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Lectures in English Module
(Online Courses)

For 1st year Master students, option: Finance and International Commerce

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Lecture 1: International Trade

Introduction:

When the customer walk into a supermarket shop and find an Italian shoe, a Brazilian coffee, and a bottle of Saudi juice, that allowed him to experiencing the products of international trade.

International trade allows countries to expand their markets and access goods and services that otherwise may not have been available domestically, as a result, the market is more competitive.

1- Definition of International Trade

International trade is the exchange of capital, goods, and services across international borders or territories because there is a need or want of goods or services.

International Trade refers to the exchange of products and services from one country to another. International trade consists of goods and services moving in two directions: Imports: flowing into a country from abroad, and Exports: flowing out of a country and sold overseas. International trade is a method of economic interaction between international entities.

Trading globally may give consumers and countries the opportunity to be exposed to new markets and products. Almost every kind of product can be found in the international market, for example: food, clothes, oil, jewellery, stocks, currencies, and water. Services are also traded, such as in tourism, banking, consulting, and transportation.

2- History of International Trade:

International trade started in ancient times. The Silk Road was the first major trade route that connected the East and the West. It was an important trade route for over 2,000 years, connecting Asia with Europe via the Middle East. The Silk Road began after the Han Dynasty (206 BC–220 AD) expanded its rule over Central Asia. This allowed Chinese people to travel to central Asia and start businesses there. The Silk Road was also known as "the road of silk" because it transported silk from China to Rome. Mercantilism affected the history of international trade in the 16th and 17th Centuries; Mercantilism was an economic theory in which a nation's wealth was measured by its gold reserves and net exports (exports minus imports). If a country sold more goods than it bought from other countries, it would have a positive balance of payments (BOP) and gain gold reserves.

The 18th Century saw the shift towards liberalism. It was in this period that Adam Smith, the father of Economics wrote the famous book 'The Wealth of Nations' in 1776 where in he defined the importance of specialization in production and brought International trade under the said scope. David Ricardo developed the Comparative advantage principle, which stands true even today.

All these economic thoughts and principles have influenced the international trade policies of each country. Though in the last few centuries, countries have entered into several pacts to move towards free trade where the countries do not impose tariffs in terms of import duties and allow trading of goods and services to go on freely.

The 19th century beginning saw the move towards professionalism, which petered down by end of the century. Around 1913, the countries in the west say extensive move towards economic liberty where in quantitative restrictions were done away with and customs duties were reduced across countries. All currencies were freely convertible into Gold, which was the international monetary currency of exchange. Establishing business anywhere and finding employment was easy and one can say that trade was really free between countries around this period. World War I started in 1914 with the assassination of Archduke Franz Ferdinand in Sarajevo. This event led to all European powers entering the war on either side. After four years of fighting, Germany surrendered on November 11, 1918. World War I left many countries in ruins and resulted in an economic crisis known as the Great Depression, that last caused by many factors, including overproduction, increased competition between companies, high tariffs on imported goods, and low export prices. All these factors led to lower demand for goods and services, resulting in unemployment rates hitting 25% in some places such as the USA and Canada. It took several years after the Great Depression ended before people started buying again because they feared losing their jobs again if they bought too much stuff. The Great Depression that lasted until the start of World War II in 1939. The post-World War II period saw a significant increase in international trade and an increasing number of countries joining the UN, which brought about more free trade agreements between member states. This period also saw the creation of many multinational corporations (MNCs) that could produce goods cheaply thanks to economies of scale and mass production techniques. These MNCs controlled much of global trade and became extremely powerful entities in their own right.

Today the understanding of international trade and the factors influencing global trade is much better understood. The context of global markets have been guided by the understanding and theories developed by economists based on Natural resources available with various countries which give them the comparative advantage, Economies of Scale of large scale production, technology in terms of e commerce as well as product life cycle changes in tune with advancement of technology as well as the financial market structures.

3- Advantages of International Trade

The 2021 FedEx Trade Trend Report, a survey of 1,000 U.S. small business leaders conducted by Morning Consult for FedEx, shows that as U.S. small businesses recover from the pandemic, international trade is increasingly seen as an opportunity.
Three in four respondents view expanding trade between the U.S. and customers in other countries as a positive trend, with nearly half believing that widening trade will help their business or company. International trade includes many advantages:

- ✓ **Increased Revenues:** One of the top advantages of international trade is increasing your number of potential clients. Each country you add to your list can open up a new pathway to business growth and increased revenues. Seventy eight percent of respondents to the 2021 FedEx Trade Trend Report agree that increasing trade will generate revenue opportunities and create more jobs

- ✓ **Benefits of increased competition**: A greater degree of competition leads to lower prices for consumers, greater responsiveness to consumer wants and needs, and a wider variety of products.

- ✓ **Comparative Advantage:** trade encourages a nation to specialize in producing or supplying only those goods and services which it can deliver more effectively and at the best price, after taking into account opportunity cost.
- ✓ **Economies of Scale:** if you sell your goods globally, you will have to produce more than if you sold just domestically. Producing in higher volumes provides greater economies of scale. In other words, the cost of producing each item is lower.
- ✓ **Competition:** international trade boosts competition. This, in turn, is good for prices and quality. If suppliers have to compete more, they will work harder to sell at the lowest price and

best quality possible. Consumers benefit by having more choice, more money left over, and top-quality goods.

- ✓ **Transfer of Technology:** increases thanks to international trade. Transfer of technology goes from the originator to a secondary user. In fact, that secondary user is often a developing nation.
- ✓ **Jobs:** great trading nations such as Japan, Germany, the UK, the USA, and South Korea have one thing in common. They have much lower levels of unemployment than protectionist countries.

- ✓ **Easier Cash-Flow Management:** Getting paid upfront may be one of the hidden advantages of international trade. When trading internationally, negotiating payment terms with vendors may look different. It could be a general practice to ask for payment upfront, whereas at home, you may generally wait longer to be paid. Expanding your business overseas could potentially help you manage cash flow better.

- ✓ **Better Risk Management:** A significant advantage of international trade is market diversification. Focusing only on the domestic market may expose you to increased risk from economic downturns, political factors, environmental events, and other factors. Becoming less dependent on a single market may help mitigate potential risks in your core market.
- ✓ **Enhanced Reputation**: Successes in one country can influence success in adjacent countries, which can raise your company's credibility abroad and at home. This is one of the advantages of international trade that may be difficult to quantify and, therefore, easy to ignore.

4- Disadvantages of International Trade:

Although there are international trade pros, there are also international trade cons. below we present some of international trade disadvantages:

- **Over-Specialization:** employees might lose their jobs in large numbers if global demand for a product decline.
- **New Companies:** find it much harder to grow if they have to compete against giant foreign firms.
- **National Security:** if a country is totally dependent on imports for strategic industries, it is at risk of being held to ransom by the exporter(s). Strategic industries include food, energy and military equipment.
- **Exchange rate risk**: Because exchange rates fluctuate there is also risk business trading in foreign currencies may not be able to forecast finances accordingly. Eve Watkins of Business Works says currency fluctuations could affect either the value of existing assets or liabilities denominated in foreign currency. She says this could ultimately result in a business becoming less competitive overnight, resulting in a loss of sales and loss of revenue.
- **Political risk**: Investing in different countries whose political regimes can change over time also poses a few risks. Governments could discriminatorily change laws, regulations or contracts governing an investment. According to the Harvard Business Review, interest in emerging markets has soared and host countries have learned more value can be extracted from foreign enterprises through regulatory control. Firms engaged in international business use a combination of legal contracts, insurance and trade in financial instruments to protect income streams. These approaches, however, offer little protection against policy risk.
- **Cultural risk**: In addition to policy, cultural differences could create problems for businesses wanting to trade overseas. UKTI states failure to take into account different cultures might lead to damaging and costly mistakes. This could range from causing offence by not observing correct protocol, to inappropriate packaging and marketing. It goes without saying that the

marketing of a certain business in one western country might differ to that of a country that is still developing and has differing cultural habits and beliefs.

- **Credit risk**: It is very easy to overlook the risk of non-payment when trading overseas too, according to UKTI. Businesses should establish the credit rating of potential clients in many countries and guard against non-payment through, for instance, letter of credit or arrange credit insurance. The risk comes with the impact of a customer's financial drawback of the firm and how to finance the offered credit period.

5- Policies of International Trade:

International trade policy are rules that define how exports and imports are conducted. It can be defined as the government's rules and regulations guiding and controlling trade with foreign countries, it is set in place by a government and affects the number of goods and services a country exports and imports. Policy-makers might want to employ a trade policy to benefit the domestic market and its industries. In an economy, there is a spectrum of trade policies. On one end there is free trade and on the other end, there is protectionism. Free trade is when there are no government restrictions on trade, under a free trade policy, there is no or very little government intervention in a country's trading practices. Protectionism is when governments set trade restrictions to help domestic industries, under protectionism, the government regulates the trade flowing in and out of a country to protect domestic industries and limit its reliance on other countries. Most countries are not one or the other but are located somewhere on this spectrum.

Lecture 2: International Market Entry Strategies

Market entry strategies allow companies to offer their products in international markets. Since there are many methods companies can use to sell their goods globally, they can choose a suitable approach based on their goals and target market. Understanding the different market entry strategies can help deciding which one offers the most benefits to a company. In this lecture, we define market entry strategies; discuss their importance and different market entry strategies that a company can use to take its products to international markets.

1. What are market entry strategies?

Market entry strategies are methods companies use to plan, distribute and deliver goods to international markets. The cost and level of a company's control over distribution can vary depending on the strategy it chooses. Companies usually choose a strategy based on the type of product they sell, the value of the product and whether shipping it requires special handling procedures. Companies may also consider their current competition and consumer needs.

To select an effective strategy, companies align their budgets with their product considerations, which often improve their chances of increasing revenue. The primary factors that affect a company's choice of international market entry strategy are:

- **Marketing:** Companies consider which countries contain their target market and how they would market their product to this segment.
- **Sourcing:** Companies choose whether to produce the products, buy them or work with a manufacturer overseas.
- **Control:** Companies decide whether to enter the market independently or partner with other businesses when presenting their products to international markets.
- **Scale of Entry:** The obvious issue here is cost. Entering a market on a large scale will require significant resources. Although this is more likely to make an impression on a new market as it will attract the attention of customers and local businesses alike, it may be risky financially if your company does not take off. Entering on a smaller scale can offer business owners the chance to learn about the new market and limit risks – however, you are much less likely to gain significant amounts of attention.

2. Why are market entry strategies important?

Market entry strategies are important because selling a product in an international market requires precise planning and maintenance processes. These strategies enable companies to stay organized before, during and after entering new markets. Since every company has its own goals for entering an international market, having the option to choose from various types of strategies can give a company the opportunity to find one that fits its needs.

3. Different market entry strategies for international markets:

There are several market entry methods that can be used.

- **Exporting**

Exporting is a typically the easiest way to enter an international market, and therefore most firms begin their international expansion using this model of entry**.** Exporting is the sale of products and services in foreign countries that are sourced from the home country. The advantage of this mode of entry is that firms avoid the expense of establishing operations in the new country. Firms must, however, have a way to distribute and market their products in the new country, which they typically do through contractual agreements with a local company or distributor. When exporting, the firm must give thought to labeling, packaging, and pricing the offering appropriately for the market. In terms of marketing and promotion, the firm will need to let potential buyers know of its offerings, be it through advertising, trade shows, or a local sales force.

Among the disadvantages of exporting are the costs of transporting goods to the country, which can be high and can have a negative impact on the environment. In addition, some countries impose tariffs on incoming goods, which will impact the firm's profits. In addition, firms that market and distribute products through a contractual agreement have less control over those operations and, naturally, must pay their distribution partner a fee for those services.

Firms export mostly to countries that are close to their facilities because of the lower transportation costs and the often greater similarity between geographic neighbors. For example, Mexico accounts for 40 percent of the goods exported from Texas.

Because the cost of exporting is lower than that of the other entry modes, entrepreneurs and small businesses are most likely to use exporting as a way to get their products into markets around the globe. Even with exporting, firms still face the challenges of currency exchange rates. While larger firms have specialists that manage the exchange rates, small businesses rarely have this expertise.

- **Licensing**

Licensing allows another company in your target country to use your property. The property in question is normally intangible – for example, trademarks, production techniques or patents. The licensee will pay a fee in order to be allowed the right to use the property.

Licensing occurs when one company transfers the right to use or sell a product to another company. A company may choose this method if it has a product that's in demand and the company to which it plans to license the product has a large market. For example, a movie production company may sell a school supply company the right to use images of movie characters on backpacks, lunchboxes and notebooks.

Licensing requires very little investment and can provide a high return on investment. The licensee will also take care of any manufacturing and marketing costs in the foreign market.

- **Franchising**

Franchising is somewhat similar to licensing in that intellectual property rights are sold to a franchisee. However, the rules for how the franchisee carries out business are usually very strict – for example, any processes must be followed, or specific components must be used in manufacturing.

A franchise is a chain retail company in which an individual or group buyer pays for the right to manage company branches on the company's behalf. Franchises occur most commonly in North America, but they exist globally and offer businesses the opportunity to expand overseas. Franchising typically requires strong brand recognition, as consumers in your target market should know what you offer and have a desire to purchase it. For well-known brands, franchising offers companies a way to earn a profit while taking an indirect management approach.

- **Outsourcing**

Outsourcing involves hiring another company to manage certain aspects of business operations for your company. As a market entry strategy, it refers to making an agreement with another company to handle international product sales on your company's behalf. Companies that choose to outsource may relinquish a certain amount of control over the sale of their products, but they may justify this risk with the revenue they save on employment costs.

- **Joint-venture**

A joint venture consists of two companies establishing a jointly-owned business. One of the owners will be a local business (local to the foreign market). The two companies would then provide the new business with a management team and share control of the joint venture.

There are several benefits to this type of venture. It allows you the benefit of local knowledge of a foreign market and allows you to share costs. However, there are some issues – there can be problems with deciding who invests what and how to split profits.

To determine if the joint-venture approach is suitable for the firm, the firm must decide what value the partner could bring to the venture in terms of both tangible and intangible aspects. The advantages of partnering with a local firm are that the local firm likely understands the local culture, market, and ways of doing business better than an outside firm. Partners are especially valuable if they have a recognized, reputable brand name in the country or have existing relationships with customers that the firm might want to access.

The disadvantages of partnering, on the other hand, are lack of direct control and the possibility that the partner's goals differ from the firm's goals.

- **Wholly owned subsidiary (greenfield venture)**

Greenfield investments are complex market entry strategies that some companies choose to use. These investments involve buying the land and resources to build a facility internationally and hiring a staff to run it. Greenfield investments may subject a company to high risks and significant costs, but they can also help companies comply with government regulations in a new market. These investments typically benefit large, established organizations as opposed to new enterprises.

The process of establishing of a new, wholly owned subsidiary is often complex and potentially costly, but it affords the firm maximum control and has the most potential to provide above-average returns. The costs and risks are high given the costs of establishing a new business operation in a new country. The firm may have to acquire the knowledge and expertise of the existing market by hiring either host-country nationals -possibly from competitive firms- or costly consultants. An advantage is that the firm retains control of all its operations.

- **Company ownership (Acquisitions)**

If your company plans to sell a product internationally without managing the shipment and distribution of the goods you produce, you might consider purchasing an existing company in the country in which you want to do business. Owning a company established in your international market gives your organization credibility as a local business, which can help boost sales. Company ownership costs more than most market entry strategies, but it has the potential to lead to a high ROI.

Acquisitions are appealing because they give the company quick, established access to a new market. However, they are expensive.

When deciding whether to pursue an acquisition strategy, firms examine the laws in the target country. China has many restrictions on foreign ownership, for example, but even a developed-world country like the United States has laws addressing acquisitions. For example, you must be an American citizen to own a TV station in the United States. Likewise, a foreign firm is not allowed to own more than 25 percent of a US airline.

Acquisition is a good entry strategy to choose when scale is needed, which is particularly the case in certain industries (e.g., wireless telecommunications).

Lecture 3: Balance of Trade (BOT) & Balance of Payments

1- What is the Balance of Trade (BOT)?

Balance of trade (BOT) is the difference between the value of a country's exports and the value of a country's imports for a given period. The balance of trade is also referred to as the trade balance, the international trade balance, the commercial balance, or the net exports.

The formula for calculating the BOT can be simplified as the total value of exports minus the total value of its imports. A country that imports more goods and services than it exports in terms of value has a trade deficit or a negative trade balance. Conversely, a country that exports more goods and services than it imports has a trade surplus or a positive trade balance.

A positive balance of trade indicates that a country's producers have an active foreign market. After producing enough goods to satisfy local demand, there is enough demand from customers abroad to keep local producers busy. A negative balance of trade means that currency flows outwards to pay for exports, indicating that the country may be overly reliant on foreign goods.

Calculating the Balance of Trade: A country's balance of trade is calculated by the following formula: <u>BOT= Exports−Imports</u>

Balance of trade is the largest component of a country's balance of payments (BOP).

2- What is the Balance of Payments?

The balance of payments (BOP), also known as the balance of international payments, is a statement of all transactions made between entities in one country and the rest of the world over a defined period, such as a quarter or a year. It summarizes all transactions that a country's individuals, companies, and government bodies complete with individuals, companies, and government bodies outside the country.

The balance of payments divides transactions into two accounts: the current account and the capital account:

- The Current Account represents a country's imports and exports of goods and services, payments made to foreign investors, and transfers such as foreign aid.

- The Capital Account indicates whether a country is importing or exporting capital. Big changes in the capital account can indicate how attractive a country is to foreign investors and can have a substantial impact on exchange rates.

Lecture 4: Financial Market

Introduction

Members of the society can be economically classified into two groups: Individual investors and savers. Individual investors are those who have the desire to create companies and institutions, and establish different projects, but they may not have the sufficient funds to do so. Individual savers, on the other hand, are those who have the money, but do not have the desire, knowledge or ability to invest it by themselves. Usually, savers belong to different classes of society such as workers, employees and retirees who can save part of their income. Investors tend to use their saved funds to help them to establish companies.

They divide corporate capital into stakes or portions where each portion is known as a share. They offer these shares for sale as each saver buys a number of those shares within the limits of his savings. This makes him a shareholder and a participant in the company's capital. Therefore, he becomes a part of its management and decisions according to his stake

in the company's capital. In other cases, investors do not wish to share the management and decision making of the company with the savers. Therefore, they tend to get the savers' money through borrowing, then dividing what they need of their corporate funds into portions, known as bonds. Savers buy these bonds within the limits of what they want and how much savings they have. In fact, they do this in anticipation for returns from holding these bonds, and then redeeming their value when their maturity is due.

1. Definitions:

- The Financial Market: a marketplace where the trading of securities occurs, including the stock market, bond market, forex market, and derivatives market, among others. Financial markets are vital to smooth operation of capitalist economies.

- Securities include: stocks, bonds and also currency trading. According to this, financial markets are divided into stock markets, bond markets and currency markets. Stocks are ownership instruments to a part of the issuer's capital, while bonds are considered debt instruments on the entity that issued them. When you purchase a stock, you become a participant or a shareholder in the company. On the other hand, if you purchase a bond, you become a creditor to this company. Savers purchase stocks for two reasons: first, to obtain part of the profits generated by the company. This is known as dividends. Second, the prices of these stocks may go up due to higher demand as a result of the company's growth and the increase in its earnings. Thus, the value of stocks owned by the investor increases. This is known as the capital gain.

Stocks are bought and sold on the market in a regulated and legal manner so dealers do not lose their rights. Usually, all these operations are made through financial brokerage firms that are authorized by a market regulator.

There are various types of stocks which are traded on the market. There are stocks that give their holder the right to attend the general assembly of the company and express his opinion on the way the company is managed. There are also bonus stocks: they are free shares granted to the owners of ordinary stocks in order to increase what they own in the company and to increase the company's capital as well. As for preferred stocks, they give their owner the right and priority to obtain his rights from the company. There are two main types of stock markets: the primary market and the secondary market.

The Primary Market:

a market where stocks are issued, that is when a company is established and offers its stocks to the dealers for the first time, or when the capital of an existing company is raised. When these stocks are listed in the market, the first buyer of the stock can sell it on a trading market, which is known as the secondary market. In other words, stocks are first issued and sold in the primary market, and then traded (bought and sold) in the secondary market.

The Secondary market:

Secondary market refers to a market where securities are traded after being initially offered to the public in the primary market and/or listed on the Stock Exchange. Majority of the trading is done in the secondary market. Secondary market comprises of equity markets and the debt markets.

2. Functions of Financial Market:

Financial markets in general, and stock markets in particular, have great importance given their multiple functions in serving the national economy. These services include the following:

Saving Encouragement: by providing fields to employ or invest funds, especially for those whom their income is higher than their expenses, and do not have enough time to pay attention to investment projects they want to start. Therefore, investing in the stock market provides good investment opportunities that encourage savers to increase their savings, take advantage of investment opportunities in the market and provide adequate capital for companies to make investments and sustain their business.

Risk mitigation: investing in the stock market reduces the risks of losing savings and money if the saver himself invested them in other areas where he does not have enough experience. In addition, one of the investment risks, inadequate liquidity, can be eliminated because the investor can sell his shares easily and quickly. He can also liquidate them whenever money is needed.

Increase economic growth: financing projects and investments listed in the stock market contributes to producing more goods and services and supporting economic growth. This leads to an increase in career opportunities for job seekers.

In addition, selecting shares of stocks in specific projects and companies contributes to steering the money and savings towards more feasible and profitable projects.

3. International Stock Markets

Newspaper and media headlines are full of news about international stock markets. As they say: the world has become globalized where the news is spread between its parties easily and simply. The most important news to be published about these markets is the performance indexes which we will define its concept then review some of the international and regional indexes as the following:

Stock Market Index:

A number that summarizes the price movement of all stocks listed in a market and usually represents the average of those prices. Stocks are not equal in their percentage representation of the index. Representing a company's stock depends on its weight in the market measured by the market value of the company divided by the market value of all listed companies in the market. Stock prices rise and fall due to supply and demand. When the demand for some corporate stock exceeds the supply, the price of this stock rises and subsequently the market index increases with the percentage represented by this stock in the index.

The Importance of the Index:

The stock market index reflects the condition of the national economy in general and the economic performance of listed companies in the market in particular. If the demand for the companies' production increased due to the economic boost, then the sales and earnings of these companies are expected to increase as well as their dividends to shareholders, which in turn pushes the prices of their stocks up and the whole market index. In this case, the market index turns green. However, if the performance in the market declines, the indicator changes its color to red.

Some of the Global Indexes:

Global financial markets have two types of indexes: General indexes that measure the market situation in general, and sector indexes that measure the market situation according to a particular sector such as banking, industrial, agricultural, communications and other sectors. In the following points we address the most important international and regional indexes.

U.S. Market Indexes:

• ***DOW Jones:*** is a major index that consists of four sub-indexes and the most famous of which is the Dow Jones Industrial Average. The value of the index is calculated based on the stocks of the thirty largest industrial companies in the United States of America.

• ***Standard and Poor's 500 (S&P 500):*** It comprises the stocks of the leading five hundred companies in several areas, including: manufacturing, transportation, utilities, money, banking, insurance, technology and services. These companies represent approximately 80% of the market value of shares traded on the New York Stock Exchange.

• ***NASDAQ:*** is the largest among all U.S. indexes. It contains the stocks of 3,200 companies, mostly technological.

European Market Indexes :

• United Kingdom :

Financial Times 100: (FT-100) this index includes the 100 most important UK companies'stocks in the London market, representing 70% of the total capital of registered companies.

• ***France***

CAC 40: this index includes the stocks of the forty most important French companies in Paris market.

• ***Germany***

DAX: this index contains the stocks of the 30 most significant companies, representing 70% of the market value of the companies registered in Frankfurt market.

Asian Market Indexes :

• ***Japan***

Nikkei Index : contains the stocks of 225 companies, representing about 70% of the market value of the companies registered in the Tokyo Stock Exchange.

4. Types of Financial Investments:

There are three aspects for savings investment: stocks, bonds and mutual funds.

• ***Stocks:*** investing in stocks is characterized by a high rate of return in the long term with a high chance of risk, which means that the investor may sustain some loss in his invested capital.

Bonds*:* it is known that private companies need financing and therefore sell bonds to savers to obtain the required funds. The government also resorts to issuing bonds to finance projects such as building schools, universities, hospitals, constructing roads, building bridges, power plants and other public projects. Although the government resources come from oil and fees, sometimes it may have to issue bonds in order to secure additional funding.

• ***Mutual Funds:*** these funds pool savings through a Muniment of title with equal values similar to stocks. They are called investment units. Investors tend to buy stocks of these funds to use some of the advantages that these funds have from the long experience in managing investment. In addition, these funds have the ability to diversify their investments, hence, reducing the risks because of the funds availability. Investors entrust the entity that manages their mutual funds to take decisions on their behalf. In general, the return on these stocks tend to be more secure with a return of more than the bond’s and less than the stock’s return .

The most important factor that drives investors to investing in a particular type of securities is searching for an investment that generates a high return and have a degree of risk which the investor can tolerate.

****Basic Conceptsrelated to Financial Markets:***

- Nominal Value, Book Value and Market Value:

An investor wanted to establish a plastic company. After studying the project’s cost, he found out that the company’s capital must be ten million Riyals. Since he does not have this amount, he turned to the savers’ money to participate in co-founding the company. Due to the large amount of capital required, he divided it into million shares. Each is worth 10 Riyals. The ten Riyals in this case are known as the share nominal value. Because the expected profitability of the project is high, a growing number of savers accepted to contribute to this project and purchase the issued stocks. The required capital was raised and the company was established. At the end of the first year, the company have generated a profit of two million Riyals, i.e. two Riyals profit per share of the company’s shares. The corporate management met to decide one of the following options: Distribute profits to shareholders, distribute part of the profits and keep the remaining, or do not distribute the profits of this year at all. Of course, when the decision is to keep the profit or part of it, the retained earnings are used in financing the company’s expansions and investments or in making provisions and reserves to face any emergencies.

If the distribution is not made, the value of the company assets in this case will be twelve million Riyals. This includes plots, buildings, machinery, equipment, production supplies available in the company, its money in treasury and in bank accounts, etc… . When the company’s assets increase to twelve million Riyals, the book value of a single share becomes twelve Riyals. (12 million Riyals ÷ one million stocks = 12 Riyals).

- ***Nominal Value:*** The share value when the company is established.

- ***Book Value:*** What shareholders expect to receive if the company were liquidated. The book value can be calculated by dividing the company’s assets by the number of shares.

- ***Provisions:*** Amounts of profit that are retained or cut off from the company’s revenue to be disposed of in one of the specific aspects of actual expenditures (such as buying new machinery or plots to expand the company) or for potential emergency expenditures (such as fire, higher production costs, or decreased company earnings).

- ***Earnings Per Share:*** Profits that are allocated to each share. It is not conditional that earnings should be in cash. They can be bonus shares distributed to shareholders. These profits, or even bonus shares, may also not be distributed, but rather reinvested and consequently the market value of the company’s shares increases.

- ***Total Return on Stock:*** return on the stock plus capital gain.

- ***Market value:*** the value of the share in the market. It is affected by the supply (the number of stocks available to investors) and the demand (the number of stocks investors wish to buy). The investor can know the market value of a share through the Stock Exchange website in addition to other means of mass media.

- ***Market Capitalization:*** it is calculated by multiplying the number of a company’s stocks by the current market price of the stock.

The company has evolved, the work expanded and the number of costumers has increased. At the end of the second year, its stocks were floated in an IPO in the stock market at a price of fifteen Riyals. Due to the good reputation of the company, the market price of the stock has risen to twenty five Riyals on the first trading Day. In other words, the market value of each share rose by ten Riyals from the offering price.

- **Securities portfolio:** it is a selected group of number of investment channels or number of securities that achieve the investor’s objectives in terms of return, degree of risk or growth.

- Bonds: It is a fixed income (debt) instrument issued for a period of more than one year with the purpose of raising capital. The central or state government, corporations and similar institutions sell bonds. A bond is generally a promise to repay the principal along with a fixed rate of interest on a specified date, called the Maturity Date.

- Mutual Funds: These are funds operated by an investment company which raises money from the public and invests in a group of assets (shares, debentures etc.), in accordance with a stated set of objectives. It is a substitute for those who are unable to invest directly in equities or debt because of resource, time or knowledge constraints. Benefits include professional money management, buying in small amounts and diversification.

- Equity/Share: Total equity capital of a company is divided into equal units of small denominations, each called a share. For example, in a company the total equity capital of $ 2,00,00,000 is divided into 20,00,000 units of $ 10 each. Each such unit of $ 10 is called a Share. Thus, the company then is said to have 20,00,000 equity shares of $ 10 each. The holders of such shares are members of the company and have voting rights.

- Debt instrument: represents a contract whereby one party lends money to another on pre-determined terms with regards to rate and periodicity of interest, repayment of principal amount by the borrower to the lender. In the Indian securities markets, the term ‘bond’ is used for debt instruments issued by the Central and State governments and public sector organizations and the term ‘debenture’ is used for instruments issued by private corporate sector.

- Index: An Index shows how a specified portfolio of share prices are moving in order to give an indication of market trends. It is a basket of securities and the average price movement of the basket of securities indicates the index movement, whether upwards or downwards.

Market Capitalization : The market value of a quoted company, which is calculated by multiplying its current share price (market price) by the number of shares in issue is called as market capitalization. E.g. Company A has 120 million shares in issue. The current market price is $. 100. The market capitalization of company A is $ 12000 million.

- Initial Public Offer (IPO): An Initial Public Offer (IPO) is the selling of securities to the public in the primary market. It is when an unlisted company makes either a fresh issue of securities or an offer for sale of its existing securities or both for the first time to the public. This paves way for listing and trading of the issuer’s securities.

Lecture 5: Project Feasibility Study

1. What is a Project Feasibility Study?

A feasibility study is an analysis that takes all of a project's relevant factors into account—including economic, technical, legal, and scheduling considerations- to ascertain the likelihood of completing the project successfully. Project managers use feasibility studies to discern the pros and cons of undertaking a project before they invest a lot of time and money into it.

Feasibility studies also can provide a company's management with crucial information that could prevent the company from entering blindly into risky businesses.

A feasibility study is simply an assessment of the practicality of a proposed plan or project. As the name implies, these studies ask: Is this project feasible? Do we have the people, tools, technology, and resources necessary for this project to succeed? Will the project get us the return on investment (ROI) that we need and expect?

A good Feasibility Study helps to objectively decide whether to proceed with a proposed project. A Feasibility Study should have broad considerations when considering whether to undertake a new project. It should consider things such as technological limitations, the marketplace, your marketing strategy, staffing requirements, schedule and financial projections.

2. The goals of feasibility studies are as follows

- To understand thoroughly all aspects of a project, concept, or plan
- To become aware of any potential problems that could occur while implementing the project
- To determine if, after considering all significant factors, the project is viable—that is, worth undertaking.

3. The Importance of Project Feasibility Study

Feasibility studies are important to business development. They can allow a business to address where and how it will operate. They can also identify potential obstacles that may impede its operations and recognize the amount of funding it will need to get the business up and running. Feasibility studies aim for marketing strategies that could help convince investors or banks that investing in a particular project or business is a wise choice.

Important: When doing a feasibility study, it's always good to have a contingency plan that you also test to make sure it's a viable alternative in case the first plan fails.

4. Conducting a Feasibility Study

Step One: Conduct a Preliminary Analysis

The primary purpose of the preliminary analysis is to screen project ideas before extensive time, effort, and money are invested. Two sets of activities are involved.

1. Describe or outline as specifically as possible the planned services, target markets, and unique characteristics of the services by answering these questions:
    - Does the practice serve a currently unserved need? (e.g., multicultural populations or age groups who are not currently being served)
    - Does the practice serve an existing market in which demand exceeds supply?
    - Can the practice successfully compete with existing practices because of an "advantageous situation," such as better design, price, location, or availability (e.g., balance assessment and rehabilitation, programmable devices)?
2. Determine whether there are any insurmountable obstacles. A "yes" response to the following indicates that the idea has little chance for success:
    - Are capital requirements for entry or continuing operations unavailable or unaffordable?
    - Do any factors prevent effective marketing to any or all referral sources?

If the information gathered so far indicates that the idea has potential, then continue with a detailed feasibility study.

Step Two: Prepare a Projected Income Statement

Anticipated income must cover direct and indirect costs, taking into account the expected income growth curve. Working backward from the anticipated income, the revenue necessary to generate that income can be derived in order to build a projected income statement.

Factors that determine this statement are services provided, fees for services, volume of services, and adjustments to revenues (e.g., actual reimbursement levels).

Step Three: Conduct a Market Survey

A good market survey is crucial. If the planner cannot perform this survey, an outside firm should be hired. The primary objective of a market survey is a realistic projection of revenues. The major steps include:

- Define the geographic influence on the market.
- Review population trends, demographic features, cultural factors, and purchasing power in the community.
- Analyze competing services in the community to determine their major strengths and weaknesses. Factors to consider include pricing, product lines, sources of referral, location, promotional activities, quality of service, consumer loyalty and satisfaction, and sales.

- Determine total volume in the market area and estimate expected market share.
- Estimate market expansion opportunities (e.g., responsiveness to new/enhanced services).

Step Four: Plan Business Organization and Operations

At this point, the organization and operations of the business should be planned in sufficient depth to determine the technical feasibility and costs involved in start-up, fixed investment, and operations. Extensive effort is necessary to develop detailed plans for:

- Equipment
- Merchandising methods
- Facility location and design (or layout)
- Availability and cost of personnel
- Supply availability (e.g., vendors, pricing schedules. exclusive or franchised products)
- Overhead (e.g., utilities, taxes, insurance).

Step Five: Prepare an Opening Day Balance Sheet

The Opening Day Balance Sheet should reflect the practice's assets and liabilities as accurately as possible at the time the practice begins, before the practice generates income.

Prepare a list of assets required for practice operations. The list should include item, source, cost, and available financing methods. Necessary assets include everything from cash necessary for working capital to buildings and land. Although the resulting list is rather simple, the amount of effort required may be extensive.

Liabilities to be incurred and the investment required by the practice must also be clarified. These items need to be considered:

- Whether to lease or buy land, buildings, and equipment
- How to finance asset purchases
- How to finance accounts receivable

Step Six: Review and Analyze All Data

This review is crucial, the planner should determine if any data or analysis performed should change any of the preceding analyses. Basically, taking this step means "Step back and reflect one more time."

- Re-examine the Projected Income Statement and compare with the list of desired assets and the Opening Day Balance Sheet. Given all expenses and liabilities, does the Income Statement reflect realistic expectations?
- Analyze risk and contingencies. Consider the likelihood of significant changes in the current market that could alter projections.

Step Seven: Make "Go/No Go" Decision

All the preceding steps have been aimed at providing data and analysis for the "go/no go" decision. If the analysis indicates that the business should yield at least the desired minimum income and has growth potential, a "go" decision is appropriate, anything less mandates a "no go" decision. Additional considerations include:

- Is there a commitment to make the necessary sacrifices in time, effort and money?
- Will the activity satisfy long-term aspirations?