



DIPLOMA SUMMER 2008 EXAMINATION

INVESTMENT ANALYSIS

DATE OF EXAM	Tuesday 24 June 2008
3 Hrs 15 mins	2.00 pm – 5.15 pm
RUBRIC	SECTION A - ALL parts of the question in this section are to be answered SECTION B – ALL questions in this section are to be answered SECTION C – TWO questions in this section are to be answered

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 one approved by the Securities & Investment Institute.
 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. The decision of the panel is final and no correspondence will be entered into concerning the grade awarded.
 8. Once submitted, the examination scripts become the property of the Securities & Investment Institute and will not be returned to candidates.
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PLEASE TURN OVER WHEN INSTRUCTED

SECTION A**TOTAL 40 MARKS**

Answer ALL parts of the question in this section. All parts refer to Kier Group plc.

Question 1

- a) Briefly describe the main activities of Kier Group plc in the year ending 2007. (3 marks)
- b) Calculate and comment upon the operating profit margin of Kier Group plc for the years ending 2006 and 2007 by each of its major business activities. (4 marks)
- c) Analyse and briefly comment upon the ability of Kier Group plc to finance new investments from free cash flow in the years ending 2006 and 2007. (4 marks)
- d) Analyse and comment upon the changing liquidity position of Kier Group plc over the years ending 2006 and 2007. (5 marks)
- e) Briefly explain the nature and control of the key risks identified by Kier Group plc. Which of these risks are beyond the Group's locus of control? (3 marks)
- f) Briefly comment on Kier's *integrated business model* as detailed on page 22. (3 marks)
- g) Prepare forecasts of profit before and after tax and earnings per share for Kier Group plc for the year ended 30th June 2008. Explain the basis of your computation and of any assumptions that you have made. (10 marks)
- h) Advise on the desirability of investment in the shares of Kier Group plc at the price shown on page 1 of the Information Pack. Explain the reasons behind the advice given. (8 marks)

SECTION B**TOTAL 30 MARKS****Answer ALL questions in this section**

- 2 What is meant by *geared* and *ungeared equity betas* and how are they related?
(4 marks)
- 3 In your own words, briefly define the following economic terms:
a) Stagflation
b) Fine-tuning
c) Economies of scale
(3 marks)

- 4 Using the Capital Asset Pricing Model (CAPM) expression, calculate the missing values (R_f , R_m and β) in the table below:

	Expected return on share	Risk-free rate	Equity beta	Expected return on the market portfolio
Share A	12.9%	R_f	1.1	12.0%
Share B	13.4%	7.0%	0.8	R_m
Share C	11.2%	4.0%	β	10.0%

(3 marks)

- 5 You purchase a £100 bond in 2008 which pays a coupon of 6% every year. If the bond matures in 2023 and similar bonds offer 4.5%, what is the value of the bond?
(3 marks)
- 6 Give three reasons why debt finance might be considered more attractive than equity finance in the funding of a company acquisition.
(4 marks)
- 7 Company XYZ plc is forecast to pay a dividend of £3.00 per share next year, thereby paying out 100% of its earnings. This will give its investors an expected return of 10%. However, if the company instead decided to reinvest 30% of its earnings at its current return on equity of 20%, what is the value of a share in XYZ plc before and after its reinvestment decision?
(4 marks)
- 8 a) Explain what is meant by the term '*warrant*' and how it differs from a *call option*.
(2 marks)
- b) The warrants of ABC plc allow the holder to buy three shares at £20 per share and they expire in 2009. The share itself is currently valued in the market at £24 per share and the warrant is priced at £12. Calculate both the intrinsic value of warrant and its time value.
(2 marks)

- 9 a) What is meant by Gross Domestic Product (GDP) and how does this differ from Gross National Product (GNP)? *(2 marks)*
- b) What is the current growth rate of real GDP for the UK economy and the Government's projection of growth over the next two fiscal years? *(2 marks)*
- c) How do the forecasts in *b)* differ from the estimates of other independent forecasters? *(1 mark)*

**Answer TWO questions in this section.
All questions carry 15 marks each.**

- 10 Discuss the determinants of a country's exchange rates.
- 11 Explain how *behavioural finance* studies have led investors to question the Efficient Markets Hypothesis.
- 12 Discuss frameworks or models appropriate for analysing the industry to which a company belongs.
- 13 What is meant by *private equity* and what need is there for it in developed financial markets?
- 14 Discuss the benefits and costs of *Depository Receipts* and the factors that have driven their recent growth in popularity.