EASTERN UNIVERSITY, SRI LANKA
FACULTY OF COMMERCE AND MANAGEMENT
DEPARTMENT OF COMMERCE

Third Year/ Second Semester Examination in Commerce- 2012/2013 (July/August 2015)
(Proper/ Repeat/Re-Repeat)

DED 3043 Capital Market and Financial Institutions

Answer all questions **Time: 03 Hours**
Non-Programmable calculator permitted

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01. (i) What are the major functions of the **Central Bank of Sri Lanka**? **(03 marks)**

(ii) Briefly explain the various domestic and foreign banking services provided by **Commercial Banks in Sri Lanka**? **(04 marks)**

(iii) What is meant by **"Merchant Banks"**? Briefly explain Fund Based Services and Fee Based Services. **(04 marks)**

(iv) Explain how the **Insurance companies** play the role in the financial market in Sri Lanka. **(06 marks)**

(v) Define **"Unit Trust"** and briefly explain the major parties who are involved in it. **(04 marks)**

(vi) What are the roles of **Finance Companies** in our economic development? **(03 marks)**

(vii) Explain how the **Employees Provident Fund (EPF)** and the **Employees Trust Fund (ETF)** contributes to the development of financial market in Sri Lanka? **(06 marks)**

(viii) What is the difference between **Money Market** and **Capital Market**? **(06 marks)**

(ix) Explain the instruments used in a developing money market and capital market with special reference to Sri Lanka **(06 marks)**

(x) Briefly explain the milestones of **Colombo Stock Exchange (CSE)** **(04 marks)**

(Total 40 Marks)

02. (i) Distinguish between the following terms:

a. Primary Share Market and Secondary Share Market

b. Main Board and Diri Savi Board

c. S & P Sri Lanka 20 Index and All Share Price Index

d. Treasury bills and Treasury bonds.

e. Inter Bank Call Money Market and Internal Foreign Currency Market

(05 x 02 = 10 Marks)

(ii) Write short notes on the following:

a. Bond Market
b. Leasing Companies
c. Investment Trust
d. Central Depository System (CDS)
e. Securities and Exchange Commission of Sri Lanka (SEC)

(05 x 02 = 10 M

(Total 20 M

03. (i) The common stock of **A Ltd.** paid Rs. 2.00 as dividends last year. Divide expected to grow at an 8% annual rate for an indefinite number of years.

a. If the **A Ltd.** current market price is Rs. 30.00, what will be the expected rate of return?

b. If the investor required rate of return is 10%, what will be the stock's e rate of return?

c. Should you make the investment? Explain.

(06

(ii) A bond has an 8% coupon rate. The interest is paid semi annually and t mature in 10 years. Its par value is Rs. 1000.00, if your required rate of r 8%

a. What is the value of bond?

b. What is its value if the interest is paid annually?

(04

(iii) An investor considers bonds of two companies. **AN PLC's** bond pays payment at 12% and **YP PLC's** at 6% per year. Both have face value 1000.00 and maturity of 03 years.

a. What will be the values of bonds if the market interest rate is 9%?
b. What will be the values of bonds if the market interest rate increases to 1
c. Which bond declines more in the value when the interest rate rises? W reason?

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(iv) The market value of Rs 1000 par value bond carrying a coupon rate of maturity after 10 years is Rs 900. What is the YTM on this bond?

(04

(Total 2

04. The securities **M** and **Y** have the following probability distribution of returns.

Economic condition	**Probability**	**Returns (%)**	
		M	**Y**
Growth	40%	30	-20
Normal	35%	20	10
Decline	25%	-10	40

Required:

a. Calculate the expected rate of returns of security **M** and security **Y**.

b. Measure the risk of investing in each of the securities and comment on the risk measured.

c. Calculate the covariance of returns and the correlation coefficient of returns between **M** and **Y** and explore the possibility of reducing the risk by creating a portfolio investing in both securities.

d. If a portfolio is created by investing 60% of wealth in security **M** and 40% in security **Y**. What will be the expected rate of return of the portfolio?

e. Measure the risk of the portfolio of its returns and comment on the risk of the portfolio.

f. Determine the optimal combination of M and Y to form minimum risk portfolio.

g. How does an investor to make their investment decision by using expected rate of return and standard deviation?

(Total 20 Marks)