Primary Market

In a primary market, securities are created for the first time for investors to purchase. New securities are issued in this market through a stock exchange, enabling the government as well as companies to raise capital

For a transaction taking place in this market, there are three entities involved. It would include a company, investors, and an underwriter. A company issues security in a primary market as an initial public offering (IPO), and the sale price of such new issue is determined by a concerned underwriter, which may or may not be a financial institution. An underwriter also facilitates and monitors the new issue offering. Investors purchase the newly issued securities in the primary market. Such a market is regulated by the Securities and Exchange Board of India (SEBI).The entity which issues securities may be looking to expand its operations, fund other business targets or increase its physical presence among others. Primary market example of securities issued includes notes, bills, government bonds or corporate bonds as well as stocks of companies.

Features of New Issue Market

1. It is the market for new long term capital.

2. The securities are issued by company for the first time directly to the investors.

3. On receiving the money from new issues, the comany will issue the securitycertificates to the investors.

4. The amount obtained by the company after the new issues are utilized forexpansion of the present business or for setting up new ventures.

5. External finance for long term such as loan from financial institutions is notincluded in new issue market. There is an option called "going public" in whichthe borrowers in new issue market raise capital for converting private capitalinto public capital.

6. The financial assests sold can be redeemed by the orginial holder of security.

Fuctions

New issue offer

The primary market organises offer of a new issue which had not been traded on any other exchange earlier. Due to this reason, it is also called a New Issue Market. Organising new issue offers involves a detailed assessment of project viability, among other factors. The financial arrangements for the purpose include considerations of promoters' equity, liquidity ratio, debt-equity ratio and requirement of foreign exchange.

Underwriting services

Underwriting is an essential aspect while offering a new issue. An underwriter's role in a primary marketplace includes purchasing unsold shares if it cannot manage to sell the required number of shares to the public. A financial institution may act as an underwriter, earning a commission on underwriting.Investors rely on underwriters for determining whether undertaking the risk would be worth its returns. It may so thus happen that an underwriter ends up buying all the IPO issue, and subsequently selling it to investors.

Distribution of new issue

A new issue is also distributed in a primary marketing sphere. Such distribution is initiated with a new prospectus issue. It invites the public at large to buy a new issue and provides detailed information on the company, issue, and involved underwriters.

Types of Primary Market Issuance

After the issuance of securities, investors can purchase such securities in various ways. There are 5 types of primary market issues.

Public issue

Public issue is the most common method of issuing securities of a company to the public at large. It is mainly done via Initial Public Offering (IPO) resulting in companies raising funds from the capital market. These securities are listed in the stock exchanges for trading.. Such public offer allows a company to raise funds for expansion of business, improving infrastructure, and repay its debts, among others. Trading in an open market also increases a company's liquidity and provides a scope for issuance of more shares in A privately held company

converts into a publicly-traded company when its shares are offered to the public initially raising further capital for business.The Securities and Exchange Board of India is the regulatory body that monitors IPO. As per its guidelines, a requisite due enquiry is conducted for a company's authenticity, and the company is required to mention its necessary details in the prospectus for a public issue.

Private placement

When a company offers its securities to a small group of investors, it is called private placement. Such securities may be bonds, stocks or other securities, and the investors can be both individual and institutional.

Private placements are easier to issue than initial public offerings as the regulatory stipulations are significantly less. It also incurs reduced cost and time, and the company can remain private. Such issuance is suitable for start-ups or companies which are in their early stages. The company may place this issuance to an investment bank or a hedge fund or place before ultra-high net worth individuals (HNIs) to raise capital.

Preferential issue

A preferential issue is one of the quickest methods available to companies for raising capital. Both listed and unlisted companies can issue shares or convertible securities to a select group of investors. However, the preferential issue is neither a public issue nor a rights issue. The shareholders in possession of preference shares stand to receive the dividend before the ordinary shareholders are paid.

Qualified institutional placement

Qualified institutional placement is another kind of private placement where a listed company issues securities in the form of equity shares or partly or wholly convertible debentures apart from such warrants convertible to equity shares and purchased by a Qualified Institutional Buyer (QIB).

QIBs are primarily such investors who have the requisite financial knowledge and expertise to invest in the capital market. Some QIBs are –

Foreign Institutional Investors registered with the Securities and Exchange Board of India.

Foreign Venture Capital Investors.

Alternate Investment Funds.

Mutual Funds.

Public Financial Institutions.

Insurers.

Scheduled Commercial Banks.

Pension Funds.

Issuance of qualified institutional placement is simpler than preferential allotment as the former does not attract standard procedural regulations like submitting pre-issue filings to SEBI. The process thus becomes much easier and less time-consuming.

Rights and bonus issues

Another issuance in the primary market is rights and bonus issue, in which the company issues securities to existing investors by offering them to purchase more securities at a predetermined price (in case of rights issue) or avail allotment of additional free shares (in case of bonus issue).

For rights issues, investors retain the choice of buying stocks at discounted prices within a stipulated period. Rights issue enhances control of existing shareholders of the company, and also there are no costs involved in the issuance of these kinds of shares. For bonus issues, stocks are issued by a company as a gift to its existing shareholders. However, the issuance of bonus shares does not infuse fresh capital.

bankers who may be Advantages of Primary Market

Companies can raise capital at relatively low cost, and the securities so issued in the primary market provide high liquidity as the same can be sold in the secondary market almost immediately.

The primary market is an important source for mobilisation of savings in an economy. Funds are mobilised from commoners for investing in other channels. It leads to monetary resources being put into investment options.

Chances of price manipulation in the primary market are considerably less when compared to the secondary market. Such manipulation usually occurs by deflating or inflating a security price, thereby deliberately interfering with fair and free operations of the market.

The primary market acts as a potential avenue for diversification to cut down on risk. It enables an investor to allocate his/her investment across different categories involving multiple financial instruments and industries.

It is not subject to any market fluctuations. The prices of stocks are determined before an initial public offering, and investors know the actual amount they will have to invest. Advantages of New Issue/ Primary Market

1. Mobilisation of savings.

2. Chanelizing savings for productive use.

3. Source of large supply of funds.

4. Rapid industrial growth.

Disadvantages of Primary Market

1. Possibility of deceiving investors.

2. No fixed norms for project appraisal.

3. Ineffective role of merchant bankers. rs may not receive share allocation.

There may be limited information for an investor to access before investment in an IPO since unlisted companies do not fall under the purview of regulatory and disclosure requirements of the Securities and Exchange Board of India.

Each stock is exposed to varying degrees of risk, but there is no historical trading data in a primary market for analysing IPO shares because the company is offering its shares to the public for the first time through an initial public offering.

In some cases, it may not be favourable for small investors. If a share is oversubscribed, small investors

.

Role of New Issue/ Primary Market

? Capital Formation: It provides attractive issue to the potential investors and with this company can raise capital at lower costs.

? Liquidity: As the securities issued in primary market can be immediately soldin secondary market. The rate of liquidity of securities is higher.

? Diversification of Risk: Many financial intermediaries invest in primarymarket, as ther e is less risk of failure in investment as the company does notdepend on a single investor.it reduces the overall risk.

- **Reduction in Cost: Prospectus containing all details about given to the investors.**

SEBI Guidelines for Issue of Securities

The guidelines were first issued on 11th June 1992 and were amended subsequently

from time to time. SEBI has now issued consolidated guidelines as SEBI (Disclosure

and investor protection) Guidelines, 2000 vide its circular No . 1 dated 19-01-2000.

These guidelines shall be applicabe to all public issues by listed and unlisted

companies all offers for sale and rights issues by listed companies whose equity share

capitalis listed, except in case of rights issues where the aggregate value of securities

offered does not exceed 50 lacs. Broadly there are three methods for issuing securities

to the public.

1. Conventional mode of receiving applications through bankers.

2. Book buildng.

3. On line system of stock exchange (e-IPO).

Primary Market Intermediaries

The major intermediaries of the primary securities market include:

? Merchant Bankers/ Lead Managers : Merchant bank is an institutiton or an organisation which provides a number of services including management of securities issues, portfolio management services, underwriting of capital issues, insurance, credit syndication, financial advices and project counselling etc. They mainly offer financial services for a fee.

? Underwriters: Underwriting is an act of undertaking the guarantee by an underwriter of buying the shares or debentures placed before the public in the event of non-subscribution. According to SEBI Rules 1993, underwriting mean agreement with or without conditions to subscribe to the securities of a body corporate when the existing shareholders of such body corporate or the public do not subscribe to the securities offered to them. "underwriter" means a person who engages in the business of underwriting of an issue of securities of a body corporate.

? Bankers to an Issue: Bankers to an issue is an important intermediary who accepts applications and application monies, collects all monies, refund application monies after allotment and participates in the payment of dividend sby companies. No person can act as a banker to an issue without obtaining a certificate of registration from SEBI. Registration is granted by SEBI after it is satisfied that the applicant possesses the necessary infrastructure ,communication and data processing facilities and requisite manpower to discharge its duties effectively.

? Registrars to an Issue & Share Transfer Agent : The Registrar to an issue is

an intermediary who performs the functions of:

1. Collecting applications from investors.

2. Keeping a record of applications.

3. Keeping a record of money received from investors or paid to sellers of

shares.

4. Assisting the companies in the determination of basis of allotment of

shares.

5. Helping in despatch of allotment letter refund orders, share certificates

etc..

? Debenture trustees : The Regulations define a debenture trustee as a trustee of a trust deed for securing any issue of debentures of a body corporate. Trust deed means a deed executed by the company in favour of trustees named

there in for the benefit of the debentureholders. Only the folowing categories of persons are eligible to act as debenture trustees.

1. A scheduled bank carrying on commercial activity. Or

2. A public financial institution within the meaning of section 4A of the companies Acts. Or

3. An insurance company. Or

4. A body corporate.

The debebture trustee performs following duties:

1. Call for periodic reports from the body corporate.

2. Carry out inspection of books of accounts/ records/documents and registers and trust property.

3. Take possession of property as per provisions of the deed.

4. Enforce security in the interest of debenture holders.

5. Resolve grievences of debenture holders with respect to receipt of certificates, interest and other dues.

6. Exercise due diligence to ensure that the property secured is sufficient to pay the dues.

7. Ensures that provisions of the relevant laws are adhered to by the body corporate.

8. Carryout such as may be necessary for the protection of interest of debenture holders.

Brokers to an issue: The person who procure subscriptions to issue from prospective investors spread over large area. A company can appoint as many number of brokers as it wants. Members are prohibited from acting as managersor brokers to issue by SEBI regulations.

Regulatory measures of SEBI for Primary Market reforms in India Primary Market Reforms in India – SEBI Guidelines

SEBI has introduced various guidelines as regulatory measures for capital issues. They are as below:

1. Disclosure of All Material Facts is made Compulsory: SEBI has made it compulsory for companies do disclose all the facts and risk factors regarding the projects undertaken by the company. The basis on which the premium amount is calculated should also be disclosed by the company as per SEBI norms. SEBI also advises the code of ethics for advertising in media regarding the public issue.

2. Encouragement to Initial Public 0ffers: In order to encourage Initial Public Offers (IPO) in the primary market, SEBI has permitted companies to determine the par value of shares issued by them. SEBI has allowed issues of IPOs to go for "Book Building" – i.e. reserve and allot shares to individual investors. But the issuer will have to disclose the price, the issue size and the number of securities to be offered to the public.

3. Increase of Popularity to Private Placement Market: In recent years, private placement market has become popular with issuers because of stringent entry and disclosure norms for public issues. Besides low cost of issuance, ease of structuring investments and saving of time lag in issuance are the other causes responsible for the rapid growth of private placement market.

4. Underwriting has made Optional: To reduce the cost of issue in primary market, SEBI has made underwriting of issue optional. However, the condition that if an issue was not underwritten and was not able to collect 90% of the amount offered to the public, the entire amount collected would be refunded to the investor is still in force.

5. Issue of Due Diligence Certificate: The lead managers have to issue due diligence certificate, which has now been made part of the offer document.

6. Conditions regarding Application Size etc.: SEBI has raised the minimum application size and also the proportion of each issue allowed for firm allotment to institutions such as mutual funds.

7. Regulation of Merchant Banking: SEBI has brought Merchant banking under its regulatory framework. The merchant bankers are now to be authorized by SEBI. Merchant bankers, now have a greater degree of accountability in the offer document and issue process.

8. Imposition of Compulsory Deposit on Companies making Public Issues: In order to induce companies to exercise greater care and diligence for timely

action in matters relating to the public issues of capital, SEBI has advised stock exchanges to collect from companies making public issues, a deposit of one per cent of the issue amount which could be forfeited in case of non-compliance of the provisions of the listing agreement and, non-dispatch of refund orders and share certificates by registered post within the prescribed time.

9. Reforms as to Mutual Funds: The Government has now permitted the setting up of private mutual funds and a few have already been set up. UTI has now been brought under the regulatory jurisdiction of SEBI. All mutual funds are allowed to apply for firm allotments in public issues. To improve the scope of investments by mutual funds, the latter are permitted to underwrite public issues. Further, SEBI has relaxed the guidelines for investment in money market instruments. Finally, SEBI has issued fresh guidelines for advertising by mutual funds.

10. Vetting of Offer Document: SEBI vets offer documents to make sure that the company listing the shares has made all disclosures in it. All the guidelines and regulatory measures of capital issues are meant to promote healthy and efficient functioning of the issue market (or the primary market).