UNIVERSITY OF COLOMBO, SRI LANKA

FACULTY OF MANAGEMENT AND FINANCE

Bachelor of Business Administration (Level II- Semester VII) Examination July 2018

FIN 2205- Security Analysis

Two (02) Hours

Instructions to candidates:

1. Answer **all** questions
2. Use of calculators is permitted.

1.

i. Even though Fundamental Analysis and Technical Analysis are seen by many as polar opposites, many market participants such as investors and traders have experienced greater success by combining these two approaches. Critically evaluate the above statement by drawing some examples

(06 marks)

ii. List the Reversals and Continuation patterns identified in technical analysis.

(03 marks)

iii. Briefly explain the difference between Simple Moving Average (SMA) and Exponential Moving Average (EMA).

(04 marks)

iv. As a trader which Moving Average techniques would you choose and why?

(03 marks)

v. List four types of Moving Average strategies used by a trader.

(02 marks)

vi. Distinguished between Odd lot theory and Contrarian investing to equity.

(06 marks)

vii. What is the application of the Elliot wave theory to technical analysis?

(04 marks)

(Total 28 Marks)

2.

    i.   "Playing in the stock market is like gambling. Such speculative investment has no social value other than the pleasure people get from this form of gambling" Critically evaluate the above statement

(05 marks)

    ii.   What are the important implications (lessons) for an analyst if he assumed that stock market to be efficient?

(05 marks)

    iii.   What is rational behind concept of efficient market and behavioral finance? Which concept you believe in terms of Colombo Stock Exchange? Briefly explain

(06 marks)
(Total 16 Marks)

3.   Assume that you are managing your own portfolio based on the Value, Growth and Income investment strategies.

    i.   What is the rationale behind selecting stocks based on each of the investment strategies?

(03 marks)

    ii.   Based on what criteria would you select Value stocks, Growth stocks and Income stocks? You are required to develop at least one sample screen under each of the technique.

(09 marks)

    iii.   Briefly explain the fundamentals of Value investment and the risk involved in Value investment.

(06 marks)
(Total 18 Marks)

4.   Assume that you are a senior fundamental research analyst for an equity research firm. The CEO of the firm direct following questions to you.

    i.   What are the objectives of using Dividend Discount Model, Discounted Cash Flow method or Relative valuation approach to equity valuation?

(04 marks)

    ii.   State three types of multiples use in relative valuation and briefly explain under what circumstances said multiples are being used by the analyst.

(05 marks)

iii. Siva Associated Limited (SAL) was founded in the year 1992. Currently, it has one factory located in Kurunagala. Considering the growing demands of the industry, the owner has decided to expand the factory. The expansion will be funded by a bank loan taken at the rate of 11%. The corporate tax rate is 20%.

A recently hired analyst has done the following forecast for next three years. All figures are in '000

	2017	2018E	2019E	2020E
Revenue	37,532	40,147	42,860	45,818
EBITDA	11,550	12,055	12,291	12,540
Depreciation and Amortization	2,560	2,678	2,771	2,861
Capital Expenditure	3,001	3,032	3,055	3,079
Decreasing in Working Capital	358	301	644	179
Net Debt	9,000	9,000	9,000	9,000
Net Cash	5,000	5,500	4,500	3,500

SAL believes that the target capital structure in its industry is 65% equity and 35% debt, Risk free rate in the country is 7% per annum, market risk premium amounts to 10%. SAL historic beta is 0.4 and expects to increase by 0.1 due to the change in the capital structure and the expansion.

The Terminal Value is calculated based on the Gordon Growth model and it is assumed that long term growth rate would be 2 to 3 percent. Number of outstanding shares are 1,800,000.

You are required to compute the followings:

a) Cost of equity and WACC

b) Value of the Firm, using the free cash flow to firm

c) Value of Equity

d) Equity value per share

e) If shares of SAL currently trades at Rs. 35, what would be your recommendation to investors (Buy/Hold/Sell)? Justify your recommendation.

(14 marks)

iv.   Outline a comprehensive framework in order to carry out an industry analysis report for an industry of your own choice and you may cite example appropriately.

(12 marks)

v.   Name at least three economic forecasting techniques and briefly explain one of them

(03 marks)

(Total 38 Marks)

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