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QP CODE 35298

~~SET~~ 2

Q1(A) State whether the following statement are true or false(8 MARKS)

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

Q1(B) Multiple choice questions(7 MARKS)

1-a, 2-d, 3-d, 4-d, 5-d, 6-a, 7-c, 8-a, 9-c, 10-a

Q2(A) Derivative is a contract that derives its value from an underlying assets such underlying asset can be any thing ranging from commodities to curries to stock etc. **(2 MARKS)**

Advantages of Derivatives**(5 MARKS)**

1. Leverage:
2. Manages the risk:

Disadvantages of Derivatives:

1. High volatility:
2. Requires expertise:
3. Contract life:

Q2(B) Participants in derivatives-hedgers, arbitrageurs,speculators

(7 marks for full explanation)

Q2(C) Types of derivatives are OTC(swap and forwards) and exchange trade(futures and options)

(8 marks for full explanation)

Q2(D) Derivative is a contract that derives its value from an underlying assets such underlying asset can be any thing ranging from commodities to curries to stock etc.

(3 marks explanation of derivatives with definition)

Factors driving the growth of Derivatives:-**(4 MARKS)**

¨ Increased volatility in asset prices in financial markets

¨ Increased integration of national financial markets with the international markets,

¨ Marked improvement in communication facilities and sharp decline in their costs,

¨ Development of more sophisticated risk management tools, providing economic agents

¨ A wider choice of risk management strategies, and

¨ Innovations in the derivatives markets, which optimally combine the risks and returns

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¨ Over a large number of financial assets leading to higher returns, reduced risk as well.

¨ Transactions costs as compared to individual financial assets.

Q3(A). Explain index (3 marks) and significance of index(5 marks)

Significance-

1. stock index is an indicator of the performance of overall market or a particular sector
2. Its benchmark for the performance of portfolio
3. Used as as financial application of derivatives

Q3(B)adjustment for corporate action

1. basis shall be such that the value of the position of market participants on cum and ex-date .

2. action carried on last day on which security is traded

Adjustment means modification to position or contract specification.(basis to be satisfied are-strike price, position, market lot)

Q3(C) Explain index management?(8 marks)

(full explanation of index construction, maintenance and revision process)

Q3(D) Types of stock market indices-(7 marks)

1. Weighted average market capitalization
2. Fee-float market capitalization index
3. Price weighted index
4. Equal weighted index

Q4(A)1. Explain Option And Option Trading Strategies

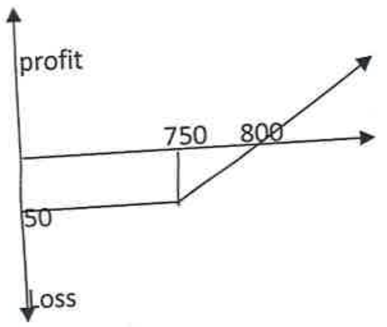
Meaning of option 3 marks

Option trading strategies-(explanation 5 marks)

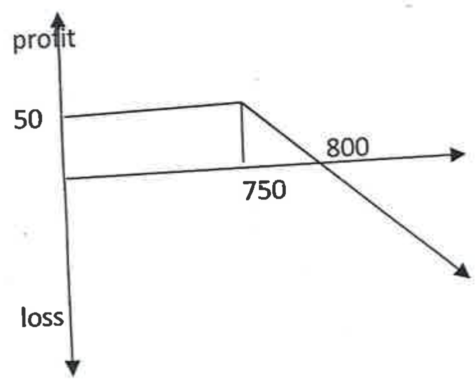
1. Spread(vertical spread, horizontal spread, diagonal spread)
2. Combination(straddle, strip, strap)
3. Synthetic(long, short)

3

Q4(B)payoff for buyers of call option-long call (3.5 marks)



Payoff for seller of call options-short call (3.5 marks)



OR

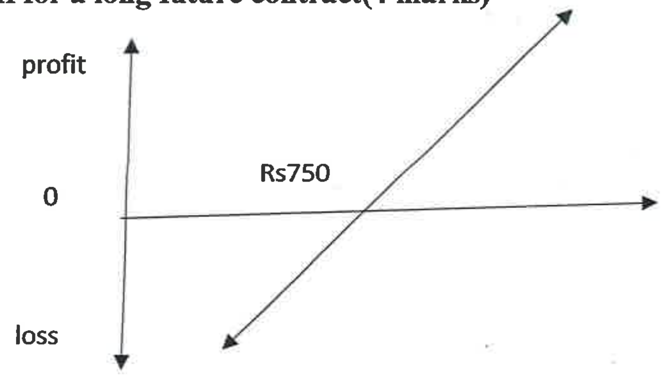
Q4(C) The call will expire worthless and investor losses the entire Rs.10,000 paid as premium

Q4(D)explain the term**(10 marks)**

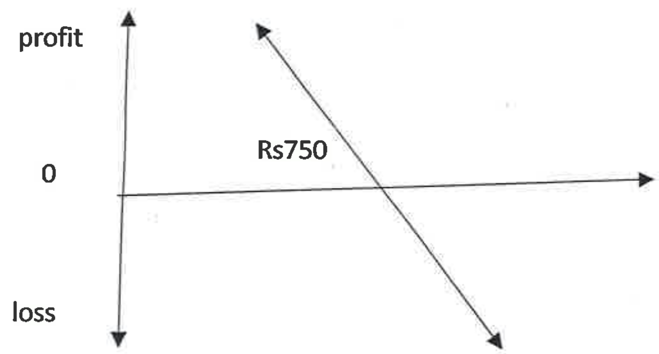
1. option price and premium- it is the price which the option buyer pays to the option seller.
2. intrinsic value-it the amount by which option is in the money before adjusting premium.
3. American option-the owner of such option can exercise his right at any time on or before the expiry date/day of the contract
4. Time value-it is differences between premium and intrinsic value
5. European option-the owner of such option can exercise his rights only on the expiry date of the contract.

Q5(A)

1.Payoff for a long future contract(4 marks)



Payoff for a short future contract(4 marks)



Q5(B)

(Meaning 2 marks)

Features of futures-(5 marks)

a) contract between parties through exchange
b) Trading platform
c) Free interactions of buyers and sellers
d) Margin are payable by both parties
e) Quality and quantity decided

Q5(C) EXPLAIN THE TERMS-(any 3)(15 MARKS)

1. Contract cycle- the period over which the future contract is traded.

2. Future price-the price at which the futures contract for such underlying asset trades in the future market
3. Expiry date-it is the date specified in the futures contract. Expiry date is the last day on which the contract will be traded
4. Marking to market- the margin account is adjusted to reflect the daily gain or loss of the investor depending upon the futures closing price.
5. Open interest-total number of contracts outstanding for an underlying assets.