NEW SYLLABUS **441**

Roll No..................................... **OPEN BOOK EXAMINATION**

Time allowed : 3 hours *Maximum marks : 100*

Total number of questions : 6 *Total number of printed pages : 9*

NOTE : *Answer **ALL** Questions.*

1. Read the following case study and answer the questions that follow :

Execution of Forward Contracts

ABC Bank, Kanpur branch is an Authorized Dealer in 'Foreign Exchange' and authorized dealer status given by Reserve Bank of India as "A Category". Number of Export/Import oriented units located in SEZ, Kanpur are the clients of ABC Bank, Kanpur Branch. As ABC Bank, Kanpur is only one 'Forex Authorized Branch' located in Kanpur, Exporters and Importers situated within the radius of 60 KM are visiting to the Branch to clarify their doubts with regard to discounting of Export Bills/Import Bills/Letter of Credit etc. from Chief Manager, Foreign Exchange Division of ABC Bank, Kanpur Branch.

The Controlling Authority of ABC Bank, Kanpur observed the above situation and instructed the Branch to conduct Exporters/Importers Meet on 9th April, 2020 to mobilize 'Foreign Exchange Business' from Exporters and Importers to the Branch books.

Accordingly, ABC Bank, Kanpur Branch followed the instructions of their Controller and invited all the Exporters/Importers surrournding to the Branch and also within a radius of 60 KM. They conducted Meet in a Five Star Hotel in Kanpur in a big way.

During the Export/Importers Meet number of questions were raised by prospective customers and the same was suitably replied by Senior Staff members of the Bank. Existing and prospective customers were satisfied with the replies given by Bank officials. One clarification sought by 'Number of Customers' is on "Forward Contract" Product of International Banking. Most of them are not utilized this Product offered by ABC Bank, Kanpur. Mr. Suresh, Chief Manager of the Branch explain the 'Forward Contracts' Product features offered by the Branch as follows :

Forward Contract is the traditional method by which Exporters and Importers were hedging their foreign currency exposure. It affords perfect hedge for foreign currency exposures.

The uncertainty about the rate that would prevail on a future date is known as the 'exchange risk'. For the exporter the exchange risk is that the foreign currency in which the transaction is designated may depreciate in future and may bring less than the expected realization in local currency terms.

The importer too faces exchange risk when the transaction is designated in a foreign currency. The risk is that the foreign currency may appreciate in value and he may be compelled to pay in local currency an amount higher than that was originally contemplated. Importers generally make arrangements for loans for payment for the imports. If the foreign currency appreciates subsequent to the arrangement of the loan, the importer may find that the resources are not sufficient to meet the importer bill putting him in a difficult situation.

Forward contract provides perfect hedge against fluctuations, but it also takes away the opportunity to make profits from favorable movements in exchange rates. Forward contracts impose an obligation on the parties to execute it on the due date irrespective of the spot rate prevailing. On execution, only the rate agreed to in the contract will be applied. If one wants to cancel the contract to take advantage of the better rate in the spot market, the counterparty will levy cancellation charges which will be greater than the benefit obtained in the spot market.

By definition, the time and amount of foreign exchange to be delivered are predetermined under a forward contract and the customer is bound by the agreement. So, theoretically, there should not be any variation and on the due date of the forward contract the customer will either deliver or take delivery of the fixed sum of foreign exchange agreed upon. But, in practice, quite often the delivery under a forward contract may take place before or after the due date, or delivery of foreign exchange may not take place at all. The bank generally agrees to these variations provided the customer agrees to bear the loss if any, that the bank may have to sustain on account of the variation.

The foreign exchange may be delivered on the due date as per the forward contract. Or, the delivery may take place earlier or later than the due date. Alternatively, the customer may request cancellation of the contract. This request for cancellation may be made on the due date, before the due date or later than the due date. Yet another alternative is that the customer may request postponement of the date of delivery under the forward contract. This request for postponement may be made on the due date, earlier than the due date or after the due date.

The various possibilities of forward contracts are summarized in the form of table below :

<table>
<tr><td rowspan="9">Forward Contract</td><td rowspan="3">Delivery</td><td>Due Date Delivery</td></tr>
<tr><td>Early Delivery</td></tr>
<tr><td>Late Delivery</td></tr>
<tr><td rowspan="3">Cancellation</td><td>Due Date Cancellation</td></tr>
<tr><td>Early Cancellation</td></tr>
<tr><td>Late Cancellation</td></tr>
<tr><td rowspan="3">Extension</td><td>Due Date Extension</td></tr>
<tr><td>Early Extension</td></tr>
<tr><td>Late Extension</td></tr>
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It is clear that a forward contract may end up in any of the following ways :

(*a*) Delivery on the Due Date.

(*b*) Early Delivery.

(*c*) Late Delivery.

(*d*) Cancellation on the Due Date.

(*e*) Early Cancellation.

(*f*) Late Cancellation.

(*g*) Extension on the Due Date.

(*h*) Early Extension.

(*i*) Late Extension.

Cancellation : The Exporter may approach the bank for cancellation when the underlying transaction becomes infructuous, or for any other reason he wishes not to execute the forward contract. If the underlying transaction is likely to take place on a day subsequent to the maturity of the forward contract already booked, he may seek extension in the due date of the contract. Such requests for cancellation or extension can be made by the customer on or before the maturity of the forward contract.

Extension : An exporter finds that he is not able to export on due date but expects to do so in about two months. An importer is unable to pay on due date but is confident of making payment a month later. In both these cases they may approach their bank with which they have entered into forward contracts to postpone the due date of the contract. Such postponement of the date of delivery under a forward contract is known as the extension of forward contract.

Based on the above information, read the following case study and answer the questions that follows :

On the next day of Exporters/Importers Meet of the Bank, an Import Customer approached ABC Bank, Kanpur Branch and booked a forward contract with the Bank on 10th April for USD 20,000 due 10th June at ₹ 49.4000. The bank covered its position in the market at ₹ 49.2800.

Particulars	**10th June**	**20th June**
Spot	USD 1 = ₹ 48.8000/8200	48.6800/7200
Spot/June	48.9200/9500	48.8000/8500
July	49.0500/0900	48.9300/9900
August	49.3000/3500	49.1800/2500
September	49.6000/6600	49.4800/5600

Exchange margin 0.10%.

Interest on outlay of funds 12%.

Based on the above particulars, please answer the following questions :

How will ABC Bank, Kanpur react if the Importer Customer request on 20th June :

(*i*) Calculate the following in case the Contract is Cancelled.

(*a*) The Exchange Difference amount. (*5 marks*)

(*b*) How much the Swap Loss Amount ? (*5 marks*)

(*c*) Interest to be charged by the Bank on Outlay of Funds. (*5 marks*)

(*d*) Charges for Cancellation by the Bank. (*5 marks*)

(*ii*) Calculate the amount in Execution of the Contract. (*6 marks*)

(*iii*) What will be exchange rate to extend the contract with due date to fall on 10th August ?

(*6 marks*)

(*iv*) What is Roll Over of a Forward Contract ? How is it done ? (*8 marks*)

(**Note :** Foreign Exchange Rates are dynamic, the above-mentioned rates are not the current market rates. Use the above rates for calculation purpose.)

2. (*a*) What is meaning of differentiated banks ? Explain two differentiated banks and their functions in India. (*3+2+2 marks*)

(*b*) Explain the following statements in brief on the point of reasoning :

(*i*) Normally Banks do not grant advance to Trust Accounts.

(*ii*) "Not Negotiable" Crossing does not mean "Not Transferable".

(*iii*) Nomination facility is provided to all Deposit Accounts.

(*iv*) Banks are entered insurance sector in a Big Way.

(*v*) Bank is giving emphasis on reduction on Non-performing Assets.

(*1 mark each×5=5*)

3. (*a*) (*i*) A 5-year 5% Bond has a Basis Point Value (BPV) of ₹ 50. How much the bond will gain or lose due to increase in the yield of bond by 2 bps ?

(*ii*) Bond A is a 7-year, 8% Coupon Bond. It has Duration of 4.2 and a Current Yield of 6.6%. If the yield were to suddenly decrease to 6.1% approximately, what will be the percentage price change for this Bond ?

(*iii*) A 10-year 12% Semi-annual Bond @ Market Yield of 8.520% has a price of ₹ 116.16 which rises to ₹ 117.45 at a Yield of 8.320%. What is the Basis Point Value (BPV) of the bond ? (Book Value of Bond is ₹ 1,000.)

(*1+2+4 marks*)

(*b*) M/s Party & Company was sanctioned a Cash Credit Facility of ₹ 4 lakh from M/s XYZ Bank against pledge of goods and personal guarantee of Mr. A who is not a partner in the firm. The bank subsequently recalled the advance and demanded repayment of the amount both from the borrowing firm and guarantor. As there was no response, the Bank sold the pledged stocks by public auction for ₹ 2,70,000 and filed a suit against the borrowing firm and the guarantor for the balance amount due in the cash credit account. Mr. A denies his liability on the ground that the pledged stocks were sold without his knowledge or consent and in doing so, the bank has prejudiced his right as guarantor.

How will you deal with the situation ?

(*5 marks*)

4. ‘‘Commercial Paper is an unsecured Money Market Instrument issued in the form of a Promissory Note introduced in the year 1990 to enable highly rated Corporates to borrow on short-term basis. It also serves as additional Money Market instrument for investment”. Explain in detail the latest terms and conditions of Reserve Bank of India in this regard. (*12 marks*)

5. (*a*) (*i*) What is MUDRA and why MUDRA has been set up ?

(*ii*) What are the roles, responsibilities and offerings of MUDRA ? How MUDRA function ? (*3+3 marks*)

(*b*) In its ‘Statement on Developmental and Regulatory Policies’ issued in December 2018, RBI said : ‘‘With the digital mode for financial transactions gaining traction in the country, there is an emerging need for a dedicated, cost-free and expeditious grievance redressal mechanism for strengthening consumer confidence in this channel. It has therefore been decided to implement an ‘Ombudsman Scheme for Digital Transactions’ covering services provided by entities falling under Reserve Bank’s regulatory jurisdiction”.

Explain in brief how the Ombudsman will deal the Customer Complaints and also explain the process for filing the complaints related to Digital Transactions raised by Bank Customers. (*6 marks*)

6. (*a*) (*i*) ''Payment in due course is one made in accordance with the apparent tenor of the instrument that is according to what appears on the face of the instrument to be intention of the parties''. Explain the conditions to qualify before the payment made to the customer by the Bank.

(*ii*) What are the duties of a Collecting Banker ? (*3+3 marks*)

(*b*) (*i*) What is the purpose of provisioning in Banks ? What is Provisioning Coverage Ratio (PCR) ?

(*ii*) What is Operational Risk ? Explain the types of Operational Risk as identified by Basel Committee.

(*3+3 marks*)

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