

## GRADE12 BUSINESS STUDIES NOTES-- CHAPTER-10 – FINANCIAL MARKET - NOTES-2025-26

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A financial market is a market for the creation and exchange of financial assets.

**Creation means** initial issue of shares and debentures by a firm.

**Exchange means** the purchase and sale of existing financial assets like equity shares, debentures and bonds.

Savers are households.

Business firms are investors which invest in these funds by issuing shares and debentures.



Financial market helps to link the saver and the investor by moving(mobilizing) funds between them. It is called **ALLOCATIVE FUNCTION**.

**Two consequences of well performed Allocative function”**

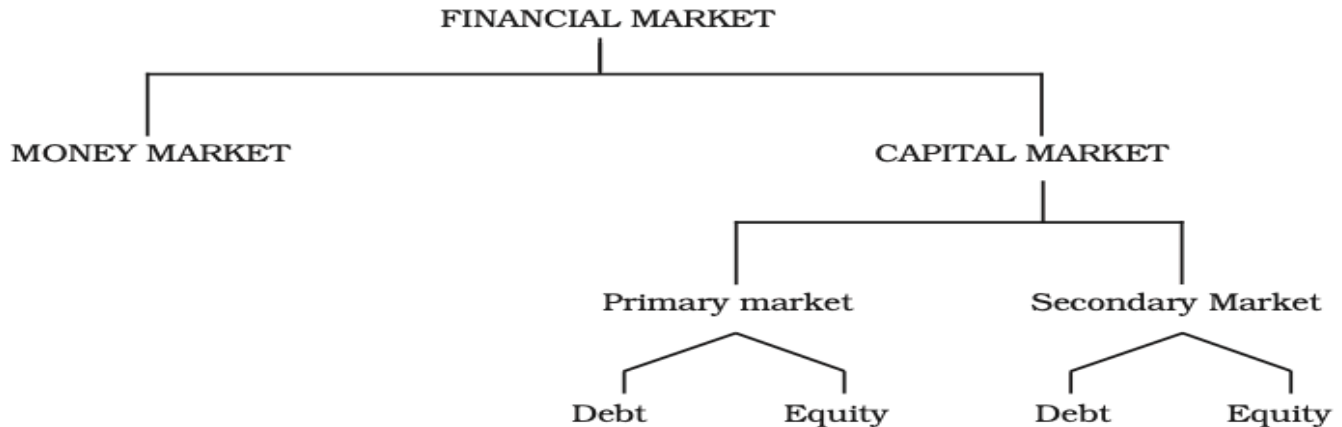
1. **Higher rate of return to household.**
2. **Scarce resources will go to highly productive firms in the country.**

**Financial intermediation:** The process by which allocation of funds is done.

### **FUNCTIONS OF FINANCIAL MARKETS**

- ❖ **Movement of Savings from saver to investors and business uses funds wisely:** it helps to transfer savings from saver to investors. Business firms use these funds in productive manner. Saver get choice of different investment schemes.
- ❖ **Helps to set price of financial securities:** Here price of financial assets is decided by interaction between saver (supplier)and Business firms (demand maker).
- ❖ **Provide liquidity to Financial assets:** this market make easy to sale and buy securities, helps to convert financial assets into cash when needed.
- ❖ **Reduce the cost of transactions:** This market gives valuable information about financial assets traded in the market. It helps to save time, money and efforts. Common platform for buyer and seller to fulfill their needs.

## Classification of Financial Markets



### 1. MONEY MARKET

- ❖ Market for short term instruments- maturity less than ONE YEAR, such as Treasury Bills, Commercial Papers, Commercial Bills.
- ❖ Fulfil the temporary shortage of cash
- ❖ Low Risk
- ❖ Highly liquid [any time we can convert security into cash]
- ❖ Unsecured – no need of collateral security.
- ❖ No physical location-Transactions conducted through Phone or Internet.
- ❖ **PARTICIPANTS**
  - RBI
  - Commercial Banks
  - State Government
  - Mutual funds
  - Non Banking Finance Companies

### CAPITAL MARKET

- ❖ Financial instruments for **more than one year** are traded in the Capital Market such as **Debentures and Shares**
- ❖ **Less liquid, more risky**
- ❖ An **ideal capital market** is one where **finance is available at reasonable cost**.
- ❖ Capital market should be **efficient in giving information, minimize transaction cost and allocate capital most productively**.
- ❖ **Helps in Economic growth** by mobilization of Savings and Channelizing them into the most productive users
- ❖ It includes **Stock exchange, Development banks and Commercial banks**
- ❖ Capital market operations are **free, fair competitive and transparent**

## DIFFERENCE BETWEEN CAPITAL MARKET AND MONEY MARKET

BASIS	CAPITAL MARKET	MONEY MARKET
DURATION	Financial instruments with long term MORE THAN ONE YEAR are sold and purchased here.	Financial instruments with short term LESS THAN ONE YEAR/single day are sold and purchased here.
Instruments/securities sold or purchased	Equity Shares, Preference shares, debentures and bonds.	Call money, commercial bills, commercial papers, certificate of deposits, T-Bills, trade bills reports etc.
participants	Financial institutions, banks, corporate bodies, foreign investors& ordinary retail investors.	RBI, Financial institutions, commercial banks, individual investors.
safety	More risk in case of returns and principal amount payment. All kind of companies can sale and purchase securities.	Less risk (minimum risk of default) because of shorter duration and securities are issued by financial institutions/ banks, govt. and financially strong companies.
Liquidity	Lesser degree of liquidity	Higher degree of liquidity
Investment Outlay	The value of units of securities is generally low i.e. Rs 10, Rs 100	Huge/ Big sums of money as the instruments are quite expensive.

### 1. PRIMARY MARKET/ NEW ISSUE MARKET- sells new/ first hand securities

- ❖ Deals with securities which are **issued in market for the first time**
- ❖ **Transfer funds from savers to investors** to establish new/ expand firms by issuing securities for the first time.
- ❖ Main investors are **Banks, Financial institutions, Mutual funds** and Insurance companies.
- ❖ Securities traded in market: **equity shares, preference shares, loans, deposits and debentures** are issued for **setting up new project, Expansion, Diversification, Modernization, Takeover, Merger.**

### 2. SECONDARY MARKET: for selling second hand securities

\*Market for sale and purchase of **existing/old/second hand securities.**

\*Known as **stock market or stock exchange.**

\* It helps the **existing investors to disinvest** and **fresh investors to reinvest**

\*It **increases liquidity and marketability** of existing securities.

\* It follows the **process of disinvestment(sale) and reinvestment(buy).**

\* It **helps in economic growth.**

\*All functions of this market are **controlled/ regulated by SEBI.**

\* Technology helps the investors to trade from anywhere through trading terminals.

## **DIFFERENCE BETWEEN PRIMARY MARKET AND SECONDARY MARKET :**

<b>Basis</b>	<b>Primary Market</b>	<b>Secondary Market</b>
<b>Securities</b>	Only new securities are traded	Existing/ SECOND HAND securities are traded
<b>Price of Securities</b>	Prices of securities are decided by the management of the company.	Prices are decided by demand and supply for the securities.
<b>Purchase and Sale</b>	Securities are sold to investors directly by the company or through middleman.	stock exchange helps to exchange securities among investors.
<b>Place of Market</b>	There is no fixed geographical location.	Located at fixed places as well as online too.
<b>Medium</b>	Only buying of securities takes place.	Both buying and selling of securities can take place.
<b>Flow of funds</b>	Primary market directly promotes capital formation.	Secondary market indirectly promotes capital formation

**Stock Exchange:** A Stock Exchange is an institution which provides a platform for buying and selling of existing securities. It facilitates “Exchange of Securities”.

- Stock exchange help companies to raise funds, enhance credit worthiness.
- Stock exchange provide Liquidity and safety of investment to the investors/ household.

**Definition:** According to Securities Contracts (Regulation) Act 1956, stock exchange means any body of individuals, whether incorporated or not, constituted for the purpose of assisting, regulating or controlling the business of buying and selling or dealing in securities.

### **Functions of a Stock Exchange:**

- 1. Providing liquidity and Marketability to Existing Securities:** Stock Exchange provides a ready and continuous market for the sale and purchase of Existing securities. Provides Liquidity and market for existing securities.
- 2. Pricing of Securities:** Constant valuation of securities provide valuable information to both buyers and sellers. It helps in setting price of securities based on the forces of demand & supply.

- 3. Safety of Transaction:** The stock exchange works through legal framework SEBI and makes sure public will get a safe and fair deal.
- 4. Contributes to Economic Growth:** Stock exchange helps to give choice of investment schemes to the investors with the process of disinvestment and reinvestment, which leads to capital formation & economic growth.
- 5. Spreading of Equity Culture:** Stock exchange helps in educating public about investments in securities, provide better trading practices which leads to spreading of Equity culture. It ensures wider share ownership by regulating new issues.
- 6. Providing Scope for Speculation:** Stock exchange provide scope for healthy speculation in a restricted and controlled manner through SEBI. It is generally accepted that a certain degree of healthy speculation is necessary to ensure liquidity and price continuity in the stock market.

### **IMPORTANT TERMS:**

**\*PAY-IN DAY:** The investor has to deliver the shares sold or pay cash for the shares bought. This is called the pay-in day.

**\*PAY-OUT DAY:** The Stock exchange will deliver the share or make payment to the other broker. This is called the pay-out day.

**CONTRACT NOTE:** This note contains details of the number of shares bought or sold, the price, the date and time of deal, and the brokerage charges. It should be issued within 24 hours of trading.

It is legal document 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.

**T+2 DAY:** The settlement cycle is on T+2 day on a rolling settlement basis, w.e.f. 1 April 2003. The deal has to be settled and finalised within two days of trading

### **Depository Services and DEMAT Accounts:**

**DEMAT ACCOUNT :** It refers to that account which is opened by the investors with depository participant to facilitate trading of securities in an electronic form.

**Depository:** 'Depository is an institution/organization which holds securities (e.g. shares, debentures, bonds, mutual funds etc.) in electronic form, in which trading is done.

It is a technology driven electronic storage system. It has no paper work relating to share certificates, transfer etc. All transactions of the investors are settled with greater speed, efficiency and use as all securities are entered in a book entry mode.

At present there are **two depositories in India:**

**NSDL (National Securities Depositories Ltd.)** and  
**CDSL (Central Depository Services Ltd.)**

**NSDL:** NSDL is the first and largest depository presently working in India. It was promoted as a joint venture of the IDBI, UTI, and the National Stock Exchange.

**CDSL:** Second depository was promoted by the Bombay Stock Exchange and the Bank of India.

Both these national level depositories operate through intermediaries who are electronically connected to the depository and serve as contact points with the investors and are called depository participants.

**\*The Depository Participant:** He opens the account of Investor and maintains securities records. For Example: [Zerodha https://zerodha.com](https://zerodha.com) (ONLINE BROKERAGE PLATFORM)

**\*The Investor:** He is a person who wants to deal in securities.

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

**Dematerialization:** this is the process to hold securities in an electronic form.

**Rematerialisation**, known as remat, is reverse of demat, i.e. getting physical certificates from the electronic securities.

### Working of Demat Account: (FOR READING)

1. Find depository participant (DP),
2. An account opening form and documentation (PAN card details, photograph, power of attorney)
3. The physical certificate is to be given to the DP along with a dematerialisation request form.
4. If shares are applied in a public offer, simple details of DP and demat account are to be given
5. If shares are to be sold through a broker, the DP is to be instructed to debit the account with the number of shares.
6. The broker then gives instruction to his DP for delivery of the shares to the stock exchange.
7. The broker then receives payment and pay the person for the shares sold.
8. All these transactions are to be completed within 2 days.

## **Benefits of Demat Account (FOR READING)**

Reduces paper work.

No delay in transfer.

Exemption of stamp duty/ save paper work.

Speedy settlement.

Attract foreign investors

## **Trading Procedure on a Stock Exchange:**

1. **Selection of Broker:** A registered broker is selected .

Investors has to

- a. **Fill a client registration form**
  - b. **Sign broker client agreement**
  - c. Submit PAN Permanent account number, date of birth, address, qualification, resident/NRI, Details of bank account, details of depository account, Client code number etc.
  - d. Broker will open **trading account** of investor.
2. **Open demat account/beneficiary account:** investor will **open Demat account with the help of depository participant** to hold securities in **electronic form**.
  3. **Placing the order:** The investor **place the order** about **type and number of securities** he wants to buy or sell.
  4. **Connecting to main stock exchange:** broker search and **match the availability** of securities at the price told by investors.
  5. **Executing the order:** The broker will buy or sell the securities as per the instructions of the investor and he will issue a **trade confirmation slip**.
  6. **Issuance of contract note:** after **execution of order broker will issue contract note to investor with in 24 hours**. **Contract note includes number of securities bought/sold, its price, date and time of deal and brokerage charges**.
  7. **Delivery of shares by investor:** if investor is selling his securities, he will handover share certificate to broker.  
**Payment of money by investor:** if investor has purchased securities he has to pay money.
  8. **Settlement of deal Before T+ 2:** Settlement of deal must be **within two days of trading** of securities.
  9. **Delivery of securities by stock exchange :** The broker will make delivery of securities to the investor who has purchased. **Payment of money by stock exchange to investor who sold securities:** The stock exchange will pay money to investor.
  10. **Delivery of securities in Demat account:** The broker will make delivery of securities in demat form directly in demat account of the investor.

**Securities and Exchange Board of India (SEBI):** SEBI was established by Government of India on 12 April 1988 as an interim administrative body under Securities and Exchange Board of India Act, 1992.

**Aim:** -- **Promote orderly and healthy growth of securities market.**  
--**Protection to investors.**

**Reasons for the establishment of SEBI:**

- Price rigging, Cornering, Unofficial private placement, Unofficial premium on new issues, Violation of rules and regulations of stock exchange, Violation of rules relating to listing requirement, Delay in delivery of shares.

**Objectives of SEBI:**

1. Regulate stock exchange and promote smooth functioning.
2. To protect the rights and interests of investors, guide & educate them.
3. To prevent malpractices (stop unfair practice)
4. To regulate and develop a code of conduct. Fair practices by intermediaries like brokers, merchant bankers etc.

**FUNCTIONS OF SEBI:**

**1. REGULATORY FUNCTIONS:**

1. **Registration of brokers** and sub brokers.
2. **Registration of investment schemes** and mutual funds.
3. **Regulation of stock brokers**, portfolio exchange, underwriters and merchant bankers.
4. **Regulation of Takeover bid: Act as a watch dog:** (Proper procedure is followed by companies in case of merger and acquisition of companies).
5. **Levying of fees or other charges.**
6. **Exercise powers** given by Government of India.
7. **Conduct Inspection, Audits and Enquiries of stock exchange and intermediaries.**

**2.DEVELOPMENTAL FUNCTIONS:**

1. **Training to intermediaries/ middleman/brokers.**
2. **Conduct Research & publish useful information** to all market participants.
3. **Adapt a flexible approach to develop Capital market.**



### **3.PROTECTIVE FUNCTIONS:**

1. **Prohibition of fraudulent and unfair trade practices** like making mis- leading statements, manipulations, price rigging etc.
2. **Control insider trading:** (To prevent insiders such as Directors/ promoters from making profits in trading of securities by using secret information of price of securities)
3. **Undertake steps to protect investors**
4. **Promotes fair trade practices and provides code of conduct** in the securities market.

### **QUESTIONS FOR PRACTICE**

Question 1.

“Money market is essentially a market for short-term funds’. In the light of this statement state any three features of money market.

(CBSE, Sample Paper, 2017)

Answer:

The three features of money market are described below:

- It is a market for short term funds whose maturity period is upto one year.
- The main participants are institutional investors.
- Since the cost of securities may be high, investment in the money market requires huge capital outlay.

Question 2.

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

1. Name the function being performed by the market in the above case.
2. Name the market segment other than the capital market segment in which unsecured and short-term debt instrument are traded. Also, give any three points of difference between the two. (CBSE, OD 2017)

Answer:

1. Mobilisation of funds is the function being performed by the financial market in the above case. It performs the allocative function by mobilisation of savings and channelising them into the most productive avenues.

2. Money market is the other segment of market.

The difference between capital market and money market is given below:

S.No	Basis	Capital Market	Money Market
1.	Participants	The main participants in capital market are banks, financial institutions , corporate bodies, foreign investors and retail investors.	The main participants are institutional investors.
2.	Investment outlay	Since, the cost of securities may be low, investment can be made in the capital market can be with less capital.	Since, the cost of securities may be high, investment in the money market requires huge capital outlay.
3.	Liquidity	The securities in capital market enjoy good liquidity.	The securities in money market enjoy high liquidity as The Discount Finance House of India works as a compulsory market maker.

### Question 3.

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

1. Name the function being performed by the market in the above case.
2. Also, explain briefly three other functions performed by this market. (CBSE, Delhi 2017)

### Answer:

1. Mobilisation of funds is the function being performed by the financial market in the above case. It performs the allocative function by mobilisation of savings and channelising them into the most productive avenues.
2. The other three functions being performed by the financial market are outlined below:
  - It helps to determine the price for the financial asset in a particular financial market through the market forces of demand and supply.
  - It provides liquidity to the financial assets by providing ready markets wherein the securities can be easily converted into cash or vice versa.
  - It provides a common platform for exchange of securities thereby reducing the cost of transactions by saving time, effort and money spent by the buyers and sellers in locating each other.

#### Question 4.

ABC Ltd. issued prospectus for the subscription of its shares for Rs. 500 crores in 2008. The issue was oversubscribed by 20 times. The company issued shares to all the applicants on pro-rata basis. Later SEBI inspected the prospectus and found some misleading statement about the management of the company in it. SEBI imposed a penalty of Rs. 5 crores and banned its three executive directors for dealing in securities market for three years. Identify the function and its type performed by SEBI in the above case. (CBSE, Sample Paper, 2017)

#### Answer:

Protective function has been performed by SEBI in the above case. And the type of Protective function is Prohibition of fraudulent and unfair trade practices.

#### Question 6.

“Unicon Securities Pvt. Ltd” was established to deal in securities. It was registered as a stock broker with National Stock Exchange (NSE) and Bombay Stock Exchange (BSE) to trade in securities listed at these exchanges. It is also a depository participant with CDSL and NSDL. In the first three years, it developed its business successfully. After that the composition of Board of Directors changed. Some customers complained to the customer care centre of the company that shares purchased by them and for which the payment has been duly made, were not transferred to their D’mat Accounts by “Unicon securities Pvt. Ltd” . The executive of customer care centre promised the aggrieved customers that their shares will be transferred to their respective D’mat Accounts very soon. But the company delayed the matter and didn’t transfer the shares of the

customers to their D'mat Accounts. This eroded investors confidence and multiplied, their grievances.

1. Identify the step of trading procedure in a stock exchange which has not been followed by “Unicon Securities Pvt. Ltd” .
2. Name the Apex statutory body of capital market to whom customer can complain to redress their grievances. (CBSE, Sample Paper, 2017)

Answer:

1. The step of trading procedure in a stock exchange which has not been followed by “Unicon Securities Pvt. Ltd” is settlement i.e. the delivery of shares through the D'mat Account of the broker to D'mat account of the investors.
2. The Securities and Exchange Board of India (SEBI) is the Apex statutory body of capital market to whom customer can complain to redress their grievances.
3. The two values not followed by Unicon Security Pvt. Ltd are':
  - Truthfulness
  - Fair practices

Question 7.

Reshu's father has gifted her the shares of a large cement company with which he had been working. The securities were in physical form. She already has a bank account and does not possess any other forms of securities.

She wished to sell the shares and approached a registered broker for the purpose. Mention one mandatory detail which she will have to provide with the broker. (CBSE, Sample Paper, 2016)

Answer:

Reshu will have to give her Permanent Account Number (PAN) to the broker as it is mandatory as per law.

Question 9.

Mr. Sanjay Nehra was the Chairman of Taran Bank. The bank was earning good profits. Shareholders were happy as the bank was paying regular dividends. The market price of their shares was also steadily rising. The bank was about to announce taking over the 'Vena Bank.' Mr. Sanjay Nehra knew that the share price of Taran Bank would rise on this announcement. Being a part of the bank, he was not allowed to buy shares of the bank. He called one of his rich friends Sudhir and asked him to invest Rs.5 crores in shares of his bank promising him the capital gains. As expected, the share prices went up by 40% and the market price of Sudhir's shares was now ? 7 crores. He earned a profit of Rs. 2 crores. He gave Rs. 1 crore to Mr. Sanjay Nehra and kept Rs. 1 crore with himself. On regular inspection and by conducting enquiries of the brokers involved, the Securities and Exchange Board of India (SEBI) was able to detect this irregularity. The SEBI imposed a heavy penalty on Mr. Sanjay Nehra.

By quoting the lines from the above paragraph, identify and state any two functions that were performed by SEBI in the above case

Answer:

The two functions performed by SEBI in the given case are stated below:

- Regulatory function is being performed by SEBI: "On regular inspection and by conducting inquiries of the brokers involved."

- Protective function is performed by SEBI: “The SEBI imposed a heavy penalty on Mr. Sanjay Nehra.”

Question 10.

Mr. Vikas Mehra was the Chairman of IBM Bank. The bank was earning good profits. Shareholders were happy as the bank was paying regular dividends. The market price of their shares was also steadily rising. The bank was about to announce the taking over of ‘UK Bank’. Mr. Vikas Mehra knew that the share price of IBM Bank, would rise on this announcement. Being a part of the bank, he was not allowed to buy shares of the bank. He

called one of his rich friends Mukand and asked him to invest Rs. 4 crores in the shares of his bank promising him the capital gains.

As expected, after the announcement, the share prices went up by 50% and the market price of Mukand’s shares was now Rs. 6 crores. Mukand earned a profit of Rs. 2 crores. He gave Rs. 1 crore to Vikas Mehra and kept Rs. 1 crore with him. On regular inspection and by conducting enquiries of the brokers involved, the Securities and Exchange Board of India (SEBI) was able to detect this irregularity. SEBI imposed a heavy penalty on Vikas Mehra.

Quoting lines from the above paragraph, identify and state any two functions performed by the SEBI in the above case. (CBSE, OD 2016)

Answer:

The two functions performed by SEBI in the given case are stated below:

- Regulatory function is being performed by SEBI: “on regular inspection and conducting inquiries of the brokers involved.”
- Protective function is performed by SEBI: “The SEBI imposed heavy penalty on Mr. Vikas Mehra.”



### Question 11.

Supriya's grandmother who, was unwell, called her and gave her a gift packet. Supriya opened the packet and saw many crumpled share certificates inside. Her grandmother told her that they had been left behind by her late grandfather.

As no trading is now done in physical form, Supriya wants to know the process by adopting which she is in a position to deal with these certificates.

1. Identify and state the process.
2. Also, give two reasons to Supriya why dealing with shares in physical form has been stopped. (CBSE, Sample Paper 2015)

Answer:

1. Dematerialisation refers to the process of holding securities in electronic form.
2. The two problems of holding shares in physical form are as follows:
  - When the shares certificates are held in physical form, there is danger of loss or theft.
  - There is risk of forgery, as the buyer may be delivered fake certificates .

### Question 13.

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

1. Name and explain the money-market instrument the company can use for the above purpose.
2. What is the duration for which the company can get funds through this instrument?
3. State any other purpose for which this instrument can be used. (CBSE, Delhi 2015)

Answer:

1. Commercial Papers can be used for Bridge financing by Ganesh Steel Ltd. as they are issued by large and credit worthy companies. The instrument is in the form of an unsecured promissory note and is freely transferable by endorsement. It is sold at discount and redeemed at par.
2. Its maturity period may range from a fortnight to a year.
3. It is also used to meet the short term seasonal and working capital requirements of a business enterprise.

Question 14. Stock exchange acts as a regulator of the securities market. It creates a continuous market where the securities are bought and sold. It gives investors the chance to disinvest and reinvest. Through this process of disinvestment and reinvestment, savings get channelized into their most productive investment avenues. To ensure that the investing public gets a safe and fair deal in the market, the membership of the stock exchange is well regulated and its dealings are well defined according to the existing legal framework. It also ensures wider share of ownership by regulating new issues, better trading practices and taking effective steps in educating the public about investments. Various functions performed by the Stock Exchange are discussed in the above para. By quoting lines from the above para, state any four functions of stock exchange.

Question 15. State any two 'Developmental Functions' of Securities and Exchange Board of India.

**OR**

What is meant by 'Allocative Function' of Financial Markets?

**Question 16. These days, the development of a country is also judged by its system of transferring finance from the sector where it is in surplus to the sector where it is needed the most. To give strength to the economy, SEBI is undertaking measures to develop the capital market. In addition to this, there is another market in which unsecured and short-term debt instruments are actively traded everyday. These markets together help the savers and investors in directing the available funds into their most productive investment opportunity.**

**(a) Name the function being performed by the market in the above case.**

**(b) Name the market segment other than the capital market segment in which unsecured and short-term debt instruments are traded. Also, give any three points of difference between the two.**

**Ans.** a. The function being performed by the market is the Allocative function.

b. The market segment other than the capital market segment in which unsecured and short-term debt instruments are traded is called the Money Market. The three points of difference between the two are as follows:

Basis of difference	Capital Market	Money Market
Time Span of Securities	It mainly deals in the trading of medium and long-term securities wherein the maturity period is more than one year	It deals in the trading of short-term securities wherein the maturity period can vary from one day to a maximum of one year
Liquidity	The securities traded are liquid in nature as they are tradable on stock exchanges. However, they are less liquid in comparison to the money market securities	The securities traded are highly liquid in nature. This is because DFHI (Discount and Finance House of India) discounts money market securities and offers a ready market for them
Expected Returns	Expected returns are higher due to the possibility of capital gains in the long term and regular dividends or bonus	Expected returns are lower due to shorter duration

**Question 19. Differentiate between Capital Market and Money Market on the basis of: (3)**

- i. **Liquidity;**
- ii. **Instruments; and**
- iii. **Expected Return.**

**Ans. Difference between Capital Market and Money Market:**

Basis	Capital Market	Money Market
(i) Liquidity	Capital market securities are Comparatively less liquid.	Money market securities are Comparatively more liquid.
(ii) Instruments	Instruments traded are shares, debentures and bonds.	Instruments traded are treasury bill, commercial paper, certificates of deposit, call money and commercial bill,
(iii) Expected return	Generally yield a higher return than money market instruments.	Money market securities yield comparatively less return.

## ADDITIONAL QUESTIONS

### Question 1.

Incorporated in 1990, Raju Dairy Ltd., is one of the leading manufacturers and marketers of dairy-based branded foods in India. In the initial years, its operations were restricted only to collection and distribution of milk. But, over the years it has gained a reasonable market share by offering a diverse range of dairy based products including fresh milk, flavoured yogurt, ice creams, butter milk, cheese, ghee, milk powders etc. In order to raise capital to finance its expansion plans, Raju Dairy Ltd. has decided to approach capital market through a mix of Offer for sale of Rs. 4 crore shares and a public issue of Rs. 2 crore shares.

In context of the above case:

1. Name and explain the segment of capital market being approached by the company.
2. Identify the two methods of floatation used by the company to raise the required capital. Give one difference between them.

Answer:

1. Primary market is the segment of capital market being approached by the company. It is also known as the new issue market as the securities are issued for the first time by the companies through this market.
2. The two methods of floatation used by the company to raise the required capital are – Issue through prospectus and Offer for sale.  
In case of issue through prospectus, the company approaches the members of the general public directly by issuing a prospectus whereas in case of Offer for sale, the company approaches members of the general public indirectly through intermediaries like issuing houses, stock brokers etc.

### Question 2.

The SEBI has imposed a penalty of Rs. 7,269.5 crore on Pearls Agrotech Corporation Limited (PACL) and its four directors — Tarlochan Singh, Sukhdev Singh, Gurmeet Singh and Subrata Bhattacharya who had mobilised funds from the general public through illegal collective investment schemes in the name of purchase and development of agriculture land. While imposing the penalty, the biggest in its history, Securities and Exchange Board of India (SEBI) said the company deserved “maximum penalty” for duping the common man. Its Prevention of Fraudulent and Unfair Trade Practices Regulations provides for “severe to severe penalties” for dealing with such violations. As per SEBI norms, it can impose a penalty of Rs. 25 crore or three times of the profit made by indulging in fraudulent and unfair trade practices and in the present case, the regulator has imposed a fine equivalent to three times of the illicit gains.

In the context of the above case:

1. State the objectives of setting up SEBI.
2. Identify the type of function performed by SEBI by quoting lines from the paragraph.

Answer:

1. The objective of setting up SEBI are outlined below:
  - To prevent trading malpractice in the securities markets.
  - To protect the rights and interest of investors, and to guide and educate them.
  - To regulate and develop a code of conduct and fair practices by intermediaries like brokers, merchant bankers, etc. with a view to making them competitive and professional.
  - To regulate stock exchanges and the securities market to promote their orderly functioning.
2. Protective function is performed by SEBI: "The SEBI has imposed a penalty of Rs. 7,269.5 crore on Pearls Agrotech Corporation Limited."

Question 3.

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

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

In the context of the above case:

1. What is a Demat account?
2. Who is acting as the depository participant for Harsh?
3. Name the document that is legally enforceable and helps to settle the claims between the investor and the broker.

Answer:

1. A Demat account is an account used for holding securities in electronic form.
2. The Broking house is acting as the depository participant for Harsh.
3. A contract note is a legally enforceable document that helps to settle the claims between the investor and the broker.

Question 4.

Make Good Technologies Ltd. is one of the top suppliers of security software products and solutions in India with a market share of over 20% in the retail segment. Its customers includes people all sections of the society i.e. both households and corporates. Its unique threat detection system works to detect security threats including virus attacks in real time to protect users' IT assets across varied platforms and devices. The company has an established track record of growth and financial performance. At present the company operates only through its website. The company now intends to launch a range of computer accessories and plans to market it by opening its own retail outlets. So, the board of directors of the company have decided to only raise capital for the first time through an issue of shares, but at the same time they do not wish to get into the hassles of launching a public issue of shares.

In context of the above case:

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

Answer:

1. The company can raise finance by allotting securities to selective individuals and institutions only through Private Placement. It is a relatively economical way of raising money as it helps to save time, cost and money involved in the process of issuing securities.
2. No, the company cannot raise capital through a right issue as it is issuing securities for the first time. A rights issue is a pre-emptive right given only to the existing shareholders to subscribe to the securities of the company as per its terms and conditions.

Question 5.

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

In context of the above case:

1. Identify the two different types of capital market being referred to by quoting lines from the para.
2. State any four differences between the two different types of capital markets as identified in part (1).

Answer:

1. The two different types of capital market being referred to are-
  - Primary Market: “Arsh urged Ajay to invest in the forthcoming IPO of a blue chip companies.”
  - Secondary Market: “Ajay was inclined to buy existing securities of the other companies to build his investment portfolio.”
2. Differences between Primary Market and Secondary Market:

S. No	BASIS	PRIMARY MARKET	SECONDARY MARKET
1.	Meaning	It is the new issue market.	It is the market for old securities.
2.	Aspects	Only buying of securities takes place.	Both buying and selling of securities takes place.
3.	Price	Prices of the securities are determined by the company.	Prices of the securities are determined by the forces of demand and supply.
4.	Parties involved	It involves dealings between the company and investors	It involves dealings between the two investors.

Question 6.

Ketan won a cash prize of Rs. 20,000 in the National level Robotics Competition. On the advise of his father, he visits a nearby bank to open a Fixed deposit account in his name with the prize money. His sister Suhasini accompanied him to the bank. On reaching the bank, he notices big banners which are placed within the premises containing information about the various arrangements through which corporates may raise their capital through the bank. Being a finance graduate, Suhasini explains to Ketan that banks play the role of the financial intermediary by helping in the process of channelizing the savings of the households into the most profitable business ventures.

In context of the above case: .

1. Name another financial intermediary that helps in the process of channelizing the savings of the households into the most productive use.
2. Also, outline any two functions of another financial intermediary as identified in part (1).

Answer:

1. Financial markets is the other financial intermediary that helps in the process of channelizing the savings of the households into the most productive use.
2. The two functions of financial market are as follows:
  - It helps to determine the price for the financial asset in a particular financial market through the market forces of demand and supply.
  - It provides liquidity to the financial assets by providing ready markets wherein the securities can be converted into cash or vice versa easily.

Question 7.

Ragu works as a waiter in a five star hotel in Mumbai. While serving the customer he overhears him at the table saying that the he has made profits higher than expected by investing in securities market. So, Ragu also decides to make a nominal investment from his savings in the stock market in pursuit of higher gains.

In context of the above case:

As a financial consultant, apprise him of the steps involved in the working of a Demat system.

Answer:

Ragu will have to initiate the following steps for trading through a Demat system:

- He will have to first open a Demat account with a depository participant (DP) who may either be a bank, broker or financial services company by furnishing certain details and information about himself including PAN number, date of birth, bank account details, income details etc.
- If he plans to buy shares through a public offer he will have to give details of his Demat account, bank account etc. On allotment the shares will be directly credited to his account.
- If he decides to buy shares otherwise, he will have to instruct his broker with the details about the name of the company, number of shares, price etc. The transaction will be executed through the depository participant and he will have to make payment for them within T + 2 days.

- On contrary, whenever he decides to sell shares, he will have to instruct his broker with the details about the name of the company, number of shares, price etc. The transaction will be executed through the depository participant and his account will be debited accordingly. He will receive the payment in T + 2 days.

#### Question 8.

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

In context of the above case:

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

Answer:

1. Securities And Exchange Board of India (SEBI) regulates the working of stock exchanges in India.
2. Three functions performed by stock exchanges are as follows:
  - Ensures liquidity and marketability of existing securities by a providing a ready and continuous market for the sale and purchase of securities.
  - Helps in determining the prices of the securities through the forces of demand and supply.
  - It provides a legal framework for fair and safe dealings.
3. Two advantages of screen-based trading are as follows:
  - As the investors get access to the stock market during real time, there is complete transparency in the dealings.
  - It provides a common platform for exchange of securities thereby increasing the efficient transactions by saving time, effort and money.

#### Question 9.

Ragunath Ahuja is one of the Promoter-Director of Vishwas Ltd. The company is engaged in the real estate sector, which has recently witnessed a steady fall in its revenue and the value of its assets due to a downward trend persisting in the market in specific and the economy in general. The periodical financial results of the company were to be declared in a fortnight time. Ragunath Ahuja, being an insider, had access to unpublished price sensitive information related to it. Consequently, he sells a major portion of his holdings in an anticipation of a fall in the market price of the shares of the Company subsequent to the announcement of periodical financial results of the company. Moreover, he doesn't inform The Securities and Exchange Commission (SEC) about the dealings.

On conducting a probe, Securities and Exchange Board Of India (SEBI) finds Ragunath Ahuja guilty of insider trading. As per law, company directors, officials or any individual with a stake of 10% or more in the company are considered to be insiders and they are required to report their insider transactions within two business days of the date the transaction occurred.

In context of the above case:

1. State the purpose of setting up SEBI.
2. Identify the type of function performed by SEBI by quoting lines from the paragraph.

Answer:

1. SEBI has to be responsive to the needs of three groups, which constitute the market namely:
  - The issuers of securities so as to provide them a platform for raising capital in an easy, effective and efficient manner.
  - The investors so as to protect their interests in securities by keeping them abreast about the developments through true and appropriate information.
  - The market intermediaries in order to provide them a framework so as to enable them perform their functions effectively and efficiently.
2. Regulatory function is being performed by SEBI: "On conducting a probe Securities and Exchange Board of India (SEBI) finds Ragunath Ahuja guilty of insider trading."

#### Question 10.

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

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

is compulsory.

In context of the above case:

1. What is screen based trading?
2. Give the meaning of 'dematerialisation'. State any two of its advantages.

Answer:

1. Screen-based trading refers to the process of buying or selling securities online.
2. Dematerialisation refers to the process of holding securities in electronic form. The two advantages of Dematerialisation as follows:
  - The securities in the demat account can be offered as security to raise loans.
  - Since the shares certificates are not held in physical form, there is no danger of loss, theft or forgery.

Question 11.

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

In context of the above case:

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

Answer:

1. Bridge financing is the other name used for the funds required to meet floatation costs.
2. Commercial Papers issued by large and credit worthy companies. The instrument is in the form of an unsecured promissory note and is freely transferable by endorsement. It is sold at discount and redeemed at par. Its maturity period may range from a fortnight to a year. It is also used to meet the short term seasonal and working capital requirements of a business enterprise. For example it is used for the purpose of bridge financing.
3. Capital Market and Money Market.

Differences between Primary Market and Secondary Market:

Differences between Capital Market and Money Market:

S. No	Basis	Capital Market	Money Market
1.	Duration	It is a market for long term funds.	It is a market for short term funds whose maturity period is upto one year.
2.	Participants	The main participants in capital market are banks, financial institutions, corporate bodies, foreign investors and retail investors.	The main participants are institutional investors.
3.	Investment outlay	Since, the cost of securities may be low, investment can be made in the capital market can be with less capital.	Since the cost of securities may be high, investment in the money market requires huge capital outlay.
4.	Liquidity	The securities in capital market enjoy good liquidity.	The securities in money market enjoy high liquidity as The Discount Finance House of India works as a compulsory market maker.
5.	Risk and return	The instruments in capital market carry high risk as the expected return is high on them.	The instruments in money market carry low risk as the expected return is low on them.

Question 12.

During navratras, Varun finalises a deal to buy a new house. So, he visits a nearby branch of 'Subh Bank' to withdraw Rs. 10 lakhs from his account in order to pay the token money to the seller. In the bank he observes that a large number of customers are present to make cash with drawls, probably because it is an auspicious time to make purchases. After sometime, he overhears one of the bank



staff members telling his colleague that, “Today ‘Subh Bank’ is likely to fall short of cash and to make up for the deficit and maintain its cash reserve ratio it will have to approach another bank.”

In context of the above case:

1. Identify the instrument that ‘Subh Bank’ will use to meet its short term requirements of funds.
2. State any three feature of the instrument as identified in part (1).

Answer:

1. Call money is the instrument used by ‘Subh Bank’ to meet its short term requirements of funds.
2. Three features of call money are as follows:
  - Call money is an instrument through which one bank may borrow money from another bank to maintain the cash reserve ratio as per the guidelines of RBI.
  - Its maturity period may be from a single day to a fortnight.
  - The rate at which the interest is paid on call money is called call rate.

Question 13.

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

In the context of the above case:

1. Identify the type of function performed by SEBI.
2. Outline any two reasons for setting up SEBI.