

Chartered Banker

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Investment

Assignment 1

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Important Assignment Information

ASSIGNMENT LENGTH

For assignments submitted on or after **1st September 2008**, there is a **maximum** word count of **2,500 words**.

From that date, if you fail to adhere to the maximum word count, a deduction will be made to your final assignment mark. Specifically, if you exceed the 2,500 limit, you will be deducted **1%** for every **100 words** or **part of 100 words** over the limit.

For example, if you write a total of **2,614** words, a **2%** deduction will be made to your mark. For clarification, the word count includes all references and attached appendices.

PASS COMPENSATION AWARD

In recognition of the importance attached to the assignments, an award of **Pass Compensation** will be made to you if you score between 45% and 54% in the final exam and if you complete the required assignment(s) under the following conditions:

1. The assignment mark must be 60% or above – where two assignments are required, then the average mark must be 60% or above **and**
2. Assignments must be in the hands of the Tutor **at least** one month prior to the **chosen examination date for each subject**.

For example, if you enrol to sit a **full** credit subject examination on **15th December**, you must have sent **both** assignments to your tutor by **15th November**.

Similarly, if you enrol to sit a **half** credit subject examination on **2nd March**, you must have sent the **sole** assignment to the tutor by **2nd February**.

Please also note the following:

- (a) Where an assignment is marked at less than 60%, this may show up as **'Fail'** in the web-based student record – this is purely with reference to the Pass Compensation award and does not necessarily mean it is a sub-standard submission
- (b) You are **not** permitted to **re-submit** an assignment in order to gain a higher mark
- (c) In the event that you fail an exam and have not completed the required assignment(s), you can subsequently complete the required assignment(s) – these will then count towards any re-sit examination undertaken. Submission dates for these assignments must comply with the relevant timescales as stated in **2** above.

Question 1

Bruce Jarvis is retired and is a long-time and extremely wealthy client of your department – one which specialises in private client investment management.

Mr Jarvis is renowned for being difficult and whilst not unduly risk averse, is known for reacting both negatively and in an exaggerated fashion when conditions in stock markets have an adverse effect on his own personal wealth.

A higher rate taxpayer on private pension income alone, he is recently divorced. At a recent meeting you had with him, you felt that the realisation that his wife was no longer with him was making him arrive at decisions which, to say the least, were more unusual than you had been used to. Having looked after his affairs for over 15 years you thought that you had become accustomed to his own particular nuances, but a letter which arrived on your desk this morning has shattered that illusion.

In the letter, he states that he has become concerned over the extreme volatility recently being witnessed in world stock markets. In order to protect his financial well-being, he has decided to seek your opinion and expert views on a number of issues and questions regarding assets he has within his portfolio – these are as follows:

- (a) As you are aware, Mr Jarvis has only one cash deposit account with your bank. Following the events of Northern Rock with great interest, he questions you on how safe his deposit with your bank might be as he is fearful of it going bust! Presently, he has £88,000 in cash and enquires what might happen to this sum should the bank “go under”. He wants to know if he should spread his funds around other deposit-taking institutions to fully protect his cash.

How will you respond?

(5 marks)

- (b) Following his divorce and the resultant settlement to his wife, Mr Jarvis was left with a very substantial holding in the ordinary shares of a company trading on the London Stock Exchange called ZAPP plc.

Whilst recent trading has been very good, the shares have been caught up in the general market malaise and so at the current 795p per share he has reacted badly to their fall from a recent high of over £10 per share. As such, he has decided that despite his higher rate tax status, he will sell his entire holding of 9,000 shares which he has held since 1st March 1989 and which were purchased for 50p per share. He asks you to sell the shares on 1st March 2008 and to:

- (i) Compute his likely tax liability. (Assume brokerage of 1.25% is payable on a sale through the bank’s Stockbroking Service).

(8 marks)

- (ii) Advise him if there are any steps he could take to mitigate such a liability.

(3 marks)

(TOTAL 16 MARKS)

Question 2

James Brownlee comes to see you regarding an investment he has acquired following the death of an aunt.

He has recently been advised by the solicitor winding up the estate that he has become the owner of a holding of £26,000 of 8% Treasury Stock 2021. Presently, the stock is trading well above par value.

Given the value of the holding, James has considered selling the investment and re-investing the funds as equally as possible in two shorter-dated gilt edged stocks, namely 4¾% Treasury Stock 2010 and 4¼% Treasury Stock 2011.

Based on the undernoted additional information you are asked to respond to James with answers to the following:

- (a) Calculate the current value to James, a basic rate taxpayer, of the investment he has been bequeathed in terms of both capital and, after tax, income.

Assume the date for valuation is 1st April 2008.

(5 marks)

- (b) Calculate how much (to the nearest whole £) of the two new gilt holdings he will be able to purchase taking into account accrued interest and expenses. Assume that the sale and purchases have been carried out on 1st April 2008.

(10 marks)

- (c) What is the effect on his post- tax annual income position now that the two new holdings have been purchased?

(2 marks)

- (d) He admits that his father-in-law has advised him to take such a course of action but he has some concerns over the risks to his capital, albeit he received this as a windfall. How will you respond?

(3 marks)

(TOTAL 20 MARKS)

Additional Information

	Price	Interest Paid	Sale Commission	Purchase Commission
8% Treasury 2021	£134.55	7 June / 7 Dec	0.75%	0.95%
4¾ % Treasury 2010	£101.50	7 June / 7 Dec	0.75%	0.95%
4¼ % Treasury 2011	£99.85	7 March / 7 Sept	0.75%	0.95%

Question 3

The following information has been extracted from the accounts of Pikanmix plc.

ASSETS	£m	LIABILITIES	£m
Bank Deposits	£3.0	Short term loan	£5.5
Stock	£10.5	Long term loan	£10.25
Plant	£2.5	Creditors	£7.25
Premises	£8.75		
Debtors	£4.25		

Pikanmix has 20 million shares in issue at a current share price of 150p per share.

Recently the company reported an excellent and record year, with profits before tax of £6.25m and, for the first time in the company's history, it expects to pay a dividend to shareholders of 15p per share. The tax charge for the company is 10%. The average stockholders' equity is £16m.

Calculate the following **and** explain the relevancy of your answer.

- (a) What is the Price to Net Asset Value ratio of Pikanmix plc and what is the significance of this ratio?
(5 marks)
- (b) Calculate the P/ E ratio for Pikanmix and provide an explanation of what this means.
(5 marks)
- (c) If average stockholders' equity throughout the accounting period was £115m, what is the Return on Equity and what does this mean for the shareholder?
(4 marks)
- (d) Calculate the dividend cover and dividend yield for the company and explain what each means.
(4 marks)
- (e) Why are dividends considered an important part of the return available for a prospective equity investor?
(6 marks)

(TOTAL 24 MARKS)

TOTAL ASSIGNMENT MARKS – 60