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B.Com Honours

Semester V

Calicut University

ESSENTIALS OF INVESTMENT BANKING OPERATIONS

Course Code: COM5EJ316 • Module 2 Notes

Module II: Asset Management, Reconciliation, ISDA, & TLC

Covers mutual fund NAV calculations, hedge fund fee mechanics (2/20 rule), investment banking reconciliations (Nostro/Vostro), ISDA master agreements, and Trade Life Cycle (TLC) settlement.

Unit 4: Asset Management & Mutual Fund NAV Calculations

Structure: Sponsor, Trustee, AMC (Asset Management Company), Custodian. Net Asset Value (NAV):
$$\text{NAV} = \frac{\text{Market Value of Investments} + \text{Receivables} - \text{Accrued Liabilities}}{\text{Total Outstanding Units}}$$

Unit 5: Hedge Fund Operations & Fee Calculations

Hedge Funds: Private pooled investment vehicles for accredited investors. Fee Structure: 2/20 Rule (2% Annual Management Fee on AUM + 20% Performance Fee above Hurdle Rate subject to High-Water Mark).

Unit 6: Investment Banking Reconciliation Typologies

Reconciliation Types: Nostro Reconciliation ("Our account with you"), Vostro Reconciliation ("Your account with us"), Loro Reconciliation, Intra-company, & Inter-company reconciliations.

Unit 7: Reconciliation Process & Framework Integrity

Lifecycle: Data Ingestion $\rightarrow$ Matching Algorithm $\rightarrow$ Exception / Break Identification $\rightarrow$ Investigation $\rightarrow$ Resolution. Addresses operational & settlement risk.

Unit 8: ISDA Master Agreement & Architecture

ISDA (International Swaps and Derivatives Association): Standardized legal framework for OTC derivatives. Architecture: ISDA Master Agreement, Schedule, Credit Support Annex (CSA collateral), & Trade Confirmations.

Unit 9: Trade Life Cycle (TLC) ETP vs OTC Simulation

TLC Stages: Order Placement $\rightarrow$ Execution $\rightarrow$ Trade Capture $\rightarrow$ Validation/Enrichment $\rightarrow$ Confirmation/Affirmation $\rightarrow$ Clearing $\rightarrow$ Settlement (T+1 for ETPs vs OTC bespoke settlement).

Practical Solved Problem 1 (Mutual Fund NAV Calculation): Portfolio Market Value = ₹500 Cr, Cash = ₹20 Cr, Accrued Expenses = ₹10 Cr, Liabilities = ₹10 Cr. Total Units = 4 Crore. Calculate Net Asset Value (NAV) per unit.

$$\text{NAV} = (\text{Market Value of Assets} - \text{Liabilities}) / \text{Total Units}$$

Step-by-step Solution:

1. Total Assets = \$ 500 \text{ Cr} + 20 \text{ Cr} = 520 \text{ Cr} \$.
2. Total Liabilities = \$ 10 \text{ Cr} + 10 \text{ Cr} = 20 \text{ Cr} \$.
3. Net Asset Base = \$ 520 \text{ Cr} - 20 \text{ Cr} = \mathbf{\\$500 \text{ Cr}} \$.
4. **NAV per unit** = \$ \frac{500 \text{ Cr}}{4 \text{ Cr Units}} = \mathbf{\\$125.00} \$.

Practical Solved Problem 2 (Hedge Fund 2/20 Fee Calculation): Fund AUM at start = \$100 Million. End AUM before fees = \$120 Million. Management Fee = 2%, Performance Fee = 20% above 5% Hurdle Rate. Calculate total fees.

Management Fee = AUM * 2%; Performance Fee = (Gain - Hurdle) * 20%

Step-by-step Calculation:

1. Management Fee = \$ 100 \text{ M} \times 2\% = \mathbf{\\$2.0 \text{ Million}} \$.
2. Total Gross Return = \$ 120 - 100 = \$20 \text{ Million} \$ (20% gain).
3. Hurdle Return (5%) = \$ 100 \text{ M} \times 5\% = \$5.0 \text{ Million} \$.
4. Excess Profit above Hurdle = \$ 20 - 5 = \$15 \text{ Million} \$.
5. Performance Fee = \$ 15 \text{ M} \times 20\% = \mathbf{\\$3.0 \text{ Million}} \$.
6. **Total Fees Earned** = \$ 2.0 \text{ M} + 3.0 \text{ M} = \mathbf{\\$5.0 \text{ Million}} \$. Net Return to Investor = \$115M (15%).

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