C 4880 **(Pages : 4)** **Name**

Reg. No.................

SECOND SEMESTER M.A. DEGREE EXAMINATION, JUNE 2016

(CUCSS)

Applied Economics

Optional I—SECURITY ANALYSIS AND PORTFOLIO MANAGEMENT

Time : Three Hours Maximum : 36 Weightage

Part A

Answer **all** *questions.*
Each bunch of **four** *questions carries a weightage* of **1.**

(A) Multiple Choice :

1 Although derivatives can be used as speculative instruments, businesses most often use them to

(a) Hedge.
(b) Offset debt.
(c) Attract customers.
(d) Enhance their balance sheets.

2 In words, the real rate of interest is approximately equal to :

(a) The inflation rate minus the nominal rate.
(b) The nominal rate minus the inflation rate.
(c) The inflation rate divided by the nominal rate.
(d) The nominal rate plus the inflation rate.

3 Which of the following statements regarding risk-averse investors is true ?

(a) They only accept risky investments that offer risk premiums over the risk-free rate.
(b) They accept investments that are fair games.
(c) They only care about rate of return.
(d) They are willing to accept lower returns and high risk.

4 A liquid asset may be :

(a) Converted into cash.
(b) Be converted into cash with little chance of loss.
(c) Not be converted into cash.
(d) Not be converted without loss.

Turn over

(B) Multiple Choice :

5 All things equal, diversification is most effective when ________

(a) Securities' returns are positively correlated.

(b) Securities' returns are uncorrelated.

(c) Securities' returns are high.

(d) Securities' returns are negatively correlated.

6 Risk that cannot be avoided, regardless of how much you diversify is called :

(a) Systematic risk. (b) Unique risk.

(c) Residual risk. (d) Diversifiable risk.

7 What is the risk premium of a stock that has an expected return of 20 %, assuming the rate of return on Treasury bills is 3 % ?

(a) 20 %. (b) 23 %.

(c) 17 %. (d) Cannot be determined.

8 The efficient portfolio concept was introduced by :

(a) Markowitz. (b) Samuelson.

(c) Hamilton. (d) Cootner.

(C) Fill in the blanks :

9 A stock's sensitivity to changes in the values of the market portfolio is known as ________

10 Common stock portfolios that offer the highest expected return for a given standard deviation are known as ________

11 The risk of a well-diversified portfolio depends on the ________ risk of the securities included in the portfolio.

12 Risk is usually measured by the variance of the returns or the ________, which is simply the square root of the variance.

(D) State True *or* False :

13• Beta measures the marginal contribution of a stock to the risk of the market portfolio.

14 If a stock lies below the security market line, it is undervalued.

15 Investors prefer diversified companies because they are less risky.

16 If stocks were perfectly positively correlated, diversification would not reduce risk.

(16 x $\frac{1}{4}$ = 4 weightage)

Part B (Short Answer Questions)

Answer any **ten** *questions not exceeding* **one page** *each.*
Each question carries a weightage of 2.

17 How is standard deviation used to determine risk ?

18 Discuss the basic tenets of Dow theory.

19 Explain the concept of valuation of securities. Why is it important in financial decision-making ?

20 How do you calculate the expected rate of return of a security ?

21 What factors influence the beta of a share ? Explain.

22 Illustrate the method of calculation of the portfolio return and risk for a two-security portfolio.

23 Explain the random walk hypothesis.

24 Explain systematic and unsystematic risks with examples.

25 Briefly discuss the portfolio management practices in India.

26 An asset has the following possible returns with associated probabilities :

Possible returns	20 %	18 %	8 %	0	– 6 %
Probability	0.10	0.45	0.30	0.05	0.10

Calculate the expected rate of return and the standard deviation of the rate of return.

27 Explain the difference between primary market and the secondary market.

28 "Highly variable stock prices suggest that the market does not know how to price stocks". Comment.

(10 x 2 = 20 weightage)

Part C (Essay Questions)

Answer any **three** *questions not exceeding* **three pages** *each.*
Each question carries a weightage of 4.

29 Explain the concept of the capital market efficiency. What are the different forms of the capital market efficiency ?

30 Describe some significant developments in Indian capital market. What are their implications for financial management ?

31 Elucidate Cootner's price value interaction model.

Turn over

32 Discuss the capital asset pricing model. Explain its assumptions and implications.

33 The probability distribution for the returns on stocks A and **B** provided below :

State	*Probability*	*Return on Stock A*	*Return on Stock **B***
1	20%	5%	50%
2	30%	10%	30%
3	30%	15%	10%
4	20%	20%	– 10 %

(a) Calculate the expected returns on stocks A and **B.** Which stock has the highest expected return ?

(b) Calculate the Variance and Standard Deviation on Stocks A and **B.** Which stock is more risky ?

(3 x 4 = 12 weightage)