

10 Financial Markets

Fastrack® Revision

► In an economy, there are two major sectors:

- **Households:** They save funds and are known as 'Savers'.
- **Business Firms:** They invest funds and are known as 'Investors'.

Financial markets act as a link between these two sectors.



► **Financial Market:** A financial market is a market for the creation (new issue of securities) and exchange (sale of existing securities) of financial assets.

► **Functions of Financial Market**

- **Mobilisation of Savings and Channelling them into Most Productive Use:** A financial market provides the choice of different investment options to savers, which helps them to invest or channelise their surplus funds into the most productive use.
- **Facilitates Price Discovery:** Households represent the supply of funds and the business firm represents the demand. The interaction between the demand and supply helps in price discovery of financial asset, which is being traded in a particular market.
- **Provides Liquidity to Financial Assets:** Financial market provides liquidity to financial assets as they can be easily converted into cash whenever required.
- **Reduces the Cost of Transaction:** Financial market helps in saving time, effort and money of the buyers and sellers at the time of trading in the market, by providing them valuable information.

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Scarce resources are allocated to those firms which have the highest productivity for the economy.

► **Classification of Financial Market:** Financial market can be classified as money market and capital market.

► **Money Market:** It is a market for short-term funds meant for dealing in monetary assets whose period of maturity is less than one year.

► **Features of Money Market**

- Market for short-term.
- No fixed geographical location.
- Major institutions involved in money market are RBI, Commercial Banks, LIC, GIC, etc.
- Common instruments of money market are call money, treasury bills, CP, CD, commercial bills, etc.

► **Instruments of Money Market**

► **Call Money:** Call money is short-term finance repayable on demand, whose maturity period varies from 1 day to 15 days, used for inter-bank transactions. As per RBI guidelines, commercial banks are required to maintain a minimum cash balance with RBI, known as Cash Reserve Ratio (CRR). RBI changes the CRR from time-to-time, which affects the availability of funds with commercial banks to be given as loans. Call money is used by banks to maintain the CRR. The interest rate paid on call money is known as 'Call Rate', which is highly volatile, that varies from day-to-day and sometimes even from hour-to-hour.

► **Treasury Bill (T-Bill):** It is an instrument of short-term borrowing issued by the Reserve Bank of India (RBI) on behalf of Indian Government.

It is also known as zero coupon bond, a T-Bill is issued by RBI on behalf of Central Government to meet its short-term requirement of funds. It is issued in the form of promissory note. They are highly liquid and have negligible risk. They are issued at discount and par.

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The instruments of money market are unsecured and highly liquid.

► **Commercial Bill:** It is a bill of exchange used by business firms to finance their working capital requirements. It is a short-term, negotiable, self-liquidating instrument which is used to finance the credit sales of firms. When goods are sold on credit, the buyer becomes liable to make payment on a specific date in future. The seller could wait till the specified date or make use of a bill of exchange. The seller (drawer) of the goods draws the bill and buyer (drawee) accept it. On being accepted, the bill becomes a marketable instrument and is called a trade bill. If the trade bill is accepted by a commercial bank, then it is known as a commercial bill.

► **Commercial Paper:** It is a negotiable instrument, i.e., it is freely transferable by endorsement and delivery. As CP is an unsecured instrument, it is issued only by large and creditworthy companies. It is often issued as an alternative to bank borrowings. It usually has a maturity period of 15 days to one year. It is issued to raise short-term funds at lower rates of interest than market rates. It also helps

to satisfy short-term requirements of funds like seasonal and working capital needs. It is sold at a discount and redeemed at par.

- **Certificate of Deposit:** It is issued by commercial banks or developmental financial institutions to individuals, institutions, corporations and companies. It is an unsecured, negotiable instrument in bearer form. They can be issued to individuals and corporation during periods of tight liquidity when the deposit growth of banks is slow but the demand for credit is high.
- **Capital Market:** It is a market for medium and long-term funds. It includes all the organisations, institutions and instruments that provides long-term and medium-term funds.
- **Features of Capital Market**
 - It is a market for long-term funds.
 - The main participants in capital market are banks, financial institutions, corporate bodies, foreign investors and retail investors.
 - Since the cost of securities may be low, investment can be made in the capital market with less capital.
 - The securities in capital market enjoy good liquidity.
 - The instruments in capital market carry high risk as the expected return on them is high.
- **Main Instruments of Capital Market**
 - Equity shares
 - Debentures
 - Preference shares
 - Bonds
- **Types/Segments of Capital Market**
 - Primary market
 - Secondary market
- **Constituents of Capital Market**
 - Development banks
 - Commercial banks
 - Stock exchanges

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 Capital market does not provide short-term finance up to one year.

Difference between Money Market and Capital Market

S.No.	Basis of Difference	Money Market	Capital Market
(i)	Meaning	It is a market for short-term funds.	It is a market for medium and long-term funds.
(ii)	Instruments involved	Commercial paper, treasury bill, certificate of deposit, call money, etc.	Bonds, debentures, equity and preference shares, asset securitisation, retained earnings, euro issues, etc.
(iii)	Investor types	Commercial banks, non-financial institutions, central bank, chit funds, etc.	Stock brokers, insurance companies, commercial banks, underwriters, etc.

(iv)	Market liquidity	Money markets are highly liquid.	Capital markets are comparatively less liquid.
(v)	Risk Involved	Money markets have low risk.	Capital markets are more riskier in comparison to money markets.
(vi)	Maturity of instruments	Instruments mature within a year.	Instruments take longer time to mature.
(vii)	Purpose served	To achieve short-term credit requirements of the trade.	To achieve long-term credit requirements of the trade.
(viii)	Functions served	Increasing liquidity of funds in the economy.	Stabilising economy by increase in savings.
(ix)	Return on investment achieved	ROI is usually low in money market.	ROI is comparatively high in capital market.

➤ **Primary Market (New Issue Market):** In this market, securities are sold for the first time, i.e., new securities are issued from the company.

➤ **Methods of Floatation of New Issues in Primary Market:** The securities may be issued in primary market by the following methods:

- **Public Issue through Prospectus:** Under this method, company invites public to apply for its securities through issue of prospectus.
 - A prospectus makes a direct appeal to investors to raise capital, through an advertisement in newspapers and magazines. For this, company also uses services of underwriters or brokers.
 - The issue is required to be listed on at least one stock exchange.
- **Offer for Sale:** Under this method, securities are not issued directly to the public. They are first issued to intermediaries like issue houses and stock brokers at a fixed price.
 - These intermediaries, in turn, resell the securities to the investing public at higher price.
 - This method saves the company from formalities and complexities of issuing securities directly to the public.

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 Primary market directly contributes to capital formation.

- **Private Placement:** It is the allotment of securities by a company to institutional investors and some selected individuals like UTI, LIC, GIC, etc. It is considered beneficial because it helps to raise funds more quickly than a public issue and the cost of floatation is saved.
- **Rights Issue:** Under this method, company offers the new shares to its existing shareholders in proportion of shares already held by them. Rights issue is a compulsory requirement under the Companies Act. However, this method can be used only by existing companies. This method gives

pre-emptive right to the existing shareholders to subscribe to new issue of shares according to the terms and conditions of the company.

► **Electronic Initial Public Offers (E-IPOs):** Under this method, company issues capital to public through online system of stock exchange.

- Under this, the issuing company enters into an agreement with stock exchange and has to appoint SEBI registered brokers to accept applications and place orders with the company.
- A registrar having electronic connectivity with stock exchange is also appointed.
- Securities have to be listed on any exchange other than the exchange through which company has earlier offered its securities.
- The lead manager coordinates all the activities of various intermediaries connected with the issue.

► **Secondary Market:** The secondary market is the market for the sale and purchase of previously issued or second-hand securities.

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In secondary market, securities are only exchanged between the investors.

► **Features of Secondary Market**

- It is the market for old/existing securities.
- Both buying and selling of securities takes place.
- Prices of the securities are determined by the forces of demand and supply.
- It involves dealings between two investors.
- Stock exchanges exist at fixed location.

Difference between Primary and Secondary Market

S.No.	Basis of Difference	Primary Market	Secondary Market
(i)	Meaning	In this market, securities are sold for the first time, i.e., new securities are issued from the company.	This is the market for the sale and purchase of previously issued or second-hand securities.
(ii)	Purchasing type	Direct purchase	Indirect purchase
(iii)	Parties to buying and selling	Buying and selling takes place between the company and investors.	Buying and selling takes place between the investors.
(iv)	To whom it provides financing	It provides financing to the existing companies for facilitating growth and expansion.	It does not provide any kind of financing.
(v)	Intermediaries involved	Underwriters	Brokers

(vi)	Price levels	Remains fixed	Price level varies with variations in demand and supply.
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► **Stock Exchange:** It is defined as an organisation or body of individuals, whether incorporated or not established for the purpose of assisting, regulating and controlling of business in buying, selling and dealing in securities.

► **Functions of Stock Exchange**

- Ensures liquidity and marketability of existing securities by providing a ready and continuous market for the sale and purchase of securities.
- Helps in determining the prices of the securities through the forces of demand and supply.
- It promotes the habit of saving and investment among the general public.
- It provides a legal framework for fair and safe dealings.
- It helps the companies in raising finance, thus facilitating capital formation and economic growth.
- It provides scope for healthy speculation in a controlled and restricted way.

► **Trading and Settlement Procedure:** Now a days, trading in securities is executed through an online, screen-based electronic trading system. All securities are bought and sold electronically in the broker's office through a computer terminal, which is connected to the computer system of the main stock exchange. Any member can log on to the site, feed the information about the shares, he wants to buy or sell and the price into the computer.

The following steps are involved in the trading for buying and selling of securities:

- Selection of a broker
- Opening demat account with depository
- Placing the order
- Match the share and best price
- Executing the order
- Issue of contract note
- Delivery of shares or marketing payment
- Settlement cycle
- Pay-out day working
- Delivery of shares in demat form

► **Dematerialisation:** It refers to the process of holding securities in electronic form.

► **Depository:** It is the organisation with which an investor has to open a demat account to hold securities in electronic form.

In India, there are two depositories:

- National Securities Depository Limited (NSDL)
- Central Depository Services Limited (CDSL)

The depository participant serves as a link between the investor and the depository, i.e., either NSDL or CDSL.

► **Screen-based Trading:** It refers to the process of buying or selling securities online.

► **Advantages of Screen-based Trading**

- As the investors get an access to the stock market during real time, there is complete transparency in the dealings.

- It provides a common platform for exchange of securities thereby increasing the efficient transactions by saving time, effort and money.
- This virtual market has a very wide reach hence it increases its liquidity.

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All Initial Public Offers (IPOs) are issued in dematerialisation form and more than 99% of the turnover is settled by delivery in demat form.

➤ **Securities and Exchange Board of India (SEBI):** The Securities and Exchange Board of India was established by the Government of India on 12th April, 1988 as an interim administrative body to promote orderly and healthy growth of securities market and for investor protection.

➤ Objectives of SEBI

- To regulate stock exchanges and the securities industry to promote their orderly functioning.
- To protect the rights and interests of investors, particularly individual investors and to guide and educate them.
- To prevent trading malpractices and achieve a balance between self-regulation by the securities industry and its statutory regulation.
- To regulate and develop a code of conduct and fair practices through intermediaries like brokers, merchant, bankers, etc. with a view to make them competitive and professional.

➤ Functions of SEBI

➤ Regulatory Functions of SEBI

- Registration and regulation of brokers, sub-brokers and other players in the financial market.
- Registration of collective investment schemes and mutual funds.
- Conducting enquiries and audits of stock exchanges and Intermediaries.
- Regulating portfolio exchanges, underwriters, merchant bankers and the dealings in the stock exchanges.
- Regulation of take over bids by the companies.

➤ Developmental Functions of SEBI

- Ensuring training of intermediaries of securities market.
- Conducting research and publishing information useful to all market participants.
- Facilitating flexibility in the working of capital markets.

➤ Protective Functions of SEBI

- SEBI prohibits fraudulent and unfair trade practices in the securities market.
- Promotion of fair practices and code of conduct in securities market.
- Undertaking steps for investor protection.
- Controlling insider trading and imposing penalties for such malpractices.



Practice Exercise



Multiple Choice Questions

Q 1. Which market directly contributes to capital formation?

- a. Money market
- b. Capital market
- c. Primary market
- d. Secondary market

Q 2. Ryan Ltd. requires ₹ 800 crore as additional capital to expand the business. The finance manager, Mr Rohit Saxena, suggested that the shares may be sold to investing public through intermediaries as the same will be less expensive. Identify the method through which the company decided to raise additional capital.

- a. Private placement
- b. Rights issue
- c. Offer for sale
- d. E-IPOs

Q 3. Which instrument of money market is generally used for inter-bank transactions?

- a. Treasury bill
- b. Call money
- c. Commercial paper
- d. Commercial bill

Q 4. Is issued to provide bridge financing.

- a. Commercial bill
- b. Call money
- c. Treasury bill
- d. Commercial paper

Q 5. Identify the advantage(s) of Electronic Trading System illustrated in the given picture:



- a. It ensures transparency.
- b. It increases the efficiency of operations.
- c. It increases efficiency of information being passed on, thus helping in fixing prices efficiently.
- d. All of the above

Q 6. Which of the following statement (s) is/are incorrect?
(CBSE SQP 2023-24)

- a. Providing liquidity to securities is one of the functions of stock exchange.
- b. Process of holding shares in electronic form is known as Dematerialisation.
- c. Securities and Exchange Board of India performs the regulatory function of controlling insider trading and imposing penalties for such practices.
- d. Capital market consists of commercial banks, development banks and stock exchange.

Q 7. Match the various terms of Financial Markets Column I with their respective statements in Column II.
(CBSE SQP 2023-24)

Column I	Column II
A. Financial market	(i) It is also known as the stock market
B. Primary market	(ii) It is a market for creation and exchange of financial assets
C. Secondary market	(iii) It is also known as new issue market

- | | |
|---------------------|---------------------|
| A B C | A B C |
| a. (ii), (iii), (i) | b. (i), (iii), (ii) |
| c. (iii), (ii), (i) | d. (i), (ii), (iii) |

Q 8. is a number assigned to each transaction by the stock exchange and is printed on the contract note.
(CBSE SQP 2023-24)

- Client code number
- Unique order code
- Permanent account number
- Depository participant number

Q 9. Arrange the steps involved in trading procedure at the stock exchange in correct sequence:
(CBSE SQP 2023-24)

- Settlement of Order
- Opening of Demat Account
- Placing of Order
- Execution of Order

- | | |
|---------------------------|---------------------------|
| a. (ii), (iv), (iii), (i) | b. (ii), (i), (iii), (iv) |
| c. (iii), (iv), (ii), (i) | d. (ii), (iii), (iv), (i) |

Q 10. has been established with the specific objective of providing a ready market for money market instruments.
(CBSE 2023)

- Discount Finance House of India
- Securities and Exchange Board of India
- Reserve Bank of India
- State Bank of India

Q 11. Which money market instrument is known as Zero Coupon Bonds?

- | | |
|---------------------------|--------------------|
| a. Call money | b. Commercial bill |
| c. Certificate of deposit | d. Treasury bill |

Q 12. If a company requires ₹ 50,00,000 for seven months to meet the working capital requirement, then the company should approach:

- | | |
|-------------------|-------------------|
| a. money market | b. capital market |
| c. Both a. and b. | d. None of these |

Q 13. For buying and selling of securities, it is compulsory to open:

- | | |
|--------------------|----------------------|
| a. savings account | b. recurring account |
| c. current account | d. demat account |

Q 14. Max Ltd. requires ₹ 15 crore as additional capital to expand its business. Mahesh Goel, the finance manager, thought that the public issue may be expensive on account of various mandatory and

non-mandatory expenses. So, it was decided to allot the securities to institutional investors. Identify the method through which the company decided to raise additional capital.

- | | |
|-------------------|----------------------|
| a. Rights issue | b. Private placement |
| c. Offer for sale | d. E-IPOs |

Q 15. Raghav's friend Raman works as a Chartered Accountant in Solutions Ltd. Raman, in a meeting with the Board of Directors of the company, came to know that the firm would soon be declaring a bonus issue which would result in increase in the price of shares. Considering this, Raman advised Raghav to purchase the shares of Solutions Ltd., who acted on his advice and bought the shares before time.

Which function of SEBI can control such malpractices?
(CBSE SQP 2020)

- | | |
|-------------------------|------------------------|
| a. Protective function | b. Regulatory function |
| c. Development function | d. All of these |

Q 16. Match the 'Methods of Floatation of New Issues' given under Column 'I' with the suitable statements under Column 'II'.

Column I	Column II
A. Offer for sale	(i) It involves inviting subscription from the public through issue of prospectus.
B. Rights Issue	(ii) It involves issue of capital to public through online system of stock exchange.
C. E-IPOs	(iii) It is a privilege given to existing shareholders to subscribe to a new issue of shares.
D. Offer through prospectus	(iv) It involves issue of securities through intermediaries like issuing houses.

- | | |
|---------------------------|---------------------------|
| A B C D | A B C D |
| a. (iv), (iii), (ii), (i) | b. (i), (ii), (iii), (iv) |
| c. (iv), (i), (ii), (iii) | d. (i), (iii), (ii), (iv) |

Q 17. Which money market instrument is issued by RBI on behalf of Central Government?

- | | |
|---------------------------|--------------------|
| a. Certificate of deposit | b. Treasury bill |
| c. Call money | d. Commercial bill |

Q 18. The allocative function of financial market helps in
(CBSE SQP 2023-24)

- Bringing transparency in trading procedure
- Earning higher rate of return to household sector
- Better functioning of depository
- Determining the prices of securities

Q 19. SEBI calls for information and issues a show cause notice to stock exchange and its officials seeking explanation and conducting audit and enquiry. Which function is SEBI performing?
(CBSE SQP 2023-24)

- | | |
|------------------------|-------------------------|
| a. Regulatory function | b. Development function |
| c. Protective function | d. Both a. and c. |

Q 20. This method of new issue gives pre-emptive right to the existing shareholders over such securities. Which method of floatation is highlighted in the given statement?

- a. Private placement b. Offer for sale
c. Rights issue d. E-IPOs

Q 21. Match the 'Money Market Instruments' given under Column 'I' with suitable statements under Column 'II'.

Column I	Column II
A. Commercial Paper	(i) Issued by RBI on behalf of Central Government to meet its short-term requirement of funds.
B. Certificate of Deposit	(ii) It is a bill of exchange used to finance the working capital requirements of business firms.
C. Treasury Bill	(iii) Companies use this instrument for bridge financing.
D. Commercial Bill	(iv) It is an unsecured, negotiable, short-term instruments in bearer form. Issued by commercial banks and development financial institutions.

A B C D

- a. (iii), (iv), (i), (ii)
c. (iv), (ii), (iii), (i)

A B C D

- b. (ii), (i), (iv), (iii)
d. (i), (iii), (ii), (iv)

Q 22. Only buying of securities takes place in:

- a. primary market b. secondary market
c. capital market d. None of these

Q 23. Which instrument does not relate to capital market?

- a. Call money b. Shares
c. Debentures d. Bonds

Q 24. In case of rights issue, shares are issued for:

- a. selected institutional investors
b. general public
c. existing shareholders
d. intermediaries like issuing houses

Q 25. Which of the following statement about call money is incorrect?

- a. Its maturity period varies from 1 day to 15 days
b. It is used to meet floatation cost
c. It is used to maintain the cash reserve ratio
d. It is used for inter-bank transactions

Q 26. It's a market for short-term funds that deal in monetary assets with a one-year maturity period:

- a. Primary market b. Secondary market
c. Capital market d. Money market

Q 27. For large and creditworthy enterprises, it is utilised as an alternative to bank borrowing. What exactly is it?

- a. Commercial paper b. Call money
c. Commercial bill d. None of these

Q 28. The stock exchange assigns a number to each transaction which is printed on the contract note. It is called:

- a. PAN Number b. Unique Order Code
c. Contract Note d. None of these

Q 29. The exchange will deliver the stock or make payment to the other broker on this day:

- a. Transaction day
b. Same day Immediately
c. Pay-in day
d. Pay-out day

Q 30. When opening a Demat account, an investor must supply which of the following information to the broker?

- a. Date of birth and address
b. Residential status
c. PAN number
d. All of the above

Q 31. Which of the following is a development function of Securities and Exchange Board of India? (CBSE 2023)

- a. Training of intermediaries of the securities market.
b. Promotion of fair practices and code of conduct in the securities market.
c. Undertaking steps for investor protection.
d. Prohibition of fraudulent and unfair trade practices.

Q 32. Rahul wants to buy shares of Rexter Ltd. which are being traded at the National Stock Exchange. He feels that the share prices will go up in the future. Which market should he approach for this purpose?

(CBSE 2023)

- a. Money market b. Primary market
c. Secondary market d. Both b. and c.

Q 33. Which of the following statement(s) is/are incorrect?

(CBSE 2023)

- a. Capital market refers to facilities and institutional arrangements through which long-term funds. both debt and equity are raised and invested.
b. Secondary market is the market where securities are sold by the company to the investor directly or through an intermediary.
c. Primary market is the market where only buying of securities takes place. Securities cannot be sold there.
d. Money market is a market for short-term funds which deals in monetary assets whose period of maturity is up to one year.

Q 34. The process of holding securities in electronic form is called dematerialisation. Which of the following statement does not relate to dematerialisation?

(CBSE 2023)

- a. Smooth transfer and settlement of trade through a single account in shares.
- b. Demat securities can be pledged or hypothecated to get loans.
- c. No danger of loss, theft or forgery of share certificates.
- d. Existing physical shares cannot be converted into electronic form.

Q 35. Statement I: Money market economises use of cash. Statement II: Money market deals with financial instruments that are close substitutes of money. Choose the correct option from the options given below:

- a. Statement I is true and II is false.
- b. Statement II is true and I is false.
- c. Both the statements are true.
- d. Both the statements are false.

Q 36. Statement I: Demat account is compulsory to open for buying and selling of securities. Statement II: Dematerialisation refers to the process of holding securities in electronic form. Choose the correct option from the options given below:

- a. Statement I is true and II is false.
- b. Statement II is true and I is false.
- c. Both the statements are true.
- d. Both the statements are false.

Q 37. Statement I: Electronic holdings can be converted into physical certificates with the process of dematerialisation. Statement II: There is no danger of theft, loss or forgery of share certificates in dematerialisation. Choose the correct option from the following:

(CBSE SQP 2023-24)

- a. Statement I is true and II is false.
- b. Statement II is true and I is false.
- c. Both the statements are true.
- d. Both the statements are false.



Assertion & Reason Type Questions

Directions (Q. Nos. 38-47): There are two statements marked as Assertion (A) and Reason (R). Read the statements and choose the appropriate option from the options given below:

- a. Both Assertion (A) and Reason (R) are true and Reason (R) is the correct explanation of Assertion (A).
- b. Both Assertion (A) and Reason (R) are true, but Reason (R) is not the correct explanation of Assertion (A).
- c. Assertion (A) is true, but Reason (R) is false.
- d. Assertion (A) is false, but Reason (R) is true.

Q 38. Assertion (A): Private placement is the allotment of securities by a company to institutional investors and selected individuals.

Reason (R): Primary market is expensive, so companies prefer to choose private placement.

Q 39. Assertion (A): Dematerialisation is the process by which physical form of securities are converted into electronic form.

Reason (R): SEBI's main purpose is to keep a check on malpractices and to protect the interest of investors.

Q 40. Assertion (A): Primary market is also known as the new issues market.

Reason (R): Primary market deals with the securities already traded in market.

Q 41. Assertion (A): Depository holds securities in electronic form.

Reason (R): Depository is formed for the purpose of free transferability of securities with speed, accuracy and security.

Q 42. Assertion (A): Financial market refers to the system consisting of financial institutions, financial instruments, regulatory bodies and organisations.

Reason (R): Shares, bonds and debentures are financial instruments.

Q 43. Assertion (A): Treasury bills are considered as negotiable instruments.

Reason (R): Treasury bills have assured yield and negligible risk of default due to soundness of RBI.

Q 44. Assertion (A): Commercial Paper is used for Bridge Financing.

Reason (R): Commercial Paper is a secured instrument and is issued by small companies.

Q 45. Assertion (A): Instruments of money market are close substitutes for money.

Reason (R): Discount Finance House of India provides a ready market for money instruments.

Q 46. Assertion (A): Primary market promotes capital formation directly.

Reason (R): Only buying of securities takes place in the primary market.

Q 47. Assertion (A): There exist an inverse relationship between call rate and other short-term money market instruments.

Reason (R): A rise in call rate makes other sources of finance like certificates of deposit and commercial paper cheaper and banks raise funds from these sources.

Answers

1. (c) Primary market
2. (c) Offer for sale
3. (b) Call money
4. (d) Commercial paper
5. (d) All of the above
6. (c) Securities and Exchange Board of India performs the regulatory function of controlling Insider trading and imposing penalties for such practices.
7. (a) A-(ii), B-(iii), C-(i)
8. (b) Unique order code
9. (d) A-(ii), B-(iii), C-(iv), D-(i)
10. (a) Discount Finance House of India
11. (d) Treasury bill
12. (a) money market
13. (d) demat account
14. (b) Private placement
15. (a) Protective function
16. (a) A-(iv), B-(iii), C-(ii), D-(i)
17. (b) Treasury bill
18. (b) Earning higher rate of return to household sector
19. (a) Regulatory function
20. (c) Rights Issue
21. (a) A-(iii), B-(iv), C-(i), D-(ii)
22. (a) primary market
23. (a) Call money
24. (c) existing shareholders
25. (b) It is used to meet floatation cost
26. (d) Money market
27. (a) Commercial paper
28. (b) Unique Order Code
29. (d) Pay-out day
30. (d) All of the above
31. (a) Training of Intermediaries of the securities market
32. (c) Secondary market
33. (b) Secondary market is the market where securities are sold by the company to the investor directly or through an intermediary.
34. (d) Existing physical shares cannot be converted into electronic form.
35. (c) Both the statements are true.
36. (c) Both the statements are true.
37. (b) Statement II is true and I is false.
38. (a) Both Assertion (A) and Reason (R) are true and Reason (R) is the correct explanation of Assertion (A).
39. (b) Both Assertion (A) and Reason (R) are true, but Reason (R) is not the correct explanation of Assertion (A).
40. (c) Assertion (A) is true, but Reason (R) is false.

41. (a) Both Assertion (A) and Reason (R) are true and Reason (R) is the correct explanation of Assertion (A).
42. (a) Both Assertion (A) and Reason (R) are true and Reason (R) is the correct explanation of Assertion (A).
43. (b) Both Assertion (A) and Reason (R) are true, but Reason (R) is not the correct explanation of Assertion (A).
44. (c) Assertion (A) is true but, Reason (R) is false.
45. (a) Both Assertion (A) and Reason (R) are true and Reason (R) is the correct explanation of Assertion (A).
46. (b) Both Assertion (A) and Reason (R) are true, but Reason (R) is not the correct explanation of Assertion (A).
47. (a) Both Assertion (A) and Reason (R) are true and Reason (R) is the correct explanation of Assertion (A).



Case Study Based Questions

Case Study 1

Read the extract given below and answer the questions on the basis of the same:

AsiaRec Limited is searching for options to raise ₹ 30,000 crore from the primary market for diversification and modernisation of existing projects. It hired the services of a renowned financial consultancy firm, Nile Ltd. to suggest options for the same. Nile Ltd. suggested a list of options to the Board of Directors of the company. It was decided that for the immediate requirement of ₹ 200 crore, the company will give a privilege to existing shareholders to subscribe to a new issue of shares according to the terms and conditions of the company. ₹ 5,000 crore would be raised by allotment of securities to a consortium of financial institutions, instead of inviting subscription from the public by making a direct appeal to investors to raise capital. It was further decided to raise capital to the tune of ₹ 7,000 crore through an issuing house. All these options were accepted by the Board of Directors. The Board further decided to raise ₹ 9,000 crore through the online system of the stock exchange by entering into an agreement with the exchange.

Q 1. Identify the method of floatation of new issues in the primary market, not taken up by AsiaRec Limited.

- a. offer for sale
- b. rights issue
- c. E-IPOs
- d. offer through prospectus

Q 2. " ₹ 5,000 crore would be raised by allotment of securities to a consortium of financial institutions, instead of inviting subscription from the public by making a direct appeal to investors to raise capital." Identify the method of floatation of new issues in the primary market being discussed above, which the company has decided to use.

- a. Offer for sale
- b. Private placement
- c. Rights issue
- d. Offer through prospectus

Q 3. Identify the reason which has made the firm raise funds from the institutional investor.

- a. It helps to raise funds quickly
- b. It is not expensive
- c. Both a. and b.
- d. None of the above

Q 4. How much money was raised by the company through E-IPOs?

- a. ₹ 30,000 crore
- b. ₹ 5,000 crore
- c. ₹ 9,000 crore
- d. ₹ 7,000 crore

Answers

1. (d) 2. (b) 3. (c) 4. (a)

Case Study 2

Read the extract given below and answer the questions on the basis of the same:

C. X. Ltd. Co. wants to raise funds for its new project by floating a new issue of shares in the market. Mr Akash Ranjan, the CEO of the company appointed 4 teams of experts who would suggest him regarding the methods that can be used for floatation of this new issue in the market.

Team 1, suggested that the company must send an invitation to the public to apply for its securities through an advertisement in newspapers and the contents of the invitation must be in accordance with provisions of Companies Act, SEBI disclosures and investor protection guidelines. The team also claimed this method as the most popular one.

Team 2, however, did not want the company to indulge in the formalities and complexities of issuing securities directly to the public. It suggested the CEO to issue the securities to the intermediaries like issuing houses and stock brokers at a fixed price, who would in turn sell it to the public.

Team 3, came up with an altogether different opinion and suggested that the company must sell the securities to some selected institutional investors and individuals like LIC, UTI, etc.

They claimed that the method suggested by them was the best because firstly, it was economical as it saved the mandatory and non-mandatory expenses of public issue and secondly, it helped to raise capital more quickly as compared to public issue.

Team 4, suggested to issue capital to public through an online system of stock exchange.

Mr Akash Ranjan considered all the suggestions and decided to go with the advice rendered by Team 3.

Q 1. Which method of floatation is advised by Team 1 to the CEO?

- a. E-IPOs
- b. Offer through prospectus
- c. Rights issue
- d. Offer for sale

Q 2. Which method of floatation is advised by Team 2 to the CEO?

- a. Offer for sale
- b. Rights issue
- c. Private placement
- d. E-IPOs

Q 3. Which method of floatation is advised by Team 4 to the CEO?

- a. E-IPOs
- b. Rights issue
- c. Offer through prospectus
- d. Offer for sale

Q 4. Which method of floatation is finally chosen by the CEO?

- a. Private placement
- b. Rights issue
- c. E-IPOs
- d. Offer for sale

Answers

1. (b) 2. (a) 3. (a) 4. (a)

Case Study 3

Read the extract given below and answer the questions on the basis of the same:

Tisca Lunar Limited is searching for options to raise ₹ 20,000 crore from the primary market for diversification and modernisation of existing projects. It hired the services of a renowned financial consultancy firm, Maha Laxmi Pvt. Ltd. to suggest options for the same.

Maha Laxmi Pvt. Ltd. suggested a list of options to the Board of Directors of the company. It was decided that for the immediate requirement of ₹ 1,500 crore, the company will give a privilege to existing shareholders to subscribe to a new issue of shares according to the terms and conditions of the company. ₹ 4,500 crore would be raised by allotment of securities to a consortium of financial institutions, instead of inviting subscription from the public by making a direct appeal to investors to raise capital. It was further decided to raise capital to the tune of ₹ 6,000 crore through an issuing house. All these options were accepted by the Board of Directors. The Board further decided to raise ₹ 8,000 crore through the online system of the stock exchange by entering into an agreement with the exchange.

Q 1. Identify the method of floatation of new issues in the primary market, not taken up by Tisca Lunar Limited.

- a. Offer for sale
- b. Rights issue
- c. E-IPOs
- d. Offer through prospectus

Q 2. " ₹ 4,500 crore would be raised by allotment of securities to a consortium of financial institutions, instead of inviting subscription from the public by making a direct appeal to investors to raise capital." Identify the method of floatation of new issues in the primary market being discussed above, which the company has decided to use?

- a. Offer for sale
- b. Private placement
- c. Rights issue
- d. Offer through prospectus

Q 3. Identify the reason which has made the firm raise funds from the institutional investors?

- a. It helps to raise funds quickly
- b. It is not expensive
- c. Both a. and b.
- d. None of the above

Q 4. How much money was raised by the company through E-IPOs?

- a. ₹ 8,000 crore
- b. ₹ 4,500 crore
- c. ₹ 20,000 crore
- d. ₹ 6,000 crore

Answers

1. (d) 2. (b) 3. (c) 4. (c)

Case Study 4

Read the extract given below and answer the questions on the basis of the same:

Suresh is the CEO of a leading petrochemical company. Recently, the company issued share capital to cover some expenses. However, in order to meet the floating cost of issuing shares, the company decided to conduct Bridge Financing. Therefore, it decided to issue a money market tool. The CEO's decision wisely met the company's requirements. Three months later, the company decided to issue new shares in the primary market again. According to the floating method it involves, it decided to adopt the method mainly adopted by listed companies and attract the masses by directly contacting the public. Again, success came from the company's approach and the realisation of its goals. However, when the company tried the same type again three months later, the company encountered many problems. The problem is to determine a key aspect related to the security of the new release. If the same process is carried out in the secondary market, the company will not care too much about this key aspect.

Q 1. Which type of money market instrument was issued by the company in the earlier part?

- a. Call money
- b. Treasury bill
- c. Commercial paper
- d. Certificate of deposit

Q 2. Which method of floatation was adopted by the company three months later?

- a. E-IPOs
- b. Offer through prospectus
- c. Rights issue
- d. Offer for sale

Q 3. When the company repeated the same process again after three months, it faced problem in:

- a. Primary market
- b. Money market
- c. Commodity market
- d. None of these

Q 4. What key aspect the company would not have cared about in the secondary market?

- a. Pricing of securities
- b. Regulations from the government
- c. Safety of Investor's money
- d. None of the above

Answers

1. (c) 2. (b) 3. (a) 4. (a)

Case Study 5

Read the extract given below and answer the questions on the basis of the same:

Incorporated in 1990, Deepak Ltd., is one of the leading manufacturers and marketers of dairy-based branded foods in India. In the initial years, its operations were restricted only to collection and distribution of milk. But over the years it has gained a reasonable market share by offering a diverse range of dairy-based products including fresh milk, flavoured yogurt, ice-creams, butter milk, cheese, ghee, milk powders, etc. In order to raise capital to finance its expansion plans, Deepak Ltd. has decided to approach capital market through a mix of offer for sale of ₹ 5 crore shares and a public issue of ₹ 3 crore shares.

Q 1. Name and explain the segment of capital market being approached by the company.

Ans. Primary market is the segment of capital market being approached by the company. It is also known as the new issue market as the securities are issued for first time by the companies through this market.

Q 2. Identify the two methods of floatation used by the company to raise the required capital. Give one difference between them.

Ans. The two methods of floatation used by company to raise capital are:

- (i) Issue through prospectus.
- (ii) Offer for sale.

In case of issue through prospectus, the company approaches the member of general public directly by issuing a prospectus whereas in case of offer for sale, the company approaches members of general public indirectly through intermediaries like issuing houses, stock brokers, etc.

Case Study 6

Read the extract given below and answer the questions on the basis of the same:

Virat won a cash prize of ₹ 25,000 in the national level robotics competition. On the advice of his father, he visits a nearby bank to open a fixed deposit account in his name with the prize money. His sister Monika accompanied him to the bank. On reaching the bank, he notices big banners which are placed within the premises containing information about the various arrangements, through which corporates may raise their capital through the bank. Being a finance graduate, Monika explains to Virat that banks play the role of the financial intermediary by helping in the process of channelising the savings of the households into the most profitable business ventures.

Q 1. Name another financial intermediary that helps in the process of channelising the savings of the households into the most productive use.

Ans. Financial markets is the other financial intermediary that helps in the process of channelising the savings of the households into the most productive use.

Q 2. Also, outline any two functions of another financial intermediary as identified in Q.1.

Ans. The two functions of financial market are:

- (i) It helps to determine the price for the financial asset in a particular financial market through the market forces of demand and supply.
- (ii) It provides liquidity to the financial assets by providing ready markets wherein the securities can be converted into cash or vice-versa easily.

Case Study 7

Read the extract given below and answer the questions on the basis of the same:

Nile Limited is a real estate company which was formed in 1950. In about 56 years of its existence, the company has managed to carve out a niche for itself in this sector. Lately, this sector is witnessing a boom due to the fact that the Indian economy is on the rise. The incomes of middle class are rising. More people can afford to buy homes for themselves due to easy availability of loans and accompanying tax concessions. To expand its business in India and abroad, the company is weighing various options to raise money through equity offerings in India. Whether to tap equity or debt market? Whether to raise money from domestic market or international market or combination of both? Whether to raise the necessary finance from money market or capital market? It is also planning to list itself in New York Stock Exchange to raise money through ADR's. To

make its offerings attractive it is planning to offer host of financial plans products to its stakeholders and investors and also expand its listing at NSE after complying with the regulations of SEBI.

Q 1. What are the regulations of SEBI that the company must comply with?

Ans. Company must comply with regulatory functions of SEBI.

- (i) Registration and regulation of brokers, sub-brokers and other players in the financial market.
- (ii) Registration of collective investment schemes and mutual funds.

Q 2. How does the SEBI exercise control over Nile Limited in the interest of investors?

Ans. SEBI controls over Nile Limited in the interest of investors by exercising following protective functions:

- (i) SEBI prohibits fraudulent and unfair trade practices in the securities market.
- (ii) Undertaking steps for investor protection.



Very Short Answer Type Questions

Q 1. What is meant by allocative function of financial market?

Ans. It refers to linking the savers and investors by mobilising funds between them.

Q 2. Which method of short-term finance is adopted by banks to maintain their cash reserve ratio?

Ans. Commercial paper.

Q 3. State any two functions of financial market.

Ans. (i) Facilitates Price Discovery.
(ii) Reduces the Cost of Transaction.

Q 4. How does financial market facilitate 'Price Discovery' of financial assets?

Ans. Financial market facilitates price discovery of financial assets by interaction of forces of demand and supply.

Q 5. State any one common feature of capital and money market.

Ans. Both capital and money market arrange for transfer of funds from the suppliers to the users.

Q 6. Which bearer document is issued by a bank against deposits kept by the companies and institutions for a short period?

Ans. Certificate of Deposit.

Q 7. What is capital market?

Ans. Capital market is a market for medium and long-term funds. It includes all the organisations, institutions and instruments that provides long-term and medium funds.

Q 8. Which market is known as New Issue Market?

Ans. Primary market is known as new issue market.

Q 9. Who determines the prices of securities to be issued fresh in the primary market?

Ans. Management of the company.

Q 10. Which one directly promotes capital formation?

Ans. Primary market directly promotes capital formation as funds flow directly from savers to investors.

Q 11. Name the two major alternative mechanisms through which allocation of funds can be done.

Ans. (i) Banks; (ii) Financial Markets.

Q 12. Which method of primary market securities are not issued directly to the public?

Ans. Offer for sale.

Q 13. Name the two methods of floating new issues in the primary market.

Ans. (i) Offer through prospectus; (ii) Private placement.

Q 14. State any two features of secondary market.

Ans. (i) It is the market for old/existing securities.
(ii) It involves dealings between two investors.

Q 15. What do you mean by stock exchange?

Ans. It is defined as "an organisation or body of individuals, whether incorporated or not established for the purpose of assisting, regulating and controlling of business in buying, selling and dealing in securities."

Q 16. State any one function of stock exchange.

Ans. It provides a legal framework for fair and safe dealings.

Q 17. Define screen-based trading.

Ans. It refers to the process of buying or selling securities online.

Q 18. State any one objective of SEBI.

Ans. To regulate stock exchanges and the securities industry to promote their orderly functioning.

Q 19. State any one protective function of Securities and Exchange Board of India (SEBI).

Ans. SEBI prohibits fraudulent and unfair trade practices in the securities market.

Q 20. State any one developmental function of SEBI.

Ans. Ensuring training of intermediaries of securities market.

Q 2. Metaphil Ltd. is a large creditworthy company operating in the Kashmir Valley. It is an export-oriented unit, dealing in exclusive embroidered shawls. The floods in the valley have created many problems for the company. Many craftsmen and workers have been dislocated and raw material has been destroyed. The firm is, therefore, unable to get an uninterrupted supply of raw materials and the duration of the production cycle has also increased. To add to the problems of the organisation, the suppliers of raw materials, who were earlier selling on credit, are asking the company for advance payment or cash payment on delivery. The company is facing a liquidity crisis. The CEO of the company feels that taking a bank loan is the only option with the company to meet its short-term shortage of cash.

As a finance manager of the company, name and explain the alternative to bank borrowings that the company can use to resolve the crisis.

Ans. Commercial paper may be used by Metaphil Ltd. as it is a popular short-term instrument which is issued by large and creditworthy companies.

(i) It is a short-term unsecured promissory note, negotiable and transferable by endorsement and delivery with a fixed maturity period.

(ii) It has a maturity period of 15 days to 1 year.

(iii) It is sold at discount and redeemed at par.
e.g., it is used for bridge financing.

Q 3. Why there is less risk of default in case of money market?

Ans. There is less risk of default in case of money market because of two reasons:

(i) Shorter duration of investing i.e., less than 1 year.

(ii) Financial soundness of issuers which are primarily the government, banks and highly rated companies.

Q 4. When there is possibility of earning more returns in capital market?

Ans. There is possibility of earning more returns in the capital market when securities are held for longer duration.

It is because of two reasons:

(i) There is scope of earning capital gains on equity shares.

(ii) In long run, prosperity of company is shared by way of dividend and bonus shares.

Q 5. These days, the development of a country is also judged by its system of transferring finance from the sector where it is in surplus to the sector where it is needed the most. To give strength to the economy, SEBI is undertaking measures to develop the capital market. In addition to this, there is another market in which unsecured and short-term debt instruments are actively traded every day. These markets together help the savers and investors in directing the available funds into their most productive investment opportunity.



Short Answer Type-I Questions

Q 1. 'MYKAA Limited' is dealing in all types of cosmetic products. It is enjoying increased demand for its product during the last few years. For the purpose of expansion, the company needs ₹ 100 crore as additional capital. The company decides to raise funds through equity shares. Chirag Kapoor, the finance manager of the company recommended that the shares may be sold through issuing houses or brokers. Identify and explain the method recommended by Mr Kapoor through which the company can raise additional funds for expansion purposes. (CBSE 2022, Term-2)

Ans. **Offer for Sale:** Under this method, securities are not issued directly to the public. They are first issued to intermediaries like issue houses and stock brokers at a fixed price. These intermediaries, in turn, resell the securities to the investing public at higher price. This method saves the company from formalities and complexities of issuing securities directly to the public.

- (i) Name the function being performed by the market in the above case.
- (ii) Name the market segment other than the capital market segment in which unsecured and short-term debt instruments are traded. Also, given any three points of difference between the two.

Ans. (i) Function that is being performed by the market is 'allocation function.'

(ii) Market segment that is been referred by the market is money market.

Differences between money market and capital market are:

S.No.	Basis of Difference	Money Market	Capital Market
(a)	Instruments involved	Commercial papers, treasury bills, certificate of deposits, call money, etc.	Bonds, debentures, equity and preference shares, asset securitisation, retained earnings, euro issues, etc.
(b)	Investor types	Commercial banks, non-financial institutions, central bank, chit funds, etc.	Stock brokers, insurance companies, commercial banks, underwriters, etc.
(c)	Market liquidity	Money markets are highly liquid.	Capital markets are comparatively less liquid.

Q 6. Vaibhav Steel Ltd. is a large and creditworthy company manufacturing steel for the Indian market. It now wants to cater to the Asian market and decides to invest in new hi-tech machines. Since the investment is large, it requires long-term finance. It decides to raise funds by issuing equity shares. The issue of equity shares involves huge floatation cost. To meet the expenses of floatation cost, the company decides to tap the money market.

- (i) Name and explain the money market instrument the company can use for the above purpose.
- (ii) What is the duration for which the company can get funds through this instrument?
- (iii) State any other purpose for which this instrument can be used.

Ans. (i) Commercial paper is the instrument company can use for above purpose. It is a short-term unsecured promissory note, negotiable and transferable by endorsement and delivery with a fixed maturity period.

(ii) The company can get funds for a period of 15 days to 1 year by this document.

(iii) This instrument can also be used for bridge financing.

Q 7. "Primary market directly contributes to capital formation, whereas, secondary market does so indirectly." Do you agree?

Ans. Yes, I agree with the given statement. Primary market directly contributes to capital formation as it facilitates transfer of surplus funds from savers to entrepreneurs for setting up new projects, expansion, diversification, etc. On the other hand, secondary market indirectly contributes in capital formation by providing liquidity and marketability to existing securities. Through secondary market, investors can convert their securities into cash as and when required.

Q 8. Hari has 200 shares of Reliance industries. Reliance industries comes out with a fresh issue of shares and Hari received an offer to buy 1 more share of Reliance industries for every two shares held by him. Discuss the type of issue described.

Ans. The type of issue described above is 'Rights issue'. **Rights Issue:** Under this method, company offers the new shares to its existing shareholders in proportion of shares already held by them. Rights issue is a compulsory requirement under the Companies Act. However, this method can be used only by existing companies. This method gives pre-emptive right to the existing shareholders to subscribe to new issue of shares according to the terms and conditions of the company.

Q 9. Shweta is a professor in a reputed business institute. While explaining the procedure of stock exchange trading, she shared with her students that many years back she had bought 200 shares of a leading automobiles company. As per the settlement procedure, she paid for the shares and received the share certificates in physical form. However, when she had sent those certificates to the company to get them endorsed in her name, she was informed by the company that those certificates were duplicate.

Therefore, in order to protect the investors from many such malpractices, now only screen-based trading is done and dematerialisation is compulsory.

In the context of the above paragraph:

- (i) What is screen-based trading?
- (ii) Give the meaning of 'dematerialisation'. State any two of its advantages.

Ans. (i) Screen-based trading refers to the process of buying or selling securities online.

(ii) Dematerialisation refers to the process of holding securities in electronic form. The two advantages of dematerialisation are:

(a) The securities in demat account can be offered as security to raise loans.

(b) Since, the shares certificate are not held in physical form, there is no danger of loss, theft or forgery.

Q 10. Virat has 2500 shares of Suraj Bulb Ltd. He received an offer from Suraj Bulb Ltd. to purchase two shares for every ten shares held by him. Identify and explain the method of floatation of new issue reflected in the above lines.

(CBSE 2022, Term-2)

Ans. The method of floatation of new issue reflected in the above lines is 'Right Issue'.

Right Issue: Under this method, company offers the new shares to its existing shareholders in proportion of shares already held by them. Rights Issue is a compulsory requirement under the Companies Act. However, this method can be used only by existing companies. This method gives pre-emptive right to the existing shareholders to subscribe to new issue of shares according to the terms and conditions of the company.

Q 11. Harsh works as a manager in a software company. He opened a demat account with a broking house in order to trade in securities with the money he received as his first performance bonus. Since, then, he has been very active in stock trading under the guidance of a stock broker. However, when he was hospitalised for a few days this year, his wife received several calls from his stock broker for permission to transact on Harsh's behalf. Though she told him to wait till her husband had recovered, the stock broker went ahead and executed the transactions. When Harsh got home from hospital, he discovered that the unauthorised transactions had led to a loss for him.

Harsh complained to the broking house, but they claimed that he had authorised the transactions. Keeping in view, the guidelines issued by the National Stock Exchange that he had read in the national newspaper. Harsh demanded proof and threatened to file a complain. Since, the broking house had no evidence that the deals had been authorised they made good the loss that Harsh had incurred due to the transactions.

In the context of the above paragraph:

- (i) What is a demat account?
- (ii) Who is acting as the depository participant for Harsh?
- (iii) Name the document that is legally enforceable and helps to settle the claims between the investor and the broker.

Ans. (i) A demat account is an account used for holding securities in electronic form.
(ii) The broking house is acting as the depository participant for Harsh.
(iii) A contract note is a legally enforceable document that helps to settle the claims between investor and the broker.

Q 12. Explain following functions of financial market:

- (i) Facilitates Price Discovery
- (ii) Provides Liquidity to Financial Assets

Ans. (i) **Facilitates Price Discovery:** Households represent the supply of funds and the business firm represent the demand. The interaction between the demand and supply helps in price discovery of financial asset, which is being traded in a particular market.

(ii) **Provides Liquidity to Financial Assets:** Financial market provides liquidity to financial assets as they can be easily converted into cash whenever required.

Q 13. Briefly describe following instruments of Money:

(i) Treasury Bill (T-Bill)

(ii) Commercial Bill

Ans. (i) **Treasury Bill (T-Bill):** It is an instrument of short-term borrowing issued by the Reserve Bank of India (RBI) on behalf of Indian Government.

It is also known as zero coupon bond. A T-Bill is issued by RBI on behalf of Central Government to meet its short-term requirement of funds. It is issued in the form of promissory note. They are highly liquid and have negligible risk. They are issued at discount and par.

(ii) **Commercial Bill:** It is a bill of exchange used by business firms to finance their working capital requirements. It is a short-term, negotiable, self-liquidating instrument which is used to finance the credit sales of firms. When goods are sold on credit, the buyer becomes liable to make payment on a specific date in future. The seller could wait till the specified date or make use of a bill of exchange. The seller (drawer) of the goods draws the bill and buyer (drawee) accept it. On being accepted, the bill becomes a marketable instrument and is called a trade bill. If the trade bill is accepted by a commercial bank, then it is known as a commercial bill.

Q 14. Define SEBI. What is the reason for establishment of SEBI?

Ans. **Meaning of SEBI:** The Securities and Exchange Board of India (SEBI) was established by the Government of India on 12 April 1988 as an interim administrative body to promote orderly and healthy growth of securities market and for investor protection.

Reason for Establishment of SEBI: The capital market has witnessed tremendous growth during 1980's which led to a variety of malpractices on part of:

- (i) companies,
- (ii) brokers,
- (iii) merchant bankers,
- (iv) investment consultants,
- (v) others involved in securities market.

The malpractices that were done:

- (i) rigging of prices,
- (ii) non-adherence to provisions of the Companies Act,
- (iii) delay in delivery of shares etc.

As a result, investor's confidence was evoked and investor's grievances multiplied. The Government was helpless in redressing investor's grievances.

because of lack of proper penal provisions. So, it was decided to set up a separate regulatory body known as Securities and Exchange Board of India (SEBI).

Q 15. The stock market regulator, Securities and Exchange Board of India (SEBI), has initiated a certification programme for all market intermediaries. Under this programme, people associated with stock markets in any way, will have to obtain a qualifying certificate from the regulator. The National Institute of Securities Market (NISM), a trust formed by SEBI, is tasked with the certification programme.

In the context of the above paragraph:

(i) Identify the type of function performed by SEBI.

(ii) Outline any two reasons for setting up SEBI.

- Ans.** (i) Developmental function is being carried out by SEBI by starting a certification programme for all market intermediaries.
- (ii) SEBI was set up as a regulatory body by government for the following reasons:
- To protect the interests of investors and to guide and educate them.
 - To prevent trading malpractices.
 - To protect stock exchange and securities market.
 - To develop a code of conduct and faith practices by intermediaries in the securities market.

Q 16. State any five functions of a stock exchange.

(CBSE 2022, Term-2)

OR

State any three functions performed by the stock exchange.

(CBSE SQP 2022-23)

OR

State any three functions of stock exchange.

(CBSE SQP 2023-24)

- Ans.** The main functions of stock exchange are as follows:
- Ensures liquidity and marketability of existing securities by providing a ready and continuous market for the sale and purchase of securities.
 - Helps in determining the prices of the securities through the forces of demand and supply.
 - It promotes the habit of saving and investment among the general public.
 - It provides a legal framework for fair and safe dealings.
 - It helps the companies in raising finance, thus facilitating capital formation and economic growth.

Q 17. State any three objectives of the Securities and Exchange Board of India.

(CBSE SQP 2022-23, CBSE 2023)

- Ans.** The objectives of the Securities and Exchange Board of India are:
- To regulate stock exchanges and the securities industry to promote their orderly functioning.

(ii) To protect the rights and interests of investors, particularly individual investors and to guide and educate them.

(iii) To prevent trading malpractices and achieve a balance between self-regulation by the securities industry and its statutory regulation.

Q 18. State any three development functions of Securities and Exchange Board of India.

(CBSE 2023)

Ans. The development functions of Securities and Exchange Board of India are:

- Ensuring training for intermediaries of securities market.
- Conducting research and publishing information useful to all market participants.
- Facilitating flexibility in the working of capital markets.

Q 19. Distinguish between 'Capital Market' and 'Money Market' on the basis of (i) Participants (ii) Investment outlay (iii) Safety.

(CBSE 2023)

Ans. The differences between Capital Market and Money Market are:

S.No.	Basis of Difference	Capital Market	Money Market
(i)	Participants	Stock brokers, insurance companies, commercial banks, underwriters, etc.	Commercial banks, non-financial institutions, central bank, chit fund, etc.
(ii)	Investment outlay	Bonds, debentures, equity and preference shares, asset securitisation, retained earnings, euro issues, etc.	Commercial papers, treasury bills, certificate of deposits, call money, etc.
(iii)	Safety	Riskier both with respect to return and principal payment.	Much safer with minimum risk of default.

Q 20. State the first three steps involved in the screen-based trading for buying and selling of securities.

(CBSE SQP 2023-24)

Ans. The first three steps involved in the screen-based trading for buying and selling of securities are:

- The Investor has to approach a registered broker or sub-broker and sign a broker client agreement and a client registration form before placing an order to buy or sell securities.
- The Investor has to open a 'demat' account or 'beneficial owner' account with a depository participant for holding and transferring securities in the demat form.
- The investor then places an order with the broker to buy or sell shares, the broker will go ahead with the deal and issue the order confirmation slip to the investor.



Short Answer Type-II Questions

Q 1. Financial market is a market for creation and exchange of financial assets. It helps to link the savers with the investors and directs available funds into their most productive investment opportunity. It also facilitates easy purchase and sale of financial assets through the stock exchange. The stock exchange not only facilitates buying and selling of existing securities but also educates public about how their investments in the financial market can yield good returns.

- (i) State any two functions performed by financial market.
- (ii) Explain two more functions of the stock exchange, other than those stated in the above case.

Ans. (i) Two functions of financial market are as follows:
 (a) Financial market links households (savers) and the business firms (Investor) by mobilising funds between them.
 (b) Financial market allocates funds available for investment into their most productive investment opportunity. This process of allocation of fund is called financial intermediation.
 (ii) Two functions of stock exchange are:
 (a) **Pricing of Securities:** Shares prices on a stock exchange are determined by the forces of demand and supply. Thus, stock exchange helps in determining prices of securities.
 (b) **Spreading Equity Cult:** Stock exchange plays an important role in ensuring wider share ownership by regulating new issues, better trading practices, etc.

Q 2. These days, the development of a country is also judged by its system of transferring finance from the sector where it is in surplus to the sector where it is needed most. To give strength to the economy, SEBI is undertaking measures to develop the capital market. In addition to this, there is another market in which unsecured and short-term debt instruments are actively traded everyday. These markets together help the savers and investors in directing the available funds into their most productive investment opportunity.

- (i) Name the function being performed by the market in the above paragraph.
- (ii) Also, explain briefly three other functions performed by this market.

Ans. (i) Function that is being performed is called allocation function. i.e. mobilisation of saving and channelising them into most productive use.
 (ii) Three functions of financial market are:
 (a) **Reduces the Cost of Transaction:** Financial market helps in saving time, effort and

money of the buyers and sellers at the time of trading in the market, by providing them valuable information.

(b) **Facilitates Price Discovery:** Households represent the supply of funds and the business firm represent the demand. The interaction between the demand and supply helps in price discovery of financial asset, which is being traded in a particular market.

(c) **Provides Liquidity to Financial Assets:** Financial market provides liquidity to financial assets as they can be easily converted into cash whenever required.

Q 3. Differentiate between Money Market and Capital Market on the following basis:

- (i) Expected return
- (ii) Safety
- (iii) Liquidity
- (iv) Instruments

Ans. The differences between Money Market and Capital Market are:

S.No.	Basis of Difference	Money Market	Capital Market
(i)	Expected return	Expected return is <u>less</u> .	Expected return is <u>high</u> .
(ii)	Safety	Much safer with minimum risk of default.	Riskier both with respect to return and principal payment.
(iii)	Liquidity	<u>High degree of liquidity</u> .	Securities are <u>less liquid</u> .
(iv)	Instruments	Treasury bills, commercial paper, certificate of deposit, trade credit, etc.	Shares, debentures, bonds, retained earnings, asset securitisation, euro issues, etc.

Q 4. Differentiate between Primary Market and Secondary Market on the following basis:

- (i) Company involvement
- (ii) Price determination
- (iii) Location
- (iv) Capital formation

Ans. The differences between Primary Market and Secondary Market are:

S.No.	Basis of Difference	Primary Market	Secondary Market
(i)	Company involvement	Securities are sold by company to investor <u>directly</u> .	Ownership of existing securities is exchanged between investors. <u>Company is not involved at all</u>

(ii)	Price determination	By the management of company.	By demand and supply of securities.
(iii)	Location	No fixed geographical location.	Located at specific places.
(iv)	Capital formation	The flow of funds is from savers to investors i.e., the primary market directly promotes capital formation.	Enhance liquidity of securities i.e., the secondary market promotes capital formation.

Q 5. During Navratras, Sohan finalises a deal to buy a new house. So, he visits a nearby branch of 'Labh Bank' to withdraw ₹ 10 lakh from his account in order to pay the token money to the seller. In the bank, he observes that a large number of customers are present to make cash withdrawals, probably because it is an auspicious time to make purchase. After sometime, he overhear some of the bank staff members telling his colleague that, "Today 'Labh Bank' is likely to fall short of cash and to make up for the deficit and maintain its cash reserve ratio it will have to approach another bank."

In the context of the above paragraph:

- Identify the instrument that 'Labh Bank' will use to meet its short-term requirements of funds.
- State any three features of the instrument as identified in point (i).

Ans. (i) Call money is the instrument used by 'Labh Bank' to meet its short-term requirements of funds.

(ii) Three features of call money are as follows:

- Call money is the instrument through which one bank may borrow money from another bank to maintain cash reserve ratio as per guidelines of RBI.
- Its maturity period may be from 1 day to 15 days.
- The rate at which the interest is paid on call money is called call rate.

Q 6. Make Good Technologies Ltd. is one of the top suppliers of security software products and solutions in India with a market share of over 20% in the retail segment. Its customers includes people all sections of the society i.e., both households and corporates. Its unique threat detection system works to detect security threats including virus attacks in real time to protect users' IT assets across varied platforms and devices. The company has an established track record of growth and financial performance. At present, the company operates only through its website. The company now intends to launch a range of computer

accessories and plans to market it by opening its own retail outlets. So, the board of directors of the company have decided to only raise capital for the first time through an issue of shares, but at the same time they do not wish to get into the hassles of launching a public issue of shares.

In the context of the above paragraph:

- Name and explain the way through which the company can raise finance by allotting securities to selective individuals and institutions only.
- Can the company also raise capital through a right issue? Why or why not? Give a reason to justify your answer.

Ans. (i) The company can raise finance by allotting securities to selective individuals and institutions only through Private Placement.

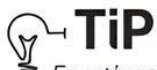
- It means allotment of securities by a company to institutional investors and some selected individuals.
- Those companies who can't afford public issue go for private placement.
- It helps to raise capital more quickly than a public issue.

(ii) No, the company cannot raise capital through right issue as it is issuing securities for the first time. A right issue is a pre-emptive right given to existing shareholders to subscribe to securities of company as per its terms and conditions.

Q 7. Stock exchange acts as a regulator of the securities market. It creates a continuous market where the securities are bought and sold. It gives investors the chance to disinvest and reinvest. Through this process of disinvestment and reinvestment, savings get channelised into their most productive investment avenues. To ensure that the investing public gets a safe and fair deal in the market, the membership of the stock exchange is well-regulated and its dealings are well-defined according to the existing legal framework. It also ensures wider share of ownership by regulating new issues, better trading practices and taking effective steps in educating the public about investments. Various functions performed by the stock exchange are discussed in the above para. By quoting lines from the above paragraph, state any four functions of stock exchange.

Ans. Functions of stock exchange are as follows:

- Ensures liquidity and marketability of existing securities by providing a ready and continuous market for the sale and purchase of securities.
- Helps in determining the prices of the securities through the forces of demand and supply.
- It helps the companies in raising finance, thus facilitating capital formation and economic growth.
- It provides scope for healthy speculation in a controlled and restricted way.



TiP

Functions of stock exchange and functions of SEBI are different. Students should not get confused between them.

Q 8. State any four methods of floatation of new issues in the primary market.

Ans. Four methods of floatation of new issues are as follows:

(i) **Public Issue through Prospectus:** Under this method, company invites public to apply for its securities through issue of prospectus.

(a) A prospectus makes a direct appeal to investors to raise capital through an advertisement in newspapers and magazines. For this, company also uses services of underwriters or brokers.

(b) The issue is required to be listed on at least one stock exchange.

(ii) **Offer for Sale:** Under this method, securities are not issued directly to the public. They are first issued to intermediaries like issue houses and stock brokers at a fixed price. These intermediaries, in turn, resell the securities to the investing public at higher price. This method saves the company from formalities and complexities of issuing securities directly to the public.

(iii) **Private Placement:** It is the allotment of securities by a company to institutional investors and some selected individuals like UTI, LIC, GIC, etc. It is considered beneficial because it helps to raise funds more quickly than a public issue and the cost of floatation is saved.

(iv) **Electronic Initial Public Offers (E-IPOs):** Under this method, company issues capital to public through online system of stock exchange.

(a) Under this, the issuing company enters into an agreement with stock exchange and has to appoint SEBI registered brokers to accept applications and place orders with the company.

(b) A registrar having electronic connectivity with stock exchange is also appointed.

(c) Securities have to be listed on any exchange other than the exchange through which company has earlier offered its securities.

(d) The lead manager coordinates all the activities of various intermediaries connected with the issue.

Q 9. Sanjeev Malik, the Managing Director of 'M.L.S. Ltd.' and Amit Puri, the Finance Manager were discussing about the avenues of investing the idle funds of the company. Sanjeev Malik was of the opinion that money should be invested in the capital market whereas Amit Puri, being more

conservative, feels that it would be better if the investment was made in money market. Since the economy was buoyant, the Managing Director convinced Amit that they should take advantage of it and invest in the capital market to get good returns. Ultimately, it was decided to invest the idle funds in the capital market.

(i) What kind of instruments should the company buy?

(ii) Why is the capital market expected to give a better return in a buoyant economy? State the reasons.

(iii) Why and how safe are the securities in this market as compared to money market?

Ans. (i) The instruments company should buy are shares, debentures and bonds.

(ii) Capital market is expected to give a better return in a buoyant economy as:

(a) Securities are held for longer duration.

(b) There is a scope of earning capital gains on shares.

(iii) Securities in capital market are riskier with respect to return and principal repayment. Issuing company may fail to perform as promoters may be fraud investors.

Q 10. Meet Securities Pvt. Ltd. was established to deal in securities. It was registered as a stock broker with National Stock Exchange (NSE) and Bombay Stock Exchange (BSE) to trade in securities listed at these exchanges it is also Depository Participant with CDSL and NSDL in the first three, it developed its business successfully after that the composition of board of directors changed some customers complained to the customer care centre of the company that shares purchased by them and for which the payment has been duly made, were not transferred to their Demat Accounts by 'Meet Securities Pvt. Ltd.' The executive of customer care centre promised the aggrieved customers that their shares will be transferred to their respective Demat Accounts very soon. But the company delayed the matter and didn't transfer the shares of the customers to their Demat Accounts. This eroded investors' confidence and multiplied their grievances.

(i) Identify the step of trading procedure in a stock exchange which has not been followed by 'Meet Securities Pvt. Ltd.'

(ii) Name the apex statutory body of capital market to whom customer can complain to redress their grievances.

(iii) Write two values not followed by 'Meet Securities Pvt. Ltd.'

Ans. (i) Delivery of shares in Demat form directly to investors Demat account by the broker.

(ii) The Securities and Exchange Board of India (SEBI).

(iii) (a) Honesty. (b) Commitment.

Q 11. Explain the following methods of floatation of new issue in primary market:

(i) Offer for sale

(ii) Private placement

Ans. (i) **Offer for Sale:** Under this method, securities are not issued directly to the public. They are first issued to intermediaries like issue houses and stock brokers at a fixed price. These intermediaries, in turn, resell the securities to the investing public at higher price. This method saves the company from formalities and complexities of issuing securities directly to the public.

(ii) **Private Placement:** It is the allotment of securities by a company to institutional investors and some selected individuals like UTI, LIC, GIC, etc. It is considered beneficial because it helps to raise funds more quickly than a public issue and the cost of floatation is saved.

Q 12. Due to various malpractices and exploitation of investors in the securities market, the Indian Government established a separate regulatory body to protect the investors and to develop and regulate the securities market.

(i) Identify the regulatory body set up by the government.

(ii) Discuss any three of its objectives.

Ans. (i) The regulatory body set up by the government is SEBI (Securities and Exchange Board of India).

(ii) Three objectives of SEBI are:

- To regulate stock exchanges and the securities industry to promote their orderly functioning.
- To protect rights and interests of investors and to guide and educate them.
- To prevent trading malpractices and to achieve a balance between self-regulation by the securities industry and its statutory regulation.

Q 13. Explain the following:

(i) Mobilisation of savings and channelling them into most productive use.

(ii) Reduces the cost of transaction.

Ans. (i) **Mobilisation of Savings and Channelising them into Most Productive Use:** A financial market provides the choice of different investment options to savers, which helps them to invest or channelise their surplus funds into the most productive use.

(ii) **Reduces the Cost of Transaction:** Financial market helps in saving time, effort and money of the buyers and sellers at the time of trading in the market, by providing them valuable information.

Q 14. State the protective functions of Securities and Exchange Board of India (SEBI).

OR

State any three protective functions of Securities and Exchange Board of India. (CBSE 2023)

Ans. The main protective functions of Securities and Exchange Board of India (SEBI) are:

- SEBI prohibits fraudulent and unfair trade practices in the securities market.
- Promotion of fair practices and code of conduct in securities market.
- Undertaking steps for investor protection.
- Controlling insider trading and imposing penalties for such malpractices.

Q 15. Anand Sharma is one of the Promoter-Director of Reliance Ltd. The company is engaged in the real estate sector, which has recently witnessed a steady fall in its revenue and the value of its assets due to a downward trend persisting in the market in specific and the economy in general. The periodical financial results of the company were to be declared in a fortnight time. Anand Sharma, being an insider, had access to unpublished price sensitive information related to it. Consequently, he sells a major portion of his holdings in an anticipation of a fall in the market price of the shares of the company subsequent to the announcement of periodical financial results of the company. Moreover, he doesn't inform the Securities and Exchange Commission (SEC) about the dealings. On conducting a probe, Securities and Exchange Board of India (SEBI) finds Anand Sharma guilty of insider trading. As per law, company directors, officials or any individual with a stake of 10% or more in the company are considered to be insiders and they are required to report their insider transactions within two business days of the date the transaction occurred.

In the context of the above paragraph:

(i) State the purpose of setting up SEBI.

(ii) Identify the type of function performed by SEBI by quoting lines from the paragraph.

Ans. (i) The purpose of setting up SEBI is:

- To regulate stock exchanges and the securities industry to promote their orderly functioning.
- To protect the rights and interests of investors, particularly individual investors and to guide and educate them.
- To prevent trading malpractices and achieve a balance between self-regulation by the securities industry and its statutory regulation.

(ii) Regulatory function is being performed by SEBI: "On conducting a probe, Securities and Exchange Board of India (SEBI) finds Anand Sharma guilty of insider trading."



Long Answer Type Questions

Q 1. Madhav's is one of the India's most trusted brands in Indian sweets and snacks segment. The company has manufacturing plants in Kota, Kanpur, New Delhi and Mumbai. Madhav's has its own retail chain stores and a range of restaurants in these cities. Now, the company plans to extend its business in 12 more cities in India. In order to raise the funds, its directors have decided to float a public issue through prospectus. Besides, it intends to raise money to meet the floatation costs in terms of brokerage, underwriting commission, advertising, etc.

In context of the above paragraph:

- What is the other name used for the funds required to meet floatation costs?
- Describe briefly the short-term instrument popularly used by the companies to raise for the funds required to meet floatation costs. Who can issue them?
- Distinguish between the two types of financial markets that the company intends to approach to meet its financial needs.

- Ans.** (i) Bridge financing.
- (ii) Commercial paper is that short-term instrument popularly used by the companies to raise funds required to meet floatation costs.
- It is a short-term unsecured promissory note, negotiable and transferable by endorsement and delivery a fixed maturity period.
 - It is issued by large and creditworthy company raise short-term funds at lower rates of interest than market rates. The purpose of commercial paper was to provide short-term funds for seasonal and working capital needs.
 - It has maturity period of 15 days to 1 year.
 - It is sold at discount and redeemed at par.
- (iii) The differences between Capital Market and Money Market are:

S.No.	Basis of Difference	Money Market	Capital Market
(i)	Instruments involved	Commercial papers, treasury bills, certificate of deposits, call money, etc.	Bonds, debentures, equity and preference shares, asset securitisation, retained earnings, euro issues, etc.

(ii)	Investor types	Commercial banks, non-financial institutions, central bank, chit funds, etc.	Stock brokers, insurance companies, commercial banks, underwriters, etc.
(iii)	Market liquidity	Money markets are highly liquid.	Capital markets are comparatively less liquid.

Q 2. After doing a course in online trading, Ashish started an online portal for stock trading under the name 'Investment Guru'. He met school friend Honey after a long time in a bank where Honey had come to open a Demat account. Ashish urged Honey to invest in the forthcoming IPO of a blue chip companies whereas Honey was inclined to buy existing securities of the other companies to build his investment portfolio.

In the context of the above paragraph:

- Identify the two different types of capital market being referred to by quoting lines from the paragraph.
- State any four differences between the two different types of capital markets as identified in point (i).

Ans. (i) The two different types of capital market being referred are:

(a) **Primary Market:** "Ashish urged Honey to invest in forthcoming IPO of a blue chip companies."

(b) **Secondary Market:** "Honey was inclined to buy existing securities of the other companies to build his investment portfolio."

(ii) The Differences between Primary and Secondary Market are:

S.No.	Primary Market (New Issue Market)	Secondary Market (Stock Exchange)
(i)	There is <u>new issues of securities by existing companies to investors</u> or there is sale of securities by new companies.	There is <u>trading of existing shares only.</u>
(ii)	Securities are sold <u>by company to the investor directly</u> or through an intermediary.	<u>Ownership of existing securities is exchanged between investors.</u> The company is not involved at all.
(iii)	The flow of funds is from <u>savers to investors</u> <u>Le., primary market directly promotes capital formation.</u>	<u>Enhance liquidity of shares Le., secondary market indirectly promotes capital formation.</u>
(iv)	<u>Only buying of securities takes place here.</u>	<u>Both buying and selling of securities takes place.</u>

Q 3. What is meant by 'New Issue Market'? Explain the various methods of flotation of new securities issues in this market. (CBSE 2018)

Ans. Meaning: Primary market is also known as 'new issue market'. It deals with new securities being issued for the first time.

Functions: Its function is to facilitate transfer of investable funds from savers to entrepreneurs seeking to establish new businesses.

(i) Public Issue through Prospectus: Under this method, company invites public to apply for its securities through issue of prospectus.

(a) A prospectus makes a direct appeal to investors to raise capital, through an advertisement in newspapers and magazines. For this, company also uses services of underwriters or brokers.

(b) The issue is required to be listed on at least one stock exchange.

(ii) Offer for Sale: Under this method, securities are not issued directly to the public. They are first issued to intermediaries like issue houses and stock brokers at a fixed price.

(a) These intermediaries, in turn, resell the securities to the investing public at higher price.

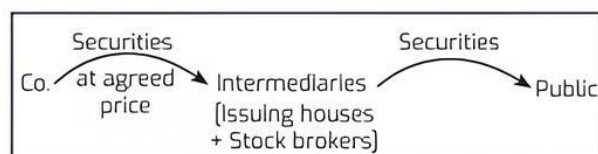
(b) This method saves the company from formalities and complexities of issuing securities directly to the public.

(iii) Private Placement: It is the allotment of securities by a company to institutional investors and some selected individuals like UTI, LIC, GIC, etc. It is considered beneficial because it helps to raise funds more quickly than a public issue and the cost of flotation is saved.

Q 4. MYKAA, a beauty products e-commerce company, is diversifying into men's grooming. It is also tapping the demand for beauty products in the fashion industry and amid professionals such as make-up artists. As it diversifies its online presence, Mykaa is also expanding its physical presence. They have 41 outlets across 18 cities presently and plan to expand to 180 outlets. Each store requires a capital expenditure of ₹ 60-80 lakh. The company has decided to raise funds by issuing equity shares but not directly to the public, rather by offering them for sale through brokers. Identify and briefly explain the method of floatation followed by the company. Also name and explain any two other methods of floatation that can be used by the company for raising funds from the public, in the primary market.

Ans. The method of floatation used is 'offer for sale.'

Offer for Sale: Under this method, securities are not issued directly to public but are offered for sale through intermediaries like issuing houses or stock brokers.



Other methods are:

(i) Private Placement:

(a) It means allotment of securities by a company to institutional investors and some selected individuals.

(b) Those companies who can't afford public issue go for private placement.

(c) It helps to raise capital more quickly than a public issue.

(ii) Rights Issue: It is a privilege given to existing shareholders to subscribe to a new issues of shares and the shareholders are offered the right to buy new shares in proportion to the number of shares they already possess.

Q 5. Sonalika got ₹ 10,00,000 after selling her parental property, which she had got as a gift from her grandmother. Her friend advised her to invest in securities in the stock market. Sonalika was unaware of procedure for the same. Her friend introduced her to a stock broker, who was registered with the national stock exchange. Sonalika approached the broker. The broker guided her to open a Demat account with a Depository, as well as a Bank account and Demat account with EXIN Bank.

(i) Identify the steps in the trading procedure for buying and selling of securities which have been discussed above.

(ii) State the next four steps of trading procedure.

Ans. (i) The steps in trading procedure are:

(a) Broker-Client Agreement and Providing Details:

- If any investor wishes to buy or sell any securities, he has to sign on a broker-client agreement and a client registration form before placing an order to buy or sell securities.



TIP

Steps in trading and settlement procedure should be memorised by students and especially sequence of steps should be correct.

- He also has to provide certain other details like:
 - PAN number (mandatory).
 - Date of birth and address.
 - Educational qualification and occupation.
 - Residential status (Indian/NRI).
 - Bank account details.
 - Depository account details.
 - Name of other broker with whom registered.

- Client code number in the client registration form, the broker then opens a trading account in the name of investor.

(b) Opening of Required Accounts: The investor has to open two accounts:

- Demat account/beneficiary owners account with a Depository Participant (DP) for holding and transferring securities in demat form.
- Bank account for cash transactions in securities market.

(ii) Next four steps of trading procedure are:

(a) Placing of Order: The investor then places an order with the broker to buy or sell shares by giving clear instructions about the number of shares and price at which the shares should be bought or sold. The broker will then go ahead with the deal. An order confirmation slip is issued to the investor by broker.

(b) Broker Go Online: The broker will then go online and connect to the main stock exchange and match the share and best price available.

(c) Execution of Order: When the shares can be bought or sold at the price mentioned, it will be communicated to the broker terminal and the order will be executed electronically. The broker will issue a trade confirmation slip to the investor.

(d) Insurance of Contract Note: After trade has been executed within 24 hours, the broker issues a contract note. This note contains details of the number of shares bought or sold, the price, the date and time of deal and the brokerage charges. A unique order code number is assigned to each transaction and is printed on contract note.

Q 6. Explain in detail the work of demat system.

Ans. Working of demat system are:

- An investor, either a bank, broker or financial services company may be identified.
- An account opening form and documentation (PAN, Photograph, Power of Attorney) may be completed.
- The physical certificate is to be given to DP along with dematerialisation form.
- If shares are applied in a public offer, simple details of DP and demat account are to be given and shares on allotment would automatically be credited to demat account.
- If shares are to be sold through a broker, the DP is to be instructed to debit the account with the number of shares.
- The broker then gives instructions to his DP for delivery of shares to the stock exchange.

(vii) The broker then receives payment and pay the person for the shares sold.

(viii) All the transactions are to be completed within 2 days, i.e., delivery of shares and payment received from buyer in on T+2 basis, settlement period.

Q 7. The Bombay Stock Exchange (BSE) is Asia's first stock exchange and the world's 11th largest stock exchange. It became the first stock exchange to be recognised by the Indian Government under the Securities Contracts Regulation Act. Its automated, screen-based trading platform called BSE Online Trading had a capacity of 8 million orders per day. The BSE has also introduced a centralised exchange based internet trading system, BSEWEBx.co.in to enable investors anywhere in the world to trade on the BSE platform.

In the context of the above paragraph:

- Name the organisation that regulates the working of stock exchanges in India.
- State any three functions performed by stock exchanges.
- Give any two advantages of screen-based trading.

Ans. (i) SEBI regulates the working of stock exchange in India.

(ii) Three functions of stock exchange are:

- Ensures liquidity and marketability of existing securities by providing a ready and continuous market for the sale and purchase of securities.
- Helps in determining the prices of the securities through the forces of demand and supply.
- It promotes the habit of saving and investment among the general public.

(iii) Two advantages of screen-based trading are:

- As the investors get an access to the stock market during real time, there is complete transparency in the dealings.
- It provides a common platform for exchange of securities thereby increasing the efficient transactions by saving time, effort and money.

Q 8. The SEBI has imposed a penalty of ₹ 7,269.5 crore on Pearls Agrotech Corporation Limited (PACL) and its four directors—Tarlochan Singh, Sukhdev Singh, Gurmeet Singh and Subrata Bhattacharya who had mobilised funds from the general public through illegal collective investment schemes in the name of purchase and development of agriculture land. While imposing the penalty, the biggest in its history, Securities and Exchange Board of India (SEBI) said that the company deserved 'maximum penalty' for duping the common man.

Its Prevention of Fraudulent and Unfair Trade Practices Regulations provides for 'severe to severe penalties' for dealing with such violations. As per SEBI norms, it can impose a penalty of ₹25 crore or three times of the profit made by indulging in fraudulent and unfair trade practices and in the present case, the regulator has imposed a fine equivalent to three times of the illicit gains.

In the context of the above situation:

- (i) State the objectives of setting up SEBI.
- (ii) Identify the type of function performed by SEBI by quoting lines from the paragraph.

- Ans. (i) The objectives of setting up SEBI are:
- (a) To the issuers, it aims to provide a market place in which they can confidently look forward to raising finances they need in an easy, fair and efficient manner.
 - (b) To the investors, it should provide protection of their rights and interests through adequate, accurate and authentic information and disclosure of information on a continuous basis.
 - (c) To the intermediaries, it should offer a competitive professionalised and expanding market with adequate and efficient infrastructure so that they are able to render better service to the investors and issuers.
- (ii) Protective function is being performed by SEBI. "The SEBI imposed a penalty of ₹ 7,269.5 crore on Pearls Agritech Corporation Ltd."

Q 9. Explain the main functions of SEBI.

Ans. The main functions of SEBI are:

(i) Regulatory Functions of SEBI

- (a) Registration and regulation of brokers, sub-brokers and other players in the financial market.
- (b) Registration of collective investment schemes and mutual funds.
- (c) Conducting enquiries and audits of stock exchanges and intermediaries.

- (d) Regulating portfolio exchanges, underwriters, merchant bankers and the dealings in the stock exchanges.
- (e) Regulation of take over bids by the companies.

(ii) Developmental Functions of SEBI

- (a) Ensuring training for intermediaries of securities market.
- (b) Conducting research and publishing information useful to all market participants.
- (c) Facilitating flexibility in the working of capital markets.

(iii) Protective Functions of SEBI

- (a) SEBI prohibits fraudulent and unfair trade practices in the securities market.
- (b) Promotion of fair practices and code of conduct in securities market.
- (c) Undertaking steps for investor protection.
- (d) Controlling insider trading and imposing penalties for such malpractices.

Q 10. State any five regulatory functions of the Securities and Exchange Board of India.

(CBSE SQP 2022, Term-2)

OR

State any three regulatory functions of the Securities and Exchange Board of India. (CBSE 2023)

Ans. The main regulatory functions of Securities and Exchange Board of India are:

- (i) Registration and regulation of brokers, sub-brokers and other players in the financial market.
- (ii) Registration of collective investment schemes and mutual funds.
- (iii) Conducting enquiries and audits of stock exchanges and intermediaries.
- (iv) Regulating portfolio exchanges, underwriters, merchant bankers and the dealings in the stock exchanges.
- (v) Regulation of take over bids by the companies.



Chapter Test

Multiple Choice Questions

Q 1. The allocated function is performed by:

- a. Financial Market
- b. Capital Market
- c. Money Market
- d. All of the above

Q 2. It is an instrument of short-term borrowing by the Government of India maturing in less than one year:

- a. Commercial bill
- b. Treasury bill
- c. Call money
- d. None of these

Q 3. The process of holding shares in electronic form is known as:

- a. Demutualisation
- b. Dematerialisation
- c. Speculation
- d. None of these

Q 4. Statement I: In secondary market, securities are only exchanged between the investors.

Statement II: SEBI prohibits fraudulent and unfair trade practices in the securities market.

Choose the correct option from the options given below:

- a. Statement I is true and II is false.
- b. Statement II is true and I is false.
- c. Both the statements are true.
- d. Both the statements are false.

Assertion and Reason Type Questions

Directions (Q. Nos. 5-6): There are two statements marked as Assertion (A) and Reason (R). Read the statements and choose the appropriate option from the options given below:

- a. Both Assertion (A) and Reason (R) are true and Reason (R) is the correct explanation of Assertion (A).
- b. Both Assertion (A) and Reason (R) are true, but Reason (R) is not the correct explanation of Assertion (A).
- c. Assertion (A) is true, but Reason (R) is false.
- d. Assertion (A) is false, but Reason (R) is true.

Q 5. Assertion (A): Instruments of the money market are close substitutes for money.

Reason (R): Discount Finance House of India provides a ready market for money market instruments.

Q 6. Assertion (A): Primary market promotes capital formation directly.

Reason (R): Only buying of securities takes place in the primary market.

Case Study Based Questions

Q 7. Read the extract given below and answer the questions on the basis of the same:

'Swarna Bank' is a bank, which needs immediate cash. ₹ 10 crore is to be raised from the primary market. For this purpose, finance manager of Punji Raksha Bank approached a renowned financial consultancy firm, Investors.com Private Limited for suggesting options for the same. It was decided that for the immediate requirement of ₹ 5 crore the company will give a privilege to existing shareholders to subscribe to a new issue of shares according to the terms and conditions of the bank. ₹ 2 crore would be raised by allotment of securities to a consortium of financial institutions, instead of inviting subscription from the public by making a direct appeal to investors to raise capital. All these options were accepted by the Board of Directors. The Board of Directors further decided to raise ₹ 3 crore through the online system of the stock exchange by entering into an agreement with the exchange.

(i) How much money was raised by the company through E-IPOs?

- a. ₹ 5 crore
- b. ₹ 2 crore
- c. ₹ 10 crore
- d. ₹ 3 crore

(ii) Identify the reason which has made the bank raise funds from the institutional investors.

- a. It helps to raise funds quickly
- b. It is not expensive
- c. Both a. and b.
- d. None of the above

(iii) Identify the method of floatation of new issues in the primary market, not taken up by Swarna Bank.

- a. Offer for sale
- b. Rights Issue
- c. E-IPO
- d. Offer through prospectus

(iv) "₹ 2 crore would be raised by allotment of securities to a consortium of financial institutions, instead of inviting subscription from the public by making a direct appeal to investors to raise capital." Identify the method of floatation of new issues in the primary market being discussed in the case which the company has decided to use.

- a. Offer for sale
- b. Private placement
- c. Right issue
- d. Offer through prospectus

Q 8. Read the extract given below and answer the questions on the basis of the same:

A company wanted to raise funds so it reached out to facilities an institutional arrangements through which long-term funds (debt + equity) were raised and invested. A lot of thinking was done whether the company should have gone for debt or equity. Finally, it decided to go for equity. The owner of the company decided to follow the guidelines of SEBI.

(i) Which concept of financial market is highlighted in the starting of the case?

(ii) Name any two objectives of SEBI.

Very Short Answer Type Questions

- Q 9. Mention the kind of issue in which stock is offered to an existing stockholder.**
- Q 10. State any one consequence of a well-performed allocative function of financial market.**
- Q 11. What is the common name for beneficiary owner account, which is to be opened by the investors for trading in securities?**

Short Answer Type-I Questions

- Q 12. Financial market plays an important role in the allocation of scarce resources in an economy of performing various functions. Explain any three functions of financial market.**
- Q 13. Explain any three methods of floatation of new issues in the primary market.**

Short Answer Type-II Questions

- Q 14. Explain any two instruments used in money market.**
- Q 15. State any four functions of stock exchange.**

Long Answer Type Questions

- Q 16. Explain the trading procedure on a stock exchange.**
- Q 17. Differentiate between primary market and secondary market.**