BUSINESS FINANCE ASSIGNMENT - 2.

1. Liquidity Preference refers to the preference of investors to hold liquid assets rather than securities or long term interest bearing investments.

2. The listing on the Indian Stock Exchange is likely to affect the dividend policy. Since there would be an increase inflow of capital i.e. money invested by private investors and the general public [shareholders], Sales and profits are likely to be increased, thus affecting the dividend policy.
Incase of conflict of Interest shareholders might be willing to recieve regular dividend payments, whereas the management would like to reinvest the profits and expand the business. This might have a negative effect on the risk managment programme and inorder to satisfy both the parties, the expected returns might be reduced.

3. Factors influencing the dividend policy of a company:-
a) Stock market:- Significant adverse reactions to announcements of dividend cuts can be displayed. Thus, in cyclical industries and for smaller and newer companies in the market, managers tend to conservatism in good years.
b) Cash Reserves:- Companies having large cash reserves accumulated over the years fear a takeover bid and hence may wish to distribute these profits thereby increasing shareholder

loyalty and limit the size of cash pile.

c) Tax:- Non-tax paying shareholders will prefer that companies distribute a large proportion of earnings in the form of dividends, rather than re-investing in projects.

d) Growth opportunities:- Companies in that project major growth potential may have high demand for capital investment to remain in competition. This demand may exceed their borrowings ability and hence they prefer to pay low dividends rather than marketing frequent rights issues.

e) Stability and Consistency- Companies with high policies attract investors seeking high payouts and vice-versa. Any changes in their policy could lead to adverse market reactions in the same that investors will now have to readjust their portfolios.

5 The individual should opt for sole proprietorship instead of floating a limited company as the former pays less taxes. This is because a corporation is treated as a seperate entity, meaning it has to pay the state as well as federal taxes on the money it earns.

4 Different types of business entities are: Sole proprietorship, Partnership, Limited Companies & Limited liability partnerships.

	SOLE PROPRIETORSHIP	PARTNERSHIP	LIMITED COMPANIES	LIMITED LIABILITY PARTNERSHIP
OWNERSHIP	Owned, managed, and controlled by an individual who is the recipient of all profits & bearer of all risks.	It is a business which is owned by more than one person. Can be owned in equal or unequal amounts by partners.	It is a business which has a seperate legal identity from the owners. Shareholders are owners of the company.	In this two or more members engage in a profit-making venture. There are no directors and Shareholders. The Company has a Seperate legal identity.
LIABILITY	Unlimited liability - if sued the total personal wealth of the sole trader can be used to pay off debts.	Unlimited liability - All partners are jointly liable and liable to the full extent of their Personal wealth for the deficiences in the business.	The owner's liability is limited to the fully paid value of their shares. If company becomes insolvent, creditors cannot claim further payment	liability of its members is limited. Actions can be taken on individual members who are found to

			from the owner's personal wealth beyond the fully paid value of their shares.	be negligent and fraudulent.
LEGAL STATUS.	No specific documentation required to establish such a business. Income tax returns need to be filed.	Most partnerships have a partnership agreement consists of rights of individual partners.	These must have: - Memorandum of Association: This records the intentions of the people concerned to form the business. - Articles of Association: This includes details of the internal rules for running the company.	No MOA or AOA required. LLP is governed. The partnership agreement that may already be in force within an existing partnership.

6. Modigliani and Miller's irrelevance propositions suggests that market value market value of any firm is independent of its capital structure. Modigliani and Miller's second irrelevance proposition is based on the expected rate of return on the common stock of a leveraged firm increases in proposition of the debt-equity ratio, expressed in market values.

7. Working capital is the cash or other liquidity assets that a business uses to cover day to day operations like paying bills and payrolls of employees. It is the difference between a company's current assets and its liabilities.

8. Economies of scale refers to the proportionate savings in costs gained by an increase level of productions. This can be done by buying inputs required for the production process in bulk or hiring more skilled and experienced managers to overlook the production or using advanced eg. better technology and getting rid of the obsolete one.

9. If a pension fund or investment company must report its financial position every year, it may be more averse to very short-term investment losses than if

it had to report only every three years. The consequences of this might be to force the fund to invest in less volatile assets to reduce the risk of having to report a poor financial position. It might therefore result in the fund investing less heavily in equities, and possibly also less heavily in long-term bonds.

10. Senario 2 is preferred over 1 as in the first case were potentially losing out on the time value of money even if its for a very insignificant amount of time. In the second senario we can potentially invest the 2000 rupees. and earn some amount in that one day even if its a small amount of time.

11. Holding costs are those associated with Strong inventory that remains unsold. The costs could include:

- Price of damaged or spoiled goods
- storage space
- Labor
- insurance.