Name : Hamad Ullah Khan

ID : 14026

Subject : Advanced Corporate Finance

Q#1) Long term investment is very much important for any business while considering strategic decision making. Bond is one of the debt financing tools available to any business. Explain the basic characteristics of bond financing.

Ans#1) Long term investment is an account on the asset side of a company’s balance sheet that represents the company’s investments, including stocks, bonds, real estate, and cash. Long term investments are assets that a company intends to hold for more than a year. Being a long term investor means that you are willing to accept a certain amount of risk in pursuit potentially higher rewards and that you can afford to be patient for a longer period of time. It also suggest that you have enough capital available to afford to tie up a set amount for a long period of time.

A long term investment is an account a company plans to keep for at least a year such as stocks, bonds, real estate, and cash.

The account appears on the asset side of a company’s balance sheet.

Long term investors are generally willing to take on more risk for higher rewards. There are different form of short term investments, which are meant to be sold within a year.

When a holding company or other firm purchases bonds or shares of common stocks as investments, the decision about whether to classify it as short term or long term has some fairly common implications for the way those assets are valued on the balance sheet.

Debt financing occurs when a firm raises money for working capital or capital expenditure by selling debt instruments to individuals or institutional investors. In return or lending the money the individuals or institutions become creditors and receive a promise that the principal and interest on the debt will be repaid.

When a company needs money through financing, it can take three routes to obtain financing, equity, debt, or some hybrid of the two. Equity represents an ownership stake in the company. It gives the shareholder a claim on future earnings, but it does not need to be paid back. If the company goes bankrupt, equity holders are the last in line to receive money. The other route is debt financing, where a company raises capital by issuing debt.

Debt financing occurs when a firm sells fixed income products, such as bonds bills, or notes, to investors to obtain the capital needed to grow and expand its operations. When a company issues a bond, the investors that purchases the bond are lenders who are either retail or institutional investors that provide the company with debt financing. The amount of the investment loan, also known as the principal must be paid back at some agreed date in the future. If the company goes bankrupt, lenders have higher claim on any liquidated assets than shareholders.

A bond is generally a form of debt which the investors pay to the issuers for a defined time frame. If a layman’s bond holder offers credit to the company issuing

Name : Hamad Ullah Khan

ID : 14026

Subject : Advanced Corporate Finance

The bond. Bonds generally have a fixed maturity date. All bonds repay the principal amount after the maturity date, however some bonds do pay the interest along with the principal to the bond holders.

Q#2) Bond financing can be done in different formation. Explain few most commonly used bond financing investment in different financial markets.

Ans#2) Bond formation includes the structure creation, ISIN number registration, base prospectus documents, and indenture of assets that back the bond formation. Formation of a bond can be built for almost any investment grade Country, as long as the assets are unemcumbered and insurable.

The common features of a bonds and the financial terms related to the bonds are as following :

Issuer : The entities that borrow money by issuing bonds are called as issuers. In the US, there are mainly 4 major issuers of bonds which includes the government, government agencies, municipal bodies, and corporations.

Face value : Every bond that issued has a face value: which is usually the principal amount that is borrowed and returned on maturity. In layman’s terms it is the value of the bond on its maturity. The rate of interest on the bond is called as a coupon.

Rating : Every bond is usually rated by credit rating agencies, higher the credit rating, lower will be the coupon required to pay by the issuer and vice versa.

Coupon payement frequency : The coupon payements on the bond usually have a payement frequency. The coupons are usually paid annually or semi-annually. However, they may be paid quarterly or monthly aswell.

Yield : The effective rate of interest.

Different types of bonds :

Zero Coupon bonds : A type of bond where there are no coupon payements made. These are also called as discount bonds if they are for longer term.

Perpetual bonds : These types of bonds pay a coupon rate on the face value till the life of the company. Bonds with maturity above 100 years are also considered to be perpetual bonds.

Name : Hamad Ullah Khan

ID : 14026

Subject : Advanced Corporate Finance

Convertible bonds : Are a special variety of bonds which have an inbuilt feature of being converted to equity shares at a specified time at a pre-set conversion price.

Callable bonds : Bonds that are issued with a specific feature where the issuer has the right to call back the bonds at a pre-agreed price and a pre-fixed date are called as callable bonds.

Financial markets refer broadly to any marketplace where the trading of secrurities occur including the stock market, bond market, forex market, and derivative markets, among others. Financial markets are vital to the smooth operations of capitalist economies.

The stock market is just one type of financial market. Financial markets are made by buying and selling numerous types of financial instruments including equities, bonds, currencies and derivatives. Financial markets rely on informational transparency to ensure that the market set prices that are efficient and appropriate. The market price of securities may not be indicative of their instrinsic value because of macroeconomics forces like taxes.

Types of financial markets :

Money markets

Bond markets

Derivatives markets

Forex market

Q#3) Equity financing is very important component of the capital structure of any business, while considering its financial strength and decision making. Explain on of the basis formations of equity financing as common stock financing. Explain the characteristics of common stock in detail.

Ans#3) Equity financing is the process of raising capital through the sale of shares. Companies raise money because they have a short term need to pay bills or they might have a long term goal and require funds to invest in their growth. By selling shares, they sell ownership in their company in return for cash, like stock financing.

Equity financing comes from many sources : for example an entrepreneur’s friend or family, investors, or an initially public offering (IDO). Industry giants such as Google and Facebook raised billion in Capital through IPOS.

While the term equity financing refers to the financing of public companies listed on an exchange, the term also applies to private company financing. Equity financing involves the sale of common equity but also the sale of others equity or equity instruments such as preffered stocks, convertible preferred stocks, and equity units

Name : Hamad Ullah Khan

ID : 14026

Subject : Advanced Corporate Finance

That include common shares and warrants.

Equity financing as common stock financing : This is the basic type of stock, which gives its holders the right to share equitably in any dividents and in the finds payout from the dissolutions or sale of a business. The holder also has the right to vote for members of the board of directors, as well as certain other company decisions.

Common stock : Common stock is a security that represents ownership in a corporation. Holders of common stock elect the board of directors and vote on corporate policies. This form of equity ownership typically yields higher rates of returns long term. However, in the event of liquidity common shareholders have rights to company’s assets only after bondholders, preferred shareholders, and often debt holders are paid in full. Common stock is reported in the stockholders equity section of a company’s balance sheet.

With common stock if a company goes bankrupt, the common stockholders do not receive their money until the creditors, bondholders, and preferred shareholders have received their respective shares. This makes common stock riskier than debt or preferred shares. The upside to common shares is they usually outperform bonds and preferred shares in the long run.

Common stock is a security that represents ownership in a corporation.

In a liquidation, common stockholders receive whatever assets remain after creditors, bondholders, and preferred stockholders are paid.

There are different varieties of stocks traded in the market. For example, value stocks are stocks that are lower in price in relation to their fundamentals.

Growth stocks are companies that tend to increase in value due to growing earnings.

Investors should diversify their portfolio by putting money into different securities based on their appetitic for risk.

Q#4) Time value of money is very important element while considering any strategic financial investment. Explain the basic concept of time value of money. End introduce the concept of capital budgeting technique known as net present value.

Ans#4) Importance of time value of money : Almost everything in life involves the time value of money. If you buy a car on credit, take out a mortage, or invest in stocks. It all involves the time value of money. If you work for a company, every decision the company makes will involve, in one way or anathor, the time value of money. If you are trying to determine whether or not to pursue a company project for find some other alternative the time value of money will weigh on your decision.

Name : Hamad Ullah Khan

ID : 14026

Subject : Advanced Corporate Finance

The time value of money (TVM) according to investopedia is the concept that money available at the present time is worth more than the identical sum in the future due to its earnings capacity. The time value of money is the concept that money you have now is worth more than the identical sum in the future due to its potential earnings capacity. This core principal of finance holds that provided money can earn interest, any amount of money is worth more the sooner it is received. TVM is also sometimes referred to as present discounted value.

The time value of money draws from the idea that rational investors prefer to receive money today rather than the same amount of money in the future because of money potential to grow in value over a given period of time. For example, money deposited into a saving, accounts earns a certain interest rate and is therefore said to be compounding in value. Time value of money is based on the idea that people would rather have money today than in the future.

Given that money can earn compound interest, it is more valuable in the present rather than the future. The formula for computing time value of money considers the payement now, the future value, the interest rate and the time frame.

The number of compounding periods during each time frame is an important determinant in the time value of money formula as well.

Depending on the exact situation in question, the time value of money formula may change slightly for. For example, in the case of annuity or perpetuity payements, the generalized formula has additional or less factors. But in general, the most fundamental TVM formula takes into account the following variables :

FV : Future value of money

PV : Present value of money

I : Interest rate

n : Number of compounding periods per year

t : Number of years

Capital budgeting : Capital budgeting is the process a business undertakes to evaluate potential major projects or investments. Construction of a new plant or a big investment in an outside venture are examples of projects that would require capital budgeting before they are approved or rejected.

As part of capital budgeting, a company might asses a prospective projects lifetime cash inflows and outflows to determine whether the potential return that would be generated meet a sufficient target benchmark. This process is also known as investment appraisal.

Capital budgeting is used by companies to evaluate major concepts and investments, such as new plants or equipments. The process involves analyzing a projects cash

Name : Hamad Ullah Khan

ID : 14026

Subject : Advanced Corporate Finance

Inflow and outflows to determine whether expected returns meets a set benchmark. The major methods of capital budgeting includes throughout discounted cash flows, and payback analysis.

Capital budgets is the method of determining and estimating the potential of long term investment options involving enormous capital expenditure. It is all about the company’s strategic decision making, which acts as a milestone in the business.