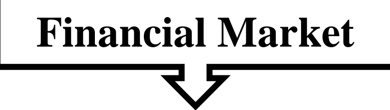
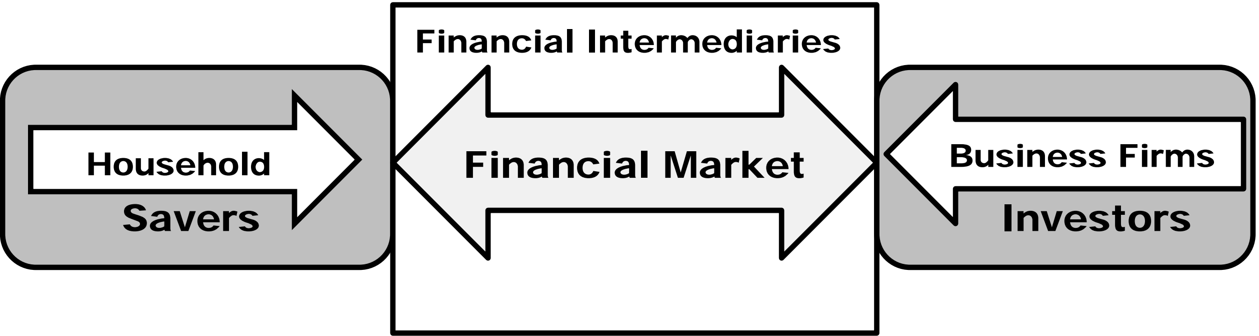
Chapter 6



Financial Market

It is a market where financial assets like shares, bonds etc. are creation and exchange.

It helps in mobilising savings and channelizing them into the most productive uses. It acts as link between the savers and the investors by mobilizing funds to channelizing between them.



The persons or institutions by which allocation of funds is done are called Financial Intermediaries. They bring together borrowers and lenders and make funds available to those willing to pay for their use,

Functions of Financial Market

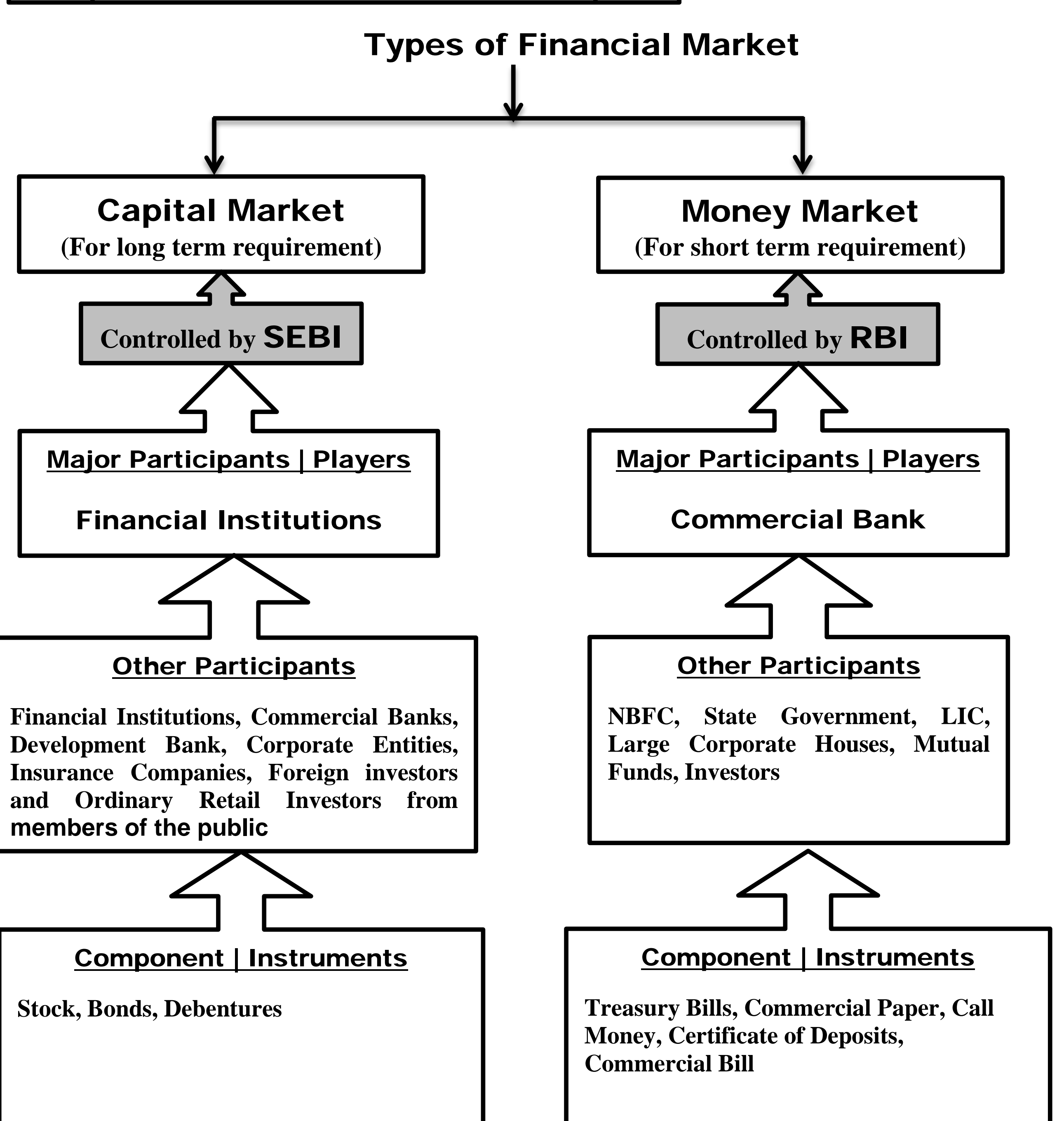
1. Mobilization of savings and channeling them into the most productive uses: A financial market facilitates the transfer of savings from savers to investors (industries) and thus helps to channelize surplus funds into the most productive use.

2. Facilitates price discovery: In the financial market, the households are suppliers of funds and business firms represent the demand. The interaction between them helps to establish a price for the financial asset which is being traded in that particular market.

3. Provide liquidity to financial assets: Financial markets facilitate easy purchase and sale of financial assets. In doing so they provide liquidity to financial assets, so that they can be easily converted into cash whenever required.

4. Reduce the cost of transactions: Financial markets provide valuable information about securities being traded in the market. It helps to save time, effort and money.

Types of Financial Markets



Money Market	Market for lending and borrowing of Short-term funds and financial instruments having a maturity period of one day to one year.
Capital Market / Security Market	Market for lending and borrowing of Long-term funds and financial instruments having a maturity period of more than one year

INDIAN MONEY MARKET

Meaning:-

The Money Market is a market for lending and borrowing of short-term funds. It deals in funds and financial instruments having a maturity period of **one day to one year**. It covers money and financial assets that are close substitutes for money. The instruments in the money market are of short term nature and highly liquid.

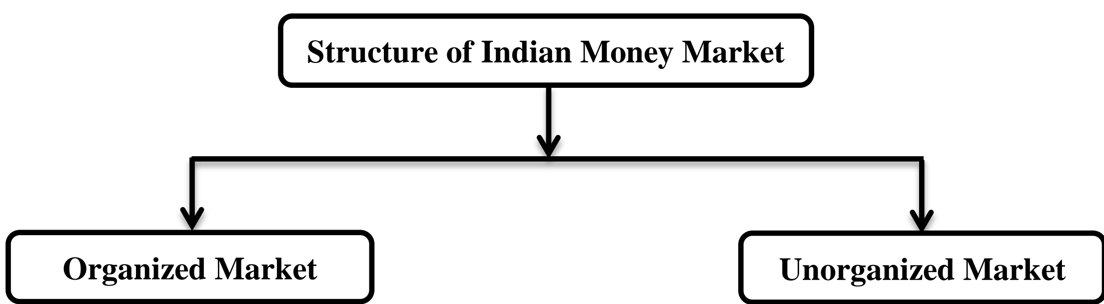
Definition :-

It is a market where low risk, unsecured and short term debt instruments that are highly liquid are issued and actively traded everyday

Structure (OR) components of Indian money market:-.

The Indian money market consists of two segments, namely organized sector and unorganized sector. The RBI is the most important constituents of Indian money market. The organized sector is within the direct purview of RBI regulation. The unorganized sector comprises of indigenous bankers, money lenders and unregulated non-banking financial institutions.

The structure or components of Indian money market



Organized Market

- **Call, Notice and Term Money Market**
- **Treasury Bills Market**
- **Commercial Bills Market**
- **Certificates of Deposits (CDs) Market**
- **Commercial Papers (CPs) Market**
- **Repurchase Agreement (Repos & Reverse Repo Market)**
- **Money Market Mutual Funds (MMMFs)**
- **Discount & Finance House of India (DFHI)**
- **Negotiable Certificates of Deposit**

Unorganized Market

- Indigenous Bankers
- Money Lenders
- Unregulated Non-Bank Financial Intermediaries (Chit Funds, Nidhis and Loan Companies)
- Finance Brokers

Money Market Instruments

1. Call Money Market | Notice Money Market | Term Money Market:

Under this market the day-to-day surplus funds (mostly of banks) are traded. The loans are of short-term duration varying from **1 to 14 days,** are traded in call money market. The money that is lent for one day in this market is known as **"Call Money",** and if it exceeds one day (but less than 15 days) it is referred to as "**Notice Money**". **Term Money** refers to Money lent for 15 days or more in the Inter-Bank Market.

Banks borrow in this money market for the following purpose:

- **To fill the gaps or temporary mismatches in funds**
- **To meet the Cash Reserve Ratio(CRR) & Statutory Liquidity Ratio(SLR) mandatory requirements as stipulated by the RBI**
- **To meet sudden** demand for funds arising out of large outflows.

Thus call money usually serves the role of equilibrating the short-term liquidity position of bank.

The main participants in the call money market are commercial banks (excluding RRBs), co-operative banks and primary dealers. Discount and Finance House of India (DFHI), Non-banking financial institutions such as LIC, GIC, UTI, NABARD etc. are allowed to participate in the call money market as lenders.

2. Treasury Bills (T-Bills):

Treasury bills or T-bills, which are money market instruments, are short term debt instruments issued by the Government of India and are presently issued in three tenors, namely, 91 day, 182 day and 364 day.

Treasury bills are zero coupon securities and pay no interest. Instead, they are issued at a discount and redeemed at the face value at maturity.

For example, a 91 day Treasury bill of Rs. 100/- (face value) may be issued at say Rs. 98.20, that is, at a discount of say, Rs.1.80 and would be redeemed at the face value of Rs.100/-. The return to the investors is the difference between the maturity value or the face value (that is Rs.100) and the issue price (

Currently, T- Bills are issued with 3 different maturity periods, which are, 91 days T-Bills, 182 days T- Bills, 1 year T – Bills.

There are no treasury bills issued by state governments.

Until 1988, the only kind of Treasury bill that was available was the 91-day bill, issued on tap; at a fixed rate of 4.5% (the rates on these bills remained unchanged at 4.5% since 1974). 182-day T-bills were introduced in 1987, and the auction process for T-bills was started. 364 day T-bill was introduced in April 1992, and in July 1997, the 14-day T-bill was also introduced. RBI had suspended the issue of 182-day T- bills from April 1992, and revived their issuance since May 1999. All T-bills are now sold through an auction process according to a fixed auction calendar, announced by the RBI. Ad-hoc treasury bills, which enabled the automatic monetisation of central government budget deficits, have been eliminated in 1997. All T-bill issuances now represent market borrowings of the central government.

91 days Treasury bill on tap: Before, 1960s the 91 days Treasury bills were sold on auction basis. Subsequently, these T-Bills were replaced by Tap sale of T-bills since mid-1960s. The tap bill

rates varied consistently with changes in the Bank Rate till 1974 and thereafter the discount rate on tap bill was fixed at 4.6%

Other maturities of T-bills: 182 days T-bills were introduced in November, 1986 on auction basis. The 182 days T-bills were replaced by introduction of 364 days T-bills on fortnightly auction basis since April, 1992. Subsequently, 91 days T-bills were introduced on auction basis in January, 1993. When the ad-hoc T-bills were discontinued in April, 1997, to enable finer cash management of the government and to provide avenue for state governments and some foreign central banks to invest surplus funds, 14-days T-bills were introduced in April, 1997. Subsequently, the 14 days T-bills and 182 days T-Bills were discontinued. Currently, 91 days T-Bills, 182 days T-Bills and 364 days T-Bills are sold on auction basis.

Treasury Bills – Chronology of Developments		
Type of T-Bill	**Introduced**	**Discontinued**
91 days T-Bill on weekly auction	**Before 1950s**	**Mid-1950s**
91 days Ad-hoc T-Bill	**Mid 1950s**	**April, 1997**
91 days T-Bill on Tap	**Mid 1950s**	**March, 1997**
182 days T-Bill on weekly auction	**November, 1986**	**April, 1992**
14 days T-Bill on weekly auction	**April, 1997**	**May, 2001**
364 days T-Bill on fortnightly auction	**April, 1992**	
91 days T-Bill on weekly auction	**January, 1993**	
182 days T-Bill on weekly auction	**Re-introduced in June, 1999**	**May, 2001**
182 days T-Bill on weekly auction	**Re-introduced in April, 2005**	

3. Commercial Bills:

Commercial bill is a short-term, negotiable, and self-liquidating instrument with low risk. They are negotiable instruments drawn by a seller on the buyer for the value of goods delivered by him. Such bills are called trade bills. When trade bills are accepted by commercial banks, they are called commercial bills. If the seller gives some time for payment, the bill is payable at future date (i.e. usance bill). Generally the maturity period is up to 90 days. During the usance period, if the seller is in need of funds, he may approach his bank for discounting the bill. Commercial banks can provide credit to customers by discounting commercial bills. The banks can rediscount the commercial bills any number of times during the usance period of bill and get money.

4. Certificates of Deposits (CDs):

CDs are unsecured, negotiable promissory notes issued at a discount to the face value. They are issued by commercial banks and development financial institutions. CDs are marketable receipts of funds deposited in a bank for a fixed period at a specified rate of interest. CDs were introduced in India in June 1989. The main purpose of the scheme was to enable commercial banks to raise funds from the market through CDs. According to the original

scheme, CDs were issued in multiples of Rs.25 lakh subject to minimum size of an issue being Rs.1 crore. They had the maturity period of 3 months to one year. They are freely transferable but only after the lock in period of 45 days after the date of issue.

5. Commercial Papers (CPs):

Commercial Paper (CP) is an unsecured money market instrument issued in the form of a promissory note with fixed maturity. They indicate the short-term obligation of an issuer. They are quite safe and highly liquid. They are generally issued by the leading, nationally reputed, highly rates and credit worthy large manufacturing and finance companies is the public as well as private sector. CPs were introduced in India January 1990. CPs were launched in India with a view to enable highly rated corporate borrowers to diversify their sources of short-term borrowings and also to provide an additional instrument to investors. RBI has modified its original scheme in order to widen the market for CPs. Corporates and primary dealers (PDs) and the all India financial institutions can issue CPs. A corporate can issue CPs provided they fulfill the following conditions: (a) The tangible net worth of the company is not less than Rs.4 crore. (b) The company has been sanctioned working capital limit by banks or all India financial institutions, and (c) The borrowed account of the company is classified as a standard asset by the financing institution or bank.

6. Trade Bill

Normally the traders buy goods from the wholesalers or manufactures on credit. The sellers get payment after the end of the credit period. But if any seller does not want to wait or in immediate need of money he/she can draw a bill of exchange in favour of the buyer. When buyer accepts the bill it becomes a negotiable instrument and is termed as bill of exchange or trade bill. This trade bill can now be discounted with a bank before its maturity. On maturity the bank gets the payment from the drawee i.e., the buyer of goods. When trade bills are accepted by Commercial Banks it is known as Commercial Bills. So trade bill is an instrument, which enables the drawer of the bill to get funds for short period to meet the working capital needs.

7. Collateral Loan Market

Collateral loan market deals with collateral loans i.e., loans backed by security. In the Indian collateral loan market, the commercial banks provide short- term loans against government securities, shares and debentures of the government, etc.

8. Repurchase Agreement (Repos & Reverse Repo Market):

A **repo** or **reverse repo** is a transaction in which two parties agree to sell and repurchase the same security. Under repo, the seller gets immediate funds by selling specified securities with an agreement to repurchase the same at a mutually decided future date and price. Similarly, the buyer purchases the securities with an agreement to resell the same to the seller at an agreed date and price. The repos in government securities were first introduced in India since December 1992.Since November 1996, RBI has introduced “Reverse Repos”, i.e. to sell government securities through auction.

9. Discount and Finance House of India (DFHI):

It was set up by RBI in April 1988 with the objective of deepening and activating money market. It is jointly owned by RBI, public sector banks and all India financial institutions which

have contributed to its paid up capital. The DFHI deals in treasury bills, commercial bills, CDs, CPs, short-term deposits, call money market and government securities. The presence of DFHI as an intermediary in the money market has helped the corporate entities, banks, and financial institutions to invest their short-term surpluses in money market instruments.

10. Money Market Mutual Funds (MMMFs):

RBI introduced MMMFs in April 1992 to enable small investors to participate in the money market. MMMFs mobilizes savings from small investors and invest them in short-term debt instruments or money market instruments such as call money, repos, treasury bills, CDs and CPs. These instruments are forms of debt that mature in less than a year.

11. Negotiable Certificates of Deposit:

Short term debt instrument offered by banks. They offer better returns than T-Bills due the fact that there is a slight degree of credit risk.

Cash Management Bills (CMBs)

In 2010, Government of India, in consultation with RBI introduced a new short-term instrument, known as Cash Management Bills (CMBs), to meet the temporary mismatches in the cash flow of the Government of India. The CMBs have the generic character of T-bills but are issued for maturities less than 91 days.

(B) UNORGANIZED SECTOR OF INDIAN MONEY MARKET

The unorganized Indian money market is largely made up of indigenous bankers, money lenders and unregulated non-bank financial intermediaries. They do operate in urban centers but their activities are largely confined to the rural sector. This market is unorganized because it’s activities are not systematically coordinated by the RBI.

The main components of unorganized money market are:

1. Indigenous Bankers:

They are financial intermediaries which operate as banks, receive deposits and give loans and deals in hundies. The hundi is a short term credit instrument. It is the indigenous bill of exchange. The rate of interest differs from one market to another and from one bank to another. They do not depend on deposits entirely, they may use their own funds.

2. Money Lenders:

They are those whose primary business is money lending. Money lenders predominate in villages. However, they are also found in urban areas. Interest rates are generally high. Large amount of loans are given for unproductive purposes. The borrowers are generally agricultural labourers, marginal and small farmers, artisans, factory workers, small traders, etc.

3. Unregulated non-bank Financial Intermediaries:

(a) Chit Funds: They are saving institutions. The members make regular contribution to the fund. The collected funds is given to some member based on previously agreed criterion (by bids or by draws). Chit Fund is more famous in Kerala and Tamilnadu.

(b) Nidhis: They deal with members and act as mutual benefit funds. The deposits from the members are the major source of funds and they make loans to members at reasonable rate of interest for the purposes like house construction or repairs. They are highly localized and peculiar to South India. Both chit funds and Nidhis are unregulated.

4. Finance Brokers:

They are found in all major urban markets specially in cloth markets, grain markets and commodity markets. They are middlemen between lenders and borrowers.

Based on the Vaghul Commitiee's recommendation's the Reserve Bank of India had jointly **set up** with the public sector banks and other all India **financial** institutions, the Discount and Finance House of India (DFHI) to deal in **money market instruments** in order to **provide liquidity** in the **money market**.

CAPITAL MARKET

Meaning

Capital market refers to the institutional arrangements for facilitating borrowing and lending of long term funds. It is the organised mechanism for effective and efficient transfer of money capital from individuals and institutional savers to entrepreneurs engaged in industry of commerce in both private sector and public sector. Modern capital markets are almost invariably hosted on computer-based electronic trading systems.
For a long time, the Indian capital market was considered too small to warrant much attention. However, this view has changed rapidly as vast amounts of international investment have poured into our markets over the last decade. The Indian market is no longer viewed as a static universe but as a constantly evolving market providing attractive opportunities to the global investing community.

Role / Functions of Capital Market:

Capital market plays an important role in mobilising resources, and diverting them in productive channels. In this way, it facilitates and promotes the process of economic growth in the country. It ensures better coordination between the flow of savings and the flow of investment that leads to capital formation and directs the flow of savings into most profitable channels.
In addition to resource allocation, capital markets also provide a medium for risk management by allowing the diversification of risk in the economy. A well-functioning capital market tends to improve information quality as it plays a major role in encouraging the adoption of stronger corporate governance principles, thus supporting a trading environment, which is founded on integrity.

Following are the main role or functions of capital market.

1. Link between Savers and Investors:

The capital market acts as a link between savers and investors. It plays an important role in mobilising the idle savings of people and diverting them in productive and profitable investment. In this way, capital market plays a vital role in transferring the financial resources from surplus and wasteful areas to deficit and productive areas, thus increasing the productivity and prosperity of the country.

2. Encouragement to Saving:

With the development of capital market, the banking and non-banking institutions provide facilities to invest money in stock market, which encourage people to save more. In the less developed countries, in the absence of a capital market, there are very little savings and those who save often invest their savings in unproductive and wasteful areas such as rela estate, gold etc.

3. Capital Formation:

The capital market facilitates lending to the businessmen and the government and thus encourages investment. It helps to mobilise the huge capital required for business. It is an important and efficient means to channel and mobilize funds to enterprises, and provide an effective source of investment in the economy.

4. Promotes Economic Growth:

The capital market not only reflects the general condition of the economy, but also smoothens and accelerates the process of economic growth. The proper allocation of resources results in the expansion of trade and industry in both public and private sectors, thus promoting balanced economic growth in the country. It plays a critical role in mobilizing savings for investment in productive assets, with a view to enhancing a country's long-term growth prospects, and thus acts as a major catalyst in transforming the economy into a more efficient, innovative and competitive marketplace within the global arena

5. Stability in Security Prices:

The capital market tends to stabilise the values of stocks and securities and reduce the fluctuations in the prices to the minimum. The process of stabilisation is facilitated by providing capital to the borrowers at a lower interest rate and reducing the speculative and unproductive activities.

6. Assists to Government:

Capital market assists the Government to close resource gap, and complement its effort in financing essential socio-economic development, through raising long-term project based capital.

7. Benefits to Investors:

Capital market is beneficial to the investors in many ways:

(a) Liquidity of Investment: Shares and bonds are easily transferable at low transaction cost as compared to other assets such as real estate. Therefore an investor can buy and sell at considerable convenience.

(b) **Hedge against inflation:** Securities prices over the long term tend to outperform inflation, therefore investment in securities can be a reliable hedge against inflation in the long term.

(c) **Higher Return:** Capital market provides comparatively higher return in the long run than other invests avenues such as real estate, gold, and bank deposits.

(d) **Collateral:** Securities represent stocks of wealth, and can be used as collateral to secure financing such as loans from lending institutions.

(e) **Flexibility:** Shares and bonds are traded in units and lots that are affordable by investors of different income levels. As such, investment in securities can be customized to the specific incomes of investors.

(f) **Tax advantage:** The government offers many tax advantages to the long term investment in equity market.

Important Financial Instruments in Capital Market:

1. Shares:

According to the Companies Act 1956, 'a share is the share in the share capital of a company'. It is a portion of capital which is divided among number of people. It is a unit of ownership interest in a corporation and offered for sale. Shares are of two types, Preference shares and Equity shares.

(i) Preference shares:

Preference shares are those shares which have a preferential right for the payment dividend during the life time of the company and for the return of capital at the time of winding up. Preference shares carry fixed rate of dividend that are paid to shareholders before equity stock dividends are paid out.

Following are the major types of preference shares.

- **Cumulative Preference Shares**: When unpaid dividends on preference shares are treated as arrears and are carried forward to subsequent years, then such preference shares are known as cumulative preference shares.

- **Non-cumulative Preference Shares**: Non-cumulative preference shares are those type of preference shares, which right to get have fixed rate of dividend out of the profits of current year only. They do not carry the right to receive arrears of dividend.

- **Redeemable Preference Shares**: Those preference shares, which can be redeemed or repaid after the expiry of a fixed period, are known as redeemable preference shares.

- **Non-redeemable Preference Shares**: Those preference shares, which cannot be redeemed during the life time of the company, are known as non-redeemable preference shares. The amount of such shares is paid at the time of liquidation of the company.

- **Participating Preference Shares**: Those preference shares, which have right to participate in any surplus profit of the company after paying the equity shareholders, in addition to the fixed rate of their dividend, are called participating preference shares.

- **Non-participating Preference Shares**: Preference shares, which have no right to participate on the surplus profit of the company, are called non-participating preference shares.

- **Convertible Preference Shares**: Those preference shares, which can be converted into equity shares at the option of the holders after a fixed period according to the terms and conditions of their issue, are known as convertible preference shares.

- **Non-convertible Preference Shares**: Preference shares, which are not convertible into equity shares, are called non-convertible preference shares.

(ii) Equity shares (Ordinary shares or Common shares):

Equity shares are the ordinary shares of a company which have no preferential rights. They are the shares representing the ownership interest. Equity shares give their holders the power to share the earnings in the company as well as a vote in the Annual General Meetings of the company. Such a shareholder has to share the profits and also bear the losses incurred by the company. Equity share holders are the real owners of the company.

2. Debenture | Bond:

A debenture is an acknowledgement of the debt of the Company. It is a long term debt instrument yielding a fixed rate of interest issued by a company. A debenture is like a certificate of loan or debt evidencing the fact that the company is liable to pay a specified amount with interest. Debenture is not secured by the physical asset of the company. Debenture holders are the creditors of the company and hence they have no voting right in the company. Bonds are the debt instruments secured by the physical asset of the company. In some countries, the term denture is used interchangeably with 'bond'.

Types | Component of Capital Market:

Capital market is mainly classified as:

(1) Government Securities Market or Gilt edged markets - In this market, Government and semi-government securities are traded.

(2) Industrial Securities Market - In this market, industrial securities, i.e. shares and debentures of new or existing corporates are traded.

This market is further divided into:

(A) Primary or New Issues Market- here companies sell fresh shares, debentures, etc. for the first time to the public.

(B) Secondary Market - here already existing shares, debentures, etc. are traded through the Stock Exchanges. Capital market can be classified into two;

1. Primary market | New Issue Market

2. Secondary market.

Primary market directly contributes in capital formation because in primary market company goes directly to investors and utilizes the funds for investment purpose. Primary market is the market where the securities are issued for the first time. It is the primary market in which the companies issue their securities. Secondary market is the market for already issued (second hand) securities. Secondary market enables the further buying and selling of issued securities.

Primary and secondary markets complement each other. **Primary market** deals with the issue of new securities. On the **other** hand, **secondary market** deals in the purchase and sale of the existing securities. That is, once the securities are issued in **primary market**, they are then traded in the **secondary market**.

Primary market Intermediaries

A number of intermediaries play a critical role in the process of issue of new securities. They are

1. **Merchant bankers/lead managers:** it is an institution that extends a number of services in connection with issue of capital. Their services include management of security issues, portfolio management services, underwriting of capital issues, credit syndication, financial advice and project counselling etc. It has now made mandatory that all public issues should be made by merchant bankers acting as lead managers.

2. **Underwriters:** underwriter guarantee that the securities offered for the public will be subscribed if it is not subscribed by the public. It is an insurance to the issuing company against the failure of issue. In case, the public fails to subscribe, the underwriter will have to take them up and pay for them. They charge a commission called underwriting commission for their service. It should not exceed 5 percent in case of shares and 2.5 percent for debentures.

3. **Bankers to an issue:** Banker to an issue accepts applications and application money, refund application money after allotment and participate in the payment of dividend by companies. No banker can act as a banker to an issue unless it possesses a registration with SEBI. SEBI grants registration only when it is satisfied that the bank has enough infrastructure, communication and data processing facilities and requisite man power to discharge such duties. The banker is required to maintain documents and records relating to the issue for a period of 3 years. It is also required to furnish information to the SEBI regarding the number of applications received, number of issues for which it has acted as a banker to an issue, date on which applications from investors were forwarded to registrar of issue, date and amount of refund to investors etc.

4. **Registrar to an issue:** It is an intermediary who performs the function of collecting application from investors (through bankers), keeping record of applications, keeping record of money received from investors, assisting companies in allotment and helping despatch of allotment letters, refund orders etc.

5. **Share transfer agents:** They maintain the record of holders of securities on behalf of companies and deals with all activities connected with transfer or redemption of securities.

6. **Debenture trustees:** A debenture is an instrument of debt issued by the company acknowledging its obligation to repay the sum along with an interest. In the case of public issue of debentures, there would be a large number of debenture holders on the register of the company. As such it shall not be feasible to create charge in favour of each of the debenture holder. A common methodology generally adopted is to create Trust Deed conveying the property of the company. A Trust deed is an arrangement enabling the property to be held by a person or persons for the benefit of some other person known as beneficiary. It has been made mandatory for any company making a public/rights issue of debentures to appoint one or more debenture trustees before issuing the prospectus or letter of offer and to obtain their consent which shall be mentioned in the offer document.

7. **Brokers to an issue:** Brokers are the persons who procure subscriptions to issue from prospective investors spread over a larger area. A company can appoint as much number of brokers as it wants.

8. **Portfolio managers:** Portfolio construction, formulation of investment strategy, evaluation and regular monitoring of portfolio is an art that requires skill and high degree of expertise. Any person who pursuant to a contract or arrangement with a client, advises or directs or undertakes on behalf of the client [whether as a discretionary portfolio manager or otherwise(adviser)] the management or administration of a portfolio of securities or the funds of the client, as the case may be is a portfolio manager.

Methods of Floating New Issue in the Primary Market

Main methods of floating of new issue of shares in primary Market

- Offer through prospectus | Public Issue by Prospectus
- Bought out deals | offer for sale
- Private placement
- Right issue
- Book building

1. Public Issue | Offer through prospectus | Public Issue by Prospectus :

Public issue means raising funds from public. The main purpose of the public issue, amongst others, is to raise money through public and get its shares listed at any of the recognized stock exchanges in India.

Methods of Public Issue:

Public issue may be an Initial Public Offering (IPO) or Further/Follow on Public Offering (FPO). During the IPO or FPO, the company offers its shares to the public either at fixed price or offers a price range, so that the investors can decide on the right price. The method of offering shares at a fixed price is called Fixed Price Public Issue and the method of offering shares by providing a price range is called as book building method.

Initial Public Offering: It is the first time issue of securities to the public. The promoters of the companies after complying with the guidelines of SEBI and the Companies Act ask the public at large to subscribe to their shares so that they can generate capital. It may be done through prospectus or Offer for Sale (Securities issued to a issue house and they sell securities to the public by issuing advertisement called OFS) Public issue through offer for sale is not popular in India.

• **Further (Follow on) Public Offering:** If an already listed company makes the issue of securities after IPO, it is called Follow on Public Offering. If an existing company again intends to raise capital from the general public after IPO, it can again make a public issue called FPO. It is a supplementary issue made by a company once it is listed and established on the stock exchange.

Book Building

Book building refers to the process of generating and recording investor demand for shares during an Initial Public Offering (IPO) or FPO during their issuance process, in order to support efficient price discovery. A price range (Price Band) is specified in the offer document with a floor price (Minimum price). Based on the demand and supply of the shares, the final price is fixed. The lowest price in the price range is known as the floor price and the highest price in the price range is known as cap price. The price at which the shares are allotted is known as cut off price. Usually, the issuer appoints a major investment bank to act as a major securities underwriter or book-runner. Book-runner/Lead manager/Syndicate manager is the underwriter/investment bank who manages the book building process.

2. Offer for Sale

Under this method new securities are offered to general public but not directly by the company but by an intermediary who buys whole lot of securities from the company. Generally the intermediaries are the firms of brokers. So sale of securities takes place in two steps: first when the company issues securities to the

intermediary at face value and second when intermediaries issue securities to general public at higher price to earn profit. Under this method company is saved from the formalities and complexities of issuing securities directly to public.

3. Right Issue:

It is an issue of rights to a company's existing shareholders that entitles them to buy additional shares directly from the company in proportion to their existing holdings, within a fixed time period. In a rights issue, the shares are generally offered at a discount to the current market price. Rights are often transferable, allowing the holder to sell them on the open market.

Bonus Issue (Gift shares):

It is an issue of additional shares to shareholders of a company instead of paying dividend. These are company's accumulated earnings which are not given out in the form of dividends, but are converted into free shares. Fully paid new shares are issued to shareholders in proportion to their holdings. For example, the company may give one bonus share for every five shares held.

4. Private Placement:

Issue of securities (by a listed company) to a selected group of investors not exceeding 49 is called Private Placement. Investors involved in private placements are usually large banks, mutual funds, insurance companies and pension funds. Private placement is the opposite of a public issue, in which securities are made available for sale on the open market. Following categories of issue can also be included in Private placement.

- **Preferential Allotment:** It is a type of Private placement by unlisted companies. Preferential Allotment is the process by which allotment of securities is done on a preferential basis to a select group of investors such as directors, existing shareholders etc.
- **Qualified Institutions Placement (QIP):** It is also part of private placement (by Listed companies).It is the issue of securities to Qualified institutional Buyers (QIB) in terms of the provisions of the Issue of Capital & Disclosure Requirements (ICDR) of SEBI.
- **Employees Stock Option Scheme (ESOS)** - A stock option scheme granted to specified employees of a company is called Employee Stock Option Scheme. ESOS carry the right, but not the obligation, to buy a certain amount of shares in the company at a predetermined price.

Secondary Market | Stock Market

Secondary Market refers to a market where securities are traded after being initially offered to the public in the primary market and/or listed on the Stock Exchange. Majority of the trading is done in the secondary market. Secondary market comprises of equity markets and the debt markets.
It is the organized mechanism for purchase and sale of existing securities. Investors in new issue market who do not want to hold the securities up to maturity can approach stock market to sell their securities. Similarly those who want to become an investor in an existing company which do not offer new issue of securities at present, approach stock market for purchasing securities.

Definition

Securities Contract & Regulation Act 1956 defines secondary market as ‘any body of individuals whether incorporated or not, constituted for the purpose of assisting, regulating or controlling the business of buying, selling of securities’.

Difference between Primary Market and Secondary Market

Primary Market	Secondary Market
It is the market for new securities	It is the market for existing or old securities.
Securities are exchanged between company and the investors.	Securities are exchanged between investors.
It promotes capital formation directly.	It promotes capital formation indirectly.
Only buying of securities takes place. Securities cannot be sold here.	Both buying and selling of securities can take place in the stock exchange / stock market.
There is no fixed geographical location.	There is a specified location.
Prices are determined and decided by the management of the company	Prices are determined by demand and supply for the security in the stock exchange.
Securities are issued to investors for the first time.	Securities may be bought and sold many times but not the first time.

Depository System

Under the depository system, securities are held in electronic form. The transfer and settlement of securities are done electronically. The depository system maintains accounts of the shareholder, enables transfer, collects dividends, bonus shares, etc. on behalf of the shareholder.

Physical Shares and Demat shares: (Dematerialisation & Rematerialisation)

Shares with share certificates printing on a paper is called Physical shares where as the shares in electronic format is called Demat (Dematerialised) shares. The process of converting the physical form of shares to dematerialised form is called Dematerialisation. The Depositories Act was passed by the parliament in 1995 and this paved the way for conversion of physical securities into electronic format. Depository and Depository participants are the organisations through which the physical shares can be converted into electronic form. If one wishes to get back his securities in physical form after dematerialisation, he can request his Depository participants for **rematerialisation**.

Party of depository system

1. The Depository: A depository is an institution which holds the shares of an investor in electronic form. There are two depository institutions in India these are NSDL and CDSL.

2. The Depository Participant: He opens the account of Investor and maintains securities records.

3. The Investor: He is a person who wants to deal in shares whose name is recorded

4. The Issuing Company: That organization which issues the securities. This issuing company sends a list of the shareholders to the depositories.

Depository:

A depository is an organisation which holds securities (like shares, debentures, bonds, government securities, mutual fund units etc.) of investors in electronic form at the request of the investors through a registered Depository Participant. It also provides services related to transactions in securities. The minimum net worth stipulated by SEBI for a depository is Rs.100 crore.

At present two Depositories are registered with SEBI.

1. National Securities Depository Limited(NSDL) and

2. Central Depository Services (India) Limited (CDSL)

Depository Participants

A Depository Participant (DP) is an agent of the depository through which it interfaces with the investor and provides depository services. Public financial institutions, scheduled commercial banks, foreign banks operating in India with the approval of the Reserve Bank of India, state financial corporations, custodians, stock-brokers, clearing corporations /clearing houses, NBFCs and Registrar to an Issue or Share Transfer Agent complying with the requirements prescribed by SEBI can be registered as DP.

Following services are provided by a depository to the beneficial owners through a depository participant:

- Opening a demat account;
- Dematerialization, i.e. converting physical securities into electronic form
- Rematerialization, i.e. converting electronic securities into physical form
- Maintaining record of securities held by the beneficial owners in the electronic form
- Settlement of trades by delivery or receipt of securities
- Settlement of off-market transactions
- Receiving electronic credit in respect of securities allotted by issuers under IPO or otherwise on behalf of demat account holders;

Grey Market

In the securities markets, the grey market is a market where a company's shares are traded, usually before they are issued in an initial public offering (IPO).

A grey market in the securities markets, is an over-the-counter market where dealers execute orders for stocks and bonds for preferred customers before they have been issued. These sales are contingent upon the issuance actually taking place, and allows underwriters and the issuer to determine demand and price the securities accordingly before the initial public offering (IPO) or bond issue. In grey market trading, while the trade is binding, it cannot be settled until official trading begins.

3. Government Securities Markets

Government security means a security created and issued by the Government for the reason of raising a public loan or for any other reason as may be notified by the Government in the Official Gazette and having one of the forms mentioned in The Public Debt Act, 1944. A Government security may, subject to such terms and conditions as may be specified, be in such forms as may be approved or in one of the following forms, namely:

i. A Government promissory note payable to or to the order of a certain persons
ii. A bearer, bond payable to bearer; or
iii. A stock; or
iv. A bond held in a bond ledger account.

The government raises short term and long term funds by issuing securities, these securities do not carry risk and are as good as gold as the government promises the payment of interest and the repayment of principal. They are, referred to as gilt-edged securities. The government securities market is the major market in any economic system and therefore, is the benchmark for other markets.

Generally Government Securities are interest bearing dated securities issued by RBI on behalf of the Government of India; Government uses these funds to meet its expenditure purpose. These securities are usually fixed maturity and fixed coupon securities carrying semi-annual coupon. Government securities are issued by the central government, state governments and semi-governments authorities which also consist of local government authorities such as city corporations and municipalities.

PGT Commerce

1. Which market directly contributes to capital formation?
(a) Money market (b) Capital market
(c) Primary market (d) Secondary market

P.G.T. K.V.S. 2017

2. Which of the following is the oldest depository of India?
(a) SEBI (b) CDSL
(c) NSDL (d) RBI

P.G.T. K.V.S. 2017

3. Which of the following is not a function of Financial Market?
(a) Facilitating Housing Loan
(b) Facilitating Price Discovery
(c) Providing Liquidity to Financial Assets
(d) Reducing the cost of Transactions

P.G.T. K.V.S. 2018

4. 'It is a market where low risks, unsecured and short-term debt instruments, that are highly liquid, are issued and actively traded every day.' This market is known as:
(a) Primary Market (b) Secondary Market
(c) Money Market (d) Capital Market

P.G.T. K.V.S. 2018

5. "Treasury Bill" is an instrument of short term borrowing maturing in a period of less than one year'. It is used by:
(a) State Government (b) Central Government
(c) Commercial Bank (d) Non-Banking Finance Companies

P.G.T. K.V.S. 2018

1. Bonds not carrying any interest are known as-
(a) Zero coupons bonds (b) Secured premium notes
(c) Callable bonds (d) Deep discount bonds

P.G.T. N.V.S. 2014

2. Book building method has been introduced in ……….in India.
(a) 1995 (b) 1985
(c) 2005 (d) 2003

P.G.T. N.V.S. 2014

3. Capital market is It market for-
(a) Long term funds and long term investments
(b) Short term funds and long term investments
(c) Long term funds and short term investments
(d) Short term funds and short term investments

P.G.T. N.V.S. 2014

4. Which of the following is the oldest depository of India?
(a) SEBI (b) CDSL
(c) NSDL (d) RBI

P.G.T. N.V.S. 2014

5. Call money is short-term finance repayable in
(a) One to fifteen days
(b) More than fifteen days but less than three months
(c) More than three months but less than a year
(d) More than one year

P.G.T. N.V.S. 2016

6. Allotment of securities by a company to institutional investors and some selected individuals is called:
(a) Private placement (b) Offer through prospectus
(c) Offer for sale (d) Rights issue

P.G.T. N.V.S. 2016

7. Which of the following is a money market instrument?
(a) Certificate of deposit (b) Bond
(c) Stock (d) Debenture

P.G.T. N.V.S. 2019

8. The major player in the Indian money market is:
(a) NBFC (b) Cooperatives banks
(c) Commercial banks (d) Indigenous bank

P.G.T. N.V.S. 2019

9. The component of a capital market is:
(a) Stock market (b) Commercial bill market
(c) Treasury bill market (d) Call money market

P.G.T. N.V.S. 2019

10. X is a marketable receipt in bearer or registered form of funds deposited in banks for a specified period at a specified rate of interest. It Represents transferable, negotiable, short-term, fixed interest bearing, maturity dated, highly liquid and riskless money instrument. Identify X?
(a) Cash management bill (b) Treasury bill
(c) Commercial paper (d) Certificate of deposit

P.G.T. N.V.S. 2019

1. Zero Coupon bonds has its origin in
(a) U.S. Security Market (b) Wall Street
(c) Japan's Security Market (d) Dalal Street

DSSSB PGT (2014 Tier I)

2. Which one of the following is not a money market security?
(a) Treasury Bills (b) National Savings Certificate
(c) Certificate of Deposit (d) Commercial Paper

DSSSB PGT (2014 Tier I)

3. Primary and Secondary markets
(a) Compete with each other (b) Complement each other
(c) Function independently (d) Control each other

DSSSB PGT (2014 Tier I)

4. A platform of an organised and regulated financial market where securities (bonds, shares, etc.) are bought and sold at prices governed by forces of demand and supply and often regulated by a professional body is called as :
(a) Money Market (b) Indigenous Lending
(c) Financial Intermediary (d) Stock Exchange

DSSSB PGT 2018 Male

5. The market for raising short term funds is called:
(a) Retail market **(b) Short-term market**
(c) Money market **(d) Capital market**
DSSSB PGT 2018 Female

6. Which of the following is not a money market security?
(a) Commercial paper **(b) Certificate of deposit**
(c) Treasury bills **(d) Debentures**
DSSSB PGT 2018 Female

7. Securities with maturity of less than one year traded in:
(a) Futures market **(b) Capital market**
(c) Forward market **(d) Money market**
DSSSB PGT 2018 Female

Army School

1. The physical possession of equity shares in case of GDR is with
(a) Depository **(b) Custodian**
(c) Foreign investor **(d) Government**
PGT Commerce - Army School - 2012

2. Which of the following provides liquidity to money market instruments by creating a secondary market where they can be traded?
(a) DFHI **(b) NSDL**
(c) SBI **(d) OTCEI**
PGT Commerce - Army School - 2012

3. The exchange market of India consists of
(a) Authorized dealers **(b) RBI**
(c) Overseas banks to some extent **(d) All of the above**
PGT Commerce - Army School – 2012

M.Com (Entrance) Jamia

1. The market for raising short term funds is called..........
(a) Capital market (b) Money market
(c) Mini market (d) Short term market
[M.Com Entrance Jamia 2016]

2. Which of the following is not a money market security?
(a) Treasury bills (b) National savings certificate
(c) Certificate of deposit (d) Commercial paper
[M.Com Entrance Jamia 2016]

3. --------------------- are zero coupon securities, pay no interest, are issued at discount and redeemed at par
(a) Commercial Paper (b) Commercial Bills
(c) Certificate of Deposit (d) Treasury Bill
[M.Com Entrance Jamia 2019]

4. Which of the following is NOT an example of the Money Markets?
(a) Call Money Market (b) T-Bills Market
(c) Stock market (d) Certificate of Deposit market
[M.Com Entrance Jamia 2019]

5. ------------------ is an unsecured money market instrument issued in the form of a promissory note by a corporation with high credit ratings to finance its short-term needs
(a) Cash Management Bills (b) Ways and Means Advances
(c) Treasury Bill (d) Commercial Papers

[M.Com Entrance Jamia 2019]

6. Assume that the price of a 91 – day Treasury bill (T- Bill) at issue is INR 98.00. After 51 days, if the same T-Bill was trading at a price of INR 99, the yield would then be:
(a) 7.23% (b) 9.22%
(c) 8.19% (d)18.62%

[M.Com Entrance Jamia 2019]

M.Com (Entrance) BHU

1. Which one of the following is not a party of depository system?
(a) The Depository Participant (b) The Investor
(c) The Broker (d) The Issuing Company

M.Com Entrance (BHU2016)

2. Which one of the following is not a method of floating new issues in the 'Primary Market'?
(a) Public issue by Prospectus (b) Offer for sale
(c) Making the contract (d) Private placement

M.Com Entrance (BHU2016)

3. In which market, old shares are purchased and sold?
(a) Capital Market (b) Primary Market
(c) Secondary Market (d) Money Market

M.Com Entrance (BHU2016)

4. Which one of the following is not a part of capital market?
(a) Gilt-edged market (b) Commercial paper market
(c) New issue market (d) Secondary capital market

M.Com Entrance (BHU2016)

5. The financial instrument with shortest maturity period is
(a) Call money (b) Certificate of deposit
(c) Commercial bill (d) Treasury bill

M.Com Entrance (BHU2016)

6. Which one of the following is not a function of the new issue market?
(a) Origination of securities (b) Underwriting of securities
(c) Distribution of securities (d) Administration of securities

M.Com Entrance (BHU2016)

7. Commercial banks or Development banks issue this document
(a) Commercial bill (b) Treasury bill
(c) Certificate of deposit (d) Commercial paper

M.Com Entrance (BHU2016)

S.E.T. Commerce

1. Which of the following are the instruments of Money Market?
(i) Call Money Market
(ii) Commercial Bill Market
(iii) Industrial Securities Market
(iv) Short-term Loan Market
(v) Treasury Bill Market
Codes:
(a) (i), (ii), (iii), and (iv) (b) (i), (ii), (iv), and (v)
(c) (i), (ii), (iii), and (v) (d) (i), (iii), (iv), and (v)

[West Bengal SET 2020 January]

UGC NET JRF - Commerce

1. The market for long term loanable funds is a:
(a) Money Market
(b) Capital Market
(c) Bond Market
(d) None of the above
UGC-NET Paper II (June 2007)

2. The short term money market comprises:
(a) The call money market
(b) The inter-bank deposit market
(c) The bills re-discounting market
(d) All of the above
UGC-NET Paper II (June 2007)

3. Which one of the following is not a money market instrument?
(a) Commercial paper
(b) Participatory certificates
(c) Warrants
(d) Treasury Bills
UGC-NET Paper III (December 2012)

4. Which one is not Non-Marketable securities?
(a) Corporate Securities
(b) Bank Deposits
(c) Deposits with companies
(d) Post Office Certificates and Deposits
UGC-NET Paper III (December 2012)

5. In the call / notice money market, which of the following participant is allowed to trade
(a) All Banks, Primary Dealers and Mutual funds
(b) All corporates
(c) Only commercial Banks
(d) All of the above
UGC-NET Paper II (June 2013)

6. Match the following:

List-I	List-II
(i) National Stock Exchange	(a) Marks the beginning of the process of dematerialization of shares of the participating companies
(ii) National Securities Depository Limited	(b) Facilitation of equal access to investors across to investors across the country.
(iii) Securities and Exchange Board of India	(c) To foster the development of an active secondary market for Government Securities
(iv) Securities Trading Corporation of India	(d) Abolition of Capital Issue control and retaining the sale authority for new capital issues.

Codes:
(a) (i)-(b), (ii)-(a), (iii)-(d), (iv)-(c)
(b) (i)-(a), (ii)-(b), (iii)-(c), (iv)-(d)
(c) (i)-(a), (ii)-(b), (iii)-(d), (iv)-(c)
(d) (i)-(d), (ii)-(c), (iii)-(b), (iv)-(a)
UGC-NET Paper III (June 2013

7. Secondary market intermediaries for corporate securities in India are
(I) Investors
(II) Jobbers
(III) Brokers and sub-brokers
(IV) Portfolio Consultant
Codes:
(a) I, II and III only
(b) II, III and IV only
(c) II and III only
(d) III and IV only
UGC-NET Paper III (December 2014)

8. Financial instruments which are issued with detachable warrants and are redeemable after certain period is known as:
(a) Deep Discount Bonds
(b) Secured premium Notes
(c) Bunny Bonds
(d) Junk Bonds
UGC-NET Paper III (June 2015)

9. Identify the incorrect statement (s), regarding money market, among the following:
(a) The call money market deals in short term financial repayable on demand, with a maturity period varying for the day to 14 days.
(b) Treasury bills are instruments of short term borrowing by the Government of India, issued as promissory notes under discount.
(c) A reduction in the repo rate help banks to get money at a cheaper rate.
(d) Money market mutual funds invest money in specifically high quality and very short maturity based money market instruments.

Codes:
(a) (a) and (c)
(b) (b)
(c) (d)
(d) None of the above

UGC-NET Paper III (December 2015)

10. Which of the following are the instruments of money market?
(i) Call money market
(ii) Commercial bill market
(iii) Industrial securities market
(iv) Short-term loans market
(v) Treasury bill market

Codes:
(a) (i), (ii), (iv), (v)
(b) (i), (ii), (v)
(c) (i), (ii), (iii), (iv), (v)
(d) (i), (ii), (iii), (iv)

UGC-NET Paper III (July 2016)

11. Which of the following are the components of capital market?
I. Government Securities Market
II. Commercial Bill Market
III. Industrial Securities Market
IV. Treasuring Bill Market
V. Long-term Loans Market

Codes:
(a) I, III, IV, V
(b) I, II, III
(c) I, III, V
(d) I, II, III, IV, V

UGC-NET Paper III (September 2016)

12. Which of the following statement are false? Indicate the correct code.
(i) Grey market is a market for dealing in listed securities
(ii) OTCEI is mainly intended for big investors.
(iii) Insider Trading is legally permitted in the capital market.
(iv) The device adopted to make profit out of the differences in price of a security in two different markets is called 'arbitage'.

Code :
(a) (i), (ii), (iii)
(b) (i), (ii), (iv)
(c) (i), (ii), (iii), (iv)
(d) (ii), (iii), (iv)

UGC-NET Paper II (July 2018)

13. The certificate which evidences an unsecured corporate debt of short term maturity is known as:
(a) Certificate of Deposit
(b) Short term loan certificate
(c) Treasury Bill
(d) Commercial paper

UGC-NET Paper II (July 2018)

14. Match List – I and List – II
List – I
(A) Inter-bank call market
(B) Commercial bills
(C) Commercial papers
(D) Treasury bills
List – II
(i) Money Market
(ii) Promissory note

(iii) Short-term maturity
(iv) Government papers
Choose the correct option from those given below :
(a) (A)-(i), (B)- (ii), (C)-(iv), (D)-(iii) **(b) (A)-(iii), (B)- (i), (C)-(ii), (D)-(iv)**
(c) (A)-(i), (B)- (iii), (C)-(iv), (D)-(ii) **(d) (A)-(iv), (B)- (iii), (C)-(ii), (D)-(i)**

[2019 June]

15. Choose incorrect statement from the following:
(a) 28 Days T-bills were introduced in 1998 **(b) 364 Days T-bills were introduced in 1992**
(c) 182 Days T-bills were introduced in 1986 **(d) 273 Days T-bills were introduced in 2006**

[2019 December]