CHUKA UNIVERSITY

UNIVERSITY EXAMINATIONS

EXAMINATION FOR THE AWARD OF DEGREE OF BACHELOR OF COMMERCE

BCOM 435: INVESTMENT & PORTFOLIO MANAGEMENT

STREAMS: BCOM (ODEL) **TIME: 2 HOURS**

DAY/DATE: WEDNESDAY 07/08/2024 **2.30 P.M. – 4.30 P.M.**

INSTRUCTIONS

- **Answer question one and any other two**

QUESTION ONE

a) Distinguish between systematic and non-systematic risk citing two sources of each. (4 marks)

b) Discuss the essential features investors consider while selecting investment alternatives. (10 marks)

c) Using suitable examples, distinguish between the following security types: Fixed income, Equities and derivatives. (6 marks)

d) The following is data on return-risk characteristics of two risky securities X and Y. The standard deviation on security X and Y is 30% and 26% respectively. The correlation of returns between X and Y is -0.5 while that between X and the market portfolio is +0.25. The standard deviation of the market portfolio is estimated to be 6%.

i. The covariance of returns on asset X and Y. (2 marks)

ii. Calculate the proportion of investment in each security that would yield lowest risk assuming that an investor combines security X and Y in a portfolio. (4 marks)

iii. Estimate the beta for security X and interpret your result (4 marks)

QUESTION TWO

a) Explain the following terms as used in portfolio management

i. Efficient portfolio (3 marks)

ii. Bond duration (3 marks)

iii. Portfolio revision (3 marks)

b) The following investment portfolios are evaluated by investor:

Portfolio	Expected rate of return, %	Standard deviation
A	12	15
B	10	8
C	10	9

Using Markowitz portfolio theory explain the choice for investor between portfolios A, B and C. (7 marks)

c) If the risk-free rate of return is 6% and the return on the market portfolio is 10%, what is the expected return on an asset having a Beta of 1.4, according to the CAPM? (4 marks)

QUESTION THREE

a) Describe the key assumptions underlying CAPM. (8 marks)

b) Explain why most investors prefer to hold a diversified portfolio of securities as opposed to placing all of their wealth in a single asset. (6 marks)

c) In terms of the Markowitz portfolio model, explain, how an investor identifies his / her optimal portfolio. What specific information does an investor need to identify optimal portfolio? (6 marks)

QUESTION FOUR

a) Distinguish between active and passive portfolio revision strategies (6 marks)

b) Explain the following fund types: Equity fund, Money market fund and balanced fund. (6 marks)

c) The dividend per share of Mavazi Limited as at 31 December 2000 was Sh.2.50. The company's financial analyst has predicted that dividends would grow at 20% for five years after which growth would fall to a constant rate of 7%. The analyst has also projected a required rate of return of 10% for the equity market. Mavazi's shares have a similar risk to the typical equity market.

Required: The intrinsic value of shares of Mavazi Ltd. As at 31 December 2000. (8 marks)

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