NOV 2019 Final New P 6B

Roll No. ....

Total No. of Case Study Questions – 5

Total No. of Printed Pages – 31

Time Allowed – 4 Hours

Maximum Marks – 100

Final New Syllabus
Paper - 6 B
Financial Services & Capital Markets

ZAB

Answers to questions are to be given only in English except in the case of candidates who have opted for Hindi Medium. If a candidate who has not opted for Hindi Medium, his/her answers in Hindi will not be valued.

The question Paper comprises **five** case study questions. The candidates are required to answer any **four** case study questions out of **five**.

Answers in respect of Multiple Choice Questions are to be marked on the OMR Answer Sheet only.

Answers to other questions to be written in the descriptive type answer book. Answer to MCQs, if written in the descriptive type answer book will not be evaluated.

Candidates may use calculator

Marks

CASE STUDY 1

The board of directors of the ABC Ltd, at its meeting held on June 11, 2019, has, with the subsequent approval of the members of the Company, by way of a special resolution through Postal Ballot ("Special Resolution"), results of which were declared on 5th August, 2019, approved the proposal to buy back its own fully paid-up Equity Shares of face value of ₹ 5 each ("Equity Shares") from the members of the Company (other than the Promoters, the Promoter Group and

Persons in Control of the Company) payable in cash, for an amount aggregating to ₹ 8,260 crores ("Maximum Buyback Size") at a price not exceeding ₹ 800 per Equity Share ("Maximum Buyback Price"), under the open market route through the stock exchanges, in accordance with Companies Act, 2013 and the SEBI Buyback Regulations.

The Buyback has been implemented by the Company by way of Open Market Purchases through the stock exchanges, by the order matching mechanism except "all or none" order matching system, as provided under the Buyback Regulations.

The buyback was completed within 6 weeks of the commencement date.

Present EPS is ₹ 35.64 with total earnings of ₹ 15,570 Crore. Present P/E multiple is 21.24

Relevant financial details are as below (All figures are in ₹ Crores) :

As on	Mar 31, 2019	Mar 31, 2018	Mar 31, 2017	Mar 31, 2016
Equity Share Capital	2,184	1,092	1,148	1,148
Reserves and surplus*	60,749	62,410	66,869	59,934
Net worth / Shareholders equity	62,933	63,502	68,017	61,082
Total debt**	20,000	18,000	16,000	15,000

*Free Reserves were ₹ 54,636 as on 31st Mar, 2019

Marks

Annexure '1' -

Shareholding Pattern

Shareholders	Pre Buyback		Post Buyback	
	No. of Equity Shares	% of Shares	No. of Equity Shares	% of Shares
Promoters and / or persons who are in the control and / or acting in concert (Promoter Group)	56,01,82,338	12.82%		
Indian Financial Institutions	31,73,073	0.07%		
Banks	17,09,234	0.04%		
Mutual Funds	58,46,44,086	13.38%		
Indian Public & Corporates	95,54,85,110	21.87%		
Foreign Institutional Investors	1,49,15,64,414	34.14%		
NRIs	2,58,96,923	0.59%		
Foreign Nationals and Overseas Corporate Bodies	21,618	0.01%		
American Depository Shares (ADS)	74,62,54,648	17.08%		
Total	**4,36,89,31,444**	**100.00%**		

Marks

Annexure '2' Share Price Scenarios

Week No.	No. of Shares offered in each week	Opening Price of Week (₹)	Closing Price of Week (₹)	Volume weighted avg price of shares (₹)
Week prior to 1	NA	740	745	750
1	Nil	760	765	755
2	1 .5 crores	750	760	740
3	2 crores	748	755	760
4	2.5 crores	775	778	785
5	3 crores	764	773	775
6	1.325 crores	770	785	790

Post closure of Buyback average closing price for ABC Ltd in Week 7 was 800, Week 8 was 810 and Week 9 was 805. It hit all time new high of 840 in the meantime.

1.1. The 'Buyback Period' as per SEBI Guidelines is defined as period between : **2**

(A) The date of Board of Directors resolution to authorise the buyback of shares and the date on which the payment of consideration to shareholders who have accepted the buyback offer is made

(B) The date of voting of postal ballot for special resolution to authorise the buyback of shares and the date on which the payment of consideration to shareholders who have accepted the buyback offer is made

(C) The record date and the date on which the payment of consideration to shareholders who have accepted the buyback offer is made

(D) The opening date of buyback on recognised stock exchange and the closing date of buyback on the recognised stock exchange

Marks

1.2. The mode through which the Buyback can be executed as per SEBI Guidelines is : **2**

(A) Spot Transaction

(B) Private Arrangement

(C) Tender Offer

(D) Negotiated Deals

1.3. The letter of offer is dispatched on 5th June 2019 (Wednesday). Please calculate the date of opening of offer and closure of offer **2**

(A) 10th June 2019 and 25th June 2019

(B) 14th June 2019 and 28th June 2019

(C) 12th June 2019 and 25th June 2019

(D) 16th June 2019 and 30th June 2019

1.4. A Small Shareholder as per SEBI Guidelines is defined as **2**

(A) who holds shares or other specified securities whose market value, on the basis of opening price of shares or other specified securities, on the recognised stock exchange in which highest trading volume in respect of such securities, as on record date is not more than two lakh rupees.

(B) who holds shares or other specified securities whose market value, on the basis of closing price of shares or other specified securities, on the recognised stock exchange in which highest trading volume in respect of such securities, as on record date is not more than five lakh rupees.

(C) who holds shares or other specified securities whose market value, on the basis of closing price of shares or other specified securities, on the recognised stock exchange in which highest trading volume in respect of such securities, as on date of offer letter is not more than two lakh rupees.

(D) who holds shares or other specified securities whose market value, on the basis of closing price of shares or other specified securities, on the recognised stock exchange in which highest trading volume in respect of such securities, as on record date is not more than two lakh rupees.

Marks

1.5. If the Buy-back is through Book Building Process then the number of Bidding Centers should be : 2

(A) Not less than thirty and there shall be at least one electronically linked computer terminal at all the bidding centers.

(B) Not less than sixty centres spread across India.

(C) In all capital cities of the states as well as union Territories of India.

(D) None of the options

1.6. You are a Financial Advisor to Mr. B, a HNI, who wants to participate in the upcoming buyback of ABC Ltd.

Mr. B holds 5000 shares of ABC Ltd. He had bought them at an average price of ₹ 580. He offered his 2000 shares in Week 2, 2500 shares in Week 3 and balance 500 shares in Week 6.

Please advise him whether he should participate in the same or not with specific focus on :

(A) Necessity of buyback for any company and its shareholders 1

(B) Pre and Post Buyback shareholding pattern - Use format in Annexure '1' and assume that the Maximum Buyback Size is completed. 1

(C) Financial returns for Mr. B and your recommendation. Please refer Annexure '2' for relevant inputs. 3

1.7. You are a CFO of ABC Ltd. Please elaborate the step by step process which will be followed in such buyback issues with specific focus on :

(A) Calculate the amount that will have to be offered in Escrow Account with 50% in cash deposit and 50% in Bank Guarantee form. 3

(B) The calculation of pay-out amount to investors if Maximum Buyback Size has been executed. Refer Annexure '2' for inputs. 2

Marks

1.8. You are a Head-Compliance (SEBI), who looks after the compliance with various guidelines of SEBI. Please highlight the buyback related compliance for the proposed transaction.

(A) Discuss the compliance with 'Maximum Buyback Size' and identify the 'Minimum Buyback Size' as on the commencement of the buyback. **3**

(B) Calculate & discuss the compliance with Debt Equity Ratio for the buyback. **2**

CASE STUDY 2

Lend & Co., is a public company which is involved in carrying out infrastructure projects. Whilst it started out as a project company aimed at executing power and defense projects, over a period, it also ventured into construction of roads, transmission lines etc. Today the company has a diverse portfolio which it operates on.

Lend & Co., also has a number of subsidiaries some of which are in the form of special purpose vehicles formed for the specific purpose of undertaking projects in the road and transmission sectors. Whilst most of the Lend group's customers are government or its agencies, it also has projects for private players in the solar sector. Given the structure of the Group, Lend & Co., is covered as an investment company under the Reserve Bank of India Guidelines and is registered as a Non-deposit taking NBFC.

Mr. Lender is the Managing Director of Lend & Co. He is also one of the promoters of the Company and is highly passionate about the Group's operations and is highly involved in business strategy and decision making. Over the last year or so, Lender has been slightly worried about the fund and liquidity management at the group level and he feels there is a lot of scope for revising its entire treasury strategy and realign its borrowing portfolio. He had a CFO, who was overseeing the treasury functions and had an excellent relationship with lenders and financiers, but due to certain medical reasons left. Mr. Diligent has now been appointed as the new CFO.

Marks

Mr. Diligent comes from a finance background and has handled numerous fund raises and headed the treasury function in his previous organization. Mr. Lender and Mr. Diligent want to undertake various initiatives in the Group to ensure the financial efficiency in the Group.

As part of the key areas which Mr. Diligent wants to touch upon the following :

- Risk management practices
- Practices in raising and deployment of funds
- Infrastructure investment trusts
- Working capital management

Risk Management practices :

Based on a review of Mr. Diligent on the treasury practices and operations of the Company, he observed the following features which he termed as "Signals" indicating a required re-look in the risk management practices of the Company:

- The Company deals with a significant amount of foreign exchange though the operations of the Group itself, which in his view, does not warrant such quantum of foreign exchange to be bought and sold. The overall gain made by the Group on foreign exchange transactions during 2018-19 was Rs. 320 Crores, including MTM adjustments to the tune of Rs. 270 Crores, and the treasury team was rewarded for the same.
- The Company had invested in some new products available in the market. Though there has been no track record in terms of the performance of these products, the junior members in the treasury team believe that these are new generation products and the Company should explore these products with an open mind as this will likely give significant gains in the short term. The overall unrealized gain on these products for FY 2018-19 was ₹ 130 Crores.
- The Company has entered into some derivative contracts which are not completely backed up by underlying assets and liabilities. One of the treasury departments KRA was to generate as much profit from the derivative transactions so that they are able to contribute to the growth of the Company.

- Though there is an "investments and hedging committee" in place, the members of the committee primarily comprise persons from the treasury department. The head of treasury had an excellent relationship with the erstwhile CFO and there were no formal approvals/reviews that were taking place.
- Praveen, who was the blue eyed boy of the Treasury head, takes huge pride in the amount of profits generated by the treasury department in the last two years and believes that of all functions within the Company, the treasury department is the one which contributes immensely to the bottom line of the Company.
- There is no risk limits set for the amount of derivative contracts that the company can enter into.

Mr. Diligent held discussions with the MD of the Company to share his thoughts on the above aspects and the MD asked him to prepare a report for discussing these with the Board of Directors of the Company.

Mr. Diligent also highlighted to the MD of Lend & Co., that it also has significant exposure in infrastructure projects undertaken by subsidiaries, which are primarily into road projects. He said about 78% of the Company's funding has been channelized to these road subsidiaries, who are facing issues in repayment of borrowing, project overruns and risk potential default in repayment of borrowings to banks. Mr. Lender felt that considering the nature of the industry, it is bound to be the case and as such this should not be a cause of concern. Mr. Diligent mentioned that, whilst nature of the industry is of course to be factored in, he noted that in some of the subsidiaries where the Company had funded, those were in the form of short term inter corporate deposits which are back to back short term loans availed by Lend & Co., though these were eventually deployed by the subsidiaries as part of their projects primarily to fund excess costs incurred (Overruns). He further mentioned that, these projects were delayed in execution and the likely project overrun including interest costs being treated as part of project costs is about 22% of the overall project costs of all these subsidiaries. Mr. Lender asked Mr. Diligent to look into the above and provide what possible options the Company can consider in respect of addressing some of the concerns expressed.

One of the options which Mr. Diligent expressed to the MD is to consider Infrastructure Investment Trusts (INVITS) for some of the revenue generating subsidiaries, which proceeds can be used for addressing the funding gaps in the subsidiaries for their ongoing projects. Mr. Diligent also mentioned that the overall value of the underlying assets in the revenue generating projects as of date is about ₹ 900 Crores. Details of these three projects under construction and the status are as below :

- Project A – ₹ 280 Crores incurred which is about 42% of the total capital cost. As per an evaluation by an internal engineer, this represents about 60% of the project completion and this project is a public private partnership.
- Project B – ₹ 620 Crores has been incurred, which is about 85% of the total capital cost. This is also a PPP and as per internal engineer, this represents about 80% of the completion status.
- Project C – is ₹ 480 Crores represents 90% of the capital cost and is almost complete in terms of physical status of the project. All approvals and certifications for commencing the project has been received. This project is with a private customer.

Mr. Diligent also studied the other loans and investments that the Company has in its balance sheet and is keen on suggestions of creating INVITs and other such structures (if any). The key inputs are as below :

- The Company has significant amount of inter corporate loans and investments in debentures issued by the infrastructure companies.
- He feels that the credit evaluation of these parties aren't something which is very positive.
- There were no hedging mechanisms in place for some of these borrowings. He feels that the Company should explore options of entering into 'credit default swaps' (CDS) for these loans which will help the Company. He wants Praveen and other treasury team members to study the same and provide their thoughts.
- Praveen shared his initial thoughts and mentioned that CDS are traded on exchanges and are subject to huge regulatory compliance and may not be worth the effort.

- Praveen also mentioned that considering the nature of the underlying assets, the premium to be paid will be quite high in terms of the CDS.
- Mr. Diligent requested Praveen to also understand the pricing theories for pricing of CDS.

Mr. Diligent also believes that the Company will have some excess cash left in the system post some of his proposals being implemented. In this connection,

- He also wanted the team to understand and provide him an update in terms of the benefits of investments in mutual funds and the options that the Company can consider for maximizing returns without compromising on basic risks.
- He was also particularly keen to evaluate whether the Company should invest in shares or in mutual funds.
- Next aspect he wanted the team to analyze are the type of mutual funds to invest in and which would be a safe bet considering the overall risk aspects of the Company.
- He was keen in knowing where the mutual funds are made : 'sector funds' or 'arbitrage funds' ?
- The factor to evaluate which funds to invest in, is a key aspect he wanted the team to consider and report back to him on.

Mr. Diligent had a conversation with his treasury team members to understand their views on the some of the proposals suggested by them. He was particularly interested in knowing what key controls that the Company has to put in place in its treasury operations and how they can proceed in respect of the same.

Mr. Lender called for a meeting at the end of the first quarter and has asked Mr. Diligent to present his proposals to him first, post which he said, he will also call upon a meeting with the Board of Directors. Mr. Diligent agreed that he will do his best to prepare the presentation duly considering all aspects and was very positive that it will be in the best interests of the Company.

Considering the above, you are required to look into the below questions and provide your responses :

Marks

Questions :

2.1. Credit default swap resembles option contracts but are more in the nature of swap arrangements because : **2**

(A) Element of choice exists

(B) Element of choice does not exist

(C) CDS is only for hedging whereas options are not for hedging

(D) None of the options.

2.2. The 'No arbitrage model' of pricing CDS is based on which of the following assumptions : **2**

(A) There is zero cost of unwinding the fixed leg of the swap on default and there is no risk free arbitrage

(B) The is risk free arbitrage

(C) There is no zero cost of unwinding the fixed leg of the swap on default

(D) There is no risk free arbitrage and there is no zero cost of unwinding the fixed leg of the swap on default.

2.3. A mutual fund which has purchase and redemption options during specific intervals at prevailing NAV prices is called : **2**

(A) Open ended fund

(B) Close ended fund

(C) Interval funds

(D) Growth funds

Marks

2.4. The percentage of assets that were spent to run a mutual fund is computed as : 2

(A) Expense / average value of portfolio, where expense includes travel cost, management consultancy and advisory fees.

(B) Expense / average value of portfolio, where expense includes travel cost, brokerage, management consultancy and advisory fees.

(C) Expense/average value of portfolio, where expense excludes travel cost, management consultancy and advisory fees.

(D) Expense/average value of portfolio, where expense represents brokerage.

2.5. A mutual fund has its net asset value calculated at the end of each trading day. An exchange traded fund has : 2

(A) Its price is based on net asset value and determined at the end of every day

(B) Is fixed and does not undergo any change during the tenure of the fund

(C) Its price changes and is determined based on net asset value

(D) Its price changes throughout the day, fluctuating with supply and demand

2.6. What are your views on the observations of Mr. Diligent on the treasury practices followed by the Group from a Risk Management perspective ? 5

2.7. If Lend & Co., has to go ahead with INVITs, outline the key aspects of how INVITs work and how this will benefit the Company ? 3

2.8. Can Lend & Co., also issue INVITs for the three projects under construction of the Group ? What conditions would need to be fulfilled for the same ? 3

2.9. What are the features of a credit default swap and how is it likely to be of use to Lend & Co ? 4

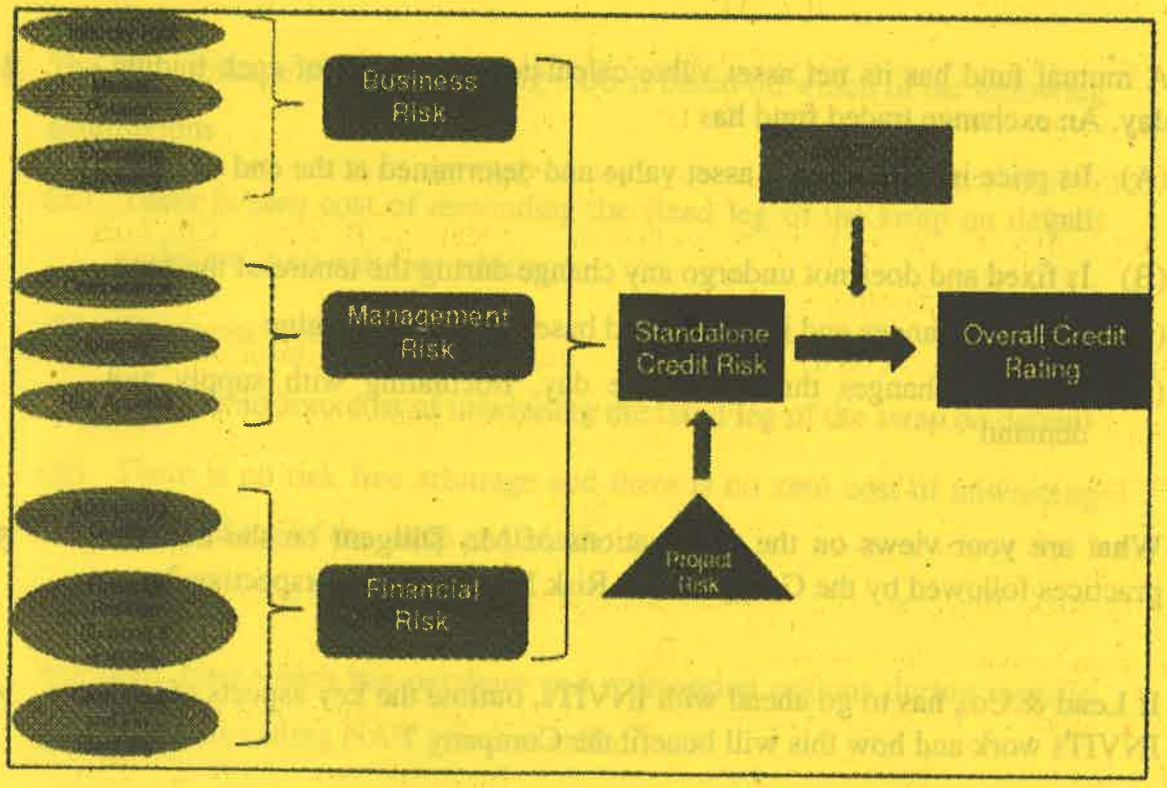
Marks

CASE STUDY 3

CRA is one of the prominent Credit Rating Agency in India. You are working there as a Chief Rating Consultant (Large Corporates Segment).

The J Rover Automotive Ltd has approached CRA to secure credit rating for its planned short-term working capital of ₹ 1,000 crores and long-term credit facilities of ₹ 2,500 crores from XYZ Bank.

CRA's Rating Methodology



Above chart summarises the overall methodology of CRA credit rating.

Business Risk carries 30% weight, Management Risk carries 20% weight and Financial Risk carries 35% weight. Parent/Govt support carries 15% weight in the absence of which 5% each is added in earlier 3 risks. Each risk is benchmarked on a scale of 1 to 5 with 5 being riskiest and 1 being safest.

Marks

Accordingly, weighted avg. rating range is 1 to 5 with below categorisation.

Rating 1 – AAA+

Rating 1 to 2 – AAA

Rating 2 to 3 – AA+

Rating 3 to 4 – AA–

Rating 4 – 5 – A+

The analysis of a company's financial ratios is core to CRA's rating process as these ratios help understand a company's overall financial risk profile.

CRA considers four broad parameters:

- Solvency - Current Ratio and Acid Test Ratio
- Coverage - Interest and Debt Service coverage analysis
- Capital Structure - Debt Equity and Debt to Capitalisation
- Operation Cycle - Debtors Collection, Inventory Holding, Creditors Payment and Operating Cycle Period

The relative importance varies on a case-specific basis and instead of arithmetic approach while assessing financial risk, CRA makes a qualitative and contextual assessment of these ratios for each case.

The final rating assessment entails the interplay of various other factors such as Industry Risk, Business risk, Project risk, Management risk, as well as support from stronger parent /group /government.

CRA's approach to rating specifically the Automotive Manufacturers involves evaluating their business, management and financial risk profiles. The parameters that are considered for evaluation of business risk profile include the sector analysis, headwinds and growth concerns, if any, company's market position and operating efficiency. Market position assessment focuses on the company's ability to maintain high volumes in a wide variety of market segments. While analysing operating efficiency, CRA assesses its ability to manufacture technologically-superior vehicles at low costs. Operations in the industry are fixed-cost intensive; therefore, well-engineered products and significant volumes are key factors. CRA also assesses the company's financial and management risk parameters to arrive at the final rating.

The brief overview of J Rover's business and summary of key events alongwith key financial data of J Rover is as below

- J Rover is one of the leading automobile manufacturers in the world, providing mobility solutions to over 100 countries. Its portfolio includes a wide range of passenger cars, utility vehicles, trucks, and buses. It has a strong global network of 80 subsidiaries, associate companies and joint ventures, including the one in the UK and in South Korea.
- The Automotive Industry across globe is undergoing significant headwinds in the context of shift to ACES (Automated, Connected, Electric and Shared) mobility.
- Below table captures the overall volume and EBIDTA margin of J Rover's International and Indian operations over last two years.

Volumes	FY 2019	FY 2018
International	5,65,000	6,33,000
Indian		
Passenger Cars	2,15,000	1,90,000
Commercial Cars	5,20,000	4,50,000
Total volume	13,00,000	12,73,000

EBIDTA Margin	FY 2019	FY 2018
International ($)	4%	8%
Indian (₹)	7%	9%

- The International operations of J Rover have been hit due to ongoing turmoil in UK due to Brexit issues which may have significant impact on the UK headquartered entity. Additionally, the major market for its marquee brands have been in slow lane in China after scorching volume growth due to purchase quotas and shift to Electric vehicles. The USA China Trade Tariff war has escalated and hence it has started impacting the overall volume sold by Chinese Subsidiary. Even in the European market, the diesel scandal and emission norms have put the buyers off and the purchase decisions have been deferred. The regulators have been laying down the roadmap for 100% transition to non-ICE vehicles which warrants investment in new products and technology. The competition from non-Auto OEMs such as Digital and Internet companies offering ride hailing, autonomous cars have changed the ownership narrative for vehicles.
- The domestic volumes have been encouraging but the overall market environment is daunting given there is subdued credit growth, NBFC sector hit with liquidity and buyers opting for ride hailing rather than to own the car. The competition intensity is also significant with ~ 10-15 new products introduced p.a. with higher features at lower price points. In the Commercial Segment, the revised axel norms have increased the capacity of existing carriage by 30% hence expected to impact volumes and replacement cycle. The sales have fallen for continuous 12 months in the last year with 30% fall in PV and 25% fall in CV sales month-on-month.
- Overall, due to slow demand offtake, the inventory has been piling up in the pipeline at dealers and distributors level forcing management to opt for higher discounts for liquidation, production cut and layoffs. The working capital funding to dealers have also increased disproportionately.
- The market price of J Rover Ltd, listed on NSE and BSE, has fallen by 70% over the period of one year from 400 to 120 eroding the market capitalisation by ~ ₹ 35,000 crores.

Marks

- In order to tide over the difficult conditions, J Rover Ltd has kicked off the 'Project Recharge' with overall outlay of $ 3 billion worth of cost and profit improvements. Of this, $ 700 million was via cut in investments, $ 400 million represented working capital improvement & $ 150 million was saved through workforce reduction in FY 19. From FY 20, reducing 6,000 head-count will yield further $ 400 million cost savings
- The management expects the overall environment to remain challenging for next 1-1.5 years until the political and regulatory stability is achieved. The demand may remain subdued due to multiple factors mentioned earlier.
- The focus of management remains firm on new technology investment and innovation in product and service levels. The management continues to tap new emerging markets for its luxury brands and export market for its domestic business. It will leverage the CV market leadership (55%) in India to consolidate the position in the passenger vehicle market (5%). It has been at forefront in launching the EV buses in India and EV passenger vehicles across globe. The overall capex spends estimate in the next two years to remain competitive is expected to be $ 5 Bn.
- The Parent Entity (45% ownership) of J Rover Ltd is $ 150 Bn entity and has strong patronage, liquidity and brand profile. The financial strength and commitment to J Rover by its parent entity cushions the overall stress. The Parent entity has credit rating of two notches above the sovereign rating.
- The Management of J Rover Ltd is mix of highly experienced and diverse individuals from Automotive background with avg. age of 50 with avg. 10 years spent with J Rover.
- Annual debt repayment was ₹ 3,500 crores in 2019 and ₹ 3,000 crores in 2018. The debt worth $ 3.5 Bn is due for repayment in next 2-3 years.
- Current rating of Long-Term Loans is AA+ and Short-Term Loans is AAA
- P & L Statement and Balance sheet of J Rove for 2019 and 2018 is as below :

Marks

Statement of P & L (₹ In Crores)

Particulars	FY 2019	FY 2018
Sales	3,00,000	2,95,000
Material Cost	2,00,000	1 ,90,000
Labour Cost	35,000	30,000
Other Expenses	32,000	27,000
	2,67,000	**2,47,000**
EBIDTA	33,000	48,000
Interest	6,000	5,500
Depreciation	24,000	22,000
Amortisation	4,000	3,500
	34,000	**31,000**
Profit/Loss before exceptional items	**– 1,000**	**17,000**
Impairment Charge	25,000	–
Profit before Tax	**– 26,000**	**17,000**
Tax	–2,500	4,000
Profit after Tax	**–23,500**	**13,000**

Marks

Balance Sheet Details (₹ In Crores)

Particulars	FY 2019	FY 2018
Assets		
Net Fixed Assets	1,60,000	1,95,000
Current Assets		
Debtors	22,000	10,000
Inventory	45,000	30,000
Cash & Cash Equivalents	20,000	23,000
Other Investments	12,000	13,000
	99,000	**76,000**
Total Assets	**2,59,000**	**2,71,000**
Liabilities		
Share Capital	1,000	1,000
Reserves	70,500	94,000
Long Term Loans	1,10,000	90,000
Vendor Payables	45,000	35,000
Other Liabilities	32,500	51,000
Total Liabilities	**2,59,000**	**2,71,000**

Please answer the following :

3.1. Which one of the below is not the component in CAMEL Model ? 2

(A) Credit

(B) Management

(C) Assets

(D) Liquidity

3.2. Each rating obtained by the listed entity w.r.t. the non-convertible debt securities shall be reviewed at least once _______ by a credit rating agency registered by the Board. 2

(A) In a year

(B) Six months

(C) In a quarter

(D) In every two year

Marks

3.3. Which one of the following does not fall within the scope of Credit Rating ? 2

(A) Opinion on debt instrument

(B) Opinion on IPO

(C) Opinion on Commercial Paper

(D) Opinion on Holding and Subsidiary companies' transactions

3.4. Which of the below event will boost the sovereign credit rating ? 2

(A) Debt to GDP ratio accelerated in last 2 years

(B) The current central government has been third government in the last 2 years

(C) Current A/c Deficit has ballooned by 50% as compared to last year

(D) GDP growth has been highest in the G7 countries

3.5. Sovereign borrowings tend to be at the ______ yields in the market with the stronger countries paying ____ than the weaker ones. 2

(A) Lowest, higher

(B) Highest, Lower

(C) Lowest, Lesser

(D) Highest, Higher

3.6. You are required to prepare draft "Credit Rating Rationale" (Report) for J. Rover Automative Ltd. based on the information/data given, which can be put up directly to "Rating Committee" for review and approval.

Please prepare "Rationale/Report" in the following manner :

(A) Evaluation of Business Risk with detailed rationale on Industry Risk, Market Position & Operating Efficiency. 4

(B) Evaluation of Management Risk. 1

(C) Evaluation of Financial Risk based on solvency, Coverage, Capital Structure & Operation Cycle. 4

(D) Evaluation of Parent Support. 1

(E) Based on the above calculate "Credit Risk Rating Scoring" for 2

(i) Long Term Debt

(ii) Short Term Debt

(F) Final Rating (Action) with articulation for Outlook 3

(i) Long Term Debt

(ii) Short Term Debt

Marks

CASE STUDY 4

Arjun and Lakshman are students who have enrolled themselves for Graduation in Financial Services and Capital Markets in the University of Chicago. As part of this curriculum, both Arjun and Lakshman will be covering various aspects including Global financial markets, policy making and impact of policies, role of capital markets, institutions and intermediaries in capital markets, commodity markets, banking operations etc. amongst other things.

Whilst their focus during the study is largely global, Mr. Derek, their professor for economics wanted both Arjun and Lakshman to undertake a special task and present a paper for discussions amongst the professor community and fellow students. Mr. Derek mentioned that, India, as a country is going through a significant development in recent years and a number of new initiatives and policies have been undertaken currently. He also mentioned that, the economy in India is also seeing a slowdown currently and there could be an impact on the overall growth and output from industries.

Given the above, Mr. Derek mentioned to Arjun and Lakshman that, it will be of great interest and a source of knowledge for the students to understand the way the Indian financial services and capital markets are structured, in what way are the aspects fundamentally different from some of the global markets and their high level views on some of the policies and happenings in the market.

Both Arjun and Lakshman were super excited with this opportunity and realised that this is also a great opportunity to understand the Indian financial system in a better manner. As they started to prepare for the same, some of the aspects Mr. Derek wanted them to consider included the below items:

Global trends in capital markets - He particularly mentioned that technology plays an important role in evolution of the global capital markets recently.

Regulators in the financial markets and how those are different when compared to the regulators in India. For this purpose,

- Mr. Derek wanted both Arjun and Lakshman to focus on two of the main regulators in India in comparison to the Securities Exchange Commission (SEC) and the Fed in the US and why their operation strategies are different.
- In one of the conversations during the discussions which Arjun had with Mr. Derek, Arjun mentioned that he sees no reason why the Reserve Bank of India (RBI) should be any different when it comes to its approach as the Central Bank, in comparison to the approach of Fed. He said the Indian policy-makers need to just replicate the Fed in terms of its approach rather than customizing their decisions for India.
- Mr. Derek listened to Arjun but prompted Lakshman to look into the views of Arjun and share his thoughts with Mr. Derek.

Credit policy : Mr. Derek wanted both Arjun and Lakshman to look into what credit policy means in the context of the Indian economy, what would be the main objectives and analyze the same in greater detail.

- He said that for the purposes of the discussion, they should also analyze the credit policies adopted by some of the other emerging economies such as Brazil and South Africa and include the same in their overall analysis as this will help the students understand the concepts better.
- He was also prompting Arjun to look into the tools and policy objectives of Fed in the above context and how is that different when it comes to the overall elements of credit policy.

Computation of following indexes : Mr. Derek wanted Arjun and Lakshman to look into :

- Cost inflation index and how is the same to be computed
- Consumer price index and how is this to be arrived at.
- Wholesale price index and how is that used.

Marks

Determination of interest rates : Mr. Derek was very particular that Arjun and Lakshman understand and analyze the determination of interest rates in greater detail. He was keen for them to let the larger student community know, how in India the interest rates are regulated & how interest rates are determined. He said it would be great if both of them can also look at the regulation of interest rates in some of the comparable global economies and how is that different when it comes to India. Specifically, few of the aspects to be considered included :

- Libor
- Mibor
- T Bills of Government
- G-Sec etc.

Arjun was also keen that during this analysis, he wanted to analyze and cover some of the developments in the last few years in the form of **debt securitization** and **money market mutual funds**. He said securitization is the buzz word in some of the recent money market evolution and this would be of huge value to the student community to understand.

Institutions and intermediaries : Lakshman normally shows keen interest in understanding the role played by various institutions and intermediaries in the functioning of the capital markets and he did not want to let go of this chance to deep dive in understanding this better in the context of India. In particular, he told Arjun that he will take the lead in analyzing and presenting the following:

- Depository system
- Stock and commodity exchanges
- Intermediaries
- Institutional investors such as the merchant bankers, registrars to an issue, underwriters, bankers and debenture trustees
- FPIs
- Custodians
- Clearing houses

Marks

Arjun, for his part, mentioned that his interest in **commodity markets** is known to everyone and he will, accordingly take lead in analyzing the commodity markets in India and compare the same with the Global Practices. He said he will look into the key Indian commodity markets such as the MCX and NCDEX which comprise the primary trading platforms in India and also analyze how they operate.

- Arjun also indicated that he will look at the problems associated with the Indian commodity markets and understand the application of derivatives in commodities. In particular, he mentioned that the Indian commodity market is plagued by :
  - High speculation and fly by night operators
  - Trading without underlying
  - Lack of exponential growth that is required for the platforms to sustain it
  - Lack of connect of the farmers to the market
  - Political ramifications
- He said that whilst futures trading is exciting, it comes with certain specific conditions such as durability, homogeneity, free from control and frequent trading and this isn't always the case in a market such as India for all the key products.

Both Arjun and Lakshman held a discussion with Mr. Derek outlining the various aspects that they will be covering during the presentation. Mr. Derek was very impressed with the aspects identified though he mentioned that many of these aspects were arising out of the discussions they had with Mr. Derek himself.

Mr. Derek indicated to both Arjun and Lakshman that he will have a short discussion with them where he will ask them a few questions for them to respond to and also provide them with his additional thoughts questions so that they are better prepared for the final discussions and presentation. They are as follows :

Marks

4.1. Which technology is deployed to remove inefficiencies in the current international capital market structure by enabling capital market firms to create digital assets for private securities which will help in direct and immediate access by regulatory bodies ? 2

(A) Private Securities Blockchain Solution

(B) Robotic process automation

(C) Blockchain and Robotic process automation

(D) SAP

4.2. Liquidity is controlled in the economic system by: 2

(A) The RBI by resorting to sale of securities at times of excess liquidity

(B) The RBI by resorting to purchase of securities at times of excess liquidity

(C) The RBI through buying securities at times of tight liquidity

(D) The Government through buying securities at times of tight liquidity

4.3. Quantum channel relating to money supply and credit comprise of : 2

(A) Bank lending channel and balance sheet channel

(B) Bank lending channel and credit channel

(C) Bank lending channel and exchange rate channel

(D) Bank lending channel and asset price channel

4.4. Repo and Reverse Repo instruments used by RBI for : 2

(A) Under Repo, the RBI borrows from the commercial banks and under Reverse Repo, commercial banks borrow from RBI

(B) Under Repo, the RBI lends to commercial banks and under Reverse Repo, RBI borrows from commercial banks

(C) Under Repo, the RBI borrows from the commercial banks and under Reverse Repo, commercial banks lend to RBI

(D) Under Repo and under Reverse Repo, commercial banks borrow from the RBI

Marks

4.5. The regulation of commodity derivatives market is by : 2

(A) Securities and Exchange Board of India under Securities Contracts Regulation Act (SCRA), 1956

(B) Securities and Exchange Board of India under Forward Contracts Regulation Act (FCRA)1952

(C) Reserve bank of India

(D) Forward Markets Commission under Forward Contracts Regulation Act

4.6. Please write a Note for Students in the University of Chicago, explaining the following :

(A) The key elements of financial markets and what are the main functions of financial markets in India ? 2

(B) What are the various instruments of credit policy prevalent ? 2

(C) What are the basic differences between Wholesale price index and consumer price index ? Elaborate on the same with examples. 3

4.7. Is Arjun right in his view on the approach adopted by RBI in comparison to Fed ? What do you think should be the response that Lakshman provide to Mr. Derek ? 3

4.8. Do you agree with Arjun's view on the problems in commodity markets in India ? What do you think is the required solution for the same ? 2

4.9. Analyze whether futures trading on a commodity exchange is possible for the below products - explain stating why ? 3

- Petrol
- Zinc
- Pulses

Marks

CASE STUDY 5

You are a Partner in M/s. Advisor & Co., a firm of Chartered Accountants which specializes in providing advisory services to its clients on investments in mutual funds and also provides advice on fund raising etc.

Recently, Innovate Limited, promoted as a tech startup, has approached you in providing some advice in respect of its investments as well as its funding requirements. You had a meeting with Mr. Satya Prakash, the MD of the Company who has provided the below facts to you :

- The Company is involved in providing niche solutions in the customer management space for its customers through innovative solutions and technologies.
- The company has grown exponentially in the recent past and many of its customers are based out of the US and China. It also has further plans to grow and also to raise some funds by attracting potential investors.
- The Company has a huge cash balance in its Indian bank account and has retained the same as part of its current account balance and fixed deposits for a considerable period of time. The MD mentioned that he has heard about mutual funds, but is not sure if corporate entities can invest in mutual funds. He is also not too sure on which types of funds to choose, both from a risk and a return perspective.
- On the Mutual funds, the MD mentioned that he has heard some experiences of few of his start-up friends in other entities who have lost a considerable amount due to the effect of some large infrastructure companies failing and as such, wanted to avoid that scenario. He, therefore, wanted some inputs on factors to consider in selection of mutual funds.
- The MD wanted advice regarding venture capital funding for Innovate and also the types of funding that would be available and its suitability.
    - The MD mentioned that the Company is currently in the stage of enhancing its market and expanding further as it has been a year since it has broken-even.
    - He is also exploring options for a long term loan from banks, but since that may take a while, a temporary option of funding from a venture capital is also being explored.

Marks

- ❑ He does not prefer a mode where the venture capitalist has a say in the affairs of the company nor does he want them to acquire any stake in the entity.
- ❑ He has seen some of his fellow startups obtain mezzanine funding from the VCs, and he is keenly evaluating that as a possibility, he could consider.

- The MD was also keen in knowing whether they can issue debt instruments such as debentures for the purpose of raising funds. He mentioned that he is keen in exploring this option and also get the debenture listed in a stock exchange.

  But he wanted to understand what the additional compliance requirements on account of listings are.

- One of the aspects that the MD is evaluating is also to scale up its support activities such as finance, administration, HR etc., as it is currently run by a few individuals. He was curious to know if, there is a mandatory law which forces them to recruit qualified professionals or they can continue to run the company the way it is currently being managed.

- The MD provided you with additional facts of the business :
  - ❑ The company has about 600 employees currently
  - ❑ It operates from 3 locations in India and has sales offices abroad
  - ❑ The Company's ERP is a home grown ERP and they plan to move to a cloud based solution
  - ❑ The finance team is currently only 4 people and they follow cash basis of accounting
  - ❑ As much as the MD wants to scale up operations, he is also cost conscious and does not want to unnecessarily incur additional costs in man power.
  - ❑ He also wanted to check if outsourcing of the finance, treasury and accounts operations is an option.
  - ❑ Since a major portion of revenues come from abroad, he was keen in knowing applicability of those regulations to the entity.

The MD mentioned, given the above information, he would like you to prepare a brief report addressing some of his questions and meet up with him in a week's time.

Marks

5.1. The maximum cost that mutual funds can incur is ________ and any extra cost is borne by ________ : 2

(A) 2.5% of the portfolio and extra cost is borne by the investor

(B) 2.5% of the portfolio and extra cost is borne by the underlying companies in which mutual funds invest

(C) 2.5% of the portfolio and extra cost is borne by the asset management company

(D) 3% and extra cost is borne by the investors

5.2. Which of the below ratios is an appropriate measure of performance for an overall portfolio particularly when it is compared to another portfolio or another index such as S&P 500, Small Cap Index etc. 2

(A) Treynor Ratio

(B) Jensen's Alpha

(C) Sharpe Ratio

(D) Net asset value

5.3. A financing mode which is typically a hybrid of debt and preferred stock finance is known as : 2

(A) Early stage funding

(B) Working capital loan

(C) Mezzanine funding

(D) Expansion funding

5.4. Since they need to bear extremely high risks, their rate of returns are the highest. Which category is this: 2

(A) Angel investors

(B) Venture capital funds

(C) Mutual funds

(D) Investment banks

Marks

5.5. Credit ratings once issued : 2

(A) Need not be revised as this is given at a point in time

(B) Needs to be revised periodically irrespective of whether the rating has changed

(C) Rating agency shall during the lifetime of the securities rated by us, continuously monitor the rating of such securities and carry out periodic reviews of all published ratings

(D) Rating agencies will need to revise it on a quarterly basis.

5.6. Please prepare a detailed Note for MD of Innovate Limited., summarizing the following :

(A) The advantages of investing in a mutual fund. 2

(B) What would be the factors you would advise the MD before selecting the right mutual funds to invest in for short term tenor of Investments as well for Long Term tenor of Investments ? 3

(C) Provide your inputs on the various types of funding by a venture capitalist. And which mode will be best suitable to Innovate Limited ? 6

5.7. Please advise if Innovate Limited, can issue debt rather than raise further capital. And what additional regulations are to be considered for listing and is Innovate Limited currently geared up to meet the requirements ? 4
