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SCHOOL OF MANAGEMENT STUDIES

UNIT – I – CAPITAL MARKETS – SBAA3003

Financial System- Structure of Indian financial system –money market and capital market- Instruments in capital market: equity shares, preference shares, debentures, bonds, Govt. securities, and new instruments - SEBI Guidelines relating to Capital markets - Recent developments in the Indian Capital market.

FINANCIAL SYSTEM - INTRODUCTION

A financial system is a collection of institutions which allow the exchange of funds, such as banks, insurance companies, and stock exchanges. The financial system exists in the corporate, national, and global level. Borrowers, lenders, and creditors are exchanging current funds to finance ventures, either for consumption or productive investment and seeking returns on their financial assets. Furthermore, the financial system includes sets of laws and policies used by creditors and lenders to determine which projects are funded, who fund the projects, and scope of financial deal.

A financial system is a network of financial institutions, financial markets, financial instruments, and financial services that facilitate money transfer. This system includes end users of saver, arbitrator, device, and money. The level of economic development depends largely on the basis and it facilitates the economy of the prevailing financial system. Proper circulation of funds is necessary for the economic development of the country.

Meaning of Financial System:

The financial system refers to set of complex and interconnected components consisting specialized and non-specialized financial institutions, organized and unorganized financial markets, financial instruments and financial services. The aim of the financial system is to facilitate the circulation of funds in an economy.

It is concerned about money, credit, and finance. Money refers to the medium of exchange or mode of payment. Credit refers to the amount of debt which is returned along with the interest. And the finance refers to the monetary resources comprising the own funds and debts of the state, company or a person.

The efficient financial system and sustainable economic growth are corollaries. The financial system mobilizes the savings and channelizes them into productive activity and thus influences the pace of economic development. Economic growth is hampered for want of an effective financial system. Broadly speaking, financial system deals with three inter-related and interdependent variables, i.e., money, credit, and finance.

Definition of Financial System:

According to Amit Chaudhary, “Financial system is the integrated form of financial institutions, financial markets, financial securities, and financial services which aim is to circulate the funds in an economy for economic growth.”

According to Dhanilal, “Financial system is the set of interrelated and interconnected components consisting of financial institutions, markets, and securities.”

The financial system provides channels to transfer funds from individuals and groups who have saved money to individuals and group who want to borrow money. Saver (refer to the lender) are suppliers of funds to borrowers in return with promises of repayment of even more funds in the future.

Functions of Financial System:

Functions and Role of the financial system, markets are given below.

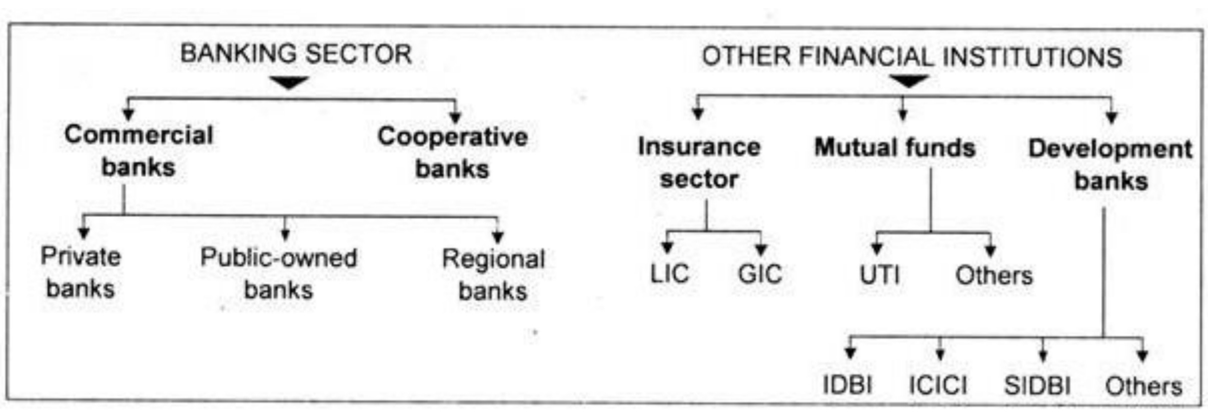
- **Pooling of Funds:** In a financial system, the Savings of people are transferred from households to business organizations. With these production increases and better goods are manufactured, which increases the standard of living of people.
- **Capital Formation:** Business requires finance. These are made available through banks, households and different financial institutions. They mobilize savings which leads to Capital Formation.
- **Facilitates Payment:** The financial system offers convenient modes of payment for goods and services. New methods of payments like credit cards, debit cards, cheques, etc. facilitate quick and easy transactions.
- **Provides Liquidity:** In the financial system, liquidity means the ability to convert into cash. The financial market provides the investors the opportunity to liquidate their investments, which are in instruments like shares, debentures, bonds, etc. Price is determined on the daily basis according to the operations of the market forces of demand and supply.

- **Short and Long-Term Needs:** The financial market takes into account the various needs of different individuals and organizations. This facilitates optimum use of finances for productive purposes.
- **Risk Function:** The financial markets provide protection against life, health, and income risks. Risk Management is an essential component of a growing economy.
- **Better Decisions:** Financial Markets provide information about the market and various financial assets. This helps the investors to compare different investment options and choose the best one. It helps in decision making in choosing portfolio allocations of their wealth.
- **Finances Government Needs:** The government needs a huge amount of money for the development of defense infrastructure. It also requires finance for social welfare activities, public health, education, etc. This is supplied to them by financial markets.
- **Economic Development:** India is a mixed economy. The Government intervenes in the financial system to influence macroeconomic variables like interest rate or inflation. Thus, credits can be made available to corporate at a cheaper rate. This leads to the economic development of the nation.

INDIAN FINANCIAL SYSTEM

Indian financial markets are sub-divided broadly into money markets (that deal in short-term funds) and capital markets (that deal in long-term funds). Structurally, money market comprises both organized and unorganized sectors.

Unorganized sector is normally made up of indigenous money lenders and bankers who do not follow formal lines of business.



Their businesses are informal and thus independent of the Reserve Bank of India or banks for any fund support. This sector is shrinking but, during the period of economic reforms launched after 1991, the activities of these institutions have become a matter of serious concern and anxiety.

The organized component of money market consists of the RBI, commercial banks and cooperative banks. The RBI is the head of the financial institutions as well as the monetary authority of the country. In the diagram, we have not shown anything about the RBI.

The second most important component of the organized money market is the commercial banks. The first commercial bank in this country Bank of Bengal was set up in 1806 in Kolkata. In addition to this Presidency Bank of Kolkata, two other Presidency Banks were established in 1840 in Mumbai and in 1843 in Chennai. Integrating these three commercial banks or Presidency Banks, the Imperial Bank of India was formed in 1921.

This Imperial Bank was nationalized in 1955 and then came to be known as the State Bank of India. Its seven subsidiary banks were nationalized in 1956. However, Indhira Gandhi nationalized 14 commercial banks having deposits of Rs. 50 crore and above in 1969. Another 6 private banks were nationalized in 1980. At present, the number of public sector banks is 27.

In terms of size and business, cooperative banks in India are rather tiny compared to commercial banks. It is a three-tier banking structure (i) with the State Cooperative Bank operating in each state as an apex bank, (ii) at the district level, the central cooperative hanks, and (iii) at the village level, the primary agricultural credit societies. However, long- term loans beyond five years are given by the Primary Cooperative Agricultural and Rural Development Banks (PCARDBs).

Although public sector commercial banks are the dominant banking sector, privately- owned banks are nonetheless important in the liberalized regime. Following the Narasimham Committee recommendations made in 1991 and in 1998, private banks are now being allowed to operate. In addition, there are some foreign banks operating in India with little or no restrictions now. Finally, regional rural banks have been functioning since 1975 to meet the credit needs of the rural people. At present, the number of regional banks stands at 76.

The main three elements of other financial institutions are: (i) insurance sector, (ii) mutual funds, and (iii) development banks. The two notable insurance institutions are the Life Insurance Corporation of India and the General Insurance Corporation.

The most prominent mutual funds institution is the Unit Trust of India. Finally, as the name suggests, development banks provide long-term capital to industries in a rather non-conventional way. At present, there are as many as 60 development banks in the country. The largest of them is the Industrial Development Bank of India (IDB1).

Finally, in industrial finance, there is an institution called capital market that provides long-term funds to both public and private sector units. Security market is the most important component of the capital market that deals in both corporate and government or gilt-edged securities. In India, the capital market has undergone a revolutionary change in recent years following the launching of the new economic policies in 1991.

The services that are provided to a person by the various Financial Institutions including banks, insurance companies, pensions, funds, etc. constitute the financial system.

Given below are the features of the Indian Financial system:

- It plays a vital role in the economic development of the country as it encourages both savings and investment
- It helps in mobilizing and allocating one's savings
- It facilitates the expansion of financial institutions and markets
- Plays a key role in capital formation
- It helps form a link between the investor and the one saving
- It is also concerned with the Provision of funds
- The financial system of a country mainly aims at managing and governing the mechanism of production, distribution, exchange and holding of financial assets or instruments of all kinds.

Components of Indian Financial System:

There are four main components of the Indian Financial System. This includes:

- Financial Institutions
- Financial Assets

- Financial Services
- Financial Markets

Let’s discuss each component of the system in detail.

1. Financial Institutions: The Financial Institutions act as a mediator between the investor and the borrower. The investor’s savings are mobilized either directly or indirectly via the Financial Markets.

The main functions of the Financial Institutions are as follows:

- A short term liability can be converted into a long term investment
- It helps in conversion of a risky investment into a risk-free investment
- Also acts as a medium of convenience denomination, which means, it can match a small deposit with large loans and a large deposit with small loans
- The best example of a Financial Institution is a Bank. People with surplus amounts of money make savings in their accounts, and people in dire need of money take loans. The bank acts as an intermediate between the two.

The financial institutions can further be divided into two types:

- **Banking Institutions or Depository Institutions** – This includes banks and other credit unions which collect money from the public against interest provided on the deposits made and lend that money to the ones in need
- **Non-Banking Institutions or Non-Depository Institutions** – Insurance, mutual funds and brokerage companies fall under this category. They cannot ask for monetary deposits but sell financial products to their customers.

Further, Financial Institutions can be classified into three categories:

- **Regulatory –** Institutes that regulate the financial markets like RBI, IRDA, SEBI, etc.
- **Intermediates** – Commercial banks which provide loans and other financial assistance such as SBI, BOB, PNB, etc.
- **Non-Intermediates** – Institutions that provide financial aid to corporate customers. It includes NABARD, SIBDI, etc.

2. Financial Assets: The products which are traded in the Financial Markets are called Financial Assets. Based on the different requirements and needs of the credit seeker, the securities in the market also differ from each other.

Some important Financial Assets have been discussed briefly below:

- **Call Money** – When a loan is granted for one day and is repaid on the second day, it is called call money. No collateral securities are required for this kind of transaction.
- **Notice Money** – When a loan is granted for more than a day and for less than 14 days, it is called notice money. No collateral securities are required for this kind of transaction.
- **Term Money** – When the maturity period of a deposit is beyond 14 days, it is called term money.
- **Treasury Bills** – Also known as T-Bills, these are Government bonds or debt securities with maturity of less than a year. Buying a T-Bill means lending money to the Government.
- **Certificate of Deposits** – It is a de-materialized form (Electronically generated) for funds deposited in the bank for a specific period of time.
- **Commercial Paper** – It is an unsecured short-term debt instrument issued by corporations.

3. Financial Services: Services provided by Asset Management and Liability Management Companies. They help to get the required funds and also make sure that they are efficiently invested.

The financial services in India include:

- **Banking Services** – Any small or big service provided by banks like granting a loan, depositing money, issuing debit/credit cards, opening accounts, etc.
- **Insurance Services** – Services like issuing of insurance, selling policies, insurance undertaking and brokerages, etc. are all a part of the Insurance services
- **Investment Services** – It mostly includes asset management
- **Foreign Exchange Services** – Exchange of currency, foreign exchange, etc. are a part of the Foreign exchange services

The main aim of the financial services is to assist a person with selling, borrowing or purchasing securities, allowing payments and settlements and lending and investing.

4. Financial Markets: The marketplace where buyers and sellers interact with each other and participate in the trading of money, bonds, shares and other assets is called a financial market.

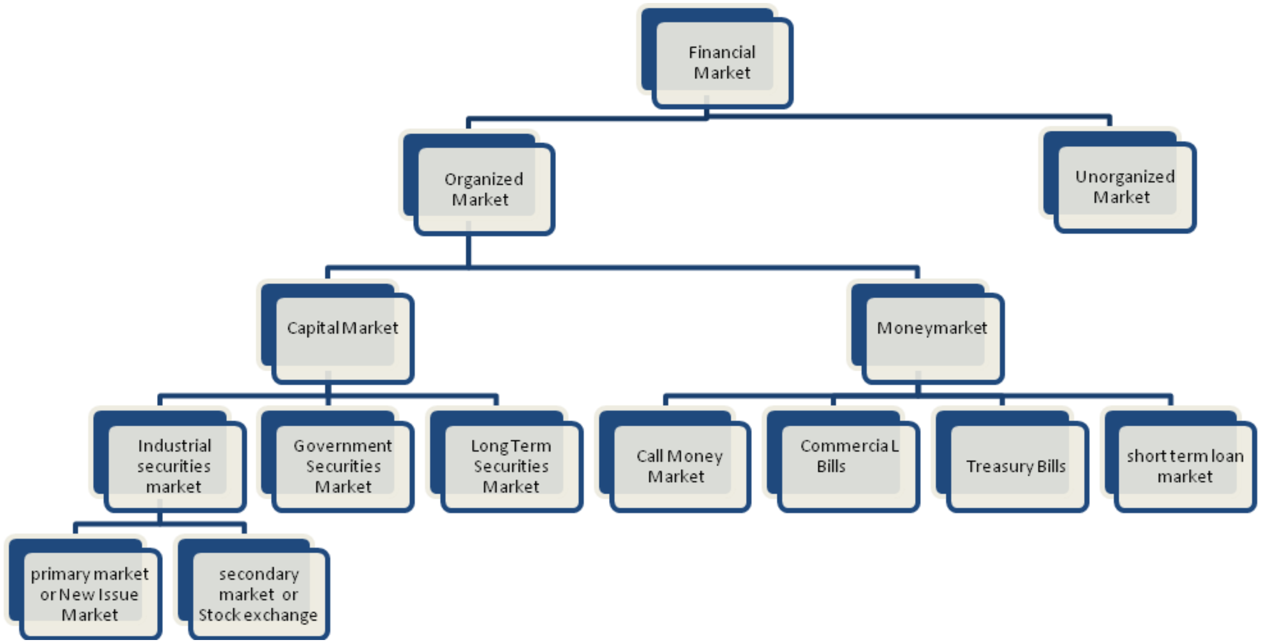
The financial market can be further divided into four types:

- **Capital Market** – Designed to finance the long term investment, the Capital market deals with transactions which are taking place in the market for over a year. The capital market can further be divided into three types:
- ✓ Corporate Securities Market
- ✓ Government Securities Market
- ✓ Long Term Loan Market
- **Money Market** – Mostly dominated by Government, Banks and other Large Institutions, the type of market is authorized for small-term investments only. It is a wholesale debt market which works on low-risk and highly liquid instruments. The money market can further be divided into two types:
- ✓ Organized Money Market
- ✓ Unorganized Money Market
- **Foreign exchange Market** – One of the most developed markets across the world, the Foreign exchange market, deals with the requirements related to multi-currency. The transfer of funds in this market takes place based on the foreign currency rate.
- **Credit Market** – A market where short-term and long-term loans are granted to individuals or organizations by various banks and Financial and Non-Financial Institutions is called Credit Market

FINANCIAL MARKETS

Generally speaking there is no specific place or location to indicate financial market. Whenever a financial transaction takes place it is deemed to have taken place in a financial market. In simple terms "Financial market can be referred as those centers and arrangements which facilitate buying and selling of financial assets"

CLASSIFICATION OF FINANCIAL MARKET:



A) ORGANIZED MARKETS:

In organized markets there are standardized rules and regulations governing the financial dealings. These markets are strictly supervised and controlled by RBI and other regulatory bodies. These organized markets are mainly classified into

1. Capital market
2. Money market

Capital market: Capital market is a market for financial assets which have long or indefinite maturity, (i.e. above one year)

It may be further divided into:

a) Industrial securities markets

b) Government securities markets

c) Long term loan markets

Industrial securities market: It is a market for industrial securities like equity shares, preference shares, debentures and bonds. It is a market where industrial concerns lays their debt by using appropriate instruments.

It can be further classified into

a) New issue market

b) Secondary market

I. Primary market (or) New issue market: The primary market deals with those securities which are issued to public for the first time. In other words new issue market deals with raising of fresh capital by companies.

II. Secondary market: Secondary market is a market for secondary sale of securities. In other words securities which have already passed through new issue markets are traded in this market.

Features of secondary market:

a) Stock exchange is a market for old securities.

b) These securities are purchased and sold continuously among investors without involvement of companies.

c) It also makes continuous evaluations of share traded in the market.

d) All stock exchanges are recognized by government of India and regulated by securities contracts (regulations act 1956).

Difference between Primary market and Secondary market:

Primary market	Secondary market
Functional differences: New securities	Buying and selling of old securities
Organizational differences : No organizational setup	Property established organizational with rules and regulations for conduct of business
No centralized control and administration for execution of business	Regulated and controlled by securities contract regulations act 1956
Nature of contribution to industrial finance: It provides direct funds for the industry. Direct contribution of funds to industry.	It does not provide direct contribution of funds. It provides only marketability to shares.

Despite the above mentioned differences they are inseparable and work in conjunctions together.

First place, both the markets are complementary in nature i.e. The securities bought from NIM can be disposed off in stock exchanges. The potential investors are assured that they will be able to disinvest of any time in the stock exchange.

Secondly, the company which makes a new issue applies for listing of their securities in a recognized stock exchange. Listing of shares adds prestige to the firm and widens the markets for investors.

Thirdly, both stock exchanges and new issue market are a part of capital market. Both the market act and react in same directions when stock market goes up new issues increase and when stock market shows a decline new issues decreases.

Government securities market: It is also gilt edged securities market it is a market where long term government securities are traded:

These are issued in denominations of Rs 100/- and interest is paid half yearly and they carry tax exemptions tax. They are generally in form of

- Stock certificates
- Promissory notes
- Bearer bonds

They are sold through public debt office of RBI

Long term loans market: Development banks and commercial banks plays are important rules in supplying long term loans to corporate customers

Money market: This deals with financial assets and securities which have maturity period up to one year. It is purely short term fund, it is subdivided into

- Call money market
- Commercial bills markets
- Treasury bills
- Short term loans markets

Call money market: Markets for extreme short periods 1-14 days

- It is highly liquid
- It is very sensitive

The interest rate varies from day to day even hour to hour

It is repayable either at the option of lender or borrower

Commercial bills market:

- It is a market for bills arising out genuine trade transactions
- Funds by discounting the bills

Treasury bills market: It is a market where short term government securities are traded

Short-Term loan market: It is a market where short term loans are given to corporate customers.

Commercial banks provide short term loans in form cash credits

Bank overdrafts

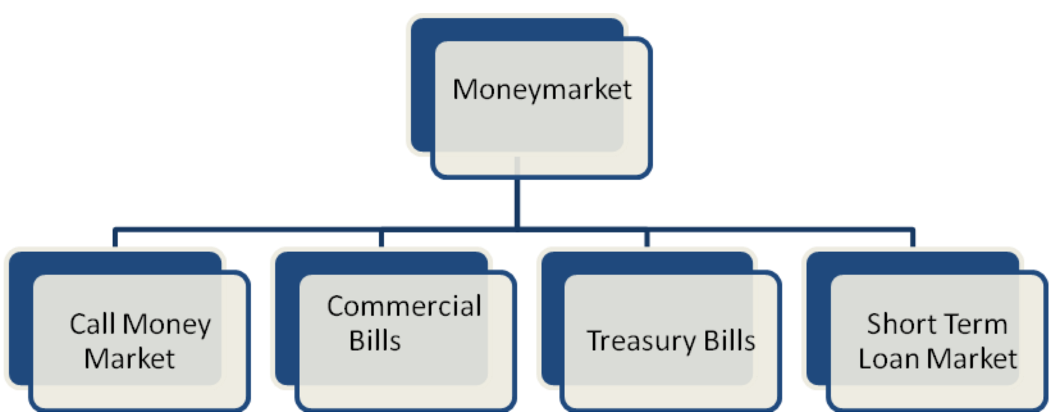
B) UNORGANIZED MARKET

- Money lender
- Indigenous bankers
- Pawn brokers
- Chit funds - Whose activity are in adequately regulated and standardized

MONEY MARKET – Meaning:

Money market is the collective name given to various firms & institutions that deal in various grades of near money like trade bills. Promissory notes and government papers. Drawn for a short personal not exceeding one year.

Money market structure:



Features of money market:

- It is a market purely for short term funds or financial assets called near money
- It deals with financial assets having a maturity date up to one year only
- There is no formal place like stock exchanges as uncase of capital market.
- Transactions have to be considered with help of brokers.

A component of money market includes:

- Central bank
- Commercial banks
- Non- banking financial companies
- Discount house & Accepting house
- Acceptance house

It is not a single homogeneous market. It has several market submarkets like

- **Call money market:** Refers to markets for extremely short period loans say 1-14days.
- **Commercial bills market/ Discount market:** Market for discounting credit bills.
- **Treasury bill market:** Treasury bills are promissory notes issued by government under certain discount for a specific period.

CAPITAL MARKET - Concept:

A good capital market is an essential pre-requisite for industrial and commercial development of a country. Credit is generally, required and supplied on short-term and long- term basis. The long term capital needs are met by the capital market. Capital market is a central coordinating and directing mechanism for free and balanced flow of financial resource into the economic system operating in a country.

The development of a good capital market in a country is dependent upon the availability of savings, proper organisation of its constituent units and the entrepreneurship qualities of its people.

FUNCTIONS OF CAPITAL MARKET

- Mobilization of financial resources on a nation-wide scale.
- Securing the foreign capital.

- Effective allocation of the mobilized financial resources.

TYPES OF CAPITAL MARKET

PRIMARY MARKET

Primary market is also known as new issue market. As in this market securities are sold for the first time i.e. new securities are issued from the company. Primary market companies goes directly to investor and utilizes these funds for investment in building, plants and machinery etc. The primary market does not includes finance in the form of loan from financial institution because when loan is issued from financial institutions it implies converting private capital into public capital and this process is called as going public.

The common securities issued in primary market are equity shares, debentures, bonds, preference shares and other innovative securities.

Methods of floatation of securities in primary market:

a) Public issue through prospectus: Under this method company issue a prospectus to inform and attract general public

b) 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.

c) Private placement: Under this method the securities are sold by the company to an intermediary at fixed price and in second step intermediaries sell these securities not to general public but selected clients at higher price.

d) Right issue (for existing companies): This is the issue of new shares to existing shareholders. It is called right issue because it is the pre- emptive right of shareholder that company must offer them the new issue before subscribing to outsiders.

e) e- IPO (electronic initial public offer): it is the new method of issuing securities through on line system of stock exchange. In this company has to appoint registered brokers for the purpose of accepting application and placing orders.

SECONDARY MARKET (STOCK EXCAHNGE)

The secondary market is the market for the sale and purchase of previously issued or second hand securities. In secondary market securities are not directly issued by the company to investors. The securities are sold by existing investors to other investors.

In secondary market companies get on additional capital as securities are bought and sold between investors only so directly there is no capital formation but secondary market indirectly contributes in capital formation by providing liquidity to securities of the company.

STOCK EXCHANGE – Definition:

The Securities Contract and Regulation Act defines a stock exchange as "An organisation or body of individuals, whether incorporated or established for the purpose of assisting, regulating and controlling of business in buying, selling and dealing in securities." Every stock exchange has a specific location. In India there are 24 recognized stock exchanges.

TYPE OF OPERATION IN STOCK EXCHANGE

a) Brokers: A broker is a member of stock exchange. He buys and sells securities on behalf of outsiders who are not the members. He charges brokerage or commission for his services.

b) Jobbers: A jobber is a member of stock exchange. He buys and sells securities on his own behalf. He is specialized in one type of security and he makes profits by selling the securities at a higher price.

c) Bulls: A bull is a speculator who expect rise in price. He buys securities with a view to selling them in future at a higher price and making profit out of it.

d) Bears: A bear is a speculator who expects fall in price. He sells securities which he does not possess.

e) Stag: A stag is also a speculator who applies for new securities in expectation that price will rise by the time of allotment and he can sell them at premium.

Functions of Stock Exchange / Secondary Market

a) Economic Barometer: It is a reliable barometer to measure the economic condition of the country. The rise or fall in the share prices indicates the boom or recession cycle of the economy

b) Pricing of Securities: The stock market helps to value the securities on the basis of demand and supply factors.

c) Safety of Transactions: In stock market only the listed securities are traded and stock exchange authorities include the companies names in the trade list only after verifying the soundness of company.

d) Contributes to Economic Growth: In stock exchange securities of various companies are bought and sold. This process of disinvestment and reinvestment helps to invest in most productive investment proposal and this leads to capital

e) Spreading of Equity Cult: Stock exchange encourages people to invest in ownership securities by regulating new issues, better trading practices and educating public about investment.

f) Providing Scope for Speculation: To ensure liquidity and demand of supply of securities the stock exchange permit healthy speculation of securities.

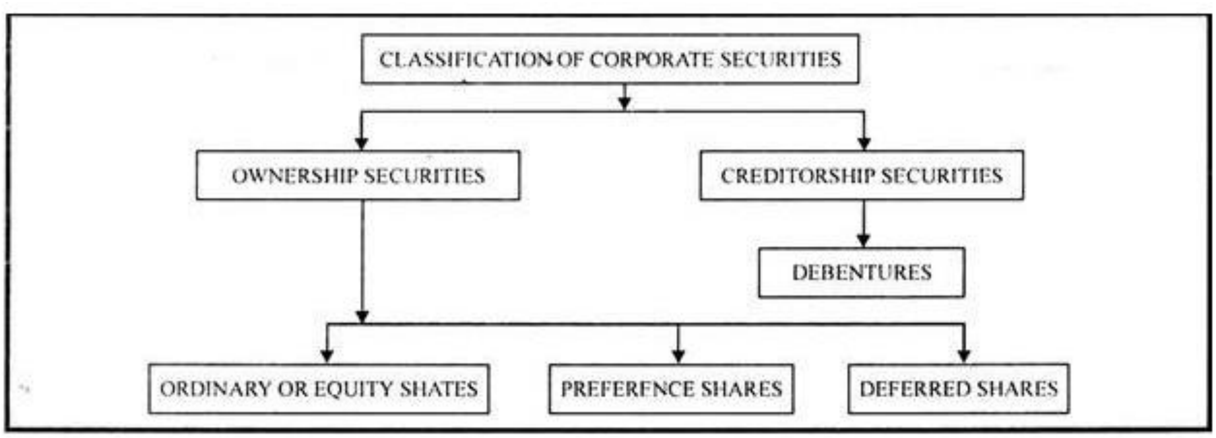
g) Liquidity: The main function of stock market is to provide ready market for sale and purchase of securities. The investors can invest in long term investment projects without any hesitation, as because of stock exchange they can convert long term investment into short term and medium term.

h) Better allocation of capital: Promotes the habits of savings and investment.

CAPITAL MARKET INSTRUMENT

The corporate securities that are dealt in primary market can classified under two categories:

1. Ownership securities or capital stock.
2. Creditorship securities or debt capital



OWNERSHIP SECURITIES

Ownership securities, also known as capital stock or shares, are the most common methods used by corporate, government, and other big companies to raise funds to help finance their operations. Section 2(46) of the companies act 1956 defines it is "a share in the share capital of a company and including stock except where a distinction between stock and shares is expressed or implied."

KINDS OF OWNERSHIP SECURITIES OR SHARES

1. EQUITY SHARES: An equity share, normally known as ordinary share is a part ownership where each member is a fractional owner and initiates the maximum entrepreneurial liability related with a trading concern. These types of shareholders in any organization possess the right to vote.

Features of Equity Shares Capital:

- Equity share capital remains with the company.
- It is given back only when the company is closed
- Equity Shareholders possess voting rights and select the company's management
- The dividend rate on the equity capital relies upon the obtain ability of the surfeit capital. However, there is no fixed rate of dividend on the equity capital.

Characteristics of Equity Shares

- Maturity
- Claims / right to income
- Claim on assets
- Right to Control or Voting Right
- Pre-emptive Right
- Limited liability

Advantages of Equity Shares Capital

a) Equity Shares does not create a sense of obligation and accountability to pay a rate of dividend that is fixed.

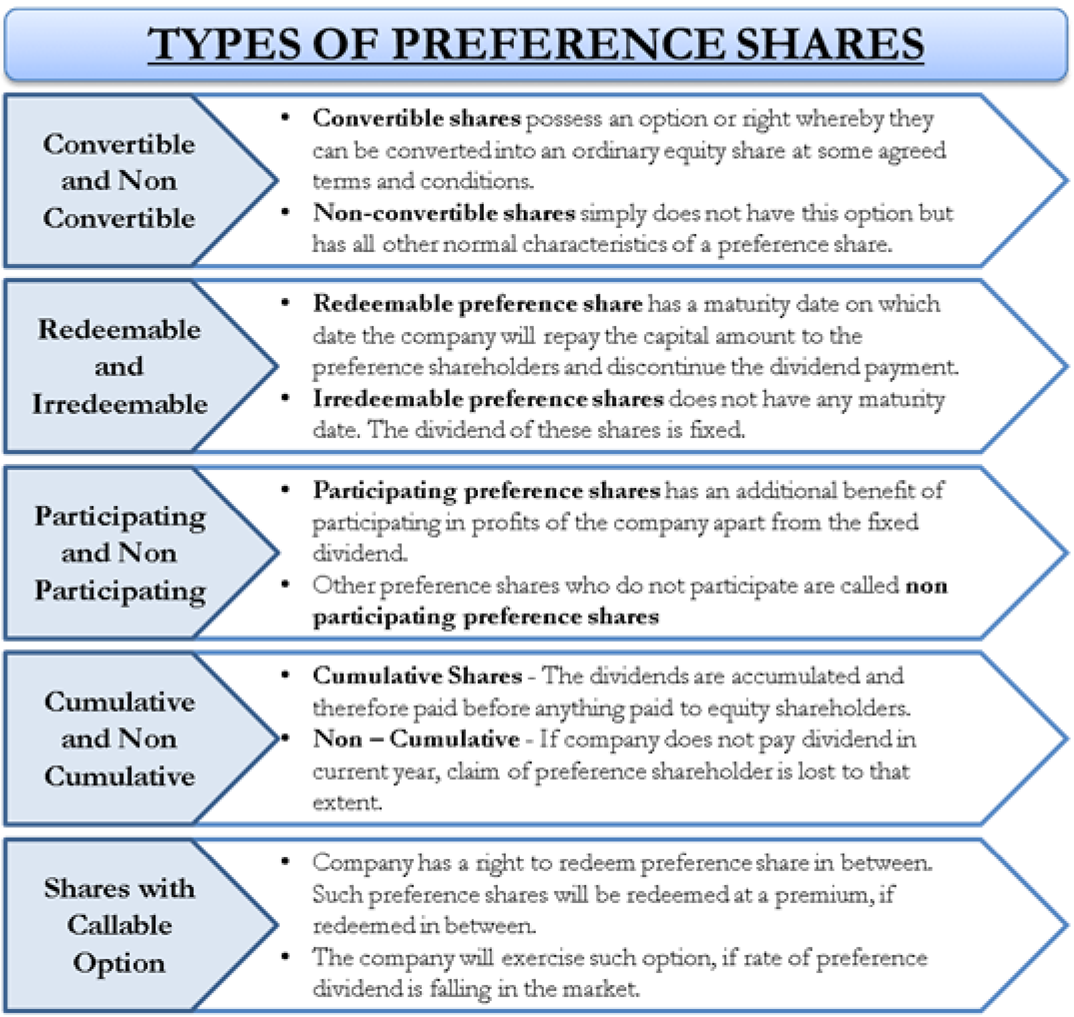
b) Equity Shares can be circulated even without establishing any extra charges over the assets of an enterprise.

c) It is a perpetual source of funding and the enterprise has to pay back; exceptional case – under liquidation.

d) Equity shareholders are the authentic owners of the enterprise who possess the voting rights.

2. PREFERENCE SHARES

Preference shares are a long-term source of finance for a company. They are neither completely similar to equity nor equivalent to debt. The law treats them as shares but they have elements of both equity shares and debt. For this reason, they are also called 'hybrid financing instruments'. These are also known as preferred stock, preferred shares, or only preferred in a different part of the world. There are various types of preference shares used as a source of finance.



Features of preference shares

a) Maturity

b) Claim on income

c) Claim on assets

d) Control

e) Hybrid from securities

Advantages:

a) Appeal to Cautious Investors: Preference shares can be easily sold to investors who prefer reasonable safety of their capital and want a regular and fixed return on it.

b) No Obligation for Dividends: A company is not bound to pay dividend on preference shares if its profits in a particular year are insufficient. It can postpone the dividend in case of cumulative preference shares also. No fixed burden is created on its finances.

c) No Interference: Generally, preference shares do not carry voting rights. Therefore, a company can raise capital without dilution of control. Equity shareholders retain exclusive control over the company.

d) Trading on Equity: The rate of dividend on preference shares is fixed. Therefore, with the rise in its earnings, the company can provide the benefits of trading on equity to the equity shareholders.

e) No Charge on Assets: Preference shares do not create any mortgage or charge on the assets of the company. The company can keep its fixed assets free for raising loans in future.

f) Flexibility: A company can issue redeemable preference shares for a fixed period. The capital can be repaid when it is no longer required in business. There is no danger of over-capitalisation and the capital structure remains elastic.

g) Variety: Different types of preference shares can be issued depending on the needs of investors. Participating preference shares or convertible preference shares may be issued to attract bold and enterprising investors.

Disadvantages:

a) Fixed Obligation: Dividend on preference shares has to be paid at a fixed rate and before any dividend is paid on equity shares. The burden is greater in case of cumulative preference shares on which accumulated arrears of dividend have to be paid.

b) Limited Appeal: Bold investors do not like preference shares. Cautious and conservative investors prefer debentures and government securities. In order to attract sufficient investors, a company may have to offer a higher rate of dividend on preference shares.

c) Low Return: When the earnings of the company are high, fixed dividend on preference shares becomes unattractive. Preference shareholders generally do not have the right to participate in the prosperity of the company.

d) No Voting Rights: Preference shares generally do not carry voting rights. As a result, preference shareholders are helpless and have no say in the management and control of the company.

e) Fear of Redemption: The holders of redeemable preference shares might have contributed finance when the company was badly in need of funds. But the company may refund their money whenever the money market is favorable. Despite the fact that they stood by the company in its hour of need, they are shown the door unceremoniously.

3. DEFERRED SHARES

Deferred shares are also called as founder shares because these shares were normally issued to founders. The shareholders have a preferential right to get dividend before the preference shares and equity shares. No Public limited company or which is a subsidiary of a public company can issue deferred shares. These shares are issued to the founder shares to control over the management by the virtue of their voting rights.

a) No Par Share or Stock: According to Indian Companies Act, the shares issued by a company must have a definite face value. The face value of the share indicates the extent of interest in and the liability of the shareholder to the company.

b) Sweat Equity: Sweat equity is the non-monetary investment that owners or employees contribute to a business venture. Startups and entrepreneurs often use this form of capital to fund their businesses by compensating their employees with stock rather than cash, which also helps to align risk and rewards. In real estate, it refers to value-enhancing improvements made by homeowners to their properties.

CREDITORSHIP SECURITIES

DEBENTURE

Debenture is used to issue the loan by government and companies. The loan is issued at the fixed interest depending upon the reputation of the companies. When companies need to borrow some money to expand themselves they take the help of debentures.

Important features of Debentures:

- Debentures are instruments of debt, which means that debenture holders become creditors of the company. They are a certificate of debt, with the date of redemption and amount of repayment mentioned on it. This certificate is issued under the company seal and is known as a Debenture Deed.
- Debentures have a fixed rate of interest, and such interest amount is payable yearly or half-yearly.
- Debenture holders do not get any voting rights. This is because they are not instruments of equity, so debenture holders are not owners of the company, only creditors. The interest payable to these debenture holders is a charge against the profits of the company. So these payments have to be made even in case of a loss.

Advantages of Debentures:

a) One of the biggest advantages of debentures is that the company can get its required funds without diluting equity. Since debentures are a form of debt, the equity of the company remains unchanged.

b) Interest to be paid on debentures is a charge against profit for the company. But this also means it is a tax-deductible expense and is useful while tax planning.

c) Debentures encourage long-term planning and funding. And compared to other forms of lending debentures tend to be cheaper.

d) Debenture holders bear very little risk since the loan is secured and the interest is payable even in the case of a loss to the company.

e) At times of inflation, debentures are the preferred instrument to raise funds since they have a fixed rate of interest.

Disadvantages of Debentures:

a) The interest payable to debenture holders is a financial burden for the company. It is payable even in the event of a loss

b) While issuing debentures help a company trade on equity, it also makes it to dependent on debt. A skewed Debt-Equity Ratio is not good for the financial health of a company

c) Redemption of debentures is a significant cash outflow for the company which can imbalance its liquidity

d) During a depression, when profits are declining, debentures can prove to be very expensive due to their fixed interest rate

Types of Debentures:

There are various types of debentures that a company can issue.

a) Secured Debentures: These are debentures that are secured against an asset/assets of the company. This means a charge is created on such an asset in case of default in repayment of such debentures. So in case, the company does not have enough funds to repay such debentures, the said asset will be sold to pay such a loan. The charge may be fixed, i.e. against a specific assets/assets or floating, i.e. against all assets of the firm.

b) Unsecured Debentures: These are not secured by any charge against the assets of the company, neither fixed nor floating. Normally such kinds of debentures are not issued by companies in India.

c) Redeemable Debentures: These debentures are payable at the expiry of their term. Which means at the end of a specified period they are payable, either in the lump sum or in installments over a time period. Such debentures can be redeemable at par, premium or at a discount.

d) Irredeemable Debentures: Such debentures are perpetual in nature. There is no fixed date at which they become payable. They are redeemable when the company goes into the liquidation process. Or they can be redeemable after an unspecified long time interval.

e) Fully Convertible Debentures: These shares can be converted to equity shares at the option of the debenture holder. So if he wishes then after a specified time interval all his shares will be converted to equity shares and he will become a shareholder.

f) Partly Convertible Debentures: Here the holders of such debentures are given the option to partially convert their debentures to shares. If he opts for the conversion, he will be both a creditor and a shareholder of the company.

g) Non-Convertible Debentures: As the name suggests such debentures do not have an option to be converted to shares or any kind of equity. These debentures will remain so till their maturity, no conversion will take place. These are the most common type of debentures.

HOW SECURITIES AND EXCHANGE BOARD OF INDIA (SEBI) CONTROLS CAPITAL MARKET OF INDIA?

The Securities and Exchange Board of India (SEBI), was initially constituted on April 12, 1988 as a non contributory body through a resolution of the government for dealing with all matters related to development and regulation of securities market and investor protection and to advice the government on all these matters. SEBI was given statutory status and powers through an ordinance promulgated on January 30, 1992.

The Securities and Exchange Board of India (SEBI) is the regulatory body for dealing with all matters related to the development and regulation of securities market in India. SEBI was established on 12th of April in 1988. SEBI was given statutory powers on 12 April 1992 through the SEBI Act, 1992.

Organisational Structure of SEBI:

SEBI is managed by six members-one chairman (nominated by Central Government), two members (officers of central ministries), one member (from RBI) and remaining two members are nominated by Central Government. The office of SEBI is situated at Mumbai with its regional offices at Kolkata, Delhi and Chennai.

In 1988 the initial capital of SEBI was 7·5 crore which was provided by its promoters (IDBI, ICICI, IFCI). This amount was invested and with its interest amount day-to-day expenses of SEBI are met. All statutory powers for regulating Indian capital market are vested with SEBI itself.

Functions of SEBI

- To safeguard the interests of investors and to regulate capital market with suitable measures.
- To regulate the business of stock exchanges and other securities market.
- To regulate the working of Stock Brokers, Sub-brokers, Share Transfer Agents, Trustees, Merchant Bankers, Underwriters, Portfolio Managers etc. and also to make their registration.
- To register and regulate collective investment plans of mutual funds.
- To encourage self-regulatory organizations.
- To eliminate malpractices of security markets.
- To train the persons associated with security markets and also to encourage investors' education.
- To check insider trading of securities.
- To supervise the working of various organizations trading in security market and also to ensure systematic dealings.
- To promote research and investigations for ensuring the attainment of above objectives.

Decisions taken by SEBI for Ensuring a Healthy Capital Market:

SEBI has adopted a number of revolutionary steps to re-establish the credit of capital market, which include the following-

1. Control on utilizing 'application amount' having no interest by companies releasing public issues - At the instance of SEBI commercial banks introduced Stock Investment Scheme under which investor has to submit stock-invests, purchased from banks, with their share application. If the investor is allotted shares/debentures, the required amount is transferred in concerned company's account by the bank issuing 'Stock invests'.

In other case (if share/debenture is not allotted), investor gets a pre-determined interest rate on invested capital. This step of SEBI ensured interest earning to the investor until he got share/ debenture allotment. It also ensures the refund of invested amount to the investor in case shares are not allotted.

2. Share Price and Premium Determination - According to the latest directions of SEBI, Indian companies are now free to determine their share prices and premium on those shares. But determined price and premium amount will be equally applicable to all without any discrimination.

3. Underwriters- The minimum asset limit has been fixed to be ~ 20 lakh to work as underwriter. Besides, SEBI has warned under writers that their registration can be cancelled if any irregularity is found in the purchase of unsubscribed part of the share' issue.

4. Control on Share Brokers- Under new rules every broker and sub-broker has to obtain registration with SEBI and any stock exchange in India.

5. Insider Trading- Companies and their employees usually adopt malpractices in Indian capital market to variate share prices. To check this type of insider trading, SEBI introduced SEBI (Insider Trading) Regulation 1992 which will ensure honesty in the capital market and will develop a feeling of faith among investors to promote investments in capital market in the long run.

6. SEBl's Control on Mutual Funds- SEBI introduced SEBI (Mutual Funds) Regulation 1993 to take over direct control of all mutual funds of government and private sector (excluding UTI). Under this new rule, the company floating a mutual fund should possess net assets of 5 crore which should consist of at least 40% contribution from promoter's side.

7. Control on Foreign Institutional Investors-SEBI has made it compulsory for every foreign institutional investor to get registered with SEBI for participating in Indian capital market. SEBI has issued directives in this regard.

Hence it can be concluded that the SEBI plays a very prominent role in the smooth operation of the capital market of India so that the precious money of the investors can give them good return with less uncertainty.

RECENT TRENDS: MEASURES TAKEN BY SEBI TO REGULATE THE INDIAN CAPITAL MARKET:

Securities Exchange Board of India acts as a watchdog for the Indian Capital Market. The Board enacted by The Securities and Exchange Board of India Act, 1992 ("the Act") has been accorded with comprehensive powers under the Act. The preamble of the Board describes its functions as to "protect the interests of investors in securities and to promote the development of, and to regulate, the securities market and for matters connected therewith or incidental thereto". In addition to the intent behind the establishment of the Board, Section 11 of the Act lays down the functions of the Board that clearly illustrate "it shall be the duty of the board to protect the interests of investors in securities and to promote the development of, and to regulate the securities market, by such measures as it thinks fit".

This provision exemplify that SEBI has been authorized to take any such measures that in its opinion would protect the interest of the investors and would aid to regulate the market. It's the reason SEBI keeps on revising and updating by formulating new measures or directions that make securities market conducive, safe and friendly for all kinds of investors that include retail or institutional investors.

In the past few months, during and after COVID-19 lockdown times, there have been some key instrumental measures that have been taken by SEBI, such as:

- **Introduction of UPI and Application through online interface for Public Issue of Debt Securities:** SEBI, in its circular dated November 23, 2020 announced the introduction of Unified Payments Interface ["UPI"] Mechanism and application through online interface for public issue of debt securities. This system has already been in existence for issue of public shares since January, 2019 but is now made available for public debt securities through this circular issued by SEBI under Section 11 of the Act. The said mechanism is in addition to an already existing specified mode under Application Supported by Blocked Amount ["ASBA"]. It would be available for securities opening up for issuance from January 1, 2021 for applications up to a limit of 2 lakhs. The concerned entities include National Payments Corporation of India ["NPCI"], UPI and the Sponsor Bank.

- **Increased Efficiency of E-Voting mechanisms for Meetings:** The Companies Act, 2013 mandates a company to provide e-voting facility to the shareholders. Section 108 of The Companies Act, 2013 along with Rule 20 of the Companies (Management & Administration) Rules, 2014 provide for such a facility. Additionally, regulation 44 of the SEBI (Listing and Obligatory Disclosure Requirement) Regulations, 2015 also contains provision to this regard.

On Dec 09, 2020, SEBI released a circular directing the listed entities to provide e-voting facility to its shareholders. The mechanism called for a system wherein the shareholders will have an option to forecast their votes directly through their Dematerialized ["DEMAT"] accounts with the depositories which will forward their votes to the E-voting service providers ["ESP"]. The process would take place in two phases. First phase, wherein the shareholders can cast their vote either through the depository's website or their DEMAT account. After which, the depositories will give the confirmation of the votes to the shareholders once received from ESP's. In the second phase, the depository will set up an OTP system for login. For this new and much efficient mechanism, SEBI has also asked the Depositories and the ESP's to provide helpline services to shareholders, whereas ESP's have been directed to provide links for disclosures by the companies and the report of proxy advisors for investor's awareness.

- **Reclassification rules of promoters as public shareholders and disclosure of their shareholding pattern:** Rules for reclassification of promoters have been mentioned in Regulation 31A of SEBI (Listing Obligations and Disclosure Requirements) Regulation, 2015. On 23rd of November, 2020, SEBI released a consultative paper on the same that proposed a few amendments to the existing rules pertaining to promoter reclassification. It composed of the following proposed amendments:

Promoters with shareholding up to 15%, seeking to reclassify should be allowed with shareholding's status quo maintained. One-month duration for meeting between board & shareholders and for reclassification request to be put up before exchange. Promoters seeking reclassification pursuant to an order/direction of government or regulator should be exempted like reclassification pursuant to resolution approved under Insolvency and Bankruptcy Code, 2016. Promoters seeking reclassification pursuant to an offer should be exempted from the reclassification procedure where intent for reclassification is mentioned in the offer letter which needs to be in accordance with SEBI Substantial Acquisition of Shares and Takeover [“SAST”] Regulations and Regulation 31A(3)(b) and 31A(3)(c) of SEBI(LODR) Regulations, 2015.

Pursuant to an offer, where the former promoters aren’t traceable by the listed entity or not cooperative towards it, exemption from reclassification procedures should be given if erstwhile promoters aren’t in control of the company and diligent efforts have been made by the listed company to reach out to them.

Mandatory disclosure of promoters.

Additionally, SEBI has been looking forward to revamp the grievance redressal system for the stock exchange, for which the regulator issued directions to the Bombay Stock Exchange regarding the clients of the defaulting trading members. All inclusive, SEBI keeps on making endeavors to structure the capital market in the interest of the investors, listed entities or any stakeholders that form a part of the capital market. The recent measures have been taken keeping into account, the shortcomings of the laid down procedures or regulations of investing in share market. The Indian capital market should essentially avail the benefit of the rise in fintech like any other sectors of the economy.

QUESTION BANK

UNIT – I

PART - A

S. No	Questions	CO	Level
1	Explain the functions of a financial market.	CO1	L1
2	State and explain in brief about various new capital market instruments in Indian Securities Market.	CO1	L1
3	List out the prime objectives of SEBI.	CO1	L2
4	"Money Market is essentially a Market for short term funds." Discuss.	CO1	L2
5	Distinguish between Capital Market and Money Market.	CO1	L2
6	Explain preference shares.	CO1	L2
7	Pure Instruments and Hybrid Instruments – explain.	CO1	L2
8	Differentiate organized and un-organized market.	CO1	L1
9	Distinguish between: Money Market & Securities Market	CO1	L3
10	Give a brief note on Hybrid Instruments.	CO1	L3

PART – B

S. No	Questions	CO	Level
1	Briefly discuss the evolution, growth and functions of financial system in India.	CO1	L2
2	"Money market is very important segment of Indian Financial System". Comment and discuss various features of money market.	CO1	L3
3	Discuss the various powers and functions of the SEBI.	CO1	L4
4	Explain the role of SEBI in strengthening regulatory framework and fostering investor confidence.	CO1	L3
5	Explain the various Money Market Instruments.	CO1	L3
6	Explain the recent Capital Market reforms in India.	CO1	L3

7	Explain briefly with reference to capital market: Dual option warrant.	CO1	L5
8	Discuss briefly the regulatory framework governing the securities in India.	CO1	L5
9	Describe the activities that would be carried on by a Broker.	CO1	L4
10	Collect the information about the companies that have recently mobilized resources through primary market.	CO1	L6

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SCHOOL OF MANAGEMENT STUDIES

UNIT – II – CAPITAL MARKETS – SBAA3003

Primary market - Definition and Function - Methods of new issues -Right issue -Bonus issue - Secondary market-Types of brokers and speculators -Bulls ,Bears, Stag, Lame duck Primary - Stock exchange in India-BSE ,NSE- Origin Organization - Basis of Sensex and Nifty

PRIMARY MARKET - INTRODUCTION

"Primary market" may also refer to a market in art valuation. The primary market is the part of the capital market that deals with the issuance and sale of equity-backed securities to investors directly by the issuer. Investors buy securities that were never traded before. Primary markets create long term instruments through which corporate entities raise funds from the capital market. It is also known as the New Issue Market.

Since the securities are issued directly by the company to its investors, the company receives the money and issues new security certificates to the investors. The primary market plays the crucial function of facilitating the capital formation within the economy. The securities issued at the primary market can be issued in face value, premium value, and at par value.

A primary market is a source of new securities. Often on an exchange, it's where companies, governments, and other groups go to obtain financing through debt-based or equity-based securities. Primary markets are facilitated by underwriting groups consisting of investment banks that set a beginning price range for a given security and oversee its sale to investors. Once the initial sale is complete, further trading is conducted on the secondary market, where the bulk of exchange trading occurs each day.

DEFINITION:

Primary Market is a form of the capital market wherein new securities are sold by the companies for the very first time to the investors, to raise funds and that is why it is also acknowledged as New Issues Market (NIM).

FUNCTIONS OF PRIMARY MARKET:

The main function of the primary market is to mobilize the investible money from the savers to the companies or young entrepreneurs who seek funds to set up new businesses or expand the existing venture, by issuing securities.

The functions of such a market are manifold

- New issue offer
- Underwriting services
- Distribution of new issue

TYPES OF ISSUE OF SECURITIES IN PRIMARY MARKET:

There are several types of issue of securities in the primary market which are discussed as under:

Types of issue of securities in premium market

- Public issue
  - Initial public offer(IPO)
  - Further public offer (FPO)
- Right issue
- Bonus issue
- Private placement
- Preferentially allotment
- Qualified institutional placement
- Institutional placement programme

MEANING OF ISSUE MARKET:

A new issue is a stock or bond that is being sold to investors for the first time. The market that deals with these new issues is called the new issue market, as opposed to the secondary market that deals with existing shares and bonds.

TYPES OF ISSUE MARKET:

- Public Issues
- Private Placement
- Preferential Issues
- Rights Issues
- Offer for sales
- Bonus Issue

PUBLIC ISSUES:

Public Issues or Public Offering refers to the issue of shares or convertible securities in the primary market by the promoters of a company to attract new investors for a subscription. Section 23 of the Companies Act, 2013 prescribes the provisions for issuing of shares.

- **INITIAL PUBLIC OFFERING:** An initial public offering (IPO) refers to the process of offering shares of a private corporation to the public in a new stock issuance. Public share issuance allows a company to raise capital from public investors. Meanwhile, it also allows public investors to participate in the offering.

FAST TRACK ISSUE: The entire shareholding of the promoter group of the issuer is held in dematerialized form on the reference date in case of a rights issue by listed issuer, the date of filing the letter of offer with the designated stock exchange.

PREFERENTIAL ISSUES:

Preferential Offer' means an issue of shares or other securities, by a company to any select person or group of persons on a preferential basis and does not include shares or other securities offered through a public issue, right issue, employee stock option scheme, employee stock purchase scheme or an issue of sweat.

RIGHT ISSUES:

A rights issue is an invitation to existing shareholders to purchase additional new shares in the company. This type of issue gives existing shareholders securities called rights. With the rights, the shareholder can purchase new shares at a discount to the market price on a stated future date.

OFFER FOR SALE:

An Offer for Sale is a simpler method wherein promoters in public companies can sell their shares and reduce their holdings in a transparent manner through the bidding platform for the Exchange Offer for Sale mechanism is available to 200 top companies in terms of market capitalization.

PRIVATE PLACEMENT:

A private placement is a sale of stock shares or bonds to pre-selected investors and institutions rather than on the open market. It is an alternative to an initial public offering (IPO) for a company seeking to raise capital for expansion.

BONUS ISSUE:

A bonus issue, also known as a scrip issue or a capitalization issue, is an offer of free additional shares to existing shareholders. A company may decide to distribute further shares as an alternative to increasing the dividend payout. For example, a company may give one bonus share for every five shares held.

PARTIES INVOLVED IN THE NEW ISSUE:

- Managers to the issue
- Registrar to the issue
- Underwriters
- Bankers
- Advertising agencies
- Financial institutions
- Government or statutory agencies.

MANAGERS TO THE ISSUE:

The issuing company appoints the managers to manage activities relating to the issue. The merchant banking division, subsidiary of commercial banks, foreign banks, private banks and private agencies are competent to act as managers to the issue. Generally, they perform the following duties:

- Drafting of prospectus.
- Preparing budgeted expenses related to the issue.
- Determining the appropriate timing of the issue.
- Advising the company on the matters related to the appointment of registrars, underwriters, brokers, bankers to the issue, advertising agencies, etc.

REGISTRAR TO THE ISSUE:

Registrars are appointed in consultation with the lead managers to the issue. SEBI has laid down guidelines relating to the appointment of a registrar. Companies having competency and expertise, manpower, infrastructure and capital adequacy are allowed to appoint registrar to the issue. A registrar is an important intermediary who performs all the activities connected with the new issue management. Usually, the registrar to the issue performs those functions connected with the allotment of securities.

DUTIES OF THE REGISTRAR TO THE ISSUE:

- The registrars help in identifying the collection centres and collecting banker. They receive share applications from various collection centres.
- They reclassify valid applications for allotment of securities.
- They approach regional stock exchange and finalize the basis of allotment. Then they finalize the allotment of securities on the basis of approval by the stock exchange.
- The registrars arrange for the dispatch of the share certificates.
- The registrars make arrangements to pay the brokerage and underwriting commission.

- They also assist the company in getting the shares listed on the stock exchange.

UNDERWRITERS:

Underwriting is a contract in which the underwriter guarantees subscription to the issue. Underwriters may be financial institutions, banks and approved investment companies. While appointing an underwriter, his financial strength, experience in the primary market, past underwriting performance, outstanding underwriting commitment, investor clientele etc., are considered by the issuing company.

After the closure of subscription, the company furnishes the details of shares which are not subscribed to the underwriter. He would take up the agreed portion of the shares. If he fails to do so, the company may claim damages from the underwriter for any loss suffered by it.

BANKERS:

The role of bankers in connection with issue is very important. They collect application money along with application forms. They charge commission in consideration of the services performed for the issuing company. If the issue is large, more than one banker may be appointed. The banker should have branches in those collection centres specified by the central government. Bankers may be coordinating bankers or collecting bankers. Collecting bankers collect subscription, while coordinating bankers coordinate the collection work. They also monitor the issue and report to the registrars.

ADVERTISING AGENCIES:

Advertising plays an important role in promoting the issue. So, while selecting an advertising agency, the competency and the past record of the advertising agency are the factors that are considered before its appointment. Moreover, the tentative programmes (proposals) and estimated costs of various advertising agencies are scrutinized before selecting one. Finally, a suitable advertising agency is appointed in consultation with the lead managers to the issue. Advertising agencies undertake to give wide publicity to the issue through media such as newspapers, magazines, bill boards, television, etc.

FINANCIAL INSTITUTIONS:

In India, financial institutions also underwrite the issue. They also extend term loans to the issuing company. The lead manager a sends copy of the prospectus and the proposed programme for public issue to the financial institutions. On the strength of these documents, the financial institutions agree to underwrite and give financial help.

GOVERNMENT AND STATUTORY AGENCIES:

The following are the some important government and statutory agencies related to the new issue in the primary market.

- Securities Exchange Board of India (SEBI)
- Registrar of Companies.
- Reserve Bank of India in case of issue involving foreign investments.
- Stock Exchange on which the issue is to be listed.
- Industrial licensing authorities; and,
- Pollution Control authorities, whose clearance is obtained for the project, is to be stated in the prospectus.

SECONDARY MARKET - INTRODUCTION:

"Secondary Market" is where investors buy and sell securities they already own. It is what most people typically think of as the "stock market," though stocks are also sold on the primary market when they are first issued. The national exchanges, such as the New York Stock Exchange (NYSE) and the NASDAQ, are secondary markets.

Though stocks are one of the most commonly traded securities, there are also other types of secondary markets. For example, investment banks and corporate and individual investors buy and sell mutual funds and bonds on secondary markets. Entities such as Fannie Mae and Freddie Mac also purchase mortgages on a secondary market.

Transactions that occur on the secondary market are termed secondary simply because they are one step removed from the transaction that originally created the securities in question. For example, a financial institution writes a mortgage for a consumer, creating the mortgage security. The bank can then sell it to Fannie Mae on the secondary market in a secondary transaction.

In secondary markets, investors exchange with each other rather than with the issuing entity. Through massive series of independent yet interconnected trades, the secondary market drives the price of securities toward their actual value.

TYPES OF SECONDARY MARKET:

Secondary markets are primarily of two types – Stock exchanges and over-the-counter markets.

STOCK EXCHANGE:

Stock exchanges are centralized platforms where securities trading take place, sans any contact between the buyer and the seller. National Stock Exchange (NSE) and Bombay Stock Exchange (BSE) are examples of such platforms.

Transactions in stock exchanges are subjected to stringent regulations in securities trading. A stock exchange itself acts as a guarantor, and the counterparty risk is almost non-existent. Such a safety net is obtained via a higher transaction cost being levied on investments in the form of commission and exchange fees.

OVER-THE-COUNTER (OTC) MARKET:

Over-the-counter markets are decentralized, comprising participants engaging in trading among themselves. OTC markets retain higher counterparty risks in the absence of regulatory oversight, with the parties directly dealing with each other. Foreign exchange market (FOREX) is an example of an over-the-counter market.

In an OTC market, there exists tremendous competition in acquiring higher volume. Due to this factor, the securities' price differs from one seller to another. Apart from the stock exchange and OTC market, other types of secondary market include auction market and dealer market.

The former is essentially a platform for buyers and sellers to arrive at an understanding of the rate at which the securities are to be traded. The information related to pricing is put out in the public domain, including the bidding price of the offer.

Dealer market is another type of secondary market in which various dealers indicate prices of specific securities for a transaction. Foreign exchange trade and bonds are traded primarily in a dealer market. Over-the-counter trading refers to party-to-party exchanges that happen privately through extensive, decentralized networks. Companies trading on OTC market's range from basic penny stocks to household-name multinational conglomerates. Similarly, traders range from first-time investors to seasoned backers. All have enjoyed tremendous success participating in off-exchange markets.

As many well know, the New York Stock Exchange takes place in a centralized, physical location. In contrast, OTC markets don't have a set location. Instead, they consist of networks that exist almost entirely online. The OTC Markets Group is the largest and best-known coterie of trading networks. It consists of three stock exchanges: OTC Pink, OTCQB, and OTCQX. In the simplest terms, the OTC markets are "junior markets." The companies on these markets are too small to qualify for listing on the big exchanges, like the NYSE or NASDAQ. Instead, these companies can opt for trade on a network owned by the OTC Markets Group.

Trading is peer-to-peer and private with prices generally kept unpublished. Traded products range from commodities to penny stocks. Additionally, there are derivative products like CDOs and CMOs. OTC markets have significantly fewer regulations than stock exchanges. This leaves traders to make deals and bilateral contracts as they see fit. The popularity of over-the-counter trading has exploded in the past decade. Everyone can find value in these off-exchange trading networks. Traders range from amateur investors to accomplished business owners. Our OTC stock loans are about helping investors retain their well-earned portfolio diversity. At the same time, investors can access the liquidity needed to make further investments.

ADVANTAGES OF SECONDARY MARKET:

Secondary markets are markets where already issued securities trade. Such securities include stocks and bonds. They involve dealings between buying and selling investors, the issuing company does not receive any money from these transactions. Registered stock exchanges are a good example of secondary markets. Stock exchanges provide a legal and convenient way for the trading of securities by providing the necessary facilities and rules that govern the transaction of securities. Secondary markets are advantageous to businesses in many ways.

MOBILIZE SAVINGS:

When businesses or even individuals hold their money in form of shares, they can easily mobilize funds for investments. Securities traded in the secondary markets are not as liquid as cash therefore this limits the ease of accessing cash. Accumulation of funds for long-term capital projects is therefore easy and possible. The secondary market provides a convenient platform for the trade of securities hence shares can be easily converted to cash for investment.

INVESTMENT OPPORTUNITIES:

As opposed to holding money in savings accounts, the secondary market provides investors with an opportunity to save and at the same time invest. Shareholders either earn capital gain from the resale of shares or earn dividends on shares held. Investment in shares does not require a large capital outlay therefore providing small businesses with a chance to invest and expand their portfolios.

INVESTMENT ADVICE:

Apart from providing the investing public a platform to trade in securities, secondary markets also offer investment advice. Stockbrokers, investment advisers and other players in the secondary market offer investors advice on complex matters that may arise in the trade of securities. Investors therefore do not need to be stock market experts to invest in stocks or bonds. With some form of advice, any interested investors can make money in the stock exchange.

IMPROVES CORPORATE GOVERNANCE:

The shares of listed companies trade in the stock exchange, a secondary market. Managers are only custodians of the company; shareholders are the owners. Having a large variety of shareholders is beneficial to the company since managers' accountability improves: The demands of shareholders must be met hence the management has to be efficient in its operations. Management of listed companies is better than that of private companies since shareholders keep watch over the managements' actions.

DISADVANTAGES OF SECONDARY MARKET:

DATA DEFINITIONS:

Secondary Researcher needs to understand various parameters and assumptions that primary research had taken while collected information. A term may have different meaning for different people, example a term 'youth' used is ambiguous and one needs to find what is the assumed age taken by primary researcher.

INACCURACY OF DATA:

As we are not gathering our own information, first-hand, we are totally dependent on someone else's efforts. Primary researcher may have been biased or may have used questionable methods to collect data; this can be pretty risky for secondary researchers to base their report on such data.

TIME LAG ISSUES:

Information collected from books, historical surveys are usually not sync with the times and might have changed drastically. Thus making such information a foundation of research may be highly risky for the business or project.

MAY NOT BE SPECIFIC:

Extensiveness of such information is its benefit as well as drawback. Organization will not get answers to their specific issues through this data directly and one needs to 'mine' further into it to get relevant information.

PROPRIETARY ISSUES:

Some of the secondary sources might have copyrighted their information and using them without permission can lead to various legal complications. Usually it's for small organizations and projects secondary market research is preferred because the time and amount of money required is less.

BROKERS - INTRODUCTION:

Broker a person or firm who arranges transactions between a buyer and a seller for a commission when the deal is executed. A broker who also acts as a seller or as a buyer becomes a principal party to the deal. Neither role should be confused with that of an agent one who acts on behalf of a principal party in a deal.

DEFINITION:

A broker is an independent party whose services are used extensively in some industries. A broker's prime responsibility is to bring sellers and buyers together and thus a broker is the third-person facilitator between a buyer and a seller. An example would be a real estate or stock broker who facilitates the sale of a property.

Brokers can furnish market research and market data. Brokers may represent either the seller or the buyer but generally not both at the same time. Brokers are expected to have the tools and resources to reach the largest possible base of buyers and sellers. They then screen these potential buyers or sellers for the perfect match. An individual producer, on the other hand, especially one new in the market, probably will not have the same access to customers as a broker. Another benefit of using a broker is cost they might be cheaper in smaller markets, with smaller accounts, or with a limited line of products.

Some brokers, known as discount brokers, charge smaller commission, sometimes in exchange for offering less advice or services than full service brokerage firms. A broker-dealer is a broker that transacts for its own account, in addition to facilitating transactions for clients.

Brokerage firms are generally subject to regulations based on the type of brokerage and jurisdictions in which they operate. Examples of brokerage firm regulatory agencies include the U.S. Securities and Exchange Commission and the Financial Industry Regulatory Authority (FINRA), which regulate stockbrokers in the United States.

TYPES OF BROKERS:

- Full service broker
- Advisory
- Discretionary Management
- Discount brokers

FULL SERVICE BROKER:

Full-service broker is a licensed financial broker-dealer firm that provides a large variety of services to its clients; including research and advice, retirement planning, tax tips, and much more. Of course, this all comes at a price, as commissions at full-service brokerages are much higher than those at discount brokers.

Full-service brokers can provide expertise for people who don't have the time to stay up-to-date on complicated issues such as tax or estate planning; however, for those who just want to execute trades without the extra services, discount brokers are the way to go.

Full-service brokers offer customized support and interaction in facilitating trades, managing portfolios, financial planning, and wealth management services for clients. Clients are assigned to individual stockbrokers and/or financial advisors. They are the main point of contact at a full-service brokerage firm.

Clients of full-service brokerages appreciated the convenience of having a personal broker handle all their investment needs. It is a one-stop shop for investment and financial management. Most full-service firms provide online access and trading platforms. Self-directed investors tend to take advantage of these offerings. These platforms are loaded with fundamental research, order execution, and technical analysis

ADVISORY:

A broker or brokerage that, in addition to making trades on behalf of the client, provides investment advice. That is, the advisory broker recommends the client buys or sells certain securities, in accordance with his/her investment goals. The advisory broker receives a fee in addition to the commissions given for the actual trades.

DISCRETIONARY MANAGEMENT:

Discretionary investment management is a form of investment management in which buy and sell decisions are made by a portfolio manager or investment counselor for the client's account. The term "discretionary" refers to the fact that investment decisions are made at the portfolio manager's discretion.

DISCOUNT BROKERS:

A discount broker is a stockbroker who carries out buy and sells orders at reduced commission rates compared to a full-service broker. However, a discount broker does not provide investment advice or perform analysis on a client's behalf, unlike a full-service broker. Before the emergence of better communications technology, only the wealthy could afford a broker and access to the stock market.

However, the Internet has brought an explosion of discount online brokers that allow individuals with smaller capital to trade for lower fees and with less capital. In terms of the stock market, most discount brokers operate through online platforms. As a result, a discount broker is nearly synonymous with online brokerages.

Discount brokers carry out orders at less cost, but they typically just execute orders for their clients. These brokers do not offer personal consultations, advice, research, tax planning, and estate planning services for customers. The lack of these services, and because they do not spend money closing deals with high-net-worth individuals, means that discount brokers can offer lower fees. Additionally, most discount brokers operate their businesses online where the overheads are low. So low in fact, that beginning in 2019, many discount brokers even went so far as to forego commissions altogether for certain types of securities.

In the securities industry, discount brokerages provide clients with their own accounts to enter orders for execution. These investors usually do not interact with a live broker. If they do, the communication is minimal and only engaged in trade executions. The services provided by discount brokers are aimed at self-directed traders and investors, and the electronic trading platforms are built in a way that is beneficial for active traders with charting and position monitoring services.

SPECULATOR - MEANING:

In the world of finance, speculation, or speculative trading, refers to the act of conducting a financial transaction that has substantial risk of losing value but also holds the expectation of a significant gain or other major value. With speculation, the risk of loss is more than offset by the possibility of a substantial gain or other recompense.

An investor who purchases a speculative investment is likely focused on price fluctuations. While the risk associated with the investment is high, the investor is typically more concerned about generating a profit based on market value changes for that investment than on long-term investing. When speculative investing involves the purchase of a foreign currency, it is known as currency speculation. In this scenario, an investor buys a currency in an effort to later sell that currency at an appreciated rate, as opposed to an investor who buys a currency in order to pay for an import or to finance a foreign investment.

Without the prospect of substantial gains, there would be little motivation to engage in speculation. It may sometimes be difficult to distinguish between speculation and simple investment, forcing the market player to consider whether speculation or investment depends on factors that measure the nature of the asset, expected duration of the holding period and/or amount of leverage applied to the exposure.

TYPES OF SPECULATOR:

There are 4 types of speculators in a stock exchange.

They are:

- Bulls
- Bears
- Stags
- Lame Ducks.

BULL:

A Bull is a speculator who anticipates rise in the price of securities. He buys securities with a view to sell them in future at a higher price and thereby earns profits. In case the prices of securities fall, he loses. He has the option to carry forward the transaction to the next settlement by paying a charge termed, ‘contango’. In India, a bull is also known as tejiwala. He is said to be a bull because just like a bull which tries to throw its victim up in the air, he expects to profit from increase in share prices.

BEAR:

A Bear is a speculator, who anticipates fall in the price of securities. He sells-securities for future delivery. He sells securities which he does not possess with the hope to buy the securities at a lower price before the date of delivery. In India, a bear is also known as mandiwala.

STAG:

A stag is bullish in nature. A stag applies for securities of a new company with the idea of selling them at a premium after allotment. His profit is the excess of the price at which he sells his allotment over the amount paid by him while applying. He expects that the prices of securities that he applies for would increase. Let us assume Mr. X applies for 100 shares of Rs.10 each in ABC Ltd., In case he is allotted 100 shares and he sells it for Rs.15, his profit will be Rs.500 (100 x Rs.15 – 100 x Rs. 10). The activity undertaken by a stag is not free from risk. The price of securities might decline after allotment. This situation can arise even in case of at par issues but happens mostly in case of issues which carry a high premium.

Let us assume Mr. X applies for 100 shares of Rs.10 each issued at Rs.140 premium by ABC Ltd and after allotment, the price declines to Rs.70, he would suffer a loss. His loss would be Rs.8,000 i.e., the difference between the amount realized from sale minus the amount paid on application (100 x Rs.150 — 100 x Rs.70). He would neither earn a profit not incur a loss if he is not allotted securities in a public issue because of over subscription.

LAME DUCK:

This refers to the condition of a bear who is not able to meet his commitments. A bear sell securities which he does not hold, with the expectation that prices are going to fall. His intention is to buy them at a lower price later and profit from the difference. On the fixed date he may not be able to deliver the security as it may not be available in the market. The buyer may not be inclined to carry forward the transaction. In such a case, the bear is said to be struggling like a lame duck.

TYPES OF SPECULATIVE TRANSACTIONS:

The various types of transactions, which facilitate speculative dealings, can be classified into:

- Option Dealings,
- Margin Trading,
- Arbitrage,
- Wash Sales,

- Blank Transfer,
- Carry Over or Budla Transactions,
- Cornering,
- Rigging the Market.

OPTION DEALINGS:

The term option means a right. Option dealing is an arrangement of right to buy or sell a certain number of specified securities at a predetermined price within a prescribed time limit. Option dealing is a highly risky transaction in securities whose price fluctuates violently. To avoid the risk of loss, the speculators enter into option dealings.

In option dealing, the speculator enters into a contract with another person and thereby acquires the right to deal with him either to buy or sell certain securities at a specified price on a specified date. If he is a bull speculator, he shall enter into purchase options and if the speculator is a bear, he will contract sale options. The speculator should also pay a certain sum of money as consideration. It is known as option money.

However, the speculator has no actual intention to take or to give delivery of the securities, but simply to gain or lose when there is a rise or fall in the prices in future. Thus option dealings have the element of price insurance against fluctuation.

Kinds of Option dealings:

Option dealings can be classified into three categories viz.,

- Call
- Put
- Call and Put.

Besides, some authors included Gale option as a separate category.

MARGIN TRADING:

Margin trading is a system of purchasing securities with funds borrowed from brokers. For margin trading, the client opens an account with the broker by depositing a certain amount in cash or securities. He also agrees to maintain the margin at a certain level.

The broker will debit the client’s account with the amount of purchases and various charges like brokerage, commission etc. and credit the account with the cash deposited and the sale proceeds. Generally, the price difference is credited or debited as the case may be.

ARBITRAGE:

Arbitrage is a highly specialized and skilled speculative activity. It is undertaken to make profit out of the differences in prices of a security in two different markets. The speculator buys the security in one market where its price is cheaper and sells it in another market where its price is high. These transactions aim to bring about a leveling of prices in two markets.

WASH SALES:

Wash sales are fictitious transactions. Under this method, the speculator sells his securities and then repurchases the same through a broker at a higher price. Actually, no transaction takes place in the wash sales. By this process, an artificial demand can be created which mill ultimately, lead to an artificial rise in price. The speculator will then sell the securities at the increased price and makes the profit.

BLANK TRANSFER:

It is a method of the transfer without mentioning the name of the transferee in the transfer deed. Blank transfer, in fact, is a routine method of transferring the securities from one person to another. Therefore, it is not a speculative activity. However, it is quite helpful in making speculation in securities easier.

The usual method of transfer is that the transferor i.e. the seller should write the name of the transferee i.e. the buyer and he should pay the stamp duty. But in case of a blank transfer, he simply signs on the instrument of transfer and merely delivers the securities along with the instrument. By this process the shares can be transferred in any number of times and finally any transferee who wants to get the shares registered in his name can submit the blank transfer form along with the security and get them transferred in his name. It saves stamp duty on every transfer.

CARRY OVER OR BUDLA TRANSACTIONS:

In case of forward delivery contracts, if both the parties agree, the contract can be settled in the next settlement date (probably in the next month or fortnight). Such postponement is called “Carry Over” or “Budla“. This is usually done if the prices move against the expectations of the speculator.

CORNERING:

A corner is the condition of the market in which an individual or a group of individuals holds almost the entire supply of a particular security. The speculators will enter into purchasing contracts with the bears in certain securities. Thereafter, by purchasing substantially the whole of the available securities and getting their actual delivery, the speculator will make such securities to go out of the market. In such an event, he will insist the bear speculators to make actual delivery of the securities, on the fixed date.

The bears will find it difficult to effect actual delivery since such securities have already disappeared from the market. At this stage, the speculator will be able to dictate the terms and the bears in the market are said to “Squeezed“. The bear will now be a lame duck.

RIGGING THE MARKET:

Rigging means artificially forcing up the market price of a particular security. The bull speculators generally carry on this activity. Due to strong bull movement, the price of certain security will go up and a demand shall be created. When the prices rise, they will sell the securities and make the profit. Rigging is another unhealthy practice, which disturbs the free interplay of demand and supply.

ADVANTAGES OF SPECULATION:

SUSTAINABLE CONSUMPTION LEVEL:

Let’s consider some of the principles that explain the causes of shortages and surpluses and the role of speculators. When a harvest is too small to satisfy consumption at its normal rate, speculators come in, hoping to profit from the scarcity by buying.

Their purchases raise the price, thereby checking consumption so that the smaller supply will last longer. Producers encouraged by the high price further lessen the shortage by growing or importing to reduce the shortage. On the other side, when the price is higher than the speculators think the facts warrant, they sell. This reduces prices, encouraging consumption and exports and helping to reduce the surplus.

Another service provided by speculators to a market is that by risking their own capital in the hope of profit, they add liquidity to the market and make it easier or even possible for others to offset risk, including those who may be classified as hedgers and arbitrageurs.

MARKET LIQUIDITY AND EFFICIENCY:

Without speculators, only producers and consumers would participate in that market. With fewer players in the market, there would be a larger spread between the current bid and ask price of commodities. Any new entrant in the market who wanted to trade in commodities would be forced to accept an illiquid market, would enter the market with large difference in the bid price and ask price or may not find any counterparties at all.

A commodity speculator may exploit the difference and reduce the spread through competition with other speculators. Some argue that speculators increase the liquidity in a market, and therefore promote an efficient market, while others say that, as more and more speculators participate in a market, underlying real demand and supply can become diminishingly small compared to trading volume, and prices can become distorted.

BEARING RISKS:

For instance, a farmer might be considering planting cotton on some unused farmland. But he might not want to do so because he is concerned that the price might fall too far by harvest time. By selling his crop in advance at a fixed price to a speculator, the farmer can hedge the price risk and is now willing to plant the corn. Thus, speculators can actually increase production through their willingness to take on risk.

FINDING ENVIRONMENTAL AND OTHER RISKS:

Hedge funds that do “fundamental analysis “are far more likely than other investors to try to identify a firm’s “off-balance-sheet exposures”, including “environmental or social liabilities present in a market or company but not explicitly accounted for in traditional numeric valuation or mainstream investor analysis", and hence make the prices better reflect the true quality of operation of the firms.

SHORTING:

Shorting may act as a means to stop unsustainable practices earlier and thus reduce damages and forming market bubbles.

DISADVANTAGES OF SPECULATION:

WINNER'S CURSE:

Auctions are a method of squeezing out speculators from a transaction, but they may have their own perverse effects. The winner's curse says that in an auction, the winner will tend to overpay in one of two ways: The winning bid exceeds the value of the auctioned asset such that the winner is worse off in absolute terms; or The value of the asset is less than the bidder anticipated, so the bidder may still have a net gain but will be worse off than anticipated.

The winner's curse is not very significant to markets with high liquidity for both buyers and sellers, as the auction for selling the product and the auction for buying the product occur simultaneously, and the two prices are separated only by a relatively small spread. This mechanism prevents the winner's curse phenomenon from causing mispricing to any degree greater than the spread.

ECONOMIC BUBBLES:

Speculation is often associated with economic bubbles. A bubble occurs when the price for an asset exceeds its intrinsic value by a significant margin. Speculative bubbles are characterized by rapid market expansion driven by word-of-mouth as initial rises in commodity price attract new buyers and generate further inflation. Speculative bubbles are essentially social epidemics whose contagion is mediated by the structure of the market.

VOLATILITY:

For a speculator, a good performance would occur when there is a very high level of volatility. It is a controversial point whether the presence of speculators increases or decreases the short-term volatility in a market. Their provision of capital and information may help stabilize prices closer to their true values. On the other hand, crowd behaviour and positive feedback loops in market participants may also increase volatility at times.

STOCK EXCHANGE - MEANING:

The stock exchange is an organization that facilitates this process of buying and selling existing securities by providing a medium for buyers and sellers to interact with each other. As there could be a large number of buyers and sellers who want to trade in a particular security, stock exchanges facilitate arriving at a trading price based on supply and demand by providing a medium. They help both buyers and sellers arrive at a mutually satisfactory price.

As the stock exchange deals in all types of securities, it is known as the 'securities market' or 'securities exchange' also. A stock exchange is a secondary market of securities because the trading happens only for the securities that have already been issued to the public and now being allowed to be traded on the floor of a stock exchange after getting listed with the stock exchange.

DEFINITION:

The word “Stock Exchange” is made from two words 'Stock' and Exchange. Stock means part or fraction of the capital of a company, and Exchange means transferring the ownership; representing a market for purchasing and selling. Thus, we can describe the stock exchange as a market or a place where different types of securities are bought and sold. Securities traded on a stock exchange include shares issued by companies, unit trusts, derivatives, pooled investment products, and bonds.

Brigham, Eugene F, author of financial management, defines a financial market as “The place where people and organizations acting to borrow money are brought together with those having surplus funds”.

BENEFITS OF STOCK EXCHANGE:

The stock exchange has benefitted difference stakeholders in the capital market; it has greatly influenced every country’s section socially, politically and economically. Some of the significant benefits of the stock exchange are as follows;

BENEFITS FOR COMPANY AND ITS MANAGEMENT ACCESS TO CAPITAL:

- The prime objective of the stock exchange its to raise money for the listed corporation in the market; the stock exchange facilitates an easy rise in affordable capital to run business
- Stock exchange's easy marketability and liquidity ensure a quick and steady supply of capital to the business through provisioning the buying and selling of stocks and securities
- This forum also helps the companies to generate additional capital funds without any collateral.
- The stock exchange also facilitates better negotiation in issuing stocks and securities by providing fair pricing of the published stocks.

HIGH PROFILING AND ENHANCED VISIBILITY:

- Stock exchange benefits the stock listed company to gain higher status and reputation in the business marketplace by enjoying the confidence of the investing public
- It brings the company under the limelight and enhances its visibility in the public sphere, which helps fund capital and provides more significant support in increasing the market demand and supply.
- Stock exchange creates a continuous display of the listed company's name and profiles through marketing its stocks and securities on the stock exchange platform.

MORE CONTROL OVER THE MANAGEMENT

- A stock exchange facilitates the company to have more control over its management; by generating capital form the stock exchange, the company is protected from external control of its managerial affairs.

- Unnecessary interference of the financial institutions such as venture capitals, banks, and others who lend collateral loans are entirely avoided.

SAVINGS IN COST:

- High collateral value for bank loans and other capital funding are wholly avoided by listing stocks in the stock exchange. Its imposition of huge costs is saved through public issuing of capitals.
- The stock exchange allows companies to raise funds through the capital market instruments at a low cost compared to other loans.

ECONOMIC BENEFITS ENHANCE MARKET LIQUIDITY:

Liquidity refers to the degree to which an asset can be quickly bought or sold in the market at a price reflecting its intrinsic value. Stock exchange market's performance is measured with market liquidity, analyzing how well the country's stock market allows stocks and securities to be bought and sold at stable, transparent prices. One of the significant advantages of the stock exchange to the economy is that the stocks traded are liquid circulated into two market -issuers who indulge in continuous buying and selling, which is primary market and the investors to exchange stocks and investments by buying and selling the securities at any time, which is the secondary market.

WELL-REGULATED MARKET:

- Stock exchange assures securities' genuineness as the listing is made after a thorough analysis of a company's capital structure, the management pattern, and business prospect.
- Spread of stock exchanges operations geographically all over India all are regulated under one platform.
- Stock exchange abides by all government made laws, rules and regulations.
- It imposes fine, penalty and inquiry into any violations or fraudulent activities when orchestrated within the stock exchange market.

ONLINE TRADING - SPREADING GEOGRAPHICALLY:

Accessing a large pool of capital market investors through the computerized network is made possible by the recent stock exchange developments. Through a nationwide network for servicing of investors, companies listed on the stock exchange can have a large investor base spreading geographically, which boost economic growth at a global scale.

PUBLIC DEBT PLATFORM - LONG TERM BENEFITS:

- The stock exchange is also a supplier of long-term benefit schemes to the investors; it provides a public debt platform by trading government securities that produce a colossal financing resource to perform governmental activities.
- By executing public debts as government securities traded by Banks, Life Insurance Corporations, Provident funds, Pension to support governmental needs of the country's economic development, benefits economic growth.

INVESTOR BENEFIT HIGH RETURNS:

In stock exchanges, high returns are often supplied by long-term financial trends, where the price value of the stock occurs after some time but provide significantly high returns. This factor is one of the most promising benefits of the stock exchange to investors.

TRANSPARENCY:

A stock exchange facilitates transparency in managing the stock in the capital market;

- It evaluates the actual worth of securities and provides the intrinsic value of the company to avoid deceitful investments
- Safeguarding general public interest by ensuring equitable allotment, easy transfer, disclosure of proper information, etc.,
- Assures the existence of good faith or an absence of fraud concerning the issue of securities.
- Providing activities of quick transfer registration and corporate information

SAFETY IN INVESTING:

- Stock exchanges' seamless physical and electronic trading platforms perform to ensure complete safety and security to the market participants.
- Its mechanism offers more excellent protection to investors by adequately investigating the company and the projects before listing and marketing its stocks to the

capital market.

- Its fundamental function of handling stocks and securities are governed under proper rules and regulations and is abided by the stock exchange to ensure protected trading
- All the fraudulent activities will be duly enquired and sanctioned.

TAX DEFERMENTS:

Investors have the advantage of deferring from paying tax for the invested stock; there is no need to include the trading in assessment for the purchased stocks when filing tax returns.

ACCESSIBILITY:

- Since the stock exchange is a growing market and is dynamic; it creates new opportunities and serves people; it has been designed as a single-window trading platform accessible to many people throughout the country and worldwide.
- Buying and selling may be resorted to from any part of the world through online trading platforms
- It facilitates faster deal settlement for investors across the counters spread over the entire county.

OTHER BENEFITS

- The interconnected network of the stock exchange, which the country creates, facilitates financial operations by integrating the entire capital market under one roof.
- Boon to closely-held companies whose stocks are held by a small number of people, these corporations are encouraged to go public because the stocks can be listed even if only 40 per cent of public capital (now a minimum of 20 per cent in case of closely-held and new companies) is offered for public trading.
- Facilitates wider dispersal of economic activities by encouraging small companies and small investors to participate in stock exchanges to expand and diversify their businesses
- Promoting over-all stimulation to venture capital activities there-by promoting entrepreneurship.

BOMBAY STOCK EXCHANGE ORGIN:

BSE was first diagnosed in 1986 in Great Britain. Since that time, more than 190,000 cases have been confirmed world-wide. The number of cases peaked in 1992, and has declined continuously since that time, with only 29 cases worldwide in 2011. Shri Ashishkumar Chauhan is the MD & CEO of BSE (Bombay Stock Exchange), the first stock exchange of Asia. He is one of the founders of India's National Stock Exchange ("NSE") where he worked from 1992 to 2000.

MEANING:

The Bombay Stock Exchange (BSE) is the first and largest securities market in India and was established in 1875 as the Native Share and Stock Brokers' Association. Based in Mumbai, India, the BSE lists close to 6,000 companies and is one of the largest exchanges in the world, along with the New York Stock Exchange (NYSE), NASDAQ, London Stock Exchange Group, Japan Exchange Group, and Shanghai Stock Exchange.

The BSE has helped develop India's capital markets, including the retail debt market, and has helped grow the Indian corporate sector. The BSE is Asia's first stock exchange and also includes an equities trading platform for small-and-medium enterprises (SME). BSE has diversified into providing other capital market services including clearing, settlement, and risk management.

Functions of BSE

- The price determination in the secondary market depends upon the demand and supply of the securities. Bombay Stock Exchange helps in the process of valuation by constantly valuing all the listed securities.
- They provide high liquidity.

OTHER MAJOR INTERNATIONAL STOCK EXCHANGES:

In addition to the Bombay Stock Exchange (BSE), other major international stock exchanges include:

- **The New York Stock Exchange (NYSE)**

The New York Stock Exchange (NYSE) is considered the largest equities-based exchange in the world, based on the total market capitalization of its listed securities. NYSE was formerly a private organization but became public in 2005 after it acquired the electronic trading exchange Archipelago.

NASDAQ:

NASDAQ is a global electronic marketplace and the benchmark index for U.S. technology stocks. National Association of Securities Dealers (NASD) created NASDAQ in 1971 to enable investors to trade securities on a rapid, computerized, and transparent system. Today “Nasdaq” also refers to the Nasdaq Composite, an index of more than 3,000 listed technology companies including Apple, Google, Microsoft, Oracle, Amazon, Intel, and Amgen.

London Stock Exchange (LSE):

The London Stock Exchange (LSE) is the primary U.K. stock exchange and largest in Europe. The LSE developed after several regional exchanges merged in 1973. LSE was first called the Stock Exchange of Great Britain and Ireland. One hundred of the top blue chips on the LSE form the Financial Times Stock Exchange (FTSE) 100 Share Index or "Footsie." Other major international stock exchanges in Asia include the Tokyo Stock Exchange (TSE) and the Shanghai Stock Exchange.

NATIONAL STOCK EXCHANGE - ORGIN:

National Stock Exchange of India Limited (NSE) is the leading stock exchange of India, located in Mumbai, Maharashtra. It is under the ownership of diversified group of Financial Institutions, Banks, and Insurance companies. NSE was established in 1992 as the first dematerialized electronic exchange in the country. NSE was the first exchange in the country to provide a modern, fully automated screen-based electronic trading system that offered easy trading facilities to investors spread across the length and breadth of the country. Vikram Limaye is Managing Director & Chief Executive Officer of NSE.

MEANING:

The National Stock Exchange (NSE) is a stock exchange in India It allows for new listings, initial public offers (IPOs), debt issuances and Indian Depository Receipts (IDRs) by overseas companies raising capital in India. S&P CNX Nifty is the benchmark index introduced by NSE.

The National Stock Exchange of India Limited (NSE) is a financial exchange in India that provides automated trading facilities across the nation. NSE trading is driven by market orders, and the buyers and sellers remain anonymous.

The NSE offers trading and investment in debt, equity, equity derivatives, mutual funds, IPOs, currencies, and exchange traded funds (ETFs).

FUNCTIONS:

- To establish a trading facility for debt, equity, and other asset classes accessible to investors across the nation.
- To act as a communication network providing investors an equal opportunity to participate in the trading system.
- To meet the global standards set for financial exchange markets.
- To provide a shorter trade settlement period and enable the book-entry settlement system.

Benefits of the NSE:

- Investors can get trade and post-trade information through the NSE trading system. They can see the top sell orders and buy orders, as well as the number of securities available for transactions.
- The trading expenses of investors are reduced as the impact cost on the trading activity decreases owing to the volume of the trading activity.
- The trading system of the NSE processes the transaction at a pace that allows the investors to get the best prices.
- The NSE provides monthly trade statistics to the listed companies. The companies can utilize the data to track their performance.
- The electronic system of trading provides investors with a transparent and effective exchange market.

SENSEX:

The term Sensex is a portmanteau of Sensitive and Index. The Sensex is an index that reflects the Bombay Stock Exchange (BSE). The Sensex Index comprises 30 stocks on BSE. These stocks are the largest and most actively traded stocks on the BSE.

The criteria for selecting stocks are as follows:

- It should be a large to mega-cap stock.
- Relatively liquid stocks
- Revenue generated from core activities

A diversified and balanced sector involvement in line with the Indian equity market. The Sensex reflects the movements in the Indian stock market. If the Sensex increases, it means the prices of the underlying 30 stocks have increased. If the Sensex has decreased, it means the prices of the underlying 30 stocks have decreased. The Sensex is the oldest index in India, and people consider it to be a reflection of the Indian economy. Market research analysts refer to the Sensex to understand the overall growth, development in industry, country's stock market trend.

NIFTY:

Just like the Sensex, Nifty is also an index. Nifty reflects the National Stock Exchange. The name Nifty comes from the combination of National and Fifty. The Nifty 50 also is a benchmark index, and it comprises the top 50 stocks traded on the National Stock Exchange NSE. The selection of the top 50 stocks is from 12 different sectors, including information technology, financial services, consumer goods, telecommunications, automobiles, etc.

To be part of Nifty 50, the companies require to meet the following parameters and criteria:

- **Liquidity:** Over the last six months, the stock should have been traded at an average cost of 0.50% or less.
- **Float Adjustment:** the Company's float-adjusted market capitalization has to be at least twice the current smallest index composition.
- **Domicile:** The company should be listed on the NSE and be an Indian company.

QUESTION BANK

PART – A

S. No	Questions	CO	Level
1	“Primary market is of great significance to the economy.” Comment.	CO2	L1
2	Distinguish between primary market and secondary market.	CO2	L2
3	Are you aware of the term ‘securities’ and ‘securities markets’?	CO2	L3
4	Give a comparative view of various types of preference shares prevalent in the market.	CO2	L2
5	Discuss about SENSEX.	CO2	L2
6	Recall a note on various methods of raising funds by a company from the primary market.	CO2	L3
7	Do you know what ‘rights issue of shares’ is? Explain.	CO2	L3
8	State the objectives of the NSE.	CO2	L3
9	Tell about on what basis companies do issue shares to the public.	CO2	L4
10	Explain the role of the new issue market.	CO2	L3

PART – B

S. NO	Questions	CO	Level
1	Can the company also raise capital through a right issue? Why or why not? Give a reason to justify your answer.	CO2	L4
2	Explain the various segments of the NSE.	CO2	L4
3	“Primary market is of great significance to the economy.” Comment.	CO2	L3
4	Explain briefly: Surveillance at BSE.	CO2	L5
5	“A company can raise funds from the primary market through different methods, different types of issues and by means of the offer document and red herring prospectus.” Enumerate.	CO2	L5
6	Explain the structure of Indian securities markets?	CO2	L4

7	Briefly describe the Nasdaq stock market.	CO2	L5
8	Enumerate concepts related to the primary market.	CO2	L4
9	Describe how to apply through an initial public offering IPO.	CO2	L5
10	Collect data about the movements in SENSEX and NIFTY during the last one month. Find out whether the two move in same or opposite direction.	CO2	L6

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SCHOOL OF MANAGEMENT STUDIES

UNIT – III – CAPITAL MARKETS – SBAA3003

Listing of securities – process – trading mechanism-Block and Bulk deals - steps in buying and selling securities – Trading in dematerialized securities - Depository system – Depositories in India.

LISTING - MEANING

The inclusion of the name of a company in the official list of securities, which can be dealt with in a stock exchange, is called listing. It implies the securities of a company to the trading privileges on a stock exchange.

By getting its securities listed, a company can create a favorable impression in the mind of the investors about its financial soundness, profitability and the marketability of its shares and other securities. At the same time, it should also be remembered that listing would no way guarantee the earning capacity of the securities of the issuing company.

Moreover, in India, the Central Government is also empowered under Sec. 21 of the Securities Contracts (Regulation) Act to compel a public limited company to get its securities listed on any recognized stock exchange, with a view to protect the broad interests of the investing public. Any company, which wants to get its shares listed, should apply to regional stock exchange i.e. to the stock exchange nearest to its registered office. It may also get its shares listed on other stock exchanges as well.

OBJECTIVES OF LISTING

According to S. C. Kuchhal, the main objectives of listing are the following:

1. Provision of ready marketability.
2. Imparting liquidity to the securities.
3. Provision of free negotiability.
4. Protection of the interests of the investors and the general public.

LISTING OF SECURITIES - CONCEPT

For trading in the stock market, a company has to list its securities in the stock exchange. It means that the name of the company is registered in the stock exchange. The company has to fulfill certain conditions according to Companies Act. The company has to offer its shares or debentures to the public for subscription. Only then, the company will be allowed to list its security in the stock exchange. For listing shares in the stock exchange, a company must have minimum of Rs. 5 crores as its equity capital and 60% of this i.e., Rs. 3 crores is offered to the public.

CONDITIONS FOR LISTING

Before listing securities, a company has to fulfill the following conditions:

1. Shares of the company must be offered to the public through a prospectus and 25% of each class of securities must be offered.

2. The prospectus should clearly mention opening of subscription, receipt of application, etc.

3. The capital structure of the company should be broad-based and there should-be public interest in securities.

4. The minimum issued capital must be Rs. 3 crores of which Rs. 1.80 crores must be offered to the public.

5. There must be at least five public shareholders for every Rs. 1 lakh of fresh issue of capital and 10 shareholders for every Rs. 1 lakh of offer for sale of existing capital. On the excess application money, the company will have to pay interest from 4% to 15%, if there is delay in refund and delay should not be more than 10 weeks from the date of closure of subscription list.

6. A company with paid up capital of more than Rs. 5 crores should get itself listed in more than one stock exchange, it includes the compulsory listing on regional stock exchange.

7. The auditor or secretary of the company applying for listing should declare that the share certificates have been stamped so that shares belonging to the promoter's quota cannot be sold or hypothecated or transferred for a period of 5 years.

8. Articles of Association of the company must have the following provisions:

- A common form of transfer shall be used
- Fully paid shares shall be used
- No lien on fully paid shares
- Calls paid in advance will not carry a right to dividend and will not be forfeited before the claim becomes time-barred.
- Option to call off shares shall be given only after sanction by the general meeting.

9. Letter of allotment, Letter of regret and letter of rights shall be issued simu1taneously.

10. Receipts for all the securities deposited, whether for registration or split and no charges will be made for the services.

11. The company will issue consolidation and renewal certificates for split certificate, letter of allotment, letter of rights and transfer, etc. when required.

12. The stock exchange should be notified by the company regarding the date of board meeting, change in the composition of board of directors, and any new issue of securities, in place of reissue of forfeited shares.

13. Closing the transfer books for the purpose of declaration of dividend, rights issue or bonus issue. And for this purpose, due notice should be given to stock exchange.

14. Annual return of the company to be filed soon after the annual general body meeting.

15. The company will have to comply with conditions imposed by the stock exchange now and then for 1istmg of security.

TYPES OF LISTING OF SECURITIES

1. **Initial listing**: Here, the shares of the company are listed for the first time on a stock exchange.
2. **Listing for public Issue**: When a company which has listed its shares on a stock exchange comes out with a public issue.
3. **Listing for Rights Issue**: When the company which has already listed its shares in the stock exchange issues securities to the existing shareholders on rights basis.
4. **Listing of Bonus shares**: When a listed company in a stock exchange is capitalizing its profit by issuing bonus shares to the existing shareholders.
5. **Listing for merger or amalgamation**: When the amalgamated company issues new shares to the shareholders of amalgamated company, such shares are listed.

PROCEDURE FOR LISTING REQUIREMENTS

For listing the shares in the stock exchange, the public limited company will have to submit supporting documents. They are:

1. Certified copies of Memorandum, Articles of Association, prospectus and agreements with Underwriters.

2. All particulars regarding capital structure.

3. Copies of advertisements offering securities for sale during the last 5 years.

4. Copies of Balance sheet, audited accounts and auditors' report for the last 5 years.

5. Specimen copies of shares and debentures, certificate letter of allotment, and letter of regret.

6. A brief history of the company since incorporation with any changes in capital structure, borrowings, etc.

7. Details of shares and debentures issued for consideration other than cash.

8. Statement showing distribution of shares and particulars of commission, brokerage, discounts or special terms towards the issue of shares.

9. Any agreement with financial institutions.

10. Particulars of shares forfeited.

11. Details of shares or debentures for which permission to deal with is applied for.

12. Certified copy of consent from SEBI.

PROCEDURE AT THE STOCK EXCHANGE

After the application is made the Listing Committee of the stock exchange will scrutinize the application form of the company. Here, the stock exchange will ensure the following—

1. The financial position of the company is sound

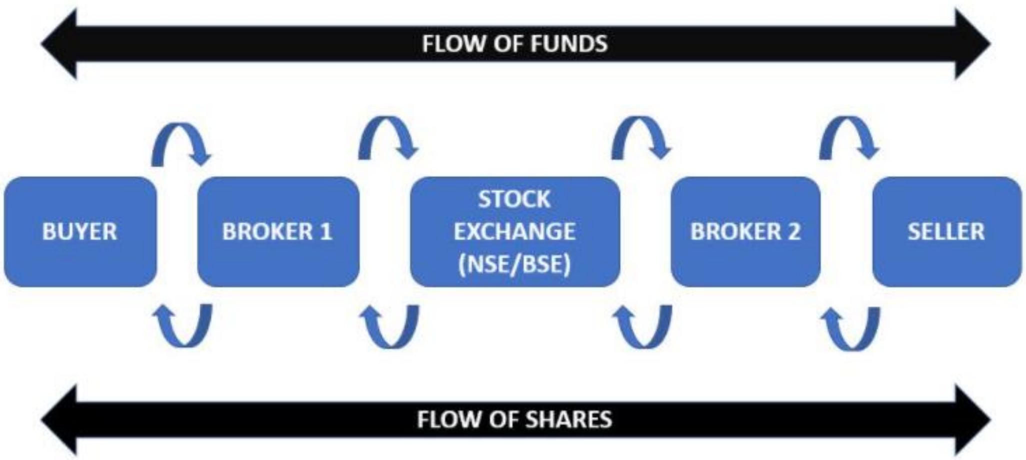
2. Solvency and liquidity positions are good

3. The issue is large and broad based to generate public interest. If the application for listing is accepted, the listed company will be called to execute listing agreement with the stock exchange. The company must follow certain obligations which are:

- The company will treat all the applications with equal fairness.
- in case of over subscription, the allotment will be decided in consultation with stock exchanges; and
- The company will notify to the stock exchange any change in its management, business, and capital structure or bonus or rights issue of shares.

THE TRADING PROCEDURE ON A STOCK EXCHANGE

Before selling the securities through stock exchange, the companies have to get their securities listed in the stock exchange. The name of the company is included in listed securities only when stock exchange authorities are satisfied with the financial soundness and other aspects of the company.



Previously the buying and selling of securities was done in trading floor of stock exchange; today it is executed through computer and it involves the following steps:

The Trading procedure involves the following steps:

1. Selection of a broker:

The buying and selling of securities can only be done through SEBI registered brokers who are members of the Stock Exchange. The broker can be an individual, partnership firms or corporate bodies. So the first step is to select a broker who will buy/sell securities on behalf of the investor or speculator.

2. Opening Demat Account with Depository:

Demat (Dematerialized) account refer to an account which an Indian citizen must open with the depository participant (banks or stock brokers) to trade in listed securities in electronic form. Second step in trading procedure is to open a Demat account.

The securities are held in the electronic form by a depository. Depository is an institution or an organization which holds securities (e.g. Shares, Debentures, Bonds, Mutual (Funds, etc.) At present in India there are two depositories: NSDL (National Securities Depository Ltd.) and CDSL (Central Depository Services Ltd.) There is no direct contact between depository and investor. Depository interacts with investors through depository participants only. Depository participant will maintain securities account balances of investor and intimate investor about the status of their holdings from time to time.

3. Placing the Order:

After opening the Demat Account, the investor can place the order. The order can be placed to the broker either (DP) personally or through phone, email, etc.

Investor must place the order very clearly specifying the range of price at which securities can be bought or sold. e.g. "Buy 100 equity shares of Reliance for not more than Rs 500 per share."

4. Executing the Order:

As per the Instructions of the investor, the broker executes the order i.e. he buys or sells the securities. Broker prepares a contract note for the order executed. The contract note contains the name and the price of securities, name of parties and brokerage (commission) charged by him. Contract note is signed by the broker.

5. Settlement:

This means actual transfer of securities. This is the last stage in the trading of securities done by the broker on behalf of their clients. There can be two types of settlement.

(a) On the spot settlement:

It means settlement is done immediately and on spot settlement follows. T + 2 rolling settlement. This means any trade taking place on Monday gets settled by Wednesday.

(b) Forward settlement:

It means settlement will take place on some future date. It can be T + 5 or T + 7, etc. All trading in stock exchanges takes place between 9.55 am and 3.30 pm. Monday to Friday.

UNDERSTANDING BULK DEALS AND BLOCK DEALS - CONCEPT

A bulk deal is a deal where the total quantity of shares bought or sold is greater than 0.5% of the share capital of the company. A bulk deal can be transacted either through the normal trading window or through the block trading window. Quite often, when a large FII or mutual fund or an HNI wants to buy a large block of shares in a particular stock, they prefer to use sliced trades through the day. This ensures that they get the best advantage of the volatility in the market and are able to reduce their overall cost of acquisition. Similarly in case of bulk selling also, the sliced approach helps them get a better selling price. Bulk deals have to be reported to the exchange by the broker executing the trade. In case the bulk deal (exceeding 0.5% of the share capital) is executed through the block window then the trade has to be reported immediately to the exchange. In case of a sliced order through the day; if the total purchase or sale exceeds 0.5% of the share capital then the bulk deal has to be reported to the exchange within 1 hour of close of trade.

Block deals, on the other hand, are block execution of a minimum of 5 lakh shares or value of Rs.5 crore. The block deal window is open for a period of 35 minutes after trading opens and any block trading executing on this window has to be reported to the exchange immediately by the broker and such a trade cannot be squared off intraday. HNIs, FIIs and mutual funds use the block window to execute large trades without the markets getting a whiff of it or even impacting the price. That brings us back to the key question; what is the effect of a bulk deal on the share price. Here are 3 important takeaways;

1. **Bulk deals are indicative of concentration of interest:** This can be looked at as a signal of building interest in a particular stock. Normally, bulk deals tend to be indicative of a sudden spurt in interest from informed investors. If you take the directional bulk deals on the NSE and BSE over a period of time and see the impact on stock price, it is quite evident that where there is concentration of interest from informed institutions, there is a positive impact on prices. The reverse holds in case of consistent selling. A word of caution is warranted here. Many smart investors skirt the bulk deal reporting by executing slightly lower than the 0.5% mark. So don't take the bulk deals data as entirely indicative.

2. **Separate the intraday trades and the bulk transfers:** Out of the bulk deals data, you need to separate the non-directional data. The first set of such data is the intraday trades' data and the short term trade data. These are proprietary books and large investors just trying to ride onto a trend for short term profits. They do not indicate anything. The second set of such data is the bulk transfers among institutions. You get to see large positions in the bulk deals segment that is nothing but FIIs, MFs, large HNIs and promoters actually shifting ownership around. Thirdly, be

cautious if the bulk deals are from arbitrage funds or if the bulk deals are backed by heavy shorting in futures. That is most likely an arbitrage position and not a directional indication.

3. **Focus on bulk deal trends over a period of time:** This is possibly the most important take-away from the bulk deals data. Ideally, take the consolidated bulk deals data for a period of 2 year and try to sort it based on the stock and the date. That will give you a clear idea of how the stock prices have moved in conjunction with the bulk deals. It will also give you an idea of which traders and investors are typically the most adept at catching on to trends as evidenced by future movement in prices. When you combine these factors, the bulk deals actually become meaningful and actionable from a stock selection perspective.

PROCEDURE FOR PURCHASE AND SALE OF SECURITIES IN A STOCK EXCHANGE

Selection of broker: – The first step is to select a broker who will buy/sell securities on behalf of the investor. This is compulsory because trading of securities can only be done through SEBI registered brokers who are the members of a stock exchange. Brokers may be individuals, partnership firms or corporate bodies. The investor has to assign a broker-client agreement and a client registration form before placing an order to buy or sell securities. He has also to provide certain other details and information. These include:

- PAN number (This is mandatory)
- Date of Birth and Address
- Educational qualification and Occupation
- Bank account details
- Depository account details
- Name of any other broker with whom registered.
- Client code number in the client registration form.

The broker then opens a trading account with the name of the investor.

Opening Demat account: – The investor has to open a Demat account or beneficial owner (BO) account with a depository participant for holding and transferring securities in the Demat form. He will also have to open a a bank account for cash transactions in the securities market.

Placing the order:- The investor then places an order with the broker to buy or sell shares. Clear instructions have to be given about the number of shares and the price at which the shares should be bought or sold. An order confirmation slip is issued to the investor by the broker.

Executing the order:- The broker then will go on-line and connect to the main stock exchange and match the share and best price available. When the shares can be bought or sold at the price mentioned, it will be communicated to the broker's terminal and the order will be executed electronically. After the trade has been executed, the broker issues a Contract Note within 24 hours. This note contains details of the number of shares bought or sold, the price, the date and time of deal, and the brokerage charges. This is a valuable document as it is legally enforceable and helps to settle disputes/claims between the investor and the broker. A Unique Order Code number is assigned to each transaction by the stock exchange and is printed on the contract note.

Settlement:- Now, the investor has to deliver the shares sold or pay cash for the shares bought. This should be done immediately after receiving the contract note or before the day when the broker shall make payment or delivery of shares to the exchange. This is called the pay-in-day. Then the broker has to make payment to the investor within 24 hours of the payout day since he has already received payment from exchange. The broker will make delivery of shares in Demat form directly to the investor's Demat account.

WHAT IS DEMATERIALISATION OF SECURITIES

Dematerialization offers flexibility along with security and convenience. Holding share certificates in physical format carried risks like certificate forgeries, loss of important share certificates, and consequent delays in certificate transfers. Dematerialization eliminates these hassles by allowing customers to convert their physical certificates into electronic format.

Dematerialization is a process through which physical securities such as share certificates and other documents are converted into electronic format and held in a Demat Account. Click here to open free Demat Account.

A depository is responsible for holding the securities of a shareholder in electronic form. These securities could be in the form of bonds, government securities, and mutual fund units, which are held by a registered Depository Participant (DP). A DP is an agent of the depository providing depository services to traders and investors.

Process of dematerialization

- Dematerialization starts with opening a Demat account. For Demat account opening, you need to shortlist a Depository Participant (DP) that offers Demat services
- To convert the physical shares into electronic/Demat form, A Dematerialization Request Form (DRF), which is available with the Depository Participant (DP), has to be filled in and deposited along with share certificates. On each share certificate, 'Surrendered for Dematerialization' needs to be mentioned
- The DP needs to process this request along with the share certificates to the company and simultaneously to registrars and transfer agents through the depository
- Once the request is approved, the share certificates in the physical form will be destroyed and a confirmation of dematerialization will be sent to the depository
- The depository will then confirm the dematerialization of shares to the DP. Once this is done, a credit in the holding of shares will reflect in the investor's account electronically
- This cycle takes about 15 to 30 days from the submission of dematerialization request
- Dematerialization is possible only with a Demat account, therefore it is essential to learn how to open a Demat account to understand dematerialization

PURCHASING DEMATERIALIZED SECURITIES:

Step 1: Choose a broker who can facilitate the purchase of the securities

Step 2: Make a payment to the broker who will then arrange for the payment to the clearing corporation on the pay-in day

Step 3: The securities are credited to the broker's clearing account on the pay-out day

Step 4: The broker will give instructions to its Depository Participant (DP) to debit the clearing account and credit the same to your account

Step 5: The depository will then confirm the dematerialization of shares to the DP. Once this is done, a credit in the holding of shares will reflect in the investor's account electronically.

Step 6: You will receive shares into your account. In order to receive the credit, you will need to give 'Receipt Instructions' to the DP if you did not give standing instructions during the opening of your account

SELLING DEMATERIALIZED SECURITIES:

Step 1: Choose a broker and sell the securities in a stock exchange linked to the NSDL (National Securities Depository Limited)

Step 2: The Depository Participant (DP) needs to be instructed to debit your account with the number of securities sold and credit the broker's clearing account

Step 3: You need to send the delivery instruction to your Depository Participant (DP) using the delivery instruction slips

Step 4: Once the request is approved, the share certificates in the physical form will be destroyed and a confirmation of dematerialization will be sent to the depository

Step 5: The broker will give instructions to its DP for delivery to the clearing corporation before the pay-in day

Step 6: You will receive the payment from the broker for the sale of your securities

WHY WAS DEMATERIALIZATION NEEDED?

- Handling of paperwork related to shares in the physical format often led to errors and unforeseen mishaps in the past
- Tracking records and share documents with respect to transfer and upkeep transactions was difficult
- The authorities in charge of updating these documents could not keep up with the increasing volume of share papers, which, if left unchecked, could cripple the financial base of the Indian share market and associated businesses

BENEFITS OF DEMATERIALIZATION

There is a wide range of benefits of dematerialization of securities. Some of them are as follows:

- You can conveniently manage your shares and transactions from anywhere
- Stamp duty is not levied on your electronic securities
- Holding charges levied are nominal
- Risks involved with physical securities such as theft, loss, forgery or damage are eliminated
- You can buy securities in odd lots and buy a single security
- Due to the elimination of paperwork, the time required for completing a transaction gets reduced

Dematerialization means converting physical share certificates into their electronic forms. It is an important milestone for the Indian equity market. It helped it to embrace digitization and made the entire trading process smooth, glitch-free, and secure. Besides, it is,

- Convenient
- Safe
- Efficient
- Paperless, and
- Multipurpose

WHY WAS DEPOSITORY SYSTEM INTRODUCED?

Companies turn towards the capital market to meet their capital requirements, because capital market is considered to be a major, flexible and responsive source of funds. Today, investors hold plenty of paper or marketable financial assets or securities. These financial assets are represented in the form of paper certificates.

As numerous securities are bought and sold, the stock brokers have to deliver a large number of paper certificates on behalf of their clients. During such a process, each share transfer deed is subject to different manual checks. However, due to some technical defects in the transfer deed, many share transfers are rejected.

Consequently, investors who have transferred their shares would experience inordinate delay in receiving their money. To overcome all these problems, depository system has been introduced. The use of electronic system while transferring shares is an important aspect of this system

MEANING AND DEFINITION OF A DEPOSITORY

Meaning of Depository

A **depository is an organization** where the securities of a shareholder are held in the electronic form at the request of the shareholder through the medium of a **depository participant**.

A depository is like a bank for securities. If an investor wishes to avail the services offered by a depository, he/she has to open an account with the depository, through a depository participant. This is very similar to opening of an account with any of the branches of a bank so as to utilize the services of that bank. The depository can legally transfer the beneficial ownership of securities.

Definition of depository

The term depository can be defined as follows:

- As a central location for keeping securities on deposit.
- As a facility for holding securities either in certificated or uncertificated form to enable book entry transfer of securities.
- As an institution which transfers the ownership of securities in electronic form on behalf of its members.

OBJECTIVES OF A DEPOSITORY

The introduction of depository system will result in the elimination of all the problems connected with ownership, trading and transfer of securities. It plays a crucial role in Indian capital market. Depository system enables the capital market to achieve the following objectives:

1. It eliminates the occurrence of bad deliveries, forgery and duplicates share certificates.
2. It avoids delay in transfer of securities.
3. It enhances liquidity of securities by facilitating their easy transfer.
4. It substantially reduces the cost of transactions for the investor.

5. It enables surrender and withdrawal of securities from it with ease.

6. It maintains an accurate record of investors' holdings by keeping the details in electronic form.

7. It attracts foreign investors by complying with global standards.

8. It provides service infrastructure in a capital market.

INSTITUTIONS INVOLVED IN DEPOSITORY PROCESS

To have a better understanding of **depository process**, it is essential to study the institutions interacting in a depository system.

1. **Central depository**: The central depository keeps securities on behalf of the investor and maintains records in electronic form. The statement given by the depository is the evidence of the ownership of shares.
2. **Share registrar and transfer agent**: The 'registrar' is an institution which controls the issuance of securities. The transfer agent retains the names and addresses of the owners of registered securities.
3. **Clearing house**: The depository interacts with the clearing house during the share transfer process. When the clearing house confirms that all funds have been received, the depository will then transfer securities from the delivering person to the receiver.

PROCESS INVOLVED IN DEPOSITORY SYSTEM

Having understood the role played by the interacting institutions, the depository processes may further be explained as follows:

Under the provisions of **Depository Ordinance**, depositories facilitate scrip-less trading in capital market through dematerialization of securities. Equity shares, debentures, warrants, bonds, units of mutual funds, venture capital funds, commercial paper, certificates of deposit, secured debt, money market instruments and unlisted securities are eligible to be admitted to the depository for dematerialization.

A depository holds all the securities in the electronic form. It can be regarded as a 'Bank' for securities. It converts physical securities into book entry securities, the process of which is called dematerialization. In this process, certificates in physical form are eliminated altogether. When an investor deposits his physical securities with the depository, his account with the depository is credited for the deposit made. The transfer is affected electronically whenever he buys and sells his shares and his account is credited or debited accordingly.

The institution which acts as a depository is the registered owner of the shares and the members owning the shares in a company will be beneficial owners. A beneficial owner is entitled to all the benefits like dividend, right shares, bonus shares and the voting rights.

A depository interacts with the investors with the help of a depository participant. He is similar to the broker who trades on behalf of the customers in the stock exchanges. As per the SEBI guidelines, financial institutions, banks, custodians, stock brokers etc., can become participants in the depository system.

According to the Depository Ordinance, the holder of securities has an option, whether to remain in **non-depository mode** or shift to **depository mode**. Investors who wish to remain in non-depository mode will hold the physical possession of certificate of securities. On the other hand, the investors who opt to hold securities in depository mode shall open an account with a depository participant. The investor who has opened such an account gets an identification number which he will refer to in all his transactions.

DEPOSITORY SYSTEM IN INDIA

In April 1996 the Governing Board of SEBI approved the draft of SEBI (Depositories and Participants) Regulations 1996. The Securities and Exchange Board of India notified these regulations on May 16, 1996. The government of India in 1996 introduced in Lok Sabha the Depository Bill to usher in scrip less trading and avoid "bad delivery, theft and forgery in share transfer and settlement".

National Securities Depositories Ltd. (NSDL) promoted by Industrial Development Bank of India, Unit Trust of India and National Stock Exchange emerged as the first depository to be registered in India. There was a great debate on central-versus multiple depository system. Ultimately multiple depository system became a choice. Considering the sheer size of the network that would have to be established, a single organisation may not be able to handle it. To have competition, multiple depositories are a must. Subsequently, another depository emerged on Indian scene i.e. Central Depository Services Limited (CDSL). It received a certificate of commencement of business from SEBI on February 8, 1999. CDSL was set up with the objective of providing convenient, dependable and secure depository services at affordable cost to all market participants. All leading stock exchanges like the National Stock Exchange, Calcutta Stock Exchange, Delhi Stock Exchange, The Stock Exchange, Ahmadabad, etc have established connectivity with CDSL.

29th November, 1996 was a red letter day for Indian capital market as in more than 100 year history of stock exchanges in India, for the first time National Stock Exchange witnessed trade in dematerialized scrips of an Indian Company i.e. 'Reliance Industries'. The very first lot of transaction was, as expected, at premium in comparison to prevailing price for physical delivery due to inherent qualities of quick settlement. Clean deliveries and exemptions from stamp duty. To make the system operational on large scale, Government of India promulgated an ordinance to amend the Depository Act to enable the shares of statutory bodies such as IDBI. SBI, UTI and other public sector banks and the units of mutual funds to transact through depositories.

The changes in last few years in mechanism of capital market have made market more efficient. About 99% of settlements are through depositories. Besides overcoming the problems of bad deliveries, paper deliveries etc. this system has cut down the time taken in settlement. Indian market now has attained T+3 settlements effectively and efficiently through NSDL and CDSL some of the important statistics about depositories in India at present (May 2004) is as under:

Features	NSDL	CDSL
DPs (no.)	216	220
Investors (Iakhs)	53.53	6.71
Demat (qty- Crores)	8672	1428
Demat (Value Rs- Cr)	912812	103338
No. of Co.s (equity)	5311	4837

(**Source:** NSDL and CDSL)

WORKING OF NATIONAL SECURITIES DEPOSITORY LIMITED (NSDL) DEPOSITORIES:

NSDL is the first depository in India till now registered with SEBI in June 1996. It has been promoted jointly by lDBI, UTI and NSE. NSDL operates through a network of DPs who interact with investors. However, as required by the Depositories Act, NSDL is responsible to every individual investor holding an account with the depository. It operates on a two-tier structure, wherein it maintains the accounts of the DPs, who in turn maintain the clients' accounts. The online software provided by NSDL to the DPs give an access to each account maintained by depository participants so that their functioning can be monitored and controlled. NSDL also maintains online connectively with the registrars and transfer agents (R& T) of the securities and perform a daily reconciliation of all the account balances to ensure that the number of securities issued and dematerialized in the depository tallies. NSDL operates through DPs to perform the relevant functions which are as under:

- Getting withdrawal and surrender of securities from and to the depository.
- Maintain investor holding in electronic form.
- Effect settlement of securities traded on the exchanges.
- Carry out settlement of trades not done on the stock exchanges, i.e. off market trades. In the operations of NSDL besides DPs there is another organisation called as National Securities Clearing Corporation Ltd. (NSCCL). It is responsible for the clearing and settlement system for its clearing members (CM) and investors to settle the trades in the depository section. **The procedure is as under:**

i) The cycle of delivering and receiving securities in this market segment broadly remains similar to the existing cycle for physical securities, that is, from Wednesday to Tuesday with the exception that pay-in and payout of both securities and funds are affected on the same day, that is Tuesday.

ii) In the physical segment, today, a seller delivers paper securities to his CM who in turn, pays in such securities in the clearing house in the depository segment, the seller is required to instruct his DP to transfer securities from his account with the DP to the CM's pool account with the DP.

iii) On or before the time specified for the pay- in by NSCCL, the CM instructs its DP to move the required balance from its pool account to its delivery account.

iv) The NSDL then moves the balances from CM's delivery accounts to NSCCL settlement account within the depository as per schedule set up for the pay in of depository securities.

v) Payout is received from NSCCL into the CM's account from where the CM instructs his DP to distribute the securities to the buyers. NSDL also provides stock lending and borrowing facilities to the investors, subject to the regulations on lending and borrowing. The investor can also receive his corporate benefits through NSDL.

The disbursement of cash benefits such as dividend/interest will be done by the registrar whereas the distribution of securities entitlements will be done by the depository based on the information provided by the registrar. Depositories in India are regulated by Depository Act 1996 and to facilitate operations of the said Act SEBI (Depositories & Participants) Regulations 1996 were issued. It is a general feeling that depository service has added to the efficiency of capital market in India.

QUESTION BANK

PART – A

S. No	Questions	CO	Level
1	Explain about debt securities.	CO3	L2
2	Depository participant provides a link between the company and investors. Comment.	CO3	L4
3	Give the meaning of ‘dematerialization’. State any two of its advantages.	CO3	L4
4	Write short note on Bulk deal.	CO3	L3
5	Discuss the procedure for settlement of securities under rolling settlement.	CO3	L2
6	IDR and GDR have distinct features. Comment.	CO3	L2
7	Explain block deal and how is it being executed in the stock exchange.	CO3	L3
8	State the circumstances under which SEBI may pass cease and desist orders in respect of any listed company.	CO3	L3
9	Explain the term: Depository Participants.	CO3	L2
10	Recall what you understand by the dematerialization of securities.	CO3	L4

PART – B

S. NO	Questions	CO	Level
1	Listing of securities with stock exchange is a matter of great importance for companies and investors'. Discuss.	CO3	L5
2	Investment in Indian depository receipts (IDRs) is an opportunity for Indian investors to invest funds in foreign equity.	CO3	L4
3	Discuss the framework for securities lending and borrowing.	CO3	L4
4	The debt market in India comprises mainly of two segments viz., the Government securities market and the Corporate securities market – Discuss.	CO3	L4
5	Explain the meaning of the following in the context of the international capital market: Global Depository Receipts.	CO3	L5
6	What do you understand by "Application Supported by Blocked Amount" (ASBA)? How does it work in Initial Public Offer (IPO)? Describe.	CO3	L5
7	Briefly outline the concept of Depository system in India.	CO3	L5
8	Explain the term 'Demat'. State the benefits of Demat securities.	CO3	L4
9	The depository system functions very much like the banking system. Comment.	CO3	L5
10	Enumerate the key features of depository system in India?	CO3	L6

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SCHOOL OF MANAGEMENT STUDIES

UNIT – IV – CAPITAL MARKETS – SBAA3003

Role and functions: Merchant Bankers, Stock Brokers, Syndicate members, Registrars and transfer Agents, underwriters, bankers to an issue, Portfolio managers, Debenture trustees, Investment advisers, Research analysts, market makers, credit rating agencies.

INTRODUCTION TO SECURITIES MARKET

The securities markets provide a regulated framework for efficient flow of capital (equity and debt) from investors to business in the financial market system. Securities markets are basically a platform for allocation of savings to investments. Like any market, the securities market is also a place where buyers and sellers get together; the only difference being that the securities market also contributes to capital formation, apart from providing liquidity and price discovery. Due to the power of securities markets, the savings of households, business firms and government can be channelized to fund the capital requirements of a business enterprise.

Key Characteristics of Securities

Before we understand what are securities markets let us first understand what a Security is? A security could be a share / bond or any other financial instrument that has value or is linked to an underlying instrument that has value. According to the Securities Contracts Regulation Act (SCRA), a security is one that is exchange tradable. Here are some key features of securities; as applicable to financial markets.

- Securities represent the terms of exchange of money between two parties; the buyer and the seller in this case.
- Securities can be issued by borrowers / equity funders to raise money at a reasonable cost and gives security ownership to investors.
- Businesses issue securities to raise money from investor with surplus funds through a regulated contract and a regulated and monitored mechanism.
- While the issuer of the security provides the terms for raising capital, investors have a claim to the rights represented by the securities.

- Securities can be broadly classified into equity (risk participation) or debt (claim on cash flows).
- While debt securities are issued for a specific period, equity securities are perpetual. Debt securities pay interest while equity pays out dividends, but it is not assured.

Security Markets: Structure and Participants

Securities market can be broken up into three broad segments, although both are very closely inter-related.

- Primary market refers to the segment of the market where the securities are issued by companies either as a new issue or as an offer for sale. Both equity and debt securities have a primary market where they are first issued.
- Secondary markets are where the actual trading of these securities takes place. Primary issues of debt and equity eventually get traded in the secondary market for price discovery. The secondary market is the normal trading market.
- Derivatives market deals in futures and options. Unlike equities that signify ownership, derivatives are just contracts and are used to manage the risk underlying in the security. Traders can also trade in derivative contracts.

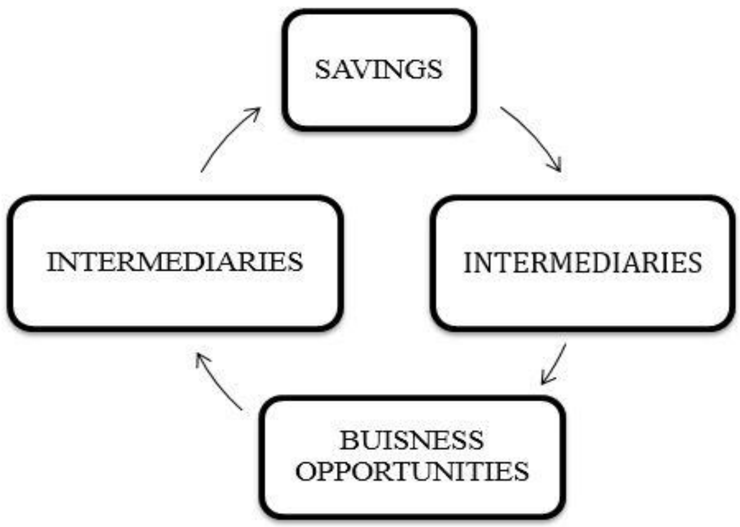
Definition

Intermediary by definition, in any field, is an individual who is in the role of a mediator facilitating an agreement or reconciliation. Accordingly, intermediaries of SEBI too are the bridges or links between the investor and the stock exchange and/or SEBI.

Section 11 and section 12 of SEBI Act, 1992 defines an Intermediary as, Stockbrokers, sub-brokers, portfolio managers, depositories, investment advisers, share transfer agents, merchant bankers, underwriters, registrars to an issue, foreign institutional investors, custodians of securities, venture capital funds, mutual funds, asset management companies, credit rating agencies, those in connection and associated with the securities market in any manner, are all broadly categorized as 'Intermediaries of SEBI'.

ROLE OF SECURITIES MARKET INTERMEDIARIES

The primary need for market intermediaries in the securities market is to match its demand and supply forces. In other words, intermediaries facilitate economies in confronting the critical challenge of the allocation of savings to investment opportunities, as shown in below chart



Flow of Funds in the Capital Market

Economies that are able to match their available resources/savings to appropriate investment opportunities are successful in the creation of novel business avenues and the generation of more wealth and progress. Thus, to say that intermediaries are capable of making or breaking economies would not be an overstatement. Further, investors and issuers are no longer homogenous; issuers and investors today are diverse and depict heterogeneous characteristics. To connect and manage such diverse groups, a mature market with sophisticated middlemen is essential.

- Intermediaries play a vital role for promoting and smooth functioning of the securities market

- all intermediaries provide different financial services to the investors and they are an integral part of securities marker
- they bring efficiency to corporate fund raising by developing expertise in pricing new issues and marketing them to the investors
- Intermediaries can be categorized in two segments as primary market and secondary market intermediaries. SEBI will provide the regulatory frame work for all these intermediaries through regulations

Additionally, in contemporary securities markets, investors and issuers rely heavily on intermediaries to operate on well-informed decisions. Investors, especially retail investors, do not have adequate information, knowledge, or expertise, and issuers do not have adequate resources to reach out to individual investors spread across the country and the globe. Therefore, intermediaries have a very crucial and sensitive role to play in making the market matrix especially anonymous order-driven trading platforms work smoothly.

The roles of the following intermediaries are as follows;

MERCHANT BANKERS

Merchant bankers play an important role in issue management process. Lead managers (category I merchant bankers) have to ensure correctness of the information furnished in the offer document. They have to ensure compliance with SEBI rules and regulations as also Guidelines for Disclosures and Investor Protection. To this effect, they are required to submit to SEBI a due diligence certificate confirming that the disclosures made in the draft prospectus or letter of offer are true, fair and adequate to enable the prospective investors to make a well informed investment decision. The role of merchant bankers in performing their due diligence functions has become even more important with the strengthening of disclosure requirements and with SEBI giving up the vetting of prospectuses. SEBI's various operational guidelines issued during the year to merchant bankers primarily addressed the need to enhance the standard of disclosures.

It was felt that a further strengthening of the criteria for registration of merchant bankers was necessary, primarily through an increase in the net worth requirements, so that their capital would be commensurate with the level of activities undertaken by them. With this in view, the net worth requirement for category I merchant bankers was raised in 1995-96 to Rs. 5 crore. In 1996-97, the SEBI (Merchant Bankers) Regulations, 1992 were amended to require the payment of fees for each letter of offer or draft prospectus that is filed with SEBI. Part III gives further details of the registration of merchant bankers during 1996-97.

Functions

Merchant Banks in India and around the world perform the following functions as part of their standard operations

- **Issue management:** Merchant Bankers advice their clients on the issuing of different types of shares such as equity shares, preference shares, and debentures, which are a type of debt instrument.
- **Credit Syndication:** The Merchant Banks provide loans to a specific set of clients for setting up or executing various projects.
- **Portfolio Counseling:** Merchant Banks also help their clients in investing and managing Portfolios, which are large investments consisting of a number of various financial instruments and investments.
- **Project Counseling:** Clients are advised on various procedural and financial aspects of their short or long-term projects.
- **Brokering in Stock Exchange:** Many Merchant Banks act as brokers of stock exchanges. They buy and sell shares of different types on behalf of their clients.
- **Advice on Expansion and Management:** Some Merchant Banks also provide advice to their customers on the expansion and modernization of their businesses. They advise on mergers, acquisitions and takeovers too.
- **Services to Private & Public Sector Units:** Merchant Bankers also offer many services to public & private sector units like helping in raising funds, marketing of securities, foreign collaborations and managing long-term finances.
- **Management of Interests and Dividends:** Merchant Banks also help their clients in the management of interest on and dividends on their invested shares, and regarding the rate of dividend as well as their timing.

- **Leasing Services:** Some Merchant Banks also help in leasing services where the lessor allows the use of specific assets to the lessee for a certain period on behalf of rentals.

STOCK BROKERS

All stock brokers dealing in securities are registered with SEBI in terms of SEBI (Stock Brokers and Sub Brokers) Regulation 1992. During 1996-97, 391 additional brokers were registered with SEBI making the total registered membership to 8,867 as on March 31, 1997.

Most stockbrokers work for a brokerage firm and handle transactions for a number of individual and institutional customers. Stockbrokers are often paid on a commission basis although compensation methods vary by employer. Brokerage firms and broker-dealers are also sometimes referred to as stockbrokers. This includes both full-service brokers and discount brokers, who execute trades but do not offer individualized investing advice. Most online brokers are discount brokers, at least at their basic levels of service, in which trades are executed for free or for a small set-price commission. Many online brokers now offer premium-level services with higher fees.

Services Provided by Stock Brokers as Share Market Intermediary

- The brokers have the rights to buy or sell company shares. So, they allow trading stocks in the market for a brokerage fee.
- Most stock broking companies nowadays offer online trading platforms
- It is the job of the brokers to issue the Contract Note, which contains all the details of all the stock trading activities that been done in a day.
- The brokers carry out and validate every fund transfer that you may need to make from your bank account to your trading account.
- Most stock broking companies either develop an in-house backend panel or hire a 3rd party company so that you can access all your stocks’ data with ease.

SYNDICATE MEMBERS

Syndicate members are commercial or investment banks responsible for underwriting IPO's. Syndicate members are usually registered with SEBI or registered as brokers with BSE / NSE Stock Exchanges.

They work as intermediaries for Issuer Company and the buyers of the IPO stocks. Investors submit their bids for IPO shares through Syndicate Members appointed by the Issuer Company. They are also known as 'The Members of the Syndicate'. The Members of the Syndicate circulate copies of the Red Herring Prospectus along with the bid cum application form to potential investors. They are also responsible for accepting the bids, payments and application forms for the public issue.

After receiving the bid for IPO Shares from an investor, Syndicate Member enters bidding detail into the electronic bidding system and generates a Transaction Registration Slip ('TRS') for each price and demand option and gives the same to the bidder.

The Bidder can make the revision to the bid any number of times during the Bidding Period. However, for any revision(s) in the Bid, the Bidders should use the services of the same member of the Syndicate through whom he or she had placed the original Bid.

At the time of registering each Bid, the members of the Syndicate enters the following details of the investor in the on-line system:

- Name of the investor.
- Investor Category - Individual, Corporate, NRI, FII, or Mutual Fund etc.
- Numbers of Equity Shares bid for.
- Bid Amount.
- Bid cum Application Form number.
- Whether Margin Amount has been paid upon submission of Bid cum Application Form.
- Depository Participant Identification Number and Client Identification Number of the beneficiary account of the Bidder.

The Members of Syndicate deposit all the money received from investors to the Escrow Account opened by the Issuer Company. The Bid cum Application Form along with other supporting documents is then send to the registrar of the issue for further processing.

REGISTRAR TO AN ISSUE AND SHARE TRANSFER AGENTS

Registrars to an issue (RTI) and share transfer agents (STA) are registered with SEBI in terms of the SEBI (Registrar to the Issue and Share Transfer Agent) Rules and Regulations, 1993. Under these regulations, registration commenced in 1993-94 and is granted under two categories: category I - to act as both registrars to the issue and share transfer agent and category II - to act as either registrar to an issue or share transfer agent. With the setting up of the depository and the expansion of the network of depositories, the traditional work of registrars is likely to undergo a change.

An intermediary plays a notable role when it comes to certain businesses, and has made their presence count. Intermediaries could be anyone who facilitates the supply of a service between two or more persons. A SEBI guideline makes it mandatory to appoint RTI and STA, in relation to the management of public offer introduced by the body corporate in general public, and to service the shareholders.

Registrar to an Issue

The role of a 'Registrar to an issue' would be the following:

- Collecting applications from investors with respect of an issue.
- Proper maintenance of applications, and any monies received from investors or paid to the seller of securities, and
- Assisting the body corporate in terms of; determining the basis of allotment of securities in consultation with the stock exchange, finalizing the list of persons entitled to allotment of securities and; processing and dispatching allotment letters, refund orders or certificates and other related documents in respect of the issue.

The merchant banker co-ordinates with the Registrar to ensure the proper execution of the process.

Share Transfer Agent

'Share transfer agent' is an agent who, on behalf of the body corporate, maintains recorders of holders of securities issued by such body corporate and deals with the processes of transfer and redemption of securities.

Certain roles, as per SEBI guidelines, must only be performed by a 'Share transfer agent'. These activities are:

- Endorsement of certificates/for allotment/call monies.
- Transmission, consolidation, sub-division of securities.
- Dispatch of transferred securities and securities received for transmission/consolidation/sub-division etc, directly to the investors.
- Cancel the name and certificate of the shareholder who had sold the shares of securities, and replace it with the new shareholder.

UNDERWRITERS

Underwriters are required to register with SEBI in terms of the SEBI (Underwriters) Rules and Regulations, 1993. In addition to underwriters registered with SEBI in terms of these regulations, all registered merchant bankers in categories I, II and III and stockbrokers and mutual funds registered with SEBI can function as underwriters. Part III gives further details of registration of underwriters. In 1996-97, the SEBI (Underwriters) Regulations, 1993 were amended mainly pertaining to some procedural matters.

Underwriters play an important role at the time of listing any new companies because they agree to buy all the securities if the share issue is not fully subscribed. They make sure that the share issue is fully subscribed by themselves or by others. Underwriters are appointed by the companies in consultation with merchant bankers.

Investors benefit a lot from the underwriting process as the information provided by an underwriting agency can help them take a more informed buying decision. An underwriter who holds a large chunk of the securities of a particular company or is the market maker for such a security provides the core liquidity for the security and enhances price stability and distribution.

Types of Underwriters

- **Mortgage Underwriters:** The most common type of underwriter is a mortgage loan underwriter. Mortgage loans are approved based on a combination of an applicant's income, credit history, debt ratios, and overall savings. Mortgage loan underwriters ensure that a loan applicant meets all of these requirements, and they subsequently approve or deny a loan. Underwriters also review a property's appraisal to ensure that it is accurate and the home is worth the purchase price and loan amount. Mortgage loan underwriters have final approval for all mortgage loans. Loans that are not approved can go through an appeal process, but the decision requires overwhelming evidence to be overturned.
- **Insurance Underwriters:** Insurance underwriters, like mortgage underwriters, review applications for coverage and accept or reject an applicant based on risk analysis. Insurance brokers and other entities submit insurance applications on behalf of clients, and insurance underwriters review the application and decide whether or not to offer insurance coverage. Insurance underwriters advise on risk management issues, determine available coverage for specific individuals, and review existing clients for continued coverage analysis.
- **Equity Underwriters:** Underwriters administer the public issuance and distribution of securities in the form of common or preferred stock from a corporation or other issuing body in the equity markets. Perhaps the most prominent role of an equity underwriter is in the IPO process. IPO underwriters are financial specialists who work closely with the issuing body to determine the initial offering price of the securities, buy the securities from the issuer, and sell the securities to investors via the underwriter's distribution network. IPO underwriters are typically investment banks that have IPO specialists on staff. These investment banks work with a company to ensure that all regulatory requirements are satisfied. To gauge interest in the investment, the IPO specialists contact a large network of investment organizations such as mutual funds and insurance companies. The amount of interest received by these large institutional investors helps an underwriter set the IPO price

of the company's stock. The underwriter also guarantees that a specific number of shares will be sold at that initial price and purchase any surplus.

- **Debt Security Underwriters:** Underwriters purchase debt securities such as government bonds, corporate bonds, municipal bonds, or preferred stock from the issuing body (usually a company or government agency) to resell them for a profit. This profit is known as the "underwriting spread." An underwriter may resell debt securities directly to the marketplace or to dealers (who will then sell them to other buyers). When the issuance of debt security requires more than one underwriter, the resulting group of underwriters is known as an underwriter syndicate.

BANKERS TO AN ISSUE

Scheduled banks acting as bankers to an issue are required to be registered with SEBI in terms of the SEBI (Bankers to the Issue) Rules and Regulations, 1994. These regulations lay down eligibility criteria for bankers to an issue and require registrants to meet periodic reporting requirements. Part III gives further details of registration of bankers to an issue.

Bankers to the issue are financial intermediaries who are responsible for banking-related processes like:-

- Acceptance of application and application amount
- Transfer of funds to the promoters of the company
- Managing refunds for rejected applications
- Payment of dividend

In the IPO process, the bankers play a critical role by enabling the movement of funds and making clear funds status available to the registrars to finalize the basis of allotment.

PORTFOLIO MANAGERS

Portfolio managers are required to register with SEBI in terms of the SEBI (Portfolio Managers) Rules and Regulations, 1993. The registered portfolio managers exclusively carry on portfolio management activities. In addition all merchant bankers in categories I and II can act as portfolio managers with prior permission from SEBI. Part III gives further details of the registration of portfolio managers.

A portfolio manager is an individual who develops and implements investment strategies for individuals or institutional investors. Under the purview of financial services industry careers, portfolio management positions are available with hedge funds, pension plans, and private investment firms, or as part of an investment department of an insurance or mutual fund company.

Portfolio managers may be called investment managers, wealth managers, asset managers, or financial advisors, but a true portfolio manager position is focused on the analytical side of investing rather than the sales aspect.

Functions:

- Portfolio managers develop and put in place investment strategies for investors (i.e., building and managing investment portfolios).
- Portfolio management typically requires at least an undergraduate degree in business, economics, or finance.
- Individuals best suited for this position have high degrees of efficiency in data interpretation and a penchant for research and analysis.

DEBENTURE TRUSTEE

Debenture Trustee is a liaison between the issuer company and the debenture holders, who hold the secured property on behalf of the issuer company, which is mortgaged in favor of debenture trustee for protecting the interest of debenture holders.

As per the provisions of the companies act, the appointment of a debenture trustee is mandatory in case of debentures/bonds with maturity beyond 18 months, irrespective of whether debentures/bonds are secured or not. However, the issue of debentures/bonds with a maturity of 18 months or less is exempt from the requirement of debenture trustee.

Debenture Trustee Role and Responsibilities

- To protect the interest of the debenture holders.

- To call for and keep a periodic check on the reports of the issuer company.
- To take possession of the trust property by provisions of the trust deed.
- To take appropriate measures to protect the interest of the debenture holders in case of any breach of the trust deed or law.
- To ensure that the debentures have been converted or redeemed as per the provisions and conditions under which they are offered to debenture holders.
- To enforce security in the interest of the debenture holders in case of any default by moving to assets for collection of debt.
- To ensure at all times that the property charged to the debenture is free from any other claim except those specifically agreed with the debenture holder and that the property is available and adequate to discharge the interest and the principal amount payable in respect of the debentures.
- To exercise due diligence to ensure that the issuer entity is compliant with provisions of the Companies Act, the listing agreement of the stock exchange, or the trust deed.
- To inform the Board immediately in case of any breach of trust deed or provision of law.
- To appoint a nominee director on the board of issuer entity when required. A nominee director can be appointed in case of below happenings:
    - Two consecutive defaults in payment of interest to debenture holder or
    - Default in the creation of security for debentures or
    - Default in the redemption of debt.

With such an important role to play for the debenture trustee, SEBI is looking to strengthen the regulatory framework for them in view of better investor protection and reducing the events of defaults by financial institutions.

INVESTMENT ADVISER

An investment adviser is a person or firm that is engaged in the business of providing investment advice to others or issuing reports or analyses regarding securities, for compensation. Investment advisers may include money managers, investment consultants, financial planners, general partners of hedge funds, and others who are compensated for providing advice about securities.

Advice about securities not only includes advice about specific securities (such as stocks, bonds, mutual funds, limited partnerships, and commodity pools), but may also include advice about market trends, the selection or retention of other advisers, the advantages of investing in securities over other types of investments (such as coins or real estate), the furnishing of a selective list of securities, and asset allocation.

Investment advisers generally must register with the Securities and Exchange Commission (SEC) or state securities authorities.

A typical investment bank's services will include:

- **Financing Services:** They help companies and governments raise capital by issuing different types of securities such as, equity, debt, private placements, commercial paper, medium-term notes.
- **Investment Services:** They trade and make a market in major equity and fixed income products. Many of them specialize in block trading.
- **Research:** Maintenance of large databases that allows them to produce research reports on economies, markets, companies, stocks, and bonds.
- **Mergers and Acquisitions:** Advise on mergers, acquisitions, and divestitures to help companies become more competitive.

RESEARCH ANALYST

A research analyst is a professional who prepares investigative reports on securities or assets for in-house or client use. Other names for this function include securities analyst, investment analyst, equity analyst, rating analyst, or simply "analyst."

The work conducted by the research analyst is in an effort to inquire, examine, find or revise facts, principles, and theories for internal use by a financial institution or an external financial client. The report an analyst prepares entails the examination of public records of securities of companies or industries, and often concludes with a "buy," "sell" or "hold" recommendation.

The Basics of Being a Research Analyst

Research analysts are usually divided into two groups: "buy-side" and "sell-side" analysts. A buy-side (brokerage) research analyst is typically employed by an asset management company and recommends securities for investment to the money managers of the fund that employs them. The research of a sell-side (investment firm) analyst tends to be sold to the buy-side. Sell-side research is also given to clients for free for consideration, such as in an attempt to win business. Such research can be used to promote companies.

- A research analyst is a professional who prepares investigative reports on securities or assets for in-house or client use.
- The report an analyst prepares entails the examination of public records of securities of companies or industries, and often concludes with a "buy," "sell," or "hold" recommendation.
- The main differences between buy-side and sell-side analysts are the type of firm that employs them and the people to whom they make recommendations.

MARKET MAKER

A market maker is a “market participant” that executes a transaction of buy and sells securities regularly at prices that are prevailing in an exchange’s trading system for its account, which is called principal trades and for customer accounts, which are called agency trades. With the help of these systems, a broker can enter and adjust quotes to buy or sell, enter, and execute orders, and clear those orders. These are member firms appointed by the stock exchange to maintain the liquidity and trade volume into stock markets.

They are commonly known as a brokerage firm that provides purchase and sale options for investors to keep the financial markets volatile. A broker firm can also be an individual intermediary/Broker.

Role of Market Makers

- **Providing Liquidity:** The role of a broker is to provide liquidity and make trading accessible to retail traders. There are required to provide the opportunity to make a trade in the market. A broker firm facilitates the smooth flow of financial markets. Makers Market helps investors and traders to buy and sell security easily in the market.

- **Matching Orders:** The broker identifies the market for buyers and sellers of the same stock/securities at a particular volume and then executes a buy order on a stock/security of the same volume to a sell order on the same stock/security with the same volume. But, there are situations when it may happen that there is no exact match for the order. It is where market makers play a vital role by acting as a buyer or seller for such a transaction. In this manner, they act as counter-party to the trade to buy a sell order from a trader or sell an asset to a trader to match the buy order.

- **Stabilizing Spreads:** Broker firm has the influence to stabilize spreads by maintaining the liquidity; it would be difficult to keep the spreads low & at a fixed rate. However, as the broker bears this risk and then fix prices for the traders, which help them to keep the spreads low and fixed. It helps in cost savings for retail traders while executing trades.

Advantages

To Companies:

- It analysis the security options, which benefits the company.
- It helps to have a continuous source of the liquidity for the company's scrips.
- They help to provide easy in valuation for the company's scrips.

To Investors:

- They help investors to liquidate their investments at a better price at any point in time.
- This concept has a tuff competition, which results in the efficient pricing of a stock.
- They benefit the investors by providing valuable information on the company.

Types of Market Makers

There are basically two types of brokers in the market:

- **Principal Market Makers (PMM):** It offers to buy and sell quotes for almost 18 months from the commencement of the initial trading.

- **Additional Market Makers (AMM):** It normally buys and sells quotes for almost one year from the actual commencement of the initial trading.

CREDIT RATING

Credit ratings provide retail and institutional investors with information that assists them in determining whether issuers of bonds and other debt instruments and fixed-income securities will be able to meet their obligations.

When they issue letter grades, credit rating agencies (CRAs) provide objective analyses and independent assessments of companies and countries that issue such securities. Here is a basic history of how the ratings and the agencies developed in the U.S. and grew to aid investors all over the globe.

Role of Rating Agencies in Capital Markets

- Rating agencies assess the credit risk of specific debt securities and the borrowing entities. In the bond market, a rating agency provides an independent evaluation of the creditworthiness of debt securities issued by governments and corporations. Large bond issuers receive ratings from one or two of the big three rating agencies. In the United States, the agencies are held responsible for losses resulting from inaccurate and false ratings.
- The ratings are used in structured finance transactions such as asset-backed securities, mortgage-backed securities, and collateralized debt obligations. Rating agencies focus on the type of pool underlying the security and the proposed capital structure to rate structured financial products. The issuers of the structured products pay rating agencies to not only rate them, but also to advise them on how to structure the tranches.
- Rating agencies also give ratings to sovereign borrowers, who are the largest borrowers in most financial markets. Sovereign borrowers include national governments, state

governments, municipalities, and other sovereign-supported institutions. The sovereign ratings given by a rating agency shows a sovereign's ability to repay its debt.

- The ratings help governments from emerging and developing countries to issue bonds to domestic and international investors. Governments sell bonds to obtain financing from other governments and Bretton Woods institutions such as the World Bank and the International Monetary Fund.

Benefits

- At the consumer level, the agency's ratings are used by banks to determine the risk premium to be charged on loans and bonds. A poor credit rating shows that the loan has a higher risk premium, and this prompts an increase in the interest charged to individuals and entities with a low credit rating. A good credit rating allows borrowers to easily borrow money from the public debt market or financial institutions at a lower interest rate.
- At the corporate level, companies planning to issue a security must find a rating agency to rate their debt. Rating agencies such as Moody's, Standards and Poor's, and Fitch perform the rating service for a fee. Investors rely on the ratings to decide on whether to buy or not to buy a company's securities.
- Although investors can also rely on the ratings given by financial intermediaries and underwriters, ratings provided by international agencies are considered more reliable and accurate since they can access lots of information that is not publicly available.
- At the country level, investors rely on the ratings given by the credit rating agencies to make investment decisions. Many countries sell their securities in the international market, and a good credit rating can help them access high-value investors. A favorable rating may also attract other forms of investments like foreign direct investments to a country.
- In addition, a low credit rating or relegation of a country from a high rating to a low rating can discourage investors from purchasing the country's bonds or making direct investments in the country. For example, the downgrading of Greece, Portugal, and Ireland by S&P in 2010 worsened the European sovereign debt crisis.
- Credit ratings also help in the development of financial markets. Rating agencies provide risk measures for various entities, and this allows investors to understand the credit risk of

various borrowers. Institutions and government entities can access credit facilities without having to go through lengthy evaluations by each lender.

- The ratings provided by rating agencies also serve as a benchmark for financial market regulations.

QUESTION BANK

PART – A

S. No	Questions	CO	Level
1	A stockbroker or sub-broker shall not be liable for prosecution under the SEBI Act, 1992 for any violation - Explain.	CO4	L3
2	Explain a short note on syndicate member.	CO4	L3
3	Recall the functions performed by debenture trustees.	CO4	L4
4	Distinguish between: merchant banker and portfolio manager.	CO4	L4
5	Highlight the roles of a portfolio manager.	CO4	L3
6	Explain the significance of intermediaries.	CO4	L3
7	Explain the types of underwriters.	CO4	L4
8	Tell about online surveillance by stock exchange.	CO4	L4
9	Explain the credit rating operations towards stock market.	CO4	L4
10	Explain the types of market makers.	CO4	L5

PART – B

S. No	Questions	CO	Level
1	“Merchant bankers are the key intermediary between the company and issue of capital.” Comment.	CO4	L5
2	Explain the role of securities market in economic growth.	CO4	L6
3	Discuss what you understand by ‘registrars to an issue and explain the various activities carried out by registrars to an issue.	CO4	L5

4	Discuss briefly the different surveillance system adopted by the stock exchanges.	CO4	L6
5	Discuss conditions of registration of Portfolio Managers and procedure where registration is not granted by SEBI.	CO4	L5
6	Explain briefly the role and responsibilities of Registrar and Transfer Agent.	CO4	L5
7	Is underwriter is compulsory for a public issue. If yes, explain the role and responsibilities of underwriter in public issue.	CO4	L5
8	Explain general obligations of Credit Rating Agencies under Chapter III of SEBI (Credit Rating Agencies) Regulations, 1999.	CO4	L5
9	Explain major provisions of SEBI (Credit Rating Agencies) Regulations, 1999.	CO4	L6
10	Investment Advisor provides guidance about financial obligations and investment. Comment on this statement and state the role of investment advisors in capital market.	CO4	L6

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SCHOOL OF MANAGEMENT STUDIES

UNIT – V – CAPITAL MARKETS– SBAA3003

The Securities and Exchange Board of India (SEBI) - Constitution, powers, functions, and role of SEBI in regulating the primary and secondary markets - Investor protection.

SEBI (SECURITIES AND EXCHANGE BOARD OF INDIA) - INTRODUCTION

The Securities and Exchange Board of India or SEBI is the main regulatory body who looks after the functioning of securities market in India. SEBI was constituted in 12th April 1988 as a non-contributory body through a resolution of the government. SEBI looks after investor protection and advices the government on all such matters.

SEBI received the statutory status and powers through an ordinance which was promulgated on 30th January 1992. The same is also referred to as the SEBI act of 1992. SEBI has a dedicated platform for investor grievance and redressal which is known as SEBI Complain and Redressal System (SCORES).

CONSTITUTION

The SEBI is a body of six members comprising the chairman, two-member from the ministry of a central bank dealing with finance and law, two members who are professionals and have experience or special knowledge relating to the securities market, and one member from RBI. All the members except the RBI member are appointed by the government who also lays down their terms of office, tenure, and conditions of services, and who also removes any member from the office under any circumstances. The central government is empowered to supersede the SEBI in the public interest or if, on account of grave emergency and some other circumstances.

The work has been organized into five operational departments each of which is headed by an executive director who reports to the Chairman. Besides, there is a legal department and investigation department. The department is further divided into divisions.

The various departments are as follows.

- The primary market policy, intermediaries, self-regulatory, organizational and investor grievance and guidance department

- The issue management and intermediaries department.
- The secondary market policy, operation, and exchange administration, new investment products and insider training department.
- The secondary market exchange administration, inspection and non-member intermediaries department institutional investment (mutual fund and foreign institutional investment
- Merger and acquisition, research and publication, and international relation department.
- Legal department
- Investigation department

The SEBI has regional offices at Calcutta, Chennai, and Delhi.IT has also formed two non-statutory advisory committees namely Primary market Advisory Committee and Secondary Market Advisory Committee with members from the market players, recognized investor associations, and other eminent persons.

WHY WAS SEBI FORMED?

At the end of the 1970s and during 1980s, capital markets were emerging as the new sensation among the individuals of India. Many malpractices started taking place such as unofficial self-styled merchant bankers, unofficial private placements, rigging of prices, non-adherence of provisions of the Companies Act, violation of rules and regulations of stock exchanges, delay in delivery of shares, price rigging, etc.

Due to these malpractices, people started losing confidence in the stock market. The government felt a sudden need to set up an authority to regulate the working and reduce these malpractices. As a result, the Government came up with the establishment of SEBI.

OBJECTIVES OF SEBI

SEBI has following objectives:

- **Protection to the investors:** The primary objective of SEBI is to protect the interest of people in the stock market and provide a healthy environment for them.

- **Prevention of malpractices:** This was the reason why SEBI was formed. Among the main objectives, preventing malpractices is one of them.
- **Fair and proper functioning:** SEBI is responsible for the orderly functioning of the capital markets and keeps a close check over the activities of the financial intermediaries such as brokers, sub-brokers, etc.

POWERS OF SEBI

SEBI has the power to regulate and approve any laws related to functions in the stock exchanges.

- It has the powers to access the books of records and accounts for all the stock exchanges and it can arrange for periodical checks and returns into the workings of the stock exchanges.
- It can also conduct hearings and pass judgments if there are any malpractices detected on the stock exchanges.
- When it comes to the treatment of companies, it has the power to get companies listed and de-listed from any stock exchange in the country.
- It has the power to completely regulate all aspects of insider trading and announce penalties and expulsions if a company is caught doing something unethical.
- It can also make companies list their shares in more than one stock exchange if they see that it will be beneficial to investors.
- Coming to investor protection, SEBI has the power to draft legal rules to ensure the protection of the general public.
- It also has the power to regulate the registration of brokers and other middlemen who will deal with investors in the market.

ORGANIZATIONAL STRUCTURE OF SEBI

SEBI consists of a chairman and six members, which are nominated by the Central Government. There are two members who are officers from central ministries. SEBI also consists of one member from the Reserve Bank of India and two members nominated by the Central Government. The SEBI headquarters are located in Mumbai, with branch offices in the remaining metros of India, namely Delhi, Kolkata and Chennai.

SEBI was formed with an initial capital of 7.5 crore INR in 1988. The funding was provided by the promoters - IDBI, ICICI and IFCI. This amount was invested, and the interest generated on the same is usually used for all day to day expenses of the department. All statutory powers for regulating the Indian capital markets are vested with SEBI.I

FUNCTIONS OF SEBI

Let us now discuss about the functions performed by the Securities and Exchange Board of India. The key functions of SEBI include:

1. Regulating the Capital Markets by undertaking suitable measures
2. Safeguarding the interest of investors
3. Regulating the functioning of stock exchanges and security markets
4. Regulating the functioning of Stockbrokers and transfer agents, merchant bankers etc.
5. Registration of Brokers, Investment Advisors and other entities
6. Encouraging Self-Regulatory Organizations (SRO)
7. Eliminating the loopholes and malpractices in the security markets
8. Ensuring investor's education
9. Management of Complaint and Redressal System for investors (SCORES)
10. Ensuring systematic dealings and supervising the overall functioning of the system

These are some of the key functions which are performed by SEBI. There are various other functions as well which the regulator looks after.

DECISIONS TAKEN BY SEBI TO ENSURE A HEALTHY CAPITAL MARKET

SEBI is the regulatory body for the Indian capital markets and has adopted various steps and functions to ensure smooth and healthy functioning of the capital markets. Let us take a look at some of them.

- **Determination of Premium and Share Prices:** As per the latest announcement of SEBI, all listed Indian companies have been given a free hand in determining their stock prices and premium on those prices. However, SEBI ensures that the determined pricing and premium is equally applicable for all without any sort of discrimination.
- **Eligibility Criteria for Under Writers:** SEBI has fixed the minimum asset limit at 20 lakhs INR to work as an under writer. Also, SEBI looks after the functioning if under writers as well and holds the full authority to cancel their registration if any irregularity is found in the purchase of unsubscribed part of the share issue.
- **Abolishing Insider Trading:** Insider trading was one of the biggest loopholes of the Indian Capital Markets. A recent web series has also portrayed how insider trading was used for making huge profits. SEBI introduced the SEBI regulation 1992 which ensures honesty and transparency in the Capital Markets.
- **The control on Mutual Funds:** SEBI announced the SEBI Mutual Funds Regulation in 1993 which gave the authority to take over the direct control of all mutual funds of private sector and government. As per the announcement, any company which floats a mutual fund should necessarily have net assets worth over INR 5 Crores and should consist a contribution of at least 40% from the promoter.
- **Control on FIIs:** Foreign Institutional Investors or FIIs, now need to be registered with SEBI before they step in the Indian Capital Markets. The directives issued by SEBI in this regard state that every FII who is investing in Indian Capital Markets needs to have a SEBI registration.

These are some of the major directives and decisions which are undertaken by SEBI to ensure smooth and healthy functioning of the Indian Capital Markets.

THE ROLE OF SEBI IN REGULATING THE PRIMARY MARKET FOR SECURITIES

Securities and Exchange Board of India [SEBI] is a regulator of securities market in India. Initially, it was formed for the purpose of observing the activities afterward in May 1992, Government of India granted legal status to SEBI.

Functions of Primary Market under SEBI

- Primary Market facilitates capital growth by encouraging individuals to convert savings into investments.
- Primary Market being the part of Capital market also issues new securities.
- Government or Public sector institutions and companies can obtain funds in exchange of a new stock or bond issues via an investment Bank or financial Syndicate of securities dealers.
- It encourages Initial Public Offerings [IPO]

Role of SEBI

Protecting the interest of investors

- SEBI ensures that the investors do not get be fooled by misleading and false advertisements. In return, SEBI issued guidelines so as to protect investors and also ensured that the advertisement is fair and concise.
- Regulation of price rigging: Price rigging refers to manipulation of prices by way of fluctuating the prices with the object of inflating and depressing the market price of securities.
- SEBI make efforts to educate investors so that they are able to make choices between the offerings of different companies and choose the most profitable securities.
- SEBI has issued guidelines to investigate cases of fraud and insider trading. Adding to this the provisions for fine and Imprisonment.
- To ensure Development activities in Stock Exchange
- E-Trading: Concept of E-trading has been introduced few years back by SEBI to eliminate the discomfort. It simplifies the process of buying and selling of securities.
- The initial public offering of Primary Market (which is a part of Capital market) permits through stock exchange.

- SEBI promotes training of intermediaries of securities market with the object of smooth functioning.

Regulate the business of stock exchange and activities of stock exchange

SEBI introduced proper Code of Conduct applicable to everyone who is a part of the process of buying and selling of securities, stock exchange, etc. Following are the areas of concern:

- Rules and Regulations to regulate intermediaries such as Broker, underwriters, etc.
- Registers and regulates the working of merchant Bankers, sub-brokers, stock-brokers, and share transfer agent, trustees, etc.
- Registers the working of mutual Funds.
- SEBI regulates turnover of the companies.
- It also conducts inquiry and audits.

To Regulate Insider Trading

Insider trading has been a problem since the introduction of the Market dealing with buying and selling of securities, stock exchange, etc. An Insider is a person or a group of people having first-hand knowledge about the internal issues and Ups and downs of a company. The moment insider gets to know about the loss which is going to occur, the shares under insider's name are sold immediately. Hence, company suffers a huge amount of loss.

Process of Issuance of Securities

Preparation of Prospectus

The prospectus must contain following information:

- Name
- Address
- Registered Office
- Names and Addresses of
- Company Promoters
- Managers
- Managing Directors

- Director
- Company Secretary
- Legal Advisor
- Auditors
- Bankers

It also includes information related to project, plant location, Technology, collaboration, products, export obligations, etc. Intermediaries include underwriters and Brokers are separately appointed by the company to sell the minimum number of shares. Prospects issued by the company must be approved by SEBI. A company offers minimum of 49 percent of the amount of shares to the public.

FOLLOWING MENTIONED ARE THE WAYS OF ISSUING STOCKS IN MARKET

1. **Initial Public Offering [IPO]**

When a company make public issue of shares for the very first time it is referred to as Initial Public Offering. Process of Initial public offering as per the guidelines of SEBI includes: Firstly, issuance of prospectus is the first and foremost task, the prospectus must include every detail about the company and about the issue; Secondly, issuance of share Application Forms by the intermediaries (underwriters and brokers); Thirdly, brokers make a list of orders collected from clients and then place orders with the company; Fourthly, company then begins with the allotment of Shares with the help of stock exchange. After the Allotment procedure share certificates are delivered to the investors or credited to their respective Demat Accounts. Investors must be vigilant about additional offers and tempting IPO which company offers.

FACTORS MUST BE KEPT IN MIND WHILE STUDYING AN IPO OFFER DOCUMENT

- Promoter
- Performance
- Prospects
- Price

2. **Private Placement**

The securities are offered for sale privately to some specific individuals and other institutions. No prospectus is issued to cut the cost and time involved in the process of allotment and issuance. This method is very popular among investors these days. This way, shares are concentrated in few hands only. Thus this increases the price temporarily and is sold to the small and common investors.

3. **Offer For Sale**

Process of offer for sale is somewhat similar to private placements. Stock Brokers negotiate with companies regarding the price and terms and conditions based of which the shares are being issued. After negotiation, intermediaries buy shares from the company. Securities are then sold to the investors at a higher price to earn some extra profit. This method is adopted to save time and cost of the process.

4. **Bought out deals**

Bought out deals are those deals wherein a company in order to introduce its shares to the market sells all its equity shares to a single broker. The sale under Bought out deals is similar to that of Offer for sale.

5. **Right Issue**

Right issue is made by a company to its existing shareholders in proportion to the number of shares that they posses.

GUIDELINES BY SEBI

- Only listed company can make right issue.
- Right can be made only in respect of fully paid up shares.
- Company will have to make announcement before such issue and this cannot be withdrawn.
- The right issue should be open for minimum period of 30 days, and maximum up to 60 days.
- Company will have to make an agreement with the depository to issue the shares in Demat form.

6. **Bonus Issue**

Extra Bonus received is treated as a part of Profit under Share Capital and thus it is divided between the shareholders of a company.

7. **Book- Building**

Under normal circumstances, brokers are the intermediaries through which shares are allotted whereas under book building process feedbacks of the investors are taken for the fixation of price of the shares

SEBI GUIDELINES FOR PROTECTING INTEREST OF INVESTORS

The main object of SEBI is not only to regulate stock markets but also to protect the interest of investors. For this purpose, SEBI has given following guidelines:

- SEBI has been encouraging investor-education. For this purpose, certain investors' associations have been registered.
- Companies raising public deposits as well as huge capital must undergo credit rating. Credit rating by an authorized authority gives a fair view about the financial strength of the organization. For this purpose, there are four credit rating agencies. They are:
  - CRISIL
  - ICRA
  - CARE and
  - Duff and Phelps Credit Rating India Pvt. Ltd.
- SEBI has taken the responsibility of disclosing fair and adequate information for investors for the purpose of investment decisions.
- For the benefit of the investors, company has to disclose its capacity utilization, adverse events and material changes of key personnel.
- Disclosure on market prices for listed company.
- Arrangement for disclosing investor's grievances and redressal system.
- Compulsory disclosure in the prospectus.
- Contribution by promoters whose name figure in the prospectus.
- In case of over subscription of any company issue, SEBI representatives will be present there to look into the allotment process.
- Setting up of investor's grievances cell for handling complaints of investors.
- SEBI has right to cancel registration of any underwriter who fails to furnish business details to SEBI.

- SEBI has made it mandatory for Merchant bankers to attach diligence certificate with the prospectus for extending their accountability to the investors. The diligence certificate gives a detailed position of the issue of shares. Only by such a certificate, the investor can file a case of incorrect statement in the prospectus on erring companies.
- There is an advertisement code by SEBI which has to be followed by companies or investors.
- To avoid any malpractice in allotment process, SEBI has appointed its representatives to look into allotment process which boosts the confidence of individual investors.
- Underwriters, registrar to issue and share transfer agent and portfolio managers have been brought under SEBI for the first time.
- Even the mutual funds have been brought under SEBI and they have to disclose NPV (Net present value) of units every day which benefits investors.
- For the benefit of the individual investors, a new scheme called stock invest account has been introduced in banks. From this stock invest account; the new issue of shares will be applied. In that, the investor will intimate the stock invest account to the company issuing the shares.
- In case of allotment, the company will inform the banker as per SEBI guidelines, and funds will be released from the stock invest account to the bank.

QUESTION BANK

PART – A

S. No	Questions	CO	Level
1	State the purpose of setting up SEBI.	CO5	L3
2	Identify the type of function performed by SEBI.	CO5	L3
3	Outline the reasons for setting up SEBI.	CO5	L5
4	Discuss the objectives of NSDL.	CO5	L4
5	Highlight the importance of debt market.	CO5	L3
6	Recall the decisions taken by SEBI to ensure a healthy capital market.	CO5	L3

7	Explain the role of SEBI in protecting the interest of investors.	CO5	L2
8	List and explain the factors of IPO offer document.	CO5	L5
9	Explain book building.	CO5	L4
10	Brief the guidelines given by SEBI for right issue.	CO5	L5

PART – B

S. No	Questions	CO	Level
1	Explain the role of SEBI in strengthening regulatory framework and fostering investor confidence.	CO5	L5
2	Discuss the SEBI guidelines regarding regulation of stock exchange.	CO5	L6
3	Discuss a note on the operators at the stock exchanges. Also discuss the weaknesses of the Indian stock exchanges.	CO5	L5
4	Enumerate the functions of SEBI. In your opinion, are these sufficient to regulate the capital market in India?	CO5	L6
5	Explain briefly the functions of stock market in India. Critically evaluate the role of SEBI as stock market developer.	CO5	L6
6	Explain the uses of market indices? Discuss in detail the various factors which are considered while constructing market indices.	CO5	L6
7	Explain SEBI along with its objectives by critically evaluating the performance of SEBI in the achievement of stated objectives.	CO5	L5
8	Discuss in brief the rules governing functioning of stock exchanges in India.	CO5	L5
9	Elaborate the membership rules of stock exchanges in India.	CO5	L6
10	“SEBI has failed to perform its duty as the regulator of securities market in India”. Give your comments along with proper justification.	CO5	L6

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