

CBSE Test Paper - 02
Chapter - 10 Financial Markets

1. Which of the following is a method of floatation? **(1)**
 - a. Private Placement
 - b. All of these
 - c. Offer for sale
 - d. Offer through prospectus
2. _____ Market instruments enjoy higher degree of liquidity. **(1)**
 - a. Capital market
 - b. Both money and capital market
 - c. None of these
 - d. Money market
3. The total number of Stock Exchanges in India is: **(1)**
 - a. 23
 - b. 21
 - c. 22
 - d. 20
4. Which of the following is not a part of capital market? **(1)**
 - a. Stock Exchanges
 - b. Financial Institutions
 - c. Banks
 - d. RBI
5. State any two **Developmental Functions** of Securities and Exchange Board of India. **(1)**
6. Name the form of shares in which they are stored under Depository system? **(1)**
7. State the function of financial markets is highlighted here " Financial markets facilitate easy purchase and sale of financial assets". **(1)**

8. Define 'Capital Market'? **(1)**

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

In context of the above case:

- a. Name and explain the way through which the company can raise finance by allotting securities to selective individuals and institutions only.
- b. Can the company also raise capital through a right issue? Why or why not? Give a reason to justify your answer. **(3)**

10. Give the meaning of the following money market instruments

- i. Treasury bill; and
- ii. Call money **(3)**

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

- i. Name the function being performed by the market in the above case.

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- ii. Name the market segment other than the capital market segment in which unsecured and short-term debt instruments are traded. Also, give any three points of difference between the two. **(4)**
12. These days, the development of a country is also judged by its system of transferring finance from the sector where it is in surplus to the sector where it is needed most. To give strength to the economy, SEBI is undertaking measures to develop the capital market. In addition to this there is another market in which unsecured and short-term debt instruments are actively traded everyday. These markets together help the savers and investors in directing the available funds into their most productive investment opportunity.
- i. Name the function being performed by the market in the above case.
- ii. Also, explain briefly three other functions performed by this market. **(4)**
13. After doing a course in online trading, Arsh started an online portal for stock trading under the name 'Investment Guru'. He met his school friend Ajay after a long time in a bank where Ajay had come to open a D-Mat account. Arsh urged Ajay to invest in the forthcoming IPO of a blue chip company whereas Ajay was inclined to buy existing securities of the other companies to build his investment portfolio.
- In the context of the above case:
- a. Identify the two different types of the capital market being referred to by quoting lines from the para.
- b. State any four differences between the two different types of capital markets as identified in part (a). **(5)**
14. Explain the regulatory functions of SEBI. **(5)**
15. Explain the concept of depository and name and explain two types of depositories in India? **(6)**

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Answer

1. b. All of these

Explanation:

There are various methods of floating new issues in the primary market:

- i. Offer Through Prospectus This involves inviting subscription from the public through issue of prospectus.
- ii. Offer for Sale Under this method securities are not issued directly to the public but offered for sale through intermediaries like issuing houses or stock brokers.
- iii. Private Placement Private placement is the allotment of securities by a company to institutional investors and some selected individuals.
- iv. Rights Issue This is a privilege given to existing shareholders to subscribe to a new issue of shares according to the terms and conditions of the company.
- v. e-IPOs A company proposing to issue capital to the public through the on-line system of the stock exchange has to enter into an agreement with the stock exchange.

2. d. Money market

Explanation:

Money market instrument enjoy a higher degree of liquidity. A segment of the financial market in which financial instruments with high liquidity and very short maturities are traded.

3. c. 22

Explanation:

Total number of stock exchanges in India: 22. They are in: Ahmedabad, Bangalore, Calcutta, Chennai, Delhi etc. There is also a National Stock Exchange (NSE) which is located in Mumbai. More than 6,000 stocks listed.

4. d. RBI

Explanation:

The Reserve Bank of India is India's central banking institution, which controls the monetary policy of the Indian rupee. RBI is not a part of capital market.

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5. **Under developmental categories following functions are performed by SEBI:**
- a. SEBI promotes training of intermediaries of the securities market.
 - b. SEBI tries to promote activities of stock exchange by adopting a flexible and adaptable approach.
6. The form of shares in which they are stored under Depository system is electronic form.
7. The function of financial markets is "Provide liquidity to financial assets"
8. A capital market is a financial market in which long-term debt (over a year) or equity-backed securities are bought and sold. Capital markets channel the wealth of savers to those who can put it to long-term productive use, such as companies or governments making long-term investments.
9. a. Equity financing is the process of raising capital through the sale of shares. Companies raise money because they might have a short-term need to pay bills or they might have a long-term goal and require funds to invest in their growth. The company can raise finance by allotting securities to selective individuals and institutions only through Private Placement. It is a relatively economical way of raising money as it helps to save time, cost and money involved in the process of issuing securities.
- b. No, the company cannot raise capital through a rights issue as it is issuing securities for the first time. A rights issue is a pre-emptive right given only to the existing shareholders to subscribe to the securities of the company as per its terms and conditions.
10. i. **Treasury bill:** Also known as zero coupon bond, a T-Bill is issued by RBI on behalf of Central Government to meet its short-term requirement of funds and is thus categorised as money market instrument. It is issued in the form of promissory note.
- They are highly liquid and have negligible risk. They are issued at discount and redeemed at par, e.g. 91 days, treasury bill of face value of Rs1,00,000 is purchased at Rs 96,000 and at the maturity investor gets Rs 1,00,000, Rs 4000 being the interest received by him. The Reserve Bank of India conducts auctions usually every Wednesday to issue T-bills. The rationale is that since their maturity is lower, it is more convenient to avoid intra period interest payments.
- ii. **Call money:** Call money is a short-term finance repayable on demand, with a

maturity of 1 to 15 days. It is used for inter bank transactions. Banks have to maintain a minimum cash balance known as Cash Reserve Ratio. Call money is a method by which banks borrow from each other to be able to maintain Cash Reserve Ratio. The interest paid on call money loans is called call rate, which is very volatile and changes even from hour to hour.

11. i. The function performed by the market in the above case is—Mobilisation of savings and channelising them into the most productive use or allocative function.
- ii. Money market is the market segment where unsecured, short-term debt instruments are traded. The three points difference between money and capital market are

Basis	Capital market	Money market
Meaning	It refers to the whole network of organisations, institutions and instruments that deal in medium and long-term funds. Capital markets channel the wealth of savers to those who can put it to long-term productive use, such as companies or governments making long-term investments.	Money market is a market for short-term funds which deals in monetary assets whose period of maturity is upto one year.
Duration	Period of maturity is more than one year.	Period of maturity ranges from one day to one year.
Liquidity	Only actively traded securities have ready market.	In this market, there is a formal arrangement for creating liquidity.

12. i. The function performed by the market here is mobilisation of savings and channelising them into the most productive use/allocative function.
- ii. The other three functions of financial market are:
 - a. **Facilitating price discovery:** The price of any goods or services is determined by the forces of demand and supply. Like goods and services, the investors also try to discover the price of their securities. The financial market is helpful to

the investors in giving them proper price.

- b. **Reduce the cost of transactions:** Financial market provides complete information regarding price, availability and cost of various financial securities. So, investors and companies do not have to spend much on getting this information.
- c. **Provides liquidity to financial assets:** The investors can invest their money, wherever they desire, in securities through the medium of financial market and convert them into cash by selling their financial assets through the mechanism of financial market.

13. a. Capital market is a market for medium and long term funds. It includes all the organisations, institutions and instruments that provides long term and medium term funds. According to VK Bhalla, "Capital market can be defined as the mechanism which channellises saving into investment or productive use. Capital market allocates the capital resources amongst alternative uses. It intermediates flow of savings of those who save a part of their income from those who want to invest it in productive assets". The two different types of the capital market being referred to are-

- i. Primary Market: "Arsh urged Ajay to invest in the forthcoming IPO of a blue-chip company."
- ii. Secondary Market: "Ajay was inclined to buy existing securities of the other companies to build his investment portfolio."

- b. Differences between Primary Market and Secondary Market:

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

		investors.	
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14. Regulatory functions of SEBI are as follows

- i. To regulate business in stock exchanges.
- ii. To register and regulate the working of intermediaries.
- iii. To register and regulate the working of mutual funds.
- iv. To conduct inquiries and audit of stock exchange.
- v. Regulation of taken-over bids by companies.
- vi. To register and regulate the working of stock brokers, sub-brokers, share transfer agents, bankers to an issue, trustees of trust deeds, registrars to an issue, merchant bankers, underwriters, portfolio managers, investment advisors and such other intermediaries who may be associated with securities markets in any name.
- vii. To register and regulate the working of the depositories, participants, custodians of securities, foreign institutional investors, credit rating agencies.
- viii. To register and regulate the working of venture capital funds and collective investment schemes including mutual funds
- ix. To promote and regulate self-regulatory organizations
- x. To prohibit fraudulent and unfair trade practices relating to securities markets

15. A depository in a simple term means a place where something is a deposit for storage and security, however in our capital market, this term has a lot of relevance, we define **“Depository as an institution that works like the bank”** Likewise our bank holds investor fund, similarly, depository maintains an account for investors securities (share, debentures, mutual fund etc) hold by them in a dematerialized or an electronic form. Investor used to hold the securities in the form of physical certificate which has their own disadvantages and to take control over the irregularities of the capital market for the protection of an investor`s interest, Depository system has been introduced in India where the securities could be handled in an electronic form by the process of dematerialization. **Depositories in India:** We have 2 depositories in India which are well known as NSDL (National securities depository limited) and CSDL (Central Depository Services (India) Limited). They interface with the investors through their agents called Depository participants (DPs). DPs could be the banks (private, public and foreign), financial institutions and Sebi-registered trading members.