FINANCIAL MARKET FOR PRELIMS
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CAPITAL MARKET

- A medium for long term funds.
  - Developmental Financial Institution
  - Financial Intermediaries
  - Securities market :
    - Govt securities market : New issue and old issue market
    - Industrial securities market : New issue and old issue market

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Securities market

- It deals with shares and debt instruments.
- Fund raising mechanism
- In case of shares, the investors have a share in the capital and profit.
- In case of debt instruments , the investors do not have any share in the capital. Regardless of profit or loss, the debt instrument holders are entitled to receive interest income.
- In case of Debentures, there is some surety.

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- Shares are of two types :
- Equity shares : are shares that has claim over capital,profit or loss.
- Preference shares : are shares that have entitlement to a fixed amount of dividend . In the case of winding up of company, they have the right to get capital next to bond holders.
- The new issue market is known as primary market
- The old issue market is known as secondary market.

New Issue market

- Public issue
  - » Initial public offering
  - » Follow on public offering
- Other issue
  - » Private placement
  - » Rights issue
  - » Bonus issue
  - » Sweat equity issues

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- IPO : in the new issue market if any company or financial corporation issues shares for the first time, it is called IPO
- FPO : if any company or corporation that has already issued shares , issues shares again to raise additional fund

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Other Issue

- Private Placement : offering shares directly to the financial institutions, mutual funds and high worth investors.
  - PP are made to qualified institutional buyers.

  QIB: are those who are deemed financially sophisticated and are recognised by security market regulator to need less protection from issuers than most of the public investors.

  : Institutions like mutual funds, financial institutions, scheduled commercial banks, insurance companies, provident funds, pension funds, state industrial development corporation etc. falls under QIB

- Rights issue : means offer of security to the existing shareholders in the FPO. It flows to the existing shareholders as a matter of legal right.
- Bonus Issue : means offer of shares against distributable profit to existing shareholders.
- Sweat Equity Issue : means offer of shares to employees or Directors of the company which issue shares as recognition of their hard labour.

Shares	Debentures
Share capital is an ownership capital.	Debentures capital is credit to the company.
A shareholder is the owner of the company.	A debenture holder is the creditor of the company
Share capital is not returnable in the life time of the company. However, the redeemable preference shares are refunded during the life-time of the company.	Debenture capital returnable during the lifetime of the company. The exception is the irredeemable debentures which are not redeemable during the life-time of the company.
Equity Shareholders enjoy the voting rights.	Debentures holders do not have the voting rights.
Dividend is payable on shares & it is an appropriation of profits	Interest on debentures is payable at a fixed rate on specified date irrespective of profits of the company.

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Different types of capital

- Authorised Capital : means the maximum amount authorised by Memorandum of Association of a company that can be raised by the company. A company necessarily need not issue shares to the extent of authorised capital.
- Issued Capital : the actual amount issued by the issuer.
- Subscribed capital: the actual amount subscribed by the public after the company issues shares.

- Paid up Capital : the amount actually paid by subscribers when the money is demanded by issuer.
- Reserve Capital : Usually the issuer does not demand the whole amount from subscriber. A small portion of money is left undemanded. This uncalled (undemanded) portion of money is called reserve capital.

- Old Issue Market : 2 types
- 1) stock exchange : an institution for orderly buying and selling of listed securities.
- 2) Over the counter exchange : a platform for trading in securities that are not listed on a recognised stock exchange.

- Trading process
  - **Brokers** are registered members with stock exchanges to trade on behalf of clients.
  - **Sub Brokers** are trading persons affiliated with brokers. They act like branches to brokers. They are subject to SEBI guidelines.

Cash Trading : In this, the sale and purchase of securities take place in the prevailing price on the day of trading.

Forward Trading : both buyer and seller agree to buy and sell respectively at a future date at a pre agreed price, irrespective of the price that prevails on the day.

- 2 types of Forward Trade :
- 1) **Futures** : In this case, both buyer and seller have to execute the agreement.
- 2) **Option** : here, the seller or buyer can withdraw from the agreement. To have this option the buyer or seller has to deposit premium.
- The choice available to seller not to execute the agreement is called **Put Option**.
- If it is available to buyer it is called **Call Option**.

- The Futures and Options are Derivatives.
- **Derivatives** means any agreement which doesn’t have any independent value.
- **Depositories** are institutions that keep securities of investors in electronic format(Demat Format).
- NSDL is the first depository in India. It as established by UTI,NSE and IDBI.
- CDSL was established by BSE, Bank of India, Bank of Baroda, SBI and HDFC bank.

- NSE : established in 1993.
- BSE : established in 1887.
- **SENSEX :** stands for Sensitive Index. This measures the price movement of top 30 company shares. The top 30 companies are called Blue Chip Companies.
- **Nifty** : stands for National Index for Fifty.

- **Venture Capital Fund** : it provides funds to companies that produce new products based on innovations and to new industries.
- **Merchant banks** are also called as Investment Company.
- **Stock Broking Company** : are those who are registered with and recognised by SEBI to mediate or help investor in buying and selling of securities.

- **Face Value** is the actual value of shares.
- **Issue Price** means price of share including share premium.
- **Premium** means extra price a share claims in the market due to high demand for it.
- **Bull and Bear** : Rise in price is associated with bull and fall in price is associated with bear.
- **Securitisation** : is the method of converting existing assets into securities.

- **Buy Back** : means the issuer buying the securities again to accumulate share in his hands.
- **Net Asset Value** : is the net value of the outstanding shares. Net value means the total asset value minus liabilities of the mutual fund.
- **High Net Worth Individuals** are those who have net financial asset of atleast $ 1 million and those who have net worth atleast $30 million financial assets are called **ultra high net worth individuals**.

- **Mutual Funds** : mobilise the savings of the people and invest in securities.
- **Hedge Funds** : Incase of hedge funds, it is not public but a hand full of investors join together and form fund of their own and invest in different securities and use different investment strategies.
- So they do not need protection of SEBI and they are unregistered and unregulated.

- **Offer for Sale** : dilutes the shareholding of promoters in a listed company.
- As per Securities Contract Regulation Rules 157, at leastS 25% of all type of securities issued by a listed company should be in the hands of public.

Inflation Indexed Bonds (IIBs)

- Inflation Indexed Bond (IIB) is a bond issued by the Sovereign, which provides the investor a constant return irrespective of the level of inflation in the economy.
- The main objective of Inflation Indexed Bonds is to provide a hedge and to safeguard the investor against macroeconomic risks in an economy.

Gold Reserve Fund

- Gold Reserve Fund is a fund created by the Government of India to take care of the risk associated with its two schemes – Gold Monetization Scheme (GMS) and Sovereign Gold Bonds Scheme(SGB)– due to an increase in gold price.
- Gold Reserve fund is created by depositing the notional savings enjoyed by the Government in the costs of borrowing from GMS and SGB, as compared with the existing rate on government borrowings.

Sovereign Gold Bonds

- Sovereign Gold Bonds (SGBs) are a kind of Government bonds that are issued (by the RBI on behalf of the Government) on payment of rupees but denominated in grams of gold.
- The value of these bonds is tied to the value of gold.
- On redemption, the investor gets interest income and the prevailing price of gold.
- These bonds are thus, different from usual Government securities (G-secs) as the redemption value at the time of maturity is not a fixed sum, but linked to the price of an underlying commodity called gold.
- Like G-secs, SGBs are also backed by a sovereign guarantee.
- The introduction of the Sovereign Gold Bonds was announced in the Union Budget 2015-16

Gold Monetisation Scheme

- Monetization refers to a process of converting a commodity into domestic currency– rupee.
- Gold Monetization refers to unlocking the value of gold in terms of rupee.
- Gold Monetization Scheme (GMS) refers to a process wherein a depositor deposits gold (say jewellery, coin, etc.) with a bank which is then lent by the bank to its borrowers (say jewellery makers), after melting into gold bars.
- This is akin to a normal banking operation (like a savings bank account), but carried out in terms of gold instead of in rupee.
- GMS allows the depositors of gold to earn tax free market determined interest income (denominated in gold but recoverable either in gold or in rupee [mandatorily in rupee if it is deposited for a medium or long term]) from the pure gold they deposit with banks in their "Gold Savings Accounts" and permits the jewelers to obtain their raw material -gold bars created from the melting of the gold deposited with the banks- as loans in their "Metal account".
- In addition, Banks / other dealers would also be able to monetize their gold.

- Gold can be submitted in any form (bullion, jewellery etc) but the amount deposited with the bank is calculated on the basis of the pure gold content of that deposit (after removing the weights of precious stones in jewellery etc.), which is verified through an accredited assayer.
- Both principal and interest to be paid to the depositors of gold, will be 'valued' in gold.
- For example if a customer deposits 100 gms of gold and gets 1 per cent interest, then, on maturity he has a credit of 101 gms.
- The customer will have the option of redemption either in cash or in gold, which will have to be exercised in the beginning itself (at the time of making the deposit).

- **Objectives**

The Gold Monetization Scheme (GMS) was announced in the Union Budget Speech of 2015-16 with the following objectives:

- To mobilize the gold held by households, trusts and various institutions in India and put it into productive use.
- To provide a fillip to the gems and jewellery sector in the country by making gold available as raw material on loan from the banks.
- To be able to reduce reliance on import of gold over time to meet the domestic demand, as India is one of the largest consumers of gold with virtually no domestic production. (India imports as much as 800-1000 tonnes of gold each year. Though stocks of gold in India are estimated to be over 20,000 tonnes, most of this gold is neither traded, nor monetized.)
- To make the existing schemes for mobilising Gold (Gold Deposit Scheme and Gold Metal Loan Scheme) more effective and to broaden their ambit from merely mobilizing gold, to putting this gold into a broad range of productive uses including strengthening the reserve requirements of the Central Bank.

MIBOR and MIBID

- Mumbai Inter-Bank Offer Rate (MIBOR) and Mumbai Inter-Bank Bid Rate (MIBID) are the benchmark rates at which Indian banks lend and borrow money to each other. The **bid** is the price at which the market would *buy* and the **offer** (or **ask**) is the price at which the market would *sell*. These rates reflect the short term funding costs of major banks. In other words, MIBOR reflects the price at which short term funds are made available to participating banks.
- MIBID is the rate at which banks would like to borrow from other banks and MIBOR is the rate at which banks are willing to lend to other banks. Contrary to general perception, MIBID is *not* the rate at which banks attract deposits from other banks.
- MIBOR is the Indian version of London Interbank Offer Rate (LIBOR). MIBOR is fixed for overnight to 3 month long funds and these rates are published every day at a designated time

Infrastructure Investment Trust (InvITs)

- Infrastructure Investment Trusts (InvITs) are mutual fund like institutions that enable investments into the infrastructure sector by pooling small sums of money from multitude of individual investors for directly investing in infrastructure so as to return a portion of the income (after deducting expenditures) to unit holders of InvITs, who pooled in the money.

- InvITs can invest in infrastructure projects, either directly or through a special purpose vehicle (SPV).
- In case of Public Private Partnership (PPP) projects, such investments can only be through SPV.
- InvITs are regulated by the securities market regulator in India- Securities and Exchange Board of India.
- InvITs are very much similar to the Real Estate investment Trusts.

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Participatory Notes (P-Notes)

- Participatory Notes (P-Notes) are instruments used by foreign funds and investors not registered with the SEBI to invest in Indian securities.
- They are generally issued overseas by associates of India based foreign brokerages (FPIs) and domestic institutional investors.
- Technically, P-Notes are Offshore Derivative Instruments (ODIs) issued by FPIs and their subaccounts against underlying Indian securities (like shares).

- In a recent development, on July 8, 2017, SEBI issued a circular banning FPIs from issuing Participatory Notes for investing in equity derivatives. At the same time, FPIs can issue PNs to overseas investors if the equity derivatives investments are used for hedging the equity shares held by them

Offshore Derivatives Instruments

Offshore derivatives instruments (ODIs) are investment vehicles used by overseas investors for an exposure in Indian equities or equity derivatives.

These investors are not registered with SEBI, either because they do not want to, or due to regulatory restrictions.

These investors approach a foreign institutional investor (FII), who is already registered with SEBI.

The FII makes purchases on behalf of those investors and the FII's affiliate issues them ODIs.

The underlying asset for the ODI could be either stocks or equity derivatives like Nifty futures.