PONDICHERRY UNIVERSITY

MBA DEGREE EXAMINATION JANUARY/FEBRUARY 2023

Third Semester

FINANCIAL MARKETS AND SERVICES – (Answer Key)

(2021-22 Regulation)

Part A (6*5 = 30 Marks)

1. Define financial engineering.

Financial engineering is the application of mathematical methods to solve financial problems. Financial engineering encompasses a broad, multidisciplinary field of study and practice that, essentially, applies an engineering approach and methodology to the world of finance. It integrates and utilizes information obtained from different fields, such as economics, mathematics, computer science, and financial theory. Much of financial engineering consists of converting financial theories into practical applications in the financial world.

Uses of Financial Engineering

Financial engineering is used across a broad range of tasks in the financial world. Some of the areas where it is most commonly applied are the following:

Corporate Finance

Arbitrage Trading

Technology and Algorithmic Finance

Risk Management and Analytics

Pricing of Options and other Financial Derivatives

Behavioral Finance

Creation of Structured Financial Products and Customized Financial Instruments

Quantitative Portfolio Management

Credit Risk and Credit Management

Importance of Financial Engineering

- Financial engineering is the use of mathematical techniques to solve financial problems.
- Financial engineers test and issue new investment tools and methods of analysis.
- They work with insurance companies, asset management firms, hedge funds, and banks.

- Financial engineering led to an explosion in derivatives trading and speculation in the financial markets.
- It has revolutionized financial markets, but it also played a role in the 2008 financial crisis.

2. List out types of securities.

Securities like stocks and bonds are financial instruments that hold value and can be bought, sold, and traded. Financial securities are divided into four categories—debt securities, equity securities, hybrid securities (which have characteristics of both debt and equity securities), and derivative securities.

a. Debt Securities

Debt securities—like corporate bonds, government bonds, and certificates of deposit—are essentially loans. Owners of debt securities lend a certain amount of money (the principal) to another party. That party is then obligated to pay pre-determined interest payments to the owner at regular intervals per the terms specified in their agreement until the instrument matures, at which time the debtor must pay back the security owner in the amount of the principal.

b. Equity Securities

Equity securities indicate partial ownership of an entity—often a business. The most common example of an equity security is a share of a company's stock. Shares of mutual funds are also considered equity securities, as are shares of certain ETFs (those that do not include debt securities like bonds).

While individuals purchase debt securities in order to receive periodic payments in exchange for the temporary use of their money, individuals usually purchase equity securities as investments for the purpose of realizing capital gains over time. An equity security is an asset, so if its value increases, the party that holds it can sell it for a profit.

Equity securities also come with greater risk, however. While a company or entity's potential value is limitless, that value could also change in a negative direction, resulting in capital losses for shareholders. If a business goes bankrupt, its shareholders are only entitled to their portion of whatever value remains after the business has paid all of its creditors and fulfilled all of its obligations per the terms of the bankruptcy.

c. **Hybrid Securities**

Hybrid securities behave like debt securities in some ways and like equity securities in other ways. The most common type of hybrid security is a convertible bond. These behave like bonds in that they involve regular payments, but they differ from bonds in that they can also be converted into a specific number of shares of a stock at the holder's discretion. Another example is an equity warrant, which an option is issued directly by an entity to its shareholders to buy or sell a security for a specific price on or before a specific date.

d. **Derivative Securities**

A derivative is a security whose value is based on a specific asset or group of assets (like a stock or commodity). A derivative usually takes the form of a contract between two parties relating to the purchase or sale of a specific asset or pool of assets. Derivatives are often used by individuals and institutions to mitigate risk, but they can also be used speculatively by investors to make money. One common derivative is a futures contract, which is an agreement to buy or sell an asset at a pre-determined future date for a specific price.

3. Explain the concept of mutual funds?

A mutual fund is a pool of money managed by a professional fund manager. It is a trust that collects money from a number of investors who share a common investment objective and invests the same in equities, bonds, money market instruments and/or other securities. And the income/gains generated from this collective investment are distributed proportionately amongst the investors after deducting applicable expenses and levies, by calculating a scheme's "Net Asset Value" or NAV. Simply put, the money pooled in by a large number of investors is what makes up a Mutual Fund.

Types of mutual fund:

Open-ended funds are mutual funds that allow you to invest and redeem investments at any time, i.e. they are perpetual in nature. They are liquid in nature and don't come with a specific investment period.

Close-ended schemes have a fixed maturity date. You can only invest at the time of the new fund offer and redemption can only be done on maturity. You cannot purchase the units of a close-ended mutual fund whenever you please.

4. What is meant by insider trading?

Insider trading refers to the practice of purchasing or selling a publicly-traded company's securities while in possession of material information that is not yet public information. Material information refers to any and all information that may result in a substantial impact on the decision of an investor regarding whether to buy or sell the security.

By non-public information, we mean that the information is not legally out in the public domain and that only a handful of people directly related to the information possessed. An example of an insider may be a corporate executive or someone in government who has access to an economic report before it is publicly released.

Insider trading can be broken down into two general categories: (1) buying securities prior to the announcement of good news, such as unexpectedly high quarterly earnings, or a promising merger; or (2) selling securities prior the announcement of bad news, such as a decline in quarterly revenue.

5. Role of OTCE.

The Over-The-Counter Exchange of India (OTCEI) is an Indian electronic stock exchange composed of small- and mid-cap companies.

The purpose of the OTCEI is for smaller companies to raise capital, which they cannot do at the national exchanges due to their inability to meet the exchange requirements.

The OTCEI implements specific capitalization rules that make it suited for small- to medium-sized companies while preventing larger companies from being listed.

The key players in the OTCEI include brokers, market makers, custodians, and transfer agents.

The OTCEI is based in Mumbai, India, and operates solely over a computer network. The exchange is recognized by India's Securities Contract Regulation Act, meaning all listed stocks on the OTCEI benefit equally as other listed securities on other exchanges in India.

The exchange was established in 1990 to provide investors and companies with an additional way to trade and issue securities. It arose primarily from small companies in India finding it difficult to raise capital through mainstream national stock exchanges because they could not fulfill the stringent requirements to be listed on them.

The OTCEI has rules that are not as rigid as the national exchanges, allowing small companies to gain access to the capital they need to grow. The objective is that once they grow to a certain level and are able to meet the requirements to be listed on the national stock exchanges, they will make the switch over and leave the OTCEI behind.

Thanks to advances in technology that have yielded improvements in electronic trading platforms, the differences between traditional exchanges and over-the-counter (OTC) networks are no longer vast, greatly benefiting the small- and medium-sized companies.

Features of the Over-The-Counter Exchange of India (OTCEI)

- The OTCEI has some special features that make it a unique exchange in India as well as a growth catalyst for small- to medium-sized companies.
- Stocks that are listed on other exchanges will not be listed on the OTCEI and, conversely, stocks listed on the OTCEI will not be listed on other exchanges.

6. List the types of equity funds.

Equity funds are those mutual fund schemes that primarily invest in the equity markets. As per the current SEBI Mutual Fund categorisation, equity mutual funds are mandated to invest at least 65% of their total assets in equity- and equity-related instruments. These funds have the potential to generate returns by investing in the stocks of companies across all market capitalisations.

Types of Equity Mutual Funds

Equity funds can be categorised based on the investment mandate and primary investment avenues. Knowing them can help you optimise your investments.

Here are the different types of equity mutual funds available to an individual:

I. Based on market capitalisation

II. Based on Investment Style

III. Based on tax benefits

7. What are the investor objectives in investing funds in stock market?

An investment objective is a set of goals that determines an investor's financial portfolio. A financial advisor determines the optimal strategy for achieving the client's goals using an investment objective.

An investor's risk tolerance and time horizon help in determining an investment objective. Commonly based on one of four strategies that include income, growth and income, growth, or trading, an individual's investment objective clarifies investment ideas to help achieve an individual's financial goals

In addition to an individual’s time horizon and risk profile, other factors that influence an individual’s investment decisions include income, capital gains tax, dividends tax, commission and fees for actively managed portfolios, and total wealth, which may include assets like Social Security benefits, expected inheritance, and pension value.

8. Explain in detail primary and secondary objectives of investment?

Safety, growth, and income are the primary objectives of an investor. Every investor has to pick an appropriate mix of these three factors. The appropriate mix for you will change over time as your life circumstances and needs change. Liquidity and Tax Savings are the secondary objectives of an investor. An investor must understand their goal before making an investment decision. Factors affecting investments include your goals, age, lifestyle, risk appetite, and returns expected.

9. What are blue chip shares? Give examples

Blue chip stocks are shares of very large and well-recognised companies with a long history of sound financial performance. These stocks are known to have capabilities to endure tough market conditions and give high returns in good market conditions.

The blue-chip stocks to buy are stocks issued by financially sound and fundamentally strong blue chip companies with humongous market capitalisation and enviable market reputation. Blue Chip companies refer to equity shares of companies with larger market capitalisation.

India's Most Profitable Bluechip Stocks.

- 1 Reliance Industries.
- 2 Oil & Natural Gas Corporation (ONGC)
- 3 Tata Steel.
- 4 Tata Consultancy Services.
- 5 HDFC Bank.
- 6 Indian Oil Corporation..
- 7 Infosys.

10. What is meant by arbitrage?

Arbitrage is the process of simultaneous buying and selling of an asset from different platforms, exchanges or locations to cash in on the price difference (usually small in percentage terms). While getting into an arbitrage trade, the quantity of the underlying asset bought and sold should be the same.

With shares, for example, arbitrage can occur when a stock is listed on exchanges in two different countries. Because of discrepancies between the foreign exchange rates in each country, the price of the share can differ between the two exchanges.

There are several types of arbitrage, including pure arbitrage, merger arbitrage, and convertible arbitrage. Global macro is another investment strategy related to arbitrage, but it's considered a different approach because it refers to investing in economic changes between countries.

PART B (5*10 = 50 Marks)

11. Outline the code of conduct for underwriters prescribed by SEBI.

As per regulation 2(f) of the Securities and Exchange Board of India (Underwriters) Rules, 1993 an underwriter is an individual who has the primary responsibility in underwriting the issue related to shares or securities.

As per the regulations no organisation or person is required to carry out the works related to underwriting an issue without holding a valid certificate from SEBI. Hence registration of underwriters with SEBI is mandatory. Such provision for registration of underwriters with SEBI is present under regulation 3(1) of the above regulations.

However, if the company or the organisation has applied for the certificate of registration or has a pending certificate of registration, then they can carry out the above activities. This is present under regulation 3 of the above regulations. Such application has to be made in compliance with Regulation 12 of the above regulations.

According to regulation 3(2), stock brokers or merchant bankers do not require a separate certificate of registration for carrying out the activities related to underwriting a specific issue. Hence from the above it is clear that Registration of Underwriters with SEBI is a mandatory step required to be considered for all organisations carrying out activities related to underwriting a specific issue. However, if the organisation is carrying out activities related to stock brokering or merchant banking, then such certificate or registration would not be required.

Procedure for Registration of Underwriters with SEBI

The following procedure has to be considered for registration of underwriters with SEBI:

The applicant has to make an application in Form A. Such application has to be made to the board. After this the board would review the application and see if the requirements of the applicant confirm with the requirements for underwriters.

If more information or documentation is required, then the board would notify the applicant related to requirement of more information. The applicant under registration of underwriters with SEBI would also be given an opportunity to appear before the board for the application.

If the application does not confirm with the above requirements then such application would be rejected. These requirements would be met if the above eligibility criterion is fulfilled by the applicant. The capital adequacy requirement has to be considered by the applicant.

Eligibility Criteria for Registration of Underwriters with SEBI

The following eligibility criterion has to be satisfied for registration of underwriters with SEBI:

a) Payment of Fees

The applicant has to pay the requisite fee for registration of underwriters with SEBI. Such requirement is present under regulation 4(c) of the Securities and Exchange Board of India (Underwriters) Rules, 1993. The amount of Non-refundable fees to be paid along with the Application for registration shall be Rs. 25000/-. Every underwriter shall pay fees of thirteen lakh thirty-three thousand & three hundred rupees at the time of grant of Certificate of initial registration.

b) Agreement with Corporate Body

The underwriter has to ensure that there is a prior agreement or a contract with a corporate body or the organisation that the applicant is going to carry out underwriting services with respect to the particular issue at hand. Such requirement is present under regulation 4(b) of the Securities and Exchange Board of India (Underwriters) Rules, 1993.

c) Compliance with Rules

The applicant has to ensure that he abides by the rules which are provided by the SEBI and other regulatory authorities. Such requirement is present under regulation 4(d) of the Securities and Exchange Board of India (Underwriters) Rules, 1993.

d) Change of Status

The applicant has to ensure if he is granted such registration, prior consent would be taken from the board members and the shareholders. Such requirement is present under regulation 4(a) of the Securities and Exchange Board of India (Underwriters) Rules, 1993.

e) Infrastructure of Office

For registration of underwriters with SEBI, there is requirement of proper infrastructure facilities present in the office. This would include the office space, presence of adequate manpower and employees to carry out all the responsibilities. This would be in accordance with regulation 6(a) of the above regulations.

f) Experience of Key Management Executives

The applicant has to have some form of past experience relating to underwriting the issue. The directors or the shareholders have to have minimum two years related to underwriting a specific issue. This would be in accordance with regulation 6(b) of the above regulations.

g) Capital Adequacy Requirement

As per regulation 6(d) of the above regulations the applicant has to ensure to suffice the requirements related to capital adequacy. The capital adequacy must be not less than the net worth of Rs. 20 Lakh.

If a stockbroker carries out activities related to underwriting a specific issue, then the capital adequacy requirements have to be fulfilled as mentioned by the stock exchange.

If a merchant banker carries out activities related to underwriting a specific issue, then the capital adequacy requirements have to be fulfilled as per regulation 7 of the Securities and Exchange Board of India (Merchant Banker) Regulations 1992.

h) No Conviction of Key Management Executives

The key management executives of the company should not have any form of criminal convictions or be undischarged as insolvent.

i) Pass Fit and Proper Person

The key management executives have to pass the requirements of a fit and proper person test. Such requirements would be conducted by the SEBI from time to time.

12. What are the salient features of insider regulation 2015?

Insider has been defined to mean any person who is (i) a connected person; or (ii) in possession of or having access to unpublished price-sensitive information ("UPSI"). Every connected person is an 'insider' under the Regulations.

Insider trading is the act of purchasing, selling, underwriting, or agreeing to underwrite the securities or stocks of an organization by key executives/personnel of the company who have access to UPSI - Unpublished Price Sensitive Information regarding the company.

The regulations provide that the communication or dissemination of any confidential information, by an insider, is prohibited. The information communicated or disseminated must be unauthorized. The information can be used by the person himself or any other person on his behalf.

The main features of insider trading thus include: (1) The insider uses the non – public information for his own advantage either by avoiding losses or making profits. (2) Insider trading puts the shareholders of the company at a disadvantageous position. (3) The information so provided should be material.

The parties involved in insider trading can be categorized into three groups: (1) the company whose securities are traded, (2) the insider (tipper) who possesses privileged information about the company and disclose the private information, and (3) the investors (tippee), who are interested in the company's securities.

13. Explain the rating methodology used by the rating agencies for manufacturing with financial services companies.

Rating Methodology — the method used by an underwriter when calculating premiums. Principal methods are manual, experience (retrospective or prospective), burning cost, or judgment.

Methodology of Credit Rating. The process of credit rating begins with the prospective issuer approaching the rating agency for evaluation. The experts in analyzing banks should be given a free hand and they will collect data and informant and will investigate the business strength and weaknesses in detail.

At the time of calculating the rating, credit rating agencies take into consideration several factors like the financial statements, level and type of debt, lending and borrowing history, ability to repay the debt, and past debts of the entity before rating them.

Best's Credit Rating Methodology (BCRM) is a comprehensive overview of the credit rating process, which consists of quantitative and qualitative evaluations of balance sheet strength, operating performance, business profile, and enterprise risk management.

Popular Types of Rating Scales

- Graphic rating scale.
- Numerical rating scale.
- Descriptive rating scale.
- Comparative rating scale.

14. Discuss on various investment avenues available for investors in India.

The most popular ones are stocks or equities, real estates, fixed deposits, gold and real estate. Mutual funds, Public Provident Fund, government bonds, corporate bonds, Exchange Traded Fund, and National Pension Scheme are few other well-known investment options.

A process of acquiring an asset is called investment. There are different types of investments available in the market. Not all investments suit all investors. Each of these has varying levels of risks. Hence investors have to choose those types of investments that best suit their financial plan and goals.

Investment is a process of acquiring an asset with an aim to generate money from it. Generating income from an asset can be through regular income or appreciation of the asset. Appreciation is the increase in the value of the asset over time.

Following are the types of investment available in India:

- Stocks.
- Certificate of Deposit.
- Bonds.
- Real Estate.
- Fixed Diposits.

- Mutual Funds.
- Public Provident Fund (PPF)
- National Pension System (NPS)

Types of investments

There are different types of investment in the market, and we have bifurcated them into three main categories. They are

- Fixed income investments: These investments give guaranteed returns in the form of interest. These are low-risk investments. Below is a list of few of the best fixed-income investments.
- Market linked investments: Market linked investments are those investments that do not guarantee returns and their returns are dependent on the market movements. These are considered high-risk investments. However, the returns from these investments are also high when the market rallies. Below is the list of the best market-linked investment options.
- Other investment: Investments that do not come under fixed income or market-linked investments are other investments. These are also called alternative investments. Below is the list of the most popular alternative investment products.

15.Explain the CAPM theory and its validity in stock market.

The Capital Asset Pricing Model (CAPM) is a model that describes the relationship between the expected return and risk of investing in a security. It shows that the expected return on a security is equal to the risk-free return plus a risk premium, which is based on the beta of that security.

To calculate the value of a stock using CAPM, multiply the volatility, known as "beta," by the additional compensation for incurring risk, known as the "Market Risk Premium," then add the risk-free rate to that value.

The major drawback of CAPM is it is difficult to determine a beta. This model of return calculation requires investors to calculate a beta value that reflects the security being invested in. It can be difficult and time-consuming to calculate an accurate beta value. In most cases, a proxy value for beta is used.

16. What is market correction? Suggest the implications of correction.

A correction is a sustained decline in the value of a market index or the price of an individual asset. A correction is generally agreed to be a 10% to 20% drop in value from a recent peak. For the market, corrections can help to readjust and recalibrate asset valuations that may have become unsustainably high. For investors, corrections can provide both the opportunity to take advantage of discounted asset prices as well as to learn valuable lessons on how rapidly market environments can change.

How to Prepare For a Market Correction

Sell profitable investments.

Focus on asset allocation

Make smart trading decisions.

Remember your investing goals.

Why Does Share Market Correction Occur?

Market corrections are an indicator of a healthy stock market as a continuous rise in the stock market might have adverse implications for an economy. Rising share prices are synonymous with an economic boom; a persistent increase in the values of benchmark indices might thus lead to high levels of inflation, affecting resident individuals, particularly low-income groups. Market corrections also restrict an asset from becoming overinflated, thereby preventing an asset bubble.

Though unpredictable, market correction also encourages investments among long term traders, as they can enjoy wealth accumulation through capital gains when the market recovers.

Such a fall in share prices is significantly different from bear markets, as market corrections allow an economy to grow even further upon readjustment of the prices of securities as per their real value.

How to Identify a Stock Market Correction?

Financial analysts and investors take the assistance of several charting methods to help them predict and track market corrections. It is quite challenging to analyse when such a correction takes place as the reasons behind it range from large-scale economic changes to financial issues in the management strategy of a single organisation.

A change in the stock market rates occurring in the course of a trading session is unhealthy for short term traders who could face significant financial losses during such periods.

As it is difficult to predict market correction, it is inconvenient even for the experts to estimate the starting and ending periods of such a decline in stock prices.

17. Discuss role of new issues in industrial financing.

A new issue refers to a stock or bond offering that is made for the first time. Most new issues come from privately held companies that become public, presenting investors with new opportunities.

New issue offering, underwriting, and distribution are the three primary functions of these markets.

The new issue market plays the role in providing both private and public issues. The new issue market is the place where new and fresh stocks or bonds are offered to the general public for the first time.

The main Roles of the New Issue Market in financing companies are given below:

The analysis of the role of the new issue market in financing companies can be undertaken by the study of the statistics of the annual volume of new issues. The data may be broken down in various ways, for example, according to the type of security issued, the kind of organisation making the issue, the method of flotation of issue and so on.

The Reserve Bank of India, for instance, has been following this method in its regular studies of capital issues in the private corporate sector.

(i) Its first shortcoming is that the technique to/aggregate the amount of all prospectus and right issues, to arrive at the new issues made in a/particular year does not reveal the true picture, as the entire sum is not necessarily raised by the issuing companies from the investing public in the same year because they are collected through various calls which may be spread over five years. This, of course, is a minor point.

(ii) The method presents absolute figures, unrelated to the use to which these funds are put.

(iii) The method leads to the treatment of the New Issue Market in isolation from the rest of the/capital market and consequently to a distorted view as to its real functions.

(iv) Further, it does not disclose as to what kind and size/of firms are obtaining funds, nor at what cost they are doing so, and, therefore, gives no clue as to efficiency. To explore such questions, obviously, a different approach is necessary.

18. Explain the mechanism of factoring.

The word 'Factoring' is derived from Latin word 'Factor' which denotes 'doer'. The definition of the word factor is "One that lends money to producers and dealers on the security of accounts receivables".

Factoring means a financial transaction which involves a firm selling its invoices of accounts receivables to a third party, which is also known as a 'Factor'. Such transfer is generally made at a discount and the firm is provided with the instant cash for financing its ongoing business.

Definition of Factoring

Alam Calpin has defined the term as :

"Factoring is a system designated to eliminate payment risk in overseas sales and ensure that the seller receives prompt settlements".

A factor is a financial institution which engages in the work of collecting account receivables of a business. Such financial institution takes the credit risk attached to such account. Factoring denotes selling of the receivables and it may be with recourse or without recourse. With this facility, a business is able to get quick cash for its operations. Following are the main elements of a factoring transaction :

The Factor

The Client (Seller)

The Customer (Buyer)

The contract between the two parties determines these elements. Such contract is drawn for a fixed period of time and is generally renewable. The contract may also be cancelled by giving due notice.

Process / Mechanism of Factoring

The basic service provided by a factor is the collection of proceeds. The factor offers its services as an intermediary between the buyer and the seller. Once a factor receives the payment, the firm's account is credited after making deduction for the services provided by the factor.

The client orders goods or services on credit. Such services or goods are delivered along with the invoice.

In a factoring arrangement, there are three parties directly involved namely; the one who sells the invoice (client), the debtor (customer of the seller), and the factor (financial organization). Seller of the product or service provider who originates the invoice is called Client and generally is a business firm.

Debtors or customers of the client are the recipient of the invoice for the goods or services rendered. They promise to pay the balance within the agreed payment terms. They owe the money for the value of goods and services bought from the seller. Assignee (the factoring company) or factor is the service provider who purchases the invoice and gives advance payment to business firm.

19.Outline the securities contract and regulation Act, 1945.

An Act to prevent undesirable transactions in securities by regulating the business of dealing therein, by providing for certain other matters connected therewith.

The objectives of these Acts are to prevent undesirable transactions in securities by regulating the business of dealing therein, to provide for the establishment of the Securities and Exchange Board of India to protect the interests of investors in securities and to promote the development of, and to regulate.

The Securities Contracts (Regulation) Act, 1956. It extends to the whole of India. It shall come into force on such date2 as the Central Government may, by notification in the Official Gazette, appoint.

“contract” means a contract for or relating to the purchase or sale of securities;

“corporatisation” means the succession of a recognised stock exchange, being a body of individuals or a society registered under the Societies Registration Act, 1860 (21 of 1860), by another stock exchange, being a company incorporated for the purpose of assisting, regulating or controlling the business of buying, selling or dealing in securities carried on by such individuals or society;

“demutualisation” means the segregation of ownership and management from the trading rights of the members of a recognised stock exchange in accordance with a scheme approved by the Securities and Exchange Board of India;

“Derivative” includes (A) A security derived from a debt instrument, share, loan, whether secured or unsecured, risk instrument or contract for differences or any other form of security;

(B) A contract which derives its value from the prices, or index of prices, of underlying securities;

"Government security" means a security created and issued, whether before or after the commencement of this Act, by the Central Government or a State Government for the purpose of raising a public loan and having one of the forms specified in clause (2) of section 2 of the Public Debt Act, 1944 (18 of 1944);

"member" means a member of a recognised stock exchange;

"option in securities" means a contract for the purchase or sale of a right to buy or sell, or a right to buy and sell, securities in future, and includes a teji, a mandi, a teji mandi, a galli, a put, a call or a put and call in securities;

"prescribed" means prescribed by rules made under this Act; (f) "recognised stock exchange" means a stock exchange which is for the time being recognised by the Central Government under section 4;

"securities" include— (i) shares, scrips, stocks, bonds, debentures, debenture stock or other marketable securities of a like nature in or of any incorporated company or other body corporate;

"stock exchange" means any body of individuals, whether incorporated or not, constituted before corporatisation and demutualisation under sections 4A and 4B, or (b) a body corporate incorporated under the Companies Act, 1956 (1 of 1956) whether under a scheme of corporatisation and demutualisation or otherwise, for the purpose of assisting, regulating or controlling the business of buying, selling or dealing in securities

20.Identify the major players in leasing business.

Lease finance can be said to be a "contract between lessor and lessee whereby the former acquires the equipment/goods/plant as required and specified by the lessee and passes on the goods to the lessee for use for a specific place and in consideration promises to pay the lessor a specified sum in a specified mode at specific interval and at a specified place".

Leasing plays an integral part in the finance industry, just like lending does. The industry lets individuals and corporations avail facilities and services, and gain access to products that their limited capital might not allow them to do so. For instance, someone with a regular source of income but little funds could lease an apartment in an expensive area, or a company, such as an airline, could lease an aircraft and then use it for profit without having to lay out the large capital expenditure that comes with such equipment.

Leasing is a unique form of intermediate term financing. To diversify, expand and modernize their business need huge amount of investment. Entrepreneurs are not wish to block their investment in plants and machinery.

Instead, they look for alternative means of financing the projects. In addition to debt and equity financing, leasing has emerged as a third important source of intermediate and long-term financing of corporate enterprises recently.

World over leasing has emerged as an innovative technique of financing industrial equipment. In India leasing has been developed as an important supplementary source of finance and is gaining acceptance from the industries.

In the Indian context the fundamental difference between a lease transaction and other asset financing plans like hire purchase is that a lease contract cannot provide for a transfer of ownership from the lessor to the lessee whereas the other asset based financing plans carry this feature. Consequently the tax and accounting aspects of lease transactions are different from that of other financing plans.

Types of Lease

The classification is based on the extent to which the risk and rewards incidental to the ownership of the leased asset lie with the lessor or the lessee.

1. Finance and Operating Lease:

Under the financial lease a substantial part of the risks and rewards associated with the ownership of the asset are transferred from the lessor to the lessee. A finance lease is non-cancellable for a specified period and the lessee is responsible for the maintenance of the assets and its insurance. Therefore a financial lease transfers a major portion of risks and rewards associated with the ownership of the asset to the lessee.

Under the operating lease the lessor himself selects and purchases the equipment and leases it out. The lease is for a shorter period as compared to finance lease. During the tenure of the lease the lessor is responsible for insurance and maintenance of the asset. The lessor bears the risk of economic and functional obsolescence of the asset and has continued interest in the leased equipment.

The equipment cost is not fully amortised over the lease period of course the lessor can release the equipment or may dispose it off at a profit (selling price – Book value at the end of the lease period). The lessee has the option to terminate the lease contract by notice. It involves higher payment of rentals for lessor obligations are not confined to mere financing but span over maintenance repair and technical advice.

2. Sale and Lease Back and Direct Lease:

In a sale and lease back transaction the owner of an equipment sells it back to the erstwhile owner. The 'lease-back' arrangement in this transaction can be in the form of a 'finance lease' or an 'operating lease'. In general the 'Sale and lease back arrangement' is a readily available source of funds for financing the expansion and diversification programmes of a firm.

In cases where capital investment in the past has been funded by high-cost short term debt the sale and lease back transactions provide an opportunity to substitute the short-term debt by medium term finance.

A direct lease can be defined as any lease transaction which is not a 'sale and leaseback transaction'. In other words in a direct lease the lessee and the owner are two different entities.

3. Single Investor Lease and Leveraged Lease:

In a single investor lease transaction, there are only 2 parties to the transaction the lessor and the lessee in contrast to a leveraged lease transaction where there are 3 parties to the transaction the lessor the lender and the lessee.

PART C (1*20 = 20 Marks)

21. a. Risk relationship of various investment alternatives available.

Alternative investments include investments in five main categories: hedge funds, private capital, natural resources, real estate, and infrastructure.

One of the key risks that investors need to focus on when investing into alternative investment is liquidity. Investors may find that less liquid investments become unmarketable during a market downturn.

The investment alternatives available to investors in India

- Direct equity (Stocks)
- Equity mutual fund.
- Debt mutual fund.
- Public provident fund.
- Fixed Deposit.
- Real Estate.
- Gold.
- Sukanya Samruddhi Account.

b. Maximizing return and minimizing risk- comment

Investments are usually like to earn high returns, but high returns come with high risks. Hence, to maximize your returns and minimize the risks, you need to diversify your portfolio. With a diversified investment strategy, you spread the risks of your investments across various asset classes.

To reduce risk diversify which means to spread out your investments among a number of different asset classes. Investing in different asset classes reduces your exposure to economic, asset class, and market risks.

c. What is systematic risk and examples

Systematic risk is indicative of a larger factor that affects either the entire market or a sector of the market. This type of risk includes natural disasters, weather events, inflation, changes in interest rates and even socioeconomic issues like war or even terrorism.

d. Unsystematic risk and effect on returns

Unsystematic risk occurs on a much smaller level. Also called specific risk or diversifiable risk, it's a risk factor associated with a specific company or industry. Strikes, mismanagement, or shortage of a necessary component in the manufacturing process all qualify as unsystematic risks.

To reduce unsystematic risk through diversification, you need to create a portfolio of securities whose returns are negatively correlated. That simply means that the change in return of one security is offset by the change in return on another security. These changes offset each other, which reduces the overall change on the portfolio's return from one period to the next. A well-diversified portfolio will also often protect you against a financial crisis, because risks will be reduced.