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M-1659

SL.No. 0438

Total No. of Pages : 3

II Semester M.Com. Examination, May/June - 2018

(Scheme:CBCS)

COMMERCE

Capital Market Instruments (HC Paper)

Time : 3 Hours

Max. Marks : 70

PART-A

Answer any five of the following. Each question carries five marks. [5 × 5 = 25]

1. What are the unique features of equity share as a capital market instrument?
2. What are the prerequisites for issuing ADRs by a company?
3. Explain the principal merits of ETFs.
4. What are derivatives? Enlist different types of derivatives traded today.
5. Distinguish between a futures contract and an options contract.
6. What is an interest rate swap? Illustrate with a suitable example.
7. A company is planning to sell Zero Coupon Bonds with a face value of each bond being Rs 10,000 and matures in 4 years from now. It can be sold at a discount of 39% Alternatively the company can issue 12% coupon bonds with same face value and maturity. Given the yield on the coupon bond as 11.2% which alternative is better for the company?
8. A commodity is currently selling in the spot market at a price of Rs. 3400/q. What is its theoretical fair futures price , given that risk free rate is 8% (continuously compounded) and cost of carry is Rs.310/q and T = 4 months.

P.T.O.

PART-B

Answer any **three** questions. Each question carries ten marks, [3 × 10 = 30]

9. Discuss the factors that contributed for the growth of derivatives markets.
10. What are 'futures'? Explain their merits and limitations.
11. What are options? How are they different from futures?
12. PPM Ltd. Started functioning last May 2017. The face value of company's stock is Rs 10. It declared 80% dividend for the current year. The Company plans a stable dividend payout policy with a payout ratio of 50%. The return on investment of the company will be at 14 % per annum in first four years. Thereafter, it is expected to be constant at 10% per annum. The market requires a 11% return on the company's stock. What is the present value of stock?
13. A put option on JP stock on NSE at currently traded for a premium of Rs. 145 (Strike price= K =Rs.3100). The put options expire in 2 months from now. If the theoretical price range of JP stock is Rs. 0, 400, 800, ... to Rs.5000, what is the payoff profile for the writer and holder of this put option? What is the BEP for the writer and holder? Draw a schematic diagram showing the results.

PART-C

14. Case study (Compulsory) [1 × 15 = 15]

A dealer in raw coffee is planning to sell 380 bags of raw coffee in the last week of June but concerned about the possible fall in raw coffee prices in the coming months . Accordingly he plans to hedge price risk by taking up June coffee futures contracts.

A cooperative coffee curing mill plans to buy 620 bags of raw coffee in June but is concerned about the possible rise in price of raw coffee in the market . It has decided to trade June coffee futures for hedging price risk.

Hedging policy of the Dealer and the Mill is to close the futures contract a couple of days ahead of its expiry and sell/buy raw coffee in the spot market.

June coffee futures are traded today (i.e. 15th March) on an exchange at a price of Rs. 7,000 per bag. The size of each futures contract on the exchange is 100 tons. The margin money required to be deposited is 12 of total value of futures contracts.

Suppose the coffee price fell to Rs.5500/bag at the time of expiry of June futures contract.

Questions:

- a) What position the dealer will be taking in the futures market? How many contracts he needs to take? How much margin money he has to deposit with the clearing house.
- b) What is the profit /loss on futures contract for the dealer? Is the dealer benefitted by taking futures contract?
- c) What position the Mill will be taking in the futures market? How many contracts the Mill needs to take? How much margin money it has to deposit with the clearing house?
- d) What is the profit/loss on futures contract for the Mill.
- e) Is the futures contract an ideal hedging instrument for the Mill? If not, justify your answer.

