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PAST YEARS/RTP/MTP

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QUESTION NO.7 Explain complexities involved in International Capital Budgeting. ***(Chapter 6)***

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QUESTION NO.1 Explain the problems that are faced in International Capital Budgeting Decision and how these can be overcome.***(Chapter 6)***

QUESTION NO.2 "Sustainable growth is important to enterprise long-term development". Explain this statement in context of planning healthy corporate growth.***(Chapter 1)***

QUESTION NO.3 Explain various Asset Allocation Strategies.***(Chapter 10)***

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QUESTION NO.5 Explain various Market Indicators.***(Chapter 2)***

QUESTION NO.6 Explain the term Angel Investor.***(Chapter 4)***

QUESTION NO.7 Examine briefly the various innovative methods of funding the Startups.***(Chapter 4)***

Important Note:How to present answer of difference between any two measures?
Ans:There are two ways to represent answer of difference:(1)Tabular (2) Descriptive. For example:
Exam Question: DISTINGUISH Primary participants and secondary participants in securitization.[Chapter 3]
Exam Question:Explain the difference between Forward and Future Contract.[Chapter 6]
So student should present their answer as given in this book.

1.FINANCIAL POLICY AND CORPORATE STRATEGY

QUESTION NO.1 Explain the Functions of Strategic Financial Management ? or The investment and financial decisions functions involve the many functions.Explain ?

➡The **investment and financial decisions** functions involve the following functions: **(a)** Continual search for **best investment opportunities**; **(b)** Selection of the **best profitable opportunities**; **(c)** Determination of **optimal mix of funds** for the opportunities; **(d)** Establishment of **systems for internal controls**; and **(e)** Analysis of results for **future decision-making**.

QUESTION NO.2 What are key decisions falling within the scope of financial strategy ?

1.Financing decisions: These decisions deal with the mode of financing or **mix of equity capital and debt capital.**

2. Investment decisions: These decisions involve the **profitable utilization of firm's funds** especially in long-term projects (capital projects). The projects are evaluated in relation to their expected return and risk.

3.Dividend decisions: These decisions determine the division of earnings between **payments to shareholders** and reinvestment in the company.

4.Portfolio decisions: A portfolio decision refers to a **collection of investment tools** such as stocks, shares, mutual funds, bonds, cash and so on depending on the investor's income, budget and convenient time frame.

QUESTION NO.3 Explain the different levels of enterprise strategy ? OR Enumerate 'Strategy' at different levels of hierarchy.

➡**(a) Corporate Level Strategy:**Corporate level strategy fundamentally is concerned with **selection of businesses** in which a company should compete.Corporate level strategy should be able to **answer three basic questions**:

Suitability :**Whether the strategy would work** for the accomplishment of common objective of the company.

Feasibility:Determines the **kind and number of resources required** to formulate and implement the strategy.

Acceptability:It is concerned with the **stakeholder's satisfaction**.

➡**(b)Business Unit Level Strategy**: At the business unit level, the strategic **issues are about both practical coordination of operating units** and about developing and sustaining a **competitive advantage** for the products and services that are produced.

➡**(c)Functional Level Strategy**:The functional level **is the level of the operating divisions and departments**. The strategic issues at this level are related to functional business processes and value chain. Functional level strategies in R&D, operations, manufacturing, marketing, finance, and human resources involve the development and coordination of resources through which business unit level strategies can be executed effectively and efficiently. Functional units of an organization are involved in higher level strategies by providing input to the business unit level and corporate level strategy, such as providing information on customer feedback or on resources and capabilities on which the higher level strategies can be based. Once the higher-level strategy is developed, the functional units translate them into discrete action plans that each department or division must accomplish for the strategy to succeed.

➡Among the different functional activities viz production, marketing, finance, human resources and research and development, **finance assumes highest importance** during the top down and bottom up interaction of planning. Corporate strategy deals with deployment of resources and financial strategy is mainly concerned with mobilization and effective utilization of money, the most critical resource that a business firm likes to have under its command.

QUESTION NO.4 There are 3 major components of Financial planning.What are they ?

➡There are **3 major components of Financial planning**:

(i) Financial Resources (FR) **(ii)**Financial Tools (FT) **(iii)**Financial Goals (FG) **Financial Planning: FR + FT = FG**

QUESTION NO.5 Explain briefly, how financial policy is linked to strategic management ?

➡The success of any business is measured in financial terms. Maximising value to the shareholders is the ultimate objective.For this to happen, at every stage of its operations including policy-making, the **firm should be taking strategic steps with value-maximization objective**.This is the basis of financial policy being linked to strategic management.

➡The linkage can be clearly seen in respect of many business decisions. For example :

(i) Manner of raising capital as source of finance and capital structure are the most important dimensions of strategic plan.**(ii) Cut-off rate** (opportunity cost of capital) for acceptance of investment decisions.**(iii) Investment and fund allocation** is another important dimension of interface of strategic management and financial policy. **(iv) Foreign Exchange exposure and risk management. (v) Liquidity management (vi)** A **dividend policy decision** deals with the extent of earnings to be distributed and a close interface is needed to frame the policy so that the policy should be beneficial for all**(vii)Issue of bonus share** is another dimension involving the strategic decision.

➡Thus from above discussions it can be said that **financial policy of a company cannot be worked out in isolation to other functional policies**. It has a wider appeal and closer link with the overall organizational performance and direction of growth.

QUESTION NO.6 Write a short note on Balancing Financial Goals vis-à-vis Sustainable Growth ? *(May 2014)*

➡The concept of sustainable growth **can be helpful for planning** healthy corporate growth.

➡This concept forces managers to consider the financial consequences of **sales increases and to set sales growth goals** that are consistent with the operating and financial policies of the firm.

➡Often, a conflict can arise if growth objectives are not consistent with the value of the organization's sustainable growth. Question concerning **right distribution of resources** may take a difficult shape if we take into consideration the rightness not for the current stakeholders but for the future stakeholders also.

➡**To take an illustration**, let us refer to fuel industry where resources are limited in quantity and a judicial use of resources is needed to cater to the need of the future customers along with the need of the present customers. One may have noticed the save fuel campaign, a demarketing campaign that deviates from the usual approach of sales growth strategy and preaches for conservation of fuel for their use across generation. This is an example of stable growth strategy adopted by the oil industry as a whole under resource constraints and the long run objective of survival over years.

➡**Incremental growth strategy, profit strategy and pause strategy** are other variants of stable growth strategy.

➡Sustainable growth **is important to enterprise long-term development.** Too fast or too slow growth will go against enterprise growth and development, so it should play important role in enterprise development, adopt suitable financial policy initiative to make sure enterprise growth speed close to sustainable growth ratio and have sustainable healthy development.

➡The sustainable growth rate (SGR), concept by Robert C. Higgins, of a firm is the **maximum rate of growth in sales** that can be achieved, given the firm's profitability, asset utilization, and desired dividend payout and debt (financial leverage) ratios. The sustainable growth rate is a measure of how much a firm can grow without borrowing more money. After the firm has passed this rate, it must borrow funds from another source to facilitate growth. Variables typically include the net profit margin on new and existing revenues; the asset turnover ratio, which is the ratio of sales revenues to total assets; the assets to beginning of period equity ratio; and the retention rate, which is defined as the fraction of earnings retained in the business.

SGR = ROE x (1- Dividend payment ratio)

➡**Sustainable growth models assume that the business wants to:**

1) maintain a **target capital structure** without issuing new equity;

2) maintain a **target dividend payment ratio**; and

3) increase sales as rapidly as market conditions allow.

➡Since the asset to beginning of period equity ratio is constant and the firm's only source of new equity is

retained earnings, sales and assets cannot grow any faster than the retained earnings plus the additional debt that the retained earnings can support. The sustainable growth rate is consistent with the observed evidence that most corporations are reluctant to issue new equity. If, however, the firm is willing to issue additional equity, **there is in principle no financial constraint on its growth rate.**

QUESTION NO.7 What makes an organization sustainable ? State the specific steps?

➡The concept of sustainable growth **can be helpful for planning healthy corporate growth**. This concept forces managers to consider the financial consequences of sales increases and to set sales growth goals that are consistent with the operating and financial policies of the firm. Often, a conflict can arise if growth objectives are not consistent with the value of the organization's sustainable growth. Question concerning right distribution of resources may take a difficult shape if we take into consideration the rightness not for the current stakeholders but for the future stakeholders also.

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➡**To be financially sustainable, an organisation must:**

(i) have **more than one source of income;**
(ii) have **more than one way of generating income;**
(iii) do strategic, action and **financial planning regularly;**
(iv) have **adequate financial systems;**
(v) have a **good public image;**
(vi) be clear about its **values (value clarity)**; and
(vii) have **financial autonomy** (Independence).

➡**What makes an organisation sustainable?** In order to be sustainable, an organisation must:

(i) Have a clear strategic direction;
(ii) Be able to scan its environment or context to identify opportunities for its work;
(iii) Be able to attract, manage and retain competent staff;
(iv) Have an adequate administrative and financial infrastructure;
(v) Be able to demonstrate its effectiveness and impact in order to leverage further resources; and
(vi) Get community support for, and involvement in its work.

QUESTION NO.8 "Sustainable growth is important to enterprise long-term development". Explain this statement in context of planning healthy corporate growth.

➡Sustainable growth is important to enterprise long-term development. Too fast or too slow growth will go against enterprise growth and development, so financial should play important role in enterprise development, adopt suitable financial policy initiative to make sure enterprise growth speed close to sustainable growth ratio and have sustainable healthy development.

The sustainable growth rate (SGR) of a firm is the maximum rate of growth in sales that can be achieved, given

the firm's profitability, asset utilization, and desired dividend payout and debt (financial leverage) ratios. The sustainable growth rate is a measure of how much a firm can grow without borrowing more money. After the firm has passed this rate, it must borrow funds from another source to facilitate growth. Variables typically include the net profit margin on new and existing revenues; the asset turnover ratio, which is the ratio of sales revenues to total assets; the assets to beginning of period equity ratio; and the retention rate, which is defined as the fraction of earnings retained in the business.

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➡**Sustainable growth models assume that the business wants to:**

(1)maintain a target capital structure without issuing new equity;

(2)maintain a target dividend payment ratio; and

(3)increase sales as rapidly as market conditions allow.

QUESTION NO.9 Explain the Interface of Financial Policy and Strategic Management ?

➡The interface of strategic management and financial policy will be clearly understood if we appreciate the fact that the **starting point of an organization is money and the end point of that organization is also money**. No organization can run an existing business and promote a new expansion project without a suitable internally mobilized financial base or both internally and externally mobilized financial base.

➡**Sources of finance and capital structure are the most important dimensions of a strategic plan**. The generation of funds may arise out of ownership capital and or borrowed capital. A company may issue equity shares and / or preference shares for mobilizing ownership capital.

➡Along with the mobilization of funds, **policy makers should decide on the capital structure** to indicate the desired mix of equity capital and debt capital. There are some norms for debt equity ratio. However this ratio in its ideal form varies from industry to industry. It also depends on the planning mode of the organization under study.

➡**Another important dimension** of strategic management and financial policy interface is the **investment and fund allocation decisions.** A planner has to frame policies for regulating investments in fixed assets and for restraining of current assets. Investment proposals mooted by different business units may be addition of a new product, increasing the level of operation of an existing product and cost reduction and efficient utilization of resources through a new approach and or closer monitoring of the different critical activities.

➡Now, given these three types of proposals a planner should evaluate each one of them by making within group comparison in the light of **capital budgeting exercise.**

➡**Dividend policy** is yet another area for making financial policy decisions affecting the strategic performance of the company. A close interface is needed to frame the policy to be beneficial for all. Dividend policy decision deals with the extent of earnings to be distributed as dividend and the extent of earnings to be retained for future expansion scheme of the firm.

➡It may be noted from the above discussions that financial policy of a company **cannot be worked out in isolation of other functional policies.** It has a wider appeal and closer link with the overall organizational performance and direction of growth. These policies being related to external awareness about the firm, specially the awareness of the investors about the firm, in respect of its internal performance. There is always a process of evaluation active in the minds of the current and future stake holders of the company. As a result preference and patronage for the company depends significantly on the financial policy framework. And hence attention of the corporate planners must be drawn while framing the financial policies not at a later stage but during the stage of corporate planning itself.

2.SECURITY ANALYSIS

QUESTION NO. 1 What is Fundamental Analysis ?

➡**Fundamental Analysis** is based on the premise that **"All securities can be valued by calculating the present**

value of their future cash flows".

QUESTION NO.2 What is the Key Variables Of Fundamental Analysis ?

The key variables that an investor must monitor in order to carrying out his fundamental analysis are :

1. Economy Analysis **2.** Industry Analysis **3.** Firm/Company Analysis

1. Economy Analysis:

Factors Affecting Economic Analysis: Some of the economy wide factors are discussed as under:

(a) Growth Rates of National Income and Related Measures: The estimated growth rate of the economy is important for the industrial sector, and and also for the returns, investors can expect from investment in shares.

(b) Growth Rates of Industrial Sector: This can be further broken down into growth rates of various industries or groups of industries if required. The growth rates in various industries are estimated based on the estimated demand for its products.

(c) Inflation: Inflation is measured in terms of either wholesale prices (the Wholesale Price Index or WPI) or retail prices (Consumer Price Index or CPI). The demand in some industries,particularly the consumer products industries, is significantly influenced by the inflation rate.Therefore, firms in these industries make continuous assessment about inflation rates likely to prevail in the near future so as to fine-tune their pricing, distribution and promotion policies to the anticipated impact of inflation on demand for their products.

(d) Monsoon: Because of the strong forward and backward linkages*, monsoon is of great concern to investors in the stock market too.

Some of the techniques used for economic analysis are:

(a) Anticipatory Surveys: They help investors to form an opinion about the future state of the economy.It incorporates **expert opinion** on construction activities, expenditure on plant and machinery, levels of inventory all having a definite bearing on economic activities. Also future spending habits of consumers are taken into account.

(b) Barometer/Indicator* Approach: Various indicators are used to find out how the economy shall perform in the future. The indicators have been classified as under:

(i) Leading Indicators: They **lead** the economic activity in terms of their outcome. They relate to the **time series data*** of the variables that **reach high/low points in advance** of economic activity.

(ii) Roughly Coincidental Indicators: They reach their **peaks(high) and troughs(low) at approximately the same time** in the economy.

(iii) Lagging Indicators: They are **time series data** of variables that **lag** behind in their consequences vis-a- vis the economy. They reach their turning points **after the economy** has reached its own already.

(c) Economic Model Building Approach: In this approach, a precise and clear relationship between dependent and independent variables is determined. The steps used are as follows:**(i)**Estimate Total Income by**(ii)**Estimating levels of various components of Total Income **(iii)** and calculate Forecasted GNP **(iv)**Comparison:Comparison is then made of total GNP thus arrived with that from an independent agency and then the overall forecast is tested for consistency.

2. Industry Analysis:

Factors Affecting Industry Analysis:

(a) Product Life-Cycle : An industry usually exhibits high profitability in the initial and growth stages, medium but steady profitability in the maturity stage and a sharp decline in profitability in the last stage of growth.

(b) Demand Supply Gap: Excess supply reduces the profitability of the industry because of the decline in the unit price realization, while insufficient supply tends to improve the profitability because of higher unit price realization.

(c) Barriers to Entry : Some of these barriers are related to the product and the technology of production, while other barriers are created by existing firms in the industry.

(d) Government Attitude : The attitude of the government towards an industry is a crucial determinant of its prospects.

(e)State of Competition in the Industry: Factors to be noted are- firms with leadership capability and the nature

of competition.

(f)Cost Conditions and Profitability: Profitability depends on the state of competition in the industry, cost control measures adopted by its units and growth in demand for its products.

(g)Technology and Research: They play a vital role in the growth and survival of a particular industry.

Some of the techniques used for Industry Analysis are:

(a) Regression Analysis **(b)** Input–Output Analysis

3. Firm/Company Analysis:

Factors Affecting Company Analysis:

(a)Net Worth and Book Value : Net Worth is sum of equity share capital,and free reserves less intangible assets and any carry forward of losses. The total net worth divided by the number of shares is known as book value of a share.

(b) Sources and Uses of Funds: The identification of sources and uses of funds is known as Funds Flow Analysis.One of the major uses of funds flow analysis is to find out whether the firm has used short term sources of funds to finance long-term investments.

(c) Cross-Sectional and Time Series Analysis: One of the main purposes of examining financial statements is to compare two firms, compare a firm against some benchmark figures for its industry and to analyse the performance of a firm over time. The techniques that are used to do such proper comparative analysis are: common-sized statement, and financial ratio analysis.

(d) Size and Ranking:A rough idea regarding the size and ranking of the company within the economy, in general,and the industry, in particular, would help the investment manager in assessing the risk associated with the company.

(e) Growth Record: The following three growth indicators may be particularly looked into:

(a) Price earnings ratio,**(b)**Percentage growth rate of earnings per annum,**(c)** Percentage growth rate of net block.

(f) Financial Analysis: From the investment point of view, the most important figures are earnings per share, price earning ratios, yield, book value and the intrinsic value of the share.

(g) Quality of Management: This is an intangible factor. Yet it has a very important bearing on the value of the shares. Every investment manager knows that the shares of certain business houses command a higher premium than those of similar companies managed by other business houses. This is because of the quality of management.

(h) Location and Labour-Management Relations: The locations of the company's manufacturing facilities determines its economic viability which depends on the availability of crucial inputs like power, skilled labour and raw-materials, etc.

(i) Pattern of Existing Stock Holding: An analysis of the pattern of existing stock holdings of the company would also be relevant. This would show the stake of various parties in the company.

(j) Marketability of the Shares: Another important consideration for an investment manager is the marketability of the shares of the company.

Some of the techniques used for company analysis are:

(a) Correlation & Regression Analysis **(b)** Trend Analysis: **(c)** Decision Tree Analysis

QUESTION NO.3 What is Technical Analysis,Its Assumption & its Principles ?

➡**Meaning:**It is a method of **share price movements based on a study of price graphs or charts .**

➡**Assumptions:** Technical Analysis is based on the following assumptions:

(i) The market value of stock is actually depending on the **supply and demand** for a stock.

(ii) The supply and demand is actually **governed by several factors**. For instance, recent initiatives taken by the Government to reduce the Non-Performing Assets (NPA) burden of banks may actually increase the demand for banking stocks.

(iii) Stock **prices generally move in trends** which continue for a substantial period of time. Therefore, if there is a bull market going on, there is every possibility that there will soon be a substantial correction which will provide an opportunity to the investors to buy shares at that time.

(iv) Technical analysis **relies upon chart analysis** which shows the past trends in stock prices rather than the

information in the financial statements like balance sheet or profit and loss account.

➡**Principles of Technical Analysis:**Technical analysis is based on the following **three principals**:

(a)The Market Discounts Everything: Technical analysts generally have the view that a company's share price includes everything including the fundamentals of a company.

(b) Price Moves in Trends: Technical analysts believe that prices move in trends. In other words, a stock price is more likely to continue a past trend than move in a different direction.

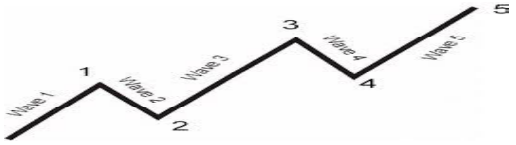
(c)History Tends to Repeat Itself: Technical analysts believe that history tends to repeat itself.

QUESTION NO.4 Explain the Elliot Wave Theory of technical analysis?

➡**Inspired by the Dow Theory** and by observations found throughout nature, Ralph Elliot formulated Elliot Wave Theory in 1934.➡This theory was based on analysis of **75 years stock price movements** and charts. ➡From his studies, he **defined price movements in terms of waves**.As per this theory wave is a movement of the market price from one change in the direction to the next change in the same direction.These waves are resulted from buying and selling impulses emerging from the demand and supply pressures on the market.Depending on the demand and supply pressures, waves are generated in the prices.➡Accordingly, this theory was **named Elliot Wave Theory**. ➡As per this theory, waves can be classified into **two parts**:-

(i) Impulsive patterns**(ii)** Corrective patterns.➡Let us discuss each of these patterns.

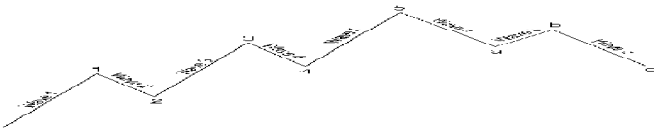
(a) Impulsive Patterns-(Basic Waves) - ➡In this pattern there will be 3 or 5 waves in a given direction (**going upward or downward**). ➡These waves shall **move in the direction of the basic movement**. ➡This movement can **indicate bull phase or bear phase**.



(b) Corrective Patterns- (Reaction Waves) - ➡These waves are **against the basic direction** of the basic movement. ➡Correction involves **fall in case of bull market and rise in case of bear market**.

As shown in the following diagram waves **1, 3 and 5** are basic movements, which are separated or corrected by wave **2 & 4,** termed as corrective movements.

➡**Complete Cycle:**One complete cycle consists of waves made up of two distinct phases, bullish and bearish.



QUESTION NO.5 What is the Dow Jones Theory ?

➡The Dow Theory is one of the **oldest and most famous** technical theories.➡It was **originated by Charles Dow**, the founder of Dow Jones Company in late nineteenth century.➡It is a helpful tool for **determining the relative strength** of the stock market. ➡It can also be used as a **barometer of business**.➡The Dow Theory is based upon the movements of two indices, constructed by Charles Dow, **Dow Jones Industrial Average (DJIA) and Dow Jones Transportation Average (DJTA)**.➡These averages reflect the aggregate impact of **all kinds of information** on the market.➡The movements of the market are **divided into three classifications**, all going at the same time; the primary movement, the secondary movement, and the daily fluctuations.

➡**The primary movement** is the main trend of the market, which lasts from one year to 36 months or longer. This trend is commonly called bear or bull market. ➡**The secondary movement** of the market is shorter in duration than the primary movement, and is opposite in direction. It lasts from two weeks to a month or more. ➡**The daily fluctuations** are day-to-day movements. These fluctuations are not part of the Dow Theory interpretation of the stock market. ➡However, daily movements must be carefully studied, along with primary and secondary movements, as they go to **make up the longer movement** in the market.

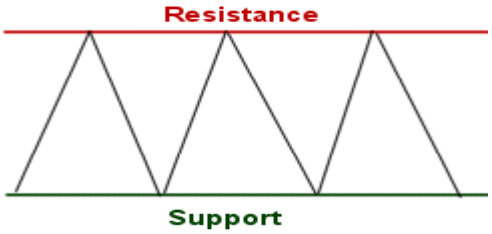
➡Thus, the **Dow Theory's purpose** is to determine where the market is and where is it going.The theory, in

practice, states that **if successively high and the successive lows are higher**, then the market trend is up and a bullish market exists. Contrarily, **if the successive highs and successive lows are lower,** then the direction of the market is down and a bearish market exists.

➦Charles Dow proposed that the **primary uptrend would have three moves up**, the **first one** being caused by accumulation of shares by the far-sighted, knowledgeable investors, the **second move** would be caused by the arrival of the first reports of good earnings by corporations, and the **last move** up would be caused by widespread report of financial well-being of corporations. The third stage would also see rampant speculation in the market. Towards the end of the third stage, the far-sighted investors, realizing that the high earnings levels may not be sustained, would start selling, starting the **first move down of a downtrend**, and as the non-sustainability of high earnings is confirmed, the **second move down** would be initiated and then the **third move down** would result from distress selling in the market.

QUESTION NO.6 Explain Support and resistance level with diagram?

➦When the index/price **goes down from a peak**, the peak becomes the **resistance level.** ➦When the index/price **rebounds after reaching a trough(bottom)** subsequently, the lowest value reached becomes the **support level.** ➦The price is then expected to move between **these two levels.** ➦Whenever the price approaches the resistance level, there is a **selling pressur**e while ➦whenever the price approaches the support level, there is a **buying pressure.**



QUESTION NO.7 What do you mean by GAP ?

➦**A gap up** occurs when the next day opening price is higher than the price of the previous day.

➦**A gap-down** occurs when the opening price of the stock is lower than the previous day's price.

QUESTION NO.8 Differentiate between Fundamental Analysis and Technical Analysis ?

Basis	Fundamental Analysis	Technical Analysis
1.Method	Prospects are measured by analyzing economy's macro factors such as Country's GDP, Inflation Rate, Interest Rate, Growth Rate etc. and company's micro factors like its Sales, Profitability, Solvency, Asset & Liabilities and Cash position etc.	Predicts future prices and their direction using purely historical market data and information such as their Price Movements, Volume, Open Interest etc.
2.Rule	Prices of a share discounts everything	Price captures everything
3.Usefulness	For Long-Term Investing	For Short-term Investing

QUESTION NO.9 Explain the Random Walk Theory ?

➦This theory states that the **behaviour of stock market prices is unpredictable** and that there is no relationship between the present prices of the shares and their future prices. ➦Proponents of this theory argue that **stock market prices are independent**. ➦A British statistician, M. G. Kendell, found that changes in security prices behave nearly as if they are generated by a suitably **designed roulette wheel*** for which each outcome is statistically independent of the past history. ➦In the layman's language it may be said that prices on the stock exchange behave exactly the way a **drunk would behave** while walking in a blind lane, i.e., up and down,

with an unsteady way going in any direction he likes, bending on the side once and on the other side the second time.➦The supporters of this theory put out a simple **argument**. It follows that:
(i) Prices of shares in stock market **can never be predicted**. **(ii)**The reason is that the price trends are not the result of any underlying factors, but that **they represent a statistical expression of past data**.**(iii)**There may be periodical ups or downs in share prices, but **no connection can be established** between two successive peaks (high price of stocks) and troughs (low price of stocks).

QUESTION NO.10 Write a short note on Evaluation Of Technical Analysis?
➦Technical Analysis has several supporters as well several critics. The **advocates of technical analysis** offer the following interrelated argument in their favour:
(a) Under influence of **crowd psychology*,** trend persist for some time. Tools of technical analysis help in identifying these trends early and help in investment decision making.**(b)** Shift in demand and supply are gradual rather then instantaneous. Technical analysis **helps in detecting this shift rather** early and hence provides clues to future price movements.**(c)** Fundamental information about a company is observed and absorb by the market over a period of time. Hence **price movement tends to continue more or less in same direction** till the information is fully assimilated in the stock price.
➦**Detractors of technical analysis** believe that it is an useless exercise; their arguments are as follows:
(a) Most technical analysts are **not able to offer a convincing explanation** for the tools employed by them.**(b)** Empirical evidence in **support of random walk hypothesis** cast its shadow over the usefulness of technical analysis.**(c)** By the time an up trend and down trend may have been signalled by technical analysis **it may already have taken place.(d)** Ultimately technical analysis must be **self defeating proposition**. With more and more people employing it, the value of such analysis tends to decline.

QUESTION NO.11 Explain the different levels or forms of Efficient Market Theory?
(i)Weak form efficiency - Price reflect all information found in the record of **past prices and volumes.**
(ii)Semi - Strong efficiency - Price reflect not only all information found in the record of past prices and volumes but also all other **publicly available information**.
(iii)Strong form efficiency - Price reflect all available information **public as well as private**.

QUESTION NO.12 Explain the Misconception about Efficient Market Hypothesis (EMH) Theory ?
➦Efficient Market Theory implies that **market prices factor in all available information** and as such it is not possible for any investor to earn consistent long term returns from market operations.
➦Although price tends to fluctuate **they cannot reflect fair value**. This is because the future is uncertain. The market springs surprises continually and as prices reflect the surprises they fluctuate.
➦Inability of institutional portfolio managers to achieve superior investment performance implies that they **lack competence in an efficient market.** It is not possible to achieve superior investment performance since market efficiency exists due to portfolio mangers doing this job well in a competitive setting.
➦The random movement of stock prices suggests that **stock market is irrational.** Randomness and irrationality are two different things, if investors are rational and competitive, price changes are bound to be random.

QUESTION NO.13 Explain the different challenges to Efficient Market Theory ?
(a) Limited information processing capabilities – Human information processing capabilities are sharply limited.
(b) Irrational Behaviour – Most of the times investors behaviour shows irrationality between market prices and intrinsic values.
(c) Monopolistic Influence – A market is regarded as highly competitive. No single buyer or seller is supposed to have undue influence over prices.In practice, powerful institutions and big operators have great influence over the market. The monopolistic power enjoyed by them diminishes the competitiveness of the market.

QUESTION NO.14 Explain various "Market Indicators".

The various market indicators are as follows:

(i)Breadth Index: It is an index that covers all securities traded. It is computed by dividing the net advances or declines in the market by the number of issues traded. The breadth index either supports or contradicts the movement of the Dow Jones Averages. If it supports the movement of the Dow Jones Averages,
this is considered sign of technical strength and if it does not support the averages, it is a sign of technical weakness i.e. a sign that the market will move in a direction opposite to the Dow Jones Averages. The breadth index is an addition to the Dow Theory and the movement of the Dow Jones Averages.

(ii)Volume of Transactions: The volume of shares traded in the market provides useful clues on how the market would behave in the near future. A rising index/price with increasing volume would signal buy behaviour because the situation reflects an unsatisfied demand in the market. Similarly, a falling market with increasing volume signals a bear market and the prices would be expected to fall further. A rising market with decreasing volume indicates a bull market while a falling market with dwindling volume indicates a bear market. Thus, the volume concept is best used with another market indicator, such as the Dow Theory.

(iii)Confidence Index: It is supposed to reveal how willing the investors are to take a chance in the market. It is the ratio of high-grade bond yields to low- grade bond yields. It is used by market analysts as a method of trading or timing the purchase and sale of stock, and also, as a forecasting device to determine the turning points of the market. A rising confidence index is expected to precede a rising stock market, and a fall in the index is expected to precede a drop in stock prices. A fall in the confidence index represents the fact that low-grade bond yields are rising faster or falling more slowly than high grade yields. The confidence index is usually, but not always a leading indicator of the market. Therefore, it should be used in conjunction with other market indicators.

(iv)Relative Strength Analysis: The relative strength concept suggests that the prices of some securities rise relatively faster in a bull market or decline more slowly in a bear market than other securities i.e. some securities exhibit relative strength. Investors will earn higher returns by investing in securities which have demonstrated relative strength in the past because the rela tive strength of a security tends to remain undiminished over time. Relative strength can be measured in several ways. Calculating rates of return and classifying those securities with historically high average returns as securities with high relative strength is one of them. Even ratios like security relative to its industry and security relative to the entire market can also be used to detect relative strength in a security or an industry.

(v)Odd - Lot Theory: This theory is a contrary - pinion theory. It assumes that the average person is usually wrong and that a wise course of action is to pursue strategies contrary to popular opinion. The odd-lot theory is used primarily to predict tops in bull markets, but also to predict reversals in individual securities.

3.SECURITIZATION

QUESTION NO.1 What are the Features of Securitization ?

(i)Creation of Financial Instruments - The process of Securitization can be viewed as process of creation of additional financial product of securities in market backed by collaterals.

(ii)Bundling and Unbundling - When all the assets are combined in one pool it is bundling and when these are broken into instruments of fixed denomination it is unbundling.

(iii)Tool of Risk Management - In case of assets are securitized on non-recourse* basis, then securitization process acts as risk management as the risk of default is shifted.

(iv)Structured Finance - In the process of securitization, financial instruments are tailor structured to meet the risk return trade profile of investor, and hence, these securitized instruments are considered as best examples of structured finance.

(v)Trenching* - Portfolio of different receivable or loan or asset are split into several parts based on risk and return they carry called 'Trenche'. Each Trench carries a different level of risk and return.

(vi)Homogeneity* - Under each trenche the securities are issued of homogenous nature and even meant for

small investors who can afford to invest in small amounts.

QUESTION NO.2 What are the BENEFITS OF SECURITIZATION ?

➥From the angle of originator

(i)Off - Balance Sheet Financing: When loan/receivables are securitized it release a portion of capital tied up in these assets resulting in off Balance Sheet financing leading to improved liquidity position which helps expanding the business of the company.

(ii)More specialization in main business: By transferring the assets, the entity could concentrate more on core business as servicing of loan is transferred to SPV(Special Purpose Vehicle). Further, in case of non-recourse* arrangement even the burden of default is shifted.

(iii)Helps to improve financial ratios: Especially in case of Financial Institutions and Banks, it helps to manage Capital -To-Weighted Asset Ratio effectively.

(iv)Reduced borrowing Cost: Securitized papers are rated and due to credit enhancement these securities can be issued at reduced rate of debts and hence the originator earns a spread*, resulting in reduced cost of borrowings.

➥From the angle of investor

1.Diversification of Risk: Purchase of securities backed by different types of assets provides the diversification of portfolio resulting in reduction of risk.

2.Regulatory requirement: Acquisition of asset backed belonging to a particular industry say micro industry helps banks(which can also act as an Investor) to meet regulatory requirement of investment of fund in industry specific.

3.Protection against default: In case of recourse* arrangement if there is any default by any third party then originator will be responsible and there can be insurance arrangement for compensation for any such default.

QUESTION NO.3 Who are the PARTICIPANTS IN SECURITIZATION ? OR DISTINGUISH between:Primary participants and secondary participants in securitization ?

Broadly, the participants in the process of securitization can be divided into two categories; one is Primary Participant and the other is Secondary Participant.

➥Primary Participants: Primary Participants are main parties to this process. The primary participants in the process of securitization are as follows:

(a) Originator: It is the initiator of deal or can be termed as securitizer. It is an entity which sells the assets lying in its books and receives the funds generated through the sale of such assets. The originator transfers both legal as well as beneficial interest to the Special Purpose Vehicle .

(b)Special Purpose Vehicle: Also, called SPV is created for the purpose of executing the deal. Since issuer originator transfers all rights in assets to SPV, it holds the legal title of these assets. It is created especially for the purpose of securitization only and normally could be in form of a company, a firm, a society or a trust.The main objective of creating SPV is to remove the asset from the Balance Sheet of Originator. Further, it also issues the securities to the investors.

(c) The Investors: Investors are the buyers of securitized papers which may be an individual, an institutional investor such as mutual funds, provident funds, insurance companies, mutual funds, Financial Institutions etc.

➥Secondary Participants: Besides the primary participants, other parties involved into the securitization process are as follows:

(a)Obligors: Actually they are the main source of the whole securitization process. They are the parties who owe money to the firm and are assets in the Balance Sheet of Originator.

(b) Rating Agency: Rating agency assesses the following:**(i)**Strength of the Cash Flow.**(ii)** Mechanism to ensure timely payment of interest and principle repayment.**(iii)** Credit quality of securities.**(iv)** Liquidity support.**(v)** Strength of legal framework.

(c)Receiving and Paying agent (RPA): Also, called Servicer or Administrator, it collects the payment due from obligor and passes it to SPV. It also follow up with defaulting borrower and if required initiate appropriate legal

action against them. Generally, an originator or its affiliates acts as servicer.

(d)Agent or Trustee: Trustees are appointed to oversee that all parties to the deal perform in the true spirit of terms of agreement. Normally, it takes care of interest of investors who acquires the securities.

(e)Credit Enhancer*: Since investors in securitized instruments are directly exposed to performance of the loan,they seek additional comfort in the form of credit enhancement. Originator itself or a third party say a bank may provide this additional context called Credit Enhancer.

(f)Structurer: It brings together the originator, investors, credit enhancers and other parties to the deal of securitization. It ensures that deal meets all legal, regulatory, accounting and tax laws requirements.

QUESTION NO.4 What are the steps /MECHANISM OF SECURITIZATION ?

1. Creation of Pool of Assets: The process of securitization begins with creation of pool of assets by segregation of assets backed by similar type of mortgages in terms of interest rate, risk, maturity and concentration units.

2. Transfer to SPV: One assets have been pooled, they are transferred to Special Purpose Vehicle (SPV) especially created for this purpose.

3. Sale of Securitized Papers:SPV designs the instruments based on nature of interest, risk, tenure etc. based on pool of assets. These instruments can be Pass Through Security or Pay Through Certificates.[PTS & PTC will be explained later]

4. Administration of assets: The administration of assets where originator collects principal and interest from underlying assets and transfer it to SPV, which works as a conduct.

5. Recourse* to Originator:Performance of securitized papers depends on the performance of underlying assets and unless specified in case of default they go back to originator from SPV.

6.Repayment of funds:SPV will repay the funds in form of interest and principal that arises from the assets pooled.

7.Credit Rating to Instruments: Sometimes before the sale of securitized instruments credit rating can be done to assess the risk of the issuer.

QUESTION NO.5 What are the main PROBLEMS IN SECURITIZATION especially in indian context?

1. Stamp Duty: Stamp Duty is one of the obstacle in India. Under Transfer of Property Act, 1882, a mortgage debt stamp duty which even goes upto 12% in some states of India and this impeded the growth of securitization in India. It should be noted that since pass through certificate does not evidence any debt only able to receivable, they are exempted from stamp duty.

Moreover, in India, recognizing the special nature of securitized instruments in some states has reduced the stamp duty on them.

2. Taxation: Taxation is another area of concern in India. In the absence of any specific provision relating to securitized instruments in Income Tax Act, expert's opinion differ a lot. Some are of opinion that SPV as a trustee is liable to be taxed in a representative capacity then other are of view that instead of SPV, investors will be taxed on their share of income. Clarity is also required on the issues of capital gain implications on passing payments to the investors.

3. Accounting: Accounting and reporting of securitized assets in the books of originator is another area of concern. Although securitization is slated to an off-balance sheet instrument but in true sense receivables are removed from originator's balance sheet. Problem arises especially when assets are transferred without recourse*.

4. Lack of standardization: Every originator follows own format for documentation and administration, hence lack of standardization is another obstacle in growth of securitization.

5. Inadequate Debt Market: Lack of existence of a well-developed debt market in India is another obstacle that hinders the growth of secondary market of securitized or asset backed securities.

6.Ineffective Foreclosure* laws:Foreclosure laws are not supportive to lending institutions and this makes securitized instruments especially mortgaged backed securities less attractive as lenders face difficulty in transfer of property in event of default by the borrower.

QUESTION NO.11 Explain various Market Indicators.

➡**Following are major Market Indicators**:

(i)Breadth Index: It is an index that covers all securities traded. It is computed by dividing the net advances or declines in the market by the number of issues traded. The breadth index either supports or contradicts the movement of the Dow Jones Averages. If it supports the movement of the Dow Jones Averages, this is considered sign of technical strength and if it does not support the averages, it is a sign of technical weakness i.e. a sign that the market will move in a direction opposite to the Dow Jones Averages. The breadth index is an addition to the Dow Theory and the movement of the Dow Jones Averages.

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(iv)Relative Strength Analysis: The relative strength concept suggests that the prices of some securities rise relatively faster in a bull market or decline more slowly in a bear market than other securities i.e. some securities exhibit relative strength. Investors will earn higher returns by investing in securities which have demonstrated

QUESTION NO.6 What are the SECURITIZATION INSTRUMENTS ?Or Differentiate between PTS and PTC?

1. Pass Through Certificates (PTCs)

➡As the title suggests, originator (seller of the assets) **transfers the entire receipt** of cash in form of interest or principal repayment from the assets sold. ➡Thus, these securities **represent direct claim of the investors** on all the assets that has been securitized through SPV.➡Since all cash flows are transferred, the **investors carry proportional beneficial interest** in the asset held in the trust by SPV.➡It should be noted that since it is a direct route, **any prepayment of principal** is also proportionately distributed among the securities holders. ➡Further, due to these characteristics, on completion of securitization by the **final payment of assets**, all the securities are terminated simultaneously.➡**Skewness* of cash flows** occurs in early stage if principals are repaid before the scheduled time.

2. Pay Through Security (PTS)

➡As mentioned earlier,since, in PTCs all cash flows are passed to the performance of the securitized assets. To overcome this limitation and **limitation to single mature** there is another structure i.e. PTS.➡In PTS, SPV can issue debt securities backed by the assets and hence it **can restructure different tranches* from varying maturities** of receivables.➡In other words, this structure **permits desynchronization*** of servicing of securities issued from cash flow generating from the asset. ➡Further, this structure also **permits the SPV to reinvest surplus funds** for short term as per their requirement.➡Since, in Pass Through Certificates, all cash flow are immediately passed ,In PTS in case of **early retirement of receivables** ,cash can be used for short term yield.
➡This structure also **provides the freedom to issue several debt trances* with varying maturities**.

3.Stripped Securities

➡Stripped Securities are created by dividing the cash flows associated with underlying securities into **two new securities**. Those two securities are as follows:

(i)Interest Only (IO) Securities (ii)Principle Only (PO) Securities

➡As each investor receives a combination of principal and interest, it **can be stripped into two portion of Interest and Principle.**➡Accordingly, the holder of IO securities **receives only interest** while PO security holder **receives only principal.** ➡Being highly volatile in nature these securities are **less preferred** by investors.➡In case **yield to maturity(interest) in market rises**, **PO price tends to fall** as borrower prefers to postpone the payment of principal amount. Reason is simple if they pay early they will have to borrow money at high rate of interest.Hence they prefer to postpone their principal payment.➡Whereas **if interest rate in market falls**,**PO price tends to rise** as the borrower tends to repay the loans fast as they prefer to borrow fresh at lower rate of interest.➡In contrast, **value of I0's securities increases** **when interest rate goes** up in the market as more interest is collected on borrowings.As borrower will pay interest on time as they know that they are paying less interest than prevailing rate.➡Whereas **if interest rate in market falls**, the borrower tends to repay the loans fast rather than interest.And due to prepayments of principals, **IO's tends to fall**.➡Thus, from the above, it is clear that it is **mainly perception of investors** that determines the prices of IOs and POs

QUESTION NO.7 How PRICING OF THE SECURITIZED INSTRUMENTS are done?Or Explain the pricing of the securitized Instruments?

➡Pricing of securitized instruments in an important aspect of securitization. While pricing the instruments, it is important that it should be acceptable to both originators as well as to the investors. On the same basis pricing of securities can be divided into following two categories:

➡**From Originator's Angle:**From originator's point of view, the instruments can be priced at a rate at which **originator has to incur an outflow** and if that outflow can be amortized over a period of time then it should match the amount raised through securitization.

➡**From Investor's Angle:**From an investor's angle security price can be determined by discounting best estimate of expected future cash flows **using rate of yield to maturity(Kd)** of a security of comparable security with respect to credit quality and average life of the securities.This yield can also be estimated by referring the **yield curve available for marketable securities**, though some adjustments is needed on account of spread* points, because of credit quality of the securitized instruments.

QUESTION NO.8 Write a short note on SECURITIZATION IN INDIA ?

➡It is the **Citi Bank** who pioneered the concept of securitization in India by bundling of auto loans in securitized instruments.➡Thereafter many organizations securitized their receivables. Although started with securitization of **auto loans** it moved to other types of receivables such as **sales tax deferrals, aircraft receivable** etc.➡In order to encourage securitization, the Government has come out with Securitization and Reconstruction of Financial Assets and Enforcement of Security Interest **(SARFAESI) Act, 2002**, to tackle menace of **Non Performing Assets (NPAs) without approaching to Court.**➡With growing sophistication of financial products in Indian Capital Market, **securitization has occupied an important place.**➡As mentioned above, though, initially started with auto loan receivables, it has become an important **source of funding for micro finance companies and NBFCs** and even now a days commercial mortgage backed securities are also emerging.➡The important highlight of the scenario of securitization in Indian Market is that it is dominated by a few players e.g. **ICICI Bank, HDFC Bank, NHB etc.**➡As per a report of CRISIL, securitization transactions in India scored to the **highest level of approximately Rs. 70000 crores, in Financial Year 2016. (Business Line,15th June, 2016).**➡In order to further enhance the investor base in securitized debts, **SEBI allowed FPIs(Foreign Portfolio Investment) to invest in securitized debt of unlisted companies upto a certain limit.**

4.STARTUP FINANCE

QUESTION NO.1 What are the INNOVATIVE WAYS TO FINANCE A STARTUP? OR Explain some of the sources for funding a start-up? OR Examine briefly the various innovative methods of funding the Startups.

➡**Here are some of the innovative sources for funding a Startup:**

(i)Personal financing. It may not seem to be innovative but you may be surprised to note that most budding

entrepreneurs never thought of saving any money to start a business. This is important because most of the investors will not put money into a deal if t hey see that you have not contributed any money from your personal sources.

(ii)Personal credit lines. One qualifies for personal credit line based on one's personal credit efforts. Credit cards are a good example of this. However, banks are very cautious while granting personal credit lines. They provide this facility only when the business has enough cash flow to repay the line of credit.

(iii)Family and friends. These are the people who generally believe in you, without even thinking that your idea works or not. However, the loan obligations to friends and relatives should always be in writing as a promissory note or otherwise.

(iv)Peer-to-peer lending. In this process group of people come together and lend money to each other. Peer to peer to lending has been there for many years. Many small and ethnic business groups having similar faith or interest generally support each other in their start up endeavors.

(v)Crowdfunding. Crowdfunding is the use of small amounts of capital from a large number of individuals to finance a new business initiative. Crowdfunding makes use of the easy accessibility of vast networks of people through social media and crowdfunding websites to bring investors and entrepreneurs together.

(vi)Microloans. Microloans are small loans that are given by individuals at a lower interest to a new business ventures. These loans can be issued by a single individual or aggregated across a number of individuals who each contribute a portion of the total amount.

(vii)Vendor financing. Vendor financing is the form of financing in which a company lends money to one of its customers so that he can buy products from the company itself. Vendor financing also takes place when many manufacturers and distributors are convinced to defer payment until the goods are sold. This means extending the payment terms to a longer period for e.g. 30 days payment period can be extended to 45 days or 60 days. However, this depends on one's credit worthiness and payment of more money.

(viii)Purchase order financing. The most common scaling problem faced by startups is the inability to find a large new order. The reason is that they don't have the necessary cash to produce and deliver the product. Purchase order financing companies often advance the required funds directly to the supplier. This allows the transaction to complete and profit to flow up to the new business.

(ix)Factoring accounts receivables. In this method, a facility is given to the seller who has sold the good on credit to fund his receivables till the amount is fully received. So, when the goods are sold on credit, and the credit period (i.e. the date upto which payment shall be made) is for example 6 months, factor will pay most of the sold amount up front and rest of the amount later. Therefore, in this way, a startup can meet his day to day expenses.

QUESTION NO.2 What is PITCH PRESENTATION?

➡Pitch deck presentation is a short and brief presentation (not more than 20 minutes) to investors explaining about the prospects of the company and why they should invest into the startup business.

➡Here, some of the methods have been highlighted below as how to approach a pitch presentation:

(i)Introduction: To start with, first step is to give a brief account of yourself i.e. who are you? What are you doing?

(ii)Team: The next step is to introduce the audience the people behind the scenes.

(iii) Problem: Further, the promoter should be able to explain the problem he is going to solve .

(iv)Solution: It is very important to describe in the pitch presentation as to how the company is planning to solve the problem.

(v)Marketing/Sales: The market size of the product must be communicated to the investors. This can include profiles of target customers, but one should be prepared to answer questions about how the promoter is planning to attract the customers.

(vi) Projections or Milestones: Financial projections include three basic documents that make up a business's financial statements.**(i)**Income statement **(ii)**Cash flow statement **(iii)**Balance sheet

(vii)Competition: Every business organization has competition even if the product or service offered is new and unique. It is necessary to highlight in the pitch presentation as to how the products or services are different from their competitors.

(viii)Business Model: The term business model is a wide term denoting core aspects of a business including purpose, business process, target customers, offerings, strategies, infrastructure, organizational structures, sourcing, trading practices, and operational processes and policies including culture.

(ix)Financing: If a startup business firm has raised money,it is preferable to talk about how much money has already been raised, who invested money into the business and what they did about it.

QUESTION NO.3 What are the MODES OF FINANCING FOR STARTUPS?

(i) Bootstrapping:**(ii)**Angel Investors:**(iii)** Venture Capital Funds

QUESTION NO.4 EXPLAIN the concept of Bootstrapping and describe the various methods of bootstrapping used by start ups. ? OR Explain the methods in which a Stratup firm can bootstrap.

➦An individual is said to be boot strapping when he or she attempts to found and build a company **from personal finances** or from the operating revenues of the new company.Here are **some of the methods** in which a startup firm can bootstrap:

(i)Trade Credit: **When a person is starting his business, suppliers are reluctant to give trade credit.** They will insist on payment of their goods supplied either by cash or by credit card. However, a way out in this situation is to prepare a well-crafted financial plan. The next step is to pay a visit to the supplier's office. If the business organization is small, the owner can be directly contacted. On the other hand, if it is a big firm, the Chief Financial Officer can be contacted and convinced about the financial plan.

Communication skills are important here. The financial plan has to be shown. The owner or the financial officer has to be explained about the business and the need to get the first order on credit in order to launch the venture. The owner or financial officer may give half the order on credit and balance on delivery. The trick here is to get the goods shipped and sell them before paying to them. One can also borrow to pay for the good sold. But there is interest cost also. So trade credit is one of the most important ways to reduce the amount of working capital one needs. This is especially true in retail operations.

(ii)Factoring: This is a financing method where **accounts receivable of a business organization is sold** to a commercial finance company to raise capital. The factor then got hold of the accounts receivable of a business organization and assumes the task of collecting the receivables as well as doing what would've been the paperwork. Factoring can be performed on a non-notification basis. It means customers may not be told that their accounts have been sold.

In addition to reducing internal costs of a business, factoring also frees up money that would otherwise be tied to receivables. This is especially true for businesses that sell to other businesses or to government; there are often long delays in payment that this would offset. This money can be used to generate profit through other avenues of the company. Factoring can be a very useful tool for raising money and keeping cash flowing.

(iii)Leasing: Another popular method of bootstrapping is to **take the equipment on lease rather than purchasing it.** It will reduce the capital cost and also help lessee (person who take the asset on lease) to claim tax exemption. So, it is better to a take a photocopy machine, an automobile or a van on lease to avoid paying out lump sum money which is not at all feasible for a startup organization.

QUESTION NO.5 Write a short note on Angel Investor ?

➦Angel investors **invest in small startups or entrepreneurs**. Often, angel investors are among an **entrepreneur's family and friends**. The capital angel investors provide may be a **one-time investment** to help the business grow **or an ongoing injection of money** to support and carry the company through its difficult early stages.

➦Angel investors provide **more favorable terms** compared to other lenders, since they usually **invest in the**

entrepreneur starting the business rather than the viability of the business. Angel investors are focused on **helping startups take their first steps**, rather than the possible profit they may get from the business. Essentially, **angel investors are the opposite of venture capitalists.**

➦Angel investors are also called **informal investors, angel funders, private investors, seed investors or business angels**. These are **affluent(rich) individuals who inject capital for startups in exchange for ownership equity or convertible debt**. Some angel investors invest through **crowdfunding platforms online or build angel investor networks** to pool in capital.

➦Angel investors typically **use their own money**, unlike venture capitalists who take care of pooled money from many other investors and place them in a strategically managed fund. Though angel investors usually represent individuals, the entity that actually provides the fund may be a **limited liability company, a business, a trust or an investment fund**, among many other kinds of vehicles.

➦Angel investors who seed startups that fail during their early stages **can lose their investments completely.** This is why professional angel investors look for opportunities for a **defined exit strategy, acquisitions or initial public offerings (IPOs).**

QUESTION NO.6 Write a short note on Venture Capital Funds ?

➦**Meaning:** **Venture capital funds** are investment **funds** that manage the money of investors who seek to invest in startup and small- to medium-sized enterprises with strong growth potential. These **investments** are generally characterized as high-risk/high-return opportunities.

➦**Structure of Venture Capital Fund in India**

Three main types of fund structure exist: one for domestic funds and two for offshore ones:

(a)Domestic Funds: ➦Domestic Funds raises funds **domestically**.➦They are usually structured as: **(i)** a **domestic vehicle** for the pooling of funds from the investor, **(ii)** a **separate investment adviser** that carries those duties of asset manager. ➦Domestic Vehicle may be a **trust and a company**.India, unlike most developed countries does not recognize a **limited partnership**.➦**Trust** form is considered best due to its operational flexibility.

(b)Offshore Funds: Two common **alternatives available to offshore investors** are: the "offshore structure" and the "unified structure".

Offshore structure: ➦Under this structure, an **investment vehicle** having jurisdiction **outside India** is created.➦It can be an **LLC or an LP**.[Limited Liability Company or Limited Partnership]➦It makes **investments directly** into Indian portfolio companies. ➦Typically, the assets are managed by an **offshore manager**, while the **investment advisor in India** carries out the due diligence and identifies deals.

Unified Structure: ➦When **domestic investors** are expected to participate in the fund, a unified structure is used. ➦**Overseas investors** pool their assets in an offshore vehicle that invests in a **locally managed trust**, whereas **domestic investors** directly contribute to the trust. ➦This structure is deviced to make the **local portfolio investments**.

Characteristics of Venture Capital Financing:

(i)Long time horizon:-The fund would invest with a long time horizon in mind. Minimum period of investment would be 3 years and maximum period can be 10 years.

(ii)Lack of liquidity: When VC invests, it takes into account the liquidity factor.It assumes that there would be less liquidity on the equity it gets.They adjust this liquidity premium against the price and required return.

(iii)High Risk: VC would not hesitate to take risk. It works on principle of high risk and high return. So, high risk would not eliminate the investment choice for a venture capital.

(iv)Equity Participation: Most of the time, VC would be investing in the form of equity of a company. This would help the VC participate in the management and help the company grow. Besides, a lot of board decisions can be supervised by the VC if they participate in the equity of a company.

Advantages of bringing VC in the company:

(1) It injects **long- term equity finance** which provides a **solid capital base** for future growth.

(2) The venture capitalist is a business partner, **sharing both the risks and rewards**. Venture capitalists are

rewarded with business success and capital gain.

(3) The venture capitalist is able to **provide practical advice and assistance** to the company based on past experience with other companies which were in similar situations.

(4) The venture capitalist also **has a network of contacts** in many areas that can add value to the company.

(5) The venture capitalist may be **capable of providing additional rounds of funding** should it be required to finance growth.

(6) Venture capitalists are experienced in the process of **preparing a company for an initial public offering (IPO)** of its shares onto the stock exchanges or overseas stock exchange such as NASDAQ.

(7) They can also facilitate a trade sale*.

Stages of funding for VC:

(1)Seed Money: Low level financing **needed to prove a new idea**.

(2)Startup: Early stage firms that need funding for expenses associated with **marketing & product development.**

(3)First-Round: Early **sales and manufacturing funds**.

(4)Second-Round:Working capital for early stage companies that are selling product, but not yet turning in a profit.

(5)Third Round: Also called Mezzanine financing, this is **expansion money** for a newly profitable company.

(6)Fourth-Round- Also called bridge financing, it is intended to finance the **"going public"**process.

Risk in each stage is different. **An indicative Risk matrix is given below:**

Financial Stage	Period(Funds locked in years)	Risk Perception
SeedMoney	7-10	Extreme
Start Up	5-9	Very High
First Stage	3-7	High
Second Stage	3-5	Sufficiently high
Third Stage	1-3	Medium
Fourth Stage	1-3	Low

QUESTION NO.7 What are the steps of Venture capital Investment?

1) Deal Origination: VC operates directly or through intermediaries. Mainly many practicing Chartered Accountants would work as intermediary and through them VC gets the deal.Before sourcing the deal, the VC would inform the intermediary or its employees about the following

(a) Sector focus**(b)**Stages of business focus**(c)**Promoter focus**(d)**Turnover focus

2)Screening: Once the deal is sourced the same would be sent for screening by the VC.

3)Due Diligence: Once the decision is taken to proceed further, the VC would now carry out due diligence. This is mainly the process by which the VC would try to verify the accuracy of the documents taken.

4)Deal Structuring: The deal is structured in such a way that both parties win.

5)Post Investment Activity: The company has to adhere to certain guidelines like strong MIS(Management Information System), strong budgeting system, strong corporate governance and other restrictions of the VC and periodically keep the VC updated about certain milestones.

6)Exit plan: At the time of investing, the VC would ask the promoter or company to spell out in detail the exit plan.

QUESTION NO.8 Compare and contrast startups and entrepreneurship. Describe the priorities and challenges which startups in India are facing?

Differences between a startup and entrepreneurship:

(i) Start up is a part of entrepreneurship. Entrepreneurship is a **broader concept** and it includes a startup firm.

(ii) The main aim of startup is to **build a concern**, conceptualize the idea which it has developed into a reality and build a product or service. On the other hand, the major objective of an already established entrepreneurship concern is to **attain opportunities** with regard to the resources **they currently control**.

(iii)A startup generally does not have a major **financial motive** whereas an established entrepreneurship concern

mainly operates on financial motive.

Priorities and challenges which startups in India are facing: The **priority** is on bringing more and more **smaller firms** into existence. So, the focus is on **need based**, instead of opportunity based entrepreneurship. Moreover, the trend is to **encourage self- employment rather than large, scalable concerns.**

The **main challenge** with the startup firms is getting the **right talent**. And, **scarcity** of skilled workforce can hinder the chances of a startup organization's growth and development. Further, startups had to comply with **numerous regulations** which escalates it's cost. It leads to further **delaying** the chances of a breakeven or even earning some amount of profit.

QUESTION NO.9 EXPLAIN Startup India Initiative ?Or What is a startup to avail the benefits of government scheme ?

➦Startup India scheme was initiated by the Government of India on **16th of January, 2016**. Startup means an entity, incorporated or registered in India: **(i)** Not prior to **five years**, **(ii)** With annual turnover not exceeding **Rs. 25 crore** in any preceding financial year, and **(iii) Working towards** innovation, development, deployment or commercialization of new products, processes or services driven by technology or intellectual property.

Provided that such entity is not formed by splitting up, or reconstruction, of a business already in existence.

Provided also that an entity shall cease to be a Startup if its turnover for the previous financial years has exceeded ` 25 crore or it has completed 5 years from the date of incorporation/ registration.

Provided further that a Startup shall be eligible for tax benefits only after it has obtained certification from the Inter- Ministerial Board, setup for such purpose.

5. RISK MANAGEMENT

QUESTION NO.1 Explain how many TYPES OF RISK IS FACED BY AN ORGANIZATION?

Strategic Risk: Strategic risk is a risk in which a company's strategy becomes less effective and it struggles to achieve its goal.

Compliance Risk: Every business needs to comply with rules and regulations. For example with the advent of **Companies Act, 2013, and continuous updating of SEBI guidelines**, each business organization has to comply with plethora of rules, regulations and guidelines.

Operational Risk: This type of risk relates to internal risk. It also relates to **failure on the part of the company to cope with day to day operational problems.** Operational risk relates to 'people' as well as 'process'.

Financial Risk: Financial Risk is referred as the unexpected changes in financial conditions such as prices, exchange rate, Credit rating, and interest rate etc. ➦**Broadly Financial Risk can be divided into following categories**:

(I) Counter Party Risk: This risk occurs due to non-honoring of obligations by the counter party which can be failure to deliver the goods for the payment already made or vice-versa or repayment of borrowings and interest etc. Thus, this risk also covers the credit risk i.e. default by the counter party.

(2) Political Risk: Generally this type of risk is faced by an overseas investors, as the adverse action by the government of host country* may lead to huge loses. **This can be on any of the following form:**

(i) Confiscation or destruction of overseas properties. **(ii)** Rationing of remittance to home country. **(iii)** Restriction on conversion of local currency of host country* into foreign currency. **(iv)** Restriction as borrowings. **(v)** Invalidation of Patents **(vi)** Price control of products

(3) Interest Rate Risk: This risk occurs due to change in interest rate resulting in change in asset and liabilities. This risk is more important for banking companies as their balance sheet's items are more interest sensitive and their base of earning is spread* between borrowing and lending rates.

As we know that the interest rates are two types i.e. fixed and floating. The risk in both of these types is inherent. If any company has borrowed money at floating rate then the risk is rise in interest rate. If any company has borrowed money at fixed rate then the risk is fall in interest rate.

(4) Currency Risk: This risk mainly affects the organization dealing with foreign exchange as their cash flows

changes with the movement in the currency exchange rates. This risk can be affected by cash flow adversely or favorably. For example, if rupee depreciates or dollar appreciates, exporter will stand to gain .If rupee appreciates or dollar depreciates,importer will gain. The best case we can quote Infosys (Exporter) and Indian Oil Corporation Ltd. (Importer).

(5)Liquidity Risk: Broadly liquidity risk can be defined as inability of organization to meet it liabilities whenever they become due.This risk mainly arises when organization is unable to generate adequate cash or there may be some mismatch in period of cash flow generation.This type of risk is more prevalent in banking business where there may be mismatch in maturities and receiving fresh deposits pattern.

QUESTION NO.2: What is Financial Risk? How it can be evaluated from point of views. OR EVALUATE financial risk from different point of views(STAKEHOLDERS)?

Financial Risk is referred as the unexpected changes in financial conditions such as prices, exchange rate, Credit rating, and interest rate etc. Though political risk is not a financial risk in direct sense but same can be included as any unexpected political change in any foreign country may lead to country risk which may ultimately result in financial loss.

➡**The financial risk can be evaluated from different point of views as follows**:

(a) From shareholder's[stakeholder's] point of view:Major stakeholders of a business are equity **shareholders** and they view financial gearing i.e.**ratio of debt in capital structure** of company as risk since in event of winding up of a company they will be least prioritized.

Even for a **lender**, **existing gearing** is also a risk since company having high gearing faces more risk in default of payment of interest and principal repayment.

(b) From Company's point of view:From company's point of view if a company borrows excessively or lend to someone who defaults, then it can be forced to go into liquidation.

(c) From Government's point of view: From Government's point of view, the financial risk can be viewed as **failure of any bank** (like Lehman Brothers*),and **downgrading of any financial institution** leading to spread of distrust among society at large. Even this risk also includes willful defaulters*. This can also be extended to sovereign debt crisis*.

QUESTION NO.3 WHAT IS VALUE-AT-RISK (VAR) ?

➡VAR is a **measure of risk of investment**.Given the normal market condition in a set of period, say, one day it estimates how much an investment might lose. This investment can be a portfolio, capital investment or foreign exchange etc.

➡**VAR answers two basic questions** -**(i)**What is worst case scenario?**(ii)** What will be loss?

➡It was **first applied in 1922** in New York Stock Exchange, entered the financial world in 1990s and become world's most widely used measure of financial risk.

➡**Features of VAR**

(i)Components of Calculations:VAR calculation is based on following three components :**(a)**Time Period **(b)**Confidence Level - Generally 95% and 99%**(c)** Loss in percentage or in amount

(ii)Statistical Method: It is a type of statistical tool based on Standard Deviation.

(iii)Time Horizon: VAR can be applied for different time horizons say one day, one week, one month and so on.

(iv)Probability: Assuming the values are normally attributed, probability of maximum loss can be predicted.

(v)Control Risk: Risk can be controlled by setting limits for maximum loss.

(vi)Z Score: Z Score indicates how many standard Deviations is away from Mean value of a population. When it is multiplied with Standard Deviation it provides VAR.

➡**Application of VAR :**VAR can be applied **(a)** to measure the **maximum possible loss** on any portfolio or a trading position.**(b)** as a **benchmark for performance measurement** of any operation or trading.**(c)** to **fix limits** for individuals dealing in front office of a treasury department.**(d)** to enable the management to **decide the trading strategies**.**(e)**as a **tool for Asset and Liability Management** especially in banks.

QUESTION NO.4 Write a short note on appropriate methods for identification and management of counter party risk ?Or Briefly explain Counter party risk and the various techniques to manage this risk ?

➡**The various hints that may provide counter party risk are as follows**:**(a) Failure to obtain necessary resources** to complete the project or transaction undertaken.**(b)** Any **regulatory restrictions from the Government**.**(c)Hostile action of foreign governmen**t.**(d) Let down by third party**.**(e)Have become insolvent**.

➡**The various techniques to manage this type of risk are as follows:(1)**Carrying out **Due Diligence** before dealing with any third party.**(2) Do not over commit** to a single entity or group or connected entities.**(3) Know your exposure limits**.**(4)** Review the limits and procedure for **credit approval regularly.(5) Rapid action** in the event of any likelihood of defaults.**(6) Use of performance guarantee, insurance or other instruments.**

QUESTION NO.5 How should company assess political risk and how this risk can be identified ?

➡**Since this risk mainly relates to investments in foreign country, company should assess country**
(1) By referring **political ranking** published by different business magazines.**(2)** By evaluating **country's macro-economic conditions.(3)** By analyzing the **popularity of current government** and assess their stability.**(4)** By **taking advises from the embassies** of the home country in the host countries.**(5)** Further, following techniques can be used to mitigate(minimize) this risk.**(i)** Local sourcing of raw materials and labour.**(ii)** Entering into joint ventures**(iii)** Local financing**(iv)** Prior negotiations

➡**From the following actions by the Governments of the host country* this risk can be identified**:
1. Insistence on resident investors or labour.**2.** Restriction on conversion of currency.**3.** Repatriation* of foreign assets of the local govt.**4.** Price fixation of the products.

QUESTION NO.6 How Interest Rate Risk can be identified ?

➡**Generally, interest rate Risk is mainly identified from the following**:
1.Monetary Policy of the Government.**2.**Any action by Government such as demonetization etc.**3.**Economic Growth **4.**Release of Industrial Data **5.**Investment by foreign investors **6.**Stock market changes

QUESTION NO.7 How Currency Risk can be identified ? or Explain briefly the parameters to identify the currency risk?

➡**Some of the parameters to identity the currency risk are as follows**:
(1) Government Action: The Government action of any country has visual impact in its currency. For example, the UK Govt, decision to divorce from European Union i.e. Brexit brought the pound to its lowest since 1980's.
(2)Nominal Interest Rate: As per interest rate parity (IRP) the currency exchange rate depends on the nominal interest of that country.
(3)Inflation Rate: As per Purchasing power parity theory.inflation rate impact the value of currency.
(4)Natural Calamities: Any natural calamity can have negative impact.
(5)War, Coup, Rebellion etc.: All these actions can have far reaching impact on currency's exchange rates.
(6)Change of Government: The change of government and its attitude towards foreign investment also helps to identify the currency risk.

6. INTERNATIONAL FINANCIAL MANAGEMENT

QUESTION NO.1 List the main objectives of International Cash Management?

➡**The main objectives of an effective system of international cash management are:(1)**To minimise currency **exposure risk.(2)**To minimise overall cash requirements of the company as a whole without disturbing **smooth operations** of the subsidiary or its affiliate.**(3)**To minimise **transaction costs.(4)**To minimise **country's political risk.(5)**To take advantage of **economies of scale** as well as reap benefits of superior knowledge.

QUESTION NO.2 Briefly discuss the concept of Purchasing Power Parity. ?

➡Purchasing Power Parity theory focuses on the **'inflation - exchange rate'** relationship. ➡There are two forms of PPP theory:-

➡**The ABSOLUTE FORM**, also called the **'Law of One Price'** suggests that "prices of similar products of two different countries should be equal when measured in a common currency'. If a discrepancy in prices as measured by a common currency exists, the demand should shift so that these prices should converge (become equal).

➡**The RELATIVE FORM** is an alternative version that accounts for the possibility of market imperfections such as transportation costs, tariffs, and quotas. It suggests that 'because of these market imperfections, prices of similar products of different countries will not necessarily be the same when measured in a common currency.' However, it states that the rate of change in the prices of products should be somewhat similar when measured in a common currency, as long as the transportation costs and trade barriers are unchanged.

➡The formula for computing the forward rate using the inflation rates in domestic and foreign countries is as follows: $F = S\frac{(1+i_D)}{(1+i_F)}$ Where F— Forward Rate of Foreign Currency and S— Spot Rate i_D— Domestic Inflation Rate and i_F— Inflation Rate in foreign country

➡Thus PPP theory states that the exchange rate between two countries reflects the relative purchasing power of the two countries i.e. the price at which a basket of goods can be bought in the two countries.

QUESTION NO.3 What are the complexities involved in international capital budgeting?

➡Multinational Capital Budgeting has to take into consideration the different factors and variables which affect a foreign project and are complex in nature than domestic projects. **The factors crucial in such a situation are:** **(a)**Cash flows from foreign projects have to be **converted** into the currency of the parent organization.**(b)**Parent cash flows are **quite different** from project cash flows**(c)**Profits remitted to the parent firm are **subject to tax i**n the home country as well as the host country***(d)**Effect of foreign **exchange risk** on the parent firm's cash flow **(e)**Changes in **rates of inflation** causing a shift in the competitive environment and thereby affecting cash flows over a specific time period **(f)Restrictions imposed on cash flow** distribution generated from foreign projects by the host country* **(g)**Initial investment in the host country* to benefit from the **release of blocked funds** **(h)Political risk** in the form of changed political events reduce the possibility of expected cash flows **(i)Concessions/benefits provided** by the host country ensures the upsurge(rise) in the profitability position of the foreign project **(j)Estimation of the value** in multinational capital budgeting is difficult since the buyers in the parent company have divergent views on acquisition of the project.

QUESTION NO.4 Explain the problems that are faced in International Capital Budgeting Decision and how these can be overcome.

➡**The various types of problems faced in International Capital Budgeting analysis are as follows:**

(1) Multinational companies investing elsewhere are subjected to foreign exchange risk in the sense that currency appreciates/ depreciates over a span of time. To include foreign exchange risk in the cash flow estimates of any project, it is necessary to forecast the inflation rate in the host country during the lifetime of the project. Adjustments for inflation are made in the cash flows depicted in local currency. The cash flows are converted in parent country's currency at the spot exchange rate multiplied by the expected depreciation rate obtained from purchasing power parity.

(2) Due to restrictions imposed on transfer of profits, depreciation charges and technical differences exist between project cash flows and cash flows obtained by the parent organization. Such restriction can be diluted by the application of techniques viz internal transfer prices, overhead payments. Adjustment for blocked funds depends on its opportunity cost, a vital issue in capital budgeting process.

(3) In multinational capital budgeting, after tax cash flows need to be considered for project evaluation. The **presence of two tax regimes** along with other factors such as remittances to the parent firm in the form of royalties, dividends, management fees etc., tax provisions with held in the host country, presence of tax treaties,

tax discrimination pursued by the host country between transfer of realized profits vis-à-vis local re-investment of such profits cause serious impediments to multinational capital budgeting process. MNCs are in a position to reduce overall tax burden through the system of transfer pricing.

For computation of actual after tax cash flows accruing to the parent firm, higher of home/ host country tax rate is used. If the project becomes feasible then it is acceptable under a more favourable tax regime. If not feasible, then, other tax saving aspects need to be incorporated in order to find out whether the project crosses the hurdle rate.

QUESTION NO.5 Explain the difference between Forward and Future Contract ?

Features	Forward	Futures
1.Trading	Forward contracts are traded on personal basis or on telephone or otherwise.	Futures Contracts are traded in a competitive arena.
2.Size of Contract	Forward contracts are individually tailored and have no standardized size	Futures contracts are standardized in terms of quantity or amount as the case may be.(i.e there is lot size requirement)
3.Organized exchanges	Forward contracts are traded in an over the counter market.(Ex:Bank)	Futures contracts are traded on organized exchanges with a designated physical location.
4.Settlement	Forward contracts settlement takes place on the date agreed upon between the parties.	Futures contracts settlements are made daily via. Exchange's clearing house.
5.Delivery date	Forward contracts may be delivered on the dates agreed upon and in terms of actual delivery.	Futures contracts delivery dates are fixed on cyclical basis and it hardly takes place. However, it does not mean that there is no actual delivery.
6.Transaction costs	Cost of forward contracts is based on bid - ask spread*.	Futures contracts entail brokerage fees for buy and sell order.
7.Marking to market	Forward contracts are not subject to marking to market	Futures contracts are subject to marking to market in which the loss or profit is debited or credited in the margin account on daily basis due to change in price.
8.Margins	Margins are not required in forward contract.	In futures contracts every participants is subject to maintain margin as decided by the exchange authorities
9.Credit risk	In forward contract, credit risk is born by each party and, therefore, every party has to bother for the creditworthiness.	In futures contracts the transaction is a two way transaction, hence the parties need not to bother for the risk. [**Extra Note:**stock exchange rules are strict and hence very less chance of default.]

7. MUTUAL FUND

QUESTION NO.1 EXPLAIN the concept of side pocketing in mutual funds?

➡In simple words, a **Side Pocketing in Mutual Funds leads to separation of risky assets from other investments and cash holdings.** ➡The **purpose** is to make sure that money invested in a mutual fund, which is linked to **stressed assets, gets locked**, until the fund recovers the money from the company and avoid distress selling of illiquid securities.➡The **modus operandi* is simple**. Whenever, the rating of a mutual fund decreases, the fund shifts the illiquid assets into a side pocket so that current shareholders can be benefitted from the liquid assets. Consequently, the Net Asset Value (NAV) of the fund will then reflect the actual value of the liquid assets.

➡Side Pocketing is **beneficial** for those **investors** who wish to hold on to the units of the main funds for **long term**. ➡Therefore, the process of Side Pocketing ensures that **liquidity is not the problem** even in the

circumstances of frequent allotments and redemptions.➦Side Pocketing is **quite common internationally.** ➦However, Side Pocketing has also been resorted to **neglect the investors of genuine returns.**➦**In India** recent fraud in the **Infrastructure Leasing and Financial Services (IL&FS)** has led to many discussions on the concept of side pocketing as IL&FS and its subsidiaries have failed to fulfill its repayments obligations due to severe liquidity crisis.The Mutual Funds have given negative returns because they have completely written off their exposure to IL&FS instruments.

QUESTION NO.2 Write short note on'Exchange Traded Funds'? OR What are its key features? OR What are its advantage? OR What are the types of ETF products are available in the market ?

➦Exchange Traded Funds (ETFs) were **introduced in US in 1993 and came to India** around 2002.

Key features:➦An Exchange Traded Fund (ETF) is a **hybrid product** that combines the features of an index fund. ➦These funds are **listed on the stock exchanges** and their prices are linked to the underlying index. ➦The authorized participants act as **market makers*** for ETFs.➦ETFs can be bought and sold **like any other stock** on an exchange➦In other words, ETFs can be bought or sold any time **during the market hours** at prices that are expected to be closer to the NAV at the end of the day. ➦Therefore, one can invest at **real time prices** as against the end of the day prices as is the case with open-ended schemes.➦An ETF combines the valuation **feature of a mutual fund or unit investment trust,** which can be bought or sold at the end of each trading day for its net asset value.

Advantage:➦There is **no paper work involved** for investing in an ETF. These can be bought like any other stock by just placing an order with a broker. ➦ETFs may be attractive as investments because of their **low costs, tax efficiency, and stock-like features**.

➦**Following types of ETF products are available in the market:**

•**Index ETFs** - Most ETFs are index funds that hold securities and attempt to replicate the performance of a stock market index.

•**Commodity ETFs** - Commodity ETFs invest in commodities, such as precious metals and futures.

•**Bond ETFs** - ➦Exchange-traded funds that **invest in bonds** are known as bond ETFs. ➦They thrive **during economic recessions** because investors pull their money out of the stock market and into bonds (for example, government treasury bonds or those issues by companies regarded as financially stable). ➦Because of this cause and effect relationship, the performance of bond ETFs may be **indicative of broader economic conditions.**

•**Currency ETFs** -Currency ETFs are exchange-traded funds that track the **relative value of a currency or a basket of currencies**. Currency ETFs allow ordinary individuals to gain exposure to the forex market through a managed fund.

QUESTION NO.3 Differentiate between open ended and close ended fund ?

(i) Number Of Units : The number of units outstanding under the schemes of Open Ended Funds **keeps on changing** . Number of units under Close Ended Funds is **fixed** .

(ii) Maturity Period : Open Ended schemes usually **don't have a fixed maturity** period whereas Close Ended Schemes **have fixed maturity period** .

(iii) NAV / Market Price : The price at which an investor buys or sell shares of a Close Ended Fund after the NFO(New Fund Offer) is the **market price**, as determined by the demand and supply market principles.In contrast, the price at which an investor buys or sells shares of a mutual fund is the **NAV** of the Mutual Fund at the close of a given business day.

(iv) Sale and Purchase : The Units of Open Ended Funds are available for subscription and redemption on an **ongoing basis**.An investor is allowed to **join or withdraw from the fund at any time** by the mutual fund companies at NAV related prices . The Units of Close Ended Funds can be **purchased or sold by the investor** only from the secondary market i.e stock market after the initial public offerings .

(v) Listing : Open Ended Funds are **not listed** on any stock exchange . While **listing** of close ended funds are compulsory on any Stock Exchange .

(vi)Declaration: In case of an open ended mutual fund ,NAVs being declared on a daily basis but for a close ended mutual fund this is declared only on a weekly basis.
(vii)Liquidity: Closed ended funds are not liquid.Open ended funds are Liquid.

QUESTION NO.4 Explain tracking error in brief ?
➡Tracking error can be defined as the **divergence or deviation** of a fund's return from the benchmarks return it is following.➡The passive fund managers **closely follow or track the benchmark index**. Although they design their investment strategy on the same index but often it may not exactly replicate the index return. In such situation, there is possibility of deviation between the returns.➡The tracking error can be calculated on the basis of **corresponding benchmark return vis a vis quarterly or monthly average NAVs.**➡Higher the tracking error **higher is the risk profile** of the fund. If the funds outperform or underperform their benchmark indices; it clearly indicates that of fund managers are not following the benchmark indices properly. ➡**Other reason for tracking error are as follows**:**(i)**Transaction cost**(ii)**Fees charged by AMCs**(iii)**Fund expenses**(iv)**Cash holdings **(v)**Sampling biasness➡Thus from above it can be said that to replicate the return to any benchmark index the **tracking error should be near to zero.**➡The Tracking Error is calculated as follows: $TE = \sqrt{\frac{\sum(d-Ad)}{n-1}}$

where,d = Differential return ; Ad = Average differential return ;n = No. of observation

8. MERGER & ACQUISITION

QUESTION NO.1 Explain the reasons of Reverse Stock Split ?
➡**Reverse Stock Split** is a process whereby a company decreases the number of shares outstanding by combining current shares into fewer or lesser number of shares. ➡**For example,** in a 5:1 reverse split, a company would take back 5 shares and will replace them with one share.Considering above mentioned ratio, if company has 100 million shares outstanding before split up, the number of shares would be equal to 20 million after the reverse split up.➡Athough, reverse stock split does not result in change in **Market value or Market Capitalization** of the company but it results in **increase in price per share.**
➡**Reasons for Reverse Split Up :Generally, company carries out reverse split up due to following reasons:**
(i)Avoiding delisting from stock exchange: Sometimes as per the stock exchange regulation if the price of shares of a company goes below a limit it can be delisted. To avoid such delisting company may resort to reverse stock split up.
(ii)Avoiding removal from constituents of Index: If company's share is one of the constituents of market index then to avoid their removal of scrip from this list, the company may take reverse split up route.
(iii)To avoid the tag of "Penny Stock": If the price of shares of a company goes below a limit it may be called "Penny Stock". In order to improve the image of the company and avoiding this stage, the company may go for Reverse Stock Split.
(iv)To attract Institutional Investors and Mutual Funds: It might be possible that institutional investors may be shying away from acquiring low value shares.Hence to attract these investors, the company may adopt the route of "Reverse Stock Split" to increase the price per share.

QUESTION NO.2 Explain management buyouts and leveraged buyouts? State the purpose of a leveraged buyout with the help of an example.
Management Buy Outs ➡Buyouts initiated by the management team of a company are known as a management buyout. In this type of acquisition, the company is bought by its **own management team.**➡MBOs are considered as a useful strategy for exiting those divisions that **does not form part of the core business** of the entity.
Leveraged Buyout (LBO)➡An acquisition of a company or a division of another company which is **financed entirely or partially (50% or more) using borrowed funds** is termed as a leveraged buyout. ➡The target

company no longer remains public after the leveraged buyout; hence the transaction is also known as **going private**. ➡ The deal is usually **secured by the acquired firm's physical assets.**

Purpose of a leveraged buyout with the help of an example:

➡The **intention behind an LBO transaction** is to improve the operational efficiency of a firm and increase the volume of its sales, thereby increasing the cash flow of the firm. This extra cash flow generated will be used to pay back the debt in LBO transaction. ➡After an, LBO the target entity is managed by private investors, which makes it **easier to have a close control** of its operational activities. ➡The LBOs **do not stay permanent**. Once the LBO is successful in increasing its profit margin and improving its operational efficiency and the debt is paid back, it will go public again. ➡**Companies that are in a leading market position** with proven demand for product, have a strong management team, strong relationships with key customers and suppliers and steady growth are likely to become the target for LBOs. ➡**In India the first LBO took place** in the year 2000 when Tata Tea acquired Tetley in the United Kingdom. The deal value was Rs 2135 crores out of which almost 77% was financed by the company using debt. The intention behind this deal was to get direct access to Tetley's international market. The largest LBO deal in terms of deal value (7.6 Billion) by an Indian company is the buyout of Corus by Tata Steel.

9. DERIVATIVES

QUESTION NO.1 Write a short note on : EMBEDDED DERIVATIVES ?

➡**Meaning Of Derivative:**A derivative is defined as a contract that has **all the following characteristics**:
(i) Its **value changes** in response to a specified underlying, e.g. an exchange rate, interest rate or share price;**(ii)**It requires little or **no initial net investment**;**(iii)**It is settled at a **future date**;
The most common derivatives are **currency forwards, futures, options, interest rate swaps** etc.

➡**Meaning Of Embedded Derivative:**An embedded derivative is a derivative instrument that is **embedded in another contract** - the host contract. ➡The **host contract** might be a debt or equity instrument, a lease, an insurance contract or a sale or purchase contract.

➡**Marked-to-Market Requirement :** Derivatives **requires to be marked-to-market** through the income statement.
➡This requirement on embedded derivatives are **designed to ensure that mark-to-market through the income statement cannot be avoided** by including - embedding - a derivative in another contract or financial instrument that is not marked- to market through the income statement.

➡**Example**: A **coal purchase contract** may include a clause that links the price of the coal to a pricing formula based on the prevailing electricity price or a related index at the date of delivery. The coal purchase contract, which qualifies for the executory contract* exemption, is described as the host contract, and the pricing formula is the embedded derivative. The pricing formula is an embedded derivative because it changes the price risk from the coal price to the electricity price.

➡**How It Arises**: An embedded derivative **can arise from deliberate financial engineering and intentional shifting** of certain risks between parties. Many embedded derivatives, however, arise inadvertently* through market practices and common contracting arrangements. Even purchase and sale contracts that qualify for executory contract* treatment may contain embedded derivatives. An embedded derivative causes modification to a contract's cash flow, based on changes in a specified variable.

QUESTION NO.2 What are Types of Commodity Swaps ?

There are two types of commodity swaps: fixed-floating or commodity-for-interest.

(a)Fixed-Floating Swaps: They are **just like the fixed-floating swaps** in the interest rate swap market with the exception that both indices are commodity based indices.
General market indices in the international commodities market with which many people would be familiar include the **S&P Goldman Sachs Commodities Index (S&PGSCI) and the Commodities Research Board Index (CRB).** These two indices place different weights on the various commodities so that,they will be used according to the swap agent's requirements.

(b)Commodity-for-Interest Swaps: They are **similar to the equity swap** in which a **total return** on the commodity

in question is exchanged for some **money market rate** (plus or minus a spread).

QUESTION NO.3 EXPLAIN cash settlement and physical settlement in derivatives contracts and their relative advantages and disadvantages?

(i) The **physical settlement** in case of derivative contracts means that underlying assets are **actually delivered** on the specified delivery date. In other words, traders will have to take delivery of the shares against position taken in the derivative contract.In case of **cash settlement**, the seller of the derivative contract **does not deliver** the underlying asset but transfers the Cash. It is similar to Index Futures,where delivery is impossible,since they have to be settled in cash.

(ii) The main advantage of **cash settlement** in derivative contract is **high liquidity** because of more derivative volume in cash segment. Also due to high liquidity,difference(**spreads)** between **bid -ask is narrowed.**Also if the stock is liquid, the **impact cost*** of bigger trades will be lower.

(iii)Due to cash settlement adverse move can be hedged. For example, the investors can take a covered short derivative position by selling the future while still holding the underlying security.

(iv)Cash settlement also, **facilitates the traders to do speculation**. The speculative trading may worry the regulators but it is also true that without speculative trading, it will not be possible for the derivative market to stay liquid.So, this leads to some arguments in favour of physical settlement in derivative contract. **One advantage of physical settlement** is that it is **not subject to manipulation** by both the parties to the derivative contract. This is so because the entire activity is monitored by the broker and the clearing exchange.

(v) However, one main **disadvantage of physical delivery** is that it is almost **impossible to short sell** a stock in the Indian Market.

➡Therefore, **in the end, it can be concluded that**, though, physical settlement in derivative contract does curb manipulation , it also affects the liquidity in the derivative segment.

QUESTION NO.4 EXPLAIN Co-location/ Proximity Hosting ?

➡The co-location or proximity hosting is a **facility which is offered by the stock exchanges to stock brokers** and data vendors whereby their trading or data -vending systems are allowed to be located **within or at close proximity to the premises** of the stock exchanges, and are allowed to connect to the trading platform of stock exchanges through direct and private network.➡Moreover, pursuant to the recommendations of the TAC of SEBI, stock exchanges **are advised to allow direct connectivity** between co-location facility of one recognized stock exchange and the colocation facility of other recognized stock exchanges. ➡Stock exchanges are also **advised to allow direct connectivity** between servers of a stock broker placed in colocation facility of a recognized stock exchange and servers of the same stock broker placed in colocation facility of a different recognized stock exchange. ➡This facility should be **available to all the co-located brokers**, who are desirous to avail such connectivity, in a fair and equitable manner.➡Further, in light of the public comments received and in consultation with Technical Advisory Committee (TAC) of SEBI and Secondary Market Advisory Committee (SMAC) of SEBI and in order to facilitate small and medium sized Members, who otherwise find it difficult to avail colocation facility, due to various reasons including but not limited to high cost, lack of expertise in maintenance and troubleshooting, etc. to avail co-location facility, SEBI has directed the stock exchanges to introduce **'Managed Co-location Services'**. Under this facility, space/rack in co-location facility shall be allotted to eligible vendors by the stock exchange along with provision for receiving market data for further dissemination* of the same to their client members and the facility.

10.PORTFOLIO MANAGEMENT

QUESTION NO.1 Interprete the CAPM and state its assumption?

➡The Capital Asset Pricing Model was **developed by Sharpe, Mossin and Linter in 1960**.

➡The model explains the **relationship between the expected return, non-diversifiable risk(beta) and the valuation of securities.**➡It is based on the premises that the **diversifiable risk of a security is eliminated** when

more and more securities are added to the portfolio. However, the **systematic risk(beta) cannot be diversified**. ➡The systematic risk can **be measured by beta**.➡The **expected return** of a security is :Expected return on security = Rf + Beta (Rm - Rf)➡The model shows that the expected return of a security consists of the **risk-free rate of interest and the risk premium**. ➡The CAPM, when plotted on the graph paper is known as the **Security Market Line (SML).**

➡**Relevant Assumptions of CAPM:(i)**The investor's objective is to **maximize the utility of terminal wealth***;**(ii)**Investors make choices on the **basis of risk and return**;**(iii)**Investors have **identical time horizon**;**(iv)**Investors have **homogeneous expectations** of risk and return;**(v)Information is freely** and simultaneously available to investors;**(vi)**There is risk-free asset, and investor can **borrow and lend** unlimited amounts at the risk-free rate;**(vii)**There are no **taxes, transaction costs, restrictions on short rates* or other market imperfections**;**(viii)Total asset** quantity is fixed, and all assets are marketable and divisible.Thus, CAPM provides a conceptual framework for **evaluating any investment decision with a goal of producing future returns.**

QUESTION NO.2 What are ASSET ALLOCATION STRATEGIES ?

There are four asset allocation strategies:

(a)Integrated Asset Allocation: Under this strategy, **capital market conditions and investor objectives and constraints are examined** and the allocation that best serves the investor's needs while incorporating the capital market forecast is determined.

(b)Strategic Asset Allocation: Under this strategy, **optimal portfolio mixes based on returns, risk, and co-variances** is generated using historical information and adjusted periodically to restore target allocation within the context of the investor's objectives and constraints.

(c)Tactical Asset Allocation: Under this strategy, **investor's risk tolerance is assumed constant** and the asset allocation is changed based on expectations about capital market conditions.

(d) Insured Asset Allocation: For investors prone to risk, the insured asset allocation is the ideal strategy to adopt. It involves **setting a base asset value** from which the portfolio **should not drop** from. If it drops, the investor takes the necessary action to avert the risk.Under this strategy, risk exposure for changing portfolio values (wealth) is adjusted; more value means more ability to take risk.

11. INTEREST RATE RISK MANAGEMENT

QUESTION NO.1 What do you mean by the term 'Cheapest to Deliver' in context of Interest Rate Futures?

➡The CTD is the bond that minimizes **difference between** the quoted Spot Price of bond and the Futures Settlement Price (adjusted by the conversion factor).

➡It is called CTD bond because it is the **least expensive bond** in the basket of deliverable bonds.

➡CTD bond is determined by the **difference between** cost of acquiring the bonds for delivery and the price received by delivering the acquired bond. This difference gives the profit / loss of the seller of the futures.

➡**Profit of seller of futures** = (Futures Settlement Price x Conversion factor) - Quoted Spot Price of Deliverable Bond

➡**Loss of Seller of futures** = Quoted Spot Price of deliverable bond - (Futures Settlement Price x Conversion factor)

➡That bond is chosen as CTD bond which **either maximizes the profit or minimizes the loss.**

APPENDIX [MEANING OF SOME DIFFICULT TERMS USED IN THIS BOOKLET]

Forward and Backward Linkages:For an industry, backward linkages are directed towards suppliers; while the forward linkages are directed towards consumers.

Crowd Psychology: Crowd psychology is the broad study of how individual behavior is impacted when large crowds group is together.

Designed Roulette Wheel: It is a game of chance in which a small ball is dropped onto a wheel that is spinning and the players guess in which hole it will finally stop.A type of Gambling.

Indicator: Leading means before event occurs,Lag means after the event occurs and Coincidental means exactly at the same time when event occurs.These indicators helps in doing research in economy activity.

Time series data: Time series forecasting helps us to predict future values based on previously observed values.

Skewness: It means to twist or distort/not straight.

Desynchronization: It is the relation that exists when things occur at unrelated times.Its opposite is synchronization which means the operation or activity of two or more things at the same time or rate.

Tranches(Trenching): They are pieces of debt or securities designed to divide risk or group characteristics in order to be marketable to different investors.

Non Recourse & Recourse: Recourse debt refers to an agreement where the lender can attach borrower assets, while non-recourse debt refers to an agreement where the lender cannot do so.

Homogeneity : If a group of things are homogeneous, they're all the same or similar.

Spread: It means diffenece between inflow and ouflow.

Foreclosure:It is a legal process in which a lender attempts to recover the balance of a loan from a borrower who has stopped making payments to the lender by forcing the sale of the asset used as the collateral for the loan.

Credit Enhancer: The process of reducing credit risk by requiring collateral, insurance, or other agreements to provide the lender with reassurance that it will be compensated if the borrower defaulted.

Trade Sale:A trade sale is the sale of a business, or part of the business, to another business.

Factoring: It is a financial service in which the business entity sells its bill receivables to a third party.

Host country: When USA Company invest in india,India is termed as Host Country.

Repatriation: The sending of money back to one's own country.

Lehman Brothers: It was a company which still holds the record for the largest bankruptcy in US history.

Sovereign Debt Crisis:A sovereign debt crisis is when a country is unable to pay its loan.

Willful Defaulter:A willful defaulter is an entity or a person that has not paid the loan back despite the ability to repay it.

Inadvertently:without intention; accidentally.

Executory Contract: An executory contract is a contract made by two parties in which the terms are set to be fulfilled at a later date.

Terminal Wealth: Value of an asset at the end of its useful life.

Mezzanine Finance:It is a blend or hybrid of long term debt and equity share.

Modus Operandi:a particular way or method of doing something.

NO Restrictions on short rates: It means an entity can borrow money for short period of time .

Congeneric merger: An example of a congeneric merger is when banking giant Citicorp merged with financial services company Travelers Group in 1998. In a deal valued at $70 billion, the two companies joined forces to create Citigroup Inc. While both companies were in the financial services industry, they had different product lines.

Disarming:to deprive of a weapon

Reverse Merger:It is also defined as “When an acquiring company is weaker than the target company.

Predator:a person who ruthlessly exploits others.

Organic growth: It is the growth a company achieves by increasing output and enhancing sales internally.

Open:Here open means that in this market there is no fixed maturity.

Majors:In India currency futures are available in following currencies only :US Dollars (USD), Euro (EUR), Great Britain Pound (GBP) and Japanese Yen (JPY).

Impact cost : Impact cost is the cost that a buyer or seller of stocks incurs while executing a transaction.

Wreck:destroy

Dissemination:the action or fact of spreading something, especially information, widely.

Full capital convertibility :In layman's terms, full capital account convertibility allows local currency to be exchanged for foreign currency without any restriction on the amount.

CEDEL : Centrale de Livraison de Valeurs Mobilières. It is a centralized clearing system of EUROPE.

OTC: Over-the-counter (OTC) refers to such agrrement which are not listed in stock market.As oppose to this, there is a an exchange traded product that is traded on an organized exchange.

Indexation: It is the process that takes into account inflation from the time you bought the asset to the time you sell it.

Market Maker: a dealer in securities or other assets who undertakes to buy or sell at specified prices at all times.

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