CMR INSTITUTE OF TECHNOLOGY

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Internal Assesment Test - I

Sub:	Investment Management							Code:	16MBAFM303
Date:	27.09.17	Duration:	90 mins	Max Marks:	40	Sem:	III	Branch:	MBA

		Marks	OBE CO	OBE RBT
Part A - Answer Any Two Full Questions (16*02=32 Marks)				
1 (a)	Define the term Speculation?	[02]	CO1	L1
(b)	Describe the different functions of stock market.	[06]	CO2	L2
(c)	Explain the process of investment?	[08]	CO1	L1
2(a)	What do you mean by security market?	[02]	CO2	L2
(b)	Examine the financial instruments? Discuss its feature.	[06]	CO1	L2
(c)	Discuss the type of derivatives and its advantages and disadvantages.	[08]	CO3	L2
3(a)	What do you understand by stock market Indicator?	[02]	CO3	L2
(b)	Discuss the various functions of stock exchange.	[06]	CO2	L2
(c)	Explain the factors to be considered before entering the primary market?	[08]	CO1	L2
Part B - Compulsory (01*08=08 marks)				
4				
(a)	Elaborate the trading and Settlement procedure in secondary market.	[08]	CO1	L3

Course Outcomes		PO1	PO2	PO3	PO4	PO5	PO6	PO7	PO8	PO9
CO1:	• To familiarize the students with the stock markets in India and abroad.	1a,2a	3a							
CO2:	• To provide conceptual insights into the valuation of securities	2b,3c	3b,2c	4a						
CO3:	• To provide insight about the relationship of the risk and return and how risk should be measured to bring about a return according to the expectations of the investors									
CO4:	• To familiarize the students with the									

	fundamental and technical analysis of the diverse investment avenues									
CO5:	• To learn the Theories of Portfolio management and also the tools and techniques for efficient portfolio management									

Cognitive level	KEYWORDS
L1	List, define, tell, describe, identify, show, label, collect, examine, tabulate, quote, name, who, when, where, etc.
L2	summarize, describe, interpret, contrast, predict, associate, distinguish, estimate, differentiate, discuss, extend
L3	Apply, demonstrate, calculate, complete, illustrate, show, solve, examine, modify, relate, change, classify, experiment, discover.
L4	Analyze, separate, order, explain, connect, classify, arrange, divide, compare, select, explain, infer.
L5	Assess, decide, rank, grade, test, measure, recommend, convince, select, judge, explain, discriminate, support, conclude, compare, summarize.

PO1 - *Engineering knowledge*; PO2 - *Problem analysis*; PO3 - *Design/development of solutions*; PO4 - *Conduct investigations of complex problems*; PO5 - *Modern tool usage*; PO6 - *The Engineer and society*; PO7- *Environment and sustainability*; PO8 – *Ethics*; PO9 - *Individual and team work*; PO10 - *Communication*; PO11 - *Project management and finance*; PO12 - *Life-long learning*

ANSWER KEY

INVESTMENT MANAGEMENT

1. Speculation can increase short-term volatility (and thus, risk). It can inflate prices and lead to bubbles, as was the case in the 2005-2006 real estate market in the United States. Speculators who were betting that home prices would continue to increase purchased houses (often using leverage) intending to "flip" them for a profit. This increased the demand for housing, which raised prices further, eventually taking them beyond the "true value" of the real estate in many markets. The frenzied selling that ensued is typical for speculative markets.
2. Economic Barometer:

A stock exchange is a reliable barometer to measure the economic condition of a country. Every major change in country and economy is reflected in the prices of shares. The rise or fall in the share prices indicates the boom or recession cycle of the economy. Stock exchange is also known as a pulse of economy or economic mirror which reflects the economic conditions of a country.

2. Pricing of Securities:

The stock market helps to value the securities on the basis of demand and supply factors. The securities of profitable and growth oriented companies are valued higher as there is more demand for such securities. The valuation of securities is useful for investors, government and creditors. The investors can know the value of their investment, the creditors can value the creditworthiness and government can impose taxes on value of securities.

3. Safety of Transactions:

In stock market only the listed securities are traded and stock exchange authorities include the companies names in the trade list only after verifying the soundness of company. The companies which are listed they also have to operate within the strict rules and regulations. This ensures safety of dealing through stock exchange.

4. Contributes to Economic Growth:

In stock exchange securities of various companies are bought and sold. This process of disinvestment and reinvestment helps to invest in most productive investment proposal and this leads to capital formation and economic growth.

5. Spreading of Equity Cult:

Stock exchange encourages people to invest in ownership securities by regulating new issues, better trading practices and by educating public about investment.

6. Providing Scope for Speculation:

To ensure liquidity and demand of supply of securities the stock exchange permits healthy speculation of securities.

7. Liquidity:

The main function of stock market is to provide ready market for sale and purchase of securities. The presence of stock exchange market gives assurance to investors that their investment can be converted into cash whenever they want. The investors can invest in long term investment projects without any hesitation, as because of stock exchange they can convert long term investment into short term and medium term.

8. Better Allocation of Capital:

The shares of profit making companies are quoted at higher prices and are actively traded so such companies can easily raise fresh capital from stock market. The general public hesitates to invest in securities of loss making companies. So stock exchange facilitates allocation of investor’s fund to profitable channels.

9. Promotes the Habits of Savings and Investment:

The stock market offers attractive opportunities of investment in various securities. These attractive opportunities encourage people to save more and invest in securities of corporate sector rather than investing in unproductive assets such as gold, silver, etc.

3. Process of Investment:

The 4-Step Investment Process

4 Steps. Your Solution. Developing a sophisticated investment solution requires more than a review of historical patterns. Freedom applies forward-looking assumptions in the construction of its models, placing a premium on those factors that are most likely to add value to your portfolio.

Step 1: Capital Market Assumptions

Freedom employs forward-looking risk, return and correlation assumptions based on economic data and indicators. These tools move beyond analyzing historical data and help avoid trend-chasing behaviors.

Step 2: Asset Allocations

Whether you are taking an aggressive or conservative approach to investing, Freedom's advanced optimization process is designed to find an asset allocation intended to maximize return potential at various risk levels. The resulting portfolio strategies provide you with options for reducing the overall volatility of your portfolio while remaining in alignment with your overall goals.

Step 3: Manager Selection and Portfolio Construction

Freedom treats portfolio construction as a distinct step in the process. Asset allocations are filled with portfolio managers who are selected based on our confidence that they can consistently add value to a Freedom portfolio.

Step 4: Continual Monitoring

Proactive performance reviews are essential to maximizing the flexibility of Freedom. All managers are constantly monitored to determine whether organizational adjustments or investment process changes may impact performance. Capital market assumptions are continuously monitored and updated to maintain optimal asset allocations.

2 a. If arrears on debt and/or nonperforming loans are of economic interest, compilers should consider either or both as an optional “of which” component for relevant position items. · Arrears are shown separately in Debt Guide Table 4.1. Arrears will be defined as in the Debt Guide para. 3.36. (Cases of arrears need not be limited to Exceptional Financing. The desirability of identification of arrears is not limited by whether or not going into arrears is treated as an imputed transaction or not, as discussed in Chapter 3 Accounting Principles. However, if a transaction is imputed, all arrears are classified as short-term; if a transaction is not imputed, they will be classified according to the original instrument.) · Nonperforming loans are a related but not identical concept, often defined by payment being overdue by more than a specified time. [Questions: (i) Is this proposal suitable? (ii) Should data be limited to liability positions data, or should the possibility be opened for asset positions? (iii) Should arrears, nonperforming loans, both, or a mixture be adopted? (iv) How should the category be defined?] (j) Financial gold could be considered for reclassification as a financial asset, rather

than a good, because of its role in financial markets. As a result, international transactions would be recorded in the financial account, rather than as goods, and would be netted, rather than gross. However, the positions would not be included in the international investment position because they lack the international element that arises for monetary gold included in reserve assets. [Question: Should financial gold be treated as a financial asset?] (k) Trade-related credit. Trade credit is limited to credit extended by suppliers, so the Debt Guide paras. 6.9–11 introduce a wider concept of trade-related credit that includes trade credit, trade-related bills, and credit by third parties to finance trade. Trade-related bills and credit by third parties to finance trade could be identified as a separate component of loans as supplementary information where they are considered statistically significant and analytically useful. [Question: Should an optional category for trade-related credit be created?] (l) Reinvestment of earnings. This imputed instrument is used for the financial account entry that corresponds to the imputed income item for reinvested earnings. (Further discussion appears in Chapter 7, Financial Account, and Chapter 10, Primary Distribution of Income Account.) CHAPTER 5 Annotated Outline – April 2004 63 [Question: Are the proposals in this paragraph, other than those for which there are specific questions, suitable?] The rationale for the classification will be stated, for example, the role of currency and deposits in monetary analysis, and the residual claim nature of equity interests. It will be noted that financial innovation has resulted in new types of instruments. 3. Discussion of the classification of particular instruments 5.8 After introducing the main types of financial assets, this chapter will go on to discuss the application of the general classification to particular situations. This discussion will largely follow Chapter IV of MFSM (paras. 116–181) because the content and level of description is considered appropriate for this manual. However, it should be elaborated and updated to account for any subsequent developments in particular cases: (a) Repurchase agreements, securities lending, and gold swaps will be defined and illustrated. The instrument classification will be highlighted by identification of security and loan aspects. An example will be given. (See MFSM paras. 142–148 and BOPCOM-01/16.) (b) The borderline between monetary gold and other gold will be discussed, and the process of monetization and demonetization of gold will be explained. (In addition, if financial gold were to be recognized as a financial instrument, the borderline with nonfinancial gold would also be discussed.) (c) Gold loans, gold swaps, and gold deposits will be defined. Possible treatments are as the gold staying on the books of the gold provider, in conjunction with a loan or deposit. (See MFSM paras. 154–164, Debt Guide paras. 3.31 and 3.34, and GFSM 2001 para. 7.115.) (d) Employee stock options will be classified as a subcategory under a new instrument category “financial derivatives and employee stock options,” the other subcategory being financial derivatives. (e) Inclusion of financial leases as loans will be noted. (It is proposed that financial leases will be noted under Classifications, International Investment Position, Financial Account, and Primary Income, with a full exposition in an appendix to the manual.)

(f) Loans that have been traded will be classified as securities under certain conditions, as stated in the Debt Guide para. 3.29. It will be noted that many loans are traded but not sufficiently to become securities. (g) Depository receipts are classified in the same way as the underlying security, as noted in Economic Territory, Units, Institutional Sectors, and Residence.

4. Types of derivatives and its advantages and disadvantages
   Derivatives – Meaning, Types, Advantages, Disadvantages, Check **derivatives meaning**and **derivatives market** Information, In this article you can find complete details for Derivatives like – Meaning of Derivatives, Various Types of Derivatives, Advantages of Derivatives, Disadvantages of Derivatives etc. Now check more details from below**.**

1. Options:

These are the binding contracts between the parties to buy or sell a particular security, commodity, metal etc., at a given price. Options give the right to buy to the buyer and does not bring any obligation. An option to buy certain security at certain price is a “call option” and the other one which gives the right to sell a security is “put option”.

2. Futures:

It is a derivative where two parties enter into a contract to buy or sell a security or any property at certain agreed price for a “future delivery”. There will be an agreement to buy or sell a specified quantity securities or any commodities y in a designated future month at a price agreed upon by the buyer and seller. They facilitate the trading on future exchange.

3. Forward contracts:

Most of the difference between forwards and futures lies in terms of liquidity, trading platform and settlement. Forward contracts are customized bilateral contracts between two parties where settlement takes place in future on a specific date at a price agreed today. They are less liquid than futures.

4. Swaps:

They are the agreements between the parties to exchange the financial instruments or the resulted future cash flows in future based on agreed criteria such as rate of interest, stock indices etc.,

1. Leverage:

The ability and chances to make huge and extreme profits is high in derivatives than incase of primary securities or mutual funds.

2. Manages the risk:

Derivative contracts helps to hedge the risk of high prices in the future. Most important purpose of these contracts is managing the risk.

1. High volatility:

Since the value of derivatives is based on certain underlying things such as commodities, metals and stocks etc., they are exposed to high risk. Most of the derivatives are traded on open market. And the prices of these commodities metals and stocks will be continuously changing in nature. So the risk that one may lose their value is very high.

2. Requires expertise:

In case of mutual funds or shares one can manage with even a limited knowledge pertaining to his sector of trading. But in case of derivatives it is very difficult to sustain in the market without expert knowledge in the field.

3. Contract life:

The main problem with the derivative contracts is their limited life. As the time passes the value of the derivatives will decline and so on. So one may even have chances of losing completely within that agreed time frame.

5. Trading and settlement procedure:

Trading Procedure on a Stock Exchange:

The Trading procedure involves the following steps:
1. Selection of a broker:
The buying and selling of securities can only be done through SEBI registered brokers who are members of the Stock Exchange. The broker can be an individual, partnership firms or corporate bodies. So the first step is to select a broker who will buy/sell securities on behalf of the investor or speculator.

2. Opening Demat Account with Depository:
Demat (Dematerialized) account refer to an account which an Indian citizen must open with the depository participant (banks or stock brokers) to trade in listed securities in electronic form. Second step in trading procedure is to open a Demat account.

The securities are held in the electronic form by a depository. Depository is an institution or an organization which holds securities (e.g. Shares, Debentures, Bonds, Mutual (Funds, etc.) At present in India there are two depositories:

NSDL (National Securities Depository Ltd.) and CDSL (Central Depository Services Ltd.) There is no direct contact between depository and investor. Depository interacts with investors through depository participants only.

Depository participant will maintain securities account balances of investor and intimate investor about the status of their holdings from time to time.

3. Placing the Order:
After opening the Demat Account, the investor can place the order. The order can be placed to the broker either (DP) personally or through phone, email, etc.

Investor must place the order very clearly specifying the range of price at which securities can be bought or sold. e.g. “Buy 100 equity shares of Reliance for not more than Rs 500 per share.”

4. Executing the Order:
As per the Instructions of the investor, the broker executes the order i.e. he buys or sells the securities. Broker prepares a contract note for the order executed. The contract note contains the name and the price of securities, name of parties and brokerage (commission) charged by him. Contract note is signed by the broker.

5. Settlement:
This means actual transfer of securities. This is the last stage in the trading of securities done by the broker on behalf of their clients. There can be two types of settlement.

(a) On the spot settlement:

It means settlement is done immediately and on spot settlement follows. T + 2 rolling settlement. This means any trade taking place on Monday gets settled by Wednesday.