THE VILLAGE INTERNATIONAL SCHOOL

UNIT-6: RESOURCE MOBILIZATION

Unit 6: Resource Mobilization	
Competencies: Risk taking, Communication, Persuasion, Networking, Ethical behavior	
Contents	**Learning Outcomes**
• Capital Market: Concept • Primary market: Concept, methods of issue • Angel Investor: Features • Venture Capital: Features, funding.	After going through this unit, the student/ learner would be able to: • Understand the need of finance in Business • Discuss the various sources of funds required for a firm • Understand the ways of raising funds in primary market • Appreciate the Angel Investors and Venture Capitalists as a source of business finance.

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TOPICS: -

1.SECONDARY MARKET
2.NEED FOR AND IMPORTANCE OF SPECIALISED FINANCIAL INSTITUTIONS AND TYPES OF SPECIALISED FINANCIAL INSTITUTIONS

1	**Explain the importance of finance in business.**
Ans	The significance of finance in enterprise is elucidated like a lubricant to the process of production. It's one of the most important prerequisites to start an enterprise. Finance is the elixir that assists in the formation of new businesses, and allows businesses to take advantage of opportunities to grow and expand. Right from the very beginning i.e. conceiving an idea; finance is required to: a) Promote or establish the business b) Acquire fixed assets c) Make market investigations d) Develop product e) Keep men and machines at work f) Encourage management to make progress and create value. g) Expand, diversify, improve and grow. h) Be enough to meet unexpected/unplanned business expenses.
2	**Explain the importance of capital market.**

Ans	A capital market may be defined as an organized mechanism meant for effective and smooth transfer of money capital or financial resources from the investors to the entrepreneurs. Here, productive capital is raised and made available for industrial purposes. Capital markets are the most important source of raising finance for the entrepreneurs as this market can: a) Mobilize the financial resources on a nation-wide scale. b) Secure the required foreign capital and know-how to promote economic growth at a faster rate. c) Ensure the most effective allocation of the mobilized financial resources by directing the same either to such projects which are capable of the highest yield or to the underdeveloped priority areas where there is an urgent need to promote balanced and diversified industrialization.

3	**List the different markets available under capital market.**
Ans	As per entrepreneur's requirement they enter either of the following markets available under capital market: • Primary market (new issues market) • Secondary market
4	**Explain the concept of primary market.**
Ans	Primary market is basically to facilitate transfer of resources from the savers to the entrepreneurs' seeking funds for: a) Setting new enterprises b) Expanding c) Diversifying The 'new issues' may be issued by: 1) New companies – also called initial issues. 2) Old companies – also called further issues.
5	**List the methods of flotation of new issues.**
Ans	An entrepreneur can raise the required capital in the primary market by the following methods: 1. Public issue 2. Rights issue 3. Private placement 4. Offer to the employees
6	**Explain public issue.**
Ans	• Public issue is the most popular method of raising capital these days by the entrepreneurs. • This involves raising of funds directly from the public through the issue of prospectus. • An enterprise organizing itself as a public limited company can raise the required funds commonly by preparing a prospectus. • When an entrepreneur a offers shares to the public for subscription he/she is required to comply with all the restrictions and formalities pertaining to the initial issues, prospectus drafting and launch.

7	**When an entrepreneur decides to go public and become a public company, he/she tends to be in advantageous positions. What are the benefits of doing so?**
Ans	**1) Access to capital** The primary advantage an entrepreneur stands to gain by going public is access to capital. In addition, the capital does not have to be repaid and does not involve an interest charge. The only reward the IPO investors seek is an appreciation of their investment and possibly dividends. Entrepreneur can use the capital raised for a variety of purposes including: (1) growth and expansion, (2) retiring existing debt, (3) corporate marketing and development (4) acquisition capital. An entrepreneur's financing alternatives stands greatly increased. **2) Other advantages** • **Mergers and acquisitions:** Public stock of a company can be used for businesses to grow through acquisitions. • **Higher valuations:** Public companies are typically valued more than private companies. • **Benchmark trading price:** The trading price of a public company's stock serves as a benchmark of the offer price of other securities. • **Capital formation:** Raising capital later is typically easier because of the extra liquidity for the investors. • **Incentives:** Stock options and stock incentives can be very helpful in attracting employees.
	• **Reduced business requirements:** While an underwritten initial public offering requires significant earnings, the lack of earnings does not keep a private company from going public. • **Less dilution:** There is less dilution of ownership control compared to an IPO. • **Liquidity:** A public company provides liquidity for management, minority shareholders, and investors. • **Prestige:** Added prestige and visibility with customers, suppliers, as well as the financial community.
8	**When an entrepreneur decides to go public and become a public company, he/she tends to be in advantageous positions but there are certain drawbacks also. List the drawbacks.**
Ans	While there are benefits to going public, it also means additional obligations and reporting requirements such as: • Increasing accountability to public shareholders • Need to maintain dividend and profit growth trends • Becoming more vulnerable to an unwelcome takeover • Need to observe and adhere strictly to the rules and regulations by governing bodies • Increasing costs in complying with higher level of reporting requirements • Relinquishing some control of the company following the public offering • Suffering a loss of privacy as a result of media interest
9	**Explain Rights issue.**

Ans	• Rights issue is a method of raising additional finance from existing shareholders by offering securities to them on pro-rata basis i.e. giving them a right to a certain number of shares in proportion to the shares they are holding. • Normally, through a circular, rights issues are proposed to the existing shareholders and in case they are not willing to subscribe, they can renounce the same in favour of another person. • This method of issuing securities is considered to be inexpensive as it does not require any brokers, agents, underwriters, prospectus or enlistment, etc.
10	**Explain Private placement.**
Ans	Private placement means the direct sale by a company of its securities to a limited number of sophisticated investors. Entrepreneurs, herein, raise funds by selling the issues mainly to the institutional investors like: • Unit Trust of India • Life Insurance Corporation of India • General Insurance Corporation of India • Army Group Insurance • State Level Financial Corporations, etc.
11	**Explain Offer to employees**
Ans	Stock options or offering shares to the employees has gained much popularity in many countries of the world. This method enables employees to become shareholders and share the profits of the company leading to: a) Higher efficiency b) Low labour turnover c) Better industrial locations d) Low floatation cost e) Wider/higher generation of funds.
12	**Explain the concept of secondary market.**
Ans	Capital markets aid in the mobilization of individual savings to make them readily available to those who need them in: Industry

	Trade Finance Government • Any transaction in shares or debentures subsequent to its primary offering is called "Secondary Transaction". • Thus, the secondary capital market, which is also known as old securities market or stock exchange deals with buying and selling of old securities i.e. the market securities issued earlier are sold by existing investors in this market, thus paving way for the entrepreneurs that if they offer high returns to market, investors will remain inclined to invest therein. • The secondary market enhances the marketability of securities and thereby provides liquidity to investments. • From the investor's point of view, this market imparts liquidity to the long-term securities held by them by providing an auction market for these securities. • It operates through the medium of stock exchanges which regulate the trading activities in this market and ensures a measure of safety and fair dealings to the investors.
13	**Explain the features of stock exchange.**
Ans	**1) Association of persons:** A stock exchange is an association of persons or body of individuals which may be registered or unregistered. **2) Recognition from central government:** Stock exchange is an organized market. It requires recognition from the Central Government. **3) Market for securities:** Stock exchange is a market, where securities of corporate bodies, government and semi-government bodies are bought and sold. **4) Deals in second hand securities:** It deals with shares, debenture, bonds and such securities already issued by the companies. In short it deals with existing or second hand securities and hence it is called secondary market. **5) Regulates trade in securities:** Stock exchange does not buy or sell any securities on its own account. It merely provides the necessary infrastructure and facilities to its members and brokers who trade in securities. It regulates the trade activities so as to ensure free and fair trade. **6) Allow dealings only in listed securities:** In fact, stock exchanges maintain an official list of securities that could be purchased and sold on its floor. Securities which do not figure in the official list of stock exchange are called unlisted securities. Such unlisted securities cannot be traded in the stock exchange. **7) Transactions effected only through members:** All the transactions in securities at the stock exchange are effected only through its authorized brokers and members. Outsiders or direct investors are not allowed to enter in the trading circles of the stock exchange. Investors have to buy or sell the securities at the stock exchange through the authorized brokers only. **8) Working as per rules:** Buying and selling transactions in securities at the stock exchange are governed by the rules and regulations of stock exchange as well as SEBI Guidelines. No deviation from the rules and guidelines is allowed in any case. **9) Specific location:** Stock exchange is a particular market place where authorized brokers come together daily (i.e. on working days) on the floor of market called trading circles and conduct trading activities. The price of different securities traded are shown on electronic boards. After the working hours market is closed. All the working of stock exchange is conducted and controlled through computers and electronic system. **10) Financial barometers:** Stock exchanges are the financial barometers and development indicators of national economy of the country. Industrial growth and stability is reflected in the index of stock exchange.

14	**Explain the functions of stock exchange.**
Ans	Stock exchange performs a number of functions in respect of marketability of different types of securities for investors and borrowing companies. It is important functions are:

	a) Continuous and ready market for securities Stock exchange provides a central market for purchase and sale of securities. It provides ready and continuous outlet for buying and selling of securities. Buyers and sellers strongly believe that they would be able to buy and sell securities as and when they want. **b) Facilitates evaluation of securities** Stock exchange is useful for the evaluation of industrial securities. It publishes price quotation of the shares of the companies that have been listed with them after thorough analysis of demand and supply position. This enables investors to know the true worth of their holdings at any time. **c) Checks on brokers** Stock exchanges control the activities of brokers and protect the investors from being deceived. Now, if any broker is found indulging in malpractices as overcharging or giving wrong information, his/her licence may be cancelled. **d) Provides safety and security in dealings** Activities of the stock exchange are controlled by the provisions of the Securities Control (Regulation) Act and all this creates confidence in the minds of investors. As transactions are conducted as per well defined rules and regulations, fraudulent practices stands checked effectively ensuring safety, security and justice in dealings. **e) Regulates company management** Listed companies have to comply with rules and regulations of concerned stock exchange and work under the vigilance of stock exchange authorities. **f) Intensifying capital formation** Stock exchange accelerates the process of capital formation through creating the habit of saving, investing and risk taking among the investing class by converting their savings into profitable, safe investments. **g) Facilitates raising of new capital** Because of stock exchange, for either development, organisation or expansion, the need for more capital by the existing companies is easily met out. **h) Facilitates public borrowing** Stock exchange serves as a platform for marketing government securities. It enables government to raise public debt easily and quickly. **i) Facilitates healthy speculation** Healthy speculation, keeps the exchange active. Normal speculation is not dangerous but provides more business to the exchange. However, excessive speculation is undesirable as it is dangerous to investors & the growth of corporate sector. **j) Serves as economic barometer** Stock exchange indicates the state of health of companies and the national economy. It acts as a barometer of the economic situation/conditions and is thus referred as pulse of economy or economic mirror. **k) Facilitates bank lending** Banks easily know the prices of quoted securities. They offer loans to customers against corporate securities. This gives convenience to the owners of securities.
15	**In the view point of investors explain the importance of a stock exchange**

Ans	Stock exchange indicates about the good or bad health of an economy. It is an investment intermediary which facilities economic and industrial development of a country. For the smooth and orderly functioning of corporate sector in a free market economy, stock exchange are indispensable, because of the different roles played by them for different groups. From the viewpoint of investors **(a) Dissemination of useful information:** Stock exchange publishes useful information regarding price lists, quotations, etc., of securities through newspapers and journals. The interested persons buy and sell their securities on the basis of information provided by the stock exchanges. **(b) Ready market:** Persons desirous of converting their shares into cash may easily do so through a member of stock exchange. **(c) Investors' interests protected:** Stock exchanges formulate rules and regulations so that members may not exploit the investors. **(d) Genuine guidance about the securities listed:** The investors can safely depend upon the information provided by the stock exchanges. **(e) Barriers of distance removed:** Stock exchange removes the barriers of distance with regard to securities listed there. Without stock exchange the securities of a Delhi company may have a limited market in Delhi only. **(f) Knowledge of profit or loss on investments:** The investors can estimate the profit or loss on the total amount of investments in securities, by comparing the original amount invested and the price of securities on a particular day.

16	**In the view point of entrepreneurs /companies explain the importance of a stock exchange**
Ans	From the viewpoint of entrepreneurs /companies **(a) Recognition:** The market values of companies' shares are published in important dailies. This enhances the reputation of good companies/entrepreneurs. **(b) Wide market:** The securities of some companies are listed in some stock exchanges. The market for the securities of such companies is considerably widened. Thus, larger amounts of capital may be raised from different types of investors. **(c) Higher share values:** People have a tendency to buy shares that have some premium value. Demand of such shares increases. This leads to further increase in the price of such shares.
17	**In the view point of society explain the importance of a stock exchange**
Ans	From the viewpoint of society **(a) Rapid capital formation:** People get tempted to invest in securities when they study the trend of necessary prices of shares of good companies. This habit leads to investment of savings in corporate and government securities. The income from these securities may further be invested in buying more securities. This flow of funds leads to rapid capital formation. **(b) Economic development:** Through easy funds mobilizing, the boosted production fetches more capital, enhancing economic development. **(c) National projects:** As stock exchange promotes, the capital formation rate the projects which brings National Prosperity can be easily undertaken.
18	**Explain the organisation and management structure of stock exchange**

Ans	• The organisation, management, membership and functioning of stock exchanges in India are governed by the provisions of The Securities Contracts (Regulation) Act, 1956. • This Act permits only recognized stock exchanges to function under the rules, regulations and by-laws approved by the Central Government.
19	**What are the functions of the governing body of stock exchange?**
Ans	The governing body is responsible for policy formulation and proper functioning of the exchange, having wide range of powers viz..... 1) Elect the office bearers and set up committees. 2) Admit and expel members 3) Manage the properties and finance of the exchange 4) Interpret rules, regulations and by-laws 5) Adjudicate disputes 6) Conduct the affairs of the exchange.
20	**Explain the history of Securities and exchange board of India (SEBI).**
Ans	• SEBI was officially established by The Government of India in the year 1988 and given statutory powers in 1992 with SEBI Act 1992 being passed by the Indian Parliament. • SEBI has it's Headquarter at the business district of Bandra Kurla Complex in Mumbai, and has Northern, Eastern, Southern and Western Regional Offices in New Delhi, Kolkata, Chennai and Ahmedabad respectively. • Initially SEBI was a non–statutory body without any statutory power. • However in the year of 1995, SEBI was given additional statutory powers by the Government of India through an amendment to the Securities and Exchange Board of India Act, 1992. • In April, 1998 the SEBI was constituted as the regulator of capital markets in India under a resolution of the Government of India.
21	**When and how was SEBI established?**
Ans	SEBI was established as a supervising and regulatory body to curb certain malpractices and to promote the securities markets in India.

	SEBI is managed by its members, which consists of following: a) Chairman who is nominated by Union Government of India. b) Two members, i.e. Officers from Union Finance Ministry. c) One member from The Reserve Bank of India. d) The remaining 5 members are nominated by Union Government of India, out of them at least 3 shall be whole-time members. • SEBI has three functions rolled into one body: quasi-legislative, quasi-judicial and quasiexecutive. • It drafts regulations in its legislative capacity, it conducts investigation and enforcement action in its executive function and it passes rulings and orders in its judicial capacity. • Though this makes it very powerful, there is an appeal process to create accountability. • There is a Securities Appellate Tribunal which is three-member tribunal. • A second appeal lies directly to the Supreme Court.

22	**Explain the Powers of SEBI.**
Ans	For the discharge of its functions efficiently, SEBI has been vested with the following powers: 1. To approve by-laws of stock exchanges, SEBI 2. To enquire the stock exchange to amend their by-laws. 3. Inspect the books of accounts and call for periodical returns from recognized stock exchanges. 4. Inspect the books of accounts of financial intermediaries. 5. Compel certain companies to list their shares in one or more stocks exchanges. 6. Levy fees and other charges on the intermediaries for performing its functions. 7. Grant license to any person for the purpose of dealing in certain areas. 8. Delegate powers exercisable by it. 9. Prosecute and judge directly the violation of certain provisions of the Companies Act. 10. Power to impose monetary penalties.
23	**Who are angel investors?**
Ans	• An angel investor provides initial seed money for startup businesses, usually in exchange for ownership equity in the company. • The angel investor may be involved in a series of projects on a purely professional basis or may be found among an entrepreneur's family and friends. • The investor's involvement may be a one-time infusion of seed money or an ongoing injection of cash to get a product to market. • Angel investors aren't usually in the loan business. • They're putting money into an idea they like, with the expectation of a reward only if and when the business takes off.
24	**Explain the features of angel investors.**
Ans	• The job of an angel investor is invaluable. • They fill the gap in start-up or early-stage financing between "friends and family", by providing seed funding and formal venture capital. • Humorously, they were once given the acronym FFF – i.e. FRIENDS, FAMILY AND FOOLS. • Although it is usually difficult to raise more than a few thousands from friends and family, even the venture capitalist are least interested to make investments. • Thus, angel investments is a common second round of financing for high-growth start-ups or early stage companies. 1) Most angel investors are current or retired executives, business owners or high net worth individuals who have the knowledge, expertise, and funds that help start-ups match up to industry standards.
	2) As angel investors bear extremely high risk and are usually subject to dilution from future investment rounds. They expect a very high return on investment. 3) Apart from investing funds, most angels provide proactive advice, guidance, industry connections and mentoring start-ups in its early days. 4) Their objective is to create great companies by providing value creation, and simultaneously helping investors realize a high return on investments. 5) They have a sharp inclination to keep abreast of current developments in a particular business arena, mentoring another generation of entrepreneurs by making use of their vast experience.

25	**Explain venture capital**
Ans	• Venture capital is a type of private equity capital provided as seed funding to early-stage, high-potential, high risk, growth up companies/entrepreneurs who lack the necessary experience and funds to give shape to their ideas. • venture capital is an equity-based investment in a growth-oriented small to medium business to enable the investors to accomplish objectives, in return for minority shareholding in the business or the irrevocable right to acquire. • It is more accurate to view venture capital broadly as a professionally managed pool of equity capital. Venture capital is a way in which investors support entrepreneurial talent with finance and business skills to exploit market opportunities and obtain long-term capital gains. • As an industry, Venture Capital has originated in the United States, and American firms have traditionally been the largest participants in venture deals. • Venture capital has been used as a tool for economic development in a variety of developing regions. • In many of these regions, with less developed financial sectors, venture capital plays a role in facilitating access to finance for small and medium enterprises (SMEs), which in most cases would not quality for receiving bank loans.
26	**Explain the features of venture – capital.**
Ans	Venture capital can best be characterized as a long-term investment discipline, usually occurring over a five-year period that helps in the creation of: a) early-stage companies, b) the expansion and revitalization of existing businesses, and c) the financing of leveraged buyouts of existing divisions of major or privately owned enterprises. Thus, venture capital finance has the following features: 1) It is basically equity finance in relatively new companies. 2) It is long-term investment in growth-oriented small or medium firms. 3) Venture capitalist not only provide capital but also business skills to investee firms. 4) It involves high risk-return spectrum. 5) It is a subset of private equity. 6) The venture capital institutions have a continuous involvement in the business after making the investment. 7) Such institutions disinvest the holdings either to the promoters or in the market.
27	**Why is it difficult to raise fund from venture capitalist?**
Ans	Venture capitalists are typically very selective in deciding what to invest in and as a rule of thumb: 1) They may invest in one in four hundred opportunities presented to it, 2) Looks for the extremely rare, yet sought after qualities, such as : a) innovative technology, b) potential for rapid growth, c) a well-developed business model d) an impressive management team.

	3) Looks for an "exit" in the time frame of typically 3-7 years. 4) Is inclined towards ventures with exceptionally high growth potential. Thus, entrepreneurs are expected to carry out detailed due diligence prior to seeking venture capital as a source of financing. As venture capitalists' investments are illiquid, requiring extended time frame to harvest, an entrepreneur should carefully evaluate and analyse, the stage which he/she would require venture capitalist to assist in.
28	**When should one need to seek venture capital finance?**
Ans	Entrepreneurs can typically seek venture capital to assist at any of the following four stages in the company's development. 1) Early stage financing This stage includes: (a) Seed capital (b) Pre-start up and start up (c) Second-round financing. 2) Last stage financing /bridge /pre-public stage
29	**Explain Seed capital finance.**
Ans	• It refers to the capital required by an entrepreneur for conducting research at precommercialization stage. • During this stage, the entrepreneur has to convince the investor (VC) why his idea/product is worthwhile. The investor will investigate into the technical and the economical feasibility of the idea. • In some cases, there is some sort of prototype of the idea/product that is not fully developed or tested. • As the risk element at this stage is very high, investor (VC) may deny to assist if he does not see any potential in the idea. • Entrepreneur's ability, technological skills and competencies are required to match with the market opportunities so as to successfully convince about product/idea's feasibility to the venture capitalist.
30	**Explain Start up finance stage.**
Ans	• If the idea/product/process is qualified for further investigation and/or investment, the process will go to the second stage; this is also called the start-up stage. • A business plan is presented by the entrepreneur to the VC firm. • A management team is being formed to run the venture. • If the company has a board of directors, a person from the VC firms will take seats at the board of directors. • While the organisation is being set up, the idea/product gets its form. • The prototype is being developed and fully tested. • In some cases, clients are being attracted for initial sales. • The management-team establishes a feasible production line to produce the product. • The VC firm monitors the feasibility of the product and the capability of the managementteam from the board of directors.
31	**Explain Second-round financing.**

Ans	• At this stage, we presume that the idea has been transformed into a product and is being produced and sold. • This is the first encounter with the rest of the market, the competitors and attempt is to squeeze in the market and get some market share from the competitors. • The entrepreneur, at this stage, needs assistance from the Venture Capitalist for expansion, modernization, diversification so that the economies of scale and stability could be attained.
	• As this time, larger funds than the other early-stage financing are required, entrepreneur should be extra careful because only if he and his management team is able to prove their capability of standing against the competition, only then is the VC firm interested in financing.
32	**Explain Last stage financing /bridge /pre-public stage.**
Ans	In general, this is the last stage of the venture capital financing process. The main goal of this stage is for the venture to go public so that investors can exit the venture with a profit commensurate with the risk they have taken. At this stage, the venture achieves a certain amount of market share. This gives the venture some opportunities for example: • Merger with other companies • Keeping new competitors away from the market • Eliminate competitors • Development capital The entrepreneur must examine the product's market position and, if possible, reposition it to attract new Market segmentation. He/she should introduce the follow-up product/ services to attract new client and markets, for only that is the way to create interest for VC firms seeks to get their assistance further.

SUMMARY

- The role of transforming financial resources from the surplus units to the deficit units is referred as ‘financial intermediation
- The place where the demand for and the supply of short term funds meet is called as money market
- A capital market may be defined as an organized mechanism meant for effective and smooth transfer of money capital or financial resources from the inventory to the entrepreneur.
- Financial markets can be for initial issue and further issue
- Entrepreneurship may find it difficult to go for equity financing since the goodwill is not yet built up in the market
- Compliance with the SEBI guidelines is to be done for the investor protection
- Stock exchange is an investment intermediary & facilitate eco & industrial development of a country
- Stock exchange performs a number of functions in respect of marketability of different types of securities for investors and borrowing companies
- Securities and Exchange Board of India (SEBI) was established as a supervising and regulatory body to curb certain malpractices and to promote the securities markets in India

- Angel investors: They fill the gap in start up between family and friends and venture capitalists.
- Venture capital is a type of private equity capital provided as seed funding to early stage, high potential, high risk, growth up companies/entrepreneurs who lack the necessary experience and funds to give shape to their ideas.

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