Gujarat Board Textbook Solutions Class 12 Organization of Commerce and Management Chapter 9 Financial Market

1. Select the correct alternative and write answer to the following questions :

Question 1. Securities market having maturity period of one year or less means
(A) Capital market
(B) Primary market
(C) Money market
(D) Secondary market
Answer:
(C) Money market

Question 2. Who regulates organized money market?
(A) SEBI
(B) State Bank of India
(C) Reserve Bank of India
(D) Financial Institutions
Answer:
(C) Reserve Bank of India

Question 3. Who issues treasury bills on behalf of Indian Government?
(A) State Bank of India
(B) Reserve Bank of India
(C) Central Bank of India
(D) Financial Institutions
Answer:
(B) Reserve Bank of India

Question 4. Which statement is false with reference to commercial bills?
(A) Government Security
(B) Origin out of Business Transaction
(C) Discounted by Commercial Banks
(D) Negotiable Instrument
Answer:
(A) Government Security

Question 5. Market for sale of new issues securities means
(A) Stock exchange
(B) Primary market
(C) Secondary market
(D) Speculation market
Answer:
(B) Primary market

Question 6. Whose approval is to be obtained by stock exchange under securities contracts (Regulation) Act, 1956?
(A) Central Government
(B) SEBI
(C) Reserve Bank of India
(D) Finance Minister
Answer:
(B) SEBI

Question 7. In which year Depository Act came into existence?
(A)1991
(B)1992
(C)1995
(D)1996
Answer:
(D)1996

Question 8. From whom certificate of registration is to be obtained by a depository before starting its operation?
(A) Stock exchange
(B) Central Government
(C) SEBI
(D) Reserve Bank of India
Answer:
(C) SEBI

Question 9. How many types of orders are there in purchase-sales of securities?
(A) Two
(B) Three
(C) Four
(D) Five
Answer:
(A) Two

Question 10. Under which Act, SEBI came into existence?
(A) Companies Act
(B) Securities Contracts (Regulation) Act
(C) National Companies Act
(D) Securities and Exchange Board of India Act (SEBI Act)
Answer:
(D) Securities and Exchange Board of India Act (SEBI Act)

2. Answer the following questions in one sentence each :

Question 1. What is the time period for the maturity of instruments of money market?
Answer:
One year or less

Question 2. At what price treasury bills are issued?
Answer:
Discounted price

Question 3. Which financial instruments are traded in money market?
Answer:
Treasury bill, commercial paper, call money, etc.

Question 4. When was Bombay Stock Exchange established?
Answer:
On 9th July, 1875

Question 5. By whom are stock exchanges regulated in India?
Answer:
Through Security Exchange Board of India (SEBI) and Security Contract Regulation Act.

Question 6. By whom are depository services availed?
Answer:
In India, an investor can avail services of depositories through (1) National Securities provide the depository facilities in Depositories Limited (NSDL) and (2) Central Depository Services (India) Limited (CDSL).

Question 7. When did Depository Act come into force?
Answer:
In 1996

Question 8. When did NSDL establish and start its operation?
Answer:
In 1996

Question 9. Which is the first depository of India?
Answer:
National Securities Depositories Limited (NSDL)

Question 10. By which name screen based trading of National Stock Exchange and Bombay Stock Exchange are known?
Answer:
Screen based trading of National Stock Exchange is known as NEAT (National Bombay Stock Exchange is known as BOLT i.e. BSE Online Trading.

Question 11. What is meant by Contract note in the purchase-sales procedure of securities?
Answer:
Contract note is a confirmation of the order placed by the investor on a particular day. In other words, contract note is a summary as well as agreement about the traded securities.

3. Answer the following questions in short :

Question 1. What is unorganised money market?
Answer:
The informal form of money market which is not regulated by a government body is called unorganised money market.

Question 2. What are the instruments of money market?
Answer:

- Treasury bill,
- Commercial paper,
- Commercial bill,
- Certificate of Deposit,
- Call/Notice money, etc.

Question 3. Which instrument of money market are negotiable?
Answer:

1. Commercial paper,
2. Commercial bill and
3. Certificate of Deposit

Question 4. What is the main difference between call money and notice money?
Answer:
Call money ¡s borrowed for only 1 day whereas notice money is borrowed for minimum 2 days to maximum 14 days.

Question 5. How does stock exchange provide liquidity element to securities?
Answer:
Stock exchange ¡s a ready market in which traders (investors) can buy or sell shares as per their will. This is how stock exchange provides liquidity.

Question 6. Stock exchange is a mirror indicating economic condition of the country – How?
Answer:
Investors invest in share market. This way public savings gets converted as capital for industries and companies. When companies grow by using these funds the investors further invest in the market. The cycle of trade in stock exchange depicts how well or poor is country's economy.

Question 7. What is dematerialisation?
Answer:
The process of converting physical shares in electronic form is called Dematerialization or demat in short.

4. Answer the following questions in brief :

Question 1. What is treasury bill?
Answer:
Treasury Bills:

- When the central government is in need of funds for short term, it issues treasury bills into the financial market. Anyone willing to buy them such as individuals, firms, etc. can buy these bills.
- Thus, a treasury bill is a short term financial instrument (government security). It is issued by Reserve Bank of India on behalf of Government of India.
- Treasury bill is an important component of money market all over the world.
- Treasury bill is also known as T-Bills'.
- The lock-Mn period or maturity of these bills is 91 days, 182 days or 364 days.
- The minimum amount of a T-bill is ₹ 25,000/- and then in multiples of ₹ 25,000/-.
- Government does not pay any interest to people who buy T-bills, but sells these bills at a discounted rate. Hence, T-bill is also called 'zero coupon bond'.
- For example, government might sell Treasury bill of ₹ 25,000 at ₹ 23,500 to the investor. The investor would then be paid the actual value i.e. ₹ 25,000 on maturity date. Thus, the difference between the purchase amount and redemption amount becomes the profit for the investor.

Question 2. Give the meaning of capital market and clarify its characteristics.
Answer:

- A capital market (locally – share market) is an organized market in which capital is raised by the investment made by general public in the form of shares, debentures, bonds, etc.
- When companies issue equity shares in the market, investors buy them. The money invested becomes the capital for the company who issued the shares. So, the companies and industries get fund through the savings of general public.

Capital market is divided into two markets. They are:

1. Primary market and
2. Secondary Market

- Capital market is a source of long term capital fund for industrial enterprises.
- Long term securities like shares and debentures are traded in capital market.
- Capital market is a market for all types of securities including industrial securities and government securities.
- Since this market mobilizes savings of the community, it boosts economic growth.

Characteristics of capital market:

- Capital market is a market for raising long term capital fund.
- Instruments of capital market include government securities, debt instruments, securities of industrial enterprises like shares and debentures.
- Investment of fund is in long term securities.
- In India, capital market is strictly regulated by Securities and Exchange Board of India (SEBI).
- Ownership of shares and debentures is easily transferrable.
- Provides liquidity to financial assets (securities).
- Capital market is divided into two parts –
  1. Primary market and
  2. Secondary Market

Question 3. "Primary market means a market of new issued securities" – Explain and state the characteristics of primary market.
Answer:

- When a company publicly sells new stocks or securities and bonds for the first time in the market, the market is called the primary capital market.
- So, primary capital market is the market of newly issued securities.
- Here, the investors buy only newly issued securities as it is a market for new issued securities. The objective of the primary capital market is to raise capital fund for the company issuing the securities.

Characteristics of primary capital market:

- It is a market for newly issued securities.
- The companies issue new securities for investors to buy.
- There are numerous intermediaries in primary market like lead manager, registrar of issue, share broker, etc.
- New capital is issued through prospectus in primary market.

5. Answer the following questions in detail :

Question 1. What is money market? State its characteristics.
Answer:
Money market:

- Money market refers to a section of financial market where financial instruments (assets) with high liquidity and short-term maturities are traded. It is a market for assets or instruments which are close substitutes for money.
- Financial assets traded in money market include treasury bills, certificate of deposits, call money, money via. money lenders, pawn, indigenous bankers, shroffs, etc.
- Money is borrowed and lent for a short term. Securities or financial assets having a maturity period of one year or less are traded in this market.
- It is important to note that unlike stock exchange, money market is not a physical location, but group of various institutions trading or dealing in money.
- Transaction takes place between two parties. One is lender and the other is borrower.
- Reserve bank, commercial banks, co-operative banks, shroffs, etc. are mainly included in the group of money lenders, while individuals, business enterprises, farmers, traders, state governments, central government are the borrowers of money.

Characteristics of money market:

- Money market is divided into two parts. They are:
  (a) Organized money market and
  (b) Unorganized money market.
- Money market is a market for short term assets or instruments, whose maturity period is one year or less.
- Credit worthiness of participants in money market is important so that both the borrower and lender can trade at ease.
- Money market is not a fixed physical location but a collective structure of various institutions like Reserve Bank of India, commercial banks, financial institutions, mutual funds, insurance companies, indigenous bankers, shroffs, etc.
- It is a market of financial instruments which can easily be converted into cash (i.e. are highly liquid). For example, treasury bills, call money, etc.
- Sub-branches of money market also develop with economic and technological development, such as call money market, bond market, treasury bills market, etc.
- Most of the financial instruments are debt instruments. Element of risk is less as compared to other financial instruments.
- The success and operation of money market depends on the banking system and financial institutions.

Question 2. What are the characteristics of stock exchange?
Answer:
Characteristics of stock exchange (Secondary market):

1. Registered corporate body: Stock exchange is a registered and established corporate body that prepares rules and regulations for the transactions of securities.
2. Approval of government: Stock exchange has to obtain approval of the central government as per the provision of Securities Contracts (Regulation) Act, 1956.
3. Organized market: It is an organized market for dealing in existing listed securities.
4. Membership: Membership of stock exchange must be obtained for dealing transactions in stock exchange.
5. Market of securities: Stock exchange is an approved organized market for buying and selling of securities.
6. Listing of securities: The securities which are listed on stock exchange are transacted in stock exchange.
7. Management: It is administered and managed by board of directors.
8. Strict control over the members: The Board of Directors exercise strict control over the members through their disciplinary powers.
9. Organizational structure: The organizational structure of stock exchange is in the form of public company.
10. Regulation of stock exchange: All the stock'exchanges of India are regulated by Securities and Exchange Board of India (SEBI) and Securities Contracts (Regulation) Act.

Question 3. What are the functions of stock exchange?
Answer:
Functions of Stock Exchange (Secondary market):
1. Liquidity:

- Stock exchange provides continuous market for purchase and sale of securities. Investors can purchase and sell securities with their free will because stock exchange provides ready trade market.
- An important function of the stock exchange is to see that the securities remain liquid.

2. Valuation of the securities:

- The demand and supply of the securities in the market decide their valuation or say price.
- The valuation of securities is also determined by other factors such as dividend declared by the company, factors affecting money market, etc.
- Valuation of securities enables the investors to decide whether to purchase or sell the securities.
- The valuation of securities is also useful to the government and creditors.

3. Conversion of savings into capital:
Individuals who wish to invest their savings in the securities can easily do so. This way their savings get converted into capital.

4. Intermediary in the creation of capital:
Stock exchange itself does not create capital. It provides platform for the purchase and sale of securities. When the securities are traded the capital gets generated. Thus, the stock exchange plays the role of intermediary for creating capital.

5. Safety of transactions:

- The securities are traded as per the rules of the stock exchange. Moreover, the stock exchange is governed by SEBI which is a government body.
- The brokers working in stock exchange perform their role under the regulation of SEBI. Owing to all these things, it can be said that financial transactions are carried out safely in the stock exchange.

6. Growth of capital market:

- Investors invest in share market. This way public savings gets converted as capital for industries and companies.
- These units form long term capital. When companies grow by using these funds the investors further invest in the market. This boosts the overall economy. Thus, development of capital market also leads to development of economic development of the country.

7. Facilities to perform activities:
Stock exchange enables its members to perform their activities. The members then work to protect the interests of the investors and for healthy growth of the market.

8. Necessary facilities for speculation:

- Healthy speculation keeps the stock exchange alive.
- Stock exchange provides necessary facilities for the transactions of speculation within the legal structure.

9. Information provider:

- Stock exchange provides important information useful to the various parties. For example, information about changes in the price of securities, flow of purchase and sale of securities, etc.
- Such information serves as an important guide for investors, companies, government, SEBI, etc.

- The information is useful for the government for formulating economic policy and financial policy.
- The information also describes the economic condition and growth of company and nation. Hence, the stock exchange is called the barometer of the economic condition of the country.

10. Listing of securities:

- If companies desire that the transactions of their securities get conducted in the stock exchange, then they may get their securities listed on stock exchange.
- When securities get listed in the stock exchange, the trust of investors increase for such securities.

11. Guidance to investors:
Stock exchange discloses the financial information of listed companies. This information helps the investors to decide in which security they should invest and in which they should withdraw.

Question 4. Write a Note :
(a) National Securities Depository Limited, (b) Central Depository Services Limited (c) SEBI
Answer:
(a) National Securities Depository Limited:

- The full form of NSDL is National Securities Depository Limited. It was the first electronic securities depository of India. It was established and registered with SEBI in 1996.
- NSDL is a public depository company formed under the Companies Act. Since it is a public company, it is managed by Board of Directors.
- In order to form NSDL, the National Stock Exchange (NSE) and some financial institutions promoted it.
- NSDL appoints several depository participants which then executes the functions of NSDL. These participants work as agents between the investors and NSDL.
- NSDL does not charge any fee from the investors for their investments. NSDL takes this fee from the depository participants.
- Thus, investor has neither to pay any fee, nor any operating charges directly to NSDL. However, depository participant charges some fees from the customer/ investor.

Online Services of NSDL (via. participants):

- Dematerialization and Rematerialization
- Electronic settlement of transactions
- Crediting right and bonus shares in customer’s account
- Freezing customer’s account, etc.

(b) Central Depository Services Limited:
Central Depository Services (India) Limited (CDSL) is the second electronic depository of India.

- It was established in 1999 in Mumbai with collaboration of Bombay Stock Exchange and some banks.
- Just like NSDL, CDSL provides online depository services all over India. It aims at easy and safe services to the investors.
- It publishes the list of its registered depository participants time to time on its website.

(c) SEBI:

Securities and Exchange Board of India(SEBI) came into existence as a statutory body on January 30, 1992 under the Securities and Exchange Board of India Act 1992.

- its head office is in Mumbai. It has regional offices in Kolkata, Delhi and Chennai, SEBI is a statutory body regulating stock exchanges in India.

Objectives of SEBI:

1. To protect the interest of investors in securities
2. To encourage the development of securities market
3. To regulate the securities market

Functions of SEBI:
1. To regulate business in stock exchange:

- SEBI regulates the business in stock exchanges and the operations of the stock exchanges. It monitors whether the specified rules and guidelines are followed or not by share brokers, sub-brokers, merchant bankers.
- It keeps an effective control on the entire working of the stock exchanges.

2. Protection of the interest of the investors:
The fundamental function of the SEBI is to protect the interest of the investors. So, it enforces the intermediaries to obey the specified rules and regulations.

3. Registration and regulation of intermediaries:

- It registers the intermediaries such as merchant banker, share broker, sub-broker, registrar of securities, etc. working in stock exchange and monitors their functions.
- It plans for the training of intermediaries.

4. Registration and regulation of mutual funds:
It registers and monitors mutual funds and regulates their working. For this, SEBI has determined rules and regulations which are followed by mutual funds.

5. To prevent fraudulent trade:
It takes necessary steps to prohibit fraudulent trade in stock exchanges.

6. To cancel registration of brokers:
It cancels the registration of share brokers who do not follow rules and guidelines determined by SEBI and who fail to provide necessary information to SEBI.

7. To regulate the merger and take-over of the companies:
It regulates merger and take-over of the companies for preserving the interest of investors. SEBI has issued guidelines so that merger and take-over do not take place at the risk of small investors. .

8. Guidelines with reference to public issues:
SEBI has issued different guidelines for both, first time capital issue by new company and capital issue by existing company coming in market for capital.

9. Self-regulation:
SEBI is active for the self-regulation followed by intermediaries of stock exchange. It encourages the intermediaries to promote their professional unions.

10. Maintaining stock exchanges as an efficient market:
It maintains stability and efficiency of stock exchanges through regulations, restrictions and guidelines.

11. Inspection of books:
If necessary, it inspects the books of company that issues securities, depository participant and beneficiary owner.

12. Monitoring and inspection of stock exchange:

- SEBI can monitor and inspect whether regulations laid down for stock exchange are followed or not, whether stock exchange organization system and its working is followed as per SEBI Act or not.
- If necessary, it conducts inquiry, inspection and audit of the accounts of the intermediaries.

13. Guidelines:
SEBI has issued guidelines time to time for share brokers, and sub-brokers, merchant bankers, trustees of debenture, buy back securities by company, etc.

14. To obtain annual and periodical reports:
It receives report in form of various statements for obtaining information about working and activities of stock exchanges.

15. Research work:
SEBI undertakes the research work so that all the above functions can be done effectively.

Question 5. Explain the purchase-sale procedure of securities in stock exchange.
Answer:
The procedure of purchase and sales of securities online is as follows:
1. Opening demat account:

- First of all the investor needs to approach any depository participant (DP) and open a demat account with it.The DP opens this account under NSDL or CDSL.
- The investor can purchase/sell/hold their shares in the demat account.

2. Order to buy-sell:

- Once the demat account is active, the investor can trade online.
- Investor who wants to sell securities needs to place an online order with the broker.
- While purchasing/selling, the investor need to carefully mention the details such as name of the share, price at which the investor wants to purchase or sell, etc.

There are two types of order in purchase and sale of securities. They are:
(a) Limited order:

- When an investor selects the option of 'limited order', it means that he will set the price at which he needs to purchase or sell the shares. Thus, in this case, the price of purchase and sale is pre-determined.
- Retail investors and fund houses generally trade by placing order in this format.

(b) Market order:
When an investor wants to trade at the prices existing in the market, he selects 'market order'. Here, the buying/selling iakes place at the latest quoted market price that appeared on the trading screen order was made.

3. Execution of order:

- When the investor places the online order with the broker, the broker further executes the order. The broker places the order in stock exchange.
- The broker on behalf of his customer (investor) can conduct transaction from his office through online trading.

4. Contract note:

- Once the broker further places the order received from the investor, he prepares a contract note for the investor.
- Contract note is a confirmation of the day on which transaction took place.
- Generally, the broker sends contract note to the customer within 24 hours after transaction takes place.
- The contract note contains details such as name of the security traded, quantity, total amount of transaction, order number, brokerage, taxes applicable, etc. Thus, contract note is a summary as well as agreement about the traded securities.

5. Settlement of transaction:

- The settlement houses settle the transactions.
- The settlement house of Bombay settles the transactions done under Bombay Stock Exchange.
- NSCCL-National Securities Clearing Corporation Limited performs the settlement of transaction done in National Stock Exchange.
- Settlement of transaction occurs after a day of transaction or trade.

6. Payment of amount and delivery of security:

- If the investor has purchased the shares, he has to make the payment prior to the pay-in day. The delivery is done to the investor on pay-out day.
- If the investor has sold the shares, delivery of shares is to be done prior to the pay-in day. ,
- Customer receives money on 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.

7. Inform customer about settlement of transactions:

- If the investor has sold the securities, the broker will make the payment to the customer through bank.
  In case if the investor has purchased the securities, the broker will make payment directly from the investor's bank account.
- Settlement of transaction is informed to the customer through demat account.