Case Studies – (Chapter - 10) Financial Markets, BST Class 12

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Q. 1. Supriya’s grandmother who was unwell, called her and gave her a gift packet. Supriya opened the packet and saw many crumpled share certificates inside. Her grandmother told her that they had been left behind by her late grandfather.

As no trading is now done in physical form, Supriya wants to know the process by adopting which she is in a position to deal with these certificates.

1. Identify and state the process.
2. Also give two reasons to Supriya
3. why dealing with shares in physical form had been stopped. (3 Marks)

Ans.

1. Dematerialization – It is a process where securities held by the investor in physical form are cancelled and the investor gives an electronic entry or number so that she/he can hold it as an electronic balance in an account
2. Problems with dealing in physical form - (any two)
   1. Theft
   2. Fake/forged transfers
   3. Transfer delays
   4. Paper work associated with share certificates or debentures held in physical form.

Q. 2. The directors of a company want to modernize 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. The directors should approach a consultant for new public issue of shares. The stock exchanges deal with sale and purchase of existing securities only, not in new issue of securities.

Different methods which the company may adopt for the new public issue of shares:

1. Offer through prospectus
2. Offer for sale
3. Private placement
4. Rights issue
5. E-IPOs.

Q. 3. Reshu’s father has gifted her shares of a large cement company, with which he had been working. The securities were in physical form. She already has a bank account and does not possess any other forms of securities.

She wished to sell the shares and approached a registered broker for the purpose. Mention one mandatory detail which she will have to provide with the broker.  

Ans. Permanent account Number (PAN)

Q. 4. Saqib Ltd. is a large credit worthy company operating in the Kashmir Valley. It is an export oriented unit, dealing in exclusive embroidered shawls. The floods in the valley have created many problems for the company. Many craftsmen and workers have been dislocated and raw material has been destroyed. The firm is therefore, unable to get an uninterrupted supply of raw material, and the duration of the production cycle has also increased. To add to the problems of the organization, the suppliers of raw material who were earlier selling on credit are asking the company, for advance payment or cash payment on delivery. The company is facing a liquidity crisis. The CEO of the company feels that taking a bank loan is the only option with the company to meet its short term shortage of cash. As a finance manager of the company name and explain the alternative to bank borrowing that the company can use to resolve the crisis.  

Ans. Commercial Paper: It is a short term unsecured promissory note, negotiable and transferable by endorsement and delivery with a fixed maturity period. It is issued by large
and creditworthy companies to raise short term funds at low companies that are generally considered to be financially strong.

Q. 5. ‘Ganesh Steel Ltd.’ is a large and credit-worthy company manufacturing steel for the Indian market. It now wants to cater to the Asian market and decides to invest in new hi-tech machines. Since the investment is large, it requires long-term finance. It decides to raise funds by issuing equity shares.

The issue of equity shares involves huge floatation cost. To meet the expenses of floatation cost the company decides to tap the money market.

1. Name and explain the money-market instrument the company can use for the above purpose.
2. What is the duration for which the company can get funds through this instrument?
3. State any other purpose for which this instrument can be used. (4 Marks)

Ans.

1. Commercial paper
2. 15 days to one year
3. It can also be used for seasonal and working capital needs.

Q. 6. The Trading Procedure on Stock Exchange has been replaced by on-line 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 as an electronic balance in an account. This has increased the equity cult among the people.

1. Identify and state the process mentioned above.
2. What is the most important requirement for the process identified in (a)? State.
3. State any two values which you think have enhanced the equity cult in the society.

Ans.

1. Dematerialization – It is the process of holding securities in an electronic form.
2. For this, the investors has to open a ‘Demat account’ with a depository participant (DP) for holding and transferring securities in the demat form. He / She will also have to open a bank account for cash transactions in the securities market.

3. Values:
   ● Fair dealings (i.e., no danger of loss, theft or forgery of share certificates)
   ● Transparency (i.e., participants can see the prices of all securities during real time)
   ● Increased efficiency of information (i.e., computer screens displays information on prices)
   ● Increased efficiency of operations (i.e., reduction in time, cost and risk error) (any two)

Q. 7. 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.

1. Name the term used for trading malpractice done by the directors of this company.
2. Identify any two values that the company should have adhered to in order to gain the trust of its investors.

Ans.

1. Insider trading
2. Values:
   ● Protection and promotion of investors’ interests
   ● Transparency
   ● Efficiency of information
   ● Efficiency of operations (any two)

Q. 8. ‘R’ Limited is a real estate company which was formed in 1950. In about 56 years of its existence the company has managed out from a niche for itself in this sector. Lately this sector is witnessing a boom due to the fact that the Indian economy is on the rise. The income of middle class are rising. More people can afford to buy homes for themselves due to easy availability of loans and accompanying tax concession.

To expand its business in India and abroad the company is weighing various options to raise money through equity offerings in India. Whether to tap equity or debt market whether to raise money from domestic market or international market or combination of both? Whether
to raise the necessary finance from money market or capital market. It is also planning to list itself in New York Stock Exchange to raise money through ADR.

To make its offering attractive it is planning to offer lots of financial plans, products to its stakeholders and investors and also explain its listing at NSE after complying with the regulations of SEBI.

1. What are the regulation so SEBI that company must comply with?
Ans. Explain regulatory functions,

Q. 9. A company require Rs. 2 crore for inventory, payment of wages, salaries, maintaining bank balance, etc.

1. Suggest which financial market company may approach and why?
2. State the instruments to raise finance in that market.
Ans.

1. Money market is the market from where it can raise money to fulfill its requirement. The reason is company require money for working capital i.e. maximum for 1 year and market for short-term is money market.
2. The instrument to raise money in money market are:
   1. Call money
   2. Treasury bill
   3. Commercial bill
   4. Commercial paper
   5. Certificate of deposit.

Q. 10. Few years ago, there were many malpractices, unfair trade practices and frauds and scams were taking place in stock Exchange. All these affected investor’s confidence, faith and trust in Stock Exchange. The Government of India decided to set up a separate body for this purpose who was given control of stock exchange. This separated ownership and control of stock exchange.

1. Name the concept which separate the ownership and control of stock exchange.
2. Name the body set up by the government of India to contract the stock exchange.
3. State the objectives of that regulating body.
Ans.
1. The concept which separate ownership and control is called as demutualization.
2. The regulatory body set up by government of India is “SEBI” Securities Exchange Board of India.
3. The objectives of SEBI are:

   The overall objectives of SEBI are to protect the interest of investors and to promote the development of stock exchange and to regulate the activities of stock market. The objectives of SEBI are:

Q. 11. Mr. Vikas Mehra was the Chairman of IBM Bank. The bank was earning good profits. Shareholders were happy as the bank was paying regular dividends. The market price of their shares was also steadily rising. The bank was about to announce the taking over of ‘UK Bank’. Mr. Vikas Mehra knew that the share price of IBM Bank would rise on this announcement. Being a part of the bank, he was not allowed to buy shares of the bank. He called one of his rich friends Mukand and asked him to invest Rs. 4 crores in the shares of his bank promising him the capital gains.

   As expected, after the announcement, the share prices went up by 50% and the market price of Mukand’s shares was now Rs. 6 crores. Mukand earned a profit of Rs. 2 crores. He gave Rs. 1 crore to Vikas Mehra and kept Rs. 1 crore with him. On regular inspection and by conducting enquiries of the brokers involved, the Securities and Exchange Board of India (SEBI) was able to detect this irregularity. SEBI imposed a heavy penalty on Vikas Mehra.

   Quoting lines from the above paragraph, identify and state any two functions performed by the SEBI in the above case.

   Ans. The two functions performed by SEBI in the given case are stated below:

   1. Regulatory function is being performed by SEBI: “on regular inspection and conducting inquiries of the brokers involved.”

   2. Protective function is performed by SEBI: “The SEBI imposed heavy penalty on Mr. Vikas Mehra.

Q. 12. Mission Coach Ltd. is a large creditworthy company that manufactures coaches for the Indian Railways. It now wants to export these coaches to other countries and decides to invest in new hi-tech machines. Since the investment is large, it requires long-term finance. It decides to raise funds by issuing equity shares. The issue of equity shares involves huge
floatation cost. To meet the expenses of floatation cost, the company decides to tap the money market.

1. Name the explain the money-market instrument the company can use for the above purpose.
2. What is the duration for which the company can get funds through this instrument?
3. State any other purpose for which this instrument can be used.

Ans.

1. Commercial Papers can be used for Bridge financing by Mission coach Ltd. as it is issued by large and credit worthy companies. The instrument is in the form of an unsecured promissory note and it freely transferable by endorsement. It is sold at discount and redeemed at par.
2. Its maturity period may range from a fortnight to a year.
3. It is also used to meet the short term seasonal and working capital requirements of a business enterprise.

Q. 13. Incorporated in 1990. Raju Dairy Ltd., is one of the leading manufacturers and marketers of dairy-based branded foods in India. In the initial years, its operations were restricted only to collection and distribution of milk. But, over the years it has gained a reasonable market share by offering a diverse range of dairy based products including fresh milk, flavoured yogurt, ice creams, butter milk, cheese, ghee, milk powders etc. in order to raise capital to finance its expansion plans. Raju Dairy Ltd. has decided to approach capital market through a mix of Offer for sale of Rs. 4 crore shares and a public issue of Rs. 2 crore shares.

In context of the above case:

1. Name and explain the segment of capital market being approached by the company.
2. Identify the two methods of floatation used by the company to raise the required capital. Give one difference between them.

Ans.

1. Primary market is the segment of capital market being approached by the company. It is also known as the new issue market as the securities are issued for the first time by the companies through this market.
2. The two methods of floatation used by the company to raise the required capital are –
Issue through prospectus and Offer for sale.

In case of issue through prospectus, the company approaches the members of the general public directly by issuing a prospectus whereas in case of Offer for sale, the company approaches members of the general public indirectly through intermediaries like issuing houses, stock brokers etc.

Q. 14. Harsh works as a manager in a software company. He opened a Demat account with a broking house in order to trade in securities with the money he received as his first performance bonus. Since then he has been very active in stock trading under the guidance of a stock broker. However, when he was hospitalized for a few days this year, his wife received several calls from the his stock broker for permission to transact on Harsh’s behalf. Though she told him to wait till her husband had recovered, the stock broker went ahead and executed the transactions. When Harsh got home from hospital, he discovered that the unauthorized transactions had led to a loss for him.

Harsh complained to the broking house, but they claimed he had authorized the transactions. Keeping in new, the guidelines issued by the National Stock Exchange that he had read in the national newspaper Harsh demanded proof and threatened to file a complain. Since, the broking house had no evidence that the deals had been authorized they made good the loss that Harsh had incurred due to the transaction.

In the context of the above case?

1. What is a Demat account?
2. Who is acting as the depository participant for Harsh?
3. Name the document that is illegally enforceable and helps to settle the claims between the investor and the broker.

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1. A Demat account is an account used for holding securities in electronic form.
2. The Broking house is acting as the depository participant for Harsh.
3. A contract note is a legally enforceable document that helps to settle the claims between the investor and the broker.

Q. 15. Ketan won a cash prize of Rs. 20,000 in the National level Robotics Competition. On the advise of his father, he visits a nearby bank to open a Fixed deposit account in his name with the prize money. His sister Suhasini accompanied him to the bank. On reaching the bank, he notice big banners which are placed within the premises containing information
about the various arrangements through which corporates may raise their capital through the bank. Being a finance graduate, Suhasini explains to Ketan that banks play the role of the financial intermediary by helping in the process of channelizing the savings of the households into the most profitable business ventures.

In context of the above case:

1. Name another financial intermediary that helps in the process of channelizing the savings of the households into the most productive use.
2. Also, outline any two functions of another financial intermediary as identified in part (a)

Ans.

1. Financial markets is the other financial intermediary that helps in the process of channelizing the savings of the households into the most productive use.

Q. 16. Ragu works as a waiter in a five star hotel in Mumbai. While serving the customer he overhears him at the table saying that the he has made profits higher than expected by investing in securities market. So, Ragu also decides to make a nominal investment from his savings in the stock market in pursuit of higher gains.

In context of the above case:

As a financial consultant, apprise him of the steps involved in the working of a Demat system.

Ans. Ragu will have to initiate the following steps for trading through a Demat system:

Q.17. Sumita is a professor in a reputed business institute. While explaining the procedure of stock exchange trading, she shared with her students that many years back she had bought 200 shares of a leading automobiles company. As per the settlement procedure she paid for the shares and received the share certificates in physical form. However, when she had sent those certificates to the company to get them endorsed in her name, she was informed by the company that those certificates were duplicate.

Therefore, in order to protect the investors from many such malpractices, now only screen – based trading is done and dematerialization is compulsory.

In context of the above case:

1. What is screen based trading?
2. Give the meaning of ‘dematerialization’. State any two of its advantages.

Ans.

1. Screen – based trading refers to the process of buying or selling securities online.

Q. 18. Madhav’s is one of the India’s most trusted brands in Indian sweets and snacks segment. The company has manufacturing plants in Kota, Kanpur, New Delhi, and Mumbai. Madhav’s has its own retail chain stores and a range of restaurants in these cities. Now, the company plans to extend its business in 12 more cities in India. In order to raise the funds, its directors have decided to float a public issue through prospectus. Besides, it intends to raise money to meet the floatation cost in terms of brokerage, underwriting commission, advertising etc.

In context of the above case:

1. What is the other name used for the funds required to meet floatation costs?
2. Describe briefly the short term instrument popularly used by the companies to raise for the funds required to meet floatation costs. Who can issue them?
3. Distinguish between the two types of financial markets that the company intends to approach to meet its financial needs.

Ans.

1. Bridge financing is the other name used for the funds required to meet floatation costs.
2. Commercial Papers

Q. 19. During navratras, Varun finalizes a deal to buy a new house. So, he visits a nearby branch of ‘Subh Bank’ top withdraw Rs. 10 lakhs from his account in order to pay the token money to the seller. In the bank he observes that a large number of customers are present to make cash with drawls, probably because it is an auspicious time to make purchases. After sometime, he overhears one of the bank staff members telling his colleague that, “Today ‘Subh Bank’ is likely to fall short of cash and to make up for the deficit and maintain its cash reserve ratio it will have to approach another bank.”

In context of the above case:

1. Identify the instrument that ‘Subh Bank’ will use to meet its short term requirements of funds.
2. State any three feature of the instrument as identified in part (a).

Ans.

1. Call money is the instrument used by 'Subh Bank' to meet its short term requirements of funds.
2. Three features of call money.

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