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Question: A bond has a **par value of ₹1,000**, a **coupon rate of 12% per annum**, and a **maturity period of 3 years**. However, the bond pays **interest semi-annually**. The **required annual rate of return is 10% (compounded semi-annually)**.

Calculate the **value of this bond**, assuming reinvestment of coupons at the required rate.

$n = 3 \times 2 = 6$
$r = 10\%/2 = 5\%$
$C = 12/2 = 6\%$

0 | 0.5 | 1 | 1.5 | 2 | 2.5 | 3

📘 **Options**:

A. ₹1,052.64

B. ₹1,074.61

C. ₹1,088.40

D. ₹1,100.25

$= 60\,[PVIFA, 5\%, 6] + 1000\,[PVIF, 5\%, 6]$

$60 \times 5.0756 + 1000 \times 0.746 = \boxed{1050}$

$CY = \frac{\text{Coupon Intt}}{\text{Current market price}}$

$\frac{750}{9400}$

Question: A bank holds a bond with a **face value of ₹10,000** and a **coupon interest rate of 7.5% p.a.** The bond is currently **quoted in the market at ₹8,800**. Six months later, the market price of the bond rises to **₹9,400**

8.52%

7.97%

(a) Calculate the **initial current yield** and the **new current yield**.

(b) What is the **percentage change in current yield** over the six-month period?

$\boxed{-6.4553\%}$

$\frac{7.97-8.52}{8.52} \times 100\%$

A. Initial: 8.52%, New: 7.98%, Change: -6.34%

B. Initial: 8.25%, New: 8.00%, Change: -3.03%

C. Initial: 8.52%, New: 8.00%, Change: -6.10%

D. Initial: 8.75%, New: 8.00%, Change: -8.57%

Question: Mr. B invested in a **₹5,000 face value bond** carrying a **coupon rate of 7% per annum**. He purchased the bond at **₹5,200** and sold it exactly **1 year later** at **₹5,350**.

👉 Calculate the following:

Face value → 5000 × 7% = 350

1. **Coupon Income received during the year**
2. **Capital Gain**/loss

5350 − 5200 = +150 Capital gain

3. **Rate of Return (RoR)** 9.61%

$$\frac{350+150}{5200} \times 100\%$$

9

4. **Current Yield (CY)**

C.I / 5350

$\frac{350}{5350} \times$

📘 **Options**:

A. Coupon = ₹350, Capital Gain = ₹150, RoR = 9.62%, CY = 6.73%

B. Coupon = ₹350, Capital Gain = ₹150, RoR = 9.04%, CY = 6.25%

C. Coupon = ₹350, Capital Gain = ₹100, RoR = 8.65%, CY = 6.73%

D. Coupon = ₹350, Capital Gain = ₹150, RoR = 9.62%, CY = 7.00%

Junk bonds → Highest Risk carrying

Zero Coupon Bond → No Coupon

issued at discount

1000 → 5 year, 0% Coupon

900 → 1000

Intrinsic yield

CMP → 920, FV → 1000, Coupon → 9% p.a, n = 6 years

Question: A bond with a **par value of ₹1,000** is currently trading in the market at **₹920**. It carries a **coupon rate of 9% per annum (annual payments)** and has a **maturity period of 6 years**.

Calculate the **Yield to Maturity (YTM)** assuming the investor holds the bond till maturity.

$920 = 1000(PVIF, Kd\%, 6) + 90(PVIFA, Kd\%, 6)$

📘 **Options**:

A. 9.55%

B. 10.21%

C. 9.85%

D. 10.50%

[Hit & trial]

[CMP < FV] ⟹ $\boxed{RoR > CR}$

Kd% → 10%, 12%

Kd% → 10%

$PV_1 = 1000[PVIF, 10\%, 6] + 90[PVIFA, 10\%, 6] = 956.44$

Kd% → 12%

$PV_2 = 1000[PVIF, 12\%, 6] + 90[PVIFA, 12\%, 6] =$

$= 1000 \times 0.50663 + 90 \times 4.11 = \boxed{876.65}$

$Kd\% = \text{Lower DR} + [DR_2 - DR_1]\left[\frac{PV_1 - CMP}{|PV_1 - PV_2|}\right]$

$= 10 + 2\,\frac{956.44 - 920}{|956.44 - 876.65|} = 10.91\%$

79.79

990 ← −10 1000 +25 → 1025

Theorem	Condition	Effect on Bond Value
1	YTM = Coupon Rate	Value = Par PV = FV
2	YTM > Coupon	Value < Par (Discount)
3	YTM < Coupon PV	Value > Par (Premium) FV
4 & 5	As maturity nears, premium/discount declines	Price approaches Par
6	YTM ↑ ⇒ Price ↓ (inverse relationship)	Always true
7	Longer maturity = more sensitive to YTM changes	Price drop/rise is higher
8	YTM ↓ vs ↑ → Price rise > fall (asymmetry)	Convex price-yield curve
9	Lower coupon bonds = higher price sensitivity	Greater % change
10	Higher YTM bonds are more impacted by YTM rise	Larger % drop for higher-YTM bonds

Impact of YTM vs. Coupon Rate (Basic Theorem Application)

📘 A 4-year bond has a face value of ₹100, coupon rate of 10%, and the required rate of return is also 10%. What would be the value of this bond?

Coupon = ROR ⇒ PV = FV

A. ₹104

B. ₹96

C. ₹100

D. ₹98

Discount Bond Valuation

A 3-year bond has a face value of ₹100, a coupon rate of 9%, and the required return is 11%. Which of the following is true about its valuation?

C.R 9% < RoR 11%

$\boxed{PV < FV}$

A. Value > ₹100

B. Value = ₹100

C. Value < ₹100

D. Value = ₹0

Premium Bond Behavior Near Maturity

📘 **A 3-year bond with face value ₹100 and coupon 10% is bought when YTM is 8%. What happens to the bond's price as it approaches maturity?**

10% > 8%

PV > 100

Premium

A. Price increases above ₹100

B. Price decreases and converges toward ₹100

C. Price stays above ₹100

D. Price becomes zero

100

Maturity Impact on Price Sensitivity

📘 **Bond A and Bond B both have a face value of ₹100 and a coupon of 12%. Bond A matures in 4 years and Bond B in 6 years. YTM increases from 12% to 13%. Which bond's price will decline more in percentage terms?**

A. Bond A

B. Bond B

C. Both decline equally

D. Cannot be determined

Asymmetry in Price-Yield Curve

📘 **A 3-year bond with ₹100 face value and 10% coupon is affected by a 1% change in YTM. Which of the following is true?**

A. Price rise (YTM ↓ 1%) equals price fall (YTM ↑ 1%)

B. Price fall is more than price rise

C. Price rise is more than price fall

D. No change in price

Comparing High vs Low Coupon Bonds for Volatility

📘 **Two 3-year bonds (Face Value ₹100) have coupons of 12% and 10% respectively. YTM rises from 12% to 13%. Which bond shows a greater percentage price change?**

A. 12% Coupon Bond

B. 10% Coupon Bond

C. Both same

D. Depends on PVIFA values

Yield Effect on High vs Low YTM Bonds

Bond A has YTM of 10%, Bond B has YTM of 15%. Both are 5-year, ₹100 face value bonds with 12% coupons. YTM increases by 20%. Which bond experiences greater price decline?

A. Bond A

B. Bond B

C. Both fall equally

D. No change as coupon is same

🔶 📘 Macaulay Duration – Summary Table with Examples & Icons

🔢 Concept	📖 Explanation	📊 Formula / Rule
📌 **Definition**	Weighted average time to receive bond cash flows 📅	Duration=∑(PV×T)∑PV\text{Duration} = \frac{ \sum (PV \times T)}{\sum PV} $\frac{\sum PV \cdot T}{\sum PV}$
🧮 **Macaulay Duration Formula**	Present value weighted time of all cash flows	Duration = Σ(PV × Time) / Σ(PV)
🧠 **Modified Duration**	Measures % change in bond price for 1% change in YTM	$MD = \frac{D}{1+\gamma}$ Modified Duration=Macaulay Duration(1+r)\text{Modified Duration} = \frac{\text{Macaulay Duration}}{(1 + r)} $\gamma = \frac{YTM}{n}$
🧾 **Zero-Coupon Bond**	Pays only face value at maturity	Duration = Maturity
🔁 **Perpetual Bond** Imp.	Infinite maturity, never repaid	Duration = (1 + r) / r
🔄 **Coupon Frequency Effect**	More frequent = lower duration	Semi-annual < Annual duration
⬇️ **High Coupon Effect**	Higher coupon = lower duration	Inverse relationship
⬆️ **YTM Effect**	Higher YTM = lower duration	Duration and YTM inverse
📉 **Maturity Effect**	Duration ↓ as bond nears maturity	Duration compresses over time
🔁 **Reinvestment Assumption**	Coupons reinvested at market rate	Core assumption in duration

📝 Key Takeaways Table 🧠

📌 Feature	🔍 Impact
⏱️ **Longer maturity**	➕ Higher duration
💸 **Higher coupon**	➖ Lower duration
📈 **Higher YTM**	➖ Lower duration
♻️ **More frequent payments**	➖ Lower duration
⌛ **Nearing maturity**	➖ Duration declines
📦 **Zero coupon**	Duration = Maturity
♾️ **Perpetual bonds**	Duration = (1 + r) / r

Bond → FV → ₹100, coupon Rate → 8% yearly

maturity → 5 years YTM → 6% Duration, MD,

(T) A	[C.F] B	C [PVF]	(PV) D=B×C	PV.T E=A×D
1	8	0.94	7.52	7.52
2	8	0.89	7.12	14.24
3	8	0.84	6.72	20.15
4	8	0.79	6.32	25.28
5	$\underbrace{100+8}$ → 108	0.75	81	405

Q2

$$D = \frac{\Sigma PV.T}{\Sigma PV}$$

$$= \frac{472.37}{108.68} = 4.34 \text{ years}$$

Q1 $\Sigma PV = 108.68$ present value of bond

$\frac{472.37}{\Sigma PV.T}$

Q3

$$MD = \frac{D}{1+Y} = \frac{4.34}{1.06} = 4.10$$

Q4 YTM ↓ 1% % Change in price of bond

$= 1\% \times MD = 1 \times 4.10\%$

$= 4.10\%$ ↑

Q5 → What will be the new Bond price? $\boxed{113.13}$

Bond prices are inversely related to YTM

YTM ↓ BP ↑

✅ **SECTION A: CONCEPTS OF WORKING CAPITAL (Q1–Q5)**

Q1. A firm has current assets of ₹15 lakh and current liabilities of ₹9 lakh. Which of the following best defines the net working capital in this context?

A. ₹24 lakh

B. ₹6 lakh

C. ₹15 lakh

D. ₹9 lakh

$NWC = CA - CL$

$= 15 - 9 = 6$

Trading → WC need

Q2. A company is operating in the trading sector and holds minimal fixed assets. Which of the following statements is most accurate regarding its working capital needs?

A. It will need more fixed capital than working capital.

B. It will have balanced needs between fixed and working capital.

C. It will need significantly more working capital than fixed capital.

D. It will require negligible working capital.

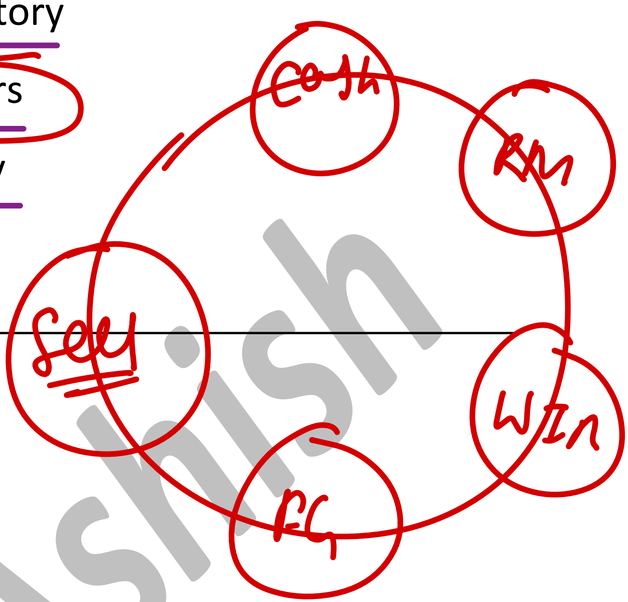
Q3. Which factor would likely cause an increase in a company's working capital requirement?

A. Implementation of just-in-time inventory

B. Extension of credit terms to customers

C. Reduction in finished goods inventory

D. Increase in prepaid expenses



Q4. Public utility services generally require minimal working capital. Why?

A. They receive government subsidies

B. They have large reserves

C. They sell mostly on cash basis

D. Their current liabilities are always zero

Q5. Which of the following best describes the working capital cycle?

A. The time taken to pay off long-term loans

B. The period between purchase of raw material and receipt of cash from sales

C. The gap between two financial years

D. The duration for preparing the balance sheet

✅ SECTION B: SOURCES OF WORKING CAPITAL (Q6–Q12)

Q6. Which of the following is not typically a component of gross working capital?

gwc → total CA

A. Receivables CA

B. Cash CA

C. Stock CA

D. Debentures LTL ✓

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Current liabilities

Q7. Accrued salaries appearing in the balance sheet are considered as:

25th march

accrued

A. Long-term liabilities

B. Operating expenses

C. Short-term liabilities ✓

D. Reserves

10th April

Q8. Which of the following is true about trade credit?

A. It must be repaid within the same day

B. It is regulated by the RBI

C. It's a short-term financing facility from suppliers

D. It requires collateral security

Q9. A company prefers to negotiate a reduced credit period in exchange for discount. This decision implies:

A. Liquidity crunch

B. Idle cash position

C. Poor credit rating

D. Negative working capital

₹1000 → 950

3M → 1M

---

excess liquidity → discount

Q10. Public deposits are not regulated by the RBI in terms of interest rate. What governs their terms instead?

A. SEBI

B. Companies Act 2013

C. Ministry of Finance

D. MSMED Act 2006

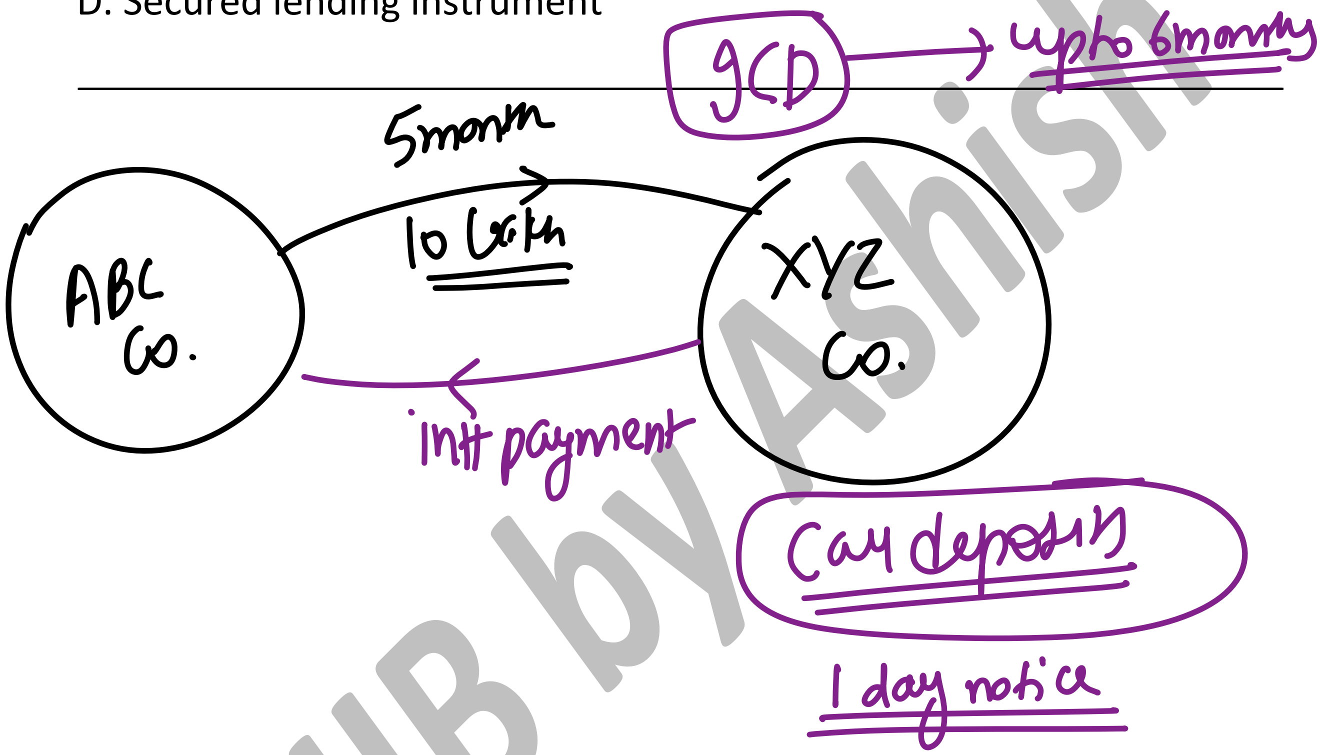
Q11. Which of the following features distinguishes inter-corporate deposits from public deposits?

A. Higher interest rate

B. Deposits accepted from public

C. Deposits accepted from another company

D. Secured lending instrument



Q12. Which of the following is **true** regarding Commercial Papers?

A. They are issued in physical format

B. Minimum maturity is 30 days

C. Issued at premium to face value

D. Minimum rating required is A3

✅ **Correct Answer: D. Minimum rating required is A3**

Explanation:

CPs must be rated A3 or above and are issued at a discount in demat form.

Company ABC → Commercial paper

unsecured MM instrument

promissory note

CC/OD

max — 1 year

min — 7 days

TNW ≮ 4 crore

WC → std

Loan → standard category

Credit Rating → CRA [SEBI]

Investment grade

min. A3

Secondary market

↳ OTC

No loan against CP

Buy back CP After 30 days

✅ SECTION C: MODES OF WORKING CAPITAL FINANCING (Q13–Q19)

Non fund Based

Q13. A letter of credit issued by a bank falls under which category?

A. Fund-based working capital finance

B. Non-fund-based ~~working capital finance~~

C. Long-term capital

D. Investment credit

CC/OD

L/C, BG, Co. acceptance

---

account receivable factoring

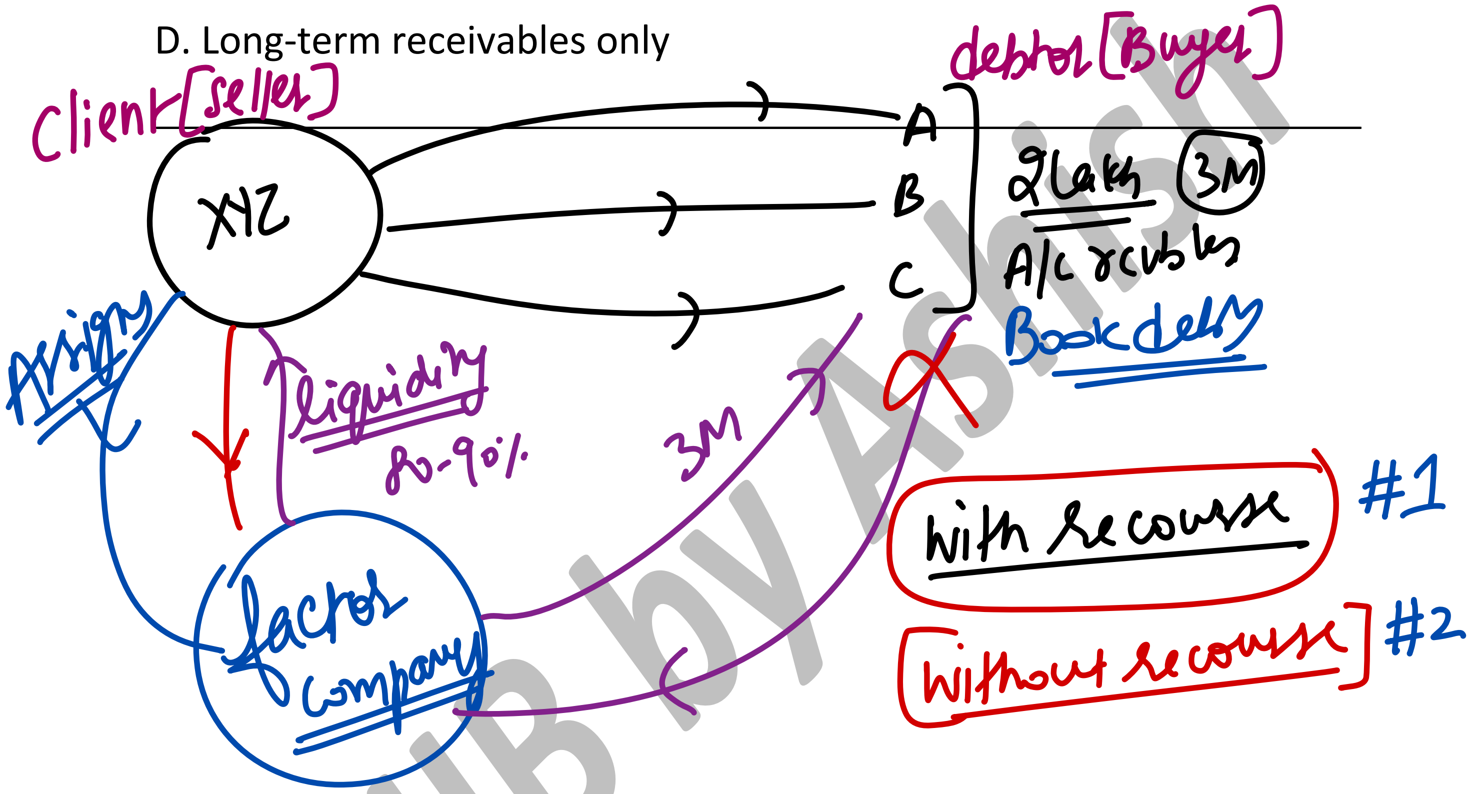
Q14. Which of the following is a feature of factoring but not forfaiting?

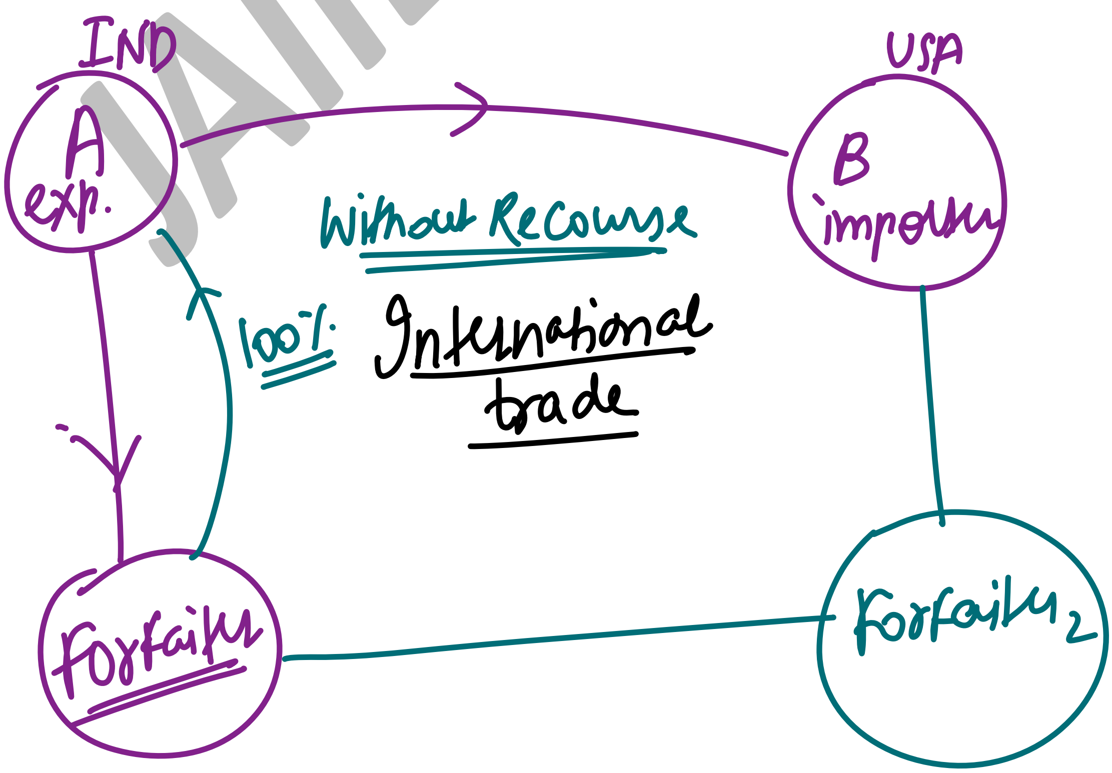
A. Involves only international trade

B. Recourse basis applicable

C. 100% finance provided

D. Long-term receivables only





Q15. In forfaiting, the exporter gets:

A. Partial finance with recourse

B. Full finance on non-recourse basis

C. No finance until maturity

D. Credit from banks with collaterals

Q16. Banks cannot directly participate in factoring services due to:

A. RBI prohibition

NBFC

B. High risk of default

C. Asset classification rules

D. SEBI restrictions

Q17. Which of the following defines a 'call deposit' in inter-corporate lending?

A. Withdrawal only after 6 months

B. Can be withdrawn by giving 1-day notice — Ans

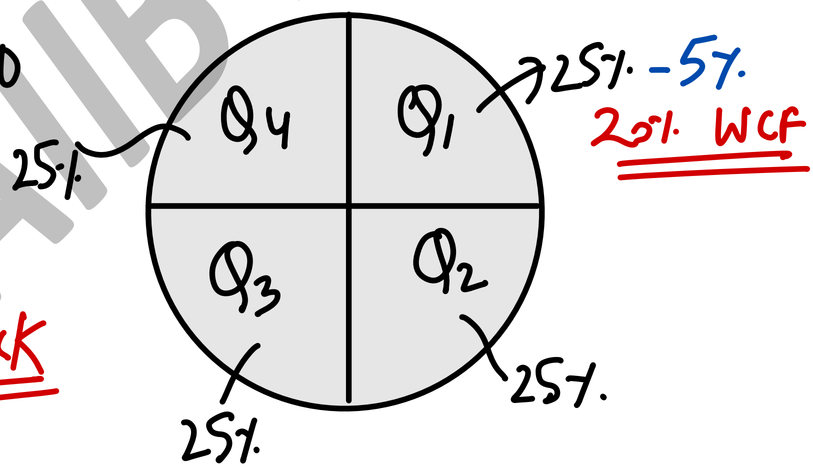
C. Convertible into equity

D. Cannot be withdrawn before maturity

Nayak Committee

→ PATO

100%



-5%

20% WCF

PATO → 50 lack

50x20%

= 10 lakh

CBM → Cash Budget management

C/O → 200 L

C/I → 150 L

deficit → 50 L

Q18. Which of the following would best suit financing a seasonal business like sugar production?

A. Tandon 2nd method

B. Cash budget method

C. Turnover method

D. Bill discounting

Method - II   min CR → 1.33:1

MPBF-II → WCG - 25% of TCA

⇒ WCG = TCA - [TCL - BB]

= 370 - [350 - 200] = 220

⇒ 220 - (25% of 370)

= 127.5

excess Bor

200 - 127.5

$\boxed{72.5}$

Method I

→ margin → 25% of WCG

MPBF-I → $\boxed{\text{WCG - 25\% of WCG} \quad \text{75\% of WCG}}$

min CR → 1.17:1

TCA

TCL

BB

[TCL other than BB]

OCL = CL - BB

WCG → TCA - OCL

TCA → 370, TCL = 350, BB = 200

$\boxed{OCL = 350 - 200 = 150}$

WCG = TCA - OCL

= 370 - 150 = 220

MPBF-I = WCG - 25% of WCG

$\boxed{= 165}$

excess $\boxed{35}$

Q19. Working capital advance in the form of discounting bills is considered:

A. Non-fund-based

B. Long-term credit

C. Fund-based

D. Not a bank product

~~Kite Flying~~

~~Accomodation Bills~~

✅ SECTION D: BANK ASSESSMENT METHODS (Q20–Q25)

Q20. Tandon Committee's 1st method calculates permissible bank finance as:

MPBF I → $\boxed{\text{WCG} - 25\% \text{ of WCG}}$

A. 25% of total liabilities

B. 25% of working capital gap

C. 25% of core current assets

D. 75% of long-term assets

None of the

Q21. Under Tandon 2nd method, excess bank borrowing indicates:

A. Surplus net worth

B. Undrawn cash credit

C. Borrowing more than permissible limit

D. Compliance with margin requirement

M-II → WCG – 25% of TCA

Q22. Which of the following is a core assumption of Nayak Committee Method?

projected Annual Turnover

50 → 70

A. Cash budget is prepared

B. Only long-term liabilities are used

C. Turnover is projected and used

D. Credit rating determines finance

Q23. Under Nayak Committee method, working capital limit is:

A. 25% of annual turnover

B. 20% of annual turnover + [5% of ATO]

C. 15% of annual turnover

D. 5% of projected profit

Q24. What is the margin requirement under the turnover method?

A. 0%

B. 5%

C. 10%

D. 15%

Q25. Which of the following methods is most suitable for IT project financing?

A. Tandon Method

B. Turnover Method

C. Cash Budget Method

D. Inventory Holding Method

→ seasonal

→ cash flow statement deficits

✅ SECTION E: CONCEPTUAL INTEGRATION & DIFFICULT (Q26–Q30)

Q26. Which of the following combinations **correctly match** source and nature of finance?

a) Trade Credit – Non-fund based

b) Letter of Credit – Fund based

c) Factoring – Recourse basis

d) Public Deposits – Unsecured

A. a, b and c

B. a, c and d

C. b and c only

D. b, c and d

Q27. Which of the following statements is **incorrect** in context of Commercial Paper issuance?

a) Can be issued in multiples ~~of ₹1 lakh~~ 5 Lakh or multiple thereof

b) Buyback allowed after 30 days

c) Loan against CP not allowed

d) Minimum rating must be A3

A. a only

B. a and b

C. b and d

~~D. All are correct~~

None of the above

Q28. Identify the incorrect match:

a) Forfaiting – Non-recourse

CL b) Accruals – Short-term source

c) Inter-corporate deposits – ~~RBI regulated~~

d) Factoring – Subsidiary led by banks

A. a and b

B. c only

C. b and d

D. All are correct

Q29. Which of the following are true about working capital advance?

NFB LC ≠ WC

a) Can be overdraft or loan

b) Includes letters of credit

c) Is always secured

d) Is used to fund fixed assets

A. a and b only

B. a, b and c

C. b and d only

D. a, c and d

Q30. Which of the following statement combinations are true?

WCFB → 5 crore
non-SSI → 2 crore

a) CP must be in dematerialised form

b) Turnover method is for units with WC up to ₹10 crore

c) Factoring involves three parties client, debtors, factor

d) ~~Tandon's 3rd method finances 25% of total CA~~

A. a, b, c

B. a, c, d

C. b, c, d

D. ~~All of the above~~ a, c

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✅ MCQs Based on Equipment Leasing

Q1. In the context of equipment leasing, which of the following statements best justifies why leasing does not reduce a firm's asset availability?

A. Leasing transfers ownership to the lessee

B. Leasing converts fixed assets into current assets

C. Leasing allows usage without ownership while preserving asset access

D. Leasing eliminates the need for financing

Q2. As per Ind AS 116, a lease must be classified as a finance lease when:

A. The lessee uses the asset for over 50% of its economic life

B. The lessor receives regular payments

C. Risks and rewards of ownership are transferred to the lessee

D. Lease rental exceeds 25% of asset's value

---

lease → finance lease

lease → operating lease

finance/sale/capital lease

[finance]

8 year

A lessor → machinery → B lessee

10 year

Q3. Which among the following is **not** a typical condition under which a lease is classified as a finance lease?

A. Lessee has an option to purchase at fair market value Ans

B. Lease covers major part of economic life

C. Present value of lease payments ≈ Fair value of asset

D. Asset is of specialized nature for lessee's use only

---

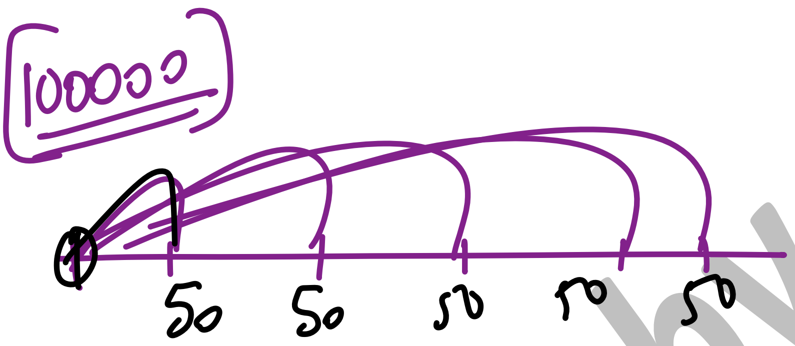
finance lease?

1) ownership tfr

2) option to purchase asset

3) lease term = major portion of econ

4)



Q4. Which one of the following distinguishes an operating lease from a finance lease?

A. Lease period covers entire economic life

B. Asset ownership is transferred

C. Lessee bears cost of maintenance

D. Substantial risks and rewards are **not** transferred Answer

---

Q5. In a **wet lease**, what is the primary role played by the lessor in addition to asset leasing?

A. Providing accounting support

B. Operating, insuring, and maintaining the asset Ans B

C. Taking security deposits

D. Collecting GST on rental value

[lessor will operate the equipment]

leverage

Q6. A lease is classified as an **international lease** when:

A. The lease agreement is written in foreign language

B. The lessee pays in foreign currency

C. Any one party is not domiciled in India / cross border lease

D. Asset is manufactured abroad

---

lender

leased Asset

A → B

Ownership → possession

Q7. Which type of lease agreement is most likely to contain terms that restrict the lessee from re-leasing the asset?

A. Dry Lease operations by lessee

B. Sub-Lease Term

C. Sale and Leaseback

D. Cancellable Lease

only ownership is transferred and not possession

Q8. One major **financial benefit** of leasing for a firm is:

A. Lower depreciation cost

B. Reduction in interest rate risk

Ans C. Avoidance of debt visibility in balance sheet (under operating lease)

D. Reduction in turnover tax liability

Asset

Fixed Asset

~~Capital Ex~~

Revenue expenditure

Reasons →

#1. Borrowing capacity is not reduced

#2 full finance

#3. No extra Docs.

#4 Tax Advantage

Q9. Under a **sale and leaseback** transaction:

A. Asset changes hands both legally and physically

B. Lessee gains depreciation benefits

C. Lessor gets possession of asset

D. Ownership is transferred but possession remains with seller finance lease

Q10. Under Ind AS 116, which of the following costs are included in the **initial measurement of right-of-use asset**?

A. Asset's residual value

B. Lessors' notional interest

C. Initial direct costs incurred by lessee

D. Expected resale value

Asset

cost + lease agreement

lessor

100 + 6

106

PV

20
20
20
20
20
20
20
20

Q11. Under the **accounting treatment** of a finance lease in the lessor's books, the leased asset is presented as:

A. Tangible fixed asset

B. Non-current investment

C. Leasehold asset

D. Receivable equal to net investment in the lease

XYZ Ltd → 200 Lakh $\xrightarrow{\text{lease}}$ ABC Ltd

10 years

36 lakh/year

initial cost (expense)

[200 + 12] C/o

int Rate → 10%

$$Df = \frac{1}{(1+r)^n} = \frac{1}{(1.1)^n}$$

36 × 0.91 =
36 =
36 =
: =
36

360 → 215 lakh

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Q12. Which of the following statements best explains why leasing offers a tax advantage to a lessee?

A. Lease rentals are capitalized

Ans. B. Lease rentals are tax deductible as expenses lease rental → expense

C. Depreciation is claimable by lessee

D. GST is waived on lease GST is applicable

Q13. In leasing decision analysis using NPV, leasing is preferred if:

A. NPV of lease cost is higher than asset cost

B. Lease IRR is equal to cost of debt

C. Lease NPV is positive

D. Lease payments are irregular

Net present value

arithmetic sum of PV of C/I & C/o

+ve →

-ve →

0 →

10% @DF

36

36

36

36

36

36

36

200

215

36 lakh → installment → loan Amt

Q15. Under the Equivalent Loan Method, leasing is beneficial only when:

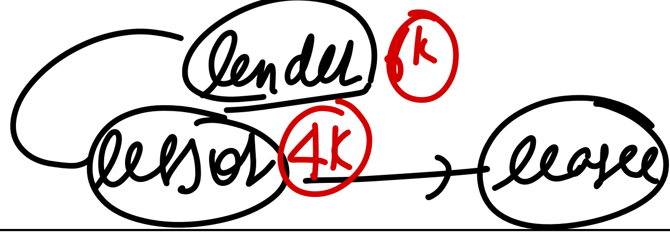
A. Lease rentals exceed depreciation

Ans B. Equivalent loan amount is lower than asset cost

C. IRR < cost of equity

D. Lease liability is greater than NPV

loan > initial



Q16. Which of the following statements about leveraged leases are correct?

a) Lessor borrows to acquire the asset

b) Lease payment is divided between lender and lessor

c) Asset ownership remains with ~~lessee~~

d) Lease rentals are not hypothecated to lender

A. a, b and d

B. a and b only

Ans.

C. a, b and c

D. All of the above

Q17. Identify the incorrect combination regarding lease classification:

a) Operating lease – Transfer of ownership

b) Finance lease – Present value ≈ asset value

c) Dry lease – Lessee handles maintenance

d) Wet lease – Lessor operates the asset

IRR $\Rightarrow$

Discount Rate

to Zero

A. a only

B. b and c

C. a and b

D. All are correct

Q18. In context of tax implications, which are **true**?

a) Lessor can claim depreciation

b) Lease rentals are deductible to lessee revenue expenditure

c) GST is applicable only to finance leases All lease

d) Sale-leaseback allows depreciation on resale value

A. a and b only

B. a, b and d

C. All except c

D. All of the above

Q19. According to Ind AS 116, which of the following apply to **lessee's accounting** for leases?

intt

depreciation

finance

lessee

a) Separate recognition of interest and depreciation

b) Lease liability = PV of lease payments

c) Depreciation claimed for both short and long leases

d) Use of implicit rate or incremental borrowing rate

Ans. $\boxed{\text{A. a, b and d}}$

B. b, c and d

C. a and c only

D. All of the above

right of use cost

lessee

initial Asset 200 Lakh

Any direct cost

dismantle, remove, restore

discount @ 10%

intt dep

36

36

36

36

36

215

NPV +ve → lease

Q20. Choose the correct set of implications based on the **financial decision model**:

a) NPV > 0 – Buy the asset lease the Asset

b) IRR > post-tax debt cost – Prefer leasing

c) Equivalent loan < asset cost – Buy is better

d) Depreciation shield is lost in leasing

A. a and b

B. b, c and d

C. a and c

D. b and d only

Forward Contract ⇒ Spot Rate ± Forward points

derivative → Hedging

→ Speculative

✅ Section A: Basics & Features of Derivatives (Q1–Q5)

Q1. Which of the following is a distinguishing characteristic of derivatives that makes them highly attractive for speculative activity?

A. They provide fixed income returns

B. They are immune to market volatility

C. They offer high leverage with low initial investment

D. They eliminate all forms of market risk

Options/Future

A fwd → $10000 after 2M

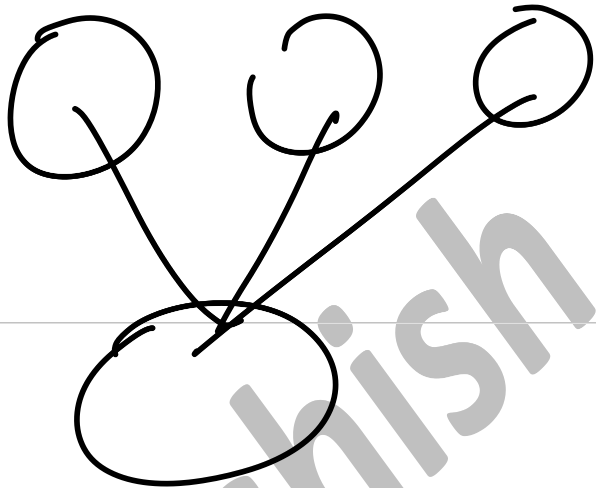
Q2. Which role in the derivatives market is primarily focused on streamlining future cash flows and avoiding value erosion?

A. Trader

B. Hedger

C. Arbitrageur

D. Speculator



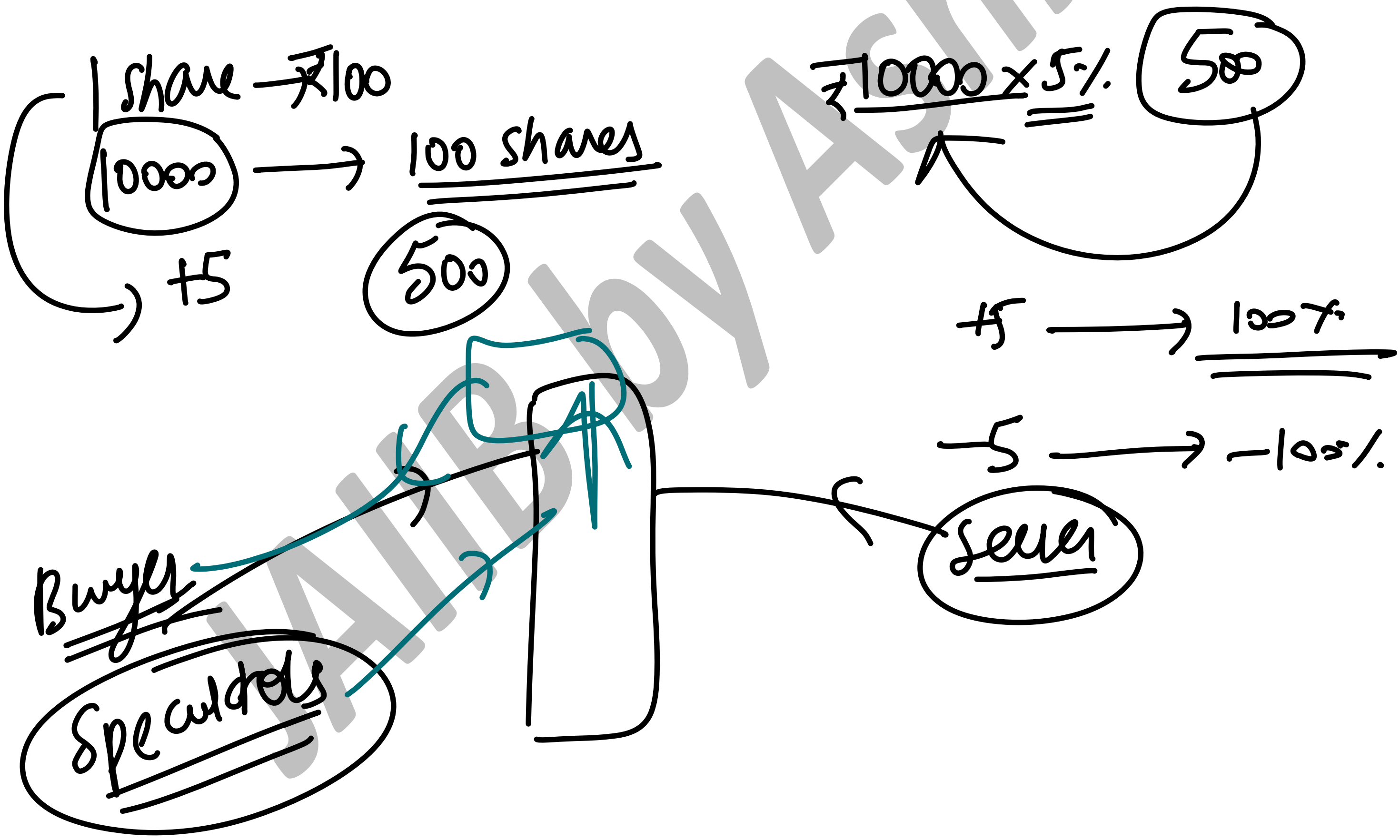
Q3. In which scenario would a derivative contract offer the **price discovery** function?

A. When it is used to fix future cash flows

B. When underlying asset prices are unknown

C. When derivative trading reflects expected future asset prices

D. When used in OTC markets for fixed pricing



derivative → OTC Forward/FRA/IRS
→ exchange

Q4. Which of the following is not a feature of exchange-traded derivatives?

A. Standardized contract size Yes

B. Counterparty risk No

C. Margin requirements Yes

D. Transparent pricing via exchange Yes

bilateral → no std format

Q5. Why are over-the-counter (OTC) derivatives considered more flexible compared to exchange-traded ones?

A. They are settled by central clearinghouses

B. They have standardized maturity and size

C. They allow customization of contract terms

D. They must be settled on the stock exchange

✅ Section B: Forward Contracts, Futures & Differences (Q6–Q10)

→ not option

Q6. In a forward contract, the primary disadvantage to the holder arises when:

A. The forward rate is better than market

B. The market rate turns favorable post-contract

C. The contract is marked-to-market

D. The exchange becomes the counterparty

A = 87.10 INR

10000

2M

84.30

ET

Q7. In which of the following key aspects do futures differ from forwards? OTC

A. Both are traded on exchanges

B. Futures carry counterparty risk

C. Futures are settled through margining system

D. Forwards are always settled daily

.

MTM

mark to mark

100 200

105 +1000

EOD2 98 -1400

Q8. When calculating futures price, which component is **subtracted** from the spot price?

A. Storage cost

B. Insurance premium

C. Income generated from the asset

D. Interest cost

Future → Spot Rate + carry cost − Income from Asset

Q9. Which of the following best describes how a corporate can hedge borrowing cost using interest rate futures?

A. By buying a 90-day T-bill futures contract

B. By short-selling a T-bill futures contract

C. By converting fixed to floating through a swap

D. By locking into currency forward

Bond prices & int Rates inversely Related

BP ↑ Int ↓

BP ↓ Int ↑

Q10. What is the key reason for increased liquidity in underlying instruments due to derivatives?

A. They increase credit worthiness of borrower

B. They hedge against physical delivery

C. They offer continuous pricing and trading

D. They reduce margin requirements

✅ Section C: Swaps & Options (Q11–Q20)

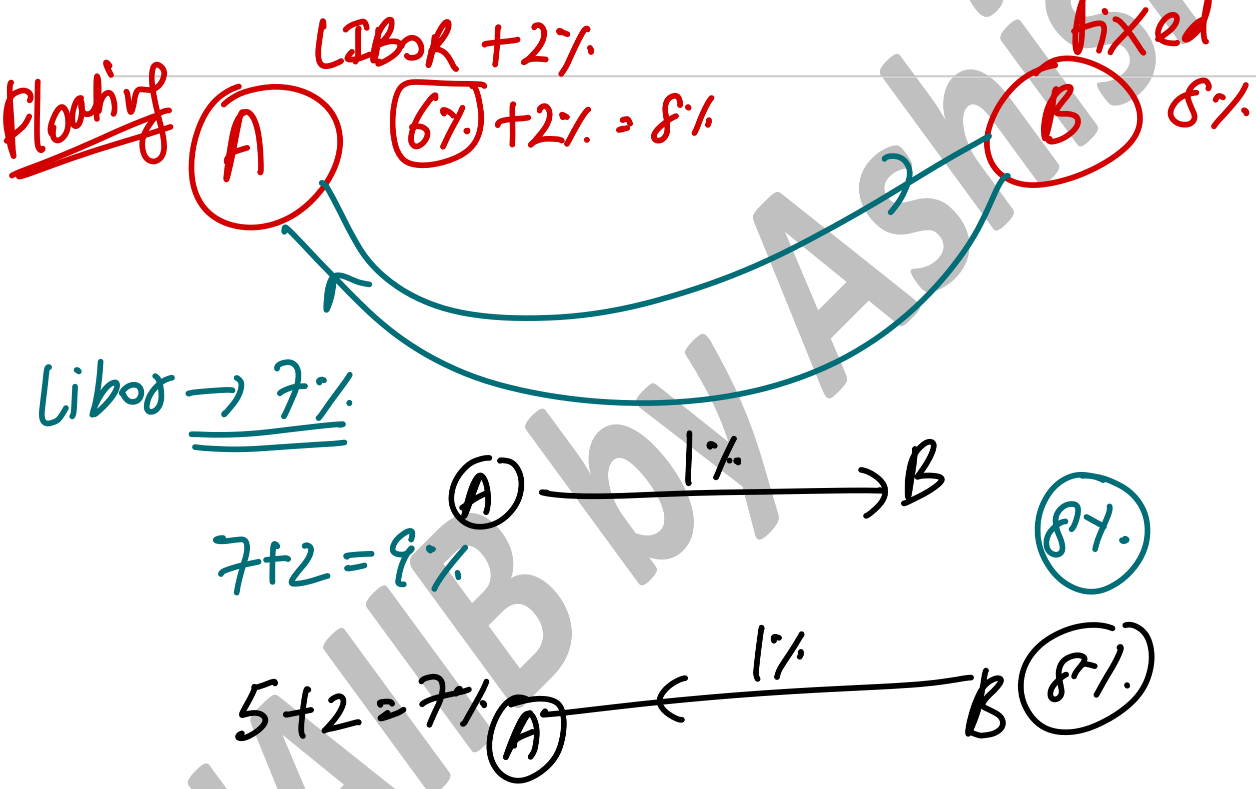
Q11. What is exchanged in an interest rate swap?

A. Principal and interest in same currency

B. Fixed interest rate for floating interest rate

C. Fixed interest for fixed principal

D. Physical delivery of assets



PoS, GS P+I

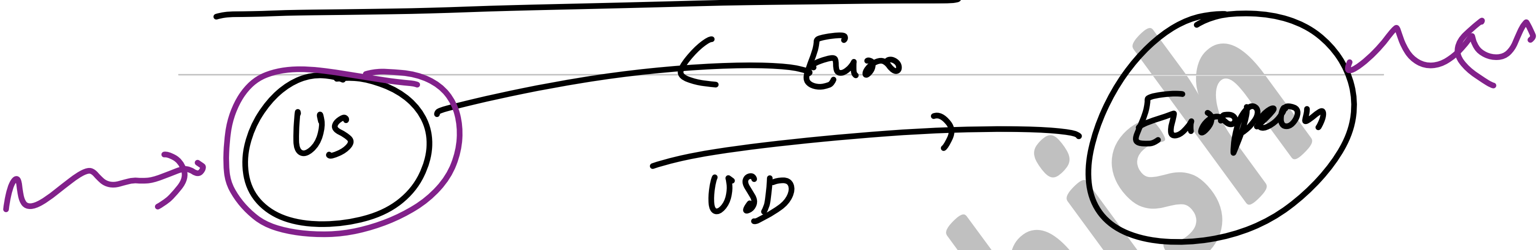
Q12. Which of the following defines a currency swap?

A. Exchange of two interest rates in the same currency

B. Exchange of interest and principal in different currencies

C. Exchange of commodity prices

D. Exchange of fixed income for derivatives



Floating $\rightleftarrows$ Fixed

Q13. What distinguishes a basis swap from a typical interest rate swap?

Floating $\rightleftarrows$ Floating
B_1 B_2

A. It uses fixed and floating legs

B. It exchanges same index cash flows

Ans C. It uses different floating rates on both legs

D. It includes exchange of principal

Q14. Which of the following is **true** about option contracts?

A. They require mandatory exercise

B. The seller has the right to exercise

C. The buyer must sell the asset

D. Buyer has right, not obligation, to buy/sell Ans.

Option writer → Call (right to buy but NO)
→ Put (right to sell but NO)

ABC PV_0 = ₹100

→ premium → not refundable

[Call] strike price → ₹110 [After 1M]

[1M] (a) MP = 130 (b) 90 (c) 110

S.P → 110 S.P 110 SP 110

Favourable Not favourable NPNL

[ITM] [OTM] [ATM]

[Put option] → S.P → 130, premium → ₹2

(sell right) PV → 100

1m → a.) CMP = ₹90

SP → 130

Favourable

[ITM]

Execution —

⇒ American option

⇒ European option

Q15. Which of the following options can be exercised **only at maturity**?

A. American Call Option

B. European Put Option

C. American Put Option

D. Collar Strategy Option

Q16. In an **interest rate cap**, which party benefits when interest rates rise beyond a threshold?

A. Option seller

B. Borrower who bought the cap

C. Lender holding a floor

D. IRS fixed-rate payer

Floating 7.25%

8%

Borrower

Cap

8.25%

0.25%

8%

Q17. What type of interest rate derivative strategy involves both buying a cap and selling a floor?

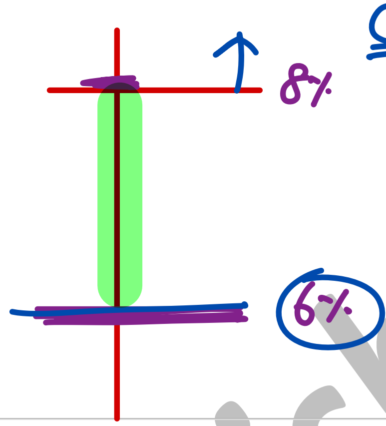
cap seller

A. Collar

B. Swap

C. Basis Swap

D. Plain Vanilla Option



Q18. In the XYZ LTD case, the purpose of purchasing a cap was to:

A. Protect against declining interest rates

B. Lock returns at fixed rates

C. Limit loss in falling bond prices

D. Protect investment spread against rising rates

Q19. The main regulatory condition for offering interest rate swaps by banks is:

A. Minimum capital threshold

B. Use of international LIBOR only

C. Proper risk infrastructure and balance sheet usage

D. Pricing based on RBI-determined rates only

Swaps

→ IRS

→ CS

→ BS

ALM

ITM → Favourable

Q20. An option is considered **in-the-money** when:

A. Strike = Spot

B. Strike is worse than market

C. Exercise leads to loss

D. Exercise leads to gain

✅ Section D: FRAs, CDS & Regulatory Framework (Q21–Q25)

Q21. What is the primary function of a FRA in interest rate risk management?

A. Lock borrowing at past interest rates

B. Speculate on currency values

C. Fix an interest rate for a future loan or deposit

D. Allow buying of physical asset on margin

gap Jump

6 vs 9 FRA

0 3M

6M

---

forward rate agreement

OTC

XYZ 3M 6M

1 crore

FRA → 3 vs 9 FRA

XYZ ← Bank

Buy 6.50%

6.25 / 6.50
B S

3 vs 9 FRA

3M

a.) corporate → 7%

FRA seller

0 6M

3M 1 crore

PV 0.5%

b.) BM → 6.25%
6.50

0.25%

notional amount → Bank

Q22. If the reference rate settles **below** the agreed FRA rate, which party compensates whom?

7%

Ref rate 6.5%

A. FRA buyer pays FRA seller

B. FRA seller pays FRA buyer

C. No payment is required

D. Central bank settles difference

Q23. Which of the following is **not** an eligible reference for CDS?

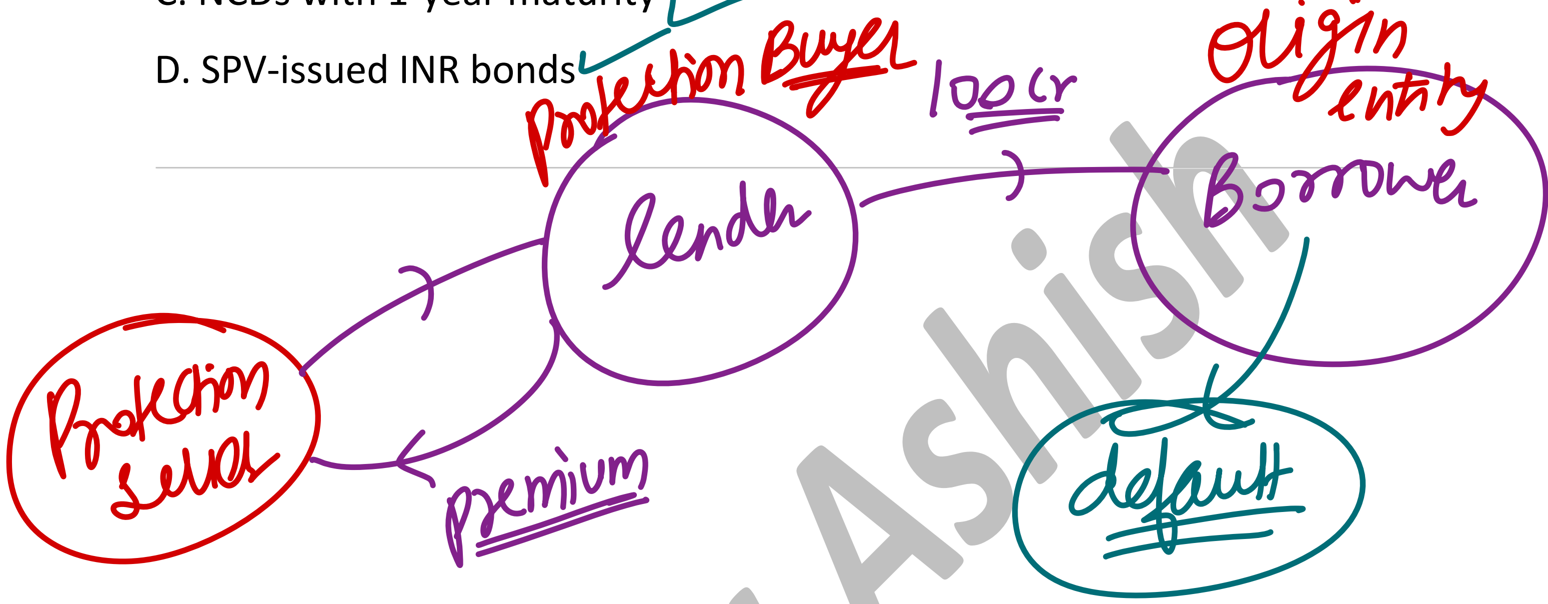
A. Rated INR bonds

B. Mortgage-backed securities

C. NCDs with 1-year maturity

D. SPV-issued INR bonds

ABS, MBS, SO



Q24. In a CDS, the **protection buyer**:

A. Writes the credit risk

B. Pays a premium and gets compensated for default

C. Earns income by assuming credit risk

D. Delivers cash flows

Q25. What settlement type is **mandatorily required** for retail users in CDS transactions?

A. Net cash settlement

B. Auction-based settlement

C. Physical settlement

D. Novation

✅ Section E: Analytical and Case-based (Q26–Q30)

Q26. Which of the following is/are true regarding forward contracts?

a) Are traded on exchange

b) Have no daily margining

c) Involve opportunity cost

d) Offer standardised contracts

A. b and c only Ans.

B. a, b and d

C. a and c

D. All of the above

Q27. Which of the following combinations is **correct**?

a) IRS – Fixed vs Floating

b) FRA – Principal exchange

c) Cap – Buyer gets compensated if rate exceeds cap

d) Basis Swap – Same floating rate benchmark

A. a, c only Ans

B. a, b, c

C. a, c, d

D. a to d all

Q28. Identify incorrect matches: call

a) Option = Obligation to buy/sell α Right

b) Futures = Daily MTM Yes put

c) CDS = Protection buyer pays premium Yes

d) Cap = Limits floating rate cost

A. a only Ans.

B. a and d

C. b and c

D. d only

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Q29. Which of the following is true about derivative usage?

a) Hedgers are speculators

b) Swaps create synthetic liabilities

c) FRA is similar to IRS

d) Caps are sold to limit returns

A. b and c only

B. a, b and d

C. a to d all

D. b, c and d

Q30. Which of the following statements are correct?

a) FRAs lock future interest rates

b) Options give obligation to act

c) CDS compensates for restructuring

d) Collar involves buying floor and selling cap

A. a, b and c

B. a and c only

C. b, c and d

D. a to d all