SET - I

1

ANSWER-KEY

[Total Marks: 100

(3 Hours)

N.B. : (1) All questions are compulsory
(2) Each question carries equal (20) marks

1. Attempt the following :
[A] Explain following concepts (any Five) **(10)**

1. Direct financing.

   Direct finance is a method of financing where borrowers borrow funds directly from the financial market without using a third party service, such as a financial intermediary.

2. Money market.

   The **money market** is where financial instruments with high liquidity and very short maturities are traded. It is used by participants as a means for borrowing and lending in the short term, with maturities that usually range from overnight to just under a year.

3. Clearing House Function.

   As bankers' bank, the central bank acts as a clearing house for transfer and settlement of mutual claims of commercial banks. Since the central bank holds reserves of commercial banks, it transfers funds from one bank to other banks to facilitate clearing of cheques.

4. Repo Rate.

   The rate at which banks borrow money from the RBI by selling their surplus government securities to RBI is known as "Repo Rate." Repo rate is short form of Repurchase Rate. Generally, these loans are for short durations up to 2 weeks. Banks enter into an agreement with the RBI to repurchase the same pledged government securities at a future date at a pre-determined price.

5. Prime Lending Rate.

   The **interest rate** charged by banks to their largest, most secure, and most creditworthy customers on short-term loans. This **rate** is used as a guide for computing **interest** rates for other borrowers.

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6. Capital Adequacy Norm.

If banks have adequate capital, then it can protect its depositors from unforeseen contingencies as well promotes the stability and efficiency of financial systems. Capital Adequacy Ratio (CAR) is the ratio of a bank's capital in relation to its risk weighted assets and current liabilities. It is decided by central banks and bank regulators to prevent commercial banks from taking excess leverage and becoming insolvent in the process.

7. Deep discount bond.

A deep discount bond is a bond bought at a price significantly lower than its face value, with the face value repaid at the time of maturity. As it is issued at a substantial discount to its redemption value, it is largely substituting capital gain for income.

8. Convertible bonds.

A convertible bond is a type of debt security that can be converted into a predetermined amount of the underlying company's equity at certain times during the bond's life, usually at the discretion of the bondholder.

[B] Select most appropriate answer from the given alternatives: **(10)**
(Right answers are underlined)

1. Objective of the financial system is:
   a. **<u>To transfer funds from surplus economic unit to deficit economic unit</u>**.
   b. To transfer funds from money market to capital market.
   c. To transfer funds from deficit economic unit to surplus economic unit.

2. When financial institution is set up as per the requirements of the clients, it is called:
   a. Supply leading approach.
   b. **<u>Demand following approach</u>**
   c. None of the above.

3. Giving loans to the public is one of the functions of :
   a. Reserve Bank of India.
   b. **<u>Commercial Banks in the country.</u>**
   c. Central Bank of the country.

4. Under Marginal Standing Facility, the banks can borrow funds from the RBI:
   a. For a period of one month to six months.
   b. For a period of six months to one year.
   c. **<u>For an overnight period.</u>**

5. Which one is not an objective of the Monetary Policy:
   a. **<u>Reduction in the fiscal deficit.</u>**
   b. Reduction in income inequality.

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c. Reduction in the rising prices.

6. Reduction in the SLR by the Central Bank:
   a. Increases the loan giving capacity of the commercial banks.
   b. Reduces the loan giving capacity of the commercial banks.
   c. **Only alters the composition of loans between private sector and the government.**

7. Narsimham Committee, 1991 has recommended for :

   a. **No further nationalization of commercial banks.**
   b. Further nationalization of commercial banks.
   c. None of the above.

8. Narsimham Committee, 1998 has recommended for :

   a. Broad banking.
   b. **Narrow Banking.**
   c. None of the above.

9. An investor gives the funds permanently to the firm, when he purchases :

   a. Bond.
   b. Debenture.
   c. **Equity.**

10. In floating rate bond, the coupon is :

   a. **Tied to some reference rate in the money market.**
   b. Tied to inflation rate in the country.
   c. None of the above.

2. **Attempt any two of the following :** **(20)**
   a. Explain the components of the financial system.
   Financial institutions, financial ~~institutions,~~ financial markets and Financial services.
   instruments

   b. Explain the role of the financial system.

   - Financial intermediaries enhance the **investment** in the economy, by the means of the direct and indirect investments
   - The process of transferring the **monetary resources** of the public into the financial resources by the financial intermediaries involves maturity intermediation, risk reduction through diversification, reducing costs of transaction and provides a payment mechanism, which in turn is the sole objective of the financial market.

   c. Examine the indicators of financial development.

Financial Interrelations Ratio (FIR), Finance Ratio (FR), Intermediation Ratio (IR) and New Issue Ratio (NIR).

3. **Attempt any two of the following :** **(20)**

a. Discuss the objectives of monetary policy of the RBI.

Economic growth, Price Stability, Full employment, Social Justice and Exchange Rate Stability.

b. Explain quantitative instruments of monetary policy of the RBI.

Bank Rate, Open Market Operations, CRR, SLR and Moral Suasion.

c. Discuss Narsimham Committee Report,1998.

Highlight major recommendations in the field of commercial banking for increasing competition, efficiency and profitability.

4. **Attempt any two of the following :** **(20)**

a. Examine commercial banking developments in India since mid-1980s.

Highlight the changes in the commercial banking structure as well as their functions due to recommendations of Narsimham Committee Reports, 1991 & 1998.

b. Discuss the management of NPAs of commercial banks in India.

The Debt Recovery Tribunals (DRTs) - 1993 , Credit Information Bureau - 2000, Lok Adalats - 2001, Compromise Settlement - 2001, SARFAESI Act - 2002, ARC (Asset Reconstruction Companies), Corporate Debt Restructuring - 2005, Joint Lenders Forum - 2014, Mission Indradhanush - 2015,

c. Give an overview of NBFCs in India.

A Non-Banking Financial Company (NBFC) is a company registered under the Companies Act, 1956 engaged in the business of loans and advances, acquisition of shares/stocks/bonds/debentures/securities issued by Government or local authority or other marketable securities of a like nature, leasing, hire-purchase, insurance business, chit business but does not include any institution whose principal business is that of agriculture activity, industrial activity, purchase or sale of any goods (other than securities) or providing any services and sale/purchase/construction of immovable property.

A non-banking institution which is a company and has principal business of receiving deposits under any scheme or arrangement in one lump sum or in instalments by way of contributions or in any other manner, is also a non-banking financial company (Residuary non-banking company).

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NBFCs are categorized a) in terms of the type of liabilities into Deposit and Non-Deposit accepting NBFCs, b) non deposit taking NBFCs by their size into systemically important and other non-deposit holding companies (NBFC-NDSI and NBFC-ND) and c) by the kind of activity they conduct.

5. **Attempt any two of the following :** **(20)**

   a. Explain the significance of equity as a financial instrument.
   Explain the ~~features~~ merits of equity ~~to~~ from the company and ~~to~~ from the investor.

   b. Discuss hybrid financial instruments.

   A single financial security that combines two or more different financial instruments. Hybrid securities, often referred to as "hybrids," generally combine both debt and equity characteristics.

   Preference Capital, Warrant, Convertible Debenture

   c. Explain different types of bonds.

Floating rate bonds, zero interest bonds, deep discount bonds, inverse float bonds & inflation index bonds

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