) For a change in the value of the underlying asset from N50 to N40, the value of a call option declines from N12 to N8. What is the value of the call's delta?
- (m) Find the implied present value of the exercise price of a 13-week call option, given that the value of the call is N8, the value of the put option is N5 and the current market price of the stock is N20.

- (n) What is the payoff of a 3-month NIBOR call option with a strike of 3.25%, and a N100,000,000 notional value, if NIBOR is at 3.5% at expiration? (Assume 360 days).
- (o) With respect to the futures market, explain the distinction between a normal and an inverted market.

SECTION B

**Answer four questions from this section.
Total marks for this section: 70 marks**

- 2** Ayayo Pharmaceutical Company has been approached by an entrepreneur who has patented a new drug to treat bird flu. The entrepreneur has obtained approval of the relevant government agency and has the patent rights for the next 20 years. Although the drug shows promise, it is still very expensive to manufacture and has a relatively small market. The initial investment to produce the drug is N500m and the present value of the cash flows from introducing the drug now is only N350m. The annualized variance of returns on similar pharmaceutical companies is estimated to be 529%. The relevant 20-year risk-less rate is 7%.

Required

- (a) Using the Black-Scholes option pricing model for the life of the patent, estimate the call value of the option to commercially develop and market the drug.
- (b) Provide a reasoned recommendation, based upon your calculations and any other relevant information as to whether or not the company should develop the drug

Note: State all assumptions clearly.

Total 18 marks

3 Required:

- (a) Why is option contract referred to as contract for the difference? (2 marks)
- (b) Distinguish between volatility and wasting asset. (3 Marks)
- (c) What impact does decay of time has on option price? (2 Marks)
- (d) What is bed and breakfast and how does it operate? (3 Marks)
- (e) What are the main investment attractions of put and call contract? (4 Marks)
- (f) Distinguish breaking forward from participating forward. (3 Marks)

Total 17 marks

Questions

- 4 Consider the following three securities. Assume that at one period in the future the market will move either up or down. This movement in the market produces the following payoffs for the three securities.

Security	Current price	Payoff when the Market moves down	Payoff when the market moves up
A	N70	N50	N100
B	N60	N30	N120
C	N80	N38	N112

Required:

- (a) Construct a portfolio consisting of securities B and C that replicates the payoffs on security A in both the up and down states subject to the constraint that the sum of the commitments to the two securities (B and C) is one. In other words, construct a synthetic of security A. Assume that there are no restrictions associated with short selling any of the securities.
- (b) What are the commitments to securities B and C?
- (c) How much does it cost to construct a synthetic share of security A? Which security is cheaper?
- (d) Explain the transactions necessary to engage a risk-less arbitrage. How much profit can an investor make in this risk-less arbitrage? Assume that one trades 10 shares of security A in constructing the arbitrage transactions.

Total 17 marks

- 5 (a) Below are the closing prices of options on NBC when the stock price is 58.75.

Use the information below to answer the following questions (i) – (iv):

Strike Price	Call Prices			Put Prices		
	April	May	June	April	May	June
50	5.75	6.85	7.35	0.105	0.425	1.05
60	2.28	2.86	4.15	0.325	0.715	1.35
70	1.05	1.85	2.25	3.25	4.25	5.75

Required:

- (i) What is the intrinsic value of May 50 call?
- (ii) If May 60 call is purchased, how much must the stock price increase in order for the option holder to breakeven?

- (iii) If May 70 put is purchased and the stock price subsequently climbs to 68.50 at option expiration, what will be the loss if the put holder exercises?
 - (iv) If a June 50 put is purchased, determine the stock price at option expiration in order for the put buyer to generate a profit of N1.55.
- (b) A call option on Mobil is currently selling for 6.25. Its exercise price is N80.00.

Required:

How much must the stock be selling for at expiration in order for the holder of the call to earn a N3.75 profit?

Total 18 marks

- 6** A 9-month forward contract on a dividend paying stock is entered into when the stock price is N80.00 and the risk-free rate of interest is 10% with continuous compounding for all maturities. Dividend of 60k and 80k are expected to be paid after 3 and 6 months respectively.

Required:

Calculate:

- (a) The present value of the dividend payments *(6 Marks)*
- (b) The forward price of the contract *(6 Marks)*
- (c) The value of the forward contract *(6 Marks)*

Total 18 marks

- 7** The result of the awareness generated by the advertisement by banks and the general growth in equity prices resulting from the increased capital base of banks and the new funds pouring into the equity market has created a wave of activities in the capital market. This is exacerbated by the funds coming from the pensions sector of the economy. With the real sector not growing at the same pace and very few companies coming as new listings, the demand pressure on the existing equity on the Stock Exchange is bidding the stock prices out of reach.

To combat the above problems, the NSE had been organising seminars and workshops to develop alternative instruments in the market. In one of those seminars, a speaker spoke about primitive instruments. It is now clear to the Exchange and SEC that derivative trading is a sine qua non to future growth of the market.

Required for question 7:

- (i) What do you understand by the term primitive instruments? Give two examples.
- (ii) What are the differences between forward contract and future contract?
- (iii) In general, futures and options contracts must stipulate specific terms of the contracts. Name five of these terms.

Total 17 marks



CHARTERED INSTITUTE OF STOCKBROKERS

March 2007 Professional Examination Level 3

PAPER 3.3: MARKETING OF FINANCIAL SERVICES

Wednesday, March 28, 2007 Morning Session

Time allowed: 3 hours (9.00 a.m. to 12.00 noon)

Additional Material: Answer Booklet

Instructions to candidates

This paper is divided into three sections.

Answer five questions in total:

*In **Section A**, answer **all** parts of **Question 1**.*

*In **Section B**, **Question 2** must be answered.*

*In **Section C**, answer any **three** of the five questions.*

The number of marks is given at the end of each question or part question.

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*The question in **Section B** carries, in total, **25 marks**.*

*The questions in **Section C** carry, in total, **45 marks**.*

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SECTION A

**Answer all parts of this question.
Unless otherwise indicated, each part question carries 1 mark.
Total marks for this question: 30 marks**

- 1** i. The best use of production life cycle to a marketing practitioner is that it helps to:
- (a) Determine the marketing strategy to be adopted
 - (b) Forecast the likely progress of a product
 - (c) Determine the fate of a product
 - (d) Know when the start up costs will be received
 - (e) Know how long it will take to complete the various stages
- ii. Reasons for developing new products do not include
- (a) Profit improvement
 - (b) Capital acquisition
 - (c) Technological change
 - (d) Political/ Legal requirement
 - (e) Competition
- iii. Legal designation giving owner exclusive right of use of a brand is:-
- (a) Brand name
 - (b) Brand mark
 - (c) Trade mark
 - (d) Trade name
 - (e) Non of the above
- iv. What completes the process of production is:-
- (a) Product positioning
 - (b) Production
 - (c) Promotion
 - (d) Distribution
 - (e) Pricing
- v. Objectives an enterprise may decide to achieve do not include:-
- (a) Growth
 - (b) Goodwill
 - (c) Market share
 - (d) Profit
 - (e) Sales force compensation
- vi. The need to satisfy customers that have preference for a particular product or exhibit similar characteristics in terms of buying habits and behaviour will influence decision to establish:
- (a) Market-oriented organization
 - (b) Product-oriented organization
 - (c) Customer-oriented organization

Questions

- (d) Matrix organization
(e) Mixed organization
- vii. Product life cycle is chronologically best described as
(a) Introductory-growth-decline-maturity
(b) Introductory-growth-maturity-decline
(c) Introductory-decline-maturity-growth
(d) Introductory-maturity-growth-decline
(e) Introductory-maturity-decline-growth.
- viii. The cheapest mode of transportation is by
(a) Sea
(b) Road
(c) Rail
(d) Air
(e) Pipeline
- ix. A non-paid and non-personal form of creating information, events and news about a company, product or service is:-
(a) Advertising
(b) Sales Promotion
(c) Personal Selling
(d) Publicity
(e) None of the above
- x. Effective modern marketing organizations are marked by a strong cooperation and customer focus among the following departments but one:-
(a) Marketing
(b) R&D/ Engineering
(c) Financing
(d) Works
(e) Purchasing
- xi. Organization of personnel along the proper principles of specialization is ----- component of a marketing audit:-
(a) Sales Force
(b) Price
(c) Marketing objectives and goals
(d) Customers
(e) Promotion
- xii. The rate of return on marketing investment (ROMI) is:-
(a) $\frac{MC}{ME}$ (b) $\frac{GMC}{ME}$ (c) $\frac{NMC}{ME}$ (d) $\frac{GOC}{ME}$ (e) $\frac{NOC}{ME}$

Questions

- xiii. Telling the product "story" using a features, advantages, benefits and value approach (FABV) is ----- step in the effective sales process.
- (a) Prospecting and qualifying
 - (b) Pre-approach
 - (c) Follow-up and maintenance
 - (d) Presentation and demonstration
 - (e) None of the above
- xiv. The attribute of a product that makes use of the core product convenient, easy and enjoyable such as brand name, packaging, styling etc. is called: -
- (a) Inner layer
 - (b) Outer layer
 - (c) Augmented
 - (d) Core
 - (e) Formal/ Fringe
- xv. That services are typically produced and consumed simultaneously is ----- characteristic of services: -
- (a) Inseparability
 - (b) Intangibility
 - (c) Variability
 - (d) Perishability
 - (e) None of the above.
- xvi. Pricing product differently at different places even though the cost of offering at each place is the same is discriminatory pricing called:-
- (a) Time Pricing
 - (b) Location Pricing
 - (c) Channel Pricing
 - (d) Customer Segment Pricing
 - (e) Image Pricing
- xvii. Goods purchased after careful and thorough plan such as food items, are called:-
- (a) Unsought goods
 - (b) Unpulse goods
 - (c) Staple goods
 - (d) Emergency goods
 - (e) Shopping goods
- xviii. Warehouse storing goods requiring the payment of tax is called:-
- (a) Integrated warehouse
 - (b) General merchandise warehouse
 - (c) Public warehouse
 - (d) Bonded warehouse
 - (e) Private warehouse

- xix. Intensive growth is made up of:
- (a) Market penetration
 - (b) Market development
 - (c) Product development
 - (d) All of the above
 - (e) Only (a) and (c)
- xx. The main objective of advertising is:
- (a) To increase
 - (b) To increase market share
 - (c) To inform about institution activities
 - (d) To announce new product
 - (e) To create awareness and sustain product acceptance
- xxi. Stages of the Buying Decision Process is in this best order:-
- (a) Problem Recognition → Information Search → Evaluation of Alternatives → Purchase Decision → Post Purchase Behaviour
 - (b) Problem Recognition → Information Search → Evaluation of Alternatives → Post Purchase Behaviour → Purchase Decision.
 - (c) Problem Recognition → Information Search → Evaluation of Alternatives → Purchase Decision.
 - (d) Problem Recognition → Information Search → Purchase Decision Evaluation of Alternatives.
 - (e) Problem Recognition → Information Search → Purchase Decision → Evaluation of Alternatives.
- xxii. The tendency to twist information into personal meanings and interpret information in a way that will fit our pre conceptions is perceptual process called:-
- (a) Selective attention
 - (b) Selective distortion
 - (c) Selective retention
 - (d) Collective attention
 - (e) Collective retention
- xxiii. Foreign investors and local investors joining hands to share ownership and control of business is a method of entering foreign market referred to as:-
- (a) Direct export
 - (b) Direct investment
 - (c) Joint ventures
 - (d) Indirect export
 - (e) Licensing

Questions

- xxiv. Setting low price to attract customers to a store and stating the actual price to them on getting into the store is called:-
- (a) Bait and switch pricing
 - (b) Moral pricing
 - (c) Perceived value pricing
 - (d) Retail pricing
- xxv. Middlemen dealing in complete assortment but in a restricted single line are called:-
- (a) General line wholesalers
 - (b) Specialty wholesalers
 - (c) General merchandise wholesalers
 - (d) Service wholesalers
 - (e) Local wholesalers
- xxvi. The three (3) additional PS for service marketing do not include:-
- (a) Process
 - (b) People
 - (c) Promotion
 - (d) Physical evidence
 - (e) None of the above
- xxvii. Attitude towards colour, brand names, design and music is called:-
- (a) Social organization
 - (b) Technological culture
 - (c) Material culture
 - (d) Aesthetics
 - (e) Mores
- xxviii. Factors uncontrollable to the market include:-
- (a) Price
 - (b) Promotion
 - (c) Product
 - (d) Distribution (Place)
 - (e) Economic
- xxix. The function of executing by the marketing manager does not include:-
- (a) None of the below
 - (b) Directing
 - (c) Leading
 - (d) Staffing
 - (e) Organizing
- xxx. Control device often used to ensure that immediate corrective action is taken while marketing operation is in progress is:-
- (a) Organizational Design Control
 - (b) Pre-action Control
 - (c) Post-Action Control
 - (d) Organizational Norms and Values Control
 - (e) Steering Control

SECTION B

**This question MUST be attempted.
Total marks for this section: 25 marks**

2 UPPERMOST BANK PLC

Uppermost Bank PLC started business in Nigeria in 1968. Workers were allowed to buy shares and become shareholders. The ownership and family atmosphere promoted made the bank non-union and gave workers a feeling of belongingness. Perfect labour relation with little supervision reigned. Pride of ownership made employees to guard their performance and be proud of the services they offered. Cooperation was unalloyed, as table-senior managers were known to assist in attending to customers to cut cues and customers delays.

The family spirit and employee-loyalty untold in the history of banking in the country made Uppermost to maintain no layoffs. When there was industrial salaries cut in in late 1970s, uppermost rewarded its workforce with a 10 percent raise. In appreciation of this gesture, employees came together and invested a substantial sum of ten billion naira into the bank.

Service satisfaction obtained in the bank made the bank a leader in the industry with 80 percent of the banking public. The introduction of a new product - "the Diaspora account" in 1979 geometrically influenced the goodwill and profit of the bank. In 1980 it declared 24 billion naira after-tax profit.

Bank recapitalization policy of the Federal Government of the country in 2006 did not catch the bank unaware, as it possessed 20 times capital required by the government policy. The level of success achieved by the bank became a thing of envy in the industry and this catapulted to scheming out Mr. Duro, its Managing Directors' chances of becoming the President of the Bankers' Institute.

The goodwill, however, deteriorated with the stiff competition and aggressive marketing by competitors immediately after the end of recapitalization. Leadership programme project was developed to return the company to profitability and leadership status.

Mr. Duro, the Chairman, President and CEO, stated at the rollout of the new programme that the company wanted to reduce cost, not jobs, and at the same time change the way it operated. The technological re-engineering resulting from those changes in the banks' operations necessitated downsizing. The downsizing commenced in three phases thus:

- (1) Leaves of absence and voluntary severance and retirement
- (2) Early retirement to people aged 50 and above and
- (3) Layoffs.

Questions

The streamlining included 2,500 jobs cut from its cleaning, security and messenger personnel. The duties from these jobs were diffused to part-time workers and outside contractors. Customer service also became casualty of the programme. The Central Bank's Department of Banking Supervision reported in early 2006 that the numbers of complaints about Uppermost were much greater than in the past year. Frequent customers were upset about fewer paying and receiving personnel, imperfect services, growing queues and delays.

"Since the past six to ten months I have noticed it is not the same" said large account holder, Titi Ishola. He contented that he once felt privileged to bank with Uppermost. As a result of the cutbacks, he complained that banking seemed like undertaking 'ESUSU' local contribution.

"They made decisions and operated contrary to their history, culture and past practices," said Sina Madojutimi, President of the Bankers Association in 2006 interview.

Uppermost executives agreed that their cutbacks may have been too extensive. Some problems with timeliness were attributed to less experienced workers' and imperfect services. Frequent complaints from employees that the direct services staff was too lean led to rehiring some counter workers whom Uppermost had previously released.

Post research shows that:

- (i) Decline in morale contributed to the customer service problem
- (ii) The way the management treated the employees directly affected the manner in which employees treat their customers.
- (iii) Feeling of security had been replaced with thought of betrayal and insecurity
- (iv) The popular slogan in the company now is "trust" nobody and "conform" to save your job.

Solution to Uppermost problem cannot be easily reached. Profit is no longer forth coming; so its executives had to make changes in order to save jobs and potentially the bank. A new combination of low employee and customer satisfaction persist for the once preferred bank.

Required:

- a. Is there a need to downsize and why?
- b. How could Uppermost rebuild its employee morale and have it passed on to its customer?
- c. What could Uppermost have done differently to maintain high levels of profit and customers' service as staff numbers were decreasing?

SECTION C

**Answer three questions from this section.
Total marks for this section: 45 marks**

3 Your organization is challenging the market leader in the brokerage industry.

Required:

Explain how you can manipulate the marketing mix elements to launch aggressive and specific attack.

Total 15 marks

4 Required:

- (a) As the marketing manager of a financial services firm, explain how you might achieve market segmentation. *(10 marks)*
- (b) How might market segmentation be used when selecting an appropriate marketing strategy for a bank's services. *(5 marks)*

Total 15 marks

5 Required:

What are the implications of the e-banking revolution in the financial services industry in terms of the benefits and constraints encountered as a result of the peculiar environmental circumstances of Nigeria?

Total 15 marks

6 "As soon as plans and programs are developed in the strategic marketing planning, managers design and develop an organization that can carry out these programs successfully"

Required:

- (a) What is the purpose of a marketing organization? *(7 marks)*
- (b) As a marketing manager of a financial services firm, what steps will you take in setting a marketing organization that can carry and support your marketing strategies and programs. *(8 marks)*

Total 15 marks

- 7** Your firm has been approached by a foreign institution with a view to engaging in a strategic business relation in your country.

Required:

- (a) What are the criteria for embarking on a business relationship with a foreign financial institution? *(8 marks)*
- (b) What are the likely hidden barriers to international business relations? *(7 marks)*

Total (15 marks)



CHARTERED INSTITUTE OF STOCKBROKERS

March 2007 Professional Examination Level 3

PAPER 3.4: REGULATIONS AND PRACTICE OF STOCKBROKING

Wednesday, March 28, 2007 Afternoon Session

Time allowed: 3 hours (2.00 p.m. to 5.00 p.m.)

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Follow the instructions on the front cover of the Answer Booklet.

Answer your questions in the Answer Booklet provided, additional sheets may be used. At the end of the examination, fasten all your work securely together.

All workings should be shown. Where calculations are required using formulae, calculators may be used but steps in the workings must be shown. Calculations with no evidence of this (for example, using the scientific functions of calculators) will receive no credit. Programmable calculators are not permitted in the examination room.

Statistical tables and graph paper are available from the invigilator, where applicable.

SECTION A

**Answer ALL parts of this question.
Each part question carries 3 marks.
Total marks for this question: 30 marks**

1 Write short notes on the following:

- (a) Dual trading
- (b) Liquidity risk
- (c) Glamour stock
- (d) Vendor consideration issue
- (e) Capitalisation issue
- (f) Registered bond
- (g) Sector rotation strategy
- (h) Defensive stock
- (i) Stock splits
- (j) Yield gap

SECTION B

This question MUST be attempted.
Total marks for this section: 25 marks

- 2** The projected balance sheet of Trim Securities Limited, a registered stockbroking firm with the Securities and Exchange Commission at December 31,2007 is as follows:

	Actual 2006 N'000	Projected 2007 N'000
Ordinary share capital	20,000	20,000
Preference share capital	6,000	6,000
Reserves	15,000	27,000
Mortgage on freehold property	950	1,800
Dividend payable	3,000	6,000
Clients' Deposit account	4,050	133,900
Overdraft	1,000	
Other creditors and accruals	4,500	21,000
	54,500	215,700
Freehold property (at cost)	16,000	16,000
Plant and machinery. (at cost less depreciation)	11,000	28,000
Margin Account	10,000	120,000
Own Investments	7,500	27,500
Debtors & other assets	10,000	16,500
Bank	-	7,700
	54,500	215,700

In preparing the 2007 projections, management decided to embark on aggressive expansionist policy to grow the company to achieve the following:

- (i) Net asset value of over N200 million by December 2007.
- (ii) To seek for and execute average daily mandate of N200 million worth of share purchases for clients.
- (iii) To achieve (ii) above, credit facilities would be offered on generous terms to clients to buy securities. 2007 year end balance on the margin account is expected to be N150 million.
- (iv) Targeted average daily sale mandate of N250 million.

The above accounts and budgeted figures were given to you by the Managing Director to review. The Managing Director is very keen to implement the budget so as to change the fortune of the company.

Required for question 2:

Comment on the projected balance sheet for 2007 in the light of all applicable rules and regulations and advise the Managing Director on steps to take if the projections are to be realised.

Total 25 marks

SECTION C

**Answer three questions from this section.
Total marks for this section: 45 marks**

- 3** (a) Describe underwriting. *(2 marks)*
- (b) Who may act as underwriters in Nigeria? *(3 marks)*

- (c) List the contents of an underwriting agreement as specified in SEC rules.
(10 marks)

Total 15 marks

- 4** The transactions cost of doing business in the Nigerian capital is very high relatively to other countries.

Required:

- (a) List three charges levied each in the primary and secondary markets.
(3 marks)
- (b) What are the implications of the high charges in the Nigerian capital market on market development?
(5 marks)
- (c) What would be the effects of a reduction in transactions cost in the Nigerian capital market?
(7 marks)

Total 15 marks

- 5** Explain the following concepts:

- (a) Fundamental analysis
(b) Technical analysis
(c) Random walk hypothesis

Total 15 marks

- 6** What major factors must be considered when constructing a stock market index?

Total 15 marks