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B.Com Honours | Semester 1 | Calicut University

Stock Market Fundamentals

Course Code: COM1FM105 (2) • Module 2 Notes

1. Primary Market Mechanics & Public Issue Frameworks

The primary capital market is the institutional channel through which corporate enterprises transition from private entities into publicly traded corporations, or through which established public companies raise incremental long-term equity capital. Under the regulatory oversight of the **Securities and Exchange Board of India (SEBI)**—specifically governed by the *SEBI (Issue of Capital and Disclosure Requirements) Regulations, 2018 (ICDR)*—the primary market ensures transparent price discovery, equitable public access, and robust corporate governance disclosures.

1.1 Comprehensive Taxonomy of Public Issues

Corporate equity issuances in India are classified into distinct structural categories based on whether securities are offered to the general public, existing shareholders, or selected institutional buyers:

1. Initial Public Offering (IPO)

The first sale of equity shares by an unlisted company to the public. An IPO transforms a closely held private company into a public entity listed on recognized stock exchanges (NSE/BSE). An IPO can consist of:

- **Fresh Issue:** New shares are minted and issued; the capital raised flows directly onto the company's balance sheet to finance capital expenditure (CapEx), debt reduction, or working capital.
- **Offer for Sale (OFS):** Existing shareholders (founders, private equity, venture capitalists) sell their personal shares to the public. The company receives zero capital; proceeds flow directly to the selling shareholders.

2. Follow-on Public Offering (FPO)

An issuance of shares by an already listed public company to the general public. Used to raise additional growth capital or to satisfy SEBI's Minimum Public Shareholding (MPS) mandate (which requires listed companies to maintain at least 25% public float). FPOs can be *dilutive* (issuing new shares, expanding total equity base) or *non-dilutive* (promoters divesting existing holdings via OFS).

3. Rights Issue & Bonus Issue

- **Rights Issue (Section 62 of Companies Act):** Offering new shares to existing shareholders in proportion to their current holdings at a discounted price within a specific subscription window. Protects existing shareholders from involuntary equity dilution.
- **Bonus Issue (Capitalization of Reserves):** Free additional shares distributed to existing shareholders in proportion to their holding (e.g., 1:1 bonus). Does not inject fresh cash; merely transfers retained earnings into paid-up capital.

4. Private Placement (QIP & Preferential)

- **Qualified Institutional Placement (QIP):** A fast-track mechanism allowing listed companies to issue equity or convertible debentures exclusively to Qualified Institutional Buyers (QIBs) without filing a public prospectus.
- **Preferential Allotment:** Allotment of shares or convertible warrants to a select group of strategic investors on a private basis under Section 42 of the Companies Act 2013.

1.2 Modes of Public Issue Pricing: Fixed Price vs. Book Building

In modern Indian primary markets, the pricing of an IPO is executed either through a traditional fixed-price mechanism or through dynamic market price discovery via book building:

COMPARATIVE ANALYSIS: PUBLIC ISSUE PRICING MECHANISMS SEBI ICDR Framework

Feature	Fixed Price Issue	Book Building Issue (Modern Standard)
Pricing Determination	Price is determined in advance by the issuer and lead managers and stated explicitly in the prospectus.	Price is discovered dynamically based on demand bids submitted by investors within a designated **Price Band**.
Price Band Limits	No band exists; a single fixed price (e.g., ₹250 per share) is quoted.	Comprises a **Floor Price** (minimum bid) and a **Cap Price** (maximum bid). Under SEBI rules, the Cap cannot exceed **120% of the Floor** (e.g., ₹100 to ₹120).
Demand Visibility	Demand is known only after the public subscription window completely closes.	Demand is tracked in real-time on stock exchange terminals as bids are entered continuously into the electronic order book.
Cut-off Price Option	Not applicable; all investors apply at the exact stated issue price.	Retail Individual Investors (RIIs) can tick the **Cut-off Option**, agreeing to purchase shares at whatever final price is discovered by institutional bidding.
Market Dominance	Rarely utilized today; restricted primarily to small micro-cap SME IPOs.	Accounts for over 95% of all mainboard IPO capital raised in India.

2. The IPO Lifecycle: Prospectus, ASBA, Evaluation, and Listing

Executing an Initial Public Offering is a sophisticated legal, financial, and operational process spanning 6 to 12 months. The lifecycle begins with the appointment of Merchant Bankers (Book Running Lead Managers - BRLMs) and culminates in the formal listing and bell-ringing ceremony on the stock exchange floor.

2.1 The Hierarchy of Statutory Disclosure Documents (Prospectus)

To ensure investor protection, Indian corporate law mandates strict disclosure documents across successive stages of public issuance:

- **Draft Red Herring Prospectus (DRHP):** The initial exhaustive disclosure document prepared by merchant bankers and filed with SEBI and stock exchanges. It details the company's business operations, promoter pedigree, audited financial statements for the prior 3 fiscal years, management discussion, and comprehensive risk factors. The DRHP is made public for at least **21 days** to invite public comments and review by SEBI officers.

- **Red Herring Prospectus (RHP):** The updated prospectus filed with the Registrar of Companies (ROC) after incorporating SEBI's observations. It contains all commercial and financial details—including the exact issue size and Price Band—but *omits the final issue price and exact number of shares offered* (hence "Red Herring"). This is the formal document upon which public bids are solicited.
- **Final Prospectus:** Filed with ROC immediately following the conclusion of the bidding period. It contains the finalized cut-off price, total subscription volume, and exact allocation metrics.
- **Shelf Prospectus & Abridged Prospectus:** A *Shelf Prospectus* allows public financial institutions or banks to make multiple non-convertible debenture issues over a 1-year period without filing a new prospectus each time. An *Abridged Prospectus* is a condensed statutory memorandum containing core features (Form 2A) that must accompany every physical application form.

2.2 Application Mechanisms: ASBA and UPI Integration

Historically, retail investors suffered severe financial friction during IPO applications: money was debited from bank accounts and held by the company for months, with refunds for unallotted shares subject to postal check delays and fraud. In 2008, SEBI introduced **ASBA**, which completely revolutionized primary market settlement.

ASBA ARCHITECTURE (APPLICATIONS SUPPORTED BY BLOCKED AMOUNT)

Investor Protection Innovation

Core Operating Philosophy: Under ASBA, the investor's application money *never leaves their personal bank account* at the time of application. Instead, the application funds are merely **blocked (lien-marked)** by a Self-Certified Syndicate Bank (SCSB).

Interest Accrual Benefit: Because the blocked capital remains inside the investor's savings bank account throughout the 3-day bidding and allotment window, the investor continues to earn bank interest on the entire sum.

Automated Settlement upon Allotment:
• *Full Allotment:* The exact blocked amount is debited and remitted to the company's escrow account, and shares are credited to the investor's Demat account.
• *Partial Allotment:* Only the proportional amount corresponding to allotted shares is debited; the remaining blocked balance is unblocked immediately.
• *Zero Allotment (Non-Allotment):* The lien on the entire blocked amount is revoked automatically by the bank within 24 hours. Zero refund checks; zero manual friction.

UPI-based ASBA for Retail Investors (RII): Retail investors can apply directly through stockbroker trading apps (Zerodha, Groww) by entering their Unified Payments Interface (UPI) ID. The National Payments Corporation of India (NPCI) routes an electronic mandate to the investor's UPI banking app (Google Pay, PhonePe, BHIM). Upon entering the UPI MPIN, the funds are instantly lien-blocked. The transaction ceiling for UPI IPO mandates is **₹5,00,000** per application.

2.3 Basis of Allotment, Reservation Quotas & Grey Market (GMP)

SEBI ICDR regulations mandate strict proportional quotas to ensure equitable allocation across investor categories in a book-built IPO:

Investor Category	Statutory Reservation Quota	Allotment Mechanics & Application Rules
Qualified Institutional Buyers (QIB)	**Minimum 50%** of Net Issue	Mutual funds, foreign portfolio investors (FPIs), insurance companies, banks, and pension funds. Allotted on a proportionate basis. Includes an **Anchor Investor** portion (up to 60% of QIB quota) allocated one day prior to public opening with lock-in restrictions (30 days for 50%, 90 days for remaining 50%).
Non-Institutional Investors (NII / HNI)	**Minimum 15%** of Net Issue	High-net-worth individuals and corporate treasuries applying for amounts exceeding ₹2,00,000. Subdivided into: (a) Small HNI (₹2L – ₹10L, 1/3rd quota) and (b) Big HNI (Above ₹10L, 2/3rd quota). Allotted on a computerized proportionate draw basis.
Retail Individual Investors (RII)	**Minimum 35%** of Net Issue	Individuals, Hindu Undivided Families (HUFs), and NRI retail investors applying for an aggregate value not exceeding **₹2,00,000**. If oversubscribed, SEBI mandates allotment of at least one minimum bid lot to as many applicants as possible via an electronic lottery system.

Understanding the Grey Market Premium (GMP)

Definition: The "Grey Market" is an informal, unofficial, over-the-counter (OTC) cash market operating completely outside the regulatory purview of SEBI and stock exchanges. In this market, applications and unallotted shares are unofficially traded before formal exchange listing.

Grey Market Premium (GMP): The premium price over and above the IPO issue price that buyers are unofficially willing to pay. For example, if an IPO issue price is ₹200 and the GMP is ₹50, the market unofficially expects the stock to list at $₹200 + ₹50 = ₹250$ (a 25% listing gain).

Kostak Rate & Subject to Sauda: *Kostak* is the fixed rupee amount an investor receives by selling their entire IPO application to a buyer regardless of allotment. *Subject to Sauda* is a deal where the buyer pays the seller a premium only if shares are actually allotted to the seller.

Academic & Regulatory Caution: GMP is completely unregulated, highly prone to artificial operator manipulation and circular trading designed to lure gullible retail investors into oversubscribing poor-quality issues. Academic investors evaluate balance sheets, not speculative GMP.

3. Secondary Market Architecture & Stock Market Indices

The secondary market provides continuous liquidity, fair price discovery, and corporate governance accountability. In India, trading is conducted across two premier national electronic stock exchanges: the **Bombay Stock Exchange (BSE)** and the **National Stock Exchange (NSE)**.

3.1 The Twin Pillars of Indian Securities Trading: BSE vs. NSE

Bombay Stock Exchange (BSE)

- **Heritage:** Established in 1875 by Premchand Roychand as "The Native Share & Stock Brokers' Association." It is Asia's oldest stock exchange.
- **Trading Platform:** Migrated from the physical "open outcry" trading ring to the electronic **BOLT** (BSE Online Trading) system in 1995.
- **Listed Universe:** Over 5,300+ listed companies (the largest listed universe globally).
- **Benchmark Index: S&P BSE SENSEX** (Sensitivity Index), introduced in 1986 with base year 1978–79 = 100, tracking 30 premier, financially sound large-cap companies.

National Stock Exchange (NSE)

- **Modern Pioneer:** Incorporated in 1992 and recognized in 1993 following the recommendations of the Pherwani Committee to dismantle regional stock exchange cartels.
- **Demutualization Pioneer:** World's first exchange to completely separate trading rights from exchange ownership (brokers were barred from exchange equity ownership).
- **Trading Platform:** Launched satellite-linked fully automated screen-based trading system **NEAT** (National Exchange for Automated Trading) in 1994.
- **Benchmark Index: NIFTY 50**, launched in 1996 with base period November 3, 1995 = 1,000, tracking 50 premier companies across 13 economic sectors.
- **Market Leadership:** World's largest derivative exchange by contract volume and dominant leader in Indian cash equity turnover.

3.2 Stock Market Index Calculation: The Free-Float Market Capitalization Methodology

A stock market index acts as the economic barometer of a nation, measuring aggregate investor sentiment and broad economic health. Both SENSEX and NIFTY 50 are calculated using the globally standardized **Free-Float Market Capitalization Weighted Methodology**.

Free-Float Index Mathematical Formulations

```
Total Market Capitalization = Total Outstanding Shares × Current Market Price (CMP)
```

```
Free-Float Factor (Investible Weight Factor - IWF) = ( Total Shares - Locked/Promoter Shares ) / Total Shares
```

```
Free-Float Market Capitalization = Total Market Capitalization × Free-Float Factor
```

```
Index Value = [ ( Current Free-Float Market Cap of Index Basket ) / Base Market Cap ] × Base Index Value
```

Numerical Demonstration: Constructing a Free-Float Weighted Index

Hypothetical Index Basket: An index consists of two companies with a Base Market Capitalization of ₹10,000 Crores and a Base Index Value of 1,000.

Company A: Total Shares = 10 Crores. CMP = ₹500. Promoter locked holding = 60%. Free-float factor $= 1.0 - 0.60 = 0.40$.
$ ext{Total Market Cap} = 10 ext{ Cr} imes ₹500 = ₹5,000 ext{ Crores}$.
$ ext{Free-Float Market Cap} = ₹5,000 ext{ Cr} imes 0.40 = mathbf{₹2,000 ext{ Crores}}$.

Company B: Total Shares = 20 Crores. CMP = ₹300. Government/Promoter locked holding = 30%. Free-float factor $= 1.0 - 0.30 = 0.70$.
$ ext{Total Market Cap} = 20 ext{ Cr} imes ₹300 = ₹6,000 ext{ Crores}$.
$ ext{Free-Float Market Cap} = ₹6,000 ext{ Cr} imes 0.70 = mathbf{₹4,200 ext{ Crores}}$.

Current Aggregate Free-Float Market Cap:
$ ext{Total Current Free-Float Cap} = ₹2,000 ext{ Cr} + ₹4,200 ext{ Cr} = mathbf{₹6,200 ext{ Crores}}$.

Index Value Calculation:
$ ext{Current Index Value} = 🡅rac{₹6,200 ext{ Crores}}{₹10,000 ext{ Crores}} imes 1,000 = mathbf{620.00}$

3.3 Global Benchmark Market Indices

To contextualize domestic trends against global macroeconomic liquidity flows, investors track international indices:

- **United States:** *Dow Jones Industrial Average (DJIA)* (price-weighted 30 blue-chips), *S&P 500* (broad market standard), and *NASDAQ Composite* (technology-weighted).

- **Europe:** *FTSE 100* (United Kingdom), *DAX 40* (Germany), and *CAC 40* (France).
- **Asia-Pacific:** *Nikkei 225* (Japan), *Hang Seng* (Hong Kong), *Shanghai Composite* (China), and *KOSPI* (South Korea).

4. Market Watch Interface, Order Types, and Circuit Filters

Trading execution requires mastering the terminal interface. Modern trading platforms present dynamic market feeds, Level-2 order depth, and diverse order configurations to manage price risk.

4.1 Deconstructing the Market Watch: LTP, OHLC, and Market Depth

Core Price Attributes

- **LTP (Last Traded Price):** The exact price at which the most recent trade was matched on the exchange order book.
- **Open Price:** The equilibrium price discovered during the 9:00 AM to 9:08 AM Pre-Market Call Auction.
- **High & Low:** The absolute highest and lowest executed prices during the current trading session.
- **Close Price:** In India, the closing price is not the last trade at 3:30 PM; it is the **Volume-Weighted Average Price (VWAP)** of all trades executed during the final 30 minutes (3:00 PM to 3:30 PM).

Level-2 Market Depth (Order Book)

A real-time electronic table displaying the top 5 highest Bid prices (buyers) and the top 5 lowest Ask/Offer prices (sellers), accompanied by the exact quantity demanded/offered.

- **Bid:** The price a buyer is willing to pay.
- **Ask / Offer:** The price a seller is willing to accept.
- **Bid-Ask Spread:** The difference between the lowest ask and highest bid. Liquid large-cap stocks have narrow spreads (e.g., ₹0.05), while illiquid stocks exhibit wide spreads, imposing slippage costs.

4.2 Circuit Breakers & Price Bands: Volatility Dampeners

To prevent catastrophic speculative flash crashes and fraudulent price manipulation, SEBI enforces a dual-layered circuit breaker framework:

SEBI VOLATILITY CONTROL ARCHITECTURE

Market Circuit Rules

Mechanism	Operating Thresholds	Regulatory Effect
Individual Stock Price Bands	Fixed daily bands of **2%, 5%, 10%, or 20%** based on stock liquidity and surveillance category (ASM/GSM).	If a stock hits its Upper Circuit, trading continues but no sell orders exist (all bids at upper limit). If it hits Lower Circuit, no buyers exist. *(Stocks in F&O segment have no fixed circuit limits, but operate with dynamic 10% flexing bands).*
Market-Wide Circuit Breakers (MWCB)	Triggered by percentage swings in either NIFTY 50 or S&P BSE SENSEX at three stages: **10%, 15%, and 20%**.	Brings about a coordinated nationwide trading halt across all equity and derivative markets: • *10% swing before 1:00 PM:* 45-minute trading halt followed by a 15-minute pre-open call auction. • *15% swing before 1:00 PM:* 1-hour and 45-minute halt. • *20% swing at any time:* Trading is suspended for the remainder of the calendar day.

4.3 Comprehensive Taxonomy of Trading Orders

1. Market Order

An order to buy or sell immediately at the best available prevailing market price on the exchange order book. Guarantees immediate execution speed, but does not guarantee execution price (subject to slippage in volatile markets).

2. Limit Order

An order to buy or sell at a specific stated price or better. A Buy Limit executes only at $le ext{Limit Price}$; a Sell Limit executes only at $ge ext{Limit Price}$. Protects price certainty, but risks non-execution if the market does not reach the specified limit.

3. Stop-Loss Order (SL)

Designed to limit potential losses. Remains dormant until the market hits a designated **Trigger Price**:
• *SL-Limit:* Becomes a limit order upon trigger.
• *SL-Market (SL-M):* Becomes a market order upon trigger (banned by SEBI in options to prevent flash spikes).

4. After Market Orders (AMO)

Orders placed outside standard market hours (e.g., between 4:00 PM and 9:00 AM). Stored on the broker's server and pumped into the exchange order book during the 9:00 AM pre-open auction. Ideal for working professionals unable to track live markets.

5. Good-Till-Triggered (GTT) Orders

A long-term conditional order valid for up to **1 year**. Stored on cloud servers until the stock price triggers a predefined target or stop-loss level, at which point an active limit order is routed to the exchange. Eliminates the need to place daily stop-loss orders.

5. Clearing, Settlement, Contract Notes & Transaction Costs

The post-trade execution lifecycle ensures that buyers receive their purchased securities in their Demat accounts and sellers receive their cash proceeds without counterparty default risk.

5.1 The T+1 Settlement Cycle & The Role of Clearing Corporations

In January 2023, India achieved global financial history by becoming the first major economy in the world to successfully transition its entire equity cash market to a **T+1 Rolling Settlement Cycle** (where T represents the trade execution date). Trades executed on Monday are completely settled on Tuesday.

The settlement process is administered by statutory **Clearing Corporations**: the *NSE Clearing Limited (NCL)* and the *Indian Clearing Corporation Limited (ICCL)*. Under the legal doctrine of **Novation**, the Clearing Corporation interposes itself between the buyer and the seller, becoming the legal counterparty to every single trade—guaranteeing that if a broker or client defaults, the Clearing Corporation's Settlement Guarantee Fund (SGF) settles the obligation, completely eradicating systemic credit risk.

5.2 The Contract Note: Legal Significance & Core Elements

A **Contract Note** is the mandatory statutory legal confirmation issued by a registered stockbroker to a client under SEBI (Stock Brokers and Sub-Brokers) Regulations, confirming the details of all trades executed on behalf of the client. Under SEBI rules, the contract note must be generated and dispatched electronically (digitally signed e-Contract Note) within **24 hours** of trade execution. It serves as the primary legal evidence in any subsequent arbitration or civil dispute.

MANDATORY STATUTORY CONTENTS OF A CONTRACT NOTE Legal Document Audit

- **Identification Headers:** SEBI Registration Number of Broker, Broker CIN, Trading Member ID, and Registered Office Address.
- **Client Credentials:** Unique Client Code (UCC), PAN of Client, Client Demat BO ID, and Registered Residential Address.
- **Granular Trade Metadata:** Order Number, Order Placement Time, Trade Number, Trade Execution Time, Stock Name & ISIN, Transaction Type (Buy/Sell), and Quantity Traded.
- **Financial Ledger Breakdown:** Weighted Average Gross Execution Price, Brokerage Charged, Net Price per share, and an explicit itemized ledger of all statutory government levies (STT, Exchange Charges, SEBI Turnover Fee, Stamp Duty, GST).

5.3 Comprehensive Breakdown of Stock Market Transaction Levies

When executing a trade in the Indian equity market, the total cost incurred by an investor comprises the broker's commission plus six non-negotiable statutory government taxes and regulatory fees:

Cost Component	Statutory Rate (Equity Delivery)	Levying Authority & Objective
1. Brokerage	Zero (Discount Brokers) or up to ₹20 per executed trade / 0.1%–0.5% (Full-service).	Stockbroker revenue for execution and software terminal infrastructure.
2. Securities Transaction Tax (STT)	**0.1%** on both Buy and Sell turnover on delivery trades (or 0.025% on sell side for intraday).	Central Government (Ministry of Finance). Major revenue generator under Finance Act 2004.
3. Exchange Turnover Charges	NSE: ~0.00297% | BSE: ~0.00375% of total turnover.	Stock exchanges for operating the electronic matching server infrastructure.
4. SEBI Turnover Fee	₹10 per Crore (0.0001% of turnover).	SEBI for market regulation and surveillance funding.
5. Stamp Duty	**0.015%** (₹1,500 per Crore) on Buy side only for equity delivery.	State Governments (Indian Stamp Act, 1899 unified nationwide framework).
6. Goods & Services Tax (GST)	**18%** levied strictly on (Brokerage + Exchange Charges + SEBI Fees).	Central & State Governments (GST Council). STT and Stamp Duty are exempt from GST.
7. Depository DP Charges	Flat fee (~₹13 to ₹18.50 + GST) per company per day on **Sell side only**.	Depository (CDSL/NSDL) and DP for debiting shares from the Demat electronic locker.

Numerical Case Demonstration: Calculating Total Costs on an Equity Delivery Purchase

Trade Scenario: An investor purchases 100 shares of Reliance Industries at ₹2,500 per share on delivery via a discount broker charging flat ₹20 brokerage. Total Trade Turnover $= 100 \times ₹2,500 = \mathbf{₹2,50,000}$.

1. Brokerage: Flat ₹20.00.

2. Securities Transaction Tax (STT): $0.1\% \times ₹2,50,000 = \mathbf{₹250.00}$.

3. Exchange Transaction Charges (NSE): $0.00297\% \times ₹2,50,000 = \mathbf{₹7.43}$.

4. SEBI Turnover Fee: $0.0001\% \times ₹2,50,000 = \mathbf{₹0.25}$.

5. Stamp Duty (Buy Side): $0.015\% \times ₹2,50,000 = \mathbf{₹37.50}$.

6. GST (18% on Brokerage + Exchange + SEBI): $18\% \times (₹20.00 + ₹7.43 + ₹0.25) = 18\% \times ₹27.68 = \mathbf{₹4.98}$.

Total Statutory Levies & Charges:
$₹20.00 + ₹250.00 + ₹7.43 + ₹0.25 + ₹37.50 + ₹4.98 = \mathbf{₹320.16}$.
Effective Total Cost to Investor: $₹2,50,000 + ₹320.16 = \mathbf{₹2,50,320.16}$. (Break-even share price increases from ₹2,500 to ₹2,503.20).

6. Calicut University Examination Bank: Questions & Solutions

The following curated question-solution sets reflect the exact academic standards, conceptual depth, and analytical rigor prescribed by Calicut University for **COM1FM105 (2): Stock Market Fundamentals** (Module II: Primary Market and Secondary Market).

Part A: Short Answer Questions (2 Marks Each)

Question 1 [Part A - 2 Marks] **Cognitive Level: Understand**

What is an Initial Public Offering (IPO)? Differentiate between a Fresh Issue and an Offer for Sale (OFS).

An **IPO** is the first public sale of equity shares by an unlisted company to become listed on a recognized stock exchange. In a **Fresh Issue**, new equity shares are created, and proceeds flow directly into the corporate balance sheet for business expansion. In an **Offer for Sale (OFS)**, existing promoters or venture investors sell their personal shares, and proceeds flow directly to those selling shareholders with zero capital going to the company.

Question 2 [Part A - 2 Marks] **Cognitive Level: Remember / Understand**

Define the Book Building process in public issues. What is a Price Band?

Book Building is a dynamic price discovery mechanism where an issuer offers shares within a specified price range, allowing public investors to submit bids at different price points. A **Price Band** consists of a *Floor Price* (lower limit) and a *Cap Price* (upper limit), with SEBI mandating that the Cap Price cannot exceed 120% of the Floor Price.

Question 3 [Part A - 2 Marks] **Cognitive Level: Understand**

What does ASBA stand for, and what is its primary operational benefit?

ASBA stands for *Applications Supported by Blocked Amount*. Its primary operational benefit is that application funds are never debited immediately; they remain blocked in the investor's savings bank account, earning continuous bank interest, and are debited strictly to the extent of actual share allotment, eliminating manual refund delays.

Question 4 [Part A - 2 Marks] **Cognitive Level: Understand**

What is a Red Herring Prospectus (RHP)? Why is it termed "Red Herring"?

A **Red Herring Prospectus** is a preliminary statutory document filed with the ROC that contains complete information regarding the company's operations, assets, and price band, but *omits the final issue price and exact quantum of shares*. It is termed "Red Herring" because of a mandatory red bold disclaimer on its front cover warning investors that the document is incomplete and subject to final price discovery.

Question 5 [Part A - 2 Marks] **Cognitive Level: Understand**

Explain the Free-Float Market Capitalization methodology used in index calculation.

The **Free-Float Market Capitalization** methodology calculates index weightage by multiplying total outstanding shares by the current market price, and then scaling it by the *Free-Float Factor* (excluding locked promoter holdings, government stakes, and cross-holdings). It reflects the value of shares readily available for active public trading on the open stock exchange.

Question 6 [Part A - 2 Marks] **Cognitive Level: Understand**

What is the difference between a Limit Order and a Market Order?

A **Market Order** is executed immediately at the best available prevailing market price on the exchange order book (guaranteeing speed, but not price). A **Limit Order** specifies an exact maximum purchase price or minimum selling price, executing strictly at the specified limit price or better (guaranteeing price, but risking non-execution if market moves away).

Question 7 [Part A - 2 Marks] **Cognitive Level: Understand**

Define Upper Circuit and Lower Circuit in secondary market trading.

Upper and Lower Circuits are statutory price bands (typically 2%, 5%, 10%, or 20%) set by stock exchanges on individual stocks based on the previous day's closing price. If a stock surges to its *Upper Circuit*, trading continues but sell orders cease. If it plummets to its *Lower Circuit*, buy orders cease, preventing uncontrolled speculative panic.

Question 8 [Part A - 2 Marks] **Cognitive Level: Understand**

What is a Contract Note, and within what timeframe must a broker dispatch it?

A **Contract Note** is the mandatory legal trade confirmation document issued by a SEBI-registered broker detailing trade price, order execution time, Unique Client Code (UCC), brokerage, and statutory levies. Under SEBI regulations, it must be generated and dispatched electronically to the client within **24 hours** of trade execution.

Part B: Short Essay / Conceptual Questions (5 Marks Each)

Question 9 [Part B - 5 Marks] **Cognitive Level: Analyze**

Explain the ASBA and UPI payment mechanisms for IPO applications. Trace the step-by-step lifecycle of an application from submission to allotment.

1. ASBA & UPI Architecture: ASBA (Applications Supported by Blocked Amount) allows retail investors to apply for IPOs by lien-marking funds in their savings bank account. With UPI ASBA (capped at ₹5,00,000), investors apply via broker trading apps, which routes a mandate request to their UPI banking app.

2. Step-by-Step Lifecycle:

- *Step 1 (Application & Bidding):* The retail investor selects the IPO, enters the bid lot quantity at the Cut-off price, and enters their UPI ID.
- *Step 2 (Mandate Authorization):* The investor receives a mandate notification on Google Pay/PhonePe/BHIM and inputs their UPI MPIN. The bank places a lien block on the specified sum (e.g., ₹14,500).
- *Step 3 (Bidding Window Close & Allotment):* The registrar (e.g., Link Intime, KFintech) compiles all valid bids and conducts the electronic Basis of Allotment.
- *Step 4 (Settlement / Debit / Unblock):* If allotted, the blocked funds are debited from the bank account and shares are credited to the Demat account on T+1 after allotment. If not allotted, the registrar sends an automated electronic instruction to the bank to release the lien within 24 hours.

Question 10 [Part B - 5 Marks] **Cognitive Level: Analyze**

Distinguish between the National Stock Exchange (NSE) and the Bombay Stock Exchange (BSE) across historical origin, benchmark indices, and operational structure.

Parameter	Bombay Stock Exchange (BSE)	National Stock Exchange (NSE)
Establishment & Heritage	Founded in 1875 by Premchand Roychand; Asia's oldest stock exchange.	Incorporated in 1992 following the Pherwani Committee recommendations.
Benchmark Index	**S&P BSE SENSEX** (composed of 30 blue-chip large-cap stocks; base 1978–79 = 100).	**NIFTY 50** (composed of 50 large-cap stocks across 13 sectors; base 1995 = 1,000).
Electronic Trading Platform	**BOLT** (BSE Online Trading), launched in 1995.	**NEAT** (National Exchange for Automated Trading), pioneer of satellite screen trading in 1994.
Corporate Structure	Historically a broker-owned association; corporatized and listed on NSE in 2017.	Demutualized from inception; owned by institutional financial institutions.
Market Dominance	Largest number of listed companies (5,300+), but lower cash and derivative turnover.	Undisputed global leader in equity derivatives and dominant leader in cash market volume.

Question 11 [Part B - 5 Marks] **Cognitive Level: Understand & Apply**

Explain the operational mechanism of Market-Wide Circuit Breakers in India. What are the percentage thresholds and corresponding trading halt durations?

Mechanism: Market-Wide Circuit Breakers (MWCB) are coordinated systemic volatility filters enforced by SEBI that apply across all equity and derivative markets nationwide. They are triggered when either the **NIFTY 50 or S&P BSE SENSEX** breaches predetermined percentage thresholds relative to the previous day's closing value:

1. 10% Circuit Breaker:

- *Before 1:00 PM:* 45-minute complete trading halt + 15-minute pre-open auction.
- *At or after 1:00 PM up to 2:30 PM:* 15-minute trading halt + 15-minute pre-open auction.
- *At or after 2:30 PM:* No halt; trading continues normally.

2. 15% Circuit Breaker:

- *Before 1:00 PM:* 1-hour and 45-minute trading halt + 15-minute pre-open auction.
- *At or after 1:00 PM up to 2:00 PM:* 45-minute trading halt + 15-minute pre-open auction.
- *At or after 2:00 PM:* Trading is suspended for the remainder of the day.

3. 20% Circuit Breaker: Triggered at *any time of the day*, resulting in immediate complete suspension of all securities and derivative trading for the remainder of the calendar day.

Part C: Comprehensive Essay & Problem Solving (10 / 15 Marks)

Question 12 [Part C - 15 Marks] **Cognitive Level: Evaluate & Synthesize**

Comprehensive Essay: Describe the end-to-end procedural journey of an Initial Public Offering (IPO) in India. Detail the regulatory prerequisites under SEBI ICDR, the book building pricing process, the reservation quotas for different investor classes, and the post-issue allotment and listing mechanics.

The Complete Architecture & Procedural Roadmap of an Indian IPO

An Initial Public Offering (IPO) represents the ultimate regulatory and corporate milestone for an enterprise. Governed by the **SEBI (Issue of Capital and Disclosure Requirements) Regulations, 2018** and Chapter III of the Companies Act, 2013, the process spans four rigorous chronological phases:

Phase 1: Pre-Issue Structuring & Due Diligence

- **Eligibility Criteria (SEBI ICDR Regulation 6(1)):** The issuer must satisfy three financial thresholds: (a) Net tangible assets of at least ₹3 Crores in each of the preceding 3 fiscal years; (b) Average operating profit of at least ₹15 Crores during the 3 preceding years; and (c) Net worth of at least ₹1 Crore in each of the preceding 3 years. *(Firms failing this profitability route must allocate at least 75% of net issue to QIBs under Regulation 6(2)).*
- **Appointment of Intermediaries:** The issuer appoints SEBI-registered Book Running Lead Managers (BRLMs), legal counsels, statutory auditors, and Registrar and Transfer Agents (RTAs).
- **Filing the DRHP:** The BRLMs draft the Draft Red Herring Prospectus, filing it simultaneously with SEBI and stock exchanges. It is hosted publicly for 21 days for public scrutiny. SEBI reviews the disclosures and issues binding observation letters.

Phase 2: Pricing Discovery via Book Building

- **Filing the RHP:** Incorporating SEBI's observations, the Red Herring Prospectus is registered with the ROC, announcing the **Price Band** (Floor Price and Cap Price, where Cap $le 120%$ of Floor) and bid lot size (minimum number of shares an investor can bid for).
- **Anchor Investor Allocation:** One day prior to public opening, up to 60% of the QIB quota is allocated to Anchor Investors at a fixed price, establishing institutional credibility.
- **Public Bidding Window:** The issue remains open for public bidding for **3 to 5 working days**. Bids are submitted electronically via ASBA/UPI. Retail investors have the unique privilege of bidding at the "*Cut-off Price*".

Phase 3: Allotment Formulation & Reservation Quotas

Under SEBI regulations, the net offer is divided into mandatory statutory tranches:

- **Qualified Institutional Buyers (QIB - 50%):** Proportionate allotment among institutional mutual funds, FPIs, and banks.
- **Non-Institutional Investors (NII - 15%):** High-net-worth bids above ₹2 Lakhs, subdivided into Small HNI (₹2L–₹10L) and Big HNI (>₹10L).
- **Retail Individual Investors (RII - 35%):** Applications $le ₹2,00,000$. If oversubscribed, SEBI mandates that maximum retail applicants receive at least one minimum lot via an electronic randomized computerized lottery.

Phase 4: Settlement, Demat Credit & Exchange Listing

- **Finalizing Basis of Allotment:** The registrar audits all applications, eliminates technical rejections (e.g., mismatched PAN or failed UPI mandate), and finalizes the cut-off price based on institutional demand.
- **Lien Debit & Unblock:** The SCSBs debit the exact funds corresponding to allotted shares and release the lien on unallotted funds.
- **Demat Credit & Listing (T+3 Standard):** Under modern SEBI rules, the entire IPO cycle from issue closure to formal listing has been compressed to **T+3 working days**. Shares are credited to the investor's demat account on T+2, and the stock formally commences trading on the stock exchanges on T+3 morning.

Question 13 [Part C - 15 Marks] **Cognitive Level: Apply & Calculate**

Secondary Market Financial & Practical Problem:

1. **A stock market index consists of three companies: Alpha Ltd, Beta Ltd, and Gamma Ltd. The base year market capitalization is ₹25,000 Crores, and the base index value is 1,000. Using the following data, calculate: (a) Total Market Capitalization, (b) Total Free-Float Market Capitalization, and (c) The Current Value of the Stock Market Index.**
   - **Alpha Ltd: 20 Crore shares; CMP = ₹400; Promoter locked holding = 50%.**
   - **Beta Ltd: 50 Crore shares; CMP = ₹150; Promoter locked holding = 40%.**
   - **Gamma Ltd: 10 Crore shares; CMP = ₹1,000; Promoter locked holding = 70%.**
2. **An investor sells 200 shares of Alpha Ltd at ₹420 per share on equity delivery through a discount broker charging flat ₹20 brokerage. Calculate the net cash payout received by the investor after deducting all statutory levies: Brokerage (₹20), STT (0.1% on delivery sell), Exchange transaction charges (0.00297%), SEBI turnover fee (0.0001%), Stamp duty (0% on sell), GST (18% on Brokerage + Exchange + SEBI), and Depository DP Charges (flat ₹15.50 + 18% GST).**

Comprehensive Mathematical Solutions

Part 1: Free-Float Index Calculation

Step 1: Calculate Total Market Capitalization:

- Alpha Ltd: $20 ext{ Cr shares} imes ₹400 = mathbf{₹8,000 ext{ Crores}}$.
- Beta Ltd: $50 ext{ Cr shares} imes ₹150 = mathbf{₹7,500 ext{ Crores}}$.
- Gamma Ltd: $10 ext{ Cr shares} imes ₹1,000 = mathbf{₹10,000 ext{ Crores}}$.
- **(a) Total Market Cap:** $₹8,000 + ₹7,500 + ₹10,000 = mathbf{₹25,500 ext{ Crores}}$.

Step 2: Calculate Free-Float Factor (IWF) & Free-Float Market Cap:

- Alpha Ltd: $ ext{Free-Float Factor} = 1.0 - 0.50 = 0.50$.
  $ ext{Free-Float Cap} = ₹8,000 ext{ Cr} imes 0.50 = mathbf{₹4,000 ext{ Crores}}$.
- Beta Ltd: $ ext{Free-Float Factor} = 1.0 - 0.40 = 0.60$.
  $ ext{Free-Float Cap} = ₹7,500 ext{ Cr} imes 0.60 = mathbf{₹4,500 ext{ Crores}}$.
- Gamma Ltd: $ ext{Free-Float Factor} = 1.0 - 0.70 = 0.30$.
  $ ext{Free-Float Cap} = ₹10,000 ext{ Cr} imes 0.30 = mathbf{₹3,000 ext{ Crores}}$.
- **(b) Total Free-Float Market Cap:** $₹4,000 + ₹4,500 + ₹3,000 = mathbf{₹11,500 ext{ Crores}}$.

Step 3: Calculate Index Value:

$ ext{Current Index Value} = ⬆rac{ ext{Current Free-Float Market Cap}}{ ext{Base Market Cap}} imes ext{Base Index Value} = ⬆rac{₹11,500 ext{ Crores}}{₹25,000 ext{ Crores}} imes 1,000 = mathbf{460.00}$

Part 2: Transaction Charges on Equity Delivery Sale

Gross Sale Proceeds: $200 ext{ shares} imes ₹420 = mathbf{₹84,000.00}$.

- **1. Brokerage:** Flat **₹20.00**.
- **2. Securities Transaction Tax (STT):** $0.1% imes ₹84,000 = mathbf{₹84.00}$.
- **3. Exchange Transaction Charges (NSE):** $0.00297% imes ₹84,000 = mathbf{₹2.50}$.
- **4. SEBI Turnover Fee:** $0.0001% imes ₹84,000 = mathbf{₹0.08}$.
- **5. Stamp Duty: ₹0.00** (Stamp duty is levied strictly on Buy side).
- **6. GST (18% on Brokerage + Exchange + SEBI):** $ ext{GST Base} = ₹20.00 + ₹2.50 + ₹0.08 = ₹22.58 implies 18% imes ₹22.58 = mathbf{₹4.06}$
- **7. Depository DP Charges:** Flat ₹15.50 + 18% GST ($₹15.50 + ₹2.79$) = **₹18.29**.

Total Deductions:
$ ext{Total Deductions} = ₹20.00 + ₹84.00 + ₹2.50 + ₹0.08 + ₹0.00 + ₹4.06 + ₹18.29 = mathbf{₹128.93}$.

Net Cash Payout Received by Investor:
$ ext{Net Payout} = ₹84,000.00 - ₹128.93 = mathbf{₹83,871.07}$