



Unit - 10 : FINANCIAL MARKET

Summary of the Chapter

Financial Market: This market refers to that market where financial securities are exchanged.

Functions of Financial Market

1. Facilitates Price Discovery
2. Provides Liquidity Financial Assets
3. Reduce the cost of transactions
4. Mobilise savings and channelize them into most productive uses.

Types of Financial Market-

1. Capital Market –

Where long term securities are sold and purchased.

2. **Money Market :** Which deals in short term securities i.e. whose maturity period is less than 01 year.

Types of capital market-

1. Primary or new issue market
2. Secondary Market (Stock Exchange)

Primary or new issue market-It refers to that market in which securities are sold for the first time for collecting long term capital.

Secondary Market-Where already issued securities are sale and purchase,

Various methods of floating capital-

1. **Public Issue-** Under this method, the company issues a prospectus and invites the general public to purchase shares or debentures.
2. **Offer for Sale-**Under this method, Firstly the new securities are offered to an intermediary at a fixed price. They further resell the same to the general public.
3. **Private Placement-**The Company sell securities to the institutional investors or brokers instead of selling them to the general public.
4. **Right Issue –** When an existing company issues new securities, First of all it invites its existing shareholders.
5. **Electronic Initial Public offer (e-IPO's) –** Under this method ,companies issue their securities through the electronic medium (i.e. internet)

Money Market –This is the market in which short term securities are trades.

Instruments:

- | | |
|---------------------------------|---------------------------------|
| 1. Treasury Bill (T-bills) | 2. Commercial Paper |
| 3. Call Money: | 4. Certificate of Deposit (CD): |
| 5. Commercial Bill (Trade Bill) | |



BUSINESS STUDIES

Depository:- A Depository is an institution which holds the shares of an investor in electronic form. It acts as a bank where investors can open a securities account and deposit the electronic form of securities. At present, there are two depository institutions in India:

NSDL – National Securities Depository Limited.

CDSL – Central Depository Services Limited.

D’MAT/Demat Account:- D’Mat Account refers to that account which is opened by the investors with depository participant to facilitate trading in shares.

Stock exchange- The stock exchange is a market in which existing securities are bought and sold.

Functions of stock exchange

1. Providing Liquidity and Marketability to Existing Securities
2. Pricing of Securities:
3. Safety of Transactions:
4. Contributes to Economic Growth:
5. Spreading of Equity Cult:
6. Providing Scope for Speculation:

Trading procedure in the stock exchange-

1. Selection of broker
2. Opening Demat Account
3. Placing the order
4. Executing the order
5. Settlement

SEBI (The Securities Exchange Board of India)- The Securities Exchange Board of India was established in 1992 to protect the interest of investors and to regulate and control the trading of financial securities.

Objectives of SEBI-

1. **Regulation of stock exchange-** It regulates stock exchanges so that efficient services may be provided to all the parties operating there.
2. **Protection to the Investors-** SEBI protects interest of investors from wrong information given by the company and reducing the risk of delivery and payment etc
3. **Checking the Insider Trading-**

Functions of SEBI-

1. Regulatory Functions
2. Development Function
3. Protective Functions



Very Short Type Questions – (1 Mark)

Q.1. You are a finance expert. One of your friends come to you and tells you that the capital market and the money are one and the same, whereas you differ with him. How would you convince him? Give any four reasons.

Ans. I will convince my friend by telling him the point of difference between capital market and money market.

Q.2. “All securities can be traded in the stock exchange.” Do you agree?

Ans. No, I do not agree with the given statement. Securities of only those companies can be traded in the stock exchange, which have completed its listing requirement.

Q.3. Why do money market instrument are more liquid as compare to capital market instrument?

Ans. Money market instrument are more liquid as compare to capital market instrument due to presence of Discount Finance House of India (DFHI) in money market. DFHI provides a ready market for money market instrument and that is why, these instruments enjoy higher liquidity.

Q.4) Due to various malpractices and exploitation of investors in the securities market, the Indian Government established a separate regulatory body to protect the investors and to develop and regulate the securities market. Identify the regulatory body set up by the government.

Ans. Securities and Exchange Board of India (SEBI).

Q.5. Supriya’s grandmother who was unwell, called her and gave her a gift packet. Supriya opened the packet and saw many crumpled share certificate inside. Her grandmother told her that they had been left behind by her late grandmother. 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.

(i) Identify and state the process.

(ii) Also give two reasons to Supriya why dealing with shares in physical form had been stopped.

Ans. (i) Dematerialization: It is a process where securities held by the investors in physical form are cancelled and the investors give an electronic entry or number so that she/he holds it as an electronic balance in an account.

(ii) Problems with dealing in physical form: (a) Theft; (b) Transfer delays.

Q.6. “Financial markets reduces the cost of transactions.” Comment.

Ans. Financial markets provide valuable information about securities being traded in the market, which saves time, efforts and money of both buyers and sellers of financial assets in finding each other.



BUSINESS STUDIES

Q.7. What is meant by 'Allocative Function' performed by financial market?

Ans.. Allocative function of financial market refers to linking the savers and investors by mobilizing funds between them.

Q.8. Which bearer document is issued by a bank against deposit kept by the companies and institutions for a short period?

Ans. Certificate of Deposit.

Q.9. Name the two methods of floating new issues in the primary market.

Ans. (I) Offer through prospectus; (ii) Private Placement.

Q.10. What is meant by right issue?

Ans. Right issue refers to a method in which company offers the new shares to its existing shareholders in proportion of shares already held by them.

Q.12. State any one objective of setting up of Securities and Exchange Board of India (SEBI).

Ans. To regulate stock exchange to promote their orderly functioning.

Short Answer Type Question (3 or 4 marks)

Q1. Mr. Rohit is a holder of financial securities in Futura limited. He wants to sell his securities to purchase new securities of another company. You are required to suggest him the markets where he can sell his securities and describe the concept. Explain two function of that market.

Ans. Financial Market: This market refers to that market where financial securities are exchanged.

Functions of Financial Market

- 1. Facilitates Price Discovery:** - The price of any goods or services is determined by the forces of demand and supply. Like goods and services, the investors also try to discover the price of their securities. The financial market is helpful to the investors in giving them proper price.
- 2. Provides Liquidity Financial Assets:-** This is market where the buyers and the sellers of all the securities are available all the times. This is a reason that it provides liquidity securities. It means that they invest their money, whenever they desire, in securities through the medium of financial market. They can also convert their investment into money whenever they so desire.

Q 2. What do you mean by the SEBI? Explain its objectives.

Ans. The Securities Exchange Board of India was established in 1992 to protect the interest of investors and to regulate and control the trading of financial securities.

Objectives of SEBI-

- 1. Regulation of stock exchange-**It regulate stock exchanges so that efficient services may be provided to all the parties operating there.



2. **Protection to the Investors**-SEBI protects interest of investors from wrong information given by the company and reducing the risk of delivery and payment etc
3. **Checking the Insider Trading**-It means the buying and selling of securities by those persons(Directors, Promoters etc) who have some secret information about the company and who wish to take advantages of this secret information. **SEBI** check insider trading.

Q 3: What is Primary or New issue market? Explain various methods of floating capital.

Ans. It refers to that market in which securities are sold for the first time for collecting long term capital.

Various methods of floating capital.-

6. **Public Issue**- Under this method, the company issues a prospectus and invites the general public to purchase shares or debentures.
7. **Offer for Sale**-Under this method, Firstly the new securities are offered to an intermediary at a fixed price. They further resell the same to the general public.
8. **Private Placement**-The company sell securities to the institutional investors or brokers instead of selling them to the general public.
9. **Right Issue** – When an existing company issues new securities, First of all it invites its existing shareholders.
10. **Electronic Initial Public offer (e-IPO's)** – Under this method ,companies issue their securities through the electronic medium (i.e. internet)

Q 4. What do you mean by the Depository? Explain

Ans. Depository:-A Depository is an institution which holds the shares of an investor in electronic form. It act as bank where investors can open a securities account and deposit the electronic form of securities .At present, there are two depository institutions in India:

1. NSDL – National Securities Depository Limited.
2. CDSL – Central Depository Services Limited.

Q 5. What do mean by the D' Mat account? Explain.

Ans. D'Mat (Dematerialization) Account refers to that account which is opened by the investors with depository participant to facilitate trading in shares.

Q 6. What are the functions of SEBI? Explain.

Ans. Functions of SEBI-

- (i) **Regulatory Functions**-These functions aim to regulate the functioning of the stock exchange. It includes registration of brokers, Investment schemes, and regulation of stock bankers.



- (ii) **Development Function-** These functions aim to promote the development of stock exchange. It includes registration of brokers, Investment schemes, and regulation of stock bankers. It includes training of intermediaries of the securities market.
- (iii) **Protective Functions-** These functions aim to protect interest of investors, controlling insider trading, unfair trade practice etc.

Long Answer type Questions (5 or 6 marks)

Q 1. Which financial market meets the short term financial requirement of business? Identify concept and Explain instruments of that market.

Ans. **Money Market**

Instruments:

1. **Treasury Bill (T-bills):** It is basically an instrument of short-term borrowing by the Government of India maturing in less than one year. They are also known as Zero Coupon Bonds.
2. **Commercial Paper:** It is a short-term unsecured promissory note, negotiable and transferable by endorsement and delivery with a fixed maturity period. It is issued by large and creditworthy companies to raise short-term funds at lower rates of interest than market rates. It usually has a maturity period of 15 days to one year.
3. **Call Money:** It is a short-term finance repayable on demand, with a maturity period of one day to fifteen days, used for inter-bank transactions. It is a method by which banks borrow from each other to be able to maintain the cash reserve ratio.
4. **Certificate of Deposit (CD):** It is an unsecured, negotiable short-term instrument in bearer form, issued by commercial banks and development financial institutions. It can be issued to individuals, corporations and companies.
5. **Commercial Bill (Trade Bill):** It is a short-term, negotiable, self-liquidating instrument which is used to finance the credit sales of firms. The bill can be discounted with a bank if the seller (drawer) needs funds before the bill maturity.

Q 2. Give the meaning and definition of Stock exchange? Explain the functions of stock exchange.

Ans. **Meaning-** The stock exchange is a market where existing securities are bought and sold.

Definition- The securities contract (regulation) act, 1956 defines “a stock exchange as an association, organization, body of individuals, whether incorporated or not, established for the purpose of assisting, regulating and controlling of business in buying, selling and dealing in securities”.

Functions of stock exchange

1. **Providing Liquidity and Marketability to Existing Securities:** It gives investors the chance to disinvest and re-invest. This provides both liquidity and easy marketability to already existing securities in the market.



2. **Pricing of Securities:** Share prices on a stock exchange are determined by the forces of demand and supply. A stock exchange is a mechanism of constant valuation through which the prices of securities are determined.
3. **Safety of Transactions:** The membership of a stock exchange is well regulated and its dealings are well defined according to the existing legal frame work. This ensures that the investing public gets a safe and fair deal on the market.
4. **Contributes to Economic Growth:** A stock exchange is a market in which existing securities are re-sold or traded. Through this process of disinvestment and re-investment savings get channelized into their most productive investment avenues. This leads to capital formation and economic growth.
5. **Spreading of Equity Cult:** The exchange can play a vital role in ensuring wider share ownership by regulating new issues, better trading practices and taking effective steps in educating the public about investments.
6. **Providing Scope for Speculation:** The stock exchange provides sufficient scope within in the provisions of law for speculative activity in a restricted and controlled manner.

Q 3. Describe procedure to trade securities in a Stock Exchange.

Ans. Trading Procedure:-

The procedure for purchase and sale of securities in a stock exchange involves the following steps:

1. Selection of broker

The first step is to select a broker who will buy/sell securities on behalf of the investor. This is necessary because trading of securities can only be done through SEBI registered brokers who are the members of a stock exchange. Brokers may be individual, partnership firms or corporate books. The broker charges brokerage / commission for his services.

2. Opening Demat account

The next step is to open a Demat account. Demat (Dematerialized) account refers to an account which an Indian citizen must open with the depository participant (banks, stock, brokers) to trade in listed securities in electronic form.

The securities are held in the electronic form by a depository. At present, there are two depositories in India **NSDL** (National Securities Depository Ltd.) and **CDSL** (Central Depository Services Ltd.)

Depository interacts with the investors through depository participants. Your Depository Participant will maintain your securities account balances and intimate to you the status of your holding from time to time.

**3. Placing the order**

The next step is to place the order with the broker. The order can be communicated to the broker either personally or through telephone, cell phone, e-mail etc.

The instructions should specify the securities to be bought or sold and the price range within which the order is to be executed. Only the securities of listed companies can be traded on the stock exchange.

4. Executing the order

According to the instructions of the investor, the broker buys or sells securities.

The broker then issues a contract note. A copy of the contract note is sent to the client. The contract note contains the name and the price of the securities, names of the parties, brokerage charged. It is signed by the broker.

5. Settlement

This is the last stage in the trading of securities done by the brokers on behalf of their clients. The mode of settlement depends upon the nature of the contract.

Equity spot market follows a T+2 rolling settlement. This means that any trade taking place on Monday gets settled by Wednesday. All trading on stock exchanges takes place between 9:55 am and 3:30 pm. Indian Standard Time, Monday to Friday. Delivery of shares must be made in dematerialized form, and each exchange has its own clearing house, which assumes all settlement risk.