FEATURES OF CAPITAL MARKET

The features of capital market are as follows:

Deals in new and existing securities: One of the most important features of the capital market is that dealings in this market are done through new as well as existing securities like shares and debentures.

Security prices: The prices of securities that are dealt with in the capital market are flexible rather than administered/fixed like management commission charges. The variability of price depends on several factors such as levels of demand and supply of funds in the market, yield on security and attitude of investors.

Location: The capital market is not confined to certain locations. The market may be local, regional, national or international.

Participants: The main participants in the capital market include:

Investment agencies and societies

Stock exchange or security market

Insurance companies such as LIC, GIC

Financial intermediaries such as merchant banks and mutual funds

Information structure: The information structure is complex and is highly asymmetric, for example, initial public offer (IPOs) involves companies about which market knows nothing, N et issuers know them inside out.

FUNCTIONS OF CAPITAL MARKET

The functions of an efficient capital market are as follows:

Allocation function: Capital market is a place where the investment avenue is continuously available for long-term investment. It helps in proper allocation of these resources. It can have regulation over resources so that it can direct funds in a qualitative manner.

Liquidity function: This is a liquid market as it makes fiend available on continuous basis. Both buyer and sellers can easily buy and sell securities as they are readily available. Basically traded transactions in the capital market transactions in capital market are related to stock market. Thus, marketability in the capital market becomes easy.

Savings and investment function: Capital market is an important source for mobilising savings from the economy. It mobilizes funds from people for further investment in the productive channels of an economy. It provides an investment avenue for people who wish to invest resources for a long period of time. Instruments such as bonds, equities, units of mutual hinds and insurance policies definitely provides such diverse investment avenue for the public.

Merger function: The capital market facilitates take over mechanism in order to put the management and administration of inefficient companies to more efficient and competent hands.

Service function: Capital market provides various types of services which include long-term and medium loans to industry, underwriting services, consultancy services and export finance.

Indicative function: Capital market enhances production and productivity in the national economy. It also helps in research and development. It acts as a barometer showing not only increasing production and productivity of a company but also of the economy as a whole by generation of employment, development of infrastructure and through price movements of security.

Capital formation: India requires high rate of growth to expedite the journey towards development. For this purpose, high rate of long-term investment and capital formation is required. A well-developed capital market offers adequate incentives which attract people, domestic financial institutions as well as foreign institutional investors to invest their savings in the capital market. Capital market provides liquidity and reasonable return which indulge savings and accelerates the capital formation of the country.

STRUCTURE OF INDIAN CAPITAL MARKET

The constituents of capital market are explained in the following text.

Investment Agencies or Societies

These are such institutions which collect funds from people through specific financial instruments such as unit, share and debenture and then invest these pooled funds in suitable securities, depending upon the objective of that scheme. The basic objective of such investment companies is to get enhanced benefits of large and pooled resources through low risk and expertise. A lot of information and adequate knowledge are required for successful investment of funds. These incur a huge cost for collecting information and hiring experts of this field. The major investment type companies include investment trusts, mutual funds, common trust funds of commercial banks, management investment companies and unit trusts. These investment companies can be classified into two categories:

- Management investment companies
- Unit trusts

Management Investment Companies

These companies are also known as discretionary trusts or mutual funds. The management of these trusts enjoys wide discretionary powers relating to selection of various securities for designing of their investment portfolio. In other words, the investment pattern of such trust will not be fixed but be rather flexible depending upon development of the market. These companies can further be divided into two

categories: close ended and open ended. In the first category, the capitalization of the company is fixed and not changed before a particular period. In other words, shareholders cannot get back their investment from these companies before a particular period, whereas in the case of open-ended companies, the investors can sell and buy their shares from the company, and hence, no limit to capitalization. In other words. such companies make a continuous offering of new shares at prices near to their net assets value and shares are redeemable at net asset value on short notice.

Unit Trust

This is a specific type of investment company which is normally established under a particular act. The funds are raised from the large number of investors through selling of units, and the persons to whom

Industrial Securities Market

Industrial securities market is an ideal market l'or trading corporate securities such as bonds and equi_ ties This market consists of the folloNA

- Primary market/new issue market
- Secondary market:stock exchange

8.4.2.1 Primary Markets/New Issue Market

Primary market is a segment in which new issues are made for raising fresh capital in the form of shares and debentures. It is for this reason that primary market is also called new issue market. In this market equity shares, fully convertible debentures, partially convertible debentures and non-convertible debentures are the securities commonly issued by non-government public limited companies. Government companies issue equity shares and bonds.

In the primary market, issues are made either 'at par' or 'at premium'. Pricing new issues is regulated under 'Guidelines for disclosure and investors protection' issued by the Securities and Exchange Board of India (SEBI).

In the primary market, new issues may be made in three ways, namely, public issue, right issue and private placement. Public issues involve sale of securities to members of public. Rights issue involves sale of securities to the existing shareholders/denture holders. Private placement involves selling securities privately to a selected group of investors.

Secondary Market/Stock Exchange

In a secondary market, there is no additional flow of funds for further investments. Transactions in the secondary market do not result in fresh capital being made available to the producers as they deal in existing securities. The secondary market

renders a very important service to them, because if there is no active secondary market, most of the long-term industrial securities would become nearly permanent investment in the hands of investors. Without organized market, investors would have to make personal efforts for the sale and purchase of their securities. In the case of an inactive secondary market, the sellers would have to incur losses because true worth of the securities is not known. If there is no liquidity and marketability then investors would not have invested their funds in securities. Consequently, companies would have faced a lot of problems in raising funds by issuing shares and debentures. Consequently, the level of industrial development would have been lower. Thus, level of development in the secondary' market determines the efficiency and growth of the primary market.

Buying and selling of securities in secondary market is fairly simple. Investors have to open an account with a member of stock exchange and then place orders through the member. For an orderly functioning of stock market, a set of institutions is required. The role of these institutions assumes importance in securities market because the market deals with high value, financial assets. Institutions connected with securities markets are stock exchanges, members of stock exchanges (popularly' called brokers), clearing corporation, and depository (national Securities Depository Limited and Central Depository Services (India) Limited), transfer agents and SEBI.

New Issue Market

In this chapter, an attempt has been made to discuss the functions of new issue market, the instruments of issue, functionaries of new issue market and mechanism of new issue. The capital market, which is concerned with demand and supply of long-term funds, is dichotomized into primary or new issue market and secondary or stock exchange. The New Issue Market deals with new securities offered to the investing public while the Stock Exchange deals with the existing securities. The joint stock companies raise funds from new issue market but such new issues are also listed with stock markets which provide them regular market, ensure regular valuation and stability in prices of such securities, safety in dealings of the securities, channelise funds in the desired directions and ensure wider ownership of the securities.

As stated earlier, the new issue market plays a vital role in mobilizing funds from savers to entrepreneurs who seek to establish new enterprises or to carry out expansion/ diversification / modernization of existing ones. This may be done by issue of fresh equity or preference shares at par or premium, issue of debentures convertible and non-convertible, issue of cumulative convertible preference shares or issue shares or debenture through public issue, private placement while the existing enterprises may issue shares as rights or bonus as well.

The new issues, placed first in the new issue market, can be disposed of subsequently in the stock exchange. The stock exchange provides the mechanism for regular and continuous purchase and sale of securities. This facility is of immense utility to potential investors who are assured that they may be able to dispose of the allotment of shares at any time. Thus, the two markets are complementary in nature. Both the markets are connected to each other even at the time of new issue. The companies, which make new issue, apply for listing of shares on a recognized stock exchange. Listing of shares adds prestige to the firm and widens the market for the investors. The companies, which want stock exchange listing, have to comply with statutory rules and regulations of the stock exchange to ensure fair dealings in them. The stock exchanges, thus, exercise considerable control over the organization of new issues.

1) Functions of New Issue Market

As stated earlier, the main function of new issue market is to facilitate transfer of resources from savers to the users. The savers are individuals, commercial banks, insurance company etc. The users are public limited companies and the government. The new issue market plays an important role of transferring shares for production purposes, an important requisite for economic growth. It is not only a platform for raising finance to establish new enterprises but also for expansion/ diversification/ modernization of existing units. NIM performs three main functions which include 1) Origination 2) Underwriting and 3) Distribution.

a) Origination

It refers to the work of investigation, analysis and processing of new project proposals. This function starts before an issue is actually floated in the market. There are two aspects of this function. A careful study of the technical, economic and

financial viability is necessary to ensure soundness of the project. This is a preliminary investigation undertaken by the sponsors of the issue. The other aspect is advisory services, which improve the quality of capital issues and ensure its success. The function of origination is done by merchant bankers who may be commercial banks, all India financial institutions or private firms.

b) Underwriting

It is an agreement whereby the underwriter promises to subscribe to a specified number of shares or debentures or a specified quantity of stock in the event of public not subscribing to the issue. If the issue is fully subscribed, then there is no liability for the underwriter. If a part of share issues remain unsold, the underwriter will buy the unsold shares.

c) Distribution

Distribution is tiie function of sale of securities to ultimate investors. This service is performed by brokers and agents who maintain regular and direct contact with the ultimate investors.

2) Designing the Instrument

A wide array of financial instruments designed for varying risk-reward levels and liquidity preferences have been developed. Designing of financial products calls for exacting skills in financial engineering. The limitations imposed by the legal framework have also to be taken into consideration. There are various factors that influence the choice of instrument decision and a few of which are listed below:

a) Purpose of the Offer

While designing an issue, the purpose for which the issue is made will largely determine the type of security to be used. Tangible assets are more readily financed by debt while growth opportunities which involve intangible assets such as intellectual property rights are better financed with equity.

b) Debt Servicing

The choice of security issued is also dictated by the ability of the firm to service periodic payments for the interest and principal for debt securities. While debt securities help in leveraging the firm's earnings per share, it also entails the additional financial risk of not being able to meet future obligations. The lead manager should weigh the pros and cons before deciding on the selection of the security.

c) Tax Considerations

The tax implications to the issuer and the investor should be examined. The implications vary depending on the nature of the instrument. In case of debt instruments, the amount of interest paid is tax-deductible to the issuer. However, the amount of interest received is taxable for the investor. The issuer has to pay a special dividend tax on the amount distributed as dividends also. However, the dividends are totally tax free for the investor.

d)Credit Rating

The riskiness of the firm also has an impact on the debt/equity choice. Firms whose debt issues have high ratings will be able to borrow at a lower interest cost. Such firms may also be able to price favourably their equity issues. The best altemafive would be based on the precise impact of the choice of debt/equity on the firm's projected EPS and its effect on expected stock price.

e) Asset Cover

Lenders of debt normally insist on adequate security. Debt securities, secured and backed by tangible assets, are more attractive to lenders. Debenture/bond trustees often indicate the minimum asset cover. Therefore, companies without adequate asset cover are forced to issue equity.

f) Dilution of Ownership

Equity offers dilute the ownership control of the promoter group. Companies susceptible to takeover threats prefer issuing debt to equity.

g) Innovations in Financial Instruments

In the recent past, there have been innovations in the financial instruments witnessed by the Indian capital market, owing mainly to the liberalizafion measures. The various instruments of issues are as follows.

i) Secured Premium Notes with Detachable Warrants (SPN)

Secured Premium Notes are issued along with a detachable warrant. The warrant attached to it ensures the holder the right to apply and get equity shares after a notified period provided the Notes are fully paid up. The investor can dispose of the Secured Premium Notes on allotment at premium if the share of the issuing company commands a high premium in the market.

ii) Equity Shares with Detachable Warrants

In this instrument, along with fully paid up equity shares, detachable warrants are issued, which entifie the warrant holder to apply for a specified number of shares at a pre-determined price. Detachable warrants are registered separately with the stock exchange

and traded separately.

iii) Preference Shares with Warrants

This instrument shall carry a certain number of warrants entitling the holder to apply for equity shares "at premium" at any time in one or more stages between the third and fifth year from the date of allotment.

iv) Non-Convertible Debentures with Detachable Equity Warrants

The holder of this instrument is given an option to buy a specified number of shares from the company at a predetermined price within definite time frame. There is a specific lock in period after which the holder can exercise his option to apply for equity shares.

v) Fully Convertible Cumulative Preference Shares

This instrument has two parts. The first part is convertible into equity shares automatically on the date of allotment without application by the allotee. The second part will be redeemed at par/ converted into equity after a lock in period at the option of the investors.

vi) Zero Interest Fully Convertible Debentures (FCDs)

This instrument has no interest paid to the holders of this instrument fill the lock in period. After a notified period, these debentures will be automafically and compulsorily converted into shares. Before the conversion of FCDs into equity, if the company issues rights, it would be available to the holders in the proportion decided by the company.

vii) Fully Convertible Debentures (FCDs) with Interest

This instrument carries no interest for a specified period. After this period, opfion is given to apply for equities at premium for which no additional amount is payable. However, interest on FCDs is payable at a pre-determined rate from the date of first conversion, second and last conversion and equity will be issued in lieu of interest amount.

viii) Zero Interest Partly Convertible Debentures (FCDs) with Detachable and Separately Tradable Warrants

This partly convertible debentures has two parts. The first part is convertible into equity shares at a fixed amount on the date of allotment. The second part is non-convertible and redeemed at par at the end of a specific period. The second part will also carry a detachable and separately tradable warrant.

ix) Zero Interest Bonds

The instrument is sold at a discount from their eventual maturity value and bears no interest. In India, companies issue zero interest convertible bonds. These bonds do not carry any interest till the date of conversion and are converted into equity shares at par or premium on the expiry of fixed period.

x) Deep Discount Bonds

These types of bonds are sold at a large discount to their nominal value. There is no interest payment on these bonds and the investors get returns as accretion to the par value of the instrument over its life.

xi) Option Bonds

Option bonds may be cumulative or non- cumulative as per the option of the holder of the bonds. In case of cumulative bonds, interest is accumulated and is payable on maturity only. In case of non- cumulative bonds, the interest is paid periodically.

xii) Bonds with Warrants

A warrant allows the holder to buy a number of equity shares at a pre- specified price in future. The warrants are usually attached to debentures or preference shares issued by companies as sweetener to make issues more attractive.

4) Functionaries in the New Issue Market

The functionaries in the new issue market are those concerned with the formation of joint stock companies and the issue of their securities to the public. There are many functionaries in the new issue market. The important of them are discussed below.

A) Merchant Bankers

The financial institutions in India could not meet the demand for long term funds required by the ever-expanding industry and trade. The corporate sector, therefore, meet their requirements through issue of shares and debentures in the capital market. To raise money from the capital market, promoters depend upon merchant bankers who manage the whole show by rendering multifarious services. The merchant bankers also advise the investors of the incentives available in the form of tax reliefs and statutory obligations. They help the company in carrying out functions related to new issues, such as determination of security - mix to be issued, drafting of prospectus, application forms, allotment letters and a host of other documents, appointment of registrars for handling share applications and transfers, making arrangements for underwriting, placement of shares, selection and appointment of brokers and bankers to the issue, publicity of the issue, etc.

B) Promoters

Modem industrial enterprises require large amount of capital which can be raised only by resorting to the joint stock form of organization. Company promoters and syndicates do the work of establishing a joint stock company. It is the promoter who is responsible for conception or discovery of the idea to exploit the possibility of some industrial proposition. They work up details, formulate the financial plan which they usually do with the help of an issue house and finally they have to procure funds to put the proposition into active operation.

In case the company is successfully established and investors come forth to take up its shares, the promoter is duly rewarded. If the venture fails, he stands to lose not only his money he had sunk in the venture but his reputation as well. The promoters, in the case of projects of large dimensions, form a syndicate. All members of the syndicate work up the possibilities of the proposition and undertake the investigation and examination of the scheme. After completing the financial plan, the work of drawing up the prospectus, the memorandum of association and articles of association for the formal incorporation as a company is launched. After all the formalities are completed, the new company is ready to be launched and its issue is to be placed before the public.

C) Underwriters

Underwriting is an agreement whereby certain parties assure the issuing company to take up shares, debentures or other securities to a specified extent in case the public subscription does not come up to the expected levels. It is necessary for a public company, which invites public subscription for its securities to ensure that its issue is fully subscribed. The company cannot depend on its advertisements to bring in the full subscription. Usually the underwriters can be divided into two

categories, namely, Financial Institutions and Banks, on the one hand, and Broker - Underwriters and Approved Investment Companies / Trusts, on the other.

D) Registrars

The Registrars, sometimes also called the "Issue House", are responsible normally for receiving the share applications from various collection centers through controlling branches of bankers to the issue, analyzing them, recommending the basis of allotment, in consultation with the managers to the regional stock exchanges, for approval, arranging for dispatch of allotment letters and preparing the register of members etc. Their job normally starts with the opening of the subscription list and continues till the share certificates are dispatched.

E) Brokers

Brokers are the people who actually bring the prospective investors and the company together. It may not be an exaggeration to state that success or failure of a public issue depends to a large extent on the strategy of the brokers. Generally, they are members of recognized stock exchanges. With a view to providing better and professional services to investing public and to promote development of capital market on healthy lines, the Government has since allowed multiple membership to members of stock exchanges and accorded recognition to corporate entities and financial institutions including subsidiaries of the banks.

F) Bankers

The commercial banks receive the share application money along with the share application forms from the prospective investors. Depending upon the size of the issue, at least 4 or 5 banks are designated as bankers to the issue. Different branches of these banks are named at various locations where such application money is accepted. These collecting branches send the application forms and money received by them to a specified branch called "Controlling Branch".

G) Financial Institutions

The financial institutions at tlie time of sanctioning underwriting support/ term loans to the company, usually stipulate that they approve the draft of the prospectus and also the proposed programme for public issue. There are three principal All India Financial Institutions - IDBI, IFCI and ICICI. Even when all the three institutions jointly finance a project under their participating finance scheme, one of them is generally chosen as the **"Lead Financial Institution"** which acts on behalf of the other two. Hence it is generally adequate if the company obtains the necessary approval only from the Regional Office of the Lead Institution. Therefore an advance copy of the draft prospectus is sent to them with a request to forward their comments, if any, direct to the Lead Institution.

H) Publicity and Advertising Agents

Public issue is an effort to motivate and persuade members of the public to invest in the shares of the company. It is, therefore, essential that the general public is made aware of the company, its activities, its plans for future, etc. It is of vital importance that publicity is given before the public issue by giving Newspaper and TV Advertisements. Press Releases, Press/ Brokers' Conference, Leaflets,

Brochures, Posters and even Audio-Visual Shows are the usual media of publicity used for the public issue. There are some advertising agencies which specialize in financial advertising and publicity campaign for public issues.

I) Government Statutory Agencies

Besides the various agencies which are directly connected with a public issue, there are some statutory/government agencies that are connected with public issue. These are:

(1) SEBI which provides guidelines for public issue, (2) Registrar of the Companies with whom the prospectus has to be filed and registered before the public issue under Section 60 of the Companies Act, 1956, (3) Reserve Bank of India from whom necessary permission has to be obtained for non-resident investment, if any, in the company, (4) The Stock Exchange where the company's shares/debentures are to be listed, (5) Industrial Licensing Authorities for necessary industrial license to be obtained for the project or other statutory bodies like DGTD etc, with whom the capacity of the project has to be registered, and (6) Pollution Control Authorities and other Local Authorities from whom the clearance may have to be obtained and such clearance is mentioned in the prospectus.

J) Other Agencies

In addition, the company will also have interaction with other agencies like auditors, legal advisers, taxation or technical experts whose names or statements are mentioned or quoted in the prospectus.

5) Mechanism of New Issues

The following are the mechanism of new issues

1. Public Issue Through Prospectus
2. Offer for Sale
3. Initial Public Offers (IPOs) through Secondary Market
4. Rights Issue
5. Bonus Issues
6. Tender Method
7. Over The Counter Placement(OTCEI)
8. Stock Option
9. Book Building
10. Green Shoe Option
11. Private Placement and
12. e - IPOs

a) Public Issue through Prospectus

This is the most common method of issue of securities by companies. Under this method, the company issues a prospectus which is an invitation to the investing public for subscription. It is a direct offer by the issuing company to the general

public to subscribe to the securities of the company at a stated price. Public issue through prospectus is underwritten to safeguard against an unsatisfactory response from the public. The prospectus contains the following information.

i) Company's name and address of its registered office,

ii) Names and addresses of the company's promoters, manager, managing director, directors, company secretary, legal adviser, auditors, bankers, brokers, etc,

iii) Date of opening and closing of subscription list,

iv) Contents of articles or any contract relating to terms and conditions of appointment of managing director or manager,

v) Names and addresses of underwriters, the amount underwritten and the underwriting commission,

vi) Material details regarding the project i.e. location, plant and machinery, technology, collaboration, performance guarantee, infrastructure facilities etc.,

vii) Nature of products, marketing set-up, export potential and obligations

viii) Past performance and future prospects

ix) Management's perception regarding risk factor

x) Credit rating obtained from CRISIL or any other recognized rating agency

xi) Statement that the company will make an application to specified stock

exchange(s) for listing its securities, and so on.

b) Offer for Sale

Under this method, the company does not directly offer its shares to the public but through intermediaries, brokers. The issue is also underwritten to avoid the possibility of the issue largely remaining with the issue houses. Sale of securities, in this case, is done in two stages. In the first stage, the issuing company makes an en bloc sale of securities to the issue houses or stockbrokers at an agreed fixed price. The second stage involves re-sale of these securities by issue houses or stockbrokers to ultimate investors at a higher price. The issuing houses have to meet various expenses such as, underwriting commission, prospectus cost, advertisement expenses, etc,

c) Initial Public Offers (IPOs) througii Secondary Market

This system is the reverse of the secondary market wherein brokers place orders on behalf of clients through a special window on the trading terminal. After the basis of allocation is finalized and brokers advised on the success of applications, successfial allottees submit the application form and the amount payable through the broker to the clearinghouse. Subsequently, the share certificates would be delivered to the investors by creating the depository account in the name of the investor.

d) Rights Issue

Rights issue is an invitation to the existing shareholders to subscribe for additional shares to be issued by a company. Rights simply means an option to buy certain securities at a certain privileged price within a certain specified period. Section 81 of the Companies Act, 1956 has provided for a pre-emptive privilege to the existing shareholders of a company to purchase shares in the further issue of the company.

e) Bonus Issues

Issue of bonus shares does not result in raising ft-esh capital. It is merely a conversion of existing reserves and surpluses into share capital. It represents just a book entry subject to certain rules and regulations. Total resource base of the company does not change due to issue of bonus shares. Choice of issue mechanism is influenced by the resources at the command of the issuer, the size of the issue, the type of securities issued, and market standing of the group and/ or the company making the issue and the market sentiments at the time of issue.

f) Tender Method

Under the tender method of marketing the securities, the issue price is not predetermined. The company announces the public issue without indicating the issue price and invites bids from various interested parties. The parties participating in the tender submit their maximum offers indicating the maximum price they are willing to pay as well as the number of shares they are willing to buy.

g) Over The Counter Placement (OTCEI)

The Over The Counter Exchange of India began its operations as second tier bourse only in 1992. It permits smaller companies to raise funds. The procedure involved under this method is that the company wishing to raise capital through OTC Exchange appoints a mernber of the OTCEI as sponsor. The sponsor appraises the project and values the shares of the company. The sponsor ensures the success of the issue even if it has to subscribe to all the shares by itself The OTCEI members and dealers operate counters to facilitate trading with the investing public.

h) Stock Option

Employees Stock Option Scheme (ESOP) is a voluntary scheme on the part of the company to encourage employees to participate in the company. The scheme also offers an incentive to the employees to stay in the company. The scheme is particularly useful in case of companies whose business activity is dominantly based on the talent of the employees.

i) Book Building

The aim of Book Building is to price the issue as high as possible but it cannot be so high that the investor loses interest. On the lower side, the issue price should not be lower than what the investor is willing to shell out.

j) Green Shoe Option (GSO)

SEBI has recently introduced Green Shoe Option (GSO), a new phenomenon for Indian investors. A company making an Initial Public Offer (IPO) through the Book Building mechanism can hold the GSO. This is an option that allows underwriter of

an Initial Public Offering to sell additional shares to the public. The objective of introducing GSO by SEBI is to create a safety net for investors who participate in the initial public offer of a company. It is to be used as a mechanism to stabilize the post-listing share price. The introduction of GSO came at a time when primary market in India was going through a bad phase. The IPOs were overpriced and prices used to fall after listing on the stock exchanges. This hurt the retail investors as it created a loss immediately on listing. As a result, investors were shying away from the primary market.

k) Private Placement

The private placement involves issue of securities, debt or equity, to a limited number of subscribers, such as banks, FIs, MPs and high net worth individuals. It is arranged through a merchant/ investment banker, who acts as an agent of the issuer and brings together the issuer and the investor(s) on the presumption that these are allotted to a few sophisticated and experienced investors and the public at large are not taken into confidence. The securities offered in a private placement are exempt from the public disclosure regulations and registration requirements of the regulatory body. What distinguishes private placement from public issue is that while the latter invite application from many subscribers, the subscription in the private placement are normally restricted to a limited number.

l) e-IPOs

A company proposing to issue capital to public through on- line system of the stock exchange has to comply with section 55 to 68A of the Companies Act, 1956 and SEBI (DIP) Guidelines 2000. The company is required to enter into an agreement with the stock exchange(s), which have the requisite system for on-line offer of securities. The agreement should cover rights, duties, responsibilities and obligations of the company and the stock exchanges inter-se, with provision for a dispute resolution mechanism between the company and the stock exchange. The issuer company appoints a registrar to the issue having electronic connectivity with the stock exchanges. The issuer company can apply for listing of its securities at any exchange through which it offers its securities to public through on- line system, apart from the requirement of listing on the regional stock exchange. The stock exchange appoints brokers for the purpose of accepting applications and placing orders with the company. The lead manager would co- ordinate all the activities amongst various intermediaries connected to the system.

From the above discussion it is understood that new issue market plays an important role in mobilizing fund from savers. It is a platform to raise finance for expansion, diversification and modernization of existing unit. Introduction of new innovative financial instruments in the new issue market minimizes the risk and maximizes the returns. In recent past there has been a lot of innovations taking place in the financial instruments with the objective of liberalizing the existing measures. On the other hand, functionaries in the new issue market have also gradually increased and it increases the competitiveness among the market players (functionaries).

Secondary Market

The secondary market is defined as a marketplace where financial instruments that were issued previously are bought and sold. These include futures, options, bonds, stock, and also the loans which are sold to investors by a mortgage bank.

In some cases, the secondary market is used to describe a market for assets or used goods or alternative use by an existing product.

Meaning

In simple terms, the secondary market is described as a financial market where the securities that are already owned by an investor are bought and sold. Several other names like popularly know the secondary market

- Stock market
- Aftermarket
- Follow on public offering

One of the most popularly traded securities is stocks, and besides these, you will find other types of secondary markets as well. Investment banks, as well as individual and corporate investors, can deal in buying and selling of bonds and mutual funds.

For the general investor, it is an efficient marketplace for trading securities, and for a company, it is a monitoring and controlling channel.

Examples of secondary market

Prime examples are national exchanges like NSE (National Stock Exchange), LSE (London Stock Exchange), NASDAQ, and NYSE (New York Stock Exchange).

If an investor wants to buy shares of a company, he will have to do so from a secondary market similarly when he wants to sell then he will have to do so again in a secondary market.

Functions of Secondary market

The functions of the secondary market are as follows-

1. Is an economic barometer

It is an economic barometer that can measure the economic condition of a country effectively.

It is considered a reliable tool as every change in the economy is reflected via the share prices.

2. Pricing of securities

Supply and demand forces determine the price of securities.

The constant valuation in the secondary market provides instant information that is utilized by both the buyer and seller as per his wishes

3. Liquidity

The main function of a secondary market is to provide a marketplace ready for liquidity. The presence of this marketplace is an assurance in itself that their investment can be converted into liquid cash whenever they need it.

4. Spreading of the equity cult

It ensures wider share ownership by educating the interested parties about investments, ensuring better trading practices and regulating new issues thus spreading of the equity cult

5. Safety of transactions

The secondary market is regulated, and its dealings defined as per the legal framework. It ensures a haven for the investor so that they can get a fair deal.

6. Marketability and liquidity to existing securities

The first and foremost function of a secondary market is to offer marketability and liquidity to the existing securities. It allows an investor to invest, disinvest, and reinvest.

7. Allocation of capital

The shares of organizations that are making profits are quoted at high prices and are traded actively so that it becomes easy to raise fresh capital. The secondary market enables better allocation of capital to profitable channels

8. Have a say in economic growth

The secondary market indirectly promotes capital formation and has a say in the economic growth of a country.

As the securities are traded, the savings get channelized into investment avenues. This results in capital formation.

9. Offers scope for speculation

The secondary market offers scope for speculation in a controlled manner within legal boundaries.

10. Promotes the habit of investment and savings

It seems very lucrative to an investor as you can trade for the short term and earn some quick money. It offers opportunities for both savings and investment to an investor.

Characteristics of secondary market

The characteristics of the secondary market are-

1. The IPO is primarily sold on the primary market, but after that, they are traded in secondary markets
2. Price is determined as per the demand and supply of a stock share
3. Brokers are hired by investors so as to manage their trading for a fee
4. It is possible to purchase as many shares he/she wants in the financial marketplace
5. The sale proceeds of a transaction go to the investors who are selling them
6. The prices of the shares fluctuate as they are affected by the change

Features of secondary market

The features of secondary market are as follows-

1. It is treated as an alternative to savings
2. The secondary market is prompt and can make viable adjustments in the price due to any recent developments
3. It offers liquidity to the investors as it is easy to sell the securities if he is in need of cash. This is possible because there are numerous buyers in the marketplace ready for transactions
4. The high volume of transaction results in lower transaction costs
5. Supply and demand economies lead to price discovery
6. There are high regulations in place by the government to ensure the safety of investor's money

Tools and players in the secondary market

The secondary market is a popular trading place as it deals in

- Variable income – These include derivatives and equity
- Fixed income – it includes preference shares and debt securities like debentures and bonds
- Hybrid instruments – It includes convertible debentures and preference shares.

The important players in the secondary market are

- Retail investors
- Financial Intermediaries – mutual fund, insurance companies, banks, non-banking financial companies
- Brokerage and Advisory services – security dealers, commission broker, etc

Types of secondary market

There are two types of the secondary market which have been described below-

1. OTC or Over-The-Counter Markets

An OTC market is considered a decentralized place where the members trade amongst themselves. The competition to get higher volumes is fierce; hence, the price of securities differs from one to another seller.

The interested parties deal on a one-to-one basis with each other, so the counterparty risk is much higher if compared with Exchanges. Example of the OTC market is FOREX or Foreign Exchange Market.

2. Exchanges

In this marketplace, you will not find any direct contact between the two main parties, the seller and the buyer. Heavy regulations are in place to make it a safe zone for trading securities. The exchange in itself is a guarantor, and the probability for counterparty risk is almost zero.

The transaction cost is a bit high because of the commission and exchange fees. Examples of Exchanges are the New York Stock Exchange (NSE) and the London Stock Exchange (LSE).

The secondary market can be further divided into

1. Auction market

It is a platform where both the seller and buyer meet and then announce the rate at which they are willing to trade their securities. Everything is announced publicly, and that includes the offeror bidding price.

2. Dealer market

In this type of secondary market, the transactions happen through an electronic network like telephones and fax machines.

Advantages of secondary market

The advantages are as follows-

1. Secondary markets offer a chance to the investor to save as well as invest and thus earn some returns.
2. It offers an opportunity for quick and good gains in a shorter time frame
3. Investment does not require a huge amount hence it is possible to do so with a small amount of money
4. The stock prices in the secondary market help to value a company effectively
5. It is an apt indicator of the economic condition of a company as the dropping or rising prices suggest a recession or a boom, respectively in the economy.
6. A firm can monitor as well as control public perceptions through its activities in the secondary market
7. It is easy to sell or buy securities hence ensures liquidity for an investor
8. When money is held in the form of shares, the mobilization of savings becomes easier.
9. Investing in the shares of a company gives you the feeling of ownership even if it is a minority and very small
10. Besides being an investment platform, the secondary market also offers investment advice on complex matters. There are key players for this role, for example, investment advisors and stockbrokers.
11. In several companies, even minority ownership allows the investor to vote and voice your opinion at the general meeting
12. The shareholders are the owners of a company whose shares are traded in a secondary market. It tends to improve corporate governance as the managers have to be accountable for every action in front of the shareholders.

Disadvantages of Secondary Market

1. The price fluctuates in secondary markets, and the volatility of the unpredictable market can result in a quick and sudden loss
2. It s a time-consuming process as an investor has to complete certain formalities before he can buy or sell in secondary markets
3. Sometimes government policies act as a hindrance and misguide the market situations. This results in great upheavals, and it is the companies that have to bear the loss and damage.
4. The risk is greater as the market is influenced by various external forces that can result in an upward or downward trend within minutes

5. An investor has to pay a brokerage commission every time he decides to buy or sell the shares. It simply lessens the profit margin