UNIVERSITY OF CALICUT
SCHOOL OF DISTANCE EDUCATION

STUDY MATERIAL

Core Course

BBA *(Specialization - Finance)*

VI Semester

**INDIAN FINANCIAL SYSTEM**

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MODULE I

INDIAN FINANCIAL SYSTEM

Introduction

The term "finance" in our simple understanding, is perceived as equivalent to 'Money'. But finance exactly is not money; it is the source of providing fund for a particular activity. Finance is a facility that built the Gap between deficit sectors to surplus sector by shifting funds.

Finance as a function is defined by the dictionary as under:
1: "To provide or raise the fund or capital"
2: "To supply fund ."
3: "To furnish credit ."

Financial System

Every country aiming at its progress depends on the efficiency of this economic system which depends upon financial system. The economic development of a nation is reflected by the progress of the various economic units. These units are broadly classified into corporate sector, government and household sector. While performing their activities these units will be placed in a surplus/deficit/balanced budgetary situations.

There are organisations or people with surplus funds and there are those with a deficit. A financial system or financial sector functions as an intermediary and facilitates the flow of funds from the areas of surplus to the areas of deficit. A Financial System is a composition of various institutions, markets, regulations and laws, practices, money manager, analysts, transactions and claims and liabilities. The financial system is the network of institutions and individuals who deal in financial claims to various instruments. Financial System of any country consists of financial markets, financial intermediation and financial instruments or financial products.

Definition of Financial System

“It is a set of institutions instruments and markets which fosters saving and channels them to their most efficient use”.-(H.R. Machiraju)

In the worlds of Van Horne, “financial system allocates savings efficiently in an economy to ultimate users either for investment in real assets or for consumption”.

According to Prasanna Chandra, “financial system consists of a variety of institutions, markets and instruments related in a systematic manner and provides the principal means by which savings are transformed into investments”.

Structure of Indian Financial System

1) Financial Market: -

It is a system through which funds are transferred from surplus sector to the deficit sector. On the basis of the duration of financial Assets and nature of product money market can be classified into 3 types:

a) Money Market: -

It is the institutional arrangement of borrowing and lending into 2 sectors i.e. organised sector headed by RBI and unorganized sector no way related with RBI. Further depending upon the type of instrument used money is divided into various sub market
b) Capital Market: -

It deals with long term lending's and borrowings. It is a market for long term instruments such as shares, debentures and bonds. It also deals with term loans. This market is also dividend into 2 types:-

A) Primary or New Issue Market

B) Secondary Market of Stock exchange.

c) Foreign Exchange market: -It deals with foreign exchange. It is a market where the exchanging of currencies will takes place. It is the market where currencies of different country are purchased and sold. Depending on the exchange rate that is applicable, the transfer of funds takes place in this market. This is one of the most developed and integrated market across the globe.

d) Credit Market- Credit market is a place where banks, FIs and NBFCs purvey short, medium and long-term loans to corporate and individuals.

ii) Financial Institution: -

It is classified into categories:-

a. Banking Institution:-

It includes commercial banks, private bank and foreign banks are operating in India. There are 27 Commercial Banks of Public Sector further, we have Development Banks (ICICI, IDBI), Agriculture Bank (RRB, Cooperative Banks, NABARD).

b. Non-Banking Institution: -

These are established to mobilise saving idifferent modes. These institutions do not offer banking services such as accepting deposit and Lending Loans. For example LIC, UTI, GIC.

Financial institutions are financial intermediaries. They intermediate between savers and investors. They lend money. They also mobilise savings. The various financial intermediaries, their performing areas and respective roles are given in following table:
Intermediary | Market | Role
--- | --- | ---
Stock Exchange | Capital Market | Provide Secondary Market to securities
Investment Bankers | Capital Market, Credit Market | Corporate advisory services, Issue of securities
Underwriters | Capital Market, Money Market | Subscribe to unsubscribed portion of securities
Registrars, Depositories, Custodians | Capital Market | Issue securities to the investors on behalf of the company and handle share transfer activity
Primary Dealers Satellite Dealers | Money Market | Market making in government securities
Forex Dealers | Forex Market | Ensure exchange in currencies

iii) Financial Instruments:

It includes through these instruments financial Institution mobilise saving. These are of 2 type’s i.e.

a) Long Term:

Shares, Debenture, Mutual Funds, Term Loans.

b) Short Term:

Call Loan (money market), Promissory Notes, Bills of exchange etc.

iv) Financial Services:

a) Banking service provided by Commercial banks and Development banks. Accepting Deposits and lending loans.

b) Non-Banking Services:

These services are provided by Non-Banking Companies such as LIC and GIC. They accept saving in different modes and mobiles to various channels of investments.

c) Other Services:

In modern days banks are providing various new services such as ATM, Credit Cards, Debit Cards, Electronic Transfer of Funds (ETF), Internet Banking, E-Banking, off shore Banking.
Functions/important and role of financial system

1. It links the savers and investors. It helps in mobilizing and allocating the savings efficiently and effectively. It plays a crucial role in economic development through saving-investment process. This savings – investment process is called capital formation.

2. It helps to monitor corporate performance.

3. It provides a mechanism for managing uncertainty and controlling risk.

4. It provides a mechanism for the transfer of resources across geographical boundaries.

5. It offers portfolio adjustment facilities (provided by financial markets and financial intermediaries).

6. It helps in lowering the transaction costs and increase returns. This will motivate people to save more.

7. It promotes the process of capital formation.

8. It helps in promoting the process of financial deepening and broadening. Financial deepening means increasing financial assets as a percentage of GDP and financial broadening means building an increasing number and variety of participants and instruments.

In short, a financial system contributes to the acceleration of economic development. It contributes to growth through technical progress.

Growth and Development of Indian Financial System

At the time of independence in 1947, there was no strong financial institutional mechanism in the country. The industrial sector had no access to the savings of the community. The capital market was primitive and shy. The private and unorganised sector played an important role in the provision of liquidity. On the whole, there were chaos and confusions in the financial system.

After independence, the government adopted mixed economic system. A scheme of planned economic development was evolved in 1951 with a view to achieve the broad economic and social objective. The government started creating new financial institutions to supply finance both for agricultural and industrial development. It also progressively started nationalizing some important financial institutions so that the flow of finance might be in the right direction. The following developments took place in the Indian financial system:

1. Nationalisation of financial institutions:

2. Establishment of Development Banks:
4. Establishment of institution for housing finance:

5. Establishment of Stock Holding Corporation of India (SHCIL):

6. Establishment of mutual funds and venture capital institutions:


**Weaknesses of Indian Financial System**

Even though Indian financial system is more developed today, it suffers from certain weaknesses. These may be briefly stated below:

1. **Lack of co-ordination among financial institutions:** There are a large number of financial intermediaries. Most of the financial institutions are owned by the government. At the same time, the government is also the controlling authority of these institutions. As there is multiplicity of institutions in the Indian financial system, there is lack of co-ordination in the working of these institutions.

2. **Dominance of development banks in industrial finance:** The industrial financing in India today is largely through the financial institutions set up by the government. They get most of their funds from their sponsors. They act as distributive agencies only. Hence, they fail to mobilise the savings of the public. This stands in the way of growth of an efficient financial system in the country.

3. **Inactive and erratic capital market:** In India, the corporate customers are able to raise finance through development banks. So, they need not go to capital market. Moreover, they do not resort to capital market because it is erratic and enactive. Investors too prefer investments in physical assets to investments in financial assets.

4. **Unhealthy financial practices:** The dominance of development banks has developed unhealthy financial practices among corporate customers. The development banks provide most of the funds in the form of term loans. So there is a predominance of debt in the financial structure of corporate enterprises. This predominance of debt capital has made the capital structure of the borrowing enterprises uneven and lopsided. When these enterprises face financial crisis, the financial institutions permit a greater use of debt than is warranted. This will make matters worse.

5. **Monopolistic market structures:** In India some financial institutions are so large that they have created a monopolistic market structures in the financial system. For instance, the entire life insurance business is in the hands of LIC. The weakness of this large structure is that it could lead to inefficiency in their working or mismanagement. Ultimately, it would retard the development of the financial system of the country itself.
6. **Other factors:** Apart from the above, there are some other factors which put obstacles to the growth of Indian financial system. Examples are:

   a. Banks and Financial Institutions have high level of NPA.
   b. Government burdened with high level of domestic debt.
   c. Cooperative banks are labelled with scams.
   d. Investors confidence reduced in the public sector undertaking etc.,
   e. Financial illiteracy.

   In the recent past, the most notable aspect of Indian economy is its financial system. Perhaps no system in the world has changed so much as that of our financial system. Indian financial system undergoing fast development and hence not matured like that of developed countries. The government should take reasonable reforms to mould our financial system as healthy one.

**MONEY MARKET**

**Meaning**

Money market is a segment of financial market. It is a market for short term funds. It deals with all transactions in short term securities. These transactions have a maturity period of one year or less. Examples are bills of exchange, treasury bills etc. These short term instruments can be converted into money at low transaction cost and without much loss. Thus, money market is a market for short term financial securities that are equal to money.

According to Crowther, “Money market is a collective name given to various firms and institutions that deal in the various grades of near money”.

Money market is not a place. It is an activity. It includes all organizations and institutions that deal in short term financial instruments. However, sometimes geographical names are given to the money market according to the location, e.g. Mumbai Money Market.

**Characteristics of Money Market**

The following are the characteristics of money market:

1) It is basically an over the phone market.
2) It is a wholesale market for short term debt instruments.
3) It is not a single market but a collection of markets for several instruments.
4) It facilitates effective implementation of monetary policy of a central bank of a country.

5) It is a market for short term financial assets that are close substitutes of money.

6) Transactions are made without the help of brokers.

7) It establishes the link between the RBI and banks.

8) The players in the money market are RBI, commercial banks, and companies.

**Functions of Money Market**

Money market performs the following functions:

1. Facilitating adjustment of liquidity position of commercial banks, business undertakings and other non-banking financial institutions.

2. Enabling the central bank to influence and regulate liquidity in the economy through its intervention in the market.

3. Providing a reasonable access to users of short term funds to meet their requirements quickly at reasonable costs.

4. Providing short term funds to govt. institutions.

5. Enabling businessmen to invest their temporary surplus funds for short period.

6. Facilitating flow of funds to the most important uses.

**Characteristics of a Developed Money Market**

In every country some types of money market exists. Some of them are highly developed while others are not well developed. A well developed and efficient money market is necessary for the development of any economy. The following are the characteristics or prerequisites of a developed and efficient money market:

1. Highly developed commercial banking system

2. Presence of an efficient central bank

3. Existence of sub markets

4. Availability of ample credit instruments

5. Existence of secondary market

6. Availability of ample resources

7. Demand and supply of funds

8. Other factors:
E.g.; a. industrial development, b. volume of international trade, c. political stability,
d. trade cycles, e. foreign investment, f. price stabilisation etc.

**Money Market Instruments**

The money market can be defined as a market for short-term money and financial assets that are near substitutes for money. The term short-term means generally a period up to one year and near substitutes to money is used to denote any financial asset which can be quickly converted into money with minimum transaction cost.

Important money market instruments are:

1. Call/Notice Money
2. Treasury Bills
3. Term Money
4. Certificate of Deposit
5. Commercial Papers
6. REPO
7. MMMF
8. ADR/GDR

1. **Call /Notice-Money Market**

   Call/Notice money is the money borrowed or lent on demand for a very short period. When money is borrowed or lent for a day, it is known as Call (Overnight) Money. Intervening holidays and/or Sunday are excluded for this purpose. Thus money, borrowed on a day and repaid on the next working day, (irrespective of the number of intervening holidays) is "Call Money".

   When money is borrowed or lent for more than a day and up to 14 days, it is "Notice Money". No collateral security is required to cover these transactions.

2. **Inter-Bank Term Money**

   Inter-bank market for deposits of maturity beyond 14 days is referred to as the term money market. The entry restrictions are the same as those for Call/Notice Money except that, as per existing regulations, the specified entities are not allowed to lend beyond 14 days.

3. **Treasury Bills.**

   Treasury Bills are short term (up to one year) borrowing instruments of the union government. It is an IOU of the Government. It is a promise by the Government
to pay a stated sum after expiry of the stated period from the date of issue (14/91/182/364 days i.e. less than one year). They are issued at a discount to the face value, and on maturity the face value is paid to the holder. The rate of discount and the corresponding issue price are determined at each auction.

Types of T-Bills

1. Ordinary or Regular T-Bills: These are issued to the public, banks and other institutions to raise money for meeting the short term financial needs of the Govt. These are freely marketable. These can be bought and sold at any time.

2. Ad hoc T-Bills: These are issued in favour of the RBI only. They are not sold through tender or auction. They are purchased by the RBI on tap. The RBI is authorised to issue currency notes against these.

On the basis of periodicity T-bills may be classified into four. They are as follows:

1. 91-Day T-Bills: The maturity of this T-bills is 91 days. They were discontinued from April 1, 1997.

2. 14-Day T-Bills: This was introduced from April 1, 1997. The maturity period is 14 days.

3. 182-Day T-Bills: These were introduced in November 1986 to provide short term investment opportunities to financial institutions and others. The maturity period of this T-bill is 182 days.

4. 364-Day T-Bills: In April 1992, the 364-day T-bills were introduced to replace 182 day T-bills. The maturity period is 364 days.

4. Certificate of Deposits

Certificates of Deposit (CDs) is a negotiable money market instrument and issued in dematerialised form or as a Usance Promissory Note, for funds deposited at a bank or other eligible financial institution for a specified time period. Guidelines for issue of CDs are presently governed by various directives issued by the Reserve Bank of India, as amended from time to time.

CDs can be issued by (i) scheduled commercial banks excluding Regional Rural Banks (RRBs) and Local Area Banks (LABs); and (ii) select all-India Financial Institutions that have been permitted by RBI to raise short-term resources within the umbrella limit fixed by RBI. Banks have the freedom to issue CDs depending on their requirements. An FI may issue CDs within the overall umbrella limit fixed by RBI, i.e., issue of CD together with other instruments viz., term money, term deposits, commercial papers and intercorporate deposits should not exceed 100 per cent of its net owned funds, as per the latest audited balance sheet.
Features of CDs

1. These are unsecured promissory notes issued by banks or financial institutions.
2. These are short term deposits of specific maturity similar to fixed deposits.
3. These are negotiable (freely transferable by endorsement and delivery)
4. These are generally risk free.
5. The rate of interest is higher than that on T-bill or time deposits
6. These are issued at discount
7. These are repayable on fixed date.
8. These require stamp duty.

5. Commercial Paper

CP is an unsecured promissory note privately placed with investors at a discount rate to face value determined by market forces. CP is freely negotiable by endorsement and delivery. A company shall be eligible to issue CP provided –

(a) The tangible net worth of the company, as per the latest audited balance sheet, is not less than Rs. 4 crore;

(b) The working capital (fund-based) limit of the company from the banking system is not less than Rs.4 crore and

(c) The borrower account of the company is classified as a Standard Asset by the financing bank/s.

(d) The minimum maturity period of CP is 7 days. The minimum credit rating shall be P-2 of CRISIL or such equivalent rating by other agencies.

(e) CPs can be issued in multiples of Rs. 5 lakhs subject to the minimum issue size of Rs. 50 lakhs

6. Repurchase Agreements (REPO)

REPO is basically a contract entered into by two parties (parties include RBI, a bank or NBFC. In this contract, a holder of Govt. securities sells the securities to a lender and agrees to repurchase them at an agreed future date at an agreed price. At the end of the period the borrower repurchases the securities at the predetermined price. The difference between the purchase price and the original price is the cost for the borrower. This cost of borrowing is called repo rate.
A transaction is called a Repo when viewed from the perspective of the seller of the securities and reverse when described from the point of view of the suppliers of funds. Thus whether a given agreement is termed Repo or Reverse Repo depends largely on which party initiated the transaction.

Thus Repo is a transaction in which a participant (borrower) acquires immediate funds by selling securities and simultaneously agrees to repurchase the same or similar securities after a specified period at a specified price. It is also called ready forward contract.

7. Money Market Mutual Funds (MMMFs)

Money Market Mutual Funds mobilise money from the general public. The money collected will be invested in money market instruments. The investors get a higher return. They are more liquid as compared to other investment alternatives.

The MMMFs were originated in the US in 1972. In India the first MMMF was set up by Kothari Pioneer in 1997. But this did not succeed.

8. American depository receipt and Global depository receipt

ADRs are instruments in the nature of depository receipt and certificate. These instruments are negotiable and represent publicly traded, local currency equity shares issued by non-American company. For example, an NRI can invest in Indian Company’s shares without bothering dollar conversion and other exchange formalities.

If the facilities extended globally, these instruments are called GDR. ADR are listed in American Stock exchanges and GDR are listed in other than American Stock exchanges, say Landon, Luxembourg, Tokyo etc.,

Components / Constituents / Composition of Money Market (Structure of Money Market)

Money market consists of a number of sub markets. All submarkets collectively constitute the money market. Each sub market deals in a particular financial instrument. The main components or constituents or sub markets of a money markets are as follows:

1. Call money market
2. Commercial bill market
3. Treasury bill markets
4. Certificates of deposits market
5. Commercial paper market
6. Acceptance market
7. Collateral loan market

(Details of the above components already explained under the sub title 'money market instruments' except the following)

**Commercial Bills and its market**

When goods are sold on credit, the seller draws a bill of exchange on the buyer for the amount due. The buyer accepts it immediately. This means he agrees to pay the amount mentioned therein after a certain specified date. After accepting the bill, the buyer returns it to the seller. This bill is called trade bill. The seller may either retain the bill till maturity or due date or get it discounted from some banker and get immediate cash. When trade bills are accepted by commercial banks, they are called commercial bills. The bank discounts this bill by deducting a certain amount (discount) and balance is paid.

A bill of exchange contains a written order from the creditor (seller) to the debtor (buyer) to pay a certain sum, to a certain person after a certain period.

According to Negotiable instruments Act, 1881, a bill of exchange is ‘an instrument in writing containing an unconditional order, signed by the maker, directing a certain person to pay a certain sum of money only to, or to the order of a certain person or to the bearer of the instrument’.

Features of Commercial Bills

1. These are negotiable instruments.
2. These are generally issued for 30 days to 120 days. Thus these are short term credit instruments.
3. These are self liquidating instruments with low risk.
4. These can be discounted with a bank. When a bill is discounted with a bank, the holder gets immediate cash. This means bank provides credit to the customers. The credit is repayable on maturity of the bill. In case of need for funds, the bank can rediscount the bill in the money market and get ready money.
5. These are used for settling payments in the domestic as well as foreign trade.
6. The creditor who draws the bill is called drawer and the debtor who accepts the bill is called drawee.
Types of Bills

Many types of bills are in circulation in a bill market. They may be broadly classified as follows:

1. Demand Bills and Time Bills: Demand bill is payable on demand. It is payable immediately on presentation or at sight to the drawing. Demand bill is also known as sight bill. Time bill is payable at a specified future date. Time bill is also known as usance bill.

2. Clean Bills and Documentary Bills: When bills have to be accompanied by documents of title to goods such as railway receipts, bill of lading etc. the bills are called documentary bills. These may be further classified into documents against payment (D/P) and documents against acceptance (D/A). In case of D/A bills, the documents accompanying bills have to be delivered to the drawee immediately after his acceptance of the bill. Thus a D/A bill becomes a clean bill immediately after acceptance. On the other hand, the documents have to be handed over to the drawee only against payment in the case of D/P bills. When bills are drawn without accompanying any document, they are called clean bills. In such a case, documents will be directly sent to the drawee.

3. Inland and Foreign Bills: Inland bills are bills drawn upon a person resident in India and are payable in India. Foreign bills are bills drawn outside India and they may be payable either in India or outside India.

4. Accommodation Bills and Supply Bills: In case of accommodation bills, two parties draw bills on each other purely for the purpose of mutual financial accommodation. These bills are then discounted with the bankers and the proceeds are shared among themselves. On the due dates, the parties make payment to the bank. Accommodation bills are also known as ‘wind bills’ or ‘kite bills’. Supply bills are those drawn by suppliers or contractors on the Govt. departments for the goods supplied to them. These bills are not considered as negotiable instruments.

Acceptance Market

Acceptance Market is another component of money market. It is a market for banker’s acceptance. The acceptance arises on account of both home and foreign trade. Bankers acceptance is a draft drawn by a business firm upon a bank and accepted by that bank. It is required to pay to the order of a particular party or to the bearer, a certain specific amount at a specific date in future. It is commonly used to settle payments in international trade. Thus acceptance market is a market where the bankers’ acceptances are easily sold and discounted.
Collateral Loan Market

Collateral loan market is another important sector of the money market. The collateral loan market is a market which deals with collateral loans. Collateral means anything pledged as security for repayment of a loan. Thus collateral loans are loans backed by collateral securities such as stock, bonds etc. The collateral loans are given for a few months. The collateral security is returned to the borrower when the loan is repaid. When the borrower is not able to repay the loan, the collateral becomes the property of the lender. The borrowers are generally the dealers in stocks and shares.

Features or Defects of the Indian Money Market

The features or defects of the Indian money market are as follows:

1. **Existence of unorganised segment**: The unorganised segment comprises of indigenous bankers, moneylenders etc. This unorganised sector does not follow the rules and regulations of the RBI. Besides, a higher rate of interest prevails in the unorganised market.

2. **Lack of integration**: Another important drawback of the Indian money market is that the money market is divided into different sections. Unfortunately these sections are loosely connected to each other.

3. **Disparities in interest rates**: Too many interest rates are prevailing in the market. For example, borrowing rates of Govt. lending rate of commercial banks, the rates of co-operative banks and rates of financial institutions. This disparity in interest rates is due to lack of mobility of funds from one segment to another.

4. **Seasonal diversity of money market**: The demand for money in Indian money market is of seasonal in nature.

5. **Absence of bill market**: The bill market in India is not well developed. There is a great paucity of sound commercial bills of exchange in our country.

6. **Limited instruments**: The supply of short term instruments like commercial bills, treasury bills etc. are very limited and inadequate.

7. **Restricted secondary market**: Secondary market for money market instruments is mainly restricted to rediscounting of commercial bills and treasury bills.

8. **No contact with foreign money markets**: Indian money market has little contract with money markets in other countries.

In totality it can be concluded that Indian money market is relatively underdeveloped.
Players or Participants in the Indian Money Market

The following are the players in the Indian money market:

1. Govt.
2. RBI
3. Commercial banks
4. Financial institutions like IFCI, IDBI, ICICI, SIDBI, UTI, LIC etc.
5. Discount and Finance House of India.
6. Brokers
7. Mutual funds
8. Public sector undertakings
9. Corporate units

Recent Developments in the Indians Money Market

In recent years, the Indian money market is undergoing structural changes. Several measures have been taken to transform the restricted and narrow market to an active and broad market. The recent developments in the Indian money market are as follows:

1. Integration of unorganised sector with the organised sector
2. Widening of call money market
3. Introduction of innovative instruments
4. Introduction of negotiable dealing system
5. Offering of market rates of interest
6. Satellite system dealership
7. Promotion of bill culture
8. Introduction of money market mutual funds
9. Setting up of credit rating agencies
10. Adoption of suitable monetary policy
11. Establishment of Discount and Finance House of India (DFHI)
12. Setting up of Securities Trading Corporation of India Ltd. (STCI)

Money market is a need based market where the demand for and supply of money are major factors determining the terms and conditions of operations. Money market
provides a platform for the players in financial market to meet the short term fund requirements. It also helps the participants to keep an optimum balance between liquidity and profitability.

Capital Market

Meaning

Capital market simply refers to a market for long term funds. It is a market for buying and selling of equity, debt and other securities. Generally, it deals with long term securities that have a maturity period of above one year.

Capital market is a vehicle through which long term finance is channelized for the various needs of industry, commerce, govt. and local authorities. According to W.H. Husband and J.C. Dockeray, “the capital market is used to designate activities in long term credit, which is characterised mainly by securities of investment type”.

Capital market may be defined as an organized mechanism for the effective and smooth transfer of money capital or financial resources from the investors to the entrepreneurs.

Functions of a Capital Market

The functions of an efficient capital market are as follows:

1. Mobilise long term savings for financing long term investments.
2. Provide risk capital in the form of equity or quasi-equity to entrepreneurs.
3. Provide liquidity with a mechanism enabling the investor to sell financial assets.
4. Improve the efficiency of capital allocation through a competitive pricing mechanism.
5. Disseminate information efficiently for enabling participants to develop an informed opinion about investment, disinvestment, reinvestment etc.
6. Enable quick valuation of instruments – both equity and debt.
7. Provide insurance against market risk through derivative trading and default risk through investment protection fund.
8. Provide operational efficiency through: (a) simplified transaction procedures, (b) lowering settlement times, and (c) lowering transaction costs.
9. Develop integration among: (a) debt and financial sectors, (b) equity and debt instruments, (c) long term and short term funds.
10. Direct the flow of funds into efficient channels through investment and disinvestment and reinvestment.

Components of Capital Market

There are four main components of capital market. They are:

1. Primary market
2. Secondary Market (Details are given in last module)
4. Financial Institutions

These components of capital market may be discussed in detail in the following pages:

Primary Market /New Issue Market (NIM)

When a company wishes to raise long term capital, it goes to the primary market. Primary market is an important constituent of a capital market. In the primary market the security is purchased directly from the issuer.

The primary market is a market for new issues. It is also called new issue market. It is a market for fresh capital. It deals with the new securities which were not previously available to the investing public. Corporate enterprises and Govt. raises long term funds from the primary market by issuing financial securities.

Both the new companies and the existing companies can issue new securities on the primary market. It also covers rising of fresh capital by government or its agencies. The primary market comprises of all institutions dealing in fresh securities. These securities may be in the form of equity shares, preference shares, debentures, right issues, deposits etc.

In short, primary market is a market where the securities are offered to the investing public for the first time.

Functions of Primary Market

The main function of a new issue market is to facilitate transfer of resources from the savers to the users. The savers are individuals, commercial banks, insurance companies etc. The users are public companies and the government.

The main function of a primary market can be divided into three service functions. They are: origination, underwriting and distribution.

1. **Origination:** Origination refers to the work of investigation, analysis and processing of new project proposals. Origination begins before an issue is
actually floated in the market. The function of origination is done by merchant bankers who may be commercial banks, all India financial institutions or private firms.

2. **Underwriting:** When a company issues shares to the public it is not sure that the whole shares will be subscribed by the public. Therefore, in order to ensure the full subscription of shares (or at least 90%) the company may underwrite its shares or debentures. The act of ensuring the sale of shares or debentures of a company even before offering to the public is called underwriting. It is a contract between a company and an underwriter (individual or firm of individuals) by which he agrees to undertake that part of shares or debentures which has not been subscribed by the public. The firms or persons who are engaged in underwriting are called underwriters.

3. **Distribution:** This is the function of sale of securities to ultimate investors. This service is performed by brokers and agents. They maintain a direct and regular contact with the ultimate investors.

**Methods of Raising Fund in the Primary Market (Methods of Floating New Issues)**

A company can raise capital from the primary market through various methods. The methods include public issues, offer for sale, private placement, right issue, and tender method.

1. **Public Issues**

This is the most popular method of raising long term capital. It means raising funds directly from the public. Under this method, the company invites subscription from the public through the issue of prospectus (and issuing advertisements in newspapers). On the basis of offer in the prospectus, the investors apply for the number of securities they are willing to take. In response to application for securities, the company makes the allotment of shares, debentures etc.

**Types of Public Issues:** Public issue is of two types, namely, initial public offer and follow-on public offer.

**Initial Public Offering (IPO):** This is an offering of either a fresh issue of securities or an offer for sale of existing securities or both by an unlisted company for the first time in its life to the public. In short, it is a method of raising securities in which a company sells shares or stock to the general public for the first time.

**Follow-on Public Offering (FPO):** This is an offer of sale of securities by a listed company. This is an offering of either a fresh issue of securities or an offer for sale to the public by an already listed company through an offer document.
2. Offer for Sale Method

Under this method, instead of offering shares directly to the public by the company itself, it offers through the intermediary such as issue houses/merchant banks/investment banks or firms of stock brokers.

Under this method, the sale of securities takes place in two stages. In the first stage, the issuing company sells the shares to the intermediaries such as issue houses and brokers at an agreed price. In the second stage, the intermediaries resell the securities to the ultimate investors at a market related price. This price will be higher. The difference between the purchase price and the issue price represents profit for the intermediaries. The intermediaries are responsible for meeting various expenses. Offer for sale method is also called bought out deal. This method is not common in India.

3. Private Placement of Securities

Private placement is the issue of securities of a company direct to one investor or a small group of investors. Generally the investors are the financial institutions or other existing companies or selected private persons such as friends and relatives of promoters. A private company cannot issue a prospectus. Hence it usually raises its capital by private placement. A public limited company can also raise its capital by placing the shares privately and without inviting the public for subscription of its shares. Company law defines a privately placed issue to be the one seeking subscription from 50 members. In a private placement, no prospectus is issued. In this case the elaborate procedure required in the case of public issue is avoided. Therefore, the cost of issue is minimal. The process of raising funds is also very simple. But the number of shares that can be issued in a private placement is generally limited.

Thus, private placement refers to the direct sale of newly issued securities by the issuer to a small number of investors through merchant bankers.

4. Right Issue

Right issue is a method of raising funds in the market by an existing company. Under this method, the existing company issues shares to its existing shareholders in proportion to the number of shares already held by them. Thus rights issue is the issue of new shares in which existing shareholders are given pre-emptive rights to subscribe to the new issue on a pro-rata basis.

According to Section 81 (1) of the Companies Act, when the company wants to increase the subscribed capital by issue of further shares, such shares must be issued first of all to existing shareholders in proportion of their existing shareholding. The existing shareholders may accept or reject the right. Shareholders who do not wish to
take up the right shares can sell their rights to another person. If the shareholders neither subscribe the shares nor transfer their rights, then the company can offer the shares to public.

5. **Tender method:**

Under tender method, the issue price is not predetermined. The company announces the public issue without indicating the issue price. It invites bids from various interested parties. The parties participating in the tender submit their maximum offers indicating the maximum price they are willing to pay. They should also specify the number of shares they are interested to buy. The company, after receiving various offers, may decide about the price in such a manner that the entire issue is fairly subscribed or sold to the parties participating in the tender.

6. **Issue of bonus shares:**

Where the accumulated reserves and surplus of profits of a company are converted into paid up capital, it is called bonus issue. It simply refers to capitalization of existing reserves and surpluses of a company.

7. **Offer to the employees:**

Nowadays companies issue shares on a preferential basis to their employees (including whole time directors). This attracts, retains and motivates the employees by creating a sense of belonging and loyalty. Generally shares are issued at a discount. A company can issue shares to their employees under the following two schemes: (a) Employee stock option scheme and (b) employee stock purchase scheme.

8. **Offer to the creditors:**

At the time of reorganization of capital, creditors may be issued shares in full settlement of their loans.

9. **Offer to the customers:**

Public utility undertakings offer shares to their customers.

**Procedure of Public Issue**

Under public issue, the new shares/debentures may be offered either directly to the public through a prospectus (offer document) or indirectly through an offer for sale involving financial intermediaries or issue houses. The main steps involved in public issue are as follows:

1. **Draft prospectus:** A draft prospectus has to be prepared giving all required information. Any company or a listed company making a public issue or a right issue
of value more than Rs. 50 lakh has to file a draft offer document with SEBI for its observation. The company can proceed further after getting observations from the SEBI. The company can open its issue within 3 months from the date of SEBI’s observation letter.

2. Fulfilment of Entry Norms: The SEBI has laid down certain entry norms (parameters) for accessing the primary market. A company can enter into the primary market only if a company fulfils these entry norms.

3. Appointment of underwriters: Sometimes underwriters are appointed to ensure full subscription.

4. Appointment of bankers: Generally, the company shall nominate its own banker to act as collecting agent. The bankers along with their branch network process the funds procured during the public issue.

5. Initiating allotment procedure: When the issue is subscribed to the minimum level, the registrars initiate the allotment procedure.

6. Appointment of brokers to the issue: Recognised members of the stock exchange are appointed as brokers to the issue.

7. Filing of documents: Documents such as draft prospectus, along with the copies of the agreements entered into with the lead manager, underwriters, bankers, Registrars, and brokers to the issue have to be filed with the Registrar of Companies.

8. Printing of prospectus and application forms: After filing the above documents, the prospectus and application forms are printed and dispatched to all merchant bankers, underwriters and brokers to the issue.

9. Listing the issue: It is very essential to send a letter to the stock exchange concerned where the issue is proposed to be listed.

10. Publication in news papers: The next step is to publish an abridged version of the prospectus and the commencing and closing dates of issues in major English dailies and vernacular newspapers.

11. Allotment of shares: After close of the issue, all application forms are scrutinised tabulated and then the shares are allotted against those applications received.

Players or Participants (or Intermediaries) in the Primary market/Capital Market

There are many players (intermediaries) in the primary market (or capital market). Important players are as follows:
1 Merchant banker: In attracting public money to capital issues, merchant bankers play a vital role. They act as issue managers, lead managers or co-managers (functions in detail is given in following pages)

2. Registrars to the issue: Registrars are intermediaries who undertake all activities connected with new issue management. They are appointed by the company in consultation with the merchant bankers to the issue.

3. Bankers: Some commercial banks act as collecting agents and some act as coordinating bankers. Some bankers act as merchant bankers and some are brokers. They play an important role in transfer, transmission and safe custody of funds.

4. Brokers: They act as intermediaries in purchase and sale of securities in the primary and secondary markets. They have a network of sub brokers spread throughout the length and breadth of the country.

5. Underwriters: Generally investment bankers act as underwriters. They agreed to take a specified number of shares or debentures offered to the public, if the issue is not fully subscribed by the public. Underwriters may be financial institutions, banks, mutual funds, brokers etc.

Government Securities Market

Govt. securities are also known as Gilt-edged securities. Gilt refers to gold. Thus govt. securities or gilt-edged securities are as pure as gold. This implies that these are completely risk free (no risk of default). Govt. securities market is a market where govt. securities are traded. It is the largest market in any economic system. Therefore, it is the benchmark for other market. Government securities refer to the marketable debt issued by the government of semi-government bodies. A government security is a claim on the government. It is a totally secured financial instrument ensuring safety of both capital and income. That is why it is called gilt-edged security or stock. Central Government securities are the safest among all securities. Government securities are issues by:

- Central Government
- State Government
- Semi-Government authorities like local government authorities, e.g., city corporations and municipalities
- Autonomous institutions, such as metropolitan authorities, port trusts, development trusts, state electricity boards.
- Public Sector Corporations
- Other governmental agencies, such as SFCs, NABARD, LDBs, SIDCs, housing boards etc.
Characteristics of Gilt-edged Securities Market

Gilt-edged securities market is one of the oldest markets in India. The market in these securities is a significant part of Indian stock market. Main characteristics of government securities market are as follows:

a. Supply of government securities in the market arises due to their issue by the Central, State of Local governments and other semi-government and autonomous institutions explained above.

b. Government securities are also held by Reserve Bank of India (RBI) for purpose and sale of these securities and using as an important instrument of monetary control.

c. The securities issued by government organisations are government guaranteed securities and are completely safe as regards payment of interest and repayment of principal.

d. Gilt-edged securities bear a fixed rate of interest which is generally lower than interest rate on other securities.

e. These securities have a fixed maturity period.

f. Interest on government securities is payable half-yearly.

g. Subject to the limits under the Income Tax Act, interest on these securities is exempt from income tax.

h. The gilt-edged market is an 'over-the-counter' market and each sale and purpose has to be negotiated separately.

i. The gilt-edged market is basically limited to institutional investors.

Financial Institutions

Financial institutions are the most active constituent of the Indian capital market. There are special financial institutions which provide medium and long term loans to big business houses. Such institutions help in promoting new companies, expansion and development of existing companies etc. The main special financial institutions of the Indian capital are IDBI, IFCI, ICICI, UTI, LIC, NIDC, SFCs etc.

Capital Market Instruments.

1) Traditional instruments

This includes: a. Equity shares

b. Preference shares and its various classes

c. Debentures and its types

d. bonds etc.,
2) Innovative/recent instruments

Some of the new financial instruments introduced in recent years may be briefly explained as below:

1. **Floating rate bonds**: The interest rate on these bonds is not fixed. It is a concept which has been introduced primarily to take care of the falling market or to provide a cushion in times of falling interest rates in the economy. It helps the issuer to hedge the loss arising due to interest rate fluctuations. In India, SBI was the first to introduce FRB for retail investors.

2. **Zero interest bonds**: These carry no periodic interest payment. These are sold at a huge discount. These can be converted into equity shares or non-convertible debentures.

3. **Deep discount bonds**: These bonds are sold at a large discount while issuing them. These are zero coupon bonds whose maturity is very high (say, 15 years). There is no interest payment. IDBI was the first financial institution to offer DDBs in 1992.

4. **Auction related debentures**: These are a hybrid of CPs and debentures. These are secured, redeemable, non-convertible instrument. The interest on them is determined by the market. These are placed privately with bids. ANZ Grind lays designed this new instrument for Ashok Leyland Finance.

5. **Secured Premium Notes**: These are issued along with a detachable warrant. This warrant gives the holder the right to apply for, or seek allotment of one equity share, provided the SPN is fully paid. The conversion of detachable warrant into equity shares is done within the time limit notified by the company. There is a lock in period during which no interest is paid for the invested amount. TISCO was the first company to issue SPN (in 1992) to the public along with the right issue.

6. **Option bonds**: Option bonds can be converted into equity or preference shares at the option of the investor as per the condition stated in the prospectus. These may be cumulative or non-cumulative. In case of cumulative bonds the interest is accumulated and is payable at maturity. In case of non-cumulative bonds, interest is payable at periodic intervals.

7. **Warrants**: A share warrant is an option to the investor to buy a specified number of equity shares at a specified price over a specified period of time. The warrant holder has to surrender the warrant and pay some cash known as ‘exercise price’ of the warrant to purchase the shares. On exercising the
option the warrant holder becomes a shareholder. Warrant is yet to gain
popularity in India, due to the complex nature of the instrument.

8. **Preference shares with warrants**: These carry a certain number of
warrants. These warrants give the holder the right to apply for equity shares
at premium at any time in one or more stages between the third and fifth year
from the date of allotment.

9. **Non-convertible debentures with detachable equity warrants**: In this
instrument, the holder is given an option to buy a specified number of shares
from the company at a predetermined price within a definite time frame.

10. **Zero interest fully convertible debentures**: On these instruments, no
interest will be paid to the holders till the lock in period. After a notified
period, these debentures will be automatically and compulsorily converted
into shares.

11. **Fully convertible debentures with interest**: This instrument carries no
interest for a specified period. After this period, option is given to apply for
equities at premium for which no additional amount is payable. However,
interest is payable at a predetermined rate from the date of first conversion to
second / final conversion and equity will be issued in lieu of interest.

12. **Non-voting shares**: The Companies Bill, 1997 proposed to allow companies to
issue non-voting shares. These are quasi-equity instruments with differential
rights. These shares do not carry voting right. Their divided rate is also not
predetermined like preference shares.

13. **Inverse float bonds**: These bonds are the latest entrants in the Indian
capital market. These are bonds carrying a floating rate of interest that is
inversely related to short term interest rates.

14. **Perpetual bonds**: These are debt instruments having no maturity date. The
investors receive a stream of interest payment for perpetuity.

**Reforms of Indian Capital Market**

Capital market reforms to the institutional arrangements for long term lending
and borrowings with a view to increase number of service to introduce improved
practices, the Government had various reforms of capital market in the post reforms
era (1992) few of those are discussed below:-
General Reforms:-

i. Statutory Status to SEBI:- With an act of parliament, statutory status was given to SEBI from March 31, 1992. It was provided with the necessary power to control regulate and supervise stock market.

ii. Permission to foreign institutional investors:- Investment norms for NRIs have been liberalized so as to attract more funds into the capital market. The foreign institutional investors can invest into the Indian Capital Market on registration with SEBI.

iii. Permission to Indian Companies: Indian companies have been permitted to raise capital for modernization and raise capital from the international capital market.

Reforms of Primary Market:-

The important reforms of Indian primary market areas under:-

1. Merchant banking has been brought under the regulation act of SEBI.

2. Companies are required to disclose all material facts and specific risk factors, which are associated with their project while making public issues.

3. Stock exchanges are required to ensure that the companies should have a valid acknowledgement card issued by SEBI. In other words the companies should fulfil all the requirements to be listed in the stock market as per SEBI guidelines.

4. SEBI has also introduced a code of advertisement for public issue to ensure fair and truthful disclosures.

Reforms of Secondary Market:

i. Unit Trust of India has been brought under the regulatory jurisdiction of SEBI.

ii. Private Mutual Funds have been permitted and all Mutual Funds are allowed to apply for firm allotment in public issues.

iii. Fresh guidelines were issued for advertising mutual funds.

iv. SEBI has also introduced capital adequacy norms for brokers and main rules for marking client broker relationship more transparent.

v. SEBI also issued guidelines to make the governing body of stock exchange more broad based. It should have 5 elected members not more than 4 members
are nominated by SEBI and 3 or 4 members are nominated as public representatives further an Executive Director will also be there

**Differences between Money Market and Capital Market**

<table>
<thead>
<tr>
<th>Money market</th>
<th>Capital market</th>
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<tbody>
<tr>
<td>2. Operational/WC needs.</td>
<td>2. FC/PC requirements.</td>
</tr>
<tr>
<td>3. Instruments are: bills, CPs, T-bills, CDs etc., .</td>
<td>3. Shares, debentures, bonds etc.</td>
</tr>
<tr>
<td>4. Huge face value for single instrument.</td>
<td>4. Small face value of securities.</td>
</tr>
<tr>
<td>5. Central and coml. banks are major players.</td>
<td>5. Development banks, investment institutions are major players.</td>
</tr>
<tr>
<td>6. No formal place for transactions.</td>
<td>6. Formal place, stock exchanges.</td>
</tr>
<tr>
<td>7. Usually no role to brokers.</td>
<td>7. Brokers playing a vital role.</td>
</tr>
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</table>

Primary markets are markets in which companies raise funds through new issue of stocks. The new securities are sold to initial investors such as households and qualified institutional buyers (QIBs). As the new issue market (NIM)/ Primary market directs the flow of savings into long term investments, it is of paramount importance for the economic growth and industrial development of a country. The availability of financial resources for the corporate enterprises, to the great extent, depends upon the status of primary market in a country.
MODULE II
FINANCIAL SERVICES

Meaning of Financial Services

In general, all types of activities which are of financial nature may be regarded as financial services. In a broad sense, the term financial services means mobilisation and allocation of savings. Thus, it includes all activities involved in the transformation of savings into investment.

Financial services refer to services provided by the finance industry. The finance industry consists of a broad range of organisations that deal with the management of money. These organisations include banks, credit card companies, insurance companies, consumer finance companies, stock brokers, investment funds and some government sponsored enterprises.

Financial services may be defined as the products and services offered by financial institutions for the facilitation of various financial transactions and other related activities.

Financial services can also be called financial intermediation. Financial intermediation is a process by which funds are mobilised from a large number of savers and make them available to all those who are in need of it and particularly to corporate customers. There are various institutions which render financial services. In short, services provided by financial intermediaries are called financial services.

Characteristics or Nature of Financial Services

From the following characteristics of financial services, we can understand their nature:

1. **Intangibility**: Financial services are intangible. Therefore, they cannot be standardized or reproduced in the same form. The institutions supplying the financial services should have a better image and confidence of the customers. Otherwise, they may not succeed. They have to focus on quality and innovation of their services. Then only they can build credibility and gain the trust of the customers.

2. **Inseparability**: Both production and supply of financial services have to be performed simultaneously. Hence, there should be perfect understanding between the financial service institutions and its customers.

3. **Perishability**: Like other services, financial services also require a match between demand and supply. Services cannot be stored. They have to be supplied when customers need them.
4. **Variability:** In order to cater a variety of financial and related needs of different customers in different areas, financial service organisations have to offer a wide range of products and services. This means the financial services have to be tailor-made to the requirements of customers.

5. **Dominance of human element:** Financial services are dominated by human element. Thus, financial services are labour intensive. It requires competent and skilled personnel to market the quality financial products.

6. **Information based:** Financial service industry is an information based industry. It involves creation, dissemination and use of information. Information is an essential component in the production of financial services.

**Role/Importance of Financial Services**

The importance of financial services may be understood from the following points:

1. **Economic growth:** The financial service industry mobilises the savings of the people, and channels them into productive investments by providing various services to people in general and corporate enterprises in particular. In short, the economic growth of any country depends upon these savings and investments.

2. **Promotion of savings:** The financial service industry mobilises the savings of the people by providing transformation services. It provides liability, asset and size transformation service by providing huge loan from small deposits collected from a large number of people. In this way financial service industry promotes savings.

3. **Capital formation:** Financial service industry facilitates capital formation by rendering various capital market intermediary services. Capital formation is the very basis for economic growth.

4. **Creation of employment opportunities:** The financial service industry creates and provides employment opportunities to millions of people all over the world.

5. **Contribution to GNP:** Recently the contribution of financial services to GNP has been increasing year after year in almost countries.

6. **Provision of liquidity:** The financial service industry promotes liquidity in the financial system by allocating and reallocating savings and investment into various avenues of economic activity. It facilitates easy conversion of financial assets into liquid cash.

**Types of Financial Services**

Financial service institutions render a wide variety of services to meet the requirements of individual users. These services may be summarized as below:
1. **Provision of funds:**
   (a) Venture capital
   (b) Banking services
   (c) Asset financing
   (d) Trade financing
   (e) Credit cards
   (f) Factoring and forfaiting

2. **Managing investible funds:**
   (a) Portfolio management
   (b) Merchant banking
   (c) Mutual and pension funds

3. **Risk financing:**
   (a) Project preparatory services
   (b) Insurance
   (c) Export credit guarantee

4. **Consultancy services:**
   (a) Project preparatory services
   (b) Project report preparation
   (c) Project appraisal
   (d) Rehabilitation of projects
   (e) Business advisory services
   (f) Valuation of investments
   (g) Credit rating
   (h) Merger, acquisition and reengineering

5. **Market operations:**
   (a) Stock market operations
   (b) Money market operations
   (c) Asset management
   (d) Registrar and share transfer agencies
   (e) Trusteeship
(f) Retail market operation
(g) Futures, options and derivatives

6. **Research and development:**
(a) Equity and market research
(b) Investor education
(c) Training of personnel
(d) Financial information services

**Scope of Financial Services**

The scope of financial services is very wide. This is because it covers a wide range of services. The financial services can be broadly classified into two: (a) fund based services and (b) non-fund services (or fee-based services)

**I. Fund based Services**

The fund based or asset based services include the following:
1. Underwriting
2. Dealing in secondary market activities
3. Participating in money market instruments like CPs, CDs etc.
4. Equipment leasing or lease financing
5. Hire purchase
6. Venture capital
8. Insurance services
9. Factoring
10. Forfaiting
11. Housing finance
12. Mutual fund

**II. Non-fund based Services**

Today, customers are not satisfied with mere provision of finance. They expect more from financial service companies. Hence, the financial service companies or financial intermediaries provide services on the basis of non-fund activities also. Such services are also known as fee based services. These include the following:
1. Securitisation
2. Merchant banking
3. Credit rating
4. Loan syndication
5. Business opportunity related services
6. Project advisory services
7. Services to foreign companies and NRIs.
8. Portfolio management
9. Merger and acquisition
10. Capital restructuring
11. Debenture trusteeship
12. Custodian services
13. Stock broking

The most important fund based and non-fund based services (or types of services) may be briefly discussed as below:

A. Asset/Fund Based Services

1. Equipment leasing/Lease financing: A lease is an agreement under which a firm acquires a right to make use of a capital asset like machinery etc. on payment of an agreed fee called lease rentals. The person (or the company) which acquires the right is known as lessee. He does not get the ownership of the asset. He acquires only the right to use the asset. The person (or the company) who gives the right is known as lessor.

2. Hire purchase and consumer credit: Hire purchase is an alternative to leasing. Hire purchase is a transaction where goods are purchased and sold on the condition that payment is made in instalments. The buyer gets only possession of goods. He does not get ownership. He gets ownership only after the payment of the last instalment. If the buyer fails to pay any instalment, the seller can repossess the goods. Each instalment includes interest also.

3. Bill discounting: Discounting of bill is an attractive fund based financial service provided by the finance companies. In the case of time bill (payable after a specified period), the holder need not wait till maturity or due date. If he is in need of money, he can discount the bill with his banker. After deducting a certain amount (discount), the banker credits the net amount in the customer’s account. Thus, the bank...
purchases the bill and credits the customer’s account with the amount of the bill less
discount. On the due date, the drawee makes payment to the banker. If he fails to
make payment, the banker will recover the amount from the customer who has
discounted the bill. In short, discounting of bill means giving loans on the basis of the
security of a bill of exchange.

4. **Venture capital**: Venture capital simply refers to capital which is available for
financing the new business ventures. It involves lending finance to the growing
companies. It is the investment in a highly risky project with the objective of earning
a high rate of return. In short, venture capital means long term risk capital in the
form of equity finance.

5. **Housing finance**: Housing finance simply refers to providing finance for house
building. It emerged as a fund based financial service in India with the establishment
of National Housing Bank (NHB) by the RBI in 1988. It is an apex housing finance
institutions in the country. Till now, a number of specialised financial
institutions/ companies have entered in the field of housing finance. Some of the
institutions are HDFC, LIC Housing Finance, Citi Home, Ind Bank Housing etc

6. **Insurance services**: Insurance is a contract between two parties. One party is the
insured and the other party is the insurer. Insured is the person whose life or property
is insured with the insurer. That is, the person whose risks are insured is called
insured. Insurer is the insurance company to whom risk is transferred by the insured.
That is, the person who insures the risk of insured is called insurer. Thus insurance is
a contract between insurer and insured. According to Mc Gill, “Insurance is a process
in which uncertainties are made certain”. In the words of Jon Megi, “Insurance is a
plan wherein persons collectively share the losses of risks”.

   Insurance is a device by which a loss likely to be caused by uncertain event is
spread over a large number of persons who are exposed to it and who voluntarily join
themselves against such an event. The document which contains all the terms and
conditions of insurance (i.e. the written contract) is called the ‘insurance policy’. The
amount for which the insurance policy is taken is called 'sum assured'. The
consideration in return for which the insurer agrees to make good the loss is known as
‘insurance premium’. This premium is to be paid regularly by the insured. It may be
paid monthly, quarterly, half yearly or yearly.

7. **Factoring**: Factoring is an arrangement under which the factor purchases the
account receivables (arising out of credit sale of goods/services) and makes immediate
cash payment to the supplier or creditor. Thus, it is an arrangement in which the
account receivables of a firm (client) are purchased by a financial institution or
banker. Thus, the factor provides finance to the client (supplier) in respect of account
receivables. The factor undertakes the responsibility of collecting the account
receivables. The financial institution (factor) undertakes the risk. For this type of service as well as for the interest, the factor charges a fee for the intervening period. This fee or charge is called factorage.

8. Forfaiting: Forfaiting is a form of financing of receivables relating to international trade. It is a non-recourse purchase by a banker or any other financial institution of receivables arising from export of goods and services. The exporter surrenders his right to the forfaiter to receive future payment from the buyer to whom goods have been supplied. Forfaiting is a technique that helps the exporter sells his goods on credit and yet receives the cash well before the due date. In short, forfaiting is a technique by which a forfaitor (financing agency) discounts an export bill and pay ready cash to the exporter. The exporter need not bother about collection of export bill. He can just concentrate on export trade.

9. Mutual fund: Mutual funds are financial intermediaries which mobilise savings from the people and invest them in a mix of corporate and government securities. The mutual fund operators actively manage this portfolio of securities and earn income through dividend, interest and capital gains. The incomes are eventually passed on to mutual fund shareholders.

Non-Fund Based/Fee Based Financial Services

1. Merchant banking: Merchant banking is basically a service banking, concerned with providing non-fund based services of arranging funds rather than providing them. The merchant banker merely acts as an intermediary. Its main job is to transfer capital from those who own it to those who need it. Today, merchant banker acts as an institution which understands the requirements of the promoters on the one hand and financial institutions, banks, stock exchange and money markets on the other. SEBI (Merchant Bankers) Rule, 1992 has defined a merchant banker as, “any person who is engaged in the business of issue management either by making arrangements regarding selling, buying or subscribing to securities or acting as manager, consultant, advisor, or rendering corporate advisory services in relation to such issue management”.

2. Credit rating: Credit rating means giving an expert opinion by a rating agency on the relative willingness and ability of the issuer of a debt instrument to meet the financial obligations in time and in full. It measures the relative risk of an issuer’s ability and willingness to repay both interest and principal over the period of the rated instrument. It is a judgement about a firm’s financial and business prospects. In short, credit rating means assessing the creditworthiness of a company by an independent organisation.
3. **Stock broking**: Now stock broking has emerged as a professional advisory service. Stock broker is a member of a recognized stock exchange. He buys, sells, or deals in shares/securities. It is compulsory for each stock broker to get himself/herself registered with SEBI in order to act as a broker. As a member of a stock exchange, he will have to abide by its rules, regulations and by-laws.

4. **Custodial services**: In simple words, the services provided by a custodian are known as custodial services (custodian services). Custodian is an institution or a person who is handed over securities by the security owners for safe custody. Custodian is a caretaker of a public property or securities. Custodians are intermediaries between companies and clients (i.e. security holders) and institutions (financial institutions and mutual funds). There is an arrangement and agreement between custodian and real owners of securities or properties to act as custodians of those who hand over it. The duty of a custodian is to keep the securities or documents under safe custody. The work of custodian is very risky and costly in nature. For rendering these services, he gets a remuneration called custodial charges.

Thus custodial service is the service of keeping the securities safe for and on behalf of somebody else for a remuneration called custodial charges.

4. **Loan syndication**: Loan syndication is an arrangement where a group of banks participate to provide funds for a single loan. In loan syndication, a group of banks comprising 10 to 30 banks participate to provide funds wherein one of the banks is the lead manager. This lead bank is decided by the corporate enterprises, depending on confidence in the lead manager.

A single bank cannot give a huge loan. Hence a number of banks join together and form a syndicate. This is known as loan syndication. Thus, loan syndication is very similar to consortium financing.

5. **Securitisation (of debt)**: Loans given to customers are assets for the bank. They are called loan assets. Unlike investment assets, loan assets are not tradable and transferable. Thus loan assets are not liquid. The problem is how to make the loan of a bank liquid. This problem can be solved by transforming the loans into marketable securities. Now loans become liquid. They get the characteristic of marketability. This is done through the process of securitization. Securitisation is a financial innovation. It is conversion of existing or future cash flows into marketable securities that can be sold to investors. It is the process by which financial assets such as loan receivables, credit card balances, hire purchase debtors, lease receivables, trade debtors etc. are transformed into securities. Thus, any asset with predictable cash flows can be securitised.
Securitisation is defined as a process of transformation of illiquid asset into security which may be traded later in the opening market. In short, securitization is the transformation of illiquid, non-marketable assets into securities which are liquid and marketable assets. It is a process of transformation of assets of a lending institution into negotiable instruments.

Securitisation is different from factoring. Factoring involves transfer of debts without transforming debts into marketable securities. But securitisation always involves transformation of illiquid assets into liquid assets that can be sold to investors.
MODULE III

MERCHANT BANKING

History of Merchant banking:

The origin of merchant banking is to be traced to Italy in late medieval times and France during the seventeenth and eighteenth centuries. The Italian merchant bankers introduced into England not only the bill of exchange but also all the institutions and techniques connected with an organized money market during seventeenth and eighteenth centuries. In France a merchant banker (le merchant banquer) was not merely a trader but an entrepreneur par excellence. He invested his accumulated profits in all forms of promising activities. He added banking business to his merchant activities and became a merchant banker.

In the United Kingdom, merchant’s banks came into operation in the late eighteenth century and early nineteenth century. Industrial revolution made England into a powerful trading nation. Rich merchant houses that made their fortunes in colonial trade diversified into banking. Their principal activity started with the acceptance of commercial bills pertaining to domestic as well as international trade. The acceptance of the trade bills and discounting gave rise to acceptances houses, discount houses and issue houses. Merchant banker was primarily a merchant rather than a banker but he was entrusted with funds by his customers.

Merchant banking activity was formally initiated into the Indian capital Markets when Grindlays bank received the license from reserve bank in 1967. Grindlays started with management of capital issues, recognized the needs of emerging class of entrepreneurs for diverse financial services ranging from production planning and system design to market research. Citibank Setup its merchant banking division in 1970. The various tasks performed by this divisions namely assisting new entrepreneur, evaluating new projects, raising funds through borrowing and issuing equity. Indian banks started merchant banking Services as a part of multiple services they offer to their clients from 1972. State bank of India started the merchant banking division in 1972 and ICICI Bank in 1974. In the Initial years the SBI's objective was to render corporate advice And Assistance to small and medium entrepreneurs. Merchant banking activities is OF course organized and undertaken in several forms. Commercial banks and foreign development finance institutions have organized them through formation divisions, nationalized banks have formed subsidiaries companies and share brokers and consultancies constituted themselves into public limited companies or registered themselves as private limited companies. Some merchant banking outfits have entered into collaboration with merchant bankers abroad with several branches.
Meaning and Definition of Merchant Banking

Merchant banking is non-banking financial activity. But it resembles banking function. It is a financial service. It includes the entire range of financial services.

According to Random House Dictionary, “merchant bank is an organization that underwriters securities for corporations, advises such clients on mergers and is involved in the ownership of commercial ventures. These organizations are sometimes banks which are not merchants and sometimes merchants who are not bankers and sometimes houses which neither merchants nor banks”. According to SEBI (Merchant Bankers) Rules 1992, “A merchant banker has been defined as any person who is engaged in the business of issue management either by making arrangements regarding selling, buying or subscribing to securities or acting as manager, consultant advisor or rendering corporate advisory services in relation to such issue management”. In short, “merchant bank refers to an organization that underwrites securities and advises such clients on issues like corporate mergers, involving in the ownership of commercial ventures”.

Nutshell, merchant banking involves servicing any financial need of the client.

Setting up and management of merchant banks in India

In India a common organizational set up of merchant bankers to operate is in the form of divisions of Indian and Foreign banks and financial institutions, subsidiary companies established by bankers like SBI, Canara Bank, Punjab National Bank, Bank of India, etc. some firms are also organized by financial and technical consultants and professionals. Securities and exchanges Board of India (SEBI) has divided the merchant bankers into four categories based on their capital adequacy. Each category is authorized to perform certain functions. From the point of Organizational set up India’s merchant banking organizations can be categorized into 4 groups on the basis of their linkage with parent activity. They are:

a) Institutional Base:-

Where merchant banks function as an independent wing or as subsidiary of various Private/ Central Governments/State Governments Financial institutions. Most of the financial institutions in India are in public sector and therefore such set up plays a role on the lines of governmental priorities and policies.

b) Banker Base:-

These merchant bankers function as division/ subsidiary of banking organization. The parent banks are either nationalized commercial banks or the foreign banks operating in India. These organizations have brought professionalism in merchant banking sector and they help their parent organization to make a presence in capital market.
c) Broker Base:-

In the recent past there has been an inflow of Qualified and professionally skilled brokers in various Stock Exchanges of India. These brokers undertake merchant banking related operating also like providing investment and portfolio management services.

d) Private Base:-

These merchant banking firms are originated in private sectors. These organizations are the outcome of opportunities and scope in merchant banking business and they are providing skill oriented specialized services to their clients. Some foreign merchant bankers are also entering either independently or through some collaboration with their Indian counterparts. Private Sectors merchant banking firms have come up either as sole proprietorship, partnership, private limited or public limited companies. Many of these firms were in existence for quite some time before they added a new activity in the form of merchant banking services by opening new division on the lines of commercial banks and All India Financial Institution (AIFI).

Merchant banks Vs Commercial banks

1. Commercial banks basically deal in debt and debt related finance. Their activities are clustered around credit proposals, credit appraisal and loan sanctions. On the other hand, the area of activity of merchant bankers is equity and equity related finance. They deal with mainly funds raised through money market and capital market.

2. Commercial banks’ lending decisions are based on detailed credit analysis of loan proposals and the value of security offered. They generally avoid risks. They are asset oriented. But merchant bankers are management oriented. They are willing to accept risks of business.

3. Commercial banks are merely financiers. The main activity of merchant bankers is to render financial services for their clients. They undertake project counselling, corporate counselling in areas of capital restructuring, mergers, takeovers and many others.

Functions (Services) of Merchant Bankers (Scope of Merchant Banking)

The functions of merchant banks in India are as follows:

1. Corporate counselling: One of the important functions of a merchant banker is corporate counselling. Corporate counselling refers to a set of activities undertaken to ensure efficient functioning of a corporate enterprise through effective financial
management. A merchant banker guides the client on aspects of organizational goals, vocational factors, organization size, choice of product, demand forecasting, cost analysis, allocation of resources, investment decisions, capital and expenditure management, marketing strategy, pricing methods etc. The following activities are included in corporate counseling:

(a) Providing guidance in areas of diversification based on the Government’s economic and licensing policies.

(b) Undertaking appraisal of product lines, analyzing their growth and profitability and forecasting future trends.

(c) Rejuvenating old-line companies and ailing sick units by appraising their technology and process, assessing their requirements and restructuring their capital base.

(d) Assessment of the revival prospects and planning for rehabilitation through modernization and diversification and revamping of the financial and organizational structure.

(e) Arranging for the approval of the financial institutions/banks for schemes of rehabilitation involving financial relief, etc.

2. Project counselling: Project counselling relates to project finance. This involves the study of the project, offering advisory services on the viability and procedural steps for its implementation. Project counselling involves the following activities:

(a) Undertaking the general review of the project ideas/project profile.

(b) Providing advice on procedural aspects of project implementation.

(c) Conducting review of technical feasibility of the project on the basis of the report prepared by own experts or by outside consultants.

(d) Assisting in the preparation of project report from a financial angle, and advising and acting on various procedural steps including obtaining government consents for implementation of the project.

(e) Assisting in obtaining approvals/licenses/permissions/grants, etc from government agencies in the form of letter of intent, industrial license, DGTD registration, and government approval for foreign collaboration.

(f) Identification of potential investment avenues.

3. Pre-investment studies: Another function of a merchant banker is to guide the entrepreneurs in conducting pre-investment studies. It involves detailed feasibility study to evaluate investment avenues to enable to decide whether to invest or not. The important activities involved in pre-investment studies are as follows:
(a) Carrying out an in-depth investigation of environment and regulatory factors, location of raw material supplies, demand projections and financial requirements in order to assess the financial and economic viability of a given project.

(b) Helping the client in identifying and short-listing those projects which are built upon the client’s inherent strength with a view to promote corporate profitability and growth in the long run.

(c) Offering a package of services, including advice on the extent of participation, government regulatory factors and an environmental scan of certain industries in India.

4. Loan syndication: A merchant banker may help to get term loans from banks and financial institutions for projects. Such loans may be obtained from a single financial institution or a syndicate or consortium. Merchant bankers help corporate clients to raise syndicated loans from commercial banks. The following activities are undertaken by merchant bankers under loan syndication:

(a) Estimating the total cost of the project to be undertaken.

(b) Drawing up a financing plan for the total project cost which conforms to the requirements of the promoters and their collaborators, financial institutions and banks, government agencies and underwriters.

(c) Preparing loan application for financial assistance from term lenders/financial institutions/banks, and monitoring their progress, including pre-sanction negotiations.

(d) Selecting institutions and banks for participation in financing.

(e) Follow-up of term loan application with the financial institutions and banks, and obtaining the approval for their respective share of participation.

(f) Arranging bridge finance.

(g) Assisting in completion of formalities for drawing of term finance sanctioned by institutions by expediting legal documentation formalities, drawing up agreements etc. as prescribed by the participating financial institutions and banks.

(h) Assessing working capital requirements.

5. Issue management: Issue management involves marketing or corporate securities by offering them to the public. The corporate securities include equity shares, preference shares, bonds, debentures etc. Merchant bankers act as financial intermediaries. They transfer capital from those who own it to those who need it. The security issue function may be broadly classified into two – pre-issue management and post-issue management. The pre-issue management involves the following functions:
(a) Public issue through prospectus.
(b) Marketing and underwriting.
(c) Pricing of issues.

6. Underwriting of public issue: In underwriting of public issue the activities performed by merchant bankers are as follows:
(a) Selection of institutional and broker underwriters for syndicating/underwriting arrangements.
(b) Obtaining the approval of institutional underwriters and stock exchanges for publication of the prospectus.
(c) Co-ordination with the underwriters, brokers and bankers to the issue, and the Stock Exchanges.

7. Portfolio management: Merchant bankers provide portfolio management service to their clients. Today every investor is interested in safety, liquidity and profitability of his investment. But investors cannot study and choose the appropriate securities. Merchant bankers help the investors in this regard. They study the monetary and fiscal policies of the government. They study the financial statements of companies in which the investments have to be made by investors. They also keep a close watch on the price movements in the stock market.

The merchant bankers render the following services in connection with portfolio management:
(a) Undertaking investment in securities.
(b) Collection of return on investment and re-investment of the same in profitable avenues, investment advisory services to the investors and other related services.
(c) Providing advice on selection of investments.
(d) Carrying out a critical evaluation of investment portfolio.
(e) Securing approval from RBI for the purchase/sale of securities (for NRI clients).
(f) Collecting and remitting interest and dividend on investment.
(g) Providing tax counselling and filing tax returns through tax consultants.

8. Merger and acquisition: A merger is a combination of two or more companies into a single company where one survives and others lose their corporate existence. A take over refers to the purchase by one company acquiring controlling interest in the
share capital of another existing company. Merchant bankers are the middlemen in setting negotiation between the offeree and offeror. Being a professional expert they are apt to safeguard the interest of the shareholders in both the companies. Once the merger partner is proposed, the merchant banker appraises merger/takeover proposal with respect to financial viability and technical feasibility. He negotiates purchase consideration and mode of payment. He gets approval from the government/RBI, drafts scheme of amalgamation and obtains approval from financial institutions.

9. Foreign currency financing: The finance provided to fund foreign trade transactions is called ‘Foreign Currency Finance’. The provision of foreign currency finance takes the form of export-import trade finance, euro currency loans, Indian joint ventures abroad and foreign collaborations. The main areas that are covered in this type of merchant activity are as follows:

(a) Providing assistance for carrying out the study of turnkey and construction contract projects.

(b) Arranging for the syndication of various types of guarantees, letters of credit, pre-shipment credit, deferred post-shipment credit, bridge loans, and other credit facilities.

(c) Providing assistance in opening and operating bank accounts abroad.

(d) Arranging foreign currency loans under buyer’s credit scheme for importing goods.

(e) Arranging deferred payment guarantees under suppliers credit scheme for importing capital goods.

10. Working capital finance: The finance required for meeting the day-to-day expenses of an enterprise is known as ‘Working Capital Finance’. Merchant bankers undertake the following activities as part of providing this type of finance:

(a) Assessment of working capital requirements.

(b) Preparing the necessary application to negotiations for the sanction of appropriate credit facilities.

11. Acceptance credit and bill discounting: Merchant banks accept and discount bills of exchange on behalf of clients. Merchant bankers give loans to business enterprises on the security of bill of exchange. For this purpose, merchant bankers collect credit information relating to the clients and undertake rating their creditworthiness.
12. **Venture financing:** Another function of a merchant banker is to provide venture finance to projects. It refers to provision of equity finance for funding high-risk and high-reward projects.

13. **Lease financing:** Leasing is another function of merchant bankers. It refers to providing financial facilities to companies that undertake leasing. Leasing involves letting out assets on lease for a particular period for use by the lessee. The following services are provided by merchant bankers in connection with lease finance:
   (a) Providing advice on the viability of leasing as an alternative source for financing capital investment projects.
   (b) Providing advice on the choice of a favourable rental structure.
   (c) Providing assistance in establishing lines of lease for acquiring capital equipment, including preparation of proposals, documentations, etc.

14. **Relief to sick industries:** Merchant bankers render valuable services as a part of providing relief to sick industries.

15. **Project appraisal:** Project appraisal refers to evaluation of projects from various angles such as technology, input, location, production, marketing etc. It involves financial appraisal, marketing appraisal, technical appraisal, economic appraisal etc. Merchant bankers render valuable services in the above areas.

**Role of Merchant Bankers in Managing Public Issue**

The most important aspect of merchant banking business is to function as lead managers to the issue management. The role of the merchant banker as an issue manager can be studied from the following points:

1. **Easy fund raising:** An issue manager acts as an indispensable pilot facilitating a public/ rights issue. This is made possible with the help of special skills possessed by him to execute the management of issues.

2. **Financial consultant:** An issue manager essentially acts as a financial architect, by providing advice relating to capital structuring, capital gearing and financial planning for the company.

3. **Underwriting:** An issue manager allows for underwriting the issues of securities made by corporate enterprises. This ensures due subscription of the issue.

4. **Due diligence:** The issue manager has to comply with SEBI guidelines. The merchant banker will carry out activities with due diligence and furnish a Due Diligence Certificate to SEBI. The detailed diligence guidelines that are prescribed by the Association of Merchant Bankers of India (AMBI) have to be strictly observed. SEBI has also prescribed a code of conduct for merchant bankers.
5. Co-ordination: The issue manager is required to co-ordinate with a large number of institutions and agencies while managing an issue in order to make it successful.

6. Liaison with SEBI: The issue manager, as a part of merchant banking activities, should register with SEBI. While managing issues, constant interaction with the SEBI is required by way of filing of offer documents, etc. In addition, they should file a number of reports relating to the issues being managed.

Merchant Banking in India

Prior to the enactment of Indian Companies Act, 1956, managing agents acted as merchant bankers. They acted as issue houses for securities, evaluated project reports, provided venture capital for new firms etc. Few share broking firms also functioned as merchant bankers.

With the rapid growth in the number and size of the issues made in the primary market, the need for specialized merchant banking service was felt. Grindlays Bank (foreign bank) opened its merchant banking division in 1967, followed by Citybank in 1970. SBI started its merchant banking division in 1972 and it followed up by setting up a fully owned subsidiary in 1980, namely SBI Capital Markets Ltd. The other nationalized banks and financial institutions, like IDBI, IFCI, ICICI, Securities and Finance Company Ltd., Canara Bank (Can Bank Financial Services Ltd.), Bank of India (BOI Finance Ltd.) and private sector financial companies, like JM Financial and Investment Consultancy Services Ltd., DSP Financial Consultance Ltd. have also set up their merchant banking divisions.

With over 1,100 merchant bankers operating in the country, the primary market activity is picking up. Merchant banking services have assumed greater importance in the present capital market scenario. With the investor becoming more cautious and discerning, the role of merchant banker has gained more prominence.

In India, apart from the overall control by the RBI, merchant bankers’ operations are closely supervised by the SEBI for their proper functioning and investor protection.

Classification of Merchant Banks

Merchant bankers are classified into four categories according to the SEBI (Merchant Banking) Regulations 1992. These are as follows:

(a) Category – I: To carry on any activity relating to issue management and act as adviser, consultant manager, underwriter and portfolio manager for capital issues.

(b) Category – II: To act as adviser, consultant, co-manager, underwriter and portfolio manager for capital issues.
(c) Category – III: To act as underwriter, adviser, and consultant to an issue.

(d) Category – IV: To act only as adviser or consultant to an issue.

SEBI guidelines on Merchant Banking in India

1. Qualifications

According to the book "Financial Services," major merchant banking guidelines were first established in 1990, with SEBI amendments being introduced after the Securities and Exchange Board of India Act in 1992.

The guidelines require that all merchant bankers must have experience in finance, law or business management, as well as adequate office space, equipment and manpower to provide service of a professional calibre. Sufficient manpower is considered to be at least two persons with proficiency in merchant banking.

2. Classification

According to the 1992 guidelines, merchant bankers were classified into one of four categories: management, consulting, advising or underwriting. In 2007, however, a merchant banker's role became more restricted and was limited to buying, selling or advising on investment securities. A merchant banker must file a separate registration for underwriting and portfolio manager privileges.

Further, a merchant banker cannot perform functions typical to a retail bank, such as accepting deposits or leasing, but must involve itself only in matters directly related to the capital market.

3. Oversight

The SEBI oversees all aspects of merchant banking and may suspend or revoke a merchant banker's status if guidelines or laws are violated. Merchant bankers must submit quarterly reports detailing all transactions, including the names of involved companies or parties and the transaction amount. Transactions involving more than $21 million (as of 2007, converted from Indian Rupees) may be handled by a maximum of five lead managers. In addition, corporate bodies and other parties must be aware of mutual rights, liabilities and obligations before finalizing any transaction.

The SEBI also monitors merchant banking employees by mandating that information about each employee be submitted for entry into an SEBI-managed database.

Factoring
Meaning and Definition of Factoring

The word factor is derived from the Latin word *facere*. It means to make or do or to get things done. Factoring simply refers to selling the receivables by a firm to another party. The buyer of the receivables is called the factor. Thus factoring refers to the agreement in which the receivables are sold by a firm (client) to the factor (financial intermediary). The factor can be a commercial bank or a finance company. When receivables are factored, the factor takes possession of the receivables and generally becomes responsible for its collection. It also undertakes administration of credit i.e. credit control, sales accounting etc.

Thus factoring may be defined as selling the receivables of a firm at a discount to a financial organisation (factor). The cash from the sale of the receivables provides finance to the selling company (client). Out of the difference between the face value of the receivables and what the factor pays the selling company (i.e. discount), it meets its expenses (collection, accounting etc.). The balance is the profit of the factor for the factoring services.

Objectives of Factoring

Factoring is a method of converting receivables into cash. There are certain objectives of factoring. The important objectives are as follows:

1. To relieve from the trouble of collecting receivables so as to concentrate in sales and other major areas of business.

2. To minimize the risk of bad debts arising on account of non-realisation of credit sales.

3. To adopt better credit control policy.

4. To carry on business smoothly and not to rely on external sources to meet working capital requirements.

5. To get information about market, customers’ credit worthiness etc. so as to make necessary changes in the marketing policies or strategies.

Types of Factoring

There are different types of factoring. These may be briefly discussed as follows:

1. **Recourse Factoring:** In this type of factoring, the factor only manages the receivables without taking any risk like bad debt etc. Full risk is borne by the firm (client) itself.
2. **Non-Recourse Factoring:** Here the firm gets total credit protection because complete risk of total receivables is borne by the factor. The client gets 100% cash against the invoices (arising out of credit sales by the client) even if bad debts occur. For the factoring service, the client pays a commission to the factor. This is also called *full factoring*.

3. **Maturity Factoring:** In this type of factoring, the factor does not pay any cash in advance. The factor pays clients only when he receives funds (collection of credit sales) from the customers or when the customers guarantee full payment.

4. **Advance Factoring:** Here the factor makes advance payment of about 80% of the invoice value to the client.

5. **Invoice Discounting:** Under this arrangement the factor gives advance to the client against receivables and collects interest (service charge) for the period extending from the date of advance to the date of collection.

6. **Undisclosed Factoring:** In this case the customers (debtors of the client) are not at all informed about the factoring agreement between the factor and the client. The factor performs all its usual factoring services in the name of the client or a sales company to which the client sells its book debts. Through this company the factor deals with the customers. This type of factoring is found in UK.

**Process of Factoring (Factoring Mechanism)**

The firm (client) having book debts enters into an agreement with a factoring agency/institution. The client delivers all orders and invoices and the invoice copy (arising from the credit sales) to the factor. The factor pays around 80% of the invoice value (depends on the price of factoring agreement), as advance. The balance amount is paid when factor collects complete amount of money due from customers (client’s debtors). Against all these services, the factor charges some amounts as service charges. In certain cases the client sells its receivables at discount, say, 10%. This means the factor collects the full amount of receivables and pays 90% (in this case) of the receivables to the client. From the discount (10%), the factor meets its expenses and losses. The balance is the profit or service charge of the factor.

Thus there are three parties to the factoring. They are the buyers of the goods (client’s debtors), the seller of the goods (client firm i.e. seller of receivables) and the factor. Factoring is a financial intermediary between the buyer and the seller.

**Functions of a Factor**

A factor performs some important functions. These may be discussed as follows:
1. **Provision of finance:** Receivables or book debts is the subject matter of factoring. A factor buys the book debts of his client. Generally a factor gives about 80% of the value of receivables as advance to the client. Thus the non productive and inactive current assets i.e. receivables are converted into productive and active assets i.e. cash.

2. **Administration of sales ledger:** The factor maintains the sales ledger of every client. When the credit sales take place, the firm prepares the invoice in two copies. One copy is sent to the customers. The other copy is sent to the factor. Entries are made in the ledger under open-item method. In this method each receipt is matched against the specific invoice. The customer’s account clearly shows the various open invoices outstanding on any given date. The factor also gives periodic reports to the client on the current status of his receivables and the amount received from customers. Thus the factor undertakes the responsibility of entire sales administration of the client.

3. **Collection of receivables:** The main function of a factor is to collect the credit or receivables on behalf of the client and to relieve him from all tensions/problems associated with the credit collection. This enables the client to concentrate on other important areas of business. This also helps the client to reduce cost of collection.

4. **Protection against risk:** If the debts are factored without resource, all risks relating to receivables (e.g., bad debts or defaults by customers) will be assumed by the factor. The factor relieves the client from the trouble of credit collection. It also advises the client on the creditworthiness of potential customers. In short, the factor protects the clients from risks such as defaults and bad debts.

5. **Credit management:** The factor in consultation with the client fixes credit limits for approved customers. Within these limits, the factor undertakes to buy all trade debts of the customer. Factor assesses the credit standing of the customer. This is done on the basis of information collected from credit relating reports, bank reports etc.

6. **Advisory services:** These services arise out of the close relationship between a factor and a client. The factor has better knowledge and wide experience in the field of finance. It is a specialised institution for managing account receivables. It possesses extensive credit information about customer’s creditworthiness and track record. With all these, a factor can provide various advisory services to the client. Besides, the factor helps the client in raising finance from banks/financial institutions.
Advantages of Factoring

A firm that enters into factoring agreement is benefited in a number of ways. Some of the important benefits of factoring are summarised as follows:

1. **Improves efficiency:** Factoring is an important tool for efficient receivables management. Factors provide specialised services with regard to sales ledger administration, credit control etc. Factoring relieves the clients from botheration of debt collection.

2. **Higher credit standing:** Factoring generates cash for the selling firm. It can use this cash for other purposes. With the advance payment made by factor, it is possible for the client to pay off his liabilities in time. This improves the credit standing of the client before the public.

3. **Reduces cost:** The client need not have a special administrative setup to look after credit control. Hence it can save manpower, time and effort. Since the factoring facilitates steady and reliable cash flows, client can cut costs and expenses. It can avail cash discounts. Further, it can avoid production delays.

4. **Additional source:** Funds from a factor is an additional source of finance for the client. Factoring releases the funds tied up in credit extended to customers and solves problems relating to collection, delays and defaults of the receivables.

5. **Advisory service:** It provides all management and administrative support from the stage of deciding credit extension to the customers to the final stage of debt collection. It advocates the best credit policy suitable for the firm.

6. **Acceleration of production cycle:** With cash available for credit sales, client firm’s liquidity will improve. In this way its production cycle will be accelerated.

7. **Adequate credit period for customers:** Customers get adequate credit period for payment of assigned debts.

8. **Competitive terms to offer:** The client firm will be able to offer competitive terms to its buyers. This will improve its sales and profits.

Limitations of Factoring

The main limitations of factoring are outlined as below:

1. Factoring may lead to over-confidence in the behaviour of the client. This results in overtrading or mismanagement.

2. There are chances of fraudulent acts on the part of the client. Invoicing against non-existent goods, duplicate invoicing etc. are some commonly found frauds. These would create problems to the factors.

3. Lack of professionalism and competence, resistance to change etc. are some of the problems which have made factoring services unpopular.
4. Factoring is not suitable for small companies with lesser turnover, companies with speculative business, companies having large number of debtors for small amounts etc.

5. Factoring may impose constraints on the way to do business. For non-recourse factoring most factors will want to pre-approve customers. This may cause delays. Further, the factor will apply credit limits to individual customers.

**FORFAITING**

Generally there is a delay in getting payment by the exporter from the importer. This makes it difficult for the exporter to expand his export business. However, for getting immediate payment, the concept of forfeiting shall come to the help of exporters.

The concept of forfaiting was originally developed to help finance German exports to Eastern block countries.

**Meaning of Forfaiting**

The term 'forfait' is a French world. It means 'to surrender something' or 'give up one's right'. Thus forfaiting means giving up the right of exporter to the forfaitor to receive payment in future from the importer. It is a method of trade financing that allows exporters to get immediate cash and relieve from all risks by selling their receivables (amount due from the importer) on a 'without recourse' basis. This means that in case the importer makes a default the forfaitor cannot go back to the exporter to recover the money. Under forfaiting the exporter surrenders his right to a receivable due at a future date in exchange for immediate cash payment, at an agreed discount. Here the exporter passes to the forfaitor all risks and responsibilities in collecting the debt. The exporter is able to get 100% of the amount of the bill immediately. Thus he gets the benefit of cash sale. However, the forfaitor deducts the discount charges and he gives the balance amount to the exporter. The entire responsibility of recovering the amount from the importer is entrusted with the forfaitor. The forfaitor may be a bank or any other financial institution.

In short, the non-recourse purchase of receivables arising from an export of goods and services by a forfaitor is known as forfaiting.

**Characteristics of Forfaiting**

The main characteristics of forfaiting are:

1. It is 100% financing without recourse to the exporter.
2. The importer’s obligation is normally supported by a local bank guarantee (i.e., ‘aval’).
3. Receivables are usually evidenced by bills of exchange, promissory notes or letters of credit.

4. Finance can be arranged on a fixed or floating rate basis.

5. Forfaiting is suitable for high value exports such as capital goods, consumer durables, vehicles, construction contracts, project exports etc.

6. Exporter receives cash upon presentation of necessary documents, shortly after shipment.

**Advantages of Forfaiting**

The following are the benefits of forfaiting:

1. The exporter gets the full export value from the forfaitor.

2. It improves the liquidity of the exporter. It converts a credit transaction into a cash transaction.

3. It is simple and flexible. It can be used to finance any export transaction. The structure of finance can be determined according to the needs of the exporter, importer, and the forfaitor.

4. The exporter is free from many export credit risks such as interest rate risk, exchange rate risk, political risk, commercial risk etc.

5. The exporter need not carry the receivables into his balance sheet.

6. It enhances the competitive advantage of the exporter. He can provide more credit. This increases the volume of business.

7. There is no need for export credit insurance. Exporter saves insurance costs. He is relieved from the complicated procedures also.

8. It is beneficial to forfaitor also. He gets immediate income in the form of discount. He can also sell the receivables in the secondary market or to any investor for cash.

**Difference between Factoring and Forfaiting**

Forfaiting and factoring have similarities. Both have similar features of advance payment and non-recourse dealing. But there are some differences between them. The differences are as follows:
### Factoring vs. Forfaiting

<table>
<thead>
<tr>
<th>Factoring</th>
<th>Forfaiting</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Used for short term financing</td>
<td>Used for medium term financing.</td>
</tr>
<tr>
<td>2. May be with or without recourse.</td>
<td>Always without recourse.</td>
</tr>
<tr>
<td>3. Applicable to both domestic and export receivables.</td>
<td>Applicable to export receivables only</td>
</tr>
<tr>
<td>4. Normally 70 to 85% of the invoice value is provided as advance</td>
<td>100% finance is provided to the exporter.</td>
</tr>
<tr>
<td>5. The contractor is between the factor and the seller.</td>
<td>The contract is between the forfaitor and the exporter.</td>
</tr>
<tr>
<td>6. Other than financing, several other things like sales ledger administration, debt collection etc. is provided by the factor.</td>
<td>It is a financing arrangement only.</td>
</tr>
<tr>
<td>7. Bulk finance is provided against a number of unpaid invoices.</td>
<td>It is based on a single export bill resulting from only a single transaction.</td>
</tr>
<tr>
<td>8. No minimum size of transaction is specified.</td>
<td>There is a minimum specified value per transaction</td>
</tr>
</tbody>
</table>

### Credit Card and Debit Card

A credit card is a small plastic card issued to users as a system of payment. It allows its holder to buy goods and services based on the holder's promise to pay for these goods and services. The issuer of the card creates a revolving account and grants a line of credit to the consumer (or the user) from which the user can borrow money for payment to a merchant or as a cash advance to the user.

Credit card can be defined in many ways with different senses. It is difficult to give a perfect definition of credit card. Following statements are attempts to help you derive its narrow and broad meaning.

1. In **General** sense,

   “Credit card is a suitable alternative for cash payment or credit payment or deferred (instalment) payment. It is used to execute those transactions which are compiled through electronic devices like a card swapping machine, computer with internet facility, etc.”
2. In a **Financial** perspective,

“Credit card is a facility provided by a bank or non-banking financial company (NBFC) which gives its customer a preference to have a short-term borrowing of funds usually at the point of transaction (while purchasing something or carrying out sale).”

3. In terms of **Business**, 

“Credit card is a laminated plastic card issued by a bank or non-banking financial company (NBFC) to give its cardholder a preference to borrow funds on a short-period basis. Interest is imposed for lending short-term finance to the cardholder. This interest is generally charged either after a month or 30-45 days later, once credit-card transactions have occurred. The card limit is pre-communicated in written correspondence with cardholder.”

**Features of credit card**

1. **Alternative to cash**

Credit card is a better alternative to cash. It removes the worry of carrying various currency denominations to pay at the trade counters. As an alternative, credit card helps a cardholder to travel anywhere in the world without a need to carry an ample amount of cash. It also reduces the possible risk of money theft and gives its user a complete peace of mind.

2. **Credit limit**

The credit cardholder enjoys the facility of a credit limit set on his card. This limit of credit is determined by the credit card issuing entity (bank or NBFC) only after analyzing the credit worthiness of the cardholder.

The credit limit is of two types, viz.,

1. Normal credit limit, and
2. Revolving credit limit.

Normal credit limit is usual credit given by the bank or NBFC at the time of issuing a credit card. Revolving credit limit varies with the financial exposure of the credit cardholder.

3. **Aids payment in domestic and foreign currency**

Credit card aids its cardholder to make payments in any currency of choice. In other words, it gives its holder a unique facility to make payments either in domestic (native) currency or if necessary, also in foreign (non-native) currency, that too as and when required. Credit card reduces the cumbersome process of currency conversion.
4. Record keeping of all transactions

Credit card issuing entities like banks or NBFCs keeps a complete record of all transactions made by their credit cardholders. Such a record helps these entities to raise appropriate billing amounts payable by their cardholders, either on a monthly or some periodic basis.

5. Regular charges

Regular charges are basic routine charges charged by the credit card issuing entity on the usage of credit card by its cardholder. These charges are nominal in nature. The regular charges are primarily classified into two types, viz.,

1. Annual charges, and
2. Additional charges.

6. Grace period

The grace period is referred to those minimum numbers of additional days within which a credit cardholder has to pay his credit card bill without any incurring interest or financial charges.

7. Higher fees on cash withdrawals

Credit-card issuer makes charges on cash withdrawals made through credit card at the ATM outlets and other desks. Generally, cash withdrawal fees are quite higher than fees charged by the bank or NBFC for the other regular credit transactions.

8. Additional charges for delay in payment

The credit card payment is supposed to be made within a due date as mentioned on the bill of a credit card. If payment is not paid on time, then a credit-card issuer charges some additional costs, which are resulted due to delay in payment.

9. Service tax

Service tax is included in the total amount charged to the credit cardholder. This mandatory service tax imposed by the government also increases the final end cost bared by a credit cardholder.

10. Bonus points

The competition among the credit card providers is unbending (adamant). Offering various incentives is usually a trendy (fashionable) way to improve the sale of the products in the ordinary course of business. Following this trend, credit card
providers also give bonus points on the financial value of the transactions compiled by their customers.

At a later stage (i.e. after crossing pre-determined number of bonus points) accumulated bonus points are redeemed either by converting them into gifts, cash back offers, or any other similar compelling offers. To collect many bonus points, the credit cardholder has to carry out a considerable number of transactions through his credit card.

**Elements /parts / anatomy of credit card**

The front side of a credit card shows following details:

1. Logo of issuing entity.
2. Logo of payment processor.
3. Hologram.
4. Expiration date.
5. Cardholder’s name.
6. Card number.
7. Individual account identifier number.
8. Issuer identifier number (IIN).
10. Major industry identifier (MII).
11. Issue date
12. Bank identification number (BIN).

The back side of a credit card shows following details:

1. Security code (card verification number).
3. Signature panel.
4. Additional information.

**Types of Credit Card**

Credit cards now are of various types with different fees, interest rates and rewarding programs. When applying for a credit card, it is important to learn of their diverse types to know the one best suited to their lifestyle and financial status. Different types of credit cards available by banks and other companies/organizations are briefly described below.
1. **Standard Credit Card**: This is the most commonly used. One is allowed to use money up to a certain limit. The account holder has to top up the amount once the level of the balance goes down. An outstanding balance gets a penalty charge.

2. **Premium Credit Card**: This has a much higher bank account and fees. Incentives are offered in this over and above that in a standard card. Credit card holders are offered travel incentives, reward points, cash back and other rewards on the use of this card. This is also called the Reward Credit Card. Some examples are: airlines frequent flier credit card, cash back credit card, automobile manufacturers' rewards credit card. Platinum and Gold, MasterCard and Visa card fall into this category.

3. **Secured Credit Card**: People without credit history or with tarnished credit can avail this card. A security deposit is required amounting to the same as the credit limit. Revolving balance is required according to the 'buying and selling' done.

4. **Limited Purpose Credit Card**: There is limitation to its use and is to be used only for particular applications. This is used for establishing small credits such as gas credits and credit at departmental stores. Minimal charges are levied.

5. **Charge Credit Card**: This requires the card holder to make full payment of the balance every month and therefore there is no limit to credit. Because of the spending flexibility, the card holder is expected to have a higher income level and high credit score. Penalty is incurred if full payment of the balance is not done in time.

6. **Specialty Credit Card**: is used for business purposes enabling businessmen to keep their businesses transactions separately in a convenient way. Charge cards and standard cards are available for this. Also, students enrolled in an accredited 4-year college/university course can avail this benefit.

7. **Prepaid Credit Card**: Here, money is loaded by the card holder on to the card. It is like a debit card except that it is not tied up with a bank account

**Advantages** of credit card

1. They allow you to make purchases on credit without carrying around a lot of cash. This allows you a lot of flexibility.

2. They allow accurate record-keeping by consolidating purchases into a single statement.
3. They allow convenient remote purchasing - ordering/shopping online or by phone. They allow you to pay for large purchases in small, monthly instalments.

4. Under certain circumstances, they allow you to withhold payment for merchandise which proves defective.

5. They are cheaper for short-term borrowing - interest is only paid on the remaining debt, not the full loan amount.

6. Many cards offer additional benefits such as additional insurance cover on purchases, cash back, air miles and discounts on holidays.

**Disadvantages** of credit card

1. You may become an impulsive buyer and tend to overspend because of the ease of using credit cards. Cards can encourage the purchasing of goods and services you cannot really afford.

2. Credit cards are a relatively expensive way of obtaining credit if you don't use them carefully, especially because of the high interest rates and other costs.

3. Lost or stolen cards may result in some unwanted expense and inconvenience.

4. The use of a large number of credit cards can get you even further into debt.

5. Using a credit card, especially remotely, introduces an element of risk as the card details may fall into the wrong hands resulting in fraudulent purchases on the card. Fraudulent or unauthorized charges may take months to dispute, investigate, and resolve.

**Debit card**

A debit card (also known as a bank card or check card) is a plastic card that provides the cardholder electronic access to his or her bank account/s at a financial institution. Some cards have a stored value against which a payment is made, while most relay a message to the cardholder's bank to withdraw funds from a designated account in favour of the payee's designated bank account. The card can be used as an alternative payment method to cash when making purchases. In some cases, the cards are designed exclusively for use on the Internet, and so there is no physical card. In many countries the use of debit cards has become so widespread that their volume of use has overtaken or entirely replaced the check and, in some instances, cash transactions. Like credit cards, debit cards are used widely for telephone and Internet purchases. However, unlike credit cards, the funds paid using a debit card are transferred immediately from the bearer's bank account, instead of having the bearer pay back
the money at a later date. Debit cards usually also allow for instant withdrawal of cash, acting as the ATM card for withdrawing cash and as a check guarantee card. Merchants may also offer cash back facilities to customers, where a customer can withdraw cash along with their purchase.

**Debit card and ATM cards**

Obviously there is a difference between an ATM card and a debit card. An ATM card only allows you to draw cash from your account through an ATM (Automated Teller Machine). A debit card allows you to make financial transactions (purchases mostly) without paying cash. The payment is made by swiping your debit card in a machine at a shop where you made the purchase. The value of your purchase is automatically deducted from your balance in your bank account.

Nowadays, banks provide ATM debit cards, which can be used for both the purposes mentioned above. Similarly, ATM credit cards are also available. A credit card also allows you to make payments on purchases without paying cash. But instead of debiting the value of the purchases to the balance in your bank account after swiping the card at a shop, the bank settles the bill on its own and sends you a statement showing the different transactions entered into by you using your credit card. You have to settle the amount with the bank within a stipulated time. Additionally, credit cards allow you to make cash withdrawals up to certain limits from ATMs using your ATM credit card which has to be repaid within a stipulated period. Obviously credit cards have no relation to your bank balance.

**Differences between Credit card and Debit card**

<table>
<thead>
<tr>
<th></th>
<th>Credit card</th>
<th>Debit card</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>It is a “pay later product”</td>
<td>It is “pay now product”</td>
</tr>
<tr>
<td>2</td>
<td>The card holder can avail of credit for 30-45 days</td>
<td>Customers account is debited immediately</td>
</tr>
<tr>
<td>3</td>
<td>No sophisticated communication system is required for credit card operation</td>
<td>sophisticated communication network/ system is required for debit card operation (eg. ATM)</td>
</tr>
<tr>
<td>4</td>
<td>Opening bank account and maintaining required amount are not essential</td>
<td>Opening bank account and maintaining required amount are essential</td>
</tr>
<tr>
<td>5</td>
<td>Possibility of risk of fraud is high</td>
<td>Risk is minimised through using PIN</td>
</tr>
</tbody>
</table>
MODULE IV
CREDIT RATING

Meaning and Definition

Credit rating is a financial service. Credit rating simply means rating of the credit worthiness of a company by an independent agency. It is an assessment of the capacity of an issuer of debt security, by an independent agency, to pay interest and repay the principal as per the terms of issue of debt. A rating agency collects the qualitative as well as quantitative data relating to a company (which has to be rated) and assesses the relative strength and capacity of company to honour its obligations contained in the debt instrument. Credit rating is an opinion expressed by an independent professional organisation after making a detailed study of all relevant factors. Such an opinion will be of great help to investors in making investment decisions.

According to Moody’s Investor Service, ‘Ratings are designed exclusively for the purpose of grading bonds according to their investment qualities’.

According to CRISIL, “Credit rating is an unbiased and independent opinion as to issuer’s capacity to meet its financial obligations. It does not constitute a recommendation to buy/ sell or hold a particular security”.

Features of Credit Rating

The characteristic features of credit rating are as follows:

1. Credit rating is specific to a debt instrument and not for a company as whole. It is a process of grading and analysis of the credit risk associated with that particular instrument.

2. The rating is based on the relative capacity and willingness of the issuer of the instrument to service debt obligations (principal and interest), in accordance with the terms of the contract.

3. It is only a guidance to the investors and not a recommendation to buy or sell a security.

4. The ratings are expressed in code number (symbols). These are easily understandable by investors.

5. The rating process is based on information supplied by the issuer (of debt security) and also the information collected from various other sources, including personal interactions with various institutions.

6. It is an ongoing appraisal of a security i.e. for the entire life of the security.
Functions of a Credit Rating Agencies

1. Providing an unbiased opinion regarding the capability of a company to service debt obligation.
2. Providing quality information on credit risk.
3. Providing information to investors at a lower cost.
4. Providing true information to investors for taking correct investment decisions.
5. Inducing a healthy discipline on corporate borrowers.

Credit Rating Agencies in India

Some companies may have a good record, goodwill and reputation in the past, but their current state of affairs may not be that bright. Investors in such circumstances felt the need for an independent and credible agency which could judge the debt obligation of different companies and assist investors in making decisions. This need paved the way for the birth of Credit Rating Agencies in India. Presently, there are five leading Credit Rating Agencies (CRAs) approved by the RBI – CRISIL, ICRA, CARE, Fitch Ratings India Private Ltd. and Brickwork Ratings India Private Ltd. These are the five CR agencies registered with SEBI.

We discusses here the three important credit rating agencies in India.

I. Credit Rating Information Services of India Ltd. (CRISIL)

CRISIL is the first credit rating agency in India. It is a public limited company established in 1987 in the private sector. It is promoted jointly by ICICI and UTI. It started its operations on 1st January 1988. Its objectives is to accord credit rating to public limited companies which desire to float share capital, debentures, public deposits or commercial paper to raise finance from the public.

Objectives of CRISIL

Initially CRISIL was set up to rate debt obligations which would guide investors as to the risk of timely payment of interest and principal. Over the years, it aims at following:

1. To assist the investors in making investment decisions in fixed interest securities.
2. To guide the investors in understanding the risk associated with a particular debt instrument.
3. To help the companies raise large funds at a lower cost.
4. To create awareness of the concept of credit rating amongst corporations, merchant bankers, brokers, regulatory bodies.

5. To provide regulators with a market driven system in order to ensure discipline and a healthy growth of capital markets.

Services of CRISIL (Role and Functions of CRISIL)

The services rendered by CRISIL may be summarised as below:

a. **Rating services:** The main business of CRISIL is rating debentures, deposits, preference shares as well as commercial paper. Rating services is also provided to chit funds, real estate developers, banks etc.

b. **Information services:** CRISIL offers information services also. Its main product ‘CRISIL CARD’ provides corporate and balance sheet data for the sake of analysis. It assesses the outlook and solvency of the concerned companies on the basis of published data. CRISIL 500 Equity Index is an index newly launched on the basis of 500 companies representing 74% of market capitalization of the Mumbai Stock Exchange.

c. **Advisory services:** It also offers services to the Governments, banks, financial institutions etc. It provides advisory services in the areas of energy, transport, urban infrastructure, tourism, economy, corporate, capital markets, and financial services. It also undertakes credit and counter party ratings for corporates.

CRISIL provides corporate reports regularly on public sector and private sector companies. These reports contain information on the companies’ financial, business, and technical aspects. It also undertakes industry studies on requests covering topics, such as structure of industry, basis of competition and demand and supply estimates.

CRISIL is the market leader, with a 70% share in the credit rating industry. It is globally the fourth largest and India’s most influential rating agency.

II. Investment Information of Credit Rating Agency of India Ltd. (ICRA)

It is promoted by IFCI Ltd. It started operations in 1991. It offers credit rating services for rating debentures or bonds, preference shares, medium term debts, including certificates of deposits as well as short term instruments including commercial paper. It has entered into an area called Earning Prospects and Risk Analysis. ICRA also provides credit assessment and general assessment.

The primary objective of ICRA is to provide information and guidance to investors/creditors for determining the credit risk associated with a debt
instrument/credit obligation. ICRA Limited is a Public Limited Company, with its shares listed on the Bombay Stock Exchange and the national Stock Exchange. Today, ICRA and its subsidiaries together form the ICRA Group of Companies (Group ICRA).

Objectives of ICRA

1. To provide information and guidance to investors and creditors.
2. To enhance the ability of the borrower/issuer to enter into financial markets for raising resources from a wide range of investing public.
3. To help the regulators in promoting the transparency in the financial markets.
4. To enable the banks, investment bankers and brokers in placing debt with investors by providing them with a marketing tool.

Services/Functions of ICRA

ICRA has a broad-based its services to the corporate and financial sectors, both in India and overseas. It presently offer five types of services: Ratings Services, Information Grading and Research Services, Advisory services, Economic Research and Outsourcing.

1. Rating Services

ICRA rates rupee-denominated debt instruments, such as bonds and debentures (long-term), fixed deposit programmes (medium term), commercial paper and certificates of deposit (short-term), and structured obligations and sector-specific debt obligations (issued by Power, Telecom, and Infrastructure companies).

2. Grading Services

ICRA has developed highly specialised evaluation methodologies for grading of construction entities; real estate developers and projects; healthcare entities; maritime training institutes; and initial public offers (IPOs). These grading methodologies have been developed in association with reputable and specialised bodies, associated with the domain.

3. Advisory Services:

ICRA offers a wide range of management advisory services. These include: (a) strategic counselling, (b) risk management, (c) restructuring solutions, (d) inputs for policy formulation, (e) client specific need based studies in the banking and financial services, manufacturing and services sector etc.
4. Outsourcing:

ICRA Online Ltd, a subsidiary of ICRA, provides technology solution, targeted at distributors of third party financial products, insurance brokers, and stock broking houses. The BPO Division of ICRA Online serves financial service companies, financial institutions, investment banks, private equity and venture capital funds, market researchers and the like. The focus is on high and knowledge processing like financial modelling, data analysis valuation etc.

5. Software development:

ICRA Techno Analysis Ltd., a subsidiary of ICRA offers complete portfolio information technology solutions to meet the dynamic needs of present day businesses. The services range from the traditional development of client server, web-centric and mobile applications to the generation of cutting edge business analysis.

III. Credit Analysis and Research Ltd. (CARE)

It is promoted by the IDBI. It began its operations from October 1993. It offers a wide range of services. Credit rating is conducted for debentures, fixed deposits, commercial papers etc.

CARE ratings are recognised by the Government of India and regulatory agencies in India. It is registered with the Securities and Exchange Board of India (SEBI). The ratings are also recognised by RBI, NABARD, NHB and NSIC. The three largest shareholders of CARE are IDBI Bank, Canara Bank and State Bank of India. CARE s a full service rating company offering a wide range of rating and grading services. These includes rating debt instruments/enterprise ratings of corporates, banks, Financial Institutions (FIs), Public Sector Undertakings (PSUs), state government bodies, municipal corporations, NBFCs, SMEs, microfinance institutions, Structured finance and Securitisation transactions.

Services or Functioning of CARE

CARE ratings are recognised by the Government of India and regulatory agencies in India. It is registered with the Securities and Exchange Board of India (SEBI). The ratings are also recognised by RBI, NABARD, NHB and NSIC.

The services of CARE may be summarised as below:

1. **Credit rating:** It undertakes the credit rating of all types of debt instruments. The rating provides a relative ranking of the credit quality of debt instruments. It also rates quasi-debt obligations such as the ability of insurance companies to meet policy holders' obligations.
2. **Information services**: It makes available information on any company, industry, or sector required by a business enterprise. This information will enable the users to make informed decisions regarding investments.

3. **Advisory services**: It conducts sector studies and provides advisory services in the areas of financial restructuring, valuation and credit appraisal systems.

4. **Equity research**: It conducts the detailed study of the shares listed in the major stock exchanges. On the basis of this study, it can identify the potential winners and losers on the basis of the fundamentals affecting the industry, economy, market share, management capabilities and other relevant factors.

5. **Other services**: It undertakes performance rating of parallel marketers of LPG and Superior Kerosene Oil (SKO) as notified by Central Government. It also provides a valuable input in assisting decision making process in banks and Development Financial Institutions. It has a strong structured finance team and has been instrumental in developing rating methodologies for innovative asset backed securities in the Indian capital market.

The other important credit rating agencies in India are

a. Duff Phelps Credit Rating India Private Ltd. (DCR),
b. Onida Individual Credit Rating Agency Ltd. (ONICRA),
c. Fitch Rating India Pvt. Ltd.,
d. Brick Work Rating India Pvt. Ltd.

**Credit Rating Methods and Mode of Working of Credit Rating Agencies**

Generally the following methodology is adopted for conducting credit rating analysis:

(a) **Business analysis**: In this analysis, industry risk, market share, overall efficiency and legal aspects are all taken into consideration. In case of industry risk, the factors considered and analysed are existing and future demand, number of competitors, expected level of competition in the future cyclical as well as seasonal factors, etc. In the market share analysis, the existing market share of the organization, expected changes in the market share in future, SWOT (strengths, weaknesses, opportunities and threats) analysis of the product of the company, etc., are taken into consideration.

(b) **Financial analysis**: In this area, the overall accounting system, auditor’s certificates, taxation provisions, inventory valuation, depreciation policies, etc., are taken into consideration. Similarly, existing and projected future profitability, cash inflows, ability of the company to repay debt, obligations, cost structure are some of the areas which are analysed.
(c) Managerial evaluation: It another important area where the capabilities of management team are analysed by applying various parameters. This analysis probes into the track record of management, planning and control systems, depth of management talent, succession plans, goals, philosophy and strategies.

Rating Symbols

Different agencies use different symbols for rating securities. Here we give the symbols used by CRISIL only. CRISIL uses the following symbols for rating securities:

A. Long-term Instruments
   (i) High investment grades
      (a) AAA (Triple A): Highest safety
      (b) AA (Double A): High safety
   (ii) Investment grades
      (a) A: Adequate safety
      (b) BBB (Triple B): Moderate safety
   (iii) Speculation grades
      (a) BB (Double B): Inadequate safety
      (b) B: High risk
      (c) C: Substantial risk
      (d) D: Default

B. Medium-term Instruments
   (i) FAAA (F – Triple A): Highest safety
   (ii) FAA (F – Double A): High safety
   (iii) FA: Adequate safety
   (iv) FB: Inadequate safety
   (v) FC: High risk
   (vi) FD: Default

C. Short-term Instruments
   (i) P1: Highest safety
   (ii) P2: High safety
   (iii) P3: Adequate safety
   (iv) P4: Inadequate safety
   (v) P5: Default
Advantages (Importance) of Credit Rating

Credit rating offers advantages to investors, issuers, and to credit rating agencies.

A. Advantages to Investors

1. **Low cost information:** Credit rating provides relevant and reliable information to investors at low cost.

2. **Quick investment decision:** Credit rating enables investors to take quick investment decision on the basis of ratings.

3. **Systematic risk evaluation:** Rating helps the investors to undertake a detailed risk evaluation. It helps the investors to arrive at a meaningful and consistent conclusion regarding the relative credit quality of the security.

4. **Independent investment decision:** The rating symbols suggest the creditworthiness of the instrument and indicate the degree of risk involved in the instrument. Hence the investors can make direct investment decisions. They need not depend upon the advice of financial intermediaries.

5. **Protection:** the creditable and objective rating agency can provide increased disclosure, better accounting standard and improved investor protection.

B. Advantages to Issuers (Rated Companies)

1. **Index of faith:** Credit rating acts as an ideal index of faith placed by the market in the issuers.

2. **Wider investor base:** Rating increases the investor base. This enables the rated companies to raise any amount required at lower cost without difficulty.

3. **Warns risks:** Credit rating acts as a guide to companies scoring lower rating. This enables the management to take steps on their operating and marketing risks. This will change the perception against the companies in the market.

4. **Encourages financial discipline:** Rating encourages discipline among corporate borrowers to improve their financial structure and performance to get better rating.

5. **Foreign collaboration:** The foreign collaborators always ask for credit rating while negotiating with an Indian company. Credit rating enables the foreign collaborators to identify the relative credit standing of the company. Thus the foreign collaboration is made easy.
6. Benefits the industry as a whole: Relatively small and unknown companies use ratings to instill confidence in investors. High rate companies get large amount of money at a lower cost. Thus the industry as a whole can benefit from ratings.

C. Advantages to Intermediaries

1. Easy job: Merchant bankers and brokers will be relieved of the responsibility of guiding investors as to the risk of a particular investment. Their job is just to bring to the attention of their clients the rating of debt securities.

2. Effective monitoring: The stock exchange intermediaries can use ratings as an input for monitoring their risk exposure. Merchant bankers also use credit ratings for pre-packaging issues through asset securitisation/structured obligations.

Limitations of Credit Rating

Credit rating has certain drawbacks. The drawbacks or shortcomings of credit rating are as follows:

1. Only guidance: Rating provides only a guidance to investors in determining the level of risk associated with the debt instrument. It does not recommended the investors/creditors to buy/sell or hold securities.

2. Based on assumptions: Generally the rating is done on the basis of assumptions. In most of the cases, the rating is done on the basis of the information supplied by the issuer themselves. Hence there is a suspicion about the ratings.

3. Competitive ratings: Wherever a firm believes that it is not possible for it to obtain a favourable rating grade; it may try for a much favourable rating. This is possible especially due to competition between a relatively large number of players in the credit rating business.

4. Static study: Rating is a static study of present and past data of a company. A number of factors have direct impact on the working of a company. This may lead to changes in the rating.

5. Difference in rating grades: Same instrument may be rated differently by the two rating agencies. This may confuse the investors.

6. Inefficient staff: If the staffs of credit rating agency are inexperienced or less skilled, then the rating may not be perfect.

SEBI Guidelines Regarding Credit Ratings

SEBI Regulations, 2003 require every credit rating agency to follow the code of conduct as given below:
1. A credit rating agency shall make all efforts to protect the interests of investors.

2. A credit rating agency, in the conduct of its business, shall observe high standards of integrity, dignity and fairness in the conduct of its business.

3. A credit rating agency shall fulfil its obligations in a prompt, ethical and professional manner.

4. A credit rating agency shall at all times exercise due diligence, ensure proper care and exercise independent professional judgement in order to achieve and maintain objectivity and independence in the rating process.

5. A credit rating agency shall have a reasonable and adequate basis for performing rating evaluations, with the support of appropriate and in depth rating researches. It shall also maintain records to support its decisions.

6. A credit rating agency shall have in place a rating process that reflects consistent and international rating standards.

7. A credit rating agency shall not indulge in any unfair competition nor shall it wean away the clients of any other rating agency on assurance of higher rating.

8. A credit rating agency shall keep track of all important changes relating to the client companies and shall develop efficient and responsive systems to yield timely and accurate ratings. Further a credit rating agency shall also monitor closely all relevant factors that might affect the creditworthiness of the issuers.

9. A credit rating agency shall disclose its rating methodology to clients, users and the public.

10. A credit rating agency shall not make any exaggerated statement, whether oral or written to the client either about its qualification or its capability to render certain services or its achievements with regard to the services rendered to other clients.

11. A credit rating agency shall not make any untrue statements, suppress any material fact or make any misrepresentation in any documents, reports, papers or information furnished to the Board, stock exchange or public at large.

12. A credit rating agency shall maintain an appropriate level of knowledge and competence and abide by the provisions of the Act, regulations and circulars, which may be applicable and relevant to the activities carried on by the credit rating agency. The credit rating agency shall also comply with award of the Ombudsman passed under Securities and Exchange Board of India (Ombudsman) Regulations, 2003.
13. A credit rating agency shall ensure that there is no misuse of any privileged information including prior knowledge of rating decisions or changes.

14. A credit rating agency or any of his employees shall not render, directly or indirectly any investment advice about any security in the publicity accessible media.

15. A credit rating agency shall maintain an arm’s length relationship between its credit rating activity and any other activity.

**Leasing**

**Meaning**

Leasing is a process by which a firm can obtain the use of a certain fixed assets for which it must pay a series of contractual, periodic, tax deductible payments. The lessee is the receiver of the services or the assets under the lease contract and the lessor is the owner of the assets. The relationship between the tenant and the landlord is called a tenancy, and can be for a fixed or an indefinite period of time (called the term of the lease). The consideration for the lease is called rent.

Lease can be defined as the following ways:

1. A contract by which one party (lessor) gives to another (lessee) the use and possession of equipment for a specified time and for fixed payments.

2. The document in which this contract is written.

3. A great way companies can conserve capital.

4. An easy way vendors can increase sales.

**The advantages of leasing include:**

a. Leasing helps to possess and use a new piece of machinery or equipment without huge investment.

b. Leasing enables businesses to preserve precious cash reserves.

c. The smaller, regular payments required by a lease agreement enable businesses with limited capital to manage their cash flow more effectively and adapt quickly to changing economic conditions.

d. Leasing also allows businesses to upgrade assets more frequently ensuring they have the latest equipment without having to make further capital outlays.
e. It offers the flexibility of the repayment period being matched to the useful life of the equipment.

f. It gives businesses certainty because asset finance agreements cannot be cancelled by the lenders and repayments are generally fixed.

g. However, they can also be structured to include additional benefits such as servicing of equipment or variable monthly payments depending on a business’s needs.

h. It is easy to access because it is secured – largely or entirely – on the asset being financed, rather than on other personal or business assets.

i. The rental, which sometimes exceeds the purchase price of the asset, can be paid from revenue generated by its use, directly impacting the lessee's liquidity.

j. Lease instalments are exclusively material costs.

k. Using the purchase option, the lessee can acquire the leased asset at a lower price, as they pay the residual or non-depreciated value of the asset.

l. For the national economy, this way of financing allows access to state-of-the-art technology otherwise unavailable, due to high prices, and often impossible to acquire by loan arrangements.

Limitation of leasing

a. It is not a suitable mode of project financing because rental is payable soon after entering into lease agreement while new project generate cash only after long gestation period.

b. Certain tax benefits/ incentives/subsidies etc. May not be available to leased equipments.

c. The value of real assets (land and building) may increase during lease period. In this case lessee may lose potential capital gain.

d. The cost of financing is generally higher than that of debt financing.

e. A manufacturer(lessee) who want to discontinue business need to pay huge penalty to lessor for pre-closing lease agreement

f. There is no exclusive law for regulating leasing transaction.

g. In undeveloped legal systems, lease arrangements can result in inequality between the parties due to the lessor's economic dominance, which may lead to the lessee signing an unfavourable contract.
TYPES OF LEASE

(a) Financial lease
(b) Operating lease.
(c) Sale and lease back
(d) Leveraged leasing and
(e) Direct leasing.

1) Financial lease

Long-term, non-cancellable lease contracts are known as financial leases. The essential point of financial lease agreement is that it contains a condition whereby the lessor agrees to transfer the title for the asset at the end of the lease period at a nominal cost. At lease it must give an option to the lessee to purchase the asset he has used at the expiry of the lease. Under this lease the lessor recovers 90% of the fair value of the asset as lease rentals and the lease period is 75% of the economic life of the asset. The lease agreement is irrevocable. Practically all the risks incidental to the asset ownership and all the benefits arising there from are transferred to the lessee who bears the cost of maintenance, insurance and repairs. Only title deeds remain with the lessor. Financial lease is also known as 'capital lease'. In India, financial leases are very popular with high-cost and high technology equipment.

2) Operational lease

An operating lease stands in contrast to the financial lease in almost all aspects. This lease agreement gives to the lessee only a limited right to use the asset. The lessor is responsible for the upkeep and maintenance of the asset. The lessee is not given any uplift to purchase the asset at the end of the lease period. Normally the lease is for a short period and even otherwise is revocable at a short notice. Mines, Computers hardware, trucks and automobiles are found suitable for operating lease because the rate of obsolescence is very high in this kind of assets.

3) Sale and lease back

It is a sub-part of finance lease. Under this, the owner of an asset sells the asset to a party (the buyer), who in turn leases back the same asset to the owner in consideration of lease rentals. However, under this arrangement, the assets are not physically exchanged but it all happens in records only. This is nothing but a paper transaction. Sale and lease back transaction is suitable for those assets, which are not subjected depreciation but appreciation, say land. The advantage of this method is that the lessee can satisfy himself completely regarding the quality of the asset and after possession of the asset convert the sale into a lease arrangement.
4) Leveraged leasing

Under leveraged leasing arrangement, a third party is involved beside lessor and lessee. The lessor borrows a part of the purchase cost (say 80%) of the asset from the third party i.e., lender and the asset so purchased is held as security against the loan. The lender is paid off from the lease rentals directly by the lessee and the surplus after meeting the claims of the lender goes to the lessor. The lessor, the owner of the asset is entitled to depreciation allowance associated with the asset.

5) Direct leasing

Under direct leasing, a firm acquires the right to use an asset from the manufacturer directly. The ownership of the asset leased out remains with the manufacturer itself. The major types of direct lessor include manufacturers, finance companies, independent lease companies, special purpose leasing companies etc

Other types of leasing:

1) First Amendment Lease: The first amendment lease gives the lessee a purchase option at one or more defined points with a requirement that the lessee renew or continue the lease if the purchase option is not exercised. The option price is usually either a fixed price intended to approximate fair market value or is defined as fair market value determined by lessee appraisal and subject to a floor to insure that the lessor's residual position will be covered if the purchase option is exercised.

2) Full Payout Lease: A lease in which the lessor recovers, through the lease payments, all costs incurred in the lease plus an acceptable rate of return, without any reliance upon the leased equipment's future residual value.

3) Guideline Lease: A lease written under criteria established by the IRS to determine the availability of tax benefits to the lessor.

4) Net Lease: A lease wherein payments to the lessor do not include insurance and maintenance, which are paid separately by the lessee.

5) Open-end Lease: A conditional sale lease in which the lessee guarantees that the lessor will realize a minimum value from the sale of the asset at the end of the lease.

6) Sales-type Lease: A lease by a lessor who is the manufacturer or dealer, in which the lease meets the definitional criteria of a capital lease or direct financing lease.
7) Synthetic Lease: A synthetic lease is basically a financing structured to be treated as a lease for accounting purposes, but as a loan for tax purposes. The structure is used by corporations that are seeking off-balance sheet reporting of their asset based financing, and that can efficiently use the tax benefits of owning the financed asset.

8) Tax Lease: A lease wherein the lessor recognizes the tax incentives provided by the tax laws for investment and ownership of equipment. Generally, the lease rate factor on tax leases is reduced to reflect the lessor's recognition of this tax incentive.

9) True Lease: A type of transaction that qualifies as a lease under the Internal Revenue Code. It allows the lessor to claim ownership and the lessee to claim rental payments as tax deductions.

**Differences between financial lease and operating lease**

1. While financial lease is a long term arrangement between the lessee (user of the asset) and the owner of the asset, whereas operating lease is a relatively short term arrangement between the lessee and the owner of asset.

2. Under financial lease all expenses such as taxes, insurance are paid by the lessee while under operating lease all expenses are paid by the owner of the asset.

3. The lease term under financial lease covers the entire economic life of the asset which is not the case under operating lease.

4. Under financial lease the lessee cannot terminate or end the lease unless otherwise provided in the contract which is not the case with operating lease where lessee can end the lease anytime before expiration date of lease.

5. While the rent which is paid by the lessee under financial lease is enough to fully amortize the asset, which is not the case under operating lease.

**Regulatory framework for Leasing in India**

As there is no separate statute for leasing in India, the provisions relating to bailment in the Indian Contract Act govern equipment leasing agreements as well section 148 of the Indian Contract Act defines bailment as:

“The delivery of goods by one person to another, for some purpose, upon a contract that they shall, when the purpose is accomplished, be returned or otherwise disposed off according to the directions of the person delivering them. The person delivering the goods is called the 'bailor' and the person to whom they are delivered is called the 'bailee'.

Indian Financial System
Since an equipment lease transaction is regarded as a contract of bailment, the obligations of the lessor and the lessee are similar to those of the bailor and the bailee (other than those expressly specified in the lease contract) as defined by the provisions of sections 150 and 168 of the Indian Contract Act. Essentially these provisions have the following implications for the lessor and the lessee.

1. The lessor has the duty to deliver the asset to the lessee, to legally authorise the lessee to use the asset, and to leave the asset in peaceful possession of the lessee during the currency of the agreement.

2. The lessor has the obligation to pay the lease rentals as specified in the lease agreement, to protect the lessor’s title, to take reasonable care of the asset, and to return the leased asset on the expiry of the lease period.

Contents of a lease agreement: The lease agreement specifies the legal rights and obligations of the lessor and the lessee. It typically contains terms relating to the following:

1. Description of the lessor, the lessee, and the equipment.
2. Amount, time and place of lease rentals payments.
3. Time and place of equipment delivery.
4. Lessee’s responsibility for taking delivery and possession of the leased equipment.
5. Lessee’s responsibility for maintenance, repairs, registration, etc. and the lessor’s right in case of default by the lessee.
6. Lessee’s right to enjoy the benefits of the warranties provided by the equipment manufacturer/supplier.
7. Insurance to be taken by the lessee on behalf of the lessor.
8. Variation in lease rentals if there is a change in certain external factors like bank interest rates, depreciation rates, and fiscal incentives.
9. Options of lease renewal for the lessee.
10. Return of equipment on expiry of the lease period.
11. Arbitration procedure in the event of dispute.
MODULE V
STOCK EXCHANGES

Meaning of Secondary Market

Secondary market is a market for old issues. It deals with the buying and selling existing securities i.e. securities already issued. In other words, securities already issued in the primary market are traded in the secondary market. Secondary market is also known as stock market. The secondary market operates through ‘stock exchanges’.

In India, stock market consists of recognised stock exchanges. In the stock exchanges, securities issued by the central and state governments, public bodies, and joint stock companies are traded.

Stock Exchange

In India the first organized stock exchange was Bombay Stock Exchange. It was started in 1877. Later on, the Ahmadabad Stock Exchange and Calcutta Stock Exchange were started in 1894 and 1908 respectively. At present there are 24 stock exchanges in India. In Europe, stock exchanges are often called bourses.

Meaning and Definition of Stock Exchange/ Security Exchange

It is an organized market for the purchase and sale of securities of joint stock companies, government and semi- govt. bodies. It is the centre where shares, debentures and govt. securities are bought and sold.

According to Pyle, “Security exchanges are market places where securities that have been listed thereon may be bought and sold for either investment or speculation”.

The Securities Contract (Regulation) Act 1956, defines a stock exchange as “an association, organiastion or body of individuals whether incorporated or not, established for the purpose of assisting, regulating and controlling of business in buying, selling and dealing in securities”.

In short, stock exchange is a place or market where the listed securities are bought and sold.

Characteristics of a Stock Exchange

1. It is an organized capital market.

2. It may be incorporated or non-incorporated body (association or body of individuals).
3. It is an open market for the purchase and sale of securities.

4. Only listed securities can be dealt on a stock exchange.

5. It works under established rules and regulations.

6. The securities are bought and sold either for investment or for speculative purpose.

**Economic Functions of Stock Exchange**

The stock exchange performs the following essential economic functions:

1. **Ensures liquidity to capital:** The stock exchange provides a place where shares and stocks are converted into cash. People with surplus cash can invest in securities (by buying securities) and people with deficit cash can sell their securities to convert them into cash.

2. **Continuous market for securities:** It provides a continuous and ready market for buying and selling securities. It provides a ready market for those who wish to buy and sell securities.

3. **Mobilisation of savings:** It helps in mobilizing savings and surplus funds of individuals, firms and other institutions. It directs the flow of capital in the most profitable channel.

4. **Capital formation:** The stock exchange publishes the correct prices of various securities. Thus the people will invest in those securities which yield higher returns. It promotes the habit of saving and investment among the public. In this way the stock exchange facilitates the capital formation in the country.

5. **Evaluation of securities:** The prices at which transactions take place are recorded and made public in the forms of market quotations. From the price quotations, the investors can evaluate the worth of their holdings.

6. **Economic developments:** It promotes industrial growth and economic development of the country by encouraging industrial investments. New and existing concerns raise their capital through stock exchanges.

7. **Safeguards for investors:** Investors' interests are very much protected by the stock exchange. The brokers have to transact their business strictly according to the rules prescribed by the stock exchange. Hence they cannot overcharge the investors.

8. **Barometer of economic conditions:** Stock exchange reflects the changes taking place in the country’s economy. Just as the weather clock tells us which way the wind is blowing, in the same way stock exchange serves as an indicator of the phases in business cycle - boom, depression, recessions and recovery.
9. **Platform for public debt:** The govt. has to raise huge funds for the development activities. Stock exchange acts as markets of govt. securities. Thus, stock exchange provides a platform for raising public debt.

10. **Helps to banks:** Stock exchange helps the banks to maintain liquidity by increasing the volume of easily marketable securities.

11. **Pricing of securities:** New issues of outstanding securities in the primary market are based on the prices in the stock exchange. Thus, it helps in pricing of securities.

Thus stock exchange is of great importance to a country. It provides necessary mobility to capital. It directs the flow of capital into profitable and successful enterprises. It is indispensable for the proper functioning of corporate enterprises. Without stock exchange, even govt. would find it difficult to borrow for its various schemes. It helps the traders, investors, industrialists and the banker. Hence, it is described as the business of business.

**Benefits of Stock Exchange**

Stock exchange offers the following benefits:

A. Benefits to Investors
   a. The stock exchange plays the role of a friend, philosopher and guide to investors by providing information about the prices of various securities.
   b. It offers a ready market for buying and selling securities.
   c. It increases the liquidity of the investors.
   d. It safeguards the interests of investors through strict rules and regulations.
   e. It enables the investors to know the present worth of their securities.
   f. It helps investors in making wise investment decisions by providing useful information about the financial position of the companies.
   g. The holder of a listed security can easily raise loan by pledging it as a collateral security.

B. Benefits to Companies
   a. A company enjoys greater reputation and credit in the market. Image of the company goes up.
   b. A company can raise large amount of capital from different types of securities.
   c. It enjoys market for its shares.
d. The market price for shares and debentures will be higher. Due to this the bargaining power of the company increases in the events of merger or amalgamation.

C. Benefits to Community and Nation

a. Stock exchange encourages people to sell and invest their savings in shares and debentures.

b. Through capital formation, stock exchange enables companies to undertake expansion and modernization. Stock exchange is an ‘Alibaba Cave’ from which business community draw unlimited money.

c. It helps the government in raising funds through sale of government securities. This enables the government to undertake projects of national importance and social value.

d. It diverts the savings towards productive channels.

e. It helps in better utilisation of the country’s financial resources.

f. It is an effective indicator of general economic conditions of a country.

Listing of Securities

Listing of securities means permission to quote shares and debentures officially on the trading floor of the stock exchange. Listing of securities refers to the sanction of the right to trade the securities on the stock exchange. In short, listing means admission of securities to be traded on the stock exchange. If the securities are not listed, they are not allowed to be traded on the stock exchange.

Advantages of Listing

A. Advantages to Company:

a. It provides continuous market for securities (securities include shares, debentures, bonds etc.)

b. It enhances liquidity of securities.

c. It enhances prestige of the company.

d. It ensures wide publicity.

e. Raising of capital becomes easy.

f. It gives some tax advantage to the company.
B. Advantages to Investors:

a. It provides safety of dealings.

b. It facilitates quick disposal of securities in times of need. This means that listing enhances the liquidity of securities.

c. It gives some tax advantage to the security holder.

d. Listed securities command higher collateral value for the purpose of bank loans.

e. It provides an indirect check against manipulation by the management.

Disadvantages of Listing

a. It leads to speculation

b. Sometimes listed securities are subjected to wide fluctuations in their value. This may degrade the company’s reputation.

c. It discloses vital information such as dividends and bonus declared etc. to competitors.

d. Company has to spend heavily in the process of placing the securities with public

Classification of Listed Securities

The listed shares are generally divided into two categories - Group A shares (cleared securities) and Group B shares (non-cleared securities). Group A shares represent large and well established companies having a broad investor base. These shares are actively traded. Forward trading is allowed in Group A shares. These facilities are not available to Group B shares. These are not actively traded. Carry forward facility is not available in case of these securities.

Procedure for Dealing at Stock Exchange (Trading Mechanism or Method of Trading on a Stock Exchange)

Outsiders are not allowed to buy or sell securities at a stock exchange. They have to approach brokers. Dealings can be done only through brokers. They are the members of the stock exchange. The following procedure is followed for dealing at exchanges:

a. Selection of a broker: An individual cannot buy or sell securities directly at stock exchange. He can do so only through a broker. So he has to select a broker through whom the purchase or sale is to be made. The intending investor or seller may appoint his bank for this purpose. The bank may help to choose the broker.
b. **Placing an order:** After selecting the broker, the next step is to place an order for purchase or sale of securities. The broker also guides the client about the type of securities to be purchased and the proper time for it. If a client is to sell the securities, then the broker shall tell him about the favourable time for sale.

c. **Making the contract:** The trading floor of the stock exchange is divided into different parts known as trading posts. Different posts deal in different types of securities. The authorised clerk of the broker goes to the concerned post and expresses his intention to buy and sell the securities. A deal is struck when the other party also agrees. The bargain is noted by both the parties in their note books. As soon as order is executed a confirmation memo is prepared and is given to the client.

d. **Contract Note:** After issue of confirmation memo, a contract note is signed between the broker and the client. This contract note will state the transaction fees (commission of broker), number of shares bought or sold, price at which they are bought or sold, etc.

e. **Settlement:** Settlement involves making payment to sellers of shares and delivery of share certificate to the buyer of shares after receiving the price. The settlement procedure depends upon the nature of the transactions. All the transactions on the stock exchange may be classified into two - ready delivery contracts and forward delivery contracts.

   *Ready delivery contract:* A ready delivery contract involves the actual payment of the amount by the buyer in cash and the delivery of securities by the seller. A ready delivery contract is to be settled on the same day or within the time period fixed by the stock exchange authorities.

   *Forward delivery contracts:* These contracts are entered into without any intention of taking and giving delivery of the securities. The traders in forward delivery securities are interested in profits out of price variations in the future. Such transactions are settled on the settlement days fixed by the stock exchange authorities. Such contracts can be postponed to the next settlement day, if both the parties agree between themselves. Such postponement is called ‘Carry over’ or ‘badla’. Thus ‘carry over’ or ‘badla’ means the postponement of transaction from one settlement period to the next settlement period.

**Rolling Settlement**

Rolling settlement has been introduced in the place of account period settlement. Rolling settlement system was introduced by SEBI in January 1998. Under this system of settlement, the trades executed on a certain day are settled
based on the net obligations for that day. At present, the trades relating to the rolling settlement are settled on T + 2day basis where T stands for the trade day. It implies that the trades executed on the first day (say on Monday) have to be settled on the 3rd day (on Wednesday), i.e., after a gap of 2 days.

This cycle would be rolling and hence there would be number of set of transactions for delivery every day. As each day’s transaction are settled in full, rolling settlement helps in increasing the liquidity in the market. With effect from January 2, 2002, all scrips have been brought under compulsory rolling mode.

Members in a Stock Exchange

Only members of the exchange are allowed to do business of buying and selling of securities at the floor of the stock exchange. A non-member (client) can buy and sell securities only through a broker who is a member of the stock exchange. To deal in securities on recognised stock exchanges, the broker should register his name as a broker with the SEBI.

Types of Members in a Stock Exchange

- **Jobbers**: They are dealers in securities in a stock exchange. They cannot deal on behalf of public. They purchase and sell securities on their own names. Their main job is to earn profit due to price variations.

- **Commission brokers**: They are nothing but brokers. They buy and sell securities no behalf of their clients for a commission. They are permitted to deal with non-members directly. They do not purchase or sell in their own name.

- **Tarawaniwalas**: They are like jobbers. They handle transactions on a commission basis for their brokers. They buy and sell securities on their own account and may act as brokers on behalf of the public.

- **Sub-brokers**: Sub brokers are agents of stock brokers. They are employed by brokers to obtain business. They cannot carry on business in their own name. They are also known as Remisiers.

- **Arbitrageurs**: They are brokers. They buy security in one market and sell the same in another market to get opportunistic profit.

- **Authorised clerks**: Authorised clerks are those who are appointed by stock brokers to assist them in the business of securities trading.
Speculation

Speculation takes place in the forward market. Speculation means buying and selling of financial instruments (including foreign exchange) with the expectation of a profit from anticipated changes in the price of securities or foreign exchange rates. It simply means taking a foreign exchange risk in hope of making profit. One who is engaged in speculation is called speculator. His success or failure depends upon how correctly he is able to anticipate the exchange rate variations.

Type of Speculators

1. **Bull**: A bull or Tejiwala is a speculator who buys shares in expectation of selling them at higher prices in future. He believes that current prices are lower and will rise in the future.

2. **Bear**: A bear or Mandiwala is a speculator who sells securities with the intention to buy at a later date at a lower price. He expects a fall in price in future.

3. **Lame duck**: A lame duck is a bear speculator. He finds it difficult to meet his commitments and struggles like a lame duck. This happens because of the non-availability of securities in the market which he has agreed to sell and at the same time the other party is not willing to postpone the transaction.

4. **Stag**: Stag is a member who neither buys nor sells securities. He applies for shares in the new issue market. He expects that the price of shares will soon increase and the shares can be sold for a premium.

5. **Wolf**: Wolf is a broker who is fast speculator. He is very quick to perceive changes in the market trends and trade fast and make fast profit.

Speculative Transactions

Some of the speculative dealings are as follows:

1) **Option deals**: This is an arrangement or right to buy or sell securities at a predetermined price on or before a specified date in future.

2) **Wash sales**: It is a device through which a speculator is able to reap huge profits by creating a misleading picture in the market. It is a kind of fictitious transaction in which a speculator sells a security and then buys the same at a higher price through another broker. Thus he creates a false or misleading opinion in the market about the price of a security.
3) **Rigging**: If refers to the process of creating an artificial condition in the market whereby the market value of a particular security is pushed upon. Bulls buy securities, create demand for the same and sell them at increased prices.

4) **Arbitrage**: It is the process of buying a security, from a market where price is lower and selling at in another market where price is higher.

5) **Cornering**: Sometimes speculators make entire or a major share of supply of a particular security with a view to create a scarcity against the existing contracts. This is called cornering.

6) **Blank transfer**: When the transferor (seller) simply signs the transfer form without specifying the name of the transferee (buyer), it is called blank transfer. In this case share can further be transferred by mere delivery of transfer deed together with the share certificate. A new transfer deed is not required at the time of each transfer. Hence, expenses such as registration fees, stamp duty, etc can be saved.

7) **Margin trading**: Under this method, the client opens an account with his broker. The client makes a deposit of cash or securities in this account. He also agrees to maintain a minimum margin of amount always in his account. When a broker purchases securities on behalf of his client, his account (client’s account) will be debited and vice versa. The debit balance, if any, is automatically secured by the client’s securities lying with the broker. In case it falls short of the minimum agreed amount, the client has to deposit further amount into his account or he has to deposit further securities. If the prices are favourable, the client may instruct his broker to sell the securities. When such securities are sold, his account will be credited. The client may have a bigger margin now for further purchases.

**Factors Influencing Prices on Stock Exchange**

The prices on stock exchange depends upon the following factors:

- a. Financial position of the company
- b. Demand and supply position
- c. Lending rates
- d. Attitudes of the FIIs and the developments in the global financial markets.
- e. Govt. Policies (credit policies, monetary policies, taxation policies etc.)
- f. Trade cycle
- g. Speculation activities
Defects of Stock Exchanges (or Capital Market) in India

The Indian stock market is suffering from a number of weaknesses. Important weaknesses are as follows:

1. **Speculative activities**: Most of the transactions in stock exchange are carry forward transactions with a speculative motive of deriving benefit from short term price fluctuation. Genuine transactions are only less.

2. **Insider trading**: Insider trading has been a routine practice in India. Insiders are those who have access to unpublished price-sensitive information. By virtue of their position in the company they use such information for their own benefits.

3. **Poor liquidity**: The Indian stock exchanges suffer from poor liquidity. Though there are approximately 8000 listed companies in India, the securities of only a few companies are actively traded. Only that securities are liquid. This means other stocks have very low liquidity.

4. **Less floating securities**: There is scarcity of floating securities in the Indian stock exchanges. Out of the total stocks, only a small portion is being offered for sale. The financial institutions and joint stock companies control over 75% of the scrips. However, they do not offer their holdings for sale. The UTI, GIC, LIC etc. indulge more in purchasing than in selling. This creates scarcity of stocks for trading.

5. **Lack of transparency**: Many brokers are violating the regulations with a view to cheating the innocent investing community. No information is available to investors regarding the volume of transactions carried out at the highest and lowest prices.

6. **High volatility**: The Indian stock market is subject to high volatility in recent years. The stock prices fluctuate from hour to hour. High volatility is not conducive for the smooth functioning of the stock market.

7. **Dominance of financial institutions**: The Indian stock market is being dominated by few financial institutions like UTI, LIC, GIC etc. This means these few institutions can influence stock market greatly.

8. **Competition of merchant bankers**: The increasing number of merchant bankers in the stock market has led to unhealthy competition in the stock market.

9. **Lack of professionalism**: Some of the brokers are highly competent and professional. At the same time, majority of the brokers are not so professional. They lack proper education, business skills, infrastructure facilities etc.
Difference between Primary and Secondary Market

<table>
<thead>
<tr>
<th>Primary Market</th>
<th>Secondary Market</th>
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<tbody>
<tr>
<td>A. It is a market for new securities.</td>
<td>A. It is a market for existing or second hand securities</td>
</tr>
<tr>
<td>B. It is directly promotes capital formation.</td>
<td>B. It is directly promotes capital formation.</td>
</tr>
<tr>
<td>C. Investors can only buy securities. They cannot sell them.</td>
<td>C. Both buying and selling of securities takes place</td>
</tr>
<tr>
<td>D. There is no fixed geographical location.</td>
<td>D. There is a fixed geographical location (stock exchanges)</td>
</tr>
<tr>
<td>E. Securities need not be listed.</td>
<td>E. Only listed securities can be bought and sold</td>
</tr>
<tr>
<td>F. It enables the borrowers to raise capital</td>
<td>F. It enables the investors to invest money in securities and sell and encash as they need money</td>
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Major stock exchanges in India

1. Bombay Stock Exchange (BSE)

BSE is the leading and the oldest stock exchange in India as well as in Asia. It was established in 1887 with the formation of "The Native Share and Stock Brokers' Association". BSE is a very active stock exchange with highest number of listed securities in India. Nearly 70% to 80% of all transactions in the India are done alone in BSE. Companies traded on BSE were 3,049 by March, 2006. BSE is now a national stock exchange as the BSE has started allowing its members to set-up computer terminals outside the city of Mumbai (former Bombay). It is the only stock exchange in India which is given permanent recognition by the government.

Some important facts about BSE:

- BSE exchange was the first in India to launch Equity Derivatives, Free Float Index, USD adaptation of BSE Sensex and Exchange facilitated Internet buying and selling policy
- BSE exchange was the first in India to acquire the ISO authorization for supervision, clearance & Settlement
- BSE exchange was the first in India to have launched private service for economic training
- Its On-Line Trading System has been felicitated by the internationally renowned standard of Information Security Management System.
Bombay Online Trading System (BOLT)

BSE online trading was established in 1995 and is the first exchange to be set up in Asia. It has the largest number of listed companies in the world and currently has 4937 companies listed on the Exchange with over 7,700 traded instruments. BSE introduced online trading system

The only thing that an investor requires for online trading through BSE is an online trading account. The trading can then be done within the trading hours from any location in the world. In fact, BSE has replaced the open cry system with automated trading. Open cry system is a common method of communication between the investors at a stock exchange where they shout and use hand gestures to communicate and transfer information about buy and sell orders. It usually takes place on the 'pit' area of the trading floor and involves a lot of face to face interaction. However, with the use of electronic trading systems trading is easier, faster and cheaper; and is less prone to manipulation by market makers and brokers/dealers.

2. National Stock Exchange (NSE)

Formation of National Stock Exchange of India Limited (NSE) in 1992 is one important development in the Indian capital market. The need was felt by the industry and investing community since 1991. The NSE is slowly becoming the leading stock exchange in terms of technology, systems and practices in due course of time. NSE is the largest and most modern stock exchange in India. In addition, it is the third largest exchange in the world next to two exchanges operating in the USA.

The NSE boasts of screen based trading system. In the NSE, the available system provides complete market transparency of trading operations to both trading members and the participates and finds a suitable match. The NSE does not have trading floors as in conventional stock exchanges. The trading is entirely screen based with automated order machine. The screen provides entire market information at the press of a button. 3 segments of NSE are:

- Wholesale debt market segment,
- Capital market segment, and
- Futures & options trading.

NSE uses satellite communication expertise to strengthen contribution from around 400 Indian cities. It is one of the biggest VSAT incorporated stock exchange across the world.
3. Over the Counter Exchange of India (OTCEI)

The OTCEI was incorporated in October, 1990 as a Company under the Companies Act 1956. It became fully operational in 1992 with opening of a counter at Mumbai. It is recognised by the Government of India as a recognised stock exchange under the Securities Control and Regulation Act 1956. It was promoted jointly by the financial institutions like UTI, ICICI, IDBI, LIC, GIC, SBI, IFCI, etc.

The Features of OTCEI are:-
1. OTCEI is a floorless exchange where all the activities are fully computerised.
2. Its promoters have been designated as sponsor members and they alone are entitled to sponsor a company for listing there.
3. Trading on the OTCEI takes place through a network of computers or OTC dealers located at different places within the same city and even across the cities. These computers allow dealers to quote, query & transact through a central OTC computer using the telecommunication links.
4. A Company which is listed on any other recognised stock exchange in India is not permitted simultaneously for listing on OTCEI.
5. OTCEI deals in equity shares, preference shares, bonds, debentures and warrants.

OTC Exchange Of India designed trading in debt instruments commonly known as PSU bonds and also in the equity shares of unlisted companies.

STOCK INDICES

The stock market index is a barometer of market behaviour. It functions as an indicator of the general economic scenario of a country. If stock market indices are growing, it indicates that the overall general economy of country is stable if however the index goes down it shows some trouble in economy.

Construction of Stock Index. A stock index is created by choosing high performing stocks. Index can be calculated by two ways by considering the price of component stock alone. By considering the market value or size of the company called market capitalization method. Two main stock index of India are Sensex and Nifty.

Any of the following methods can be used for calculating index

a. Weighted capitalisation method - full market capitalisation and free float market capitalisation.

b. Price weighted index method

c. Equal weighting method
The important indices in India:

1. BSE Sensex
2. S&P CNX Nifty
3. S&P CNX 500
4. BSE 500
5. BSE 100
6. BSE 200/Dollex
7. BSE IT
8. BSE CG
9. BSE FMCG
10. S&P CNX Defty

**BSE SENSEX**

The 'BSE Sensex' or 'Bombay Stock Exchange' is value-weighted index composed of 30 stocks and was started in January 1, 1986. The Sensex is regarded as the pulse of the domestic stock markets in India. It consists of the 30 largest and most actively traded stocks, representative of various sectors, on the Bombay Stock Exchange. These companies account for around fifty per cent of the market capitalization of the BSE

**S&P CNX NIFTY**

The Standard & Poor's CRISIL NSE Index 50 or S&P CNX Nifty nicknamed Nifty 50 or simply Nifty (NSE: ^NSEI), is the leading index for large companies on the National Stock Exchange of India. The Nifty is a well diversified 50 stock index accounting for 23 sectors of the economy. It is used for a variety of purposes such as benchmarking fund portfolios, index based derivatives and index funds. Nifty is owned and managed by India Index Services and Products Ltd. (IISL), which is a joint venture between NSE and CRISIL. IISL is India's first specialized company focused upon the index as a core product. IISL has a marketing and licensing agreement with Standard & Poor's.

**Insurance**

Insurance is a contract between two parties. One party is the insured and the other party is the insurer. Insured is the person whose life or property is insured with
the insurer. That is, the person whose risks are insured is called insured. Insurer is
the insurance company to whom risk is transferred by the insured. That is, the person
who insures the risk of insured is called insurer. Thus insurance is a contract between
insurer and insured. It is a contract in which the insurance company undertakes to
indemnify the insured on the happening of certain event for a payment of
consideration. It is a contract between the insurer and insured under which the
insurer undertakes to compensate the insured for the loss arising from the risk
insured against.

According to Mc Gill, “Insurance is a process in which uncertainties are made
certain”. In the words of Jon Megi, “Insurance is a plan wherein persons collectively
share the losses of risks”.

Thus, insurance is a device by which a loss likely to be caused by uncertain
event is spread over a large number of persons who are exposed to it and who
voluntarily join themselves against such an event. The document which contains all
the terms and conditions of insurance (i.e. the written contract) is called the
‘insurance policy’. The amount for which the insurance policy is taken is called ‘sum
assured’. The consideration in return for which the insurer agrees to make good the
loss is known as ‘insurance premium’. This premium is to be paid regularly by the
insured. It may be paid monthly, quarterly, half yearly or yearly.

Nature and Characteristics of Insurance

Insurance follows important characteristics – These are follows

1. Sharing of risk

   Insurance is a co-operative device to share the burden of risk, which may fall on
happening of some unforeseen events, such as the death of head of family or on
happening of marine perils or loss of by fire.

2. co-operative device

   Insurance is a co-operative form of distributing a certain risk over a group of
persons who are exposed to it. A large number of persons share the losses arising
from a particular risk.

3. Large number of insured persons

   The success of insurance business depends on the large number of persons Insured
against similar risk. This will enable the insurer to spread the losses of risk among
large number of persons, thus keeping the premium rate at the minimum.
4. **Evaluation of risk**

For the purpose of ascertaining the insurance premium, the volume of risk is evaluated, which forms the basis of insurance contract.

5. **Payment of happening of specified event**

On happening of specified event, the insurance company is bound to make payment to the insured. Happening of specified event is certain in life insurance, but in the case of fire, marine of accidental insurance, it is not necessary. In such cases, the insurer is not liable for payment of indemnity.

6. **Transfer of risk**

Insurance is a plan in which the insured transfers his risk on the insurer. This may be the reason that may person observes, that insurance is a device to transfer some economic losses would have been borne by the insured themselves.

7. **Spreading of risk**

Insurance is a plan which spread the risk & losses of few people among a large number of people. John Magee writes, “Insurance is a plan by which large number of people associates themselves and transfers to the shoulders of all, risk attached to Individuals”.

8. **Protection against risks**

Insurance provides protection against risk involved in life, materials and property. It is a device to avoid or reduce risks.

9. **Insurance is not charity**

Charity pays without consideration but in the case of insurance, premium is paid by the insured to the insurer in consideration of future payment.

10. **Insurance is not a gambling**

Insurance is not a gambling. Gambling is illegal, which gives gain to one party and loss to other. Insurance is a valid contract to indemnity against losses. Moreover, Insurable interest is present in insurance contracts it has the element of investment also.

11. **A contract**

Insurance is a legal contract between the insurer and insured under which the Insurer promises to compensate the insured financially within the scope of insurance Policy, the insured promises to pay a fixed rate of premium to the insurer.
12. Social device

Insurance is a plan of social welfare and protection of interest of the people. Rieg and miller observe “insurance is of social nature”.

13. Based upon certain principle

Insurance is a contract based upon certain fundamental principles of insurance, which includes utmost good faith, insurable interest, contribution, indemnity, causa Proxima, subrogation etc, which are operating in the various fields of insurance.

14. Regulation under the law

The government of every country enacts the law governing insurance business So as to regulate, and control its activities for the interest of the people. In India General insurance act 1972 and the life insurance act 1956 are the major enactment in this direction.

15. Insurance is for pure risk only

Pure risks give only losses to the insured, and no profits. Examples of pure Risks are accident, misfortune, death, fire, injury, etc., which are all the sided risks and the ultimate

Importance of insurance

Insurance plays significant role for not only an individual or for not only an individual or for a family but it has spread over the entire nervous system of the nation. Not only does is serve the ends of individuals, it tends more and more both to pervade and transform our modern social order.

According to the author, Dins dale, “No one in modern world can afford to be without insurance.”

Insurance provides various advantages to various fields. We can classify the importance as under

I individual aspects:

For an individual, the importance of insurance is laying in the following points:

1. Security for health and property
2. Encourage savings
3. Encourage the habit of forced thrift
4. Provide mental peace
5. Increase efficiency
6. Provision for the future
7. Awareness for the future
8. Credit Facility
9. Tax exemption
10. Contribution to the conservation of health
11. Cover for legal liability
12. Security to the mortgaged property
13. Poster economic independence

II Economic aspects
1. Safety against risk
2. Protection to employees
3. Basis of Credit
4. Protection from the loss of key man
5. Encourage loss prevention methods
6. Reduction of cost
7. Promote foreign trade
8. Development of big industries
9. Increase in efficiency

III Social aspects
1. Stability in family life
2. Development of employment opportunity
3. Encourage alertness
4. Contributes to the development of basic facilities

IV National aspects
1. Increase the national savings
2. Helps in development opportunities
3. Develops the money market
4. Earns foreign exchange
5. Capitalizes the savings
Basic Principles of Contract of Insurance

Contract of insurance have all the essential elements of general contract. According to section 2(h) and section 10 of the Indian Contract Act 1872, a valid contract must have the essential elements of offer and acceptance, consideration, legal parties, sound mind and free consent of the parties. Further, Insurance transactions need be governed by special principles in order to protect the interests of the contracting parties, particularly the customer. It is in view of this that the contracts are governed by certain special basic legal principles. Following are the important essential elements or principles of a valid contract of insurance

I. Nature of contract – General to all contracts
II. Special principles of insurance contract

1. Insurable interest
2. Utmost good faith
3. Indemnity
4. Causa proxima
5. Contribution
6. Mitigation of loss
7. Subrogation

I. Nature of Contract

The nature of contract is a fundamental principle of a contract of insurance required for a valid contract. Essential elements of a valid contract are:

a. Agreement (offer and acceptance)

b. Lawful consideration- premium is consideration for insurance contract

c. Lawful objects- object of insurance is lawful and not against to public policy. It is for public welfare

d. Free consent- consent of parties to contract should be free. I.e., not by means of coercion, undue influence, fraud, misrepresentation etc.

e. Competent parties (legal capacity of parties)- parties to an insurance contract should not be idiot, lunatic, minor, insolvent etc.

f. Consensus ad idem- parties to contract should understand the subject matter of insurance in same sense.

g. Possibility and certainty of performance etc.
1. The principle of insurable interest

The existence of insurable interest is an essential ingredient of any insurance contract. Insurable interest is the pre-requisite for insurance. A general definition used for insurable interest is “The legal right to insure arising out of financial relationship, recognized under law, between the insured and the subject matter of insurance.”

2. The Principle Of Utmost Good Faith

The principle of utmost good faith is mostly discussed in the context of the duty of the insured towards the insurer, though it is equally applicable to the insurer’s duty towards the insured. In insurance contract, the prosper is the only person who is deemed to have known all the facts of the subject matter of insurance and the insurer is to completely rely on what the proposer has disclosed. The proposer, should therefore, furnish all material facts concerning the property proposed insurance which would enable the insurance company to decide the appropriate rates and the terms and condition. The duty of disclosure of material facts continues throughout the contract and the insured should advice the insurance company wherever change occurs in the property insured.

3. The Principle Of Indemnity

The object of insurance is to place insured in the same financial position as was just before the loss. This principle prevents the insured from making a profit out of loss and ensures public interest at large. For example, if a machinery insured and is destroyed by fire, the insurance company will make good to loss by taking into consideration the depreciation and wear the tear of the machinery having been in use by the insured for some time. It will not be true indemnity to pay the price of new machinery as the insured has enjoyed the use of the machinery for some years. If the insurance company pays him the money to get new machinery, it may tempt him to set fire to the sofa so that he could get new machinery for old at insurance cost.

there are four methods of indemnification and they are.

1) Cash payment

2) Repair

3) Replacement

4) Reinstatement
In case of life insurance, however, the economic value of a human life cannot be measured precisely before death. It could in fact be unlimited. Hence, life insurance cannot strictly be a contract of indemnity. This does not however, mean a person can be granted life insurance for an unlimited amount.

4. The Principle Of Subrogation

Subrogation is principle, which applied to all contracts of indemnity. It means that after payment of the loss the insurer gets the right of taking all steps to recover any money in compensation from a third party. Technically speaking “Subrogation is the right, which an insurer gets, after he has indemnified the loss, to step into the shoes of the insured and avail himself of all the rights against their party in respect of loss indemnified.” The subrogation principle prevents the insured of collecting the twice of the same loss at first instance, and wrong doer would escape liability at second. It strengthens the areas of insurer in cases of possibility of one recovery of misdoings, stealing or damaging made by third party and recovering the goods indemnified.

5. Contribution

The contribution is the right of an insurer who has paid a loss under a policy to recover a proportionate amount from other insurer who is liable for the loss. Such situations only arise

(a) When different insurer has agreed to contribute the loss by way of collecting proportionate premium.

(b) The policies are in existence at the time of loss.

(c) The policies are legally enforceable at law.

(d) The interest covered under all the policies are same, and affected in favour of a common insured.

6. The Proximate Cause

The proximate cause can be defined as “the active efficient cause that sets in motion a train of events which brings about a result, without the intervention of any force started and working actively from a new independent force.” In other words, it specifies the indemnification of losses concurrent with the perils specified under insurance contracts and not in general. Properties are exposed to various perils like fire, earthquake, explosion, perils of sea, war, riot, civil commotion and so on, and policies of insurance covering various combinations of such perils can be procured. Policies of insurance usually afford protection against some of these perils, expressly exclude certain perils from the cover, and by
implication other perils are covered. The insurer’s liability under the policy arises only if the cause of the loss is a peril insured against and not as expressly excluded or other peril.

7. Mitigation of Loss

Mitigation of loss is applied in valid insurance contract. In the event of some mishap or accident to the insured property, the insured must make necessary effort to safeguard his remaining property and minimise the loss, as much as possible. If he does make any reasonable efforts to reduce the loss, insurer will be liable for payment of all loss resulting from the peril insured against. If he is negligent to preserve the property, the insurer may avoid the payment of loss.

Types of insurances

There are different kinds of Insurance. Depending upon the types of risk insure. We can classify them into 2 groups’ i.e.

I. Life Insurance

It is governed by the LIC act 1956. It is contract in which the insurer, inconsideration of payment of premium compensate to a person on death or on the expiry of certain period whichever is earlier.

II. General Insurance

General Insurance covers a wide range of services. Section 6(b) of the insurance act 1938 defines General Insurance. It includes all the risks except life. Its classification is:

A. Marine Insurance

Marine insurance is the oldest insurance which was introduced long back to compensate on sea and to compensate the loss due to various sea perils or loss of the ship etc. In today’s context, marine insurance is an important part of trade and commerce and is a significant part of global insurance business. Marine play a key role in international trade. Law relating to marine insurance act 1963.

According to section 3 of marine insurance act, 1963 defines marine insurance as, a contract where by an insurer undertakes to indemnify the assured against marine losses that is to say the losses incidental to marine adventure.

Features of marine insurance contract:

1. Features of a valid contract: marine insurance is a contract; therefore it should possess the features of a valid contract, according to Indian contract act. They are;
• The proposal forms called slips are the offer from the merchant. The original slip is submitted along with the other material information. This is proposal from the merchant or the ship owner is the offer.

• The master and crew of the ship have an insurable interest in respect of their wages.

• Premium is consideration to contract.

• The policy is prepared, stamped and signed and it will be the legal evidence of the contract

• When slip is presented to the insurer, he checks it and satisfied he puts initial. Now the proposal is accepted. Once the slip is accepted the offer of the proposer is accepted by the insurer

2. Insurable interest in marine policy:

• Owner of the goods has insurable interest to the extent of total value of the goods.

• Owner of the ship can insure the ship to its full price

• Buyer of the goods who insured them has insurable interest even he rejects the goods.

• Insurer has an insurable interest in his risk and may reinsure in respect of it.

• The receiver freight can insure up to the amount of freight to be received by him.

• The policy holder has an insurable interest in the charges of any insurance which he may affect.

• If the subject matter insured is mortgaged, the mortgager has an insurable interest

3. Disclosure by agent: When insurance policy is taken through an agent, the must disclose to the insurer every fact. The agent is deemed to know all the details of material information. If the information is false, the insurer can avoid the policy. If negligence can be held against the broker, he may be liable for breach of contract

4. Principle of Indemnity: Marine insurance is a contract of indemnity. It implies that the policy holder cannot make profit out of a claim. In the absence of principle of indemnity, the policy holder may make profit out of claim. The insurance contract implies that the indemnifies only to the extent agreed upon. The basis of indemnity is always a cash basis.
5. Principle of subrogation: This principle specifies that the policy holder should not get more than the actual loss. The insurer has a right to pay the amount of loss after reducing the money received by the policy holder from the third party. After indemnification the insurer gets all the rights of insured on the third parties. But he cannot file suit in his name. Therefore he has to take the support of the policy holder.

**Types of marine insurance policies:**

1. **Time policy:**

   If the policy is to insure the subject matter for a definite period of time it is called time policy. For example: 6 AM of 1st July 2013 to 6 AM of 31 March 2014 or 6 Am of 1st March 2012 to 6 PM 28th February 2013. Usually time policies are taken for one year. If the policy contains a clause ‘continuation clause’, if the ship is still at sea, the policy will continue for some more time. But the policy holder should take a fresh policy duly stamped for the continuation period. Time policy is commonly taken for hull insurance.

2. **Mixed policy:**

   If a policy contains the provision of both time policy and voyage policy, it is called mixed policy. This policy covers the risk during a particular voyage for a specified period. Example: from Bombay to London for six months.

3. **Valued policy:**

   Valued policy specifies the agreed value of the subject matter insured. Therefore the value of loss to be compensated by the insurer is fixed and remains constant throughout. The insurer and the insured agree upon the value at the time of taking the policy. Thus it is also called insured value or agreed value. The insured value need not be actual value.

4. **Unvalued policy:**

   Unvalued policy does not specify the agreed value of the subject matter insured at the time of taking policy. It left to be valued when the loss takes place. Thus, it is called as open policy or insurable policy.

5. **Floating policies:**

   Floating policies gives the description of insurance in general terms. The policy just mentions the amounts for which the insurance is taken for each shipment. It leaves other details such as name of the ship etc., to be given in the declaration. Floating policies are popular in large scale international trade.
B). Fire Insurance:

Fire insurance is a recent developed concept in insurance sector. It is covered under the insurance act 1938. Definition: “Fire insurance is a cover against the risk of loss of property due to fire accident.” Fire Insurance is a contract where by the insurer undertakes in consideration of the premium paid to make good any loss cause by the fire during a specific period. The specific amount to be assured or claimed in case of loss should be mentioned or specified in the contract.

Features of Fire Insurance:

1. It is a General Contract: It is one of the important feature of fire insurance, It contains all the features of a valid contract. This is accepted by the insurer for the consideration of the premium. The insurer issues the policy with all terms and conditions of the contract.

2. Contract of Indemnity: Fire insurance is a contract of indemnity, in the event of loss the insured can recover actual amount of loss. Insured is allowed to gain excess amount out of the loss caused due to fire.

3. Insurable interest:

4. Period of the policy: Fire insurance policy is issued for one year. Therefore they are popular as Annual insurance

Types of fire policy:

- Valued policy: under this policy, the value of the property to be insured is determined at the time of the policy is taken. In the event of loss the fixed amount is payable irrespective of the actual amount of loss.

- Specific policy: This policy covers the loss up to a specified amount which is less than the real value of the property. Thus it is an under-insurance policy. The whole of the actual loss is payable provided it does not exceed the insured amount.

- Comprehensive policy: Comprehensive policy as the name indicates covers losses against risks as fire, theft, burglary, riots, civil disturbances etc. Therefore this policy is popular as ‘all in one policy’. It may also cover loss of profits during the period the business remains closed due to fire.

- Floating policy: it is a policy which covers property at different places against loss by fire. Example: goods stored in two different warehouses. It covers goods in two or more localities under one sum assured for one premium.

- Average policy: A policy with ‘average clause’ is called average policy. The amount of indemnity.
C). Miscellaneous insurance:

Health, Motor, Deposit and Postal Insurance and others come under this category.

- **Health insurance** provides for the payment of benefits to cover the loss due to sickness.

- **Motor Insurance** provides the benefits in case of damage or loss due to accident.

- **Deposit insurance** provides Insurance against bank deposit. This scheme was introduced by our government in 1962.

- **Postal insurance** was introduced in 2006 by postal department of India. This scheme provides insurance to postal saving account holders for accidental death.

- **Accident insurance policies** offered by insurer are personal accident insurance; crackle core insurance, passenger flight capon insurance, suhana safer policy, kidnap & ransom insurance, Bhagya shri policy etc.

- **The liability insurance policies** offered by insurer are professional indemnity policy, adhikari suraksha kavach, doctor's indemnity policy etc.

- **Burglary insurance policies** provide insurance coverage against burglary, theft etc of valuable goods

- **Baggage insurance policy** provides insurance coverage for loss of baggage and luggage etc in transit.

**Life Insurance Corporation of India (LIC)**

The LIC of India was set up under the LIC Act, 1956 under which the life insurance was nationalised. As a result, business of 243 insurance companies was taken over by LIC on 1-9-1956. It is basically an investment institution, in as much as the funds of policy holders are invested and dispersed over different classes of securities, industries and regions, to safeguard their maximum interest on long term basis. LIC is required to invest not less than 75% of its funds in Central and State Government securities, the government guaranteed marketable securities and in the socially-oriented sectors. At present, it is the largest institutional investor. It provides long term finance to industries.

**Objectives of LIC of India**

The LIC was established with the following objectives:

1. Spread life insurance widely and in particular to the rural areas, to the socially and economically backward claries with a view to reaching all insurable persons in the country and providing them adequate financial cover against death at a reasonable cost
2. Maximisation of mobilisation of people’s savings for nation building activities.

3. Provide complete security and promote efficient service to the policy-holders at economic premium rates.

4. Conduct business with utmost economy and with the full realisation that the money belong to the policy holders.

5. Act as trustees of the insured public in their individual and collective capacities.

6. Meet the various life insurance needs of the community that would arise in the changing social and economic environment

7. Involve all people working in the corporation to the best of their capability in furthering the interest of the insured public by providing efficient service with courtesy.

Role and Functions of LIC

The role and functions of LIC may be summarised as below:

a. It collects the savings of the people through life policies and invests the fund in a variety of investments.

b. It invests the funds in profitable investments so as to get good return. Hence the policy holders get benefits in the form of lower rates of premium and increased bonus. In short, LIC is answerable to the policy holders.

c. It subscribes to the shares of companies and corporations. It is a major shareholder in a large number of blue chip companies.

d. It provides direct loans to industries at a lower rate of interest. It is giving loans to industrial enterprises to the extent of 12% of its total commitment.

e. It provides refinancing activities through SFCs in different states and other industrial loan-giving institutions.

f. It has provided indirect support to industry through subscriptions to shares and bonds of financial institutions such as IDBI, IFCI, ICICI, SFCs etc. at the time when they required initial capital. It also directly subscribed to the shares of Agricultural Refinance Corporation and SBI.

g. It gives loans to those projects which are important for national economic welfare. The socially oriented projects such as electrification, sewage and water channelising are given priority by the LIC.

h. It nominates directors on the boards of companies in which it makes its investments.

i. It gives housing loans at reasonable rates of interest.
j. It acts as a link between the saving and the investing process. It generates the savings of small savers, middle income group and the rich through several schemes. Small and medium income groups look upon the LIC for the element of protection as well as for certain privileges like taking loans at the time of building a house or receiving certain tax exemptions. The higher income group consider it as a means of receiving full tax exemption when their income is of a large amount. Out of the total of the fund the LIC receives, it uses to play an influential role in the Indian capital market.

k. Formerly LIC has played a major role in the Indian capital market. To stabilise the capital market it has underwritten capital issues. But recently it has moved to other avenues of financing. Now it has become very selective in its underwriting pattern.

Life insurance Policies

Life insurance policies can be grouped into the following categories:

1. **Term Policy**

In case of Term assurance plans, insurance company promises the insured for a nominal premium to pay the face value mentioned in the policy in case he is no longer alive during the term of the policy. It provides a risk cover only for a prescribed period. Usually these policies are short-term plans and the term ranges from one year onwards. If the policyholder survives till the end of this period, the risk cover lapses and no insurance benefit payment is made to him.

2. **Whole Life Policy**

This policy runs for the whole life of the assured. The sum assured becomes payable to the legal heir only after the death of the assured. The whole life policy can be of three types.

   (1) Ordinary whole life policy – In this case premium is payable periodically throughout the life of the assured.

   (2) Limited payment whole life policy – In this case premium is payable for a specified period (Say 20 Years or 25 Years) Only.

   (3) Single Premium whole life policy – In this type of policy the entire premium is payable in one single payment.

3. **Endowment Life Policy**

In this policy the insurer agrees to pay the assured or his nominees a specified sum of money on his death or on the maturity of the policy whichever is earlier. The premium for endowment policy is comparatively higher than that of the whole life policy.
4. Health insurance schemes

An individual is subject to uncertainty regarding his health. He may suffer from ailments, diseases, disability caused by stroke or accident, etc. For serious cases the person may have to be hospitalized and intensive medical care has to be provided which can be very expensive. It is here that medical insurance is helpful in reducing the financial burden.

5. Joint Life Policy

This policy is taken on the lives of two or more persons simultaneously. Under this policy the sum assured becomes payable on the death of any one of those who have taken the joint life policy. The sum assured will be paid to the survivor(s). For example, a joint life policy may be taken on the lives of husband and wife, sum assured will be payable to the survivor on the death of the spouse.

6. With Profit And Without Profit Policy

Under with profit policy the assured is paid, in addition to the sum assured, a share in the profits of the insurer in the form of bonus. Without profit policy is a policy under which the assured does not get any share in the profits earned by the insurer and gets only the sum assured on the maturity of the policy. With profit and without profit policies are also known as participating and non–participating policies respectively.

7. Double Accident Benefit Policy

This policy provides that if the insured person dies of any accident, his beneficiaries will get double the amount of the sum assured.

8. Annuity Policy

Under this policy, the sum assured is payable not in one lump sum payment but in monthly, quarterly and half-yearly or yearly instalments after the assured attains a certain age. This policy is useful to those who want to have a regular income after the expiry of a certain period e.g. after retirement.

9. Policies For Women

Women, now a days are free to take life assurance policies. However, some specially designed policies suit their needs in a unique manner; important policies for women are

A. Jeevan Sathi is also known a Life Partner plan where the husband and wife are covered under this endowment policy

B. Jeevan Sukanya
10. Group Insurance

Group life insurance is a plan of insurance under which the lives of many persons are covered under one life insurance policy. However, the insurance on each life is independent of that on the other lives. Usually, in group insurance, the employer secures a group policy for the benefit of his employees. Insurer provides coverage for many people under single contract.

10. Policies For Children

Policies for children are meant for the various needs of the children such as education, marriage, security of life etc.

11. Money Back Policy

In this case policy money is paid to the insured in a number of separate cash payments. Insurer gives periodic payments of survival benefit at fixed intervals during the term of policy as long as the policyholder is alive.

General Insurance Companies

General insurance companies have willingly catered to these increasing demands and have offered a plethora of insurance covers that almost cover anything under the sun. Any insurance other than ‘Life Insurance’ falls under the classification of General Insurance. It comprises of:-

- Insurance of property against fire, theft, burglary, terrorism, natural disasters etc
- Personal insurance such as Accident Policy, Health Insurance and liability insurance which cover legal liabilities.
- Errors and Omissions Insurance for professionals, credit insurance etc.
- Policy covers such as coverage of machinery against breakdown or loss or damage during the transit.
- Policies that provide marine insurance covering goods in transit by sea, air, railways, waterways and road and cover the hull of ships.
- Insurance of motor vehicles against damages or accidents and theft

All these above mentioned form a major chunk of non-life insurance business.

General insurance products and services are being offered as package policies offering a combination of the covers mentioned above in various permutations and combinations. There are package policies specially designed for householders, shopkeepers, industrialists, agriculturists, entrepreneurs, employees and for professionals such as doctors, engineers, chartered accountants etc. Apart from standard covers, General insurance companies also offer customized or tailor-made policies based on the personal requirements of the customer.
General Insurance Corporation of India (GIC)

General insurance industry in India was nationalised and a government company known as General Insurance Corporation of India was formed by the central government in November, 1972. General insurance companies have willingly catered to these increasing demands and have offered a plethora of insurance covers that almost cover anything under the sun.

**Objective of the GIC are:**

1. To carry on the general insurance business other than life, such as accident, fire etc.
2. To aid and achieve the subsidiaries to conduct the insurance business and,
3. To help the conduct of investment strategies of the subsidiaries in an efficient and productive manner.

**Role and Functions of GIC**

a. Carrying on of any part of the general insurance, if it thinks it is desirable to do so.

b. Aiding, assisting and advising the acquiring companies in the matter of setting up of standards of conduct and sound practice in general insurance business.

c. Rendering efficient services to policy holders of general insurance.

d. Advising the acquiring companies in the matter of controlling their expenses including the payment of commission and other expenses.

e. Advising the acquiring companies in the matter of investing their fund.

f. Issuing directives to the acquiring companies in relation to the conduct of general insurance business.

g. Issuing directions and encouraging competition among the acquiring companies in order to render their services more efficiently.

**Classification of Indian General Insurance Industry**

General Insurance is also known as Non-Life Insurance in India. There are totally 16 General Insurance (Non-Life) Companies in India. These 16 General Insurance companies have been classified into two broad categories namely:

i. **PSUs (Public Sector Undertakings)**

ii. **Private Insurance Companies**

**a. PSUs (Public Sector Undertakings):**

These insurance companies are wholly owned by the Government of India. There are totally 4 PSUs in India namely:

1. National Insurance Company Ltd
2. Oriental Insurance Company Ltd
3. The New India Assurance Company Ltd
4. United India Insurance Company Ltd

b. Private Insurance Companies:

There are totally 12 private General Insurance companies in India namely:

1. Apollo DKV Health Insurance Ltd
2. Bajaj Allianz General Insurance Co. Ltd
3. Cholamandalam MS General Insurance Co. Ltd
4. Future General Insurance Company Ltd
5. HDFC Ergo General Insurance Co Ltd
6. ICICI Lombard General Insurance Ltd
7. Iffco Tokio General Insurance Pvt Ltd
8. Reliance General Insurance Ltd
9. Royal Sundaram General Insurance Co Ltd
10. Star Health and Allied Insurance
11. Tata AIG General Insurance Co Ltd
12. Universal Sompo General Insurance Pvt Ltd

Insurance is a device by which the loss likely to be caused by an uncertain event is spread over a number of persons who are exposed to it and who propose to insure themselves against such an event. In short, insurance is a mechanism for pooling of risks.

References:

7. Preserve Articles.Com
8. Kalyan City Blogspot
Model Question paper 1

SIXTH SEMESTER B.B.A DEGREE (PRIVATE/SDE)

EXAMINATION *******2013

(CCSS)

-INDIAN FINANCIAL SYSTEM

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Part I

Part A

Answer all questions.

Each question carries a weightage of 1

1. What do you mean by financial system?
2. What do you mean by financial intermediation?
3. Define money market.
4. What is certificate of deposit?
5. What are the important development banks in India?
6. Expand the following : a. DFHI   b. MMMF
7. Define stock exchange.
8. What are NBFCs?
9. What you mean by Deep Discount Bond?  ( 9 x1= 9 weightage)

Part B

Answer any 5 questions.

Each question carries a weightage of 2

10. Distinguish between money market and capital market.
11. Discuss various modes of floating of new securities.
12. Briefly explain the functions of merchant banks.
14. Discuss the role and functions of IDBI.
15. Explain the following terms;
   a. Commercial paper
   b. Treasury bills
   c. Repo
   d. GDR
16. What are the importance of gilt edged securities? (5 x 2 = 10 weightage)

**Part c**

*Answer any 2 questions.*

*Each question carries a weightage of 4*

17. Explain the role and functions of financial system. Also explain the defects of Indian financial system.
18. Discuss various components of money market.
19. Briefly explain the role and guidelines of SEBI in Primary and secondary market. (2 x 4 = 8 weightage)

**Part II**

*20 No’s of multiple choice questions*
Model Question paper 2

SIXTH SEMESTER B.B.A DEGREE (PRIVATE/SDE)

EXAMINATION ******2013

(CCSS)

-INDIAN FINANCIAL SYSTEM

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Part I

Part A

Answer all questions.

Each question carries a weightage of 1

1. What do you mean by development bank?
2. What do you mean by financial market?
3. Define G.sec market
4. What is commercial paper?
5. What are the important NBFservices in India?
6. Expand the following : a. CRISIL  b. AMFI
7. Differentiate between genuine investment and speculation.
8. What you mean by ADR?
9. What you mean by Secured premium notes? ( 9 x1= 9 weightage)

Part B

Answer any 5 questions.

Each question carries a weightage of 2

10. Distinguish between Primary market and secondary market.
11. Discuss the functions of capital market.
12. Briefly explain the functions of SEBI.
13. Briefly explain depositary system.
14. Discuss the role and functions of IFCI.
15. Explain the role of RBI as regulator of money market.
16. What are the importance of financial intermediaries? (5 x 2 = 10 weightage)

Part c
Answer any 2 questions.
Each question carries a weightage of 4

17. Discuss the growth and development of Indian financial system.
18. Define stock exchange. And also explain the method of trading on a stock exchange.
19. Define money market. What are features of an ideal or developed money market (2 x 4 = 8 weightage)

Part II
20 No’s of multiple choice questions

“ALL THE BEST”