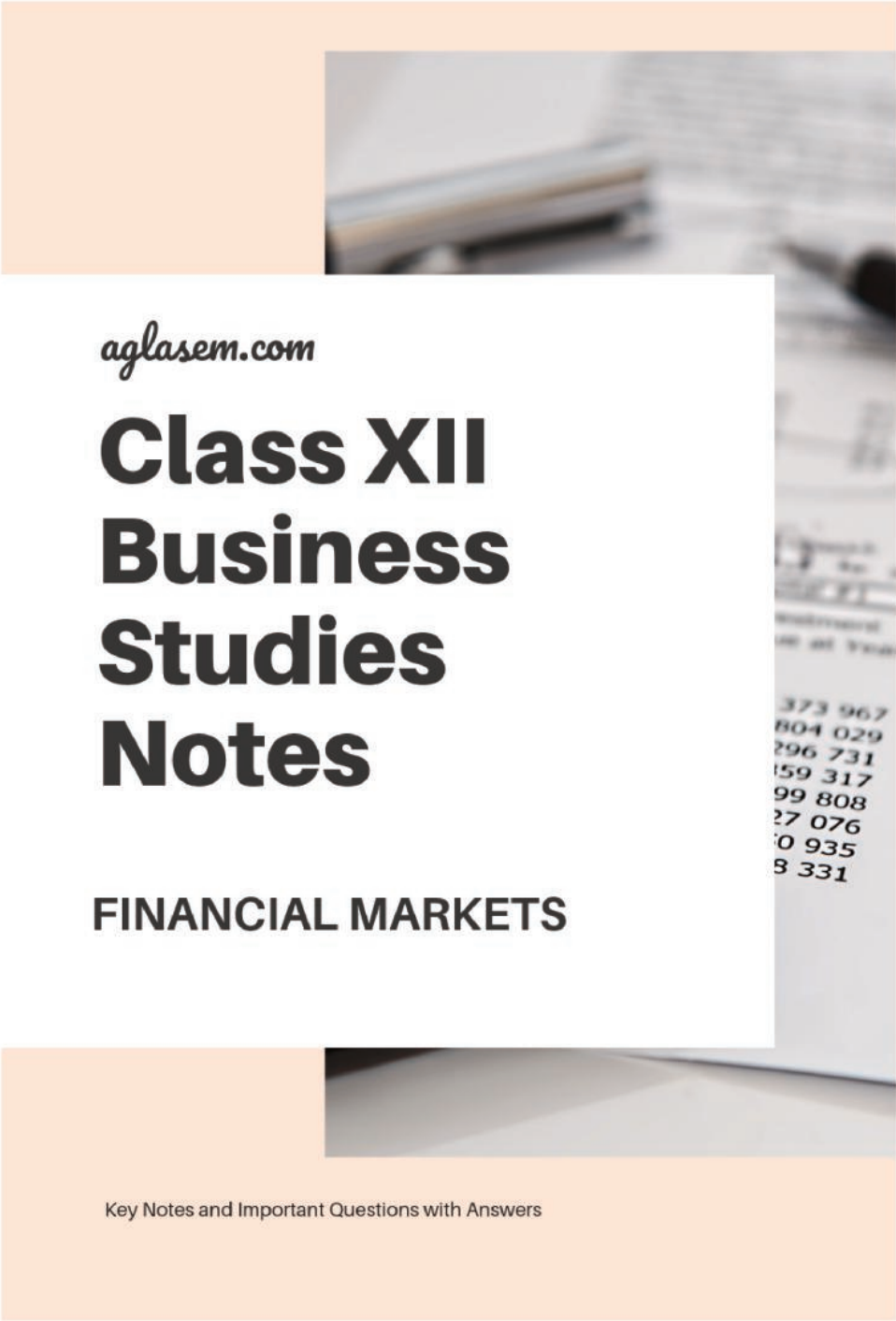




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Class XII Business Studies Notes

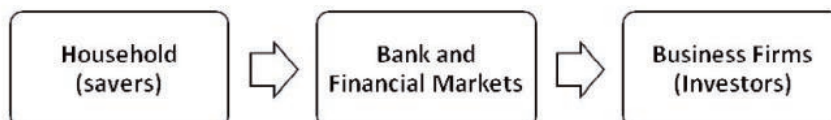
FINANCIAL MARKETS

Key Notes and Important Questions with Answers

CHAPTER – 10

FINANCIAL MARKETS

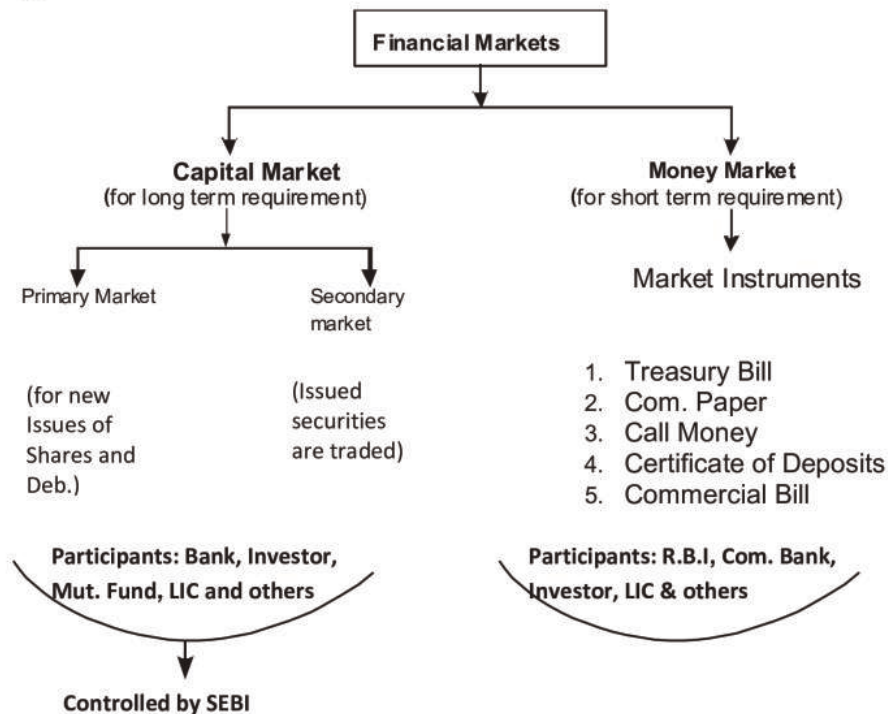
Financial Market is a market for creation and exchange of financial assets like shares, bonds etc. It helps in mobilising savings and channelizing them into the most productive uses. It helps to link the savers and the investors by mobilizing funds between them. The persons or institutions by which allocation of funds is done are called Financial Intermediaries. They bring together borrowers and lenders and make funds available to those willing to pay for their use,



Functions of Financial Markets

1. **Mobilisation of Savings and channeling them into the most productive uses** : Financial market facilitates the transfer of savings from savers to investors and thus helps to channelize surplus funds into the most productive use.
2. **Helps in Price Determination** : Financial Market helps in interaction of savers and investors which in turn helps in the determination of prices of the financial assets such as shares, debentures etc.
3. **Provides Liquidity to Financial Assets** : Financial market facilitates easy purchase and sale of financial assets. Thus, it provides liquidity to them so that they can be easily converted into cash whenever required.
4. **Reduces the Cost of Transactions** : Financial market provides valuable information about securities which helps in saving time, efforts and money and thus it reduces cost of transactions.

Types of Financial Markets



Money Market

It is a market for short term funds/securities whose period of maturity is upto one year. The major participants in the money market are RBI, Commercial Banks, Non-Banking Finance Companies, State Government, Large Corporate Houses and Mutual Funds. The main instruments of money market are as follows:

1. **Treasury Bills:** They are issued by the RBI on behalf of the Central Government to meet its short-term requirement of funds. They are issued at a price which is lower than their face value and are repaid at par. They are available for a minimum amount of Rs. 25000 and in multiples thereof. They are also known as Zero Coupon Bonds. They are negotiable instruments i.e. they are freely transferable.

2. **Commercial Paper:** They are short term unsecured promissory notes issued by large credit worthy companies to raise short term funds at lower rates of interest than market rates. They are negotiable instruments transferable by endorsement and delivery with a fixed maturity period of 15 days to one year.

This source is usually used for-

- (i) Working Capital requirements
- (ii) Seasonal needs
- (iii) Bridge financing

3. **Call Money:** It is short term finance repayable on demand, with a maturity period of one day to 15 days, used for interbank transactions. Call Money is a method by which banks borrow from each other to be able to maintain the cash reserve ratio as per RBI. The interest rate paid on call money loans is known as the call rate.
4. **Certificate of Deposit:** It is an unsecured instrument issued in bearer form by Commercial Banks & Financial Institutions. They can be issued to individuals, Corporations and companies for raising money for a short period ranging from 91 days to one year.
5. **Commercial Bill:** It is a bill of exchange used to finance the working capital requirements of business firms. A seller of the goods draws the bill on the buyer when goods are sold on credit. When the bill is accepted by the buyer it becomes marketable instrument and is called a trade bill. These bills can be discounted with a bank if the seller needs funds before the bill maturity.

Q.1	List any two participants of money market.	(1)
	[Banks, LIC]	
Q.2	What is the minimum amount of Treasury bill?	(1)
	[₹ 25,000]	
Q.3	Who is borrower of call money?	(1)
	[Banks]	

Q.4	Which bearer certificate is issued by banks against the deposits kept by companies and institutions for short period? [Hint: Certificate of deposits]	(1)
Q.5	What is other name of Zero Coupon Bonds? [Hint: Treasury bill]	(1)
Q.6	What is near money? [Hint: All short term securities]	(1)

Capital Market

It is a market for long term funds where debt and equity are traded. It consists of development banks, commercial banks and stock exchanges. The capital market can be divided into two parts:

1. Primary Market

It deals with the new securities which are issued for the first time. It is also known as the New Issue Market. The investors in this market are banks, financial institutions, insurance companies, mutual funds and individuals. It has no fixed geographical location and only buying of securities takes place in the primary market.

Methods of Floatation of New Issues in Primary Market

- 1. Offer through Prospectus/ Initial Public Offer** :It involves inviting subscription from the public through issue of prospectus. A prospectus makes a direct appeal to investors to raise capital through an advertisement in newspapers and magazines.
- 2. Offer for Sale:** Under this method security are offered for sale through intermediaries like issuing houses or stock brokers. The company sells securities to intermediary/broker at an agreed price and the broker resells them to investors at a higher price.
- 3. Private Placements:**It refers to the process in which securities are allotted to institutional investor and some selected individuals.
- 4. Rights Issue** : It refers to the issue in which new shares are offered to the existing shareholders in proportion to the number of shares they already possess.

5. **e-IPOs** : It is a method of issuing securities through an on-line system of stock exchange. 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. This is called an e-initial public offer. SEBI's registered brokers have to be appointed for the purpose of accepting applications and placing orders with the company.

Q.1	Identify the method of floatation highlighted in each statement:	
a)	Offer the entire new issue to life insurance company. [Private placement]	(1)
b)	Issue a prospectus to invite public to apply for share. (IPO)	(1)
c)	Use on line system of stock exchange. (e-IPO)	(1)
d)	First ask existing shareholders to apply for new shares as it is compulsory requirement under companies Act. (Rights issue)	(1)
Q.2	What is prospectus?	
Q.3	Pranjal has 500 shares of L&T. L&T comes out with a fresh issue of shares and Pranjal received an offer to buy 1 share of L&T for every 5 shares held by her. Which method of floating new issue is indicated in this case? [Rights issue]	(3)

2. Secondary Market

It is also known as the stock market or stock exchange where purchase and sale of existing securities takes place. They are located at specified places and both the buying as well as selling of securities takes place.

Difference between Primary and Secondary Market

Basis	Primary Market	Secondary Market
1. Securities	Only new securities are traded.	Existing securities are traded.
2. Price of securities	Prices of securities are determined by the management of the company.	Prices are determined by the forces of demand and supply of the securities.

3. Purchase and sale.	Securities are sold to investors directly by the company or through intermediary.	Investor exchange ownership of securities.
4. Place of market	There is no fixed geographical location.	Located at specified places.
5. Buying/selling	Only buying of securities takes place.	Both buying and selling of securities can take place.

Q.1 Identify the markets highlighted in following statements:

1. This market directly contributes to capital market. (Primary market)
2. This market deals in instruments whose maturity is upto one year.
(Money market)
3. It deals in medium and long term securities. (Capital market)
4. It is also known as Stock Exchange and deals in sale and purchase of previously issued securities. (Secondary market)
5. It requires less investment as value of securities is generally low.
(Capital market)

Q.2 Dinesh has 100 equity shares of a company. He wants to sell 500 of these shares. Which market should he approach? Write any three advantages of selling through such a market. (4)

[Hint: Secondary Market (any three advantages)]

Q.3 Why are money market instruments more liquid as compared to capital market instruments? (3)

[Hint: Reliable participants and duration of investment is less]

Stock Exchange/Share Market

A Stock Exchange is an institution which provides a platform for buying and selling of existing securities. It facilitates the exchange of a security i.e. share, debenture

etc. into money and vice versa. Following are some of the important functions of a Stock Exchange:-

1. **Providing liquidity and Marketability to Existing Securities** : Stock Exchange provides a ready and continuous market for the sale and purchase of securities.
 2. **Pricing of Securities** : Stock Exchange helps in constant valuation of securities which provide instant information to both buyers and sellers and thus helps in pricing of securities which is based on the forces of demand & supply.
 3. **Safety of Transaction** : The members of a stock exchange are well regulated, who are required to work within the legal framework. This ensures safety of transactions.
 4. **Contributes to Economic Growth** : Stock exchange provides a platform by which savings get channelised into the most productive investment proposals, which leads to capital formation & economic growth.
 5. **Spreading of Equity Culture** : Stock exchange helps in educating public about investments in securities which leads to spreading of Equity culture.
 6. **Providing Scope for Speculation** : Stock exchange provides scope within the provisions of law for speculation in a restricted and controlled manner.
- Bombay Stock Exchange (BSE) and National Stock Exchange (NSE) are famous stock exchanges in India.

Trading and Settlement Procedure on a Stock Exchange

1. **Selection of Broker**: In order to trade on a Stock Exchange first a broker is selected who should be a member of stock exchange as they can only trade on the stock exchange.
2. **Opening Demat Account with Depository**.
3. **Placing the order**: After selecting a broker, the investors specify the type and number of securities they want to buy or sell.
4. **Executing the order**: The broker will buy or sell the securities as per the instructions of the investor.

5. **Settlement:** Any trade taking place gets settled within 2 days of the trade date.

Q. 1 The directors of a company want to modernise its plant and machinery by making a public issue of shares. They wish to approach the stock exchange, while the finance manager prefers to approach a consultant for the new public issue of shares. Advise the directors whether to approach the stock exchange or a consultant for new public issue of shares and why. Also advise them about different methods which the company may adopt for the new public issue of shares. (Ans. Consultant) **(3)**

Difference between Capital and Money Market.

S.No. Basis	Capital Market	Money Market
1. Participants	Financial Institutions, Banks, Corporate Entities, foreign investors and individuals	RBI, Banks Financial Institutions & financ ecompanies
2. Instruments Traded	Equity shares, bonds preference shares and debentures.	Treasury Bills, Tradebills, commercial paper, call money etc
3. Outlay Investment	Does not necessarily require a huge financial outlay.	Entail huge sums of money as the instruments are quite expensive.
4. Duration	Deals in medium & long-term securities having maturity period of over one year.	Deals in short termfunds having maturityperiod upto one year.
5. Liquidity	Securities are less liquid as compared to money market securities.	Money marketinstruments are highly liquid.

6. Expected return	High return	Low return
7. Safety	Capital Market instruments are riskier both with respect to return and repayment.	Money market instruments are generally much safer with a minimum risk of default.

Depository Services and DEMAT Accounts: Keeping in the mind the difficulties to transfer of shares in physical form, SEBI has developed a new system in which trading in shares is made compulsory in electronic form. Depository services system and Demat Account are very basis of this system.

1. **Depository Services:** 'Depository is an institution/organization which holds securities (e.g. shares, debentures, bonds, mutual funds etc.) in electronic form, in which trading is done. The services provided by a Depository are termed as 'Depository Services'. At present there are two depositories in India: NSDL. (National Securities Depository Ltd.) and CDSL (Central Depository Services Ltd.).

Services provided by Depository

- (i) Dematerialisation (usually known as demat) is converting physical certificates to electronic form.
- (ii) Rematerialisation, known as remat, is reverse of demat, i.e getting physical certificates from the electronic securities.
- (iii) Transfer of securities, change of beneficial ownership.
- (iv) Players in Online Trading: Settlement of trade is done on exchange connected to the Depository. Now a days on-line paper-less trading in shares of the company is compulsory in India. Depository services is the name of that mechanism. In this system transfer of ownership in shares take place by means of book entry without the physical delivery of shares. When an investor wants to deal in shares of any company he has to open a Demat account. There are four players who participate in this system.

1. **The Depository :** A depository is an institution which holds the shares of an investor in electronic form.
2. **The Depository Participant :** He opens the account of Investor and maintains securities records. Generally banks work as depository participant.
3. **The Investor :** He is a person who wants to deal in shares whose name is recorded.
4. **The Issuing Company:** That organisation which issues the securities. This issuing company sends a list of the shareholders to the depositories.

Benefits of Depository Services

- Sale and Purchase of shares and stocks of any company on any stock Exchange.
- Saves time.
- Lower transaction costs
- Ease in trading.
- Transparency in transactions.
- No counterfeiting of security certificate
- Physical presence of investor is not required in stock exchange.
- Risk of mutilation and loss of security certificate is eliminated.

2. Demat Account

Demat account is the abbreviation of 'Dematerialized Account'. Dematerialized account refers to an account which an Indian citizen must open with the depository participant (banks, stockbrokers) to trade in listed securities in electronic form wherein one can hold shares of various companies in the Dematerialized {electronic} form. Access to De-mat account requires an internet password and a transaction password. Transfer and purchase of

securities can then be initiated. Purchase and sale of securities on the Demat account are automatically made once transaction is confirmed and completed.

Opening of Demat Account

A Demat account is opened on the same lines as that of a bank account. Prescribed account opening forms available with the DP, need to be filled in. Standard agreement is to be signed by the client and the DP, which details the rights and obligation of both parties. Along with the form, the client is required to attach photograph, attested copies of residence proof, PAN card number and proof of identity need to be submitted.

Benefits of Demat Account

1. Reduces paper work.
2. Elimination of problems on transfer of shares such as loss, theft and delay.
3. Exemption of stamp duty when transfer of shares.
4. The concept of odd lot stand abolished.
5. Increase liquidity through speedy settlement.
6. Attract foreign investors and promotes foreign investment.
7. A single demat account can hold investments in both equity and debt instruments.
8. Traders can work from anywhere.
9. Automatic credit into demat account for shares arising out of bonus/split/consolidation/merger.
10. Immediate transfers of securities.
11. Change in address recorded with a DP gets registered with all companies in which investor holds securities, eliminating the need to correspond with each of them.

Securities and Exchange Board of India (SEBI)

SEBI was established by Government of India on 12 April 1988 as an interim administrative body to promote orderly and healthy growth of securities market and for investor protection. It was given a statutory status on 30 January 1992 through an ordinance which was later replaced by an Act of Parliament known as the SEBI Act, 1992. It seeks to protect the interest of investors in new and second hand securities.

Objectives of SEBI

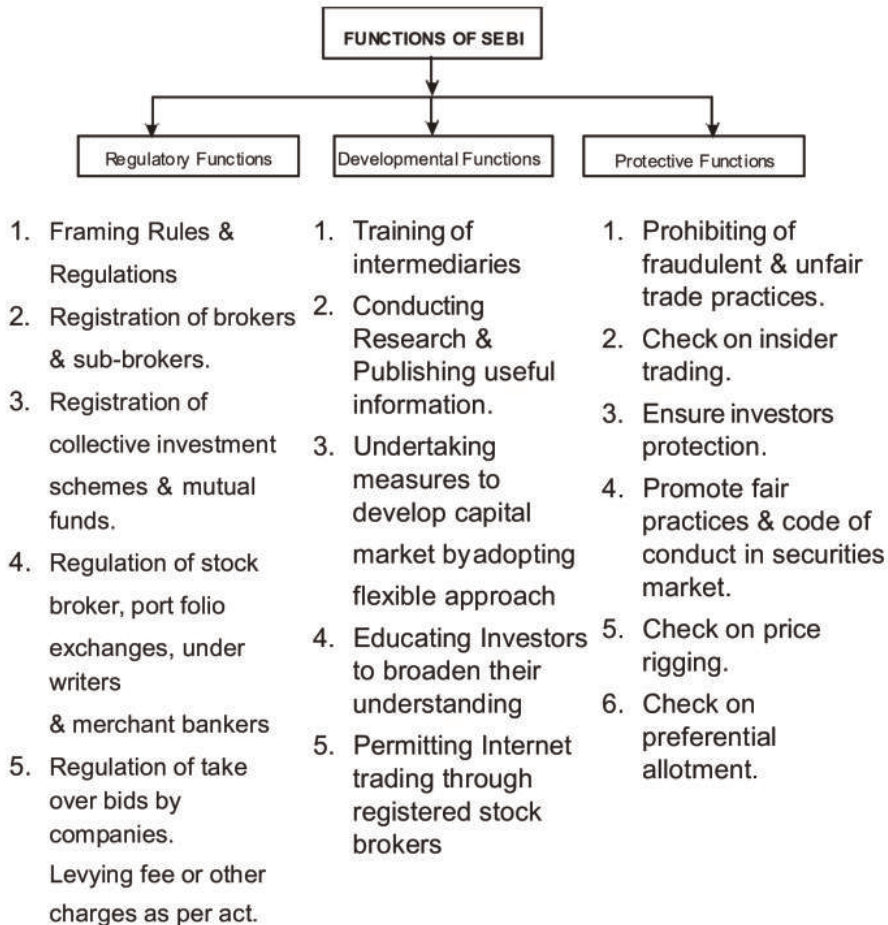
1. To regulate stock exchange and the securities market to promote their orderly functioning.
2. To protect the rights and interests of investors and to guide & educate them.
3. To prevent mal-practices in trade such as insider trading.
4. To regulate and develop a code of conduct and fair practices by intermediaries like brokers, merchant bankers etc.

Functions of SEBI

The SEBI performs three important functions

1. **Regulatory functions:** These functions are performed by SEBI to regulate the business in stock Exchange.
2. **Developmental functions:** These functions are performed by SEBI to promote and develop activities in stock market.
3. **Protective functions:** These functions are performed by SEBI to protect the interest of investors and provide safety of investments.

Functions of SEBI



- **Check on Price Rigging:** Making manipulations with sole objective of inflating or depressing the market price of securities is called 'Price Rigging'. Such practises are prohibited by law because they can defraud or cheat investors.

- **Check on Unfair Trade Practices:** SEBI does not allow the companies to make misleading statements in prospectus which are likely to induce the sale or purchase of securities by any other person.
- **Check on Insider Trading:** SEBI prohibits 'insider trading' and imposes penalties for such practices. An insider is any person connected with the company who is having price sensitive information (in respect of securities of the company), which is not available to the general public. Directors, promoters, etc. are the insiders. When such directors, promoters, etc. of the company use inside information to make individual profits, it is referred to as 'insider trading'.

Q.1	Name the organisation which has been established in India to regulate stock exchanges and to protect the rights and interest of investors. (SEBI)	(1)
Q.2	Expand the following-CDSL, NSDL, DEMAT	(3)
Q.3	Shabnam wants to invest her savings in share market. What is the base requirement for this? (DEMAT Account)	(1)
Q.4	Julie wants to get her share certificates in electronic form. What is the name of service provided by depository? (Dematerialisation)	(1)
Q.5	Bandhu Limited is a real estate company, which was formed in 1960. In about 55 years of its existence, the company has managed to carve out a niche for itself in this sector. In order to establish itself in India, the company decided to list its securities on BSE, in order to raise money through India market. State the functions performed by SEBI that make investors comfortable and secured in dealing with Bandhu Ltd.	(3)
	(Regulatory, Developmental and Protective Functions)	

Key terms to Crack Case Studies

1. New issue market — Primary market
2. Market for existing securities — Secondary market
3. Arrangement by which banks borrow from each other to be able to maintain the cash reserve ratio — Call money
4. Bridge financing — Commercial papers
5. Market for short term funds — Money market.
6. Market for medium term and long term funds — Capital market
7. Zero coupon bonds issued by RBI on behalf of Govt. of India — Treasury bills
8. Institution holding securities in electronic form — Depository
9. Holding securities in electronic form — Dematerialisation.
10. Watch dog of securities market — SEBI
11. Allotment of securities to institutional investors — Private Placement
12. Selling shares to investing public through intermediaries — Offer for sale.
13. Offering new shares to existing shareholders — Rights Issue
14. Unsecured instrument issued in bearer form by commercial banks and financial institutions during the time of tight liquidity — Certificate of deposit.
15. A person who accesses and uses the price sensitive information for his personal benefit — Insider Trading.

QUESTIONS FOR PRACTICE

- Q1.** Sudha Ltd. has sold 1 lakh equity shares of Rs. 10 each at Rs. 12 per share to an investment banker, who offered them to the public at Rs. 20 each. Identify the method of flotation.(offer for sale) (1)
- Q2.** 'Primary market contributes to capital formation directly. Whereas secondary markets do so indirectly'. Explain? (2)
- Q3.** Mohan wants to sell 50 shares of Tata Motors. Explain the trading procedure of shares. (5)
- Q4.** Charu is a chartered accountant in Prakash Ltd. During the course of meeting with directors she came to know that as against the previous years, this year company is going to declare handsome dividend offer. It is observed that when such news becomes public then the share-market jumps up. Considering it, Charu purchased large number of company's shares before this news reached the public.
- (1) Identify type of malpractice used by Charu. (1)
- (2) Name the authority which regulates such behaviour. Write any three other functions of this authority. (4)
- Q5.** A company wants to set up a new branch in Chennai. For additional capital company is planning to issue equity shares to public as there is boom period in capital market and public will prefer to invest in shares.
- While analysing the issue, finance manager found that floatation costs of the issue would be high and company is already in liquidity crunch. Company deemed it proper to depend on money market instruments for about six months.
- (i) Identify the method of flotation of capital, mentioned above.(IPO) (1)
- (ii) Besides above shares issue method, mention two other methods. (2)
- (iii) Use of what kind of instrument will be appropriate for the money market. Clarify.(commercial papers) (2)

- Q.6** Name the institution which is a body of individuals, whether incorporated or not, constituted for the purpose of assisting, regulating and controlling the business of buying and selling or dealing in securities. Explain any of its three functions.
- Q.7** The Director of Pico Limited decided to declare bonus issue of equity shares to the shareholders in its Annual General Meeting. Immediately one of the Director purchases 20,000 shares from market @ 30 per share and sold them @ 100 share as bonus issue was declared and made capital gain from it.
- (a) Name the practice used by the Director taking the benefits of internal information. (Insider Trading) (1)
 - (b) How does SEBI prohibit such practices? (2)
- Q.8** Name the financial instrument which may be used in the following situations:
- (a) A company needs funds to meet floatation cost in order to issue equity shares in the market.
 - (b) The instrument that is issued during the period of tight liquidity when the deposit growth of bank is slow but demand for credit is high.
 - (c) These are also known as zero coupon bonds and are issued by RBI on the behalf of central government.
 - (d) It is used by one bank having surplus funds to meet the funds requirements of another bank facing shortage of funds. (4)
- Q.9** Kajal has 1000 equity shares of a company. She wants to sell 500 of these shares. Which market should she approach? Give reason in support of your answer. (1)
- Q.10** Jain Ltd. has sold 1 lakh equity shares of ₹ 10 each at ₹ 12 per share to an investment banker, who offered them to the public at ₹ 20 each. Identify the method of floatation. (1)

UNIT 4

EVALUATION QUESTIONS

- Q.1** Pavco Ltd. was declared as a SICK UNIT as it was suffering from losses since last 5 years. To rehabilitate the UNIT, overall financial restructuring of a company was initiated. Mr. Rahul was appointed as new Finance Manager of the company. Mr. Rahul analysed and found that company was suffering due to scarcity of capital. He organised new issue of 1,00,000 equity shares of Rs. 1,000 each. Issue was fully subscribed with arranged capital. Mr. Rahul replaced the old plant with new one which was technologically updated and as per the industry demand. Its payback period was 3 years and it was promising a good rate of return. Just after two years, company was turned into a profitable venture.
- (a) Which two decisions are taken by Mr. Rahul as finance manager. Explain them. (2+2)
- (b) In which capital market, shares are issued? Explain. (2)
- (a) Financing decision, Investment decision (b) Primary market.
- Q.2** Managing director of a company was reviewing the newly designed capital structure of company which was framed by Finance Manager. He found that debt component was less than equity. Company was earning good return with sound and stable earnings since last 12 years. MD discussed with Finance Manager, that by having comparative less debt component, earning per share have reduced.
- (i) Name the concept of Financial Management, mentioned here. Explain it with the help of a suitable example. (1+3)
- (ii) In which market, will the New debentures be issued by company. Write any two features of such market. (1) Trading on Equity (2) Primary market) (1+1)
- Q.3** SABU Ltd. is facing liquidity crunch. Working capital is in shortage and it is finding difficult to pay the suppliers in time. Credit period which is allowed by

suppliers is two months. Finance Manager is of the opinion that for at least three months, company will not have sufficient funds to pay off creditors. Although, it has good financial reputation in market.

- (i) Which short-term financial instrument company should use? (1)
- (ii) In which market short-term financial instruments are issued? (1)
- (iii) Explain any three factors affecting requirement of working capital?(3)

[(i) Commercial Paper

(ii) Money market]

Q.4 GETO Ltd. is a company that produces school bags. Now it wants to produce water bottles also. For such diversification it needs additional capital of Rs. 50 crores, So company decided to float capital by way of equity shares issue to the general public as it is boom period in market. But company's cash position is not favourable. In order to arrange working capital, company wants to use some money market instruments. It will help in meeting floatation costs.

- (i) Identify the method of floatation of capital as mentioned in the above paragraph. (1)
- (ii) Besides above share issue method, mention two other methods. (2)
- (iii) Which money market instruments will be appropriate? Clarify. (3)

Ans. Hints: (i) Offer through prospectus

(ii) — Offer for sale, private placement

— Commercial Paper - used for bridge financing (explanation)

Q.5 A student asked teacher - "How can a company arrange for fixed capital which is to be used in long - term projects?"

Teacher explained as

"If company wants to have funds, it can issue shares directly to public or it can sell the whole issue to intermediaries. After subscribing the shares,

shareholders are not bound to keep it with them. They can sell it in the market and get them encased.

In the above paragraph, two kinds of capital markets are highlighted. Name them and write two features of each kind of markets. (2+4)

(Primary market, secondary market)

Q.6 In 2nd five year plan, "Industrialisation" was the "Main Focus". But the major problem was saving and Investment-Household used to invest in GOLD & Property only. Government had to take initiative for establishing Infrastructure and other basic industries. With pace of economic development, small savings were promoted by establishing an organised market. This market is regulated by SEBI and has attributed a lot in economic development.

(i) Identify the market. (1)

(ii) Name two functions of this market. (2)

(iii) (i) Secondary market

(ii) Promoting Savings, Economic development.

Q.7 XYZ Ltd. invited public to subscribe for equity shares of Rs. 100 each. Before the issue MD of the company had a deal with foreign company to amalgamate just after this issue. MD did not disclose this important fact in prospectus. It was highly objected, later by shareholders. Concerned Regulating Authority took action and MD was punished and penalised as per regulations.

(i) Identify the kind of capital market referred above. (1)

(ii) Name the Regulatory Body, mentioned above. (1)

(iii) Name any three other functions performed by the Regulatory Body. (3)

Ans. (Hints) (i) Primary Market

(ii) Securities Exchange board of India

(iii) To call for information.

- having fee or other charges.

- Training of intermediaries or (Any other)

Q.8 Avantika and Aanchal are close friends. They did their MBA together and got good placement from college campus as finance manager and production manager respectively in highly reputed companies.

Immediately after joining, Avantika found that her company was in dire need of additional production capacity. She arranged funds by issue of debentures and purchased a new plant with - higher production capacity.

- good rate of return.

- Low pay back period.

- less cost & Good pollution control technology.

On the other hand, Aanchal put the workers for production for more hours of work. She did not listen to the workers suggestions and grievances. She did not pay any incentive for good performance.

(i) Name two financial decisions mentioned in para 2. (2)

(ii) Quote the factors from above. Which affect the decision to purchase, fixed assets. (Any Two) (2)

Ans. (Hints) (i) Financing and Investing Decision.

(ii) Rate of Return, Payback period.

Q.9 Talco Ltd. is launching a new range of snacks which are 100% Fat free. Keeping in mind, the health conscious segment of market, company produced these cholesterol free snacks. For financing the production of snacks, company issued 10% debentures. Company was already burdened with fixed cost of salaries, Rent and 8% debentures interest.

(i) In which market, were the debentures issued? (1)

(ii) Do you think, issue of debentures was a wise choice Y/N. Justify your answer. (1+2)

(iii) What could be the other sources of finance available to Talco Ltd.

(Hints) (i) Primary Market

(ii) No Company was already burdened with fixed cost.

(iii) - Shares (Equity or Preference)

- Retained Earnings.

Q.10 Ravi was a trader dealing in woolen garments. His business flourished and he maintained a good reserve of retained earnings. Ravi expanded his business and started production of "shawls". Operating cycle period of shawls was quite long as Ravi made a policy for "Credit allowed" of four months to attract more customers. He was able to produce a good number of shawls with good quality and hand work.

(i) Name the market, through which working capital needs are satisfied.

(1)

(ii) What quantum of working capital was required when he was trader? As a producer how his need for working capital requirement has changed?

(2)

(iii) Apart from working capital, explain any three other factors, affecting requirements of working capital.

(3)

[(i) Money Market, (ii) As a trader less, as a producer-more]

Q.11 State Electricity Board under the ownership of state government was privatized in 2001. The company allotted securities to some selected individuals and institutions as this was a faster way of raising funds in public issue without any need for issuing a formal prospect. The company has since then been in operation for 15 years as a private sector company. The company has shown remarkable growth as indicated by rise in revenues, operating profit, profit after tax, resulting into maximisation of wealth of its shareholders. It has increased its assets base by buying fixed assets. As a private sector company, it has paid dividends in accordance with the policies stated in its articles.

a) Identify and explain, by quoting the lines, the decisions taken by the management in achievement of objectives of financial management after privatisation.

b) Identify the method of floatation opted by the State Electricity Board.

- c) How has the company maximised the wealth of its shareholders?

Hint:

- a) 1. "The Company allotted.....Formal prospectus.
Financing Decision
2. "It has increased.....fixed assets."
Investment decision
3. "As a private sector.....articles."
Dividend Decision
- b) Private placement
- c) By taking balanced finance decision i.e. Financing, Investment and Dividend decision as indicated by- rise in revenue, operating profit.

Q.12 The Trading procedure on Stock Exchange has been replaced by online screen based electronic trading system. This is mainly done to eliminate problems like theft, fake forged transfers, transfer delays and paper work associated with share certificates or debentures in physical form. This is a process where securities held by the investor in the physical form are cancelled and the investor is given an electronic entry or number so that he/she can hold it in an electronic balance in an account. This has increased the equity cult among the people.

- a) Identify and state the process mentioned above. (1)
- b) What is the most important requirement for the process identified in (a)? State. (1)

[(a) Dematerialisation (b) DEMAT account (c) Transparency, efficiency]

Q.13 Sakshi Ltd, a well known real estate company has managed to carve a niche for itself in this sector. Recently, it was revealed that the directors of the company have used price sensitive information for their own personal interest Adequate public disclosures were also not made. SEBI is considering action against these directors

Name the term used for trading malpractice done by the directors of this company.

Ans. Insider trading

Q.14 Bombay Stock Exchange was established in 1815 and was Asia's first stock exchange. About 6000 companies are listed on this exchange. Where investors purchase and sell their securities as shares, debentures and bonds. Price of the securities is determined by forces of demand and supply. The members of exchange are called brokers. They provide safe and fair deal to their customers. The Sensex launched in 1986 is made of 30 companies and represents 13 sectors of the economy. The change in Sensex saw the growth of economy. Explain the functions of Stock Exchange, highlighted above (3)

Ans. Hints

- (1) Platform for purchases and sale of securities
- (2) Price Discovery
- (3) Economic Growth