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B.Com Honours

Semester I

Calicut University

Basics of Financial Markets

Course Code: COM1MN105 • Module 3 Notes

1. Introduction to Capital Market and Primary Market

The capital market is the channel through which long-term funds are raised and allocated. It serves as the primary source of funding for industrial growth, infrastructure projects, and corporate expansions. This module covers the functions of the capital market, primary market intermediaries, methods of floating new issues (IPO, FPO, Rights, Bonus), and the Application Supported by Blocked Amount (ASBA) framework.

Primary Market vs. Secondary Market

The capital market is split into two complementary segments:

- **Primary Market (New Issue Market):** Deals with the issuance of brand-new securities. Transactions take place directly between the company and the investor. It contributes directly to capital formation.
- **Secondary Market (Stock Market):** Deals with the trading of existing securities among investors. It provides liquidity and price discovery but does not directly supply new capital to the company.

Intermediaries in the Primary Market

To execute a public issue successfully, companies employ several specialized intermediaries:

- **Merchant Bankers (Book Runners):** Act as lead managers who design the issue prospectus, price the shares, coordinate with SEBI, and manage the IPO launch.
- **Underwriters:** Guarantee to purchase any unsold portion of the public issue in exchange for an underwriting commission, mitigating subscription risk for the issuer.
- **Registrars to the Issue:** Maintain records of investor applications, calculate allotment ratios, and handle share credits and refund processes.
- **Bankers to the Issue:** Authorized banks that collect application money from investors and transfer it to the company's escrow account.

2. Methods of Floating New Issues

Companies choose different routes to issue new securities depending on capital requirements and target audiences:

Issue Method	Core Concept	Target Audience	Key Advantage
Initial Public Offering (IPO)	First public sale of shares by a private company.	General public, retail and institutional investors.	Access to massive capital; provides liquidity to founders.
Follow-on Public Offering (FPO)	Subsequent sale of shares by an already listed company.	General public and institutions.	Provides additional funding for growth or debt reduction.
Private Placement	Direct sale of securities to a select group of institutional investors.	Qualified Institutional Buyers (QIBs), venture capital.	Fast execution; minimal regulatory and underwriting costs.
Rights Issue	Offering additional shares to existing shareholders in proportion to their holding.	Current shareholders of the company.	Protects ownership control; usually priced at a discount.
Bonus Issue	Issuing free shares to existing shareholders by capitalizing reserves.	Current shareholders.	Increases share liquidity without cash outflow.

3. ASBA (Application Supported by Blocked Amount)

ASBA is a mandatory application process notified by SEBI for bidding in public issues (IPOs and FPOs) in India. It represents a major reform that protects retail investors from liquidity blockages during the IPO bidding process.

How ASBA Works

1. **Application Submission:** The investor submits the IPO bid through their net-banking account or broker portal, providing their PAN and DP details.
2. **Fund Blocking:** Instead of transferring cash to the issuer immediately, the application money is **blocked** in the investor's self-bank account.
3. **Interest Accrual:** The blocked money continues to earn interest for the investor throughout the bidding and allotment period.
4. **Allotment Phase:** Once the allotment ratio is finalized:
 - If the shares are fully allotted: The blocked funds are debited and shares are credited to the investor's Demat account.
 - If the shares are partially/not allotted: The block on the remaining or entire amount is lifted, making the funds immediately available.

Advantages of ASBA

ASBA eliminates the delayed refund process (which previously took weeks), prevents interest losses for retail investors, and simplifies transaction tracking for banks and companies.

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