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25 Solved Questions on
Securities Market



SEBI Officer
Grade A
2018

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1. A call money market is generally used for _____ hours
 - (1) 24
 - (2) 48
 - (3) 96
 - (4) 12
 - (5) 72

Answer key: 1

Solution:

A call money market is as short as 24 hours, one can borrow money within a quite short period of time via a standard instrument, the so-called "call money". These are funds borrowed for one day, from 12:00 PM today until 12:00 PM on the next day, after which the loan becomes "on call" and is callable at any time.

2. Which of the following was the chief regulator of commodity markets before its merger with the capital market regulator SEBI?
 - (1) Commodity markets Commission
 - (2) Multi commodity exchange (MCX)
 - (3) National commodity and derivatives exchange Ltd (NCDEX)
 - (4) Forward Markets Commission
 - (5) Agricultural produce and markets commission

Answer key: 4

Solution:

FMC has been regulating commodities markets since 1953, but lack of powers has led to wild fluctuations and alleged irregularities remaining untamed in this market segment.

The commodities market has been known to be more prone to speculative activities compared to the better-regulated stock market, while illegal activities like 'dabba trading' have also been more frequent in this segment. Besides, the high-profile NSEL scam has rocked this market and the subsequent regulatory and government interventions in this case eventually led to the government announcing FMC's merger with SEBI on 28th September 2015.

3. In order to broaden the market, the minimum size of commercial papers has been relaxed gradually from _____ to Rs. 5. Lakhs.
 - (1) 20 lakhs
 - (2) 50 lakhs
 - (3) 1 crore
 - (4) 10 crores
 - (5) 100 crores

Answer key: 3

Solution:

Conditions relating to issuing of Commercial Papers (CPs) have been relaxed gradually with a view to broad-basing the market. For instance, the maturity period has been changed from 91 days - 6 months earlier to 15 days - 1 year. The minimum size of CPs has also been reduced from Rs.1 crore to Rs. 5 lakhs. The issuer base has been widened by allowing PDs, SDs and AIFIs, apart from corporates, to issue CPs to access short-term funds.

4. Money market instruments are generally used for Liquidity adjustments, considering this statement to be true. Who are the users mostly?
 - (1) Government
 - (2) Corporates
 - (3) Venture capitalists
 - (4) Dealers
 - (5) Banks

Answer key: 5

Solution:

Money market instruments are generally used for financing short term liquidity requirements, the same is used by all scheduled commercial and private banks. A dealer is an intermediary between the counterparts, called a dealer, announces a bid and an offer rate with the difference between the two representing a spread, or the dealer's income

5. Which of the following comprises the domestic debt market in India?

- I. Government Securities
- II. Private corporate debt
- III. PSU bonds
- IV. DFIs bonds

- (1) I and III
- (2) I, II and III
- (3) III and IV
- (4) I, II, III and IV
- (5) Only I

Answer key: 4

Solution:

The domestic debt market comprises of two main segments, viz., the Government securities and other (mainly corporate) securities comprising private corporate debt, PSU bonds and DFIs bonds. The government securities market is pre-dominant, while the other segment is not very deep and liquid.

6. Who among the following are the main participants in the securities market?

- I. Issuer of securities
- II. Investors in securities
- III. Intermediaries
- IV. The state governments

- (1) Only IV
- (2) Both I and II
- (3) I, II and III
- (4) I, II, III and IV
- (5) II and III only

Answer key: 3

Solution:

The securities market essentially has three categories of participants, namely, the issuers of securities, investors in securities and the intermediaries, such as merchant bankers, brokers etc. While the corporates and the government raise resources from the securities market to meet their obligations, it is households that invest their savings in the securities market.

7. Which of the following is the clearing agency for G-secs in India?

- (1) RBI
- (2) SEBI
- (3) Ministry of Finance
- (4) FEMA
- (5) CCIL

Answer key: 5

Solution:

The Clearing corporation of India Ltd (CCIL) is the clearing agency for G-Secs. It acts as a Central Counter Party (CCP) for all transactions in G-Secs by interposing itself between two counterparties. In effect, during settlement, the CCP becomes the seller to the buyer and buyer to the seller of the actual transaction. All outright trades undertaken in the OTC market and on the NDS-OM platform are cleared through the CCIL.

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8. There are 2 types of derivatives, futures and options. Which of the following is correct about Futures contracts?
- (1) Futures contracts grant buyers rights and no obligations
 - (2) In Futures contracts both parties face a lot of risk
 - (3) It permits the buyer an option to buy call or put
 - (4) Both 1 and 2
 - (5) All 1, 2 and 3

Answer key: 2

Solution:

Derivatives are financial contracts that derive value from the underlying assets. There are 2 types of derivatives - futures and options.

1. Futures contracts grant rights with obligations to the traders with the open position settled on maturity. It obliges a person to buy or sell the underlying, at the price they agreed on, at a future date.

With futures, both parties face a lot of risk as prices could move against them.

2. Option contracts grant buyers the right but not the obligation. It permits the buyer an option to buy call or put, where the seller of the option has an obligation to comply with the contract. Here the buyer has limited risk and seller has large risk.

9. Commercial Paper is a note in evidence of the _____ of the issuer.

- (1) Equity obligation
- (2) Debt Obligation
- (3) Market Obligation
- (4) Working capital obligation
- (5) None of the above

Answer key: 2

Solution:

Commercial Paper is a note in evidence of the debt obligation of the issuer. On issuing commercial paper the debt is transformed into an instrument.

CP is an unsecured promissory note privately placed with investors at a discount rate of face value determined by market forces.

10. Treasury Bills are short-term (up to one year) borrowing instruments issued by _____

- (1) State Government
- (2) President
- (3) Governor
- (4) Union Government
- (5) Council of Ministers

Answer key: 4

Solution:

T Bills are issued by the union government. It's a promise by the Government to pay the stated sum after the expiry of the stated period from the date of issue (less than one year). They are issued at a discount off the face value and on maturity, the face value is paid to the holder.

11. Which of the following is a power of SEBI?

- (1) Regulating the business in stock exchanges only
- (2) Regulating the business in other securities markets
- (3) Regulating the flow of funds to the various organisations registered with SEBI
- (4) Both 1 and 2
- (5) Both 1 and 3

Answer key: 4

Solution:

SEBI has no power to regulate the flow of funds to the various organisations registered with SEBI as it is under their own control. SEBI only takes care of fraudulent and unfair trade practices relating to securities markets.

12. SEBI has recently approved (August 2018) new KYC norms for Foreign portfolio Investments to trade in _____
- (1) Exchange Currency markets
 - (2) Primary Markets
 - (3) Secondary Markets
 - (4) Commodity Markets
 - (5) Government Securities

Answer key: 4

Solution:

SEBI has approved a proposal to allow foreign investors to trade in commodity derivatives market, except for sensitive commodities, as well as common application form for the registration of FPIs in the domestic markets. The board has given its nod for amending delisting regulations. Further, inter-operability of clearing houses for commodities and new methodology to calculate the total expenses ratio for fund managers have been cleared.

13. What is the name of the screen based electronic order matching system for secondary market trading in government securities owned by RBI?
- (1) GDS-OM
 - (2) NDS-OM
 - (3) G-Secs module
 - (4) e-Kuber
 - (5) e-biz

Answer key: 2

Solution:

Negotiated dealing system- order matching system NDS-OM is a screen based electronic anonymous order matching system for secondary market trading in Government securities owned by RBI. Presently the membership of the system is open to entities like Banks, Primary Dealers, Insurance Companies, Mutual Funds etc. i.e entities who maintain SGL accounts with RBI. These are Primary Members (PM) of NDS and are permitted by RBI to become members of NDS-OM.

14. The minimum net worth stipulated by SEBI for a depository is _____
- (1) Rs. 100 crores
 - (2) Rs. 1000 crore
 - (3) Rs. 500 crores
 - (4) Rs. 50 crores
 - (5) None of the above

Answer key: 1

Solution:

The minimum net worth stipulated by SEBI for a depository is Rs.100 crore.

A depository is an organisation which holds securities (like shares, debentures, bonds, government securities, mutual fund units etc.) of investors in electronic form at the request of the investors through a registered depository participant. It also provides services related to transactions in securities.

15. How is the price of a bond calculated?
- (1) Sum of present values of all future cashflows
 - (2) Sum of future values of all future cashflows
 - (3) Sum of future values of all present cashflows
 - (4) Sum of all the values of the cashflows now.
 - (5) None of the above

Answer key: 1

Solution:

The price of a bond is nothing but the sum of present value of all future cash flows of the bond. The interest rate used for discounting the cash flows is the Yield to Maturity (YTM).

16. What can be said about the relationship between the yield and price of a bond?

- (1) If the market interest rate levels rise, the price of a bond falls.
- (2) If the market interest rate levels fall, the price of a bond rises.
- (3) The yield of a bond is inversely related to its price
- (4) All the above
- (5) None of the above

Answer key: 4

Solution:

Every point mentioned is true.

If the market interest rate levels rise, the price of a bond falls. Conversely, if interest rates or market yields decline, the price of the bond rises. In other words, the yield of a bond is inversely related to its price.

The relationship between yield to maturity and coupon rate of bond may be stated as follows:

When the market price of the bond is less than the face value, i.e., the bond sells at a discount, $YTM > \text{coupon yield}$.

When the market price of the bond is more than its face value, i.e., the bond sells at a premium, $\text{coupon yield} > YTM$.

When the market price of the bond is equal to its face value, i.e., the bond sells at par, $YTM = \text{coupon yield}$.

17. Which of the following is referred to as "Duration" of a bond?

- (1) The time taken to recover the initial investment in present value terms
- (2) The time taken to recover the initial investment in terms of future values.
- (3) The payback period of a bond to breakeven
- (4) Either (1) or (2)
- (5) Either (1) or (3)

Answer key: 5

Solution:

Duration (also known as Macaulay Duration) of a bond is a measure of the time taken to recover the initial investment in present value terms. In simplest form, duration refers to the payback period of a bond to break even, i.e., the time taken for a bond to repay its own purchase price. Duration is expressed in number of years.

18. What does 'STRIPS' stand for?

- (1) Stock trading and registering interest and payment of stocks.
- (2) Securities transaction related information portal system.
- (3) Separate trading of registered interest and principal of securities.
- (4) Securities trading of registered interest and principal of securities.
- (5) Stock market related information of payment and negotiation systems.

Answer key: 3

Solution:

STRIPS is the acronym for 'Separate Trading of Registered Interest and Principal of Securities'. These are basically "zero-coupon" securities where the investor receives a payment at maturity only. STRIPS allow investors to hold and trade the individual interest and principal components of eligible Government securities as separate securities of varying tenure. They are popular with investors who want to receive a known payment on a specific future date and want to hold securities of desired maturity.

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19. What do you mean by Dematerialization?

- (1) Conversion of physical shares into electronic form only.
- (2) Conversion of shares of electronic form into physical form only.
- (3) Conversion of shares of electronic form into physical form and crediting it to the investor's account with his depository participant (DP).
- (4) Conversion of physical shares into electronic form and crediting it to the investor's account with his depository participant (DP).
- (5) Making payment of the stocks sold on the secondary market.

Answer key: 4

Solution:

Dematerialization is the process by which physical certificates of an investor are converted to an equivalent number of securities in electronic form and credited to the investor's account with his Depository Participant (DP).

Earlier the securities were held in physical form in the folios which has been done away with and now every investor has to hold the shares in electronic form.

The securities are held in the electronic form in an account known as "Demat Account"

20. What is the name of the market that provides a channel for the sale of new securities?

- (1) Primary market
- (2) Secondary market
- (3) Tertiary Market
- (4) Either of the above
- (5) None of the above

Answer key: 1

Solution:

The securities market has two interdependent segments: the primary (new issues) market and the secondary market. The primary market provides the channel for sale of new securities while the secondary market deals in securities previously issued.

21. What is 'book building' in an IPO?

- (1) A process used to differentiate securities in the market.
- (2) A process for efficient lot delivery to the concerned investors.
- (3) A process used for efficient price discovery.
- (4) A process used to differentiate competitors from the organisation
- (5) A process used to record the number of securities applied.

Answer key: 3

Solution:

Book Building is basically a process used in IPOs for efficient price discovery. It is a mechanism where, during the period for which the IPO is open, bids are collected from investors at various prices, which are above or equal to the floor price. The offer price is determined after the bid closing date.

22. What is a "Prospectus" in terms of a company that is going public in the securities market?

- (1) Companies future prospects as prescribed by SEBI
- (2) Companies disclosing the reason for raising the money, the way it is spent and the return on it.
- (3) Company declaring future payment of dividends.
- (4) Company showcasing their current products to market themselves
- (5) None of the above

Answer key: 2

Solution:

A large number of new companies float public issues. While a large number of these companies are genuine, quite a few may want to exploit the investors. Therefore, it is very important that an investor before applying for any issue identifies future potential of a company. A part of the guidelines issued by SEBI (Securities and Exchange Board of India) is the disclosure of information to the public. This disclosure includes information like the reason for raising the money, the way money is proposed to be spent, the return expected on the money etc. This information is in the form of 'Prospectus' which also includes information regarding the size of the issue, the current status of the company, its equity capital, its current and past performance, the promoters, the project, cost of the project, means of financing, product and capacity etc.

23. Which of the following are the sources through which the companies in India can raise foreign currency resources?

- I. Issuing foreign currency convertible bonds
- II. Issuing ordinary shares through Global depository receipts
- III. Issuing ordinary shares through American depository receipts

- (1) I and II
- (2) I and III
- (3) I, II and III
- (4) II and III
- (5) None of the above

Answer key: 3

Solution:

Indian companies are permitted to raise foreign currency resources through two main sources: a) issue of foreign currency convertible bonds more commonly known as 'Euro' issues and b) issue of ordinary shares through depository receipts namely 'Global Depository Receipts (GDRs)/American Depository Receipts (ADRs)' to foreign investors i.e. to the institutional investors or individual investors.

24. Which of the following are clearly segregated when we compare demutualised exchange from a mutualised exchange?

- I. Ownership
- II. Management
- III. Source of funds

- (1) I, II and III
- (2) II and III
- (3) III and I
- (4) I and II
- (5) None of the above

Answer key: 4

Solution:

In a mutual exchange, the three functions of ownership, management and trading are concentrated into a single Group. Here, the broker members of the exchange are both the owners and the traders on the exchange and they further manage the exchange as well. This at times can lead to conflicts of interest in decision making.

A demutualised exchange, on the other hand, has all these three functions clearly segregated, i.e. the ownership, management and trading are in separate hands.

25. What is 'ICDR' in the ICDR regulations as prescribed by SEBI?

- (1) Issue of current equity and debt requirements
- (2) Issue of capital and disclosure requirements
- (3) Issue of convertible debentures raised through equity
- (4) Issue of currency derivatives resource
- (5) Investing capital directly in the regulated markets.

Answer key: 2

Solution:

The SEBI ICDR Regulations lay down guidelines relating to conditions for various kinds of issues including public and rights issue. The ICDR Regulations provide detailed provisions relating to public issue such as conditions relating to an IPO and Further Public Offer (FPO), conditions relating to pricing in public offerings, conditions governing promoter's contribution, restriction on transferability of promoter's contribution, minimum offer to public, reservations, manner of disclosures in offer documents, etc.

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