FINANCIAL MARKET & OPERATIONS

Second Internals Answer Scheme

Section A

1.     Primary market is that part of capital market, deals with issue of new securities.

2.     Book building is a price discovery method, in which the company gives a price bid range and invites bids from the investors. Based on the demand of the investors, price will be fixed.

3.     Greenshoe is a clause contained in the underwriting agreement of an IPO that allows underwriter to buy additional 15% of shares at offer price.

4.     MMMF is a mutual fund scheme invests exclusively on money market instruments.

5.     Load Fund is fund where mutual fund managers charge a fee at the time of purchase and sale of unit.

6.     Speculator is a person or an entity that is willing to take large risk and sacrifice the safety of principle in return for potentially large gains.

7.     European and American option is a type of option contract in which American option can be exercised at any time during its life time but European option can be exercised only at one single moment (expiring time).

8.     Money market is the market for short term instruments.

9.     Cash Reserve Rate means a portion of cash kept with RBI by commercial banks.

10.  Financial system is a set of institutions, instruments and markets which foster savings and channelize them to most efficient use.

11.  Shares that gives the holder different voting rights compare to someone who owns ordinary shares of a company. Two types: One that offer superior voting rights and one that offer lesser voting rights but higher dividends.

12.  ESOP is a type of employee benefit plan, which is intended to encourage employees to acquire shares of ownership in the company.

**Section B**

13.  Features of Primary market:

       Market for new long term capital. Also called as New issue market

       Securities are directly issued by companies to investors

       Company receives the money and issue new security certificates to the investors

       Purpose: Setting up new business or for expanding existing business

       Facilitates capital formation

 Functions of Primary Market

       Origination of new issue

       Underwriting

       Distribution of new issue

14.  Players in Derivative market:

  Hedgers: Traders who trade in products and are therefore exposed to risk and want protection

  Speculators: Speculator is a person or an entity that is willing to take large risk and sacrifice the safety of principle in return for potentially large gains.

  Arbitrageurs: they look for opportunities for making money out of price mismatches in two different markets

15.  Option Contract: Gives the buyer options to buy or selling an underlying asset at a predetermined price on or before a specified date in future.

Two Main Types: Call Option and Put Option

Call Option: Provided the holder the right to buy an underlying asset at a specified price for a certain period of time.

Put Option: Gives the holder the right to sell an underlying asset at a specified price.

16.  Innovative Financial Markets:

  Deep Discount Bonds: Bonds that is sold at a 20% blow the face value.

  Zero Coupon Bonds: Sold at discount and does not have any interest.

  Floating Rate Notes: Bonds that have variable coupon/interest, equal to money market reference rate like LIBOR

  Zero Coupon convertible Bonds: Combination of zero coupon bond and convertible bond

  Secured premium notes; financial instruments which are issued with detachable warrants and are redeemable after certain period.

  Equity with differential voting rights; Shares that gives the holder different voting rights compare to someone who owns ordinary shares of a company. Two types: One that offer superior voting rights and one that offer lesser voting rights but higher dividends.

17.  ETF: Exchange Traded Fund

An ETF is a basket of stock that reflects the composition of an index like NIFTY/BSE Sensex

Working:

  ETF own underlying assets like index shares of different companies

  Shares of different companies are pooled together and these cumulated shares form the asset base

  Cumulate assets are divided into different units and these units are listed and traded in the stock exchange as ETF

  ETFs that are listed in stock exchange can be traded like ordinary shares.

  Trading value of ETF is based on the net asset value of the underlying stocks that it represents

18.  Functions of SEBI

  Protective function: Protests interest of investors and issuers. Checks Price Rigging, Prohibits insider trading, prohibits fraudulent and unfair trade practices, investor education.

  Developmental Function: Provide training to intermediaries, investor education, conducting research and publishing information

  Regulatory Function: To regulate the business in stock exchanges

  Other Function: Registering and regulating the working of stock brokers registrars to an issue, merchant bankers, venture capitalists.

19.  Capital Market is a market for long term instruments.

Instruments: Equity Shares-Preference Shares-Debentures-Bonds-Mutual Funds

20.  Structure of Mutual Fund: Sponsor-Mutual Fund Trust-Asset Management Company-Custodian-Registrar and Transfer agent.

21.  QIP means allotment of eligible securities by a listed issuer to qualified institutional buyers on private placement basis.

Benefits:

Time Saving-Liberal Rules and Regulations-Cost efficient-No Lock in period

**Section C**

**22.** New Issue Market: Market for new issues of securities.

Intermediaries includes: Registrar to the issue-Brokers to the Issue-Bankers to the Issue-Underwriters-Merchant Bankers-Managers to the Issue

**23.** Financial Market is a physical location or virtual location were buyers and sellers meet to exchange financial products and services at prices determined by the forces of supply and demand.

Functions:

Intermediary Function-Capital Formation-Economic Growth-Determination of Prices-Provide Liquidity to financial assets-Financial Mobility-Reduce the cost of transactions

Classifications

Money Market-Capital Market-Foreign Exchange Market

**24.** Types of Mutual Fund

i)      According to ownership

a)     Public sector mutual fund

b)     Private sector mutual fund

ii)    According to scheme of operation

a)     Open Ended Scheme

b)     Close ended

c)     Interval Scheme

iii)   According to Portfolio

a)     Income Funds

b)     Growth Funds

c)     Balance Funds

d)     Stock/Equity Funds

e)     Bond Funds

f)      Specialty Funds

g)     Leverage Funds

h)     Money Market Mutual Funds

i)      Index Funds

j)      GILT Funds

k)     Dual Funds

l)      Fund of Funds

m)   Real Estate Mutual Funds

n)     Commodity funds

o)     Gold exchange traded funds

iv)   According to Location

a)     Domestic Mutual Fund

b)     Off shore Funds

v)     Other Funds

a)     Load Fund and b) No Load Fund

25) Derivatives are financial instruments whose value is derived from the value from an underlying financial instrument.

Types of Derivatives:

Forwards-Futures-Options-Swaps