Roll No. Total No. of Pages : 03

Total No. of Questions : 17

MBA(Sem.–4)

BEHAVIOURAL FINANCE

Subject Code : MBA-913-18

M.Code : 77812

Date of Examination : 07-07-22

Time : 3 Hrs. Max. Marks : 60

INSTRUCTIONS TO CANDIDATES :

1. SECTION-A contains EIGHT questions carrying TWO marks each and students have to attempt ALL questions.
2. SECTION-B consists of FOUR Subsections : Units-I, II, III & IV. Each Subsection contains TWO questions each carrying EIGHT marks each and students have to attempt any ONE question from each Subsection.
3. SECTION-C is COMPULSORY and consists of ONE Case Study carrying TWELVE marks.

SECTION-A

Write short note on the following :

1. Agency theory
2. Overreaction
3. Momentum
4. Mental Accounting
5. Risk appetite
6. Stock market bubbles
7. Noise trading
8. Efficient Market Hypothesis

SECTION-B

UNIT-I

9. *"Behavioural challenges have reduced the efficiency of traditional finance theories, hence, behavioural finance as a discipline has evolved and gaining importance in the present dynamic business environment".* Elucidate with suitable examples.

10. What is Prospect theory? Discuss the key tenets of prospect theory with suitable examples.

UNIT-II

11. What are stock market anomalies? Discuss various calendar anomalies prevalent in the stock market. Also, discuss the behavioural explanations for their presence.

12. What is Heuristic behaviour? Explain with suitable examples, how heuristic behaviour affects the decision making process of an investor?

UNIT-III

13. What areEmotions? Discuss the impact of emotions on investor's behaviour.

14. What is Value investing? Discuss the key tenets of value investing.

UNIT-IV

15. What isinformation asymmetry? Discuss the various capital budgeting distortions caused by information asymmetry between current and prospective shareholders.

16. What is a Halo effect? Discuss the role of Halo effect in understanding corporate performance.

SECTION-C

17. Case Study :

Warren Buffet, chairman and CEO of Berkshire Hathaway (Berkshire hereafter) a holding company is a quintessential value investor. Here is a sampling of his decisions:

a. When the price of Coca Cola stock crashed in 1988 in response to a disastrous roll out of Diet Coke, Warren Buffet started buying up Coca Cola like an addict. Within a few months, Berkshire acquired 7% of Coca Cola's stock for about $ 1 billion. Within 3 years, Berkshire's Coca Cola holding was worth more than the entire value of Berkshire when the investment was made. When Coca Cola's price was depressed, buffet considered it as a compelling bargain for three reasons: First, consumers have a very strong brand preference for Coca Cola. Second, an average America, when he starts drinking Coca Cola, requires five bottles a day for the rest of his life. Third, 40% of Coca Cola is just fizz.

07/10/20

b. When the stock of China Petro was selling cheap, Warren Buffet invested \$488 million. Subsequently he divested his holding for \$ 4 billion.

c. In 2002, the 6.875% 2010 euro-denominated bonds of amazon.com were selling at 57% of par. These bonds were selling at a steep discount because they were priced as junk bonds, though they were anything but junk bonds. Perceiving them to be hugely underpriced, Berkshire purchased \$ 310 Amazon.com bonds and later sold them at a gain of \$ 246 million. He commented "Yes Virginia, you can occasionally find markets that're ridiculously inefficient - or at least you can find them everywhere except the finance department of leading business school",

d. In 2002, Berkshire purchased Brazillian real, which in Buffet's assessment was undervalued *vis-a-vis* the US Dollar. This proposition yielded a profit of \$ 2.3 billion over a five year period.

e. In 2007, Berkshire sold put options on four stock indices (S&P 500 and three foreign indices). These puts had maturities of 15 or 20 years and were stuck at the market, meaning that they were exercisable at a price equal to what was prevailing in 2007. These contracts are exercisable only at their expiration dates, which-occur-between-2022 and 2027. This means that Berkshire will have to pay only if the index in question quotes at a level below the level that existed when the put was written. For writing these contracts, Berkshire received premiums of \$ 4.5 billion. Buffet believed that these contracts, in aggregate, will be profitable. Further, Berkshire would receive substantial income from investment of the premiums over 15 to 20 years.

Comment on Warren Buffet's value picks.

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MBA (Sem.–4)

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SECTION-A

1. Write briefly :

i. Prospect theory

ii. Heuristic behaviour

iii. Reversal

iv. Value investing *vs.* Growth investing

v. Information asymmetry

vi. Risk aversion *vs.* Loss aversion

vii. Stock market anomalies

viii. Animal spirits in stock market.

SECTION-B

UNIT-I

2. What is behavioural finance? Discuss the scope and importance of behavioural finance. Also, briefly discuss the role of rational expectation paradigm in evolution of behavioural finance.

3. What is Efficient Market Hypothesis? Discuss the basic premise of efficient market hypothesis. Also discuss the limitations of efficient market hypothesis.

UNIT-II

4. What is mental accounting? Discuss the role and importance of mental accounting in behavioural finance.

5. What is overconfidence? Discuss various forms of overconfidence. Explain with examples the reasons for presence of overconfidence among investors.

UNIT-III

6. What is stock market bubble? Discuss various reasons for presence of stock market bubbles. Also, discuss how presence of bubbles affects market efficiency?

7. Critically examine the role of social forces on investor's behaviour.

UNIT-IV

8. What is agency çost? Discuss the consequences of divergence between the interest of managers and shareholders.

9. What is wisdom of crowd? Discuss with suitable examples how wisdom of crowd drive the animal spirits in stock market?

SECTION-C

10. Case Study :

The UB group of India headed by Vijay Mallya, launched the Kingfisher Airlines (KFA) in 2005. After having earned the reputation of liquor baron, Vijay Mallya diversified into the totally unrelated business of airlines. He entered industry when buzzword was 'low cost' and the aviation industry in India was booming. Vijay Mallya, a colorful and flamboyant person, is known for his fondness for 'good things in life' such as IPL teams, cars, horses, private jets, yachts and exotic villas. According to some sources, Vijay Mallya set up KFA in 2005 as a birthday gift for his son, Sidharth Mallya on his 18th birthday.

The UB group under the leadership of Vijay Mallya built a successful liquor business and Mallya took great pride in building several powerful liquor brands. Fond of good things in life. Vijay Mallya conceived of KFA as a five star airline. He took special interest in building KFA as a premium airlines brand. KFA offered exotic cuisines provided choice in-flight entertainment and employed model like air hostesses. KFA won several awards. Among the more notables of them are: India's second Buzziest Brand in 2008 by The Brand Reporter. Asia Pacific's Top Airlines Brand, India's No. 1 Airline in customer satisfaction by Business World, Best airline in India / Central Asia at the Spytax World Airline Awards 2010.

The image that it created, enabled it to get the KFA brand valued by Grant Thorton at INR 4100 crore in 2011-12 even though the company was incurring losses. In March, 2016 this valuation was being probed by the Serious Fraud Investigation Office (SFIO). A Grant Thorton spokesperson said the firm fully stood by its brand valuation report on Kingfisher. He said, 'we believe it was appropriate in the context of when it was done and the purpose for which it was done". By the way, RBSA Advisors, a global valuation and transaction advisory firm carried out two valuation exercises of KFA brand in 2013 and 2015. In 2013, the KFA brand was valued at INR 200 crore and in 2015 it was valued at INR 100 crore. To the surprise of many, KFA which prided itself as a provider of premium services, acquired Air Deccan, a low cost carrier in 2007, changed its name to Simplify Deccan and subsequently to Kingfisher Red. Perhaps this acquisition was motivated by a desire to cross the legal hurdles of flying internationally quickly.

KFA started its international operations in September 2008. On September, 2011 Vijay Mallya announced that KFA would soon stop operations of Kingfisher Red as it did not believe in low-cost operations any longer. Since its inception, KFA never made money. It accumulated losses and debt. Even after two rounds of debt restructuring, it defaulted on its debt and other obligations. In September 2011, KFA made following disclosure to BSE that "the company has incurred substantial losses and its net wroth has been eroded. However, having regard to improvement in the economic sentiment, rationalization measures adopted by the company, fleet recovery and the implementation of the debt recast package with the lenders and promoters including conversion of debt into share capital, these interim financial statements have been prepared on the basis that the company is a going concern and that no adjustments are required to the carrying value of assets and liabilities".

KFA lenders later stated that they regarded the company as viable. On 15 November 2011. KFA released poor financial results indicating that the company was 'drowning in high-interest debt and loosing money'. Mallya suggested that the solution was for the Government to reduce fuel and other taxes. In 2012, the Directorate General of Civil Aviation suspended KFA's operator permit and KFA was grounded. In 2013, lenders begah to recall loans. In 2014, KFA loan was treated as NPA by lenders and United Bank of India declared KFA as a willful defaulter. According to the 2014-15 annual report of the group's holding company. United Breweries Limited, the consortium of bankers had invoked the company's corporate guarantee. In 2015, lenders began the recovery process. In 2016, SBI the lead banker in a consortium of 17 banks that have loans work INR 9000 crores to KFA said that they were trying to do everything possible to find a solution.

Questions :

Discuss the behavioural factors that may have led to the creation and destruction of KFA.

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