(1)

Q P Code :- 54617

M0133/M0285 EQUITY & DEBT MARKET   ANSWER KEY 1

BMS: FINANCE   Q.P.CODE

[Time: 2.5 Hours]   [Marks: 75]

Q1A.

1. Stock exchange
2. Money market
3. Equity share
4. RBI
5. Treasury bill
6. Mortgage loan, Guarantees loan
7. Fixed price
8. Repo rate
9. Cash reserve ratio
10. CAPM, Earnings based, Dividend based

Q1B.

True 1, 7, 8, 9
False 2 ,3 , 4, 5, 6, 10

Q2.A. RBI

Ans. A few of the Following points to be covered with appropriate explanation.

RBI – Reserve bank of India , Central bank of India.
It started functioning from 1st April 1935

TRADITIONAL FUNCTIONS
- Issue of currency notes
- Banker to other banks
- Banker to government
- Exchange rate management
- Credit control function

PROMOTIONAL/DEVELOPMENTAL FUNCTIONS
- Development of the financial system
- Development of agriculture
- Provision of industrial finance
- Provision of training
- Collection of data and publication of reports
- Promotion of Export through refinance
- Encouragement of financial literacy

SUPERVISORY FUNCTIONS
- Granting license to banks
- Bank inspection
- CoOntrol over NBFI
- Implementation of various schemes

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Q2.B. **Ans.Following points to be covered with appropriate explanation.**

Governement securities are :

- It is a tradable instrument issued by central government or the state govt.
- They are generally short term in nature and carry no risk of default.
- They are usually not openly tradable and hence not eligible as SLR security.
- Eg. Treasury bills, NSC etc.

Benefits:

- Fair return & safety
- Demat form
- Wide range of maturity from less than 91 days to 30 years
- Easily sold& settled
- Used as collateral to borrow funds in repo market
- Pricing

Instruments

Treasury bills, Cash management bills, Dated government security, State development loan

Q2.P.

Ans.Following points to be covered with appropriate explanation.

- Financial market consists of Capital & Money market
- Money market consists of organized & unorganized market with examples
- Capital market is divided into
- Industrial securities market ie. Primary & Secondary
- Government securities market
- Long term loans market ie. Term loan, Mortgage loan & Financial Guarantees loan

Q2.Q. **Ans.Following points to be covered with appropriate explanation.**

A merchant banker is defined as an organization that acts as an intermediary between the issuers and the ultimate purchaser of securities in the primary market.
Classified as Fee based merchant banking&Fund based merchant banking
Services offered by merchant bankers are:

- Consultancy services
- Government consent
- Project planning and feasibility study
- Raising financial resources
- Issue management
- Portfolio management
- Advice on expansion program
- Loan syndication
- Corporate restructuring
- Revival of sick units

Q3.A. **Ans.Following points to be covered with appropriate explanation.**

Primary market deals with

- It deals with issue of new securities.
- A company raises funds through IPO for various purposes.
- Transaction happens between issuer and investors.
- It generally happens through merchant bankers and underwriters.
- Important for capital formation.

Methods of raising funds in the primary market are

- Public issue
- Offer for sale or bought out deal
- Private placement
- Rights issue
- Electronic IPO

Q3.B. **Ans.Following points to be covered with appropriate explanation.**

Fixed price

- Security pricing is done in advance and is made known to the potential investors.
- Price band not applicable.
- Demand for shares is known only after the closure of the issue period.
- Applicants to pay the amount in advance at the time of application.
- Not very popular in developed countries.

Book Building

- Pricing not done in advance.
- Price band is applicable at the rate of 20% of floor price.
- Demand for shares at various prices as per various investors are readily available online.
- Only 10% of advance payment need to be made at the time of application by QIB's and 100% for other investors.
- Applicable globally

Q3.P. RBI has taken several measures to strengthen the Indian Money Market on the basis of reports submitted by Narshimhan Committee. The following are the measures or reforms introduced by RBI in the post-reform period:

1) Deregulation of interest rates
2) Reduction in CRR
3) Reduction in SLR
4) Introduction of new money market instruments
5) Introduction of Repo and Reverse Repo
6) Remittance of Stamp duty
7) Minimum Lock in Period
8) Recovery of Debts
9) Regulation of NBFCs
10) Forming of Clearing Corporation of India Ltd. (CCIL)

(Minimum 7 points required. If explanation is correct 1 mark for each point)

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Q3.Q. **Following points to be covered with appropriate explanation.**

Bonds are debt instruments issued by bond issuers to bond holders.
A bond is a debt security under which the bond issuer owes the bond holder a debt including interest or coupon payments and or a future repayment of the principal on the maturity date.
Features of bonds are Coupon ratePrincipal, Maturity, Rating, Issuers, safety
Types are:
Based on issuer
Based on maturity period
Based on coupon
Based on convertibility
Based on Redemption

Q4.A. **Ans.Following points to be covered with appropriate explanation.**

- Nature
- Status (Creditors & owners)
- Issuer
- Profit sharing
- Earnings
- Claim
- Trading (OTC & Stock exchange)

Q4.B. **Ans.Following points to be covered with appropriate explanation.**

IPO is a type of public offering in which shares of a company are sold for the first time to perspective investors comprising of retail, institutional clients, employees etc. It is a way to raise funds for future expansion and projects.
Steps in an IPO

- IPO approval from board.
- Selecting an investment banker.
- Letter of intent.
- Syndicate of underwriters.
- SEBI filing.
- Filing of prospectus with registrar of companies,
- Marketing of IPO
- Underwriting agreement
- Statutory announcement
- Collection and processing of applications
- Allotment of shares
- Listing of issue.

Q4. P.

Year	Interest	PVIF@16%	PV CI
1	8		6.896
2	8		5.944
3	10		6.41
4	10		5.52
5	12		5.712
6	12		4.92

7	12+100		39.648

PV IS Rs.75.05/-

Q4.Q. $YTM = \frac{\underline{I + (RV - MP / N)}}{RV + MP / 2} * 100$

Bond A = 17.65%

Bond B = 20.84%

Bond B is better

Q5.A. RM = Total Earnings / Total cost *100

Total Earnings = Total dividend + Total capital appreciation

= 291/1105 *100 = 26.33%

CAPM , KE = RF + B(RM-RF)

C/O A = 23.86%

C/O B = 22.63%

C/O C = 20.17%

C/O D = 26.21%

Q5.B. KE = RF + B (RM – RF) = 17%

D1 = D0(1+G) = 4.32

V = D1/KE-G = Rs.48/-

MP< Value of the share, Buy.

Q5. Short notes.

1. Preference shares

<u>Ans.Following points to be covered with appropriate explanation.</u>

- PS are those are those shares which enjoy preference rights over equity capital in terms of fixed annual dividends and return of capital in the event of winding up of the company.
- A company cannot issue irredeemable preference shares.
- Low capital appreciation.
- Cannot be traded on share market with exceptions.
- Less risk compared to equity shares.
- Normally issued for face value of Rs. 100.
- Not entitled for bonus shares and do not have voting rights.
- Types are cumulative, redemmable, convertible , participating and their opposites.

2. **<u>Ans. A few of the Following points to be covered with appropriate explanation.</u>**

ESOP refers to employee stock option plan. It is a scheme undertaken by the companies to attract best talents of employees.

ESOP normally focuses on general employees of the company who are working on full tie basis.

<u>Types of ESOP</u>

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ESOS (Employee stock option scheme)
Share are allotted to employees.
Acquire shares at predetermined price at future date.
Price lower than current market price.
Can be sold after lock in period.

ESPP (Employee stock purchase plan)
Share are allotted to employees.
Acquire shares at predetermined price instantly.
Price lower than current market price.
Can be sold after lock in period till which the employee has to continue with the company.

SAR (Share appreciation rights)
Share are not allotted to employees.
They are paid based on the appreciation in the value of shares between two specific dates which acts as incentive or performance bonus.

3. Equity culture & issues in India
Ans.Following points to be covered with appropriate explanation.

Measures to develop equity culture in India
- SEBI
- Professional approach
- Guarantee and simplicity
- Market based pricing
- Disclosure and transparency
- Investor education
- Companies act

Development of equity culture in India
- Increase in working size of Indian population.
- Provision for tax incentives.
- Publicity & advertisement.
- Additional source of income.
- Capital appreciation, growth & liquidity.
- Increase in no. of registered companies

4. A stock exchange is an association, organisation or body of individuals which is established for the purpose of for assisting the business of buying and selling of securities.

A Stock exchange is an entity or platform that provides services to stock brokers and traders for buying and selling of shares, bonds and other securities.

They provide a platform for free transferability of shares It also provides facilities for issue & redemption of shares & securities and other financial instruments, payment of dividend, bonus & rights issue.

Assists in raising funds
Facilitates listing of shares
Facilitates trading of shares
Generates employment

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Facilitates Capital formation
Stimulates Industrial development
Facilitates Regional development
Provides revenue to government

5. **Objectives of SEBI (2 marks)**

1) To protect the interest of investors
2) To bring professionalism in the working of intermediaries
3) To create good financial climate

Powers over Stock Exchange (5 marks)

1) To call periodical returns from recognised stock exchanges
2) To call any information or explanation from recognised stock exchange or its members
3) To order enquiries relating to affairs of stock exchanges or its members
4) To grant approval of Bye-laws of recognised stock exchanges
5) To make and amend any bye-laws
6) To control and to regulate stock exchanges

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