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# Assignment - 2



1) Liquidity Preference - It refers to the preference of an Investor on how they want to invest. They could invest in highly liquid assets ~~like~~ or non-liquid assets depending ~~on~~ on their necessity. Example: Buying government bonds because they can be sold ~~o~~ to someone else before its ~~repay~~ redemption in case need arises.

2) Yes, the listing would affect their dividend policy. This is because after listing, they are ~~a~~ more easily available to the general public for investments. This can increase their shareholders and creditors. Hence, they would have to pay more dividends and interests which would create a need to change the dividend policy.

A conflict of interest would make the board of directors very cautious about their options. They would ~~like to~~ need to look at all the details of a project that could be risky. ~~Bn~~ This would make their risk management program very intense and complicated. They need to be able to take risks to increase their shareholders wealth but also need to make sure that they don't take extremely high risks affecting their creditors negatively.

3) Factors that can affect the dividend policy of a company are:

i) Profits earned - The companies need to make sure they have excess profits after retaining some of it for their ~~etc~~ business activities.

ii) Availability of cash - Depending on how much cash that the company has it can either give cash, dividend or other forms like discounts on sales or service provided to shareholders.

iii) Expectation of shareholders – The company sometimes even needs to consider the expectations of shareholders based on the dividends of previous years and even of those from other companies in the market to make sure that they have continued support of the shareholders.

4)

| | | Sole Proprietorship | Partnership | Company | Limited Liability Partnership |
|---|---|---|---|---|---|
| i) | Ownership | Owned by one person. | Owned by more than one person known as members. | Owned by more than one shareholder who owns stocks of the company. | Owned by more than one member like a partnership. |
| ii) | Liability | Owner is severly liable | All partners are severly liable. | Owners ~~are~~ have no liability only to the extent of shares owned in the company. | Owners have limited liability to extent of ~~shares in company~~ shares in the entity like a company. |
| iii) | Legal status | The owner and business ~~don't~~ are the same. They don't have a separate legal status. | Partners can be sued individually for the entity as a whole. | It is a separate legal entity of its own. | It is also a separate legal entity. |

5) A sole proprietor needs to pay taxes on the Income of the business only as according to the law the trader and the ~~enti~~ business are a single entity.

A company is a separate legal entity, so, ~~t~~ it needs to pay tax on its taxable income. Then it distributes its dividends to shareholders. These are also taxed by ~~the~~ same government based on the amount and there are also capital gains taxes on the shares. Hence, based on the tax policy, the Individual should choose to become a sole Trader.

6) Modigliani and Miller's irrelevance propositions are:

i) The market value of any firm is independent of its capital structure.

ii) The expected rate of return on the common stock of a leveraged firm increases in proportion to the debt-equity ratio, expressed in market values.

7) Working capital - It is the short-term assets used by a company for its business activities. Example: inventories, cash, ~~debts~~ bills receivables.

Fixed capital - It is the long-term assets needed by a company ~~to~~ to gain long-term goals. Example: machinery, long-term debts, property.

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8) Economies of scale is the concept that states that the scale at which a certain ~~project~~ project is being done will determine the returns and outputs of that project. A larger input will result in a larger output Lower cost per unit will result in higher profits per unit.

9) If a pension fund/investment company is required to report its financial position annually rather than triennially, it would make the board of directors more cautious and efficient as they would fear a hostile takeover in case of mismanagement. They would make sure that the company is doing well and would not be able to use any other years reports to make it look like they were always doing well like in case of triennially reporting.

10) I would prefer Scenario 2. This is because of the time-value of money. The value of money decreases over time, though it would be very minimal in just one day, there would still be some difference. Hence, I would prefer scenario 2, where I can use the money today to get better oppurtunities.

11) Costs of holding buffer inventory are:
i) Loss of value - The stock of goods may ~~loss~~ lose it value over time due to depreciation..
ii) ~~B~~ Becoming obsolete - The goods could become obsolete due to new technology.
iii) Time-value of money - Incase, there is no change in the price of the product in the future, you would actually earn lower than you were supposed to from it due to inflation.