Indian Capital Market

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For MGU B Com Students

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PREFACE

As everyone knows, Capital Market is a concept that entirely differs from the concept of a commodity market. Business needs finance for it activities. Huge amount of capital is required for the business, where business loans are not at all a reliable source of finance.

As per SEBI reports, Indian companies raised Rs.1.1 lakh crore in the year 2020-2021 from the primary market as share capital. Mutual Funds in India have collected Rs.86.39 Lakh Crore in 2020-2021. Net foreign Portfolio investment in the year 2020-21 was Rs.2.67 Lakh crores. These figures indicate the power and importance of our capital market

This text book on 'Indian Capital Management', does not cover the actual observations or experiences. It is a text book of reference for the undergraduate students of Indian Universities. A syllabus oriented book has got its own limitations. The author has referred mainly the websites of SEBI, BSE, NSE, and other stock exchanges. Many other printed and e-resources are also used to get inference on the topics covered.

The E-Book intended for free circulation, though priced. The print version, if required cannot be given without covering the cost of book and distribution.

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Module I

Indian Financial System

A good financial system is essential for the economic development of a nation. The system consists of agencies involved in the creation, mobilization and distribution of monetary resources of a nation. Indian financial system has two sectors- Formal and informal.

I. Informal/Unorganised/ Sector:

Informal system consists of local money lenders, 'Nidhis' or 'Chit funds', indigenous banks, traders, land loads and individuals. Their functions are unorganized and unregulated. Very high rate of interest, undesirable rules and regulations and exploitation are the main drawbacks of the sector. But they are more popular in the rural segment especially among the poor and uneducated due to its flexibility, proximity and convenience. In many places they are known as 'blade banks'

II. Formal/Organised Sector:

Formal system has mainly four components: financial markets, financial institutions, financial instruments and financial services.

(1) Financial Market:-

(a) Money Market

(b) Capital Market

(2) Financial Institutions:-

(a) Regulatory Institutions

(b) Banking Institutions and

(c) Nonbanking Financial Institutions

(3) Financial Instruments:-

(a) Primary or Direct Instruments

(b) Secondary or Indirect Instruments

(4) Financial Services:-

Banking, Insurance, Merchant banking, Credit rating, Venture Capital, etc.

Role and Functions of Financial System.

1) Mobilisation of savings
2) Transfer of savings
3) Investment of savings
4) Re-allocating Old savings
5) Arranging the payment system
6) Ensuring liquidity
7) Improving Corporate Governance
8) Managing uncertainty and risk

9) Financial innovation

10) Globalising the economy

I. **Financial Market:-**

It is a collection of markets for long term and short term funds. The main players of the financial market are Borrowers of funds, Suppliers of funds and intermediaries. Financial markets are broadly classified into two –

A. Money Market

B. Capital Market.

A. Money Market:

Money market is a market of short term funds with a maturity period up to one year. It is a market for short term debt instruments with a maturity period of less than one year. It is a wholesale market of short term debt instruments. Major players are Central and state governments, RBI, Mutual Funds, Commercial banks, Public and private sector undertakings, FIIs, DIIs, Discounts Houses and NBFCs are the major players.

Features of Money Market:

(1) It is a market of short term funds with a maturity period up to one year.

(2) It is a market for short term debt instruments with a maturity period of less than one year.

(3) It is a wholesale market of short term debt instruments.

(4) It is a mechanism for evening out short term surplus and deficit of funds.

(5) It is a need based market- Demand and supply determines the terms and conditions.

(6) It helps to keep an optimum balance between liquidity and profitability.

(7) It helps RBI to regulate supply of money.

(8) It provides a platform for the RBI to influence the banking system, money circulation, interest rate, etc.

(9) It provides a platform for the RBI to intervene to control inflation and deflation.

(10) Major players are Central and state governments, RBI, Mutual Funds, Commercial banks, Public and private sector undertakings, FIIs, DIIs, Discounts Houses and NBFCs are the major players.

Money Market Instruments

(Sub Markets/ Components of money market)

Call money, T-Bills, CPs, CDs, CBs, CBLO, ICDs, BA, MMMFs, Repo and Reverse Repo are the major types of instruments used in the Money Market.

1. **Call money Market:-**

It is a whole sale market for very short term funds. They are highly liquid, because money lent can be called back at any time. It is basically an interbank money market. The dealings are mainly to maintain the statutory requirements of CRR and SLR stipulated by RBI. From 2005 only commercial banks, foreign banks, cooperative banks and primary dealers are allowed to deal in the money market. There is no need of any securities.

Lenders and borrowers contact each other and fix the amount of loan and interest rate. The interest rate is called **'call rate' or 'call money rate'**. The lender issues cheque (Banker Pay order) in favor of the borrower. The cheque will be cleared by the RBI. The borrower issues a borrowing receipt to the lender. Call money operations are possible through Discount and finance Houses.

Call money market has two types of transactions – Money at call and Money at short notice.

(a) **Money at Call or Call Money:-**

Call money is a loan given for a period of one day (24 hours). It is repayable on call – immediately on demand. It is next to cash in liquidity.

(b) **Money at Short Notice or Notice Money:-** Notice money is a loan given for a period of 2 to 14 days.

Term money:**-** Money lend for more than 14 days in the money market is called term money.

2. Treasury Bills (T-Bills)

They are money market instruments used by the central Govt. to fill the deficit between receipts and expenditure. T-Bills are issued by the RBI for the Central Govt. They are issued at a discount to the face value. The return of the investor is Face Value minus Issue Price.

They are negotiable instruments. They are highly liquid because there is an active secondary market for T-Bills. They are eligible for inclusion in the securities for SLR (Statutory Liquidity Ratio). It is a tax free source of investment. They are govt. securities and risk free. They are issued in multiples of Rs. 25’000/- Anybody can purchase T-Bills. Maturity period are 91 days, 182 days and 364 days.

They are mainly sold through auction system. Auctions are conducted by RBI in Mumbai. Two types of auctions are French Auction and Dutch Auction.

French Auction: It is multiple price based system of auction. Each bidder on or above cut off price will get T-Bills at the price quoted by him.

Dutch Auction: It is uniform price based system of auction. Each bidder on or above cut off price will get T-Bills at the cut off price

Non auction T-Bills: They are issued by RBI to state governments, Non-Government Provident Funds, and other central banks to accommodate their surplus funds.

3. Certificate of Deposits (CDs).

They are issued by commercial banks and Development Financial Institutions. CDs are similar to FDs of banks. They are negotiable instruments and transferable in nature. They can be traded in secondary money market. They are generally unsecured. CDs are issued in multiples of one lakh. The maturity period is one week to one year. Interest rate is generally high. They are introduced in 1989.

4. Commercial Papers (CPs).

CPs are short term debt instruments issued by credit worthy companies. They are promissory notes issued at a discount. They are issued in multiples of 5lakhs. Maturity period is between 7days and one year. Banks are the major subscribers of CPs. They are placed privately with the investors through merchant bankers. Under writing is not permitted. Rating by a recognized rating company is must for the issue of CPs. Every issue must be reported to RBI. CPs are introduced in 1990.

5. Commercial Bills (CBs).

A trade bill (Bill of Exchange) is a short term negotiable instrument drawn by a seller on the buyer. When a trade bill is accepted and discounted by a commercial bank, it becomes a Commercial bill. Commercial banks can get it rediscounted with RBI or other FIs to meet short term fund requirements. Generally the maturity period is 30, 60 or 90.

6. Collateralised Borrowing and Lending Obligations (CBLO).

It is a money market instrument developed by CCIL (Clearing Corporation of Indi Ltd.). CBLO enables the financial institution to lend or borrow money on the support of documents vested with the CCIL. They are transferable short term instruments backed by gilt edged securities.

Gilt Edged Securities: Securities issued by Government or a company with strong record of consistent earning.

7. Inter Corporate Deposits (ICDs):

It represents unsecured loan given by a company to another company. Generally a high rated company lends funds to lower rated companies at a higher rate of interest.

8. Bankers Acceptance (BA)

It is a money market instrument in international trade. BA is used widely where the credit worthiness of the buyer is unknown to the seller. It is a short term negotiable instrument created by a firm and guaranteed by a bank. It is an order by the drawer to the bank to pay a specified sum of money to the person or bearer. When it is accepted by the bank it becomes primary and unconditional liability of the bank. There after it is eligible for being traded in the secondary market at a discount from face value.

9. Money Market Mutual Funds (MMMFs).

They are just like other Mutual Funds, but MMMFs are invested only in money market securities. It enables small and medium investors to indirectly participate in the money market. They are more liquid in nature.

10. Primary Dealer (PDs):

The system of PDs are introduced by RBI in 1995. Banks and other financial institutions can apply for to get the status of Primary Dealer. They act as market intermediaries to govt. They directly deal with the central bank and the govt. for financial market. They are regarded as merchant bankers to govt. securities.

11. Repo and Reverse Repo:

Repo means Repurchase Offer. It is a contract between RBI and Banks for the sale of a security with a commitment to repurchase the same at a specified price on a specified date in future. For eg. SBI sells Commercial bills to RBI . This is repo for SBI.

> **Repo rate**: The difference between the original sale price and repurchase order is called 'repo rate' In other words it is the rate at which banks borrow from RBI.

Reverse Repo: RBI sells securities received through Repo, to another commercial banks with an offer to buy back the same on the settlement date.

> **Reverse Repo rate:** It is the rate which RBI borrow from banks.

C. **Capital Market:**

Foreign Exchange Market: Foreign exchange is made available by RBI, authorized dealers in foreign currency, money changers, foreign banks, exporters, importers, EXIM banks and exchange banks deals in foreign currency.

Gild Edged Market: Market for govt. and semi govt. securities.

Capital Market

The market for the issue and trading of corporate equity and long term debt securities are called capital market. In other words it is the market for shares and debentures). It is a market for Long Term Funds (More than one year)

Capital Market = Primary Market + Secondary Market.

Capital Market

= Industrial Securities Mkt + Govt. Securities Mkt

I. **Industrial Securities Market**: It is the market for ownership Securities and creditorship Securities

II. **Govt. Securities Market:** It is the market for government securities (G-Sec). It includes Short term ‘treasury bills’ and long term ‘Dated Securities’ - TBs and Bonds. These bonds are issued for meeting the huge fund required for govt. to invest in social and economic projects for development.

1. Industrial Securities Market:

It is the market for shares and debentures of industrial companies. It consists of:

(A) Ownership Securities-
Equity Share & Preference Share
(B) Creditorship Securities-
Debentures and Bonds
(C) Foreign Market Tapping Instruments (DRs)

A. Ownership Securities:

These securities contribute to the share capital of the company. They include equity shares and preference shares.

(a) **Equity Shares**: There are of two types of equity shares.

(i) Equity shares with voting rights

(ii) Equity shares with differential rights as to dividend, voting or otherwise.

Classification of equity shares on the basis of Issue:

On the basis of issue, equity shares are classified into bonus shares, sweet equity shares, right share, equity shares with detachable warrants (right to purchase additional shares at a fixed price)

(b) **Preference Shares**:
They are shares which has a preferential right over equity shares regarding:

(a) Payment of dividend during life time, and
(b) Repayment of capital on liquidation.

Types of Preference Shares

1. Cumulative Preference Shares
2. Non-cumulative Preference Shares
3. Participating Preference Shares
4. Non-participating Preference Shares
5. Convertible Preference Shares
6. Non-convertible Preference Shares
7. Redeemable Preference Shares
8. Irredeemable Preference Shares

B. Creditorship Securities:

There is no significant difference between bonds and debentures. In India the term ‘bond’ is generally used to indicate securities issued by govt. But now-a-days companies also use the term ‘bond’. Bonds are considered as more secure than debenture. Debentures can be of different types:

(a) Secured/Mortgage Debenture: Secured by any assets of the company.

(b) Unsecured Debenture.

(c) Redeemable Debenture: Those debentures which are redeemable after a fixed period.

(d) Irredeemable/Perpetual debenture

(e) Convertible Debenture: Those debentures which can be converted into shares after a fixed period.

(f) Non-convertible debenture

(g) Bearer bonds: Company doesn't keep register of holders.

(h) Registered Bonds: Company keeps register of holders.

(i) Zero Coupon (Deep Discount) Bonds: Issued at a discounted price (less than fv) and redeemed at face value. Generally no interest (a coupon) is paid.

(j) Sinking Fund Bonds: A bond issue for which the issuer is required to establish a sinking fund to provide for the orderly retirement of the bonds.

(k) Junk Bonds: High risk, high return bonds.

(l) Bunny Bonds: Holders have the option to reinvest the interest coupons as bonds with same conditions.

(m) Secured Premium Notes (SPN):

It combines the feature of both debt and equity. SPNs enables the holder to covert the detachable warrants into equity shares.

(n) Privately Placed Bonds: Sold directly to a limited number of institutional investors.

(o) Floating rate Bonds: Interest rate is not fixed. It varies as per market rate of interest.

C. Foreign Market Tapping Instruments (DRs)

They are instruments used to collect capital from the foreign market. ADR and GDR are the two types of such securities.

Depositories: A depository is an institution that holds and assists in the trading of securities. Depository Receipt (DR) is a dollar denominated negotiable instrument issued by a Depository. DRs are used by the company to raise capital from the foreign market. DRs are issued against shares deposited by the issuer company. Thus DRs represent a particular group of shares. DR holder has the right to receive dividend and other benefits declared by the company. They do not have voting rights. DRs facilitates cross border investment. Depositories minimises transaction cost.

(a) American Depository Receipts (ADR):

They are US Dollar denominated depository receipts issued in the American capital market. They are listed in the US Stock Exchanges. It helps to raise capital from the American capital market.

(b) Global Depository Receipts (GDR):

They are depository receipts issued in more than one country. They are denominated in either U.S. dollars or Euros. GDRs are offered for sale globally. It helps to raise capital from the global capital market.

(c) Indian Depository Receipt- IDR

IDR is a Depository Receipt denominated in Indian Rupees. They are created by an Indian Depository. It enables the foreign companies to raise funds from the Indian capital Markets.

II. Govt. Securities Market:

It is the market for government securities (G-sec). They are called Gilt Edged Securities or Risk Free Securities. It includes:

(a) Central Government: Include both Short term 'treasury bills' and long term 'Dated Securities'.

(b) State Governments: Include only long term 'Dated Securities' - Bonds

1. **Partly Tradable Securities**

(Savings Instruments) **-** By Central Govt.

Saving Bonds, National Savings Certificates – NSC, Special Securities – Oil Bonds, Food Corporation of India bonds, Fertiliser bonds, Power Bonds, etc

2. Fully Tradable Securities (By all govts)

(a) Fixed Rate Bonds

(b) Floating Rate Bonds

(c) Zero Coupon Bonds: Issued at a discounted price (less than fv) and redeemed at face value. Generally no interest (a coupon) is paid.

(d) Capital Indexed Bonds: Base payment rises and falls with the Consumer Price Index - CPI)

(e) Bonds with Call option: Buy back option- Option to redeem before the maturity.

(f) Bonds with Put option: Sell back to issuer- Option to sell back the bonds to the issuer before maturity.

(g) STRIPS – Separate Trading of Registered Interest and Principal Securities.

(h) State Development Loans (SDLs): bonds issued by state governments to fund their fiscal deficit. SDL issues are managed by the RBI

(i) **Sovereign Gold Bonds** are Government securities denominated in multiples of gram(s) of gold. They are substitute for investment in physical gold. These Bonds are issued by RBI on behalf of the Govt of

India and are traded on stock exchange. The bond bears an interest at the rate of 2.50% (fixed rate) per annum on the nominal value. The market price of 24carat gold will be the redemption price.

Method of Issuing G-Secs

a. Issued through 'E auctions' by the RBI.

b. Trading through Primary Dealers.

c. Tradable in SEs

Major Players in the G-Secs

1. Primary Dealers
2. Commercial banks
3. Institutional Investors: They include Insurance Companies, Mutual Funds, Provident Funds, Pension funds, etc.
4. Foreign Institutional Investors (FIIs)

Advantages of Govt. Securities:

1. Maximum safety.
2. Wide range of maturity periods- 91 days to 30 years.
3. Liquidity through SEs.
4. Active Secondary Market.

5. Can be held in Demat form.
6. Can be used as collateral security to borrow funds.
7. Transparent price dissemination mechanism.
8. D Vs P system of trading – Delivery Vs Payment (Simultaneous transfer of securities and money)

Money Market Vs Capital Market

Money Market	Capital Market
1. Maturity period is less than one year	1. Maturity period is more than one year.
2. Instruments have high denomination	2. Instruments have small face value.
3. Large Volume of transaction	3. Space of small, medium and large volume
4. Institutional Market	4. Institutions and Individuals.
5. Contacts through phone and electronic Media	5. Contacts through SEs and Brokers.
6. Low Risk	6. High Risk
7. Assured Return	7. Return is not guaranteed.
8. Less speculative	8. More Speculative

Role and functions of Indian financial System

1. Mobilization of savings of variant groups
2. Transfer of savings
3. Investment of savings
4. Re-allocation of old savings
5. Ensuring liquidity
6. Managing uncertainty and risk
7. Financial engineering
   (New and improved financial instruments)
8. Financial innovation
9. Globalisation of economy
10. Investment, Reinvestment and disinvestment of Financial Assets.
11. Extension of the coverage of the securities market
12. Provide long term equity capital
13. Provide small, medium and long term debt.

Module II
SEBI

Regulatory Agencies

Following are the regulatory agencies of Indian Securities Market.

1. DEA: Department of Economic Affairs
2. DCA: Department of Company Affairs
3. RBI: Reserve Bank of India
4. SEBI: Securities and Exchange Board of India

Main Acts Governing Indian Securities Market.

1. Companies Act 1956
2. Companies Act 2013
3. SEBI Act 1992
4. Depositories Act 1996
5. Prevention of Money Laundering Act 2002

History- Control of Capital Market

- 1947- Controlled by 'Capital Issues (Control) Act

Admin - controller of capital issues

- 1956 onwards-
  - (a)The Companies Act
  - (b) Securities Contract Regulation Act (SCRA)

SEBI- The Securities and Exchange Board of India

Special Act : The Securities and Exchange Board of India Act, 1992.

Formation :1992.

HQ : Mumbai

Regional Offices : New Delhi, Kolkata, Ahmedabad and Chennai.

Immediate Reason for formation of SEBI:

1990-92 (Harshat Mehta Scam)

Objectives of SEBI

1. To protect the interests of investors in securities Market.
2. To promote the growth and development of Securities Market.
3. To regulate the securities market.
4. To discharge responsibilities connected with the above functions.
5. Develop and improve the quality of the Indian Securities Market
6. Improve transparency in the primary market.

7. Modernisation of Stock Exchanges.
8. To conduct investor education and training programs.

SEBI- Organisation Structure

SEBI management is vested in the hands of a Management Board of 9 members. It has 17 major departments.

Management of the Board. sec 4. (1)

The Board shall consist of the following 9 members:-

(a) **A** Chairman

(b) **Two** members from amongst the officials of the Ministry of Finance and administration.

(c) **One** member from the officials of the RBI

(d) **Five** other members of whom at least three shall be the Whole-Time members to be appointed by the central Government.

Major Departments of SEBI

1. Market Intermediaries Regulation and Supervision
2. Market Regulation
3. Derivatives and New Products
4. Legal Affairs
5. Corporation Finance
6. Office of the Investor Assistance and Education
7. General Service

8. Parliament Questions Cell
9. Enforcement Cell
10. Investigations
11. Information Technology
12. Investment Management
13. Economic and Policy Analysis
14. Division of Collective Investment Scheme
15. Regional Offices
16. Vigilance Cell
17. Board
18. Matters

Functions of SEBI

1. Regulate all segments of the capital market.
2. Supervise every activity of the capital market.
3. Registration of market intermediaries such as stock brokers, sub brokers, share transfer agents, bankers to the issue, registrars to the issue, merchant bankers, underwriters, etc.
4. Regulation of market intermediaries.
5. Registration and regulation of depositories, DPs, foreign institutional investors, credit rating agencies, etc.
6. Registration and regulation of venture capital funds, MFs, etc.
7. Promotion and control of self regulatory organisations.

8. Prohibiting fraudulent and unfair trade practices.
9. Prohibiting inside trading in securities.
10. Conducting Market Researches for the above purposes.

Powers of SEBI

1. SEBI is the apex body in the capital market.
2. SEBI has the powers of a civil court in respect of matters connected with securities market.
3. Frame rules, guidelines and regulations for the market participants.
4. Impose heavy penalty on violation of law.
5. Calling for information, undertaking inspection, conducting enquiries on market intermediaries.
6. Audit of Stock Exchanges, MFs, self regulatory organisations and other market intermediaries.
7. Calling for information and record from any Bank, Board or Corporation, in respect of any transaction under investigation.
8. Charging of fee and charges for discharging the functions of SEBI.
9. Inspection of any document of a listed public company.

10. Suspend the trading of any securities in a Stock Exchange.
11. Suspend any officer of any Stock Exchange.

Powers of SEBI to impose penalty

(As per Chapter VI A of SEBI Act 1992)

SEBI has the power to impose heavy penalty on violation of law. The following acts are offences to attracts penalty.

1. Failure to furnish of any document required under law
2. Failure to maintain book of accounts.
3. Failure to agreement with client by a registered intermediary.
4. Failure to redress the grievance of investors, even after called upon by SEBI.
5. Failure to obtain registration by a Mutual Fund.
6. Failure to make proper application for the listing of Mutual Fund Schemes.
7. Failure to invest money collected by a Mutual Fund in the specified manner and specified period.
8. Failure to deliver securities to the investor by a broker.
9. Failure to make payments to the investor by a broker.

10. Charging of excessive brokerage from the investor.
11. For insider trading.
12. For providing information for insider trading.

Investor Protection by SEBI

1. SEBI acts as a regulatory authority.
2. SEBI issues investor guidelines on various matters.
3. SEBI educates investors on their rights, duties, liabilities & limitations.
4. SEBI publishes reports, newsletters, bulletins, etc.
5. SEBI conducts seminars and workshops.
6. Issue of guidelines for the listing of securities.
7. Mandatory preparation of ‘offer documents’ as per SEBI guidelines.
8. Filing of draft prospectus with SEBI and approval before public issue.
9. Compulsory credit rating for issue of debt instruments.
10. Ensuring transparency in allotment of shares.
11. Effective system of handling investor grievances.
12. Ombudsman Regulation for investor and corporate grievances.

13. Guidelines for the set up of ‘Investor Protection Fund.

Module -3

Primary market

Primary Market

New Issues (Fresh Issue) Market

Primary market is a market which deals with fresh issue of securities. It is the market from which issuers of securities collect capital. Issuers of securities, investors, and intermediaries are the major players in the primary market. SEBI act as the regulatory agency.

Functions of New Issue Market:

1. Origination,
2. Underwriting,
3. Distribution

1. Origination:

Origination is the task of the issuer. It is the function through which a new investment proposal is evaluated. It includes:

a) Evaluation of Investment proposal.

   Technical, Economic and financial viability of the project.

b) Evaluation of Prevailing investment climate.

c) Financing – Type of securities (Capital structure).

d) Evaluation and selection of financial intermediaries – brokers, bankers, Merchant Bankers, underwriters, etc

2. Underwriting:

As per the SEBI guidelines, a public issue must procure at least 90% of the net offer to public. If the company fails to achieve this minimum subscription, the entire application money must be returned to the subscribers/applicants. Underwriting is the function whereby the underwriter assumes the risk of minimum subscription. It is an agreement to ensure minimum subscription.

Underwriting was compulsory up to mid 1990s. Now it is optional.

3. Distribution:

It is the function of allotment of shares. It includes:

1) Processing of application.

2) Allotment of shares.

   a. Distribution of securities to ultimate investor

   b. Crediting De-mat account with securities.

3) Refund of excess application money.

Methods of New Issue

1. Public Issue
    a) Initial Public Offer (IPO)
    b) Follow-on-Public Offer (FPO)
2. Private Placement
    a. Preferential Allotment
    b. Qualified Institutional Placement- (QIP)
3. Right Issue
4. Employee Stock Option Plan – ESOP
5. Sweet Equity Share issue
6. Combined Issue
7. Bonus Issue
8. Issue by Conversion

I. Public Issue

"Public Issue" means an invitation by a company to public to subscribe to the securities offered through a prospectus. An offer of securities made to the public, ie when the issue is made to 50 or more persons.SEBI classification of public issue as Initial Public Offer (IPO) and Follow-on-Public Offer (FPO)

(a) Initial Public Offer (IPO): An IPO means offering the stock of a company to the public for the first time. IPOs are often issued by smaller and younger companies, but they are also done by large privately owned companies looking for public money. IPO includes:

i. Fresh issue of securities by an unlisted company

ii. Selling of securities for the first time to public -(Offer for sale)

(b) **Follow-on-Public Offer** (**FPO**)

Further / Seasoned / Subsequent Public Offer

FPO means Fresh issue by a listed company or Offer for sale by a listed company. FPO is made by a company which has already gone through the process of IPO.

Public Issue -SEBI Guidelines

SEBI issued various guidelines to protect the interest of investors.

(1) **IPO Grading**:

Every company should rate the issue, by a credit rating agency registered with SEBI. The rule is applicable for: IPO of Equity shares and Other convertible securities.

(2) **Entry Norms**:

(a) For IPO

(b) For QIB Route

(c) For FPO

(d) Appraisal Route

(3) **Promoters Contribution** and Lock-in-period:

Promoters Contribution should be at least 20% of post issue capital and there will be a minimum Lock-in-period of 3 years.

(4) **Guidelines for Allotment**

(Explained later)

(5) **Guidelines for Listing**

1. Fixed Price Public Issue: Listing within 37 days after closure of issue.
2. Book Building Issue: Listing within 3 weeks after closure of issue.

(6) **General Guidelines**

(Explained later)

Entry Norms for IPO

SEBI issued guidelines for profitability route, QIB route and FPO route separately.

(1) Entry Norm I (Profitability Route):

a) Net tangible assets in each of the preceding three full years must not be less than ₹ 3 crore.

b) Net worth of the preceding three full years must be at least ₹ 1 crore.

c) Average EBIT (pre-tax operating profit) for the last 3 out of 5 years should not be less than ₹ 15 crore.

d) If there was a change in the company's name, at least 50% of the revenue for preceding one year should be from the new activity denoted by the new name.

e) The issue size should not exceed 5 times of the pre-issue net worth (T. assets-External Liabilities).

(2) Entry Norm II (QIB Route):

For IPO and FPO

a) Issue shall be made through book building route.

b) At least 75% of net offer to the public must be allotted to the Qualified Institutional Buyers.

c) Compulsory refund of the subscription money, if the minimum subscription of QIBs is not attained.

(3) Entry Norms for FPO

(Issue by a listed issuer)

a) If there was a change in the company's name, at least 50% of the revenue for preceding one year should be from the new activity denoted by the new name.

b) The aggregate of all issues in the current year must not be more than 5 times of the pre-issue net worth.

Exemption from Entry Norms:

The following sections are exempted from entry norms.

(a) Public sector Banks

(b) Private sector Banks

(c) Infrastructure companies satisfying certain conditions

(d) Listed companies making right issue

Guidelines for Allotment

Guidelines for allotment of shares include time limit for allotment, allotment to different categories and reservation on allotment.

a. **Time limit of allotment of shares:**
   a) Fixed Price Issue : 30 days of closure.

   b) Book Building Issue: 15 days of closure.

   c) Right issue : 15 days of closure.

b. **% of allotment to different categories:**

   a) Minimum 50% to retail individual investors.

b) In case of issue through Book Building,

1. Minimum 35% to retail individual investors.
2. Minimum 15% to non-institutional investors.
3. Maximum 50% to QIBs.

c. **Categories of Reservation on allotment - Optional:**

(a) Employees of the company

(b) Shareholders of the promoting company

(c) Shareholders of group companies

(d) Indian Mutual Funds

(e) Foreign Institutional Investors

(f) Scheduled Banks

(g) Development financial Institutions

General Guidelines

General guidelines include guidelines on period of issue, advertisement and DIP

1. Period of public issue (time for application)

(a) Fixed Price Issue: 3 to 10 working days.

(b) Book Building Issues: 3-7 working days extendable by 3 days in case of revision of price band.

2. Advertisement should be made in

(a) One English National News Paper

(b) One Hindi National News Paper

(c) One Regional language newspaper (of HO) with wide circulation.

3. Disclosure and Investor Protection (DIP) Guidelines 1992

(a) Public issue must be in compliance with DIP

(b) A company having 'partly paid up shares' cannot make any public issue.

(c) Filing of 'Draft offer Document' with SEBI if issue is worth more than 50 lakhs

(c) Company must appoint a 'Compliance Officer' to liaison with SEBI, SE and to redress investor grievance.

(d) Issue must be made only in Dematerialised form.

II. Method of new issue- Private Placement:

A private placement is a capital issue to a relatively small number of selected investors, without a public offer. Both private companies and public companies can make private placement issue. SEBI guidelines include:

1) No prospectus. The private placement offer letter must be in Form ‘PAS-4’ (Com. Act 2013)
2) A private placement offer letter and application form must be issued to the specific persons only.
3) The offer letter and application should contain the name of the individual to whom the offer is made.
4) The number of offer letter and applications printed and issued should not be more than 50 at a time.
5) The maximum number of persons should not be more than 200 in a financial year. This limit excludes Qualified Institutional Buyers and Employees.
6) Minimum amount of individual offer should not be less than Rs20’000/-
7) No advertisement must be made in any media regarding the issue.

<u>Procedure of Private Placement:</u>

1) Identification of persons to whom the offer is to be made.

2)Preparation of private placement offer letter.

3)Pass a special resolution in the general meeting.

4)Circulate the offer letter to the selected persons.

5)Prepare and maintain the record of private placement offer letters.

6)File documents (PAS4,5,3) with ROC.

7)Issue share certificates.

III. Method of new issue - Rights Issue:

'Rights Issue' means offering new shares to existing members in proportion to their existing shareholding. Offer is made to the existing shareholders on a particular date called 'record date'. Generally shares are offered at a lower rate. It is offered as a reward to the existing shareholders.

As per Section 62(1) of the Companies act, 2013 if the company decides to issue fresh shares, these should be offered to existing shareholders in proportion to their existing shareholding.

The object is to ensure equitable distribution of Shares and the proportion of voting rights is not affected by issue of Fresh shares.

SEBI Regulations:

1. A listed issuer making a rights issue shall announce a record date.
2. The issuer shall not withdraw rights issue after announcement of the record date.
3. Compulsory reservation for outstanding convertible debentures must be made in the right issue.
4. The abridged letter of offer, along with application form, shall be dispatched through registered post or speed post to all the existing shareholders at least three days before the date of opening of the issue.
5. The issue price shall be decided before determining the record date.
6. A rights issue shall be open for subscription for a minimum period of fifteen days and for a maximum period of thirty days.
7. The issuer shall issue an advertisement for rights issue.
8. Advertisement should be made in: (a) One English National News Paper, (b) One Hindi National News Paper, (c) One Regional language newspaper (of HO) with wide circulation.

IV. Composite issue:

Composite issue means an issue of specified securities by a listed company on public-cum-rights basis. Here the allotment in both public issue and rights issue are made simultaneously.

V. Employee Stock Option Plan (ESOP) (Employee Stock Purchase Scheme-ESPS):-

An ESOP/ESPS is a benefit plan for employees which make them owners of the company. These plans are contracts between a company and its employees. It gives the employees the right to buy a specific number of shares at a fixed price within a certain period of time. Shares allotted under ESOP are also called sweet equity shares. The company has the freedom to fix the lock-in-period. The minimum lock-in-period must be one year.

VI. Sweet (Sweat) Equity Share issue:

As per Sec 2(88) of The Companies Act 2013 or Sec 29(a) of The Companies Act 1956

It means equity shares issued by a company to its directors or employees, at a discount or consideration other than cash, as a reward for their services. A new class of shares cannot be issued as sweet equity share.

VII. Bonus Issue:

(scrip issue or a capitalization issue):

A bonus issue is an offer of free additional shares to existing shareholders. It is done by converting the reserves into equity share capital. It is an incentive to all shareholders. It also helps to reduce the dividend pay-out. For example, a company may give one bonus share for every five shares held.

VIII. Issue by Conversion:

Companies Act 2013 {sec 62.(3)} permits the companies to convert loans or debentures into share capital. But the company should pass a special resolution before taking the loan or issue of debentures.

Steps:

(a) Approve the terms of loan by passing a special resolution.

(b) File the resolution in E-form MGT14 with ROC.

(c) Convert loan into shares

(d) Allot shares

Primary Market Advisory Committee (PMAC)

PMAC was set by SEBI to advise SEBI on matters relating the primary market.

Offer Document:

It is an invitation to subscribe the securities of a company. It should contain:

a. All relevant information about the company and promoters.
b. All relevant information about the projects.
c. Financial Details.
d. Objects of raising money, terms of issue, etc.
e. Risk factors in investment.

Types of Offer Documents:

1. Prospectus	- Public Issue
2. Abridged Prospectus	- Public Issue
3. Letter of Offer	- Right Issue
4. Abridged letter of offer	- Right Issue
5. Placement Document	- QIP
6. Red Herring Prospectus	- Public Issue under Book Building
7. Shelf Prospectus	- Series of issue within one year
8. Draft Offer Document	- Draft offer submitted to SEBI for verification before filing to Registrar.

Methods Pricing of an Issue

Fixed price issue, book building issue and differential pricing are the three methods of pricing of an issue:

I. Fixed Price Issue:

The issuer decides and fixes the offer price. This will be mentioned in the prospectus.

II. Differential Pricing

Differential pricing is a method where shares are issued at different rates to different categories of investors. As per SEBI guidelines the difference should not be more than 10%

III. Book Building Issue

Under book building process, issue price is determined through auction. Only price band will be pre decided.

Price band:- The range of lower level and the upper level.

Floor Price:- The lower level of the price band.

Cap Price:- The upper level of the price band.

Lead Manager to the issue (Book Runner): He Keeps a book of share applications and quoted price.

Book building Process/Features:

1. Offer document is called 'Red herring prospectus'
2. Red herring prospectus does not contain issue price or size of issue.
3. Applicant should quote between price bands.
4. An applicant can revise the quantity and price before the closure of the issue.
5. Applicant can cancel the bid at any time before the finalisation of the 'basis of allotment'.
6. After the finalisation of allotment, allotment or refund is made.
7. The final prospectus with the details of final issue price and the size of issue must be filed with ROC.

Method of fixing price- example

Issue size: 50'000 equity shares of Rs.10/- Price band: 50-60. Applications received as:

(a) 20'000 applications quoted @ Rs.50/-
(b) 30'000 applications quoted @ Rs.55/-

(c) 40'000 applications quoted @ Rs.60/-

Issue Price will be the weighted average:

20'000 X 50 = 10'00'000

30'000X55 = 16'50'000

40’000X60 = 24’00’000

Average Price = 50’50’000/90’000 = Rs.56.11

Moving Price band concept:

As per SEBI guidelines, based on demand, the issuer can revise the price band by 50%. ie the price band can be moved by 50% either way- upward or downwards.

Retail Investors:-

Investors applying for securities worth up to Rs.2 lakh.

Cut off Option:-

Option made by Retail investors showing their willingness to subscribe at any price fixed by the issuer within price band. Applicants who choose this option will be considered for share issue, even if the cut of price (issue price) is more than the quoted price.

Types of Book Building

Open Book and Closed Book are the two types of book building.

Open Book: The number of shares applied and price quoted are published during the bid period. This is published through websites of NSE and BSE.

Closed Book: Here the book of application is not made public.

Green Shoe Option (GSO)

This is over allotment option. GSO is a mechanism for handling the high volatility in the market price due to over subscription. As per this scheme a company can make an additional allotment up to 15% of the issue size. This is to avoid extreme volatility in the share price after listing. Following are the conditions of GSO:

1. GSO should be mentioned in the offer document.
2. The money raised through additional allotment is kept in a separate bank a/c.
3. This bank a/c will be under the control of a merchant banker called ‘Stabilising Agent’
4. The money received is used to purchase and sell securities from the market to stabilise price.
5. The merchant banker (SA) is responsible for market stabilisation.

Reverse Book Building

Reverse Book Building is a method to fix the price of the shares, in case of Buy back of shares. It is basically a process used for efficient price discovery. The following are the process:

1. Company offers to buy back shares from the share holders
2. Offers are collected from the shareholders at various prices.
3. The quoted price should be above or equal to the floor price.
4. The buyback price is determined after the closing date
5. Book Running Lead Manager manages the process.

Buy Back of Shares

A company can buy back its own shares from the shareholders. Its objectives are:

1. Increase promoters holdings
2. Increase earnings per shares
3. Overcome take-over bid
4. Use of cash surplus.

Ways (Methods) of buy back can be:

(a) By tender offer to existing shareholders.

(b) By open market purchase through reverse book building.

(c) From open Market through Stock Exchange.

(d) From odd-lot holders.

Conditions of Buy back

(SEBI guidelines)

(a) Buyback cannot exceed 25% of the share capital of the company.

(b) If the % of buyback exceeds 10%, special resolution must be passed in the Board meeting and General Meeting.

(c) Public notice must be given in national newspapers.

(d) Escrow a/c must be opened with a balance of 25% of the proposed buy back.

(e) Company can use free reserves, securities premium or fresh issue of securities for buy back.

DVR Shares

(Differential Voting Right Shares):

'DVR shares' is an equity share with fewer voting rights to the holder. They are issued to prevent take over. The issuing company must have distributable profits at least for the last three financial years. Issue cannot exceed 25% of the total issued share capital. Their market price is comparatively less.

Participants in the New Issue Market

New issue participants include the Issuers, the Investors, and the Intermediaries.

Intermediaries in the New Issue Market

1. Merchant Bankers
2. Bankers to the Issue
3. Depository
4. Underwriters
5. Brokers to the Issue
6. Registrar to the Issue
7. Share Transfer Agents
8. Registrar of Companies (ROC)

1. **Merchant Bankers:**

MBs are the most important intermediary between Issuer and buyer. He can be the Lead Manager by coordinating public issue. There can be more than one MB. Registration of Merchant Banker with SEBI is compulsory.

The first merchant bank in India is ‘ANZ Grindlays bank’ in founded in1969.

Functions of Merchant Bankers

Their functions include Pre Issue Management and Post Issue Management

A. Pre Issue Management

(a) Association in Origination

(b) Coordinating Intermediaries.

(c) Preparation of Prospectus

(d) Appointment of Registrar to the issue

(e) Appointment of Bankers to the issue

(f) Appointment of Underwriters and Brokers

(g) Pricing of the issue

(h) Marketing of the Issue - meeting with Officials, advertising agents, intermediaries, etc

(i) Organising Publicity Campaign- advt, investor meet, etc

B. Post Issue Management

(a) Supervision of Collection of applications

(b) Screening and sorting of applications

(c) Rejection of incomplete & defective applications

(d) Deciding allotment procedure

(e) Arranging for dematerialisation of securities.

(f) Mailing of allotment letters or refund.

(g) Arranging for listing in Stock Exchange.

2. Bankers to the Issue

They are scheduled banks authorised to receive the share applications along with application money. They act as an agent in the distribution of application forms. They will give updating to the Company on the applications received. On closing they will transfer all the applications to the Registrar to the issue. Application money will be kept in either ‘Escrow a/c or ASBA.

Escrow Account:-

An escrow account is a temporary pass through account held by a third party during the process of a transaction between two parties. The application money collected may be kept by the banker in this account, till the receipt of ‘certificate of commencement of business’. Refund of excess or rejected applications will also be facilitated through this a/c.

Applications Supported by Blocked Amount (ASBA)

Here the application money remains blocked in the investor’s bank account, till the finalisation of allotment. Interest on deposit will be paid by the banker to the investor. On allotment the amount of company will be transferred to the company.

3. Depository

They are market intermediaries, holding securities in electronic/demat (Dematerialised) form. At present there are two depositories in India, National Securities Depository Limited (NSDL) and Central Depository Services (CDS).

According to SEBI:

"A depository is an organisation which holds securities (like shares, debentures, bonds, government securities, mutual fund units etc.) of investors in electronic form at the request of the investors through a registered depository participant. It also provides services related to transactions in securities."

Depository Participant:

An investor can open account with a depository through depository participant. Brokers and banks generally acts as DPs.

<u>Functions/Services of Depositories</u>

1) Opening a demat account;
2) **Dematerialization: C**onverting physical securities into electronic form;
3) **Rematerialization**: Converting electronic securities balances held in a BO (Beneficial Owner) a/c into physical form.
4) Maintaining record of securities held by the beneficial owners in the electronic form;
5) Settlement of trades by delivery or receipt of securities from / in BO accounts;
6) Settlement of off-market transactions between BOs;

7) Receiving electronic credit in respect of securities allotted by issuers under IPO or otherwise on behalf of demat account holders;

8) Receiving non cash corporate benefits such as allotment of bonus and rights shares

9) Pledging of dematerialized securities & facilitating loans against shares; on behalf of its demat a/c holders.

10) Freezing of the demat account for debits, credits, or both, on behalf of its demat account holders.

Bank & Depository – An Analogy

BANK	DEPOSITORY
1) Holds funds in an a/c	1) Holds securities in an a/c
2) Transfers funds between a/cs on the instruction of the account holder	2) Transfers securities between a/cs on the instruction of the DP a/c holder
3) Facilitates transfer without handling money	3) Facilitates transfer of ownership without handling securities
4) Facilitates safekeeping of money	4) Facilitates safekeeping of securities

4. Underwriters

Underwriting is a guarantee given by the intermediary to assure minimum subscription. The financial intermediary who gives guarantee is called ‘underwriter’. They agree to subscribe the unsubscribed securities in case of under subscription. Their return is called ‘underwriting Commission’. Registration of UW with SEBI is compulsory. Underwriting is optional from 1995.

5. Brokers to the Issue:

Members of Recognised SE can be appointed as brokers to an issue. Broker is an agent who assists an investor in buying and selling of securities. He also assists the MB in framing strategies for the success of issue.

6. Registrar to the issue

A registrar is an institution, a bank or trust responsible for keeping records of security holders. He is appointed to carry on the following activities on its behalf:

(i) Collecting applications from investors.

(ii) Keeping record of applications and application money (Both receipt and Payment)

(iii) Assisting the issuer in:

(a) Determining the basis of allotment in consultation with stock exchange;

(b) Finalising list of allotment;

(c) Processing and dispatching allotment letters, refund orders

7. Share Transfer Agents

In India both ROI and STAs seems to be the same institution. SEBI Rules reads as: 'SEBI (Registrar to an Issue and Share Transfer Agents) Regulation'. But both the terms are defined separately.

STAs are appointed by public companies to keep track of the holders of their securities. Most transfer agents are also banks or trust companies. But a company can act as its own transfer agent.

Main functions of STAs:

1. Issue and cancel certificates to reflect changes in ownership.
2. Keep records of shares or bonds owned by each investor.
3. Act as an intermediary for the company to pay out interest, and dividends.
4. Act as proxy agent (sending out proxy materials), exchange agent (exchanging a

company's stock or bonds in a merger), tender agent (tendering shares in a tender offer), and mailing agent (mailing the company's quarterly, annual, and other reports).

8. Registrar of Companies (ROC)[1]

The ROC is an office under the Indian Ministry of Corporate Affairs that deals with administration of the Companies Act 1956 and Companies Act, 2013. ROCs are appointed under Section 609 of the Companies Act. There are currently 22 ROCs in India. The Central Government exercises administrative control over these offices.

Sec2 (75) of the Companies Act 2013, “Registrar means a registrar or an additional or a joint, a deputy or an assistant registrar, having the duty of registering companies under this Act”

Functions of ROC

1) The primary duty of ROC is registration of companies and LLPs.
2) To ensuring that such companies and LLPs comply with statutory requirements under the Act. To function as registry of records, relating to the companies registered with them.
3) To make available these records for inspection by members of public.

[1] http://www.mca.gov.in/MinistryV2/registrarofcompanies.html

Module 4

Secondary Market

Capital Market = Primary market + Secondary market

Secondary Market is also called Stock Exchanges

Stock Exchange

"Any body of individuals, constituted for the purpose of assisting, regulating and controlling the business of trading and dealing in securities."

The securities Contract (Regulation) Act 1956.

Role / Importance of SE

1. Provide a market place for trading securities.
2. Provide liquidity and marketability to investment in securities.
3. Helps in the economic growth of the nation.
4. Serves as a barometer of the economy.
5. Provides ready information about the financial health of companies. (through valuation of securities)
6. It compels the companies to improve their performance.
7. Ensure transparency in trading of securities.

8. It provides measures to protect the interest of investors.
9. Creates investment opportunities for small investors.
10. It acts as a link between savings and investment.

Primary market Vs Secondary Market

1. PM deals with new issue

    1. SM deals with second hand securities

2. PM provides long term funds to companies

    2. PM provides liquidity to securities

3. In PM investor makes payment to the company

    3. In SM buyer pays to the seller.

4. In PM brokers (intermediaries) are optional

    4. In SM broker is mandatory.

5. In PM allotment of scrip is not sure

    5. In SM sure to get the scrip.

6. In PM securities are created by the issuer.

    6. In SM existing securities are transferred

7. Any company can issue shares in PM

    7. Only listed companies can trade in SM

8. In PM the price is generally fixed by the issuer.

 8. Issuer has no role in fixing the prices in SM

9. Economic cycles, economic factors and goodwill affect the pricing of PM.

 9. Micro & macro-economic factors decide the price.

10. PM has broader meaning and has no fixed location

 10. Narrow meaning- Covers all the places with trading facilities.

11. PM deals with only securities

 11. SM deals with even derivatives.

12. PM has no physical existence

 12. SM has physical existence.

13. No scope for speculation in PM

 13. There is scope for speculation in SM.

New Issue Mkt & Secondary Mkt – Relationship

Primary market and secondary market are complementary to each other. They work in cooperation. Both are controlled by SEBI.

Primary market supply fresh capital through the issue of securities. The securities markets ensure liquidity to such securities. Investor purchases shares with an expectation of selling it in secondary market.

Primary market uses many facilities of secondary market. Eg. Depositories (Demat a/c), financial institutions, price movements, network and information support, expertise of brokers, etc.

Members of stock exchanges:-

Member of a stock exchange is called **'Stock broker'**. He can be an individual, companies and partnership firms. They should fulfill the eligibility criteria laid down by SEBI and SEs. He can become a member of more than one SEs.

Categories of Membership:-

Basically there are two types of membership - Trading member and Clearing member. Trading cum self clearing member, Trading cum clearing member, Professional clearing member are the other types of memberships.

1. **Trading Member (TM) :-**

   They are also called Deposit based membership in BSE. They have exclusive right to trade. This member can execute trades on his own a/c and his clients a/c. But they cannot do the clearing and settlement of trades.

2. **Professional clearing member (PCM):-** They have the right to clear and settle the trade executed by trading members.

   The process of completing an order is called clearance and settlement. It includes (a) transfer of membership of securities and (b) payment of cash to the seller.

3. **Trading cum self-clearing member (SCM)** :-

   They have the right (a) to execute trade and (b) to clear and settle the trade executed by them.

4. **Trading cum Clearing member (TCM):-**

   They have the right to (a) execute trade, (b) to clear and settle the trade executed by them and (c) to clear and settle the trade executed by other trading members.

5. **Limited trading member (LTM):-**

   He is a trading member of the derivative segment. A person need not be a member of the Exchange. He has rights, privileges, obligations & liabilities of a TM.

   Rules, Bye – laws, Regulations, BRS, guidelines & other provisions of the Derivatives Segment, Exchange & SEBI to apply to a LTM. A LTM is not entitled to hold any office of the Segment or Exchange.

A LTM has no voting rights. LTM to be registered with SEBI as TM. LTM to satisfy all the eligibility conditions specified by SEBI.

6. **Sub brokers:-**

A ‘Sub-Broker acts as an agent of a trading member. He is not a Trading Member of a Stock Exchange. He assists investors in dealing with securities through Trading Members. They should obtain a Certificate of Registration from SEBI.

The rights and responsibilities of Sub-Brokers depends on the agreement with TM. BOLT terminals can be installed at Sub-Brokers offices.

7. **Authorised persons:-**

Any person who is appointed as such by a stock broker, is an Authorised Person. He acts as an agent of the stock broker. He helps in market access and assists the investors in buying, selling or dealing in securities. He can access trading platform of a stock exchange.

He should obtain a certificate of registration from the exchange. Same person cannot act as sub-broker and Authorised Person. stock broker can share brokerage with AP.

8. **Remisier:-**

   A person who is engaged by a member-broker to solicit business in securities on a commission basis. They can operate BOLT (The Bombay On-line Trading System) terminals at member's office only. BOLT terminals cannot be installed at Remisier's Office. BOLT terminals should be installed at Members Offices' or their associated Sub-Brokers offices only. Remisiers are to be approved by the exchange only.

Types of brokers (Terminology of SE)

1. **Commission brokers:-**

   They act on behalf their clients. They purchase and sell for their clients. Their remuneration is called 'commission' or 'brokerage'.

2. **Jobbers (Tarawaniwalas):-**

   He functions as a wholesaler. His profit is called **'turn'**. They specialize in few securities. Different quotes are made for buy and sell. The differences in two quotes are called **'jobber's spread'**. They may act as 'market makers' of some companies to ensure liquidity. He is a stock broker who buys and sells securities in his own name.

3. **Arbitrageurs:-**

   He buys from one SE and immediately sells it in another SE at a high price. He exploits the price difference existing in different stock exchanges. He makes profit from the small difference in price. He does large volume of trade.

4. **Security Dealers:-**

   They specialize in govt securities. Since financial institutions became the primary dealers of govt securities, their importance is declined from 1995.

Eligibility Criteria- Individuals.

1. He must be of 21 years or more.
2. He must be a citizen of India. (exception with prior approval of C. Govt.)
3. He must have the minimum educational qualification prescribed (10+2+3).
4. He must be a solvent. (not an adjudged bankrupt.)
5. He must not be convicted for an offence of fraud or dishonesty.
6. He must not be engaged in any other business other than that of securities.

7. He must not be at any time expelled or declared a defaulter by any other Stock Exchange.
8. At least two years work experience in the field.
9. He must be financially sound. (has the minimum net worth and working capital fixed by SE) (NW –BSE-30lakh)
10. He must qualify the written test conducted by the SE.

Eligibility Criteria- Companies.

1. It must be a company formed as per the Companies Act 1956.
2. Minimum paid up capital should be Rs.30 lakhs.
3. It must satisfy the financial requirements specified by SEBI.
4. All the directors should be above 21 years of age.
5. None of the directors should be disqualified by SEBI.
6. All the directors must be solvent.
7. None of the directors should be convicted for fraud or dishonesty.

8. At least two directors must satisfy the educational and experience criteria.

Eligibility Criteria- Partnership.

1. It must be registered under the Indian Partnership Act, 1932.
2. It must register with the Income Tax Authorities.
3. There should not be any minor partner in the firm.
4. At least two designated Partners of the firm are qualified to become a trading member.
5. The designated partners share in the firm should not be less than 40%.

Investment and Speculation:

In SE investment and speculation are two different activities.

Investment:-

Investment is deploying financial resources to get long term benefits. Investor invests in stock market on a long term basis. He looks for long term gains like increase in prices, dividends, right shares, bonus shares, voting rights, etc. Investors risk and return are comparatively less. In the SE investor takes the delivery of securities. He should invest the full amount of transaction.

Speculator:-

Speculation is a risky attempt to make profit from short/ medium term fluctuations in the market. It focuses purely on price movements. Speculator trade over a short span of time. They trade frequently. They do not keep securities for a long term. Their risk and return are very high. They hope to make quick and large gains. A speculator is one who bets on the market, based on his anticipations of future price movements.

There is no importance to the fundamental values of securities. They are common in stocks, bonds, commodity futures, currencies, fine arts, real estate, collectibles, derivatives, etc

Role of Speculator:

He infuses (introduces) volatility[1] to the capital market. Reasonable level of speculation is good to the market. They absorb the excess risk of other participants. They provide liquidity. But there should not be any unfair trade practices. A healthy market needs both investors and speculators. But excessive speculation is not at all good- for speculators and market.

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[1] means unpredictability. It is a measure of variation of price of a financial instrument over time.

Speculation & Gambling

Speculation- It is a calculated movement. He will not tolerate continuous losses.

Gambling- A gambler moves on emotions. It is just betting on uncertain future.

Type of speculators:

1. **Bulls:-** A bull buys shares in the expectation price increase. He hopes to sell them at a higher price in future. He is an optimistic speculator.

   When bulls dominate the market, it is said to be bullish. Bullish tendency will increase the demand and the index will go high. Large no of buyers and few no of sellers are the characteristics of bullish market.

   The bull speculator tries to toss the security price up like a bull throw up the enemy using his horns.

2. **Bears:-** A bear sells the shares in the expectation of a fall in price. He hopes to buy them at a lower price in future. He is a pessimistic speculator.

   When bears dominate the market, it is said to be bearish. Bearish tendency will decrease the demand and the index will go down. Large no of sellers and few no of buyers are the characteristics of bearish market.

3. **Stags:-** Stags (male deer-which runs fast) are bull speculators operating in the IPO market. They apply for large quantity of shares of reputed companies. They sells them at a higher price in the secondary market immediately on listing.

4. **Lame Duck:-** When a bear speculator did short selling in some securities, may be called as 'lame duck'. Now he is unable to fulfill his commitment to the counter party. This happens (a) when the market prices increased far. (b) The securities are not available in the market.

Speculative Transactions

Old forms in out cry system :- blank transfer, badla/carry forward, etc were the main features of cry out system.

Online trading system:- Day trading, Short selling, margin trading, derivative transactions, arbitrage, etc. are the main features of OTS.

1. **Day Trading(Intra-day transactions):-**

It is a speculation within the same trading day. A day trader holds securities for a very short time-from minutes to hours. Trade positions are closed on the same day. The day trader has to keep a deposit amount with the broker as margin. He is permitted to trade several times of his deposit.

(Trade open : 9.00 close 15.30Monday - Friday); (Clearing open :15.5 close 16)

2. Short selling:-

Here the speculator sells a security, which he is not having. He expects that the price will come down and he can purchase it to settle. If price falls, he gets profit. If the price increases, he has two options: (a) square the transaction by paying the difference or (b) Pay heavy penalty charged by the stock exchange, if not able to square off.

3. Arbitrage:-

The speculator buys from one SE and immediately sells it in another SE at a high price. He exploits the price difference in existing in different stock exchanges. He makes profit from the small difference in price. He does large volume of trade.

4. Margin trading:-

The investor is provided with bank loan through broker up to 50% of requirement. Thus he needs to bring only 50% of his requirement. Conditions of MT:

(1) Only 50% of the requirement is given as loan.

(2) It is permitted for limited number of actively traded scrips.

(3) The scrips shall be kept as collateral security.

(4) This collateral security increases the purchasing power of the investor. (He can purchase more on the basis of this C. security.)

(5) The rate of bank loan is higher than the market rate.

5. Derivative transactions:-

Derivatives markets are markets that are based upon another market (underlying market). Underlying market includes securities, commodities, stock indices (e.g. the S&P CNX NIFTY), and currency markets (i.e. the forex markets). Derivative Exchange/Segment function as a Self-Regulatory Organisation (SRO).

The market is divided in to two- Exchange traded derivatives and over the counter derivatives.

i. **Exchange traded derivatives**:-

Futures & options

ii. **Over the counter derivatives**:-
Forwards, Swaps, rate agreements, credit derivatives, accumulators, etc

(i) **Exchange Traded Derivatives**:-

Futures & options

(a) **Futures:-** Futures Contract means a legally binding agreement to buy or sell the underlying security on a future date. On expiry, futures can be settled by delivery of the underlying asset or cash. They are traded in SEs.

Index Futures Contracts:- Futures contract based on an index i.e. the underlying asset is the index (NIFTY Index and BSE-30 Index)

(b) **Options:-** Options Contract gives the buyer/holder of the contract the right (but not the obligation) to buy/sell the asset at a predetermined price on or before a future date. He pays the seller a consideration called the premium. The price at which the option is to be exercised is called Strike price or Exercise price.

The seller of an option is obligated to settle the option when the buyer/holder exercises his right. The underlying asset can be securities, an index of prices of securities etc.

(i) Call option:- An Option to buy

(ii) Put option:- An option to sell

(iii) American Option:- An option exercisable on or before the expiry date.

(iv) European option:- An option exercisable only on expiry date.

(v) **Index options contract:-** An options contract based on some index.

(vi) **Warrants:-**Options for a period of more than one year. They are not traded in SE

(vii) **Baskets:-** Options where the underlying asset is an average of a basket of assets. Eg. SENSEX, NIFTY50

Mini Derivative contracts:-

The minimum contract size for the mini derivative contract on Index (Sensex and Nifty) is Rs. 1 lakh at the time of its introduction in the market. The lower minimum contract size means that smaller investors are able to hedge their portfolio using these contracts with a lower capital outlay.

(ii) **Over The Counter Derivatives**:-

Forwards, Swaps, rate agreements, credit derivatives, accumulators, etc are traded.

OTC Market –

(a) **Forwards:** Forward Contract means an agreement to buy or sell the underlying security on a future date. On expiry, forwards can be settled by delivery of the underlying asset or cash. They are traded not in SEs, but over the counter.

spot contract- is an agreement to buy or sell an asset today. The party agreeing to buy the underlying asset in the future assumes a **long position**. The party agreeing to sell the asset in the future assumes a **short position**. The price agreed upon is called the **delivery price**, equal to the forward price at the time the contract.

(b) **Swap:** It is a private agreement to exchange two assets, based on a predetermined formula. Common swaps includes interest rate swaps, currency swaps, credit swaps, commodity swaps and equity swaps.

Features of swaps:

1. Swaps are complex instruments.
2. They are not available for trade in the stock markets.
3. Retail investors do not generally engage in swaps.

4. Rather, swaps are over-the- counter contracts
5. Generally swaps are between businesses or financial institutions.

Requirements for Swap:

- Swapping requires double coincidence of Wants- Two parties with equal and opposite needs.
- Swapping requires long term agreement.

Swaptions : An option on a forward swap.

Currency Swap- How it Works[i]

An American company may be able to borrow in the United States at a rate of 6%, but requires a loan in rand for an investment in South Africa, where the relevant borrowing rate is 9%. At the same time, a South African company wishes to finance a project in the United States, where its direct borrowing rate is 11%, compared to a borrowing rate of 8% in South Africa.

Each party can benefit from the other's interest rate through a fixed-for-fixed currency swap. In this case, the American company can borrow U.S. dollars for 6%, and then it can lend the funds to the South African company at 6%. The South African company can borrow South African rand at 8%, then lend the funds to the U.S. company for the same amount.

Fraudulent and unfair trade practices.

1. **Insider Trading:-** Insider is one who knows the price sensitive information. Eg. Directors, top officers, auditors, officials of SE, SEBI, Top Govt. Officials, etc. Insider trading is an offence prohibited by law.

   Price sensitive information is one, if published, is likely to be affect the price of it's securities.

   Eg. (a) Declaration of dividend (interim/final)

   (b) Issue of bonus shares.

   (c) Issue of securities.

   (d) Buy back of shares.

   (e) Execution of new projects.

   (f) Amalgamation, merger and takeover.

   (g) Significant change in policies, plans, etc.

2. **Rigging the market:-** It means an artificial increase in the price created by a group of persons/institutions. They will sell the shares at a blown up (ballooned) price. It can be in two ways:-

   (a) Side by side trading: Buying (or selling) a security and buying (or selling) an option at the same time.

(b) Laddering: Large quantity of a stock is purchased to push the price. They will sell it at it's peak price.

3. **Wash sales:-** Sale of securities at a loss by an investor, claiming capital loss, to get a tax deduction. They will purchase the same or identical security before or after.

4. **Wash Trade:-** In wash trade an investor simultaneously sells and buys shares. The object is to artificially increase trading volume and thus the stock price. It is an illegal form of stock manipulation.

5. **Cornering the market:-** To corner the market is to get sufficient control of a particular stock or commodity. The object is to manipulate the price. A corner may (a) Purchase a Large quantity of a particular stock and hoard it, to gain control over the supply. (b) Purchase a large number of futures contracts and then sell them at a profit after inflating the price.

Measures to overcome unfair trade practices and Excessive Speculation.

1. Close watch by SE and SEBI.
2. Checking of excessive market volatility.
3. Circuit breakers:- Temporary halt of trade when the index moves beyond a specified

limit. Index-based market-wide Circuit breaker applies at 3 stages of the index movement, either way viz. at 10%, 15% and 20%.

10% - before 1pm -1.**45min**; 1-2.30 – **45mn**;
after 2.30pm – no halt
15% - before 1pm -**45min**; 1-2 – **45mn**;
after 2.00pm – Remaining day
20% - Any time (mkt hrs)– Remaining day.

Market Segments in Stock Exchanges

1. Equity
2. Derivatives
3. Indices
4. Currency derivatives
5. Interest Rate Derivatives
6. Debt
7. Securities' Lending and Borrowing
8. Exchange Traded Funds (ETFs)/Mutual Funds

Listing of Securities.

Listing means admission of securities to ‘dealings’ on a recognized stock exchange. The securities may be of any public limited company, Central or State Government, quasi governmental and other financial institutions /corporations, municipalities, etc. Listing can be done in more than one SEs.

Permitted Securities:- The securities which are actively traded in other SE, but not listed in BSE, may be permitted to trade in BSE. They are called 'Permitted securities'.

The objectives of listing are:

1. To provide liquidity to securities;
2. To mobilize savings for economic development;
3. To protect interest of investors by ensuring full disclosures.

Benefits of Listing:

1. Listing provides liquidity to the securities.
2. Listing increases the credibility of the issuer company.
3. Listing helps to raise additional capital.
4. Listing extents the profile of the company to domestic and foreign investors.
5. Listing provides media coverage through it's analytical reports.

6. Listed companies can make use of the information network of SEs.
7. Listing reduces the cost of trading of investor.
8. Listing protects the interest of investors.
9. Listing helps the independent valuation of the shares of the company.

Minimum Listing Requirements

for New Companies –BSE

For Initial Public Offerings (IPOs) & Follow-on Public Offerings (FPOs), minimum listing requirements are the following:

1. The minimum post-issue paid-up capital of the company shall be Rs.10 crore for IPOs & Rs.3 crore for FPOs.

2. The minimum issue size shall be Rs. 10 crore.

3. The minimum market capitalization of the Company shall be Rs. 25 crore (market capitalization = Post issue paid-up number of equity shares X the issue price).

4. Payment of annual Listing Fees by 30th April of every financial year

(Initial listing Fee- Rs 20’000/-

Annual listing fee – 5cr (15000),
10 cr(25’000), 20cr (40000), etc

Classification of Listed Securities.

A. Categorisation by NSE.

1. Group I.

Group I category of NSE includes those scrips:

(a) Which are traded at least 80% trading days of last 6 months.

(b) Which have mean impact cost of less than or equal to 1%

2. Group II.

Group I category of NSE includes those scrips:

(a) Which are traded at least 80% trading days of last 6 months.

(b) Which have mean impact cost of more than 1%

3. Group III.

The remaining stocks are classified in to Group III.

The impact cost is the percentage price movement caused by an order size of Rs.1 Lakh from the average of the best bid and offer price in the order book snapshot. The impact cost is calculated for both, the buy and the sell side in each order book snapshot.

B. Categorization by BSE.

Equity Segment into 'A' (blue chip cos), 'B' , 'T' and 'Z' groups. S and TS group for indonext segment. F and G represents debt market.

1. **A Group** :- A Group includes shares of blue chip companies. The scrips of top 30 companies. Sensex is composed of A group securities.
2. **B Group** :- (Non specified shares) The scrips of next best companies with top trading frequency.
3. **T Group** :- Where no short selling is permitted. They deals on a trade to trade basis.
4. **Z Group** :- Companies which fails to fulfill the listing requirements or failed to resolve investor complaints or not made arrangements for dematerialization.
5. **S Group** :- Scrips enrolled under BSE indonext segment.

   Indonext Segment: A separate trading platform introduced by BSE, for medium and small-cap companies. They are generally listed on Regional Stock Exchanges and the BSE itself. The project is aimed at improving liquidity in such companies. The BSE IndoNext, a separate trading platform under the BOLT trading system, is an initiative of the BSE and the Federation of Indian Stock Exchanges.

6. **TS Group**:- Scrips in BSE indonext segment where no short selling is permitted.
7. **F Group :-** Represents the Fixed Income Securities. (ie Debt market)
8. **G Group :-** They represents Government Securities. It is also a debt market.

Odd Lot Segment :-

Investors having quantities of less than the market lot is called odd lot segment. Odd lots are traded in odd lot segment.

For dematerialized scrip market lot is 1 share. For materialized scrip market lot is 50 or 100.

Methods of trading in SEs

1. **Outcry System**:- The traditional out dated system. The brokers and agents actually outcry the details of their deal on the floor of the exchange. (abolished gradually in 1990s)
2. **Screen Based Trading System (SBTS)**:- It is a fully automated system. The broker puts the clients requirements in the SEs computer. The screen displays the 'least quote to sell' and 'the highest quote to buy'. The

transaction is automatically executed as soon as a counter party is found.

3. **Online Trading System**:- This is the modern internet based trading facility. The display and trade systems are same as that of SBTS. This is done through SEBI approved internet based Order Routing System. ORS communicates the clients order to the SE through broker. The deal is updated to the client's de-mat account.

The Trading Process.

1. Selection of a broker
2. Open a depository (demat a/c) with any DP.
3. Opening a trading a/c with broker.
4. Getting 'Unique client code' (identity no in SE) with user id and password from the broker.
5. Placement of order either through online trading system or otherwise.
6. Automatic execution of order at a matching bid.
7. If order is not executed keep the order in 'price cum time priority books'.
8. Issue of contract note (confirmation slip of trade done) to the client by the broker.

9. Payment of fund to the seller and delivery of securities to the buyer on pay-out day.
10. Payment of brokerage to the broker. (max 2.5%)

    Now a days, an investor is allowed to trade with the help of mobile apps. Here SB a/c is linked with demat a/c to smoothen the deals.

Clearing and settlement.

Clearing is the process of determination of obligations. The obligations are discharged by settlement.

The clearing function works out:

(a) what members are due to deliver and

(b) what members are due to receive on the settlement date.

Settlement is a two way process which involves transfer of funds and securities on the settlement date.

Clearing and settlement process:

1. Automatic recording of trade.
2. Automatic confirmation of trade.
3. Determination of net obligation of trading member.

4. Delivery of securities and funds with the depository and clearing bank.
5. Pay out of funds and securities to the members.
6. The pay out of funds and securities to the clients is by the broker.

Intermediaries in Clearing and settlement.

1. **Clearing Corporations:** Their objective is to improve efficiency in trading and settlement. There are two clearing corporations:

NSCCL – National Securities Clearing Corporation Ltd.

(1995 wholly owned subsidiary of NSE)

ICCL - Indian Clearing Corporation Limited.

(2007 as a wholly owned subsidiary of BSE Ltd.)

2. **Clearing Members:** They facilitate settlement of trades. There are professional clearing members, trading cum clearing members, and self-clearing members.
3. **Custodians:** They helps to register and safeguard the securities of its clients. They also act as clearing members.
4. **Clearing Banks:** They are selected commercial banks to effect settlement of funds. Eg SBI, Canara bank, UBI for NSE

5. **Depositories:** They hold the securities in electronic forms for the investors. There are two depositories in India.

   NSDL – National Securities Depository Ltd.

   (Promoters-NSE, IDBI, UTI)1996

   CDSL – Central Depository Services (India) Ltd.

   (promoter 54% BSE) 1999.

6. **Depository Participants (DP):**

   They are agents of Depositories. The DP is the link between the investor and Depository. A demat account holder with a DP can utilise the services offered by Depositories. DP is thus a "Point of Service" for the investor. Most of the commercial banks and SE Brokers provides DP services. Eg UBI, ICICI bank, Geojith BNB Paribas Financial Services Ltd, etc.

   A DP is a financial organization. It act as an agent of the depository, to make its services available to the investors. Each DP is assigned a unique identification number known as DP-ID.

Dematerialisation

Dematerialisation is the process by which physical certificates of an investor are converted to an equivalent number of securities in electronic form and credited in the investor's account with his DP. Dematerialisation is made by depositories like NSCCL and ICCL.

"Conversion of physical certificates in to electronic form is called dematerialisation"

Shares, debentures, bonds, Units of MFs, Govt. securities, Money market instruments like CPs, CDs, etc. can be dematerialized. Dematerialized securities are identified on the basis of ISIN (International Securities Identification number).

Rematerialisation

Conversion of demat securities into physical form is called rematerialisation. Rematerilisation is also done by depositories, as per the request of the holder.

Benefits of Depositories/ Dematerialisation

1. It eliminates paper works.
2. It facilitates easy trade.
3. It reduces the minimum market lot to 1 scrip.
4. It reduces transaction cost.
5. It facilitates electronic holding of securities.
6. It facilitates immediate transfer of securities.

7. It eliminates associated risk of physical certificates.
8. It saves time in many ways.
9. It facilitates holding of all securities in one a/c.
10. It facilitates easy change of nomination, address, etc.

Rolling Settlement.

In rolling settlement each trading day is considered as a trading period. Trades done on each day are settled separately. It is done on a T+2 basis. Eg. For the trading day of Monday settlement day is Wednesday. All holidays are excluded for finding out the pay-out day.

Pay in day is the day when the brokers shall make payment or delivery of securities to the exchange.

Pay out day is the day when the exchange makes payment or delivery of securities to the broker.

In case of Rolling Settlements, pay-in and pay-out of both funds and securities is completed on the same day. The pay out of funds and securities to the clients is done by the broker within 24 hours of the payout.

Securities of "Z" group and "T" group companies, are settled only on a gross basis. Netting facility of buy and sell transactions is not available.

Settlement cycle is on T+2 rolling settlement basis w.e.f. April 01, 2003.

Members are required to make payment for securities sold and/ or deliver securities purchased to their clients within one working day (excluding Saturday, Sunday, bank & BSE trading holidays) after the pay-out of the funds and securities for the concerned settlement is completed by BSE. This is the timeframe permitted to the Members to settle their funds/ securities obligations with their clients as per the Byelaws of BSE

Physical settlement

Limited physical Market: The physical shares of securities (Material form) held by Small investors, not exceeding 500 shares can be traded in the 'Limited Physical Market' (small window). This provides an exit route for small investors with physical shares.

Stock market indices

An index number is a single figure showing the changes in the whole set of the group of variables over time and places. Index is calculated with reference to a base period. So it has a base value.

An index is a statistical measure of change in an economy or a securities market.

SE Index is an Index derived from a selected group of similar stocks listed in a stock exchange. The values of the grouped stocks are used to calculate the value of the index. Any change in the price of the stocks leads to a change in the index value. An index is thus indicative of the changes in the market.

The basis of classification (grouping) of stocks for the purpose of index calculation is given below:

1. Industry (BSE Bankex, CNX IT)
2. Size of the company (SENSEX, NIFTY50)
3. Market capitalization (Eg. BSE Small cap, NSC mid cap)
4. Some other basis like public sector, debt indices, etc..

INDICES OF BSE

BSE indices are called S&P BSE Index. For eg. S&P BSE SENSEX. S&P is Standard and Poor who is in carge of the preparation and maintenance of BSE indices.

S&P Dow Jones Indices

Standard & Poor's Financial Services LLC is an American financial services company. They are global leader in providing investable and benchmark indices to the financial markets. *Standard & Poor's introduced its first stock index in 1923. BSE and S&P Dow Jones Indices (S&P DJI) have entered into an alliance to calculate, publish, and license the widely followed suite of BSE indices from February 19, 2013.*

1. SENSEX
2. 100
3. 200
4. 500
5. DOLLEX 100
6. DOLLEX 200
7. DOLLEX 30
8. All Cap
9. MidCap
10. MidCap SELECT Index
11. Small Cap
12. Small Cap Select Index
13. LARGE CAP
14. IPO
15. SME IPO
16. PSU
17. CPSE
18. AUTO
19. BANKEX
20. FINANCE
21. Health Care
22. Information Technology
23. Oil & Gas
24. POWER
25. Telecom
26. Consumer Durables
27. Consumer Discretionary Goods & Services
28. Basic Materials
29. Capital Goods
30. Carbonex
31. ENERGY
32. Fast Moving Consumer Goods
33. India Infrastructure Index
34. India Manufacturing Index
35. INDUSTRIALS
36. METAL
37. Utility
38. REALTY
39. TECK
40. GREENEX

1. S&P BSE SENSEX (BSE 30):

S&P Bombay Stock Exchange SENSitive ind**EX**

Sensex represents Stocks represents large, well-established and financially sound companies across key sectors.

Base year is 1978-79.

Date of Launch	: 1.1.1986
Base Index Value	: 100
methodology index calculation	:"free-float market capitalization-weighted"
Number of stocks	: 30
Index calculation frequency	: Real Time

2. S&P BSE 100, 200, 500, All Cap :

Derived from the values of number of stocks representing the name of the Index. For eg. BSE 100 is composed from the values of 100 best stocks.

3. S&P BSE Small Cap, Small Cap Select Index:-

Derived from the valued of the companies having relatively smaller capitalisation. Formed in 2005 with base year as 2002-2003 and base index value as 1000.

4. S&P BSE LARGE CAP:

Derived from the values of companies with large market capitalization.

5. DOLLEX INDICES

Dollex indices are the US Dollar denomination of corresponding BSE indices. The index is widely used as a benchmarking tool among market participants.

ie S&P BSE Dollex 100 = S&P BSE 100

S&P BSE Dollex 200 = S&P BSE 200

S&P BSE Dollex 30 = S&P BSE SENSEX

6. S&P BSE IPO Index:

Formed from the values of new companies subsequent to successful completion of initial public offering (IPO). Tracks the current primary market conditions in the Indian capital market. It measure the growth in investor's wealth within a period of two years after listing of a company.

Formed in 2009, base year- 2004, base index value 1000.

7. S&P BSE PSU:

This index consists of major Public Sector Undertakings listed on BSE.

8. S&P BSE SME IPO:

Represents the Micro, Small and Medium Enterprises (MSMEs) segment in India, but seeking listing of its equity shares via IPO. Launched in 2012 with base index as 100

9. S&P BSE CPSE:

Central Public Sector Enterprises. It is formed from the values of govt. companies.

10. S&P BSE GREENEX: to promote investments in Green India

11. All others are sectoral indices.

Derived from the valued of stocks from the sector representing the name of the Index.

TECK: TMT sector –Technology, Media and Telecommunication

Debt Market Indices (Fixed Income Indices):

There are a number of debt market indices. For Eg.

- S&P BSE India 10 Year Sovereign Bond
- S&P BSE India Government Bond Index
- S&P BSE India Sovereign Bond Index
- S&P BSE India Government Bill Index
- S&P BSE India Agency Bond Index
- S&P BSE India Provincial Bond Index

NSE INDICES

NSE indices are called CNX NIFTY indices. They are so called because the indices are composed by CNX, which stands for CRISIL and NSE.

CNX Nifty

CNX stands CRISIL & NSE, They formed a joint venture called the India Index Services and Products Ltd. (IISL). IISL owns and maintains the indices of NSE. IISL is India's first specialised company focused upon the index as a core product.

CRISIL - Credit Rating Information Services of India Ltd.

NSE- National Stock Exchange of India.

Classification of NSE Indices

1. Broad Market Indices: These indices are broad-market indices, consisting of the large, liquid stocks listed on the Exchange. Eg. Nifty 50 Index, Nifty Next 50 Index, Nifty 100 Index

2. Sectoral Indices: They are sector-based index. They represents a number of companies representing a group of related industries. Eg. Nifty Auto Index, Nifty Bank Index, Nifty Financial Services Index, Nifty FMCG Index

3. Thematic Indices: They represents a number of companies representing a theme. Eg.

Nifty Commodities Index, Nifty India Consumption Index, Nifty Corporate Group Indices, Nifty Energy Index

4. Strategy Indices: They are designed on the basis of quantitative models / investment strategies. Eg. Nifty Alpha 50 Index, Nifty50 USD Index, Nifty High Beta 50 Index, India Vix

5. Fixed Income Indices: Fixed income index is used to measure performance of the bond market. Eg. Nifty 8-13 yr G-Sec Index, Nifty 10 yr Benchmark G-Sec Index, Nifty 10 yr Benchmark G-Sec (Clean Price) Index

Nifty 50 Index

This is the most popular index of NSE. It is composed of 50 stocks of from 13 sectors of the economy. They are composed from Group I stocks.

Base Period	–	1995
Base Index Value	-	1000

Nifty Next 50:

The next rung of liquid securities after Nifty 50 is the Nifty Next 50.Formed out of most liquid 50 stocks, after NIFTY 50.

Nifty 100:

100 stock accounting for **38** sectors of the economy.

India VIX*

A volatility index based on the NIFTY Index Option prices.

Free-float Market Capitalisation Methodology

It is an index construction methodology. This considers only the free-float market capitalization of a company for the purpose of index calculation. Presently most of the Indices of BSE & NSE uses Free Float Method for Index Calculation.

Free-float market capitalization: Considers only those shares that are readily available for trading in the market. It generally excludes blocked shares. Blocked Shares are shares which are not available for trade. Eg. Promoters' holding, government holding, strategic holding and other locked-in shares that will not come to the market for trading in the normal course.

Free Float Mkt Capitalisation

= (Total Shares – Blocked Shares)* MV

In other words, the market capitalization of each company in a Free-float index is reduced to the extent of its readily available shares in the market.

Blue Chip Companies.

Blue chip companies are very large and well recognized companies in with a long history of sound financial performance. They generally sell high-quality, widely accepted products and services. They are known to operate profitably in the face of adverse economic conditions. They have a long record of stable and reliable growth. They do not have extensive liabilities. Blue chip stock are shares of blue chip companies.

Blue Chip companies in India

Indian blue chip companies are included in the NIFTY50, Sensex and Dow Jones India Titans 30 indices. Asianpaint, SBI, AxisBank, ICICI Bank, HDFC Bank, HDFC, Drreddy, Sunpharma, Cipla, HindUnilvr, Bhel, Gail, ITC, LT, TCS, Wipro, Bhartiartl, Coalindia, TATAsteel, Tata motors, Maruti, Bajaj-Auto, Heromotoco, NTPC (National Termal Power Corporation), ONGC, Reliance.

Maharatna Companies are the most valuable companies in India. They are NTPC, ONGC, SAIL, BHEL, IOCL, CIL (Coal India Ltd.), GAIL (Gas Authority of India Ltd.), BPCL

Calculation of SE Index

	Co A	Co B
a) No of shares issued	1000	500
b) Market Price of a share	20	20

Total Market Capitalisation ----------------

» (a) X (b)

» 20000 + 10000 = 300000

Weight for Price movements 2/3 1/3

Full Mkt Capitalisation Method:

Total no of shares issued X MP

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[i] http://www.accaglobal.com/in/en/student/exam-support-resources/professional-exams-study-resources/p4/technical-articles/currency-swaps.html

Module V

Stock exchanges in India

Permanent Stock Exchanges in India (19 No)

1. Ahmedabad Stock Exchange Ltd.
2. Bombay Stock Exchange Ltd.
3. Calcutta Stock Exchange Ltd.
4. Delhi Stock Exchange Ltd.
5. Madras Stock Exchange Ltd.
6. National Stock Exchange of India Ltd.
7. National Commodity & Derivatives Exchange Ltd.

Other Stock Exchanges in India

(Renewed by SEBI on request up one year)

1. Jaipur Stock Exchange Ltd
2. MCX - Stock Exchange Limited
3. OTC Exchange of India
4. Pune Stock Exchange Ltd
5. The Vadodara Stock Exchange Ltd.
6. U.P. Stock Exchange Limited
7. U.P. Stock Exchange Limited
8. United Stock Exchange of India Limited
9. Magadh Stock Exchange Ltd. (Refused Renewal request in 2007)

Closed Stock Exchanges in India

Closed (Exit granted) by SEBI as per order

1. The Hyderabad Securities and Enterprises Ltd (erstwhile Hyderabad Stock Exchange)
2. Coimbatore Stock Exchange Ltd
3. Saurashtra Kutch Stock Exchange Ltd
4. Mangalore Stock Exchange
5. Inter-Connected Stock Exchange of India Ltd
6. Cochin Stock Exchange Ltd
7. Bangalore Stock Exchange Ltd
8. Ludhiana Stock exchange Ltd
9. Gauhati Stock Exchange Ltd
10. Bhubaneswar
11. Stock Exchange Ltd

Bombay Stock Exchange –BSE

Oldest Stock Exchange in Asia.

1875 Formation - 'Native Share and Stock Broker's Association'

1957 Permanent recognition under SCRA (Securities Contracts (Regulation) Act

1986 launched S&P BSE SENSEX

- India's First equity index

1990 SENSEX closes above 1000

1995 BOLT system introduced (BSE- Online Trading System)

2001 T+5 Settlement

2002 T+3 Settlement

2003 T+2 Settlement

2005 Becomes a Corporate Entity –BSE Ltd

2006 S&P BSE SENSEX closes above 10000

2008 S&P BSE SENSEX closes above 20000

2010 Mobile based Trading

2014 Market Cap of listed companies crossed Rs.10000 Crore

2015 Becomes the fastest exchange in the world with median response of 6 microseconds

2015 Dec launch an initiative called 'Sammaan' – a platform for Corporate Social Responsibility. Trusted marketplace or intermediary to identify and partner with an NGO for their CSR compliance.

Number of listed Companies - 1294

Trading Segments –

1. Equity segment (Cash Segment)
2. Derivative Segment
3. Currency Derivatives Segment
4. Exchange Traded Funds
5. Mutual Fund (STAR MF)
6. New Debt Segment (BSE NDS), etc.

Membership

1. Trading member (Deposit based membership)
2. Clearing member.
3. Trading cum self clearing member,
4. Trading cum clearing member,
5. Professional clearing member
6. Sub Brokers, Authorised Persons and Remisier for trading purpose

National Stock Exchange –NSE

1992	Formation
1993	Recognition as SE
1996	Launch of NIFTY 50
2000	Started Internet Trading

Ownership – Leading financial institutions

Management – Professionals

– They cannot trade directly or indirectly.

Formation of Rules – Executive Committees.

Trading Rights – With Trading Members.

NSE's trading system - NEAT

:- National Exchange for Automated Trading.

Membership

(a) Normal Membership- (Professional Clearing Member) &

(b) Alpha Membership

1. Trading member
2. Trading Cum Self Clearing Member
3. Trading Cum Clearing Member
4. Professional Clearing Member

Trading Segments

1. Cash Segment (Capital Market segment): equity shares, warrants, debentures, MFs, Exchange Traded Funds, etc

2. Futures & Option Segment-

Trade on derivative instruments.

3. Currency Derivatives Segment-

Currency Futures trading in USD-INR

4. Debt Segment (Wholesale Debt Mkt - WDM)

Deals with Corporate Bonds ,Govt securities, T Bills, PSU Bonds, CPs, CDs, etc

Corporate Structure

I. Board of Directors

1. Chairman
2. Vice chairman
3. Managing Director

4. Share holder Director – 3 numbers
5. Public Interest Directors – 5 numbers

II. NSE Advisory Committee

III. Mandatory Committees- 15 numbers

Mandatory Committees

1. Membership Selection Committee
2. Disciplinary Action Committee
3. Investor Grievance Redressal Committee (IGRC)
4. Defaulters' Committee
5. Compensation Committee
6. Standing committee on Technology
7. Sub-Committee for Monitoring Compliance of suggestions given in SEBI Inspection Report
8. Investor Services Committee
9. Public Interest Directors' Committee
10. Arbitration Committee
11. Ethics Committee
12. Independent oversight committee for member regulation
13. Independent oversight committee for listing function

14. Independent oversight committee for trading and surveillance function.
15. Advisory Committee

Subsidiaries of NSE

1. National Securities Clearing Corporation Limited (NSCCL)
2. NSE Infotech Services Limited (NSETECH)
3. India Index Services & Products Ltd. (IISL)
4. DotEx International. Ltd. (DotEx)
5. NSE.IT Ltd.

ASSOCIATE / AFFILIATE COMPANIES of NSE

1. National Securities Depository Ltd. (NSDL)
2. National Commodity & Derivatives Exchange Ltd. (NCDEX)
3. Power Exchange India Limited (PXIL)

1. National Securities Clearing Corporation Limited (NSCCL)

NSCCL is a wholly owned subsidiary of NSE. It was incorporated in August 1995. Commenced clearing operations in April 1, 1996. The first clearing corporation to introduce settlement guarantee. Assigned the highest corporate rating of 'AAA' for three consecutive years. This is the first Indian Clearing Corporation to get this rating.

2. **NSE Infotech Services Limited (NSETECH)**

A wholly owned subsidiary of NSDL. Incorporated to cater to the IT needs of NSE and all its group companies exclusively.

3. **India Index Services & Products Ltd. (IISL)**

A subsidiary of NSE Strategic Investment Corporation Ltd. It was setup in May 1998. It provide a variety of indices and index related services and products for the Indian capital markets.

4. DotEx International. Ltd. (DotEx):

A wholly owned subsidiary of NSDL. To provide the data and info-vending products of NSE. A professional set-up dedicated solely for this purpose. Offers a secure and reliable trading gateway, providing immediate, scalable and seamless access through internet to members and internet investors.

5. National Securities Depository Ltd. (NSDL)

NSDL is the first depository in India. The enactment of Depositories Act in August 1996 paved the way for establishment of NSDL. NSE, IDBI and UTI to promoted NSDL for the dematerialisation of securities.

6. National Commodity & Derivatives Exchange Ltd. (NCDEX)

Incorporated in 2003 under the Companies Act, 1956. NCDEX is an on-line commodity exchange at nation-level. Technology driven de-mutualised on-line commodity exchange. It provides a world-class commodity exchange platform for market participants. Trade in a wide spectrum of commodity derivatives driven by best global practices, professionalism and transparency.

7. Power Exchange India Limited (PXIL)

India's first institutionally promoted Power Exchange. It provides innovative and credible solutions to transform the Indian Power Markets. PXIL has unique combination of local insights and global perspectives. It helps its stakeholders to make better informed business and investment decisions, improves the efficiency of the power markets, and helps shape policies and projects.

The Multi Commodity Exchange of India Ltd (MCX)

India's first listed exchange, that facilitates online trading, and clearing and settlement of commodity futures transactions. The First Indian SE to initiate evening trading session. (to coincide the trading timing with international markets.)

Incorporation - April 2002

H Q - Mumbai

Commenced operations - November 2003

- India's Largest Commodity Exchange

INDICES -MCX COMDEX

Index calculation:

simple weighted average of the three group indices- MCX AGRI, MCX METAL & MCX ENERGY

Membership

(1) Trading-cum-Clearing Member (TCM)

(a) Deposit Based

(b) Non-Deposit Based

(2) Self Clearing Member

a) Deposit Based

(b) Non-Deposit Based

(3) Institutional Trading-cum-Clearing Member (ITCM)

(4) Professional Clearing Member (PCM)

(5)Trading Member (TM)

Market – List of Commodities Available for Trading

1. Bullion

a) Gold

b) Silver

2. Base Metals

a) Aluminium

b) Copper

c) Lead

d) Nickel

e) Zinc

f)

3. Energy

a) Brent Crude Oil

b) Crude Oil

c) Natural Gas

4. **Agri-commodities**

a) Cardamom

b) Cotton

c) Crude Palm Oil

d) Kapas

e) Mentha Oil

National Commodities and Derivatives Exchange Ltd

Professionally managed on-line multi commodity exchange.

Promoter shareholders:

ICICI Bank , LIC, NABARD and NSE.

Indices - Dhaanya

- based on the prices of the 10 most liquid commodity futures traded on the NCDEX platform

Market :

(a) **Agricultural Products**

Cereals and Pulses (Barley, Chana, Wheat) ,**Fibres** (Cotton), **Guar Complex** (Guar Seed, Guar Gum), **Plantation Products** (Rubber), **Others** (Potato), **Oil and Oil seeds** (Castor seeds, Cotton seed, Soy Bean, Mustard Seed, Crude Palm Oil), **Soft** (Sugar, SGur), **Spices** (Pepper, Turmeric, JEERA, Chilli, Coriander)

(b) Non Agricultural Products

Metals (Steel, Copper), **Precious Metals** (Gold, Silver), **Energy** (Crude Oil, Brent Crude Oil)

World Federation of Exchanges (WFE)

Established in 1961. Headquartered in London. The World Federation of Exchanges represents 64 regulated exchanges across the world. WFE promotes the development of fair, efficient and transparent markets.

Major International Stock Exchanges

- On the Basis of Market Capitalisation -USD Million

1. **NYSE** **16813384.50**
2. **Nasdaq - US** **6733665.30**
3. Japan Exchange Group 4522775.00
4. Shanghai Stock Exchange 3490315.40
5. **Euronext** **3190921.90**

6. Hong Kong Exchanges and Clearing 2808048.80
7. Shenzhen Stock Exchange 2651787.70
8. **Deutsche Boerse 1563409.80**
9. **TMX Group 1551219.70**
10. **SIX Swiss Exchang 1395669.00**
11. BSE India Limited 1387357.60
12. NSE of India 1360363.10

1. NYSE –New York Stock Exchange

("Big Board“)

- **Largest Capital Market in the World**
- Intercontinental Exchange with diverse markets span.
- Established - 1792
- Listed Companies : 2800
- **HQ - New York in America**
- **Indices - NYSE Composite PR**
  - **NYSE Bitcoin Index**
  - **NYSE US 100 Index**

2. NASDAQ: National Association of Securities Dealers Automated Quotations

Second Largest SE in the World. The first SE that introduces Electronic Trading.

HQ **-New York in America**

Established **-1971**

Listed Companies **: 3100**

Major Indices -NASDAQ Composite

- NASDAQ-100,

- NASDAQ OMX PHLX (PHLX)

3. Japan Exchange Group JPX

- Formation – 1.1. 2013

By Merger of Tokyo Stock Exchange and Osaka Securities Exchange.

HQ - Tokyo, Japan

Listed Companies : 3506

Indices - JPX-Nikkei 400

- TOPIX

- JASDAQ

4. Shanghai Stock Exchange

Founded : 1990

Headquarters : Shanghai, China

Listed Companies : 1084

Indices - SSE 180, SSE 50, SSE Mega Cap

5. EURONEXT

Formation – 2000 By Merger of Amsterdam, Brussels and Paris Markets.

The first Pan-European SE

Euronext Exchange locations: London, Brussels, Lisbon, Amsterdam, Paris

Listed Companies : 1300

Indices- AEX GR, AEX NR, AEX IDEX, BEL 20

6. **Hong Kong Exchanges**

- Headquartered in Hong Kong, Chaina.
- SEHK, HKFE, HKSCC are merged in 1999 under a single holding company, HKEx.
- Main index – S&P/HKEx LargeCap Index, S&P/HKEx GEM Index, Hang Seng Index, CES China HK Mainland Index +

7. Shenzhen SE (SZSE)

- Based in Shenzhen, Guangdong ,Chaina
- Created in 1990.
- Main index – SZSE Component, SZSE Energy, SZSE Composite Index

8. **Deutsche Börse**

- Based in Eschborn, Germany
- Company history starts from 1585
- Company was founded in 1992.

Main index : STOXX, DAX, MDAX, TecDAX, SDAX

9. TMX Group

- Headquarters: Toronto, Canada (America)
- Is an integrated, multi-asset class exchange group.

(Toronto Stock Exchange, TSX Venture Exchange, TSX Alpha Exchange, The Canadian Depository for Securities, Montréal Exchange, Canadian Derivatives Clearing Corporation, NGX, BOX Options Exchange, Shorcan, Shorcan Energy Brokers, AgriClear)

Main index S&P/TSX Composite Index, S&P/TSX Venture Composite Index,

DERIVATIVES

Dic. meaning: something which is based on another source.

"Derivative is a contract that *derives* its value from the performance of an underlying entity."

This underlying entity can be an asset, commodities, precious metals, currency, bonds, stocks, interest rate, stocks indices, etc. Price of Derivative depends on price of underlying commodity.

Features of Derivatives

1. Value of derivative depends on the price of the underlying asset.

2. Derivatives are tradable securities.
3. Derivatives like futures and options are traded in Stock Exchanges.
4. Derivatives like Forwards and swaps are not traded in Stock Exchange.
5. Derivatives are contracts, not assets. Securities are assets.
6. In ‘futures’ parties of contract have obligation to settle the contract
7. In ‘options’ the buyer of the contract has the right to execute or cancel the contract.

Types of Derivatives:

Financial, Commodity, Currency

Product/Instruments of Derivatives:

Options, Futures and Swaps

Participants in Derivative Market

1. **Hedgers:** Risk averse investors. Wants to enhance safety. They wish to protect themselves from the risk involved in price movements.
2. **Speculators:** Risk loving investors. They conduct risky trades to improve profits.
3. **Arbitrageurs:** Buy low in one market and sell high in the other market. Simply put, taking advantage of differences in prices in the two markets.
4. **Margin traders:** Margin trading is a unique payment mechanism of derivative market. With a small deposit, you are able to maintain a large

outstanding position. Margin traders are speculators.

Types of Derivative Contracts

Futures	Forwards
Options	Swaps

1. **Futures**

Contract to buy/sell asset on a future date. The settlement of the contract takes place on a specific future date at fixed price (agreed today).

Futures are standardised contracts.

Hence tradable in Stock Market

2. **Forwards**

Contract to buy/sell asset on a future date. The settlement of the contract takes place on a specific future date at fixed price (agreed today).

Forwards are not standardised contracts.

They are tailor made.

Hence not tradable in Stock Market

3. **Options**

Contract gives an option to buy/sell asset on a future date. The settlement of the contract takes place on a specific future date or before, at fixed price.

They are similar to Futures. The key difference is there is no obligation to buy.

Options are tradable in Stock Market

Option Premium: Price paid by the buyer to the seller to acquire the right.

Strike Price or Exercise Price: The predetermined price of the underlying asset, if the contract is settled before the expiry date.

Types of Options

(a) Call Option: The option to buy

(b) Put Option: The option to sell

(c) European Option: Option can be exercised only on the expiry date

(d) American Option: Option can be exercised on or before the expiry date

Warrants :- Options for a period of more than one year. They are not traded in SE

Baskets :- Options where the underlying asset is an average of a basket of assets.

Eg. SENSEX, NIFTY50

4. **Swap**

Swap is an act of exchanging one thing for another. It is a derivative contract where two parties exchange financial instruments.

These instruments can be almost anything.

Eg. Commodity swap, Debt equity swaps, etc

Interest Rate Swaps: Swapping one type of interest rate for another type.

Currency Swaps: Swapping one type of interest rate for another type.

4a. Swaptions: An option on a forward swap

Features of Swaps

Swaps are complex instruments.

They are not available for trade in the stock markets.

Retail investors do not generally engage in swaps.

Rather, swaps are over-the-counter contracts

Generally swaps are between businesses or financial institutions.

Requirements for Swap:

Double coincidence of Wants-

Two parties with equal and opposite needs.

Long term agreement.

History of Commodity mkt in india

- 1927 :East Indian Jute Association Ltd
- 1939 –Futures trading in several commodities banned II World war
- 1955-

Recent Trends in Global Capital Markets

Remarkable Changes after Liberalisation

1. SEBI ACT 1992.
2. Disclosure & Investor Protection (DIP) Guidelines.
3. Investor Protection measures.
4. Screen based trading.
5. Shorter Trading Cycles.
6. Derivatives Trading.
7. Demutualisation of SE.
8. Establishment of Depositories.
9. Risk Management Systems.
10. Integration with Global Markets.
11. Initiatives in G-Sec Market.
12. ASBA IN Public Issues.
13. Exit option for Ses.
14. ICDR Regulations in 2009.

Disclosure & Investor Protection

(DIP) Guidelines.

- In 1992 'Capital Issues (Control) Act was cancelled.
- Govt's control over capital issues come to an end.
- Market forces are allowed to control the capital issues.

- SEBI issues DIP guidelines periodically to ensure transparency.

Demutualisation of SE

Enforces at least 50% non-broker representation in the "Board of SEs". Separation of Management and Trading Membership.

Risk Management Systems.

- Capital adequacy of members
- Adequate margin requirements.
- Limits of exposure and turnover.
- Indemnity insurance.
- Online position monitoring.
- Automatic disablement.
- Trade-settlement guarantee.
- Index based market wide circuit breakers

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