

UNIVERSITY OF COLOMBO
FACULTY OF ARTS
THIRD YEAR EXAMINATION IN ARTS (ECONOMICS) 2018
END OF THE SECOND SEMESTER
ECN: 3265 (FINANCIAL MARKETS)
TIME ALLOWED: TWO (02) HOURS
Answer **four (04)** questions only

1.
 - i. Discuss the importance of financial markets for the economy in terms of efficient allocation of scarce financial resources. (13 Marks)
 - ii. Critically evaluate the recent developments in the Bond Market of Sri Lanka and their impact on the Sri Lankan economy. (12 Marks)
2.
 - i. Critically examine the relationship between the interest rate and investment using suitable diagrams where necessary. (12 Marks)
 - ii. An investor wants to borrow Rs. 500,000 for a five year period for a commercial project at a 9% annual interest rate. The loan is repaid at the end of five years. Calculate the value the investor has to pay after five years. (13 Marks)
3.
 - i. Briefly explain the main features of Treasury Bills, Treasury Bonds and Sri Lanka Development Bonds issued by the Government of Sri Lanka in the last four years. (15 Marks)
 - ii. Critically examine the nature of the relationship between price of bonds and the rate of interest. Use an example of your own to explain the answer. (10 Marks)
4.
 - i. Suppose an investor decided to borrow a loan worth of Rs. 5,000,000 from the bank to purchase a house at 15% interest a year. Expected inflation rate is 7%. End of the year actual inflation rate was 12%. Critically examine the current situation of the borrower and lender. (10 Marks)

ii. "Higher interest rates would result in exchange rate appreciation through foreign financial investments". Do you agree with this statement? Explain your answer.

(07 Marks)

iii. "The operations of the equity market are highly sensitive to the political stability of the country". Do you agree with this statement? Explain your answer drawing examples from Sri Lanka.

(08 Marks)

5.

i. How do you explain bull market and bear market concepts? (08 Marks)

ii. Assume that you have bought a discount bond for Rs. 850 with one year maturity. The face value of the bond is Rs. 1,000. Calculate the rate of return of the bond. (08 Marks)

iii. Calculate the amount an investor can earn from five year discount bond worth Rs. 100,000 if the interest rate is 13%. (09 Marks)

6.

i. Discuss the economic effects of the Current Bond Crisis in Sri Lankan Economy.

(12 Marks)

ii. "The excessive volatility in the forex market makes a negative impact on the stability in the financial system and the performance of the economy". Do you agree with this statement? Explain your answer. (13 Marks)

7. Write short notes on any **five (05)** of the following.

i. The functions and importance of Money Markets to the economy.

ii. Real interest rate.

iii. Primary market for bonds.

iv. Yield to maturity.

v. The functions and importance of Equity Market to the economy.

vi. Determinants of assets demand.

vii. Present value.

viii. Yield curve.

ix. Causes of Financial Crises.

(05 Marks Each)